



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Date:
October 26, 2017
Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

Number: **201801013**
Release Date: 1/5/2018

UIL: 501.33-00, 501.35-00

Dear _____ :

This letter is our final determination that you don't qualify for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code (the Code). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

Because you don't qualify as a tax-exempt organization under Section 501(c)(3) of the Code, donors can't deduct contributions to you under Section 170 of the Code. You must file federal income tax returns for the tax years listed at the top of this letter using the required form (also listed at the top of this letter) within 30 days of this letter unless you request an extension of time to file.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection (as required under Section 6110 of the Code) after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Notice 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

We'll also notify the appropriate state officials of our determination by sending them a copy of this final letter and the proposed determination letter (under Section 6104(c) of the Code). You should contact your state officials if you have questions about how this determination will affect your state responsibilities and requirements.

If you have questions about this letter, you can contact the person listed at the top of this letter. If you have questions about your federal income tax status and responsibilities, call our customer service number at 1-800-829-1040 (TTY 1-800-829-4933 for deaf or hard of hearing) or customer service for businesses at 1-800-829-4933.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

Enclosures:

Notice 437

Redacted Letter 4036, *Proposed Adverse Determination Under IRC Section 501(c)(3)*

Redacted Letter 4038, *Final Adverse Determination Under IRC Section 501(c)(3) - No Protest*



**Department of the Treasury
Internal Revenue Service**

P.O. Box 2508
Cincinnati, OH 45201

Date: August 11, 2017

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

M = state

N = date

W = company

X = individual

Y = individual

Z = individual

UIL:

501.33-00

501.35-00

Dear _____ :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(3) of the Code. This letter explains the basis for our conclusion. Please keep it for your records.

Issues

Do you qualify for exemption under Section 501(c)(3) of the Code? No, for the reasons stated below.

Facts

You were incorporated in the state of M on N. You will provide funding and promotion for creative individuals and small organizations. You will use sponsorship, fund raising and other activities to establish live or online contests, promotional events, and marketing channels to reach your goals. Your main activity will be running a contest for amateur talent to facilitate the funding and/or sale of creative content to prospective Buyers; Buyers being those who purchase said content (producers, distributors, media outlets, etc.) Participants (referred to in the contest rules as Sellers) can be organizations or individuals submitting content for consideration by contest judges, such as videos, scripts, artwork or other materials. You will grant funds to these participants that often struggle to find funding to pursue their creative contributions. You also refer to participants as beneficiaries and contestants.

Your governing body consists of X and Y, who are married, and one additional unrelated individual (Z). All three of the governing body members are involved in the performance promotion business - X and Y operate and co-own "several" performance media for-profit companies. Five were specifically named in your application, including W. Z is a managing director of a company that is a customer of one of X and Y's for-profit businesses, but not with you.

W does cross-promotion with you, and provides performing agency services for content creators receiving revenue from media distributors. It uses existing marketing to promote your activities to potential beneficiaries

(Sellers). In order for potential beneficiaries to make submissions for your contest they must use the online resources of W. All content submitted to the W Seller portal will be considered a grant application unless W is notified otherwise. You stated that the users of these resources have no financial or legal obligation to anyone but may choose to purchase expanded online resources or partner with W. Contest rules stipulate that by submitting content each participant grants non-exclusive licensing rights to both you and W to use content solely for the purpose of promoting and running the contest and to make material available via W's website and other media. W's staff and resources will occasionally be used for your operations. W staff will screen applicants to identify finalists, whose entries will then be screened at a live event by judges representing media and broadcast companies, choosing a winner. W staff will actively promote/market material on the W portal and expand the number of Buyers. You state that the responsibility of promoting/marketing intellectual property to distributors falls on the creator, but, as an added benefit to participating in your contest, as long as participants choose to keep their property in their Seller account on the W portal, those accounts can be used to market to potential Buyers. You stated that you have not nor do you intend on spending time marketing participants.

