



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

Number: **201835008**
Release Date: 8/31/2018

Date: June 6, 2018

Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

UIL Code: 501.36-03

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.

We sent a copy of this letter to your representative as indicated in your power of attorney.

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: April 9, 2018

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

B = State
C = Date
x percent = Number
y dollars = Amount

UIL:

501.36-03

Dear _____ :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (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 B on C. Your Articles of Incorporation state you are organized exclusively for charitable, religious, educational, and scientific purposes. They also state that in the event you dissolve or terminate at any time, your assets will be distributed for one or more exempt purposes as described under Section 501(c)(3) of the Code. Your purposes listed in your Form 1023 consist of:

- Supporting research internationally for cures being developed for rare and infectious diseases.
- Leading research initiatives, identifying best practices for streamlining drug therapy approvals worldwide.
- Providing professional thought leadership and unique networking activities for industry leaders.
- Increasing public awareness of the fight of ongoing disease cures globally.

To accomplish your purposes, you will provide business and consulting services to the world-wide biotech and pharmaceutical industries who are developing new treatments for people who are infected with rare diseases. You will help bridge the gap between rare disease cures being developed and ultimately approved for patient distribution by providing the necessary services to support efficient processing fast track approval applications for the developers of such drugs. Your services will be available to individuals, for profit and not for profit organizations as well as other stake holders.

You will develop a detailed road map for each client with the necessary steps to get their drugs approved and to market including providing strategy support. You also will focus on providing expert assistance to those who do not have experience or expertise in this process.

Examples of specific services that you will provide to clients include the following:

- Helping clients complete the necessary applications for more advantageous designations from regulatory agencies and in some cases completing the necessary applications and making the required submissions. This may accelerate the approval process;
- Reviewing clients' data and their scientific models to determine if they have the needed information necessary for submitting applications for approval;
- Validating clients' research required for the application process.

Furthermore, you also provide executive search services, executive coaching services, and public awareness and educational programs.

Examples of Executive Search Services consist of connecting trained scientists and researchers with work and professional development opportunities and helping clients develop strategies and techniques in competitive hiring including developing recruiting programs and developing successful retention programs.

Your Executive Coaching Services will involve providing leadership development and professional growth for leaders who are scientists and researchers in the biotech and pharmaceutical industries.

Your public awareness and educational programs will center around international conferences, training events, scientific meetings and symposiums with the goal of contributing to research for developing treatments for rare diseases.

You also have a comprehensive web site describing and promoting the services you provide and the value clients will get because you are operating as a nonprofit.

You are governed by a three-person board consisting of a director, a board chairman and a secretary who have a wide range of experience in providing consulting services in the healthcare and pharmaceutical industries as well in in the nonprofit world. You will be funded solely by fees for services. When determining your individual clients' fees, you will consider hourly rates for project based factors such as salaries, benefits, and overhead (rent, equipment usage, research time etc.). The client fees will be calculated based on the number of estimated hours to complete a request. You will ensure your fees are generally in the range of x percent below market rates by collecting intelligence on competitors through various market analysis.

Your expenses consist of salary expense, occupancy expense and outlays for professional services.

Your salary expense is % of your total expenses and % of your salary expense is for board members. You further indicated that some work performed by your board of directors is unpaid volunteer work. Furthermore, the compensation you pay is determined by the board and is based on compensation for similar positions and you indicated that your current compensation levels are below market for your senior executives. Your president and CEO is the husband of your founder who receives y dollars annually which is about % of your salary expense.

Finally, you indicated that you will provide services to clients who may not be able to pay your fees through a variety of mechanisms which include a complete review of their clinical data, and conference calls in which technical guidance is provided to position the client to move forward on their own. You also offer a reduced fee for those firms which may be financially challenged.

Law

Internal Revenue Code Section 501(c)(3) provides for exemption for organizations organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition, or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 513(a) of the Code describes an “unrelated trade or business” as any trade or business the conduct of which is not substantially related to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under Section 501 Code.

Section 513(c) of the Code provides that a “trade or business” includes any activity which is carried on producing income from the sale of goods or the performance of services. Where an activity carried on for profit constitutes an unrelated trade or business, no part of such trade or business shall be excluded from such classification merely because it does not result in profit.

Treasury Regulations Section 1.501(c)(3)-1(a)(1) states that 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 such Section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Treas. Reg. Section 1.501(c)(3)-1(c)(1) states that in order to meet the operational test, 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(e)(1) states an organization may meet the requirements of Section 501(c)(3) of the Code although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization’s exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in Section 513 of the Code. An organization which is organized and operated for the primary purpose of carrying on an unrelated trade or business is not exempt under Section 501(c)(3) of the Code, even if it has certain religious purposes, its property is held in common, and its profits do not inure to the benefit of individual members of the organization.