When someone visits your website, they have two options: they can choose to view your contest rules or they can choose W's portal. While visitors to your website do not have to visit W's website, any person who wants to participate in your contest cannot do so without visiting W's site, as it is part of the submission process. Participants in the contest must register as sellers of intellectual property on the W portal. There are links to starting an account as a Buyer or Seller, information to get funded, sold or distributed, as well as details on what the portals offer. Only active Seller content is eligible to participate in the contests. You hope to promote and market the work of creative people by publicizing the details of the contests and the names of winning and outstanding participants to the media professionals that your directors have met through years of networking. You have indicated the sharing of the portal between you and W is for efficiency and to save resources.

You define W's webpage as being "the best possible method for media professionals to share content between entities on different parts of the distribution chain, while maintaining convenience intuitiveness, quality of presentation and security." Sellers are any individual or organization that produces artistic media (singers, performers, videographers, etc.). Items that are uploaded by Sellers are finished or unfinished movies, audio and video, promotional videos, promotional posters, story concepts, sales pitches, promotional taglines and the like. W does not claim the right to distribute any intellectual property. Sellers keep the intellectual property rights.

W has two revenue streams. The first source of W's income is fees charged for the creation of a Buyer or Seller account. Most Sellers have free accounts but can opt to pay for additional data storage capacity. Fee income from Seller accounts is minimal. The second source is from fees associated with W acting as an agent for a Seller. W claims a commission from the sellers of intellectual property on transactions between registered Buyers and Sellers within the terms or agreements signed by Seller when they registered. W's "terms of service" indicate commissions are 35% of all payments for content bought for use by the Buyer or paid by the Seller and 15% for all content that is funded and/or coproduced by the Buyer. W's plan is to earn almost all revenues from commissions on actual financial transactions but recognizes value in having people know about the portal and its use, as well as goodwill from your association. Also on W's website is a statement that W has extended the deadline for their first contest, and if you are a certain provider you may submit a tax-deductible donation. Nowhere within this description is a mention of you, your website, or your activities.

You expect all of your income to come from donations. Beyond administrative and marketing expenses, all funds will be spent on running contests and funding contest winners.

Law

Section 501(c)(3) of the Code provides, in part, for the exemption from federal income tax to organizations organized and operated exclusively for charitable, religious or educational purposes, where no part of the net earnings inures to the benefit of any private shareholder or individual.

Treasury Regulation Section 1.501(c)(3)-1(a)(1) provides that, in order to be exempt as an organization described in Section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in Section 501(c)(3). If an organization fails to meet either the organizational or operational test, it is not exempt.

Treas. Reg. Section 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as “operated exclusively” for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in Section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. To meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Revenue Ruling 61-170, 1961-2 CB 112 provides that operating under the control of one person or a small, related group suggests that an organization operates primarily for non-exempt private purposes, rather than exclusively for public purposes.

Revenue Ruling 64-175, 1964-1 (Part 1) C.B. 185, holds that a corporation organized for the purpose of promoting the dramatic arts qualifies for exemption as an educational organization under section 501(c)(3) of the Code. The ruling supports the view that a nonprofit organization that preserved and maintained classical music programming in a particular locale served an educational purpose. However, in order for such an organization to qualify for exemption under section 501(c)(3) of the Code, it must serve a public rather than a private interest. Although an incidental private benefit will not destroy the qualification of an otherwise educational organization, where an organization is serving both public and private interests the private benefit must be clearly incidental to the overriding public interest. A contrary finding will indicate that the organization is serving a private interest.

Rev. Rul. 76-206, 1976-1 C.B. 154, described an organization that was formed for the purpose of promoting, maintaining and enhancing the broadcast of classical music in a particular community. The organization carried on a variety of activities designed to stimulate public interest in the classical music programs of a for-profit radio station, and thereby enable the station to continue broadcasting such music. The ruling concluded that the organization's activities enabled the radio station to increase its total revenues and therefore benefit the for-profit radio station in more than an incidental way. Therefore, the organization is serving a private rather than a public interest. Although the organization's broad purpose of promoting interest in classical music and encouraging programming of classical music provided a public benefit, the activities served the private economic interests of the for-profit radio station to a substantial degree. Therefore, because private interests were served, exemption was precluded.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of private benefit, if substantial in nature, will destroy an organization's tax-exempt status regardless of the organization's other charitable purposes or activities.

Application of law

Treas. Reg. Section 1.501(c)(3)-1(a)(1) states that if an organization fails to meet either the organizational test or the operational test, it is not exempt. Since you are conducting activities that will more than insubstantially benefit your founders or insiders, you are not operating exclusively for exempt purposes and do not meet the operational test. Further, your sole activity is providing funding to contest winners selected through a related for-profit entity, W. As a result you are not described under Section 501(c)(3) of the Code.

Your goal is to fund the arts, which is an 501(c)(3) purpose, however; you are operated in a manner that benefits private shareholders and individuals through your related for-profit, W. Although your contest brings attention to artistic works, it also promotes the contest participants and provides a benefit to W. Any participant in your contest must enroll through W and are then subject to W's terms of service and fees that apply. W also directly benefits from commissions earned from sales related to participants from your activities. In benefitting private individuals in a more than insubstantial manner you are not operated exclusively for one or more exempt purposes per Treas. Reg. Section 1.501(c)(3)-1(c)(1).

Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. All control of your operations will be done by those with interests in either W or other businesses owned by X and Y. Any participant in your activities must be subject to exposure to W, and the use of its resources. Your only other board member is a business partner through X and Y's for-profit ventures. Your contest is structured to benefit X and Y in the form of commissions, as well as indirectly through the interests generated by the use of W's portal.

Revenue Ruling 61-170 provides that operating under the control of one person or a small, related group suggests that an organization operates primarily for non-exempt private purposes, rather than exclusively for public purposes. You are operating in conjunction with and are in practice indistinguishable from W. You have not established that you will not be operated for the benefit of X and Y through W. Therefore you have not met established that you will be operated for public rather than private purposes. For this reason you are serving private interests and do not meet the qualifications per Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii).

Revenue Ruling 64-175 holds that a corporation organized for the purpose of promoting the arts qualifies for exemption as educational. However, in order for such an organization to qualify for exemption under Section 501(c)(3) of the Code, it must serve a public rather than a private interest. You are unlike the organization described in Revenue Ruling 64-175. As noted, an educational program that serves both public and private interests must show that any private interest served is incidental to the public's benefit. A contrary finding will indicate the organization is serving a private interest. Participation in your program is contingent upon participants submitting materials through W's website and connecting distributors to those participants structuring W to receive commissions. Your program serves to benefit W, and the owners of W and your board members, X and Y, in a more than incidental manner.

The organization in Rev. Rul. 76-206 was similar to you in its overall purpose, advancing the arts. And similar to that organization you are carrying on activities that will benefit a for-profit entity, W. Your activities will

enable W to increase users on its portal, have intellectual property loaded and controlled through its portal and expose contest participants to distributors that will generate commissions for W. As the owners of W, X and Y will directly benefit. Therefore, you are serving private rather than public interest, and because private interests are served, exemption is precluded.

According to Better Business Bureau of Washington, D.C., the presence of private benefit, if substantial in nature, will destroy an organization's tax-exempt status regardless of the organization's other charitable purposes or activities. As indicated above, although your programs are meant to further the arts, by requiring the use of W you are furthering the interests of a for-profit business owned by your founders. This is substantial private benefit and excludes you from recognition as a tax exempt organization.

Conclusion

Based on the facts and information submitted, you are not operated exclusively for exempt purposes. You do not meet the operational test because you benefit the private interests of individuals more than insubstantially. Further, your activities will promote and further benefit a related for-profit entity. Accordingly, you do not qualify for exemption under section 501(c)(3) of the Code and you must file federal income tax returns. Contributions to you are not deductible under section 170 of the Code.

If you don't agree

You have a right to file a protest if you don't agree with our proposed adverse determination. To do so, you must send a statement to us within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A copy of this letter highlighting the findings you disagree with
- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

Under penalties of perjury, I declare that I examined this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

For authorized representatives:

Under penalties of perjury, I declare that I prepared this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't provided a basis for reconsideration, we'll forward your case to the Office of Appeals and notify you. You can find more information about the role of the Appeals Office in Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

Where to send your protest

Please send your protest statement, Form 2848, if needed, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at www.irs.gov/formspubs. If you have questions, you can contact the person listed at the top of this letter.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

Enclosure: Publication 892