In Rev. Rul. 72-369, 1972-2 C.B. 245, an organization was formed to provide managerial and consulting services for section 501(c)(3) organizations to improve the administration of their charitable programs. The organization enters into agreements with unrelated section 501(c)(3) organizations to furnish managerial and consulting services on a cost basis. This revenue ruling stated that:

An organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. To satisfy the ‘operational test,’ the organization’s resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Code and the applicable regulations. Providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The fact that the services in this case are provided at cost and solely for exempt organizations is not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court found that the “commercial hue” permeating the organization was reflected in its charter provisions, which was dedicated to the securing of “educational and scientific advancements of business methods” so that merchants might “successfully and profitably conduct their business.” The organization’s activities were largely animated by this commercial purpose. The Supreme Court held that the presence of a single nonexempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the organization’s sole activity was to offer consulting services on rural-related policy and program development to limited-resource organizations for a fee. The organization did not limit its clientele to organizations which were themselves organizations described under Section 501(c)(3) of the Code, but only to organizations which were either nonprofit or exempt. The fees charged were set at or close to cost, but were not less than its full cost of providing its services. The organization’s financing did not resemble that of the typical organization described under Section 501(c)(3) of the Code. The organization had not solicited or received voluntary contributions from the public. Its only source of income was from fees for services, and those fees were set high enough to recoup all projected costs and to produce a net profit. It failed to show it would not be in competition with commercial enterprises. The provision of managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The Court held that the organization’s primary purpose was not educational, scientific, or charitable, but rather was the conduct of an ordinary commercial consulting enterprise in competition with other commercial firms. The organization was not operated exclusively for tax-exempt purposes within the meaning of Section 501(c)(3) of the Code.

In Easter House v. United States, 846 F. 2d 78 (Fed. Cir. 1988), aff’g 12 Cl. Ct. 476 (1987), the court found an organization that operated an adoption agency was not exempt under Section 501(c)(3) of the Code. The organization was operated for a substantial nonexempt purpose rather than for the exempt purposes of providing educational and charitable services to unwed mothers and children. The court stated that “adoption services do not in and of themselves constitute an exempt purpose.” The court found that the adoption agency was operated in a commercial manner. The agency’s operation was funded completely by the fixed fees charged to adoptive parents. It relied entirely on those fees and sought no funds from federal, state or local sources, nor engaged in fund raising programs, nor did it solicit contributions. Ultimately, the agency was not entitled to tax exempt status on basis that it was “not distinguishable from commercial adoption agency.” The court found that the adoption agency’s primary goal was furthering of a “business purpose” rather than the advancement of an educational or a charitable purpose.

In Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), the court of appeals upheld a Tax Court decision stating that the organization operated its restaurants and health food stores for a substantial commercial

purpose and it did not qualify for exemption under Section 501(c)(3) of the Code. The appellate court provided the factors that may indicate a substantial nonexempt commercial purpose. These factors include:

- Direct competition with other for-profit businesses
- Existence and amount of annual and accumulated profits
- Competitive pricing policies and lack of below-cost pricing
- Use of promotional materials to enhance sales
- Advertising of goods and services
- Lack of plans to solicit charitable contributions
- Hours of operation that are competitive with other commercial enterprises

In Airlie Foundation v. Internal Revenue Service, 283 F. Supp. 2d 58 (D.D.C., 2003), due to the commercial manner in which the organization conducted its activities, the court held that the organization was operated for a nonexempt commercial purpose, rather than for a tax-exempt purpose. The court found that the organization operated its conference center in a manner consistent with that of a commercial business. “Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, *inter alia*, whether the organization uses commercial promotional methods (e.g. advertising) and the extent to which the organization receives charitable donations.”

Application of Law

You do not meet the requirements for recognition of tax exemption under Section 501(c)(3) of the Code because you do not operate for a tax-exempt purpose under Section 501(c)(3) of the Code. Your sole activity is the conduct of a trade or business for the production of income. You conduct no other activity aside from providing consulting services to clients for a fee. Your clients are comprised of any individual, or organization whether operated on a for profit basis or a non-profit basis who are able and willing to pay your fees. Your fees are generally in the range of x percent below market rates fair market value rates comparable to other providers of similar services. You even stated that you conduct research to insure these fees are set in the range of x percent below your competitors. Compensated employees conduct your operations on a regular and continuous basis. Based on Treas. Reg. Section 1.501(c)(3)-1(e)(1), you do not meet the requirements for recognition of tax exemption under Section 501(c)(3) of the Code because you are operated for the primary purpose of carrying on an unrelated trade or business, as defined in Section 513 of the Code.

In addition, you do not meet the operational requirements for recognition of tax exemption under Section 501(c)(3) of the Code and you fail the operational test as described in Treas. Reg. Section 1.501(c)(3)-1(a)(1). You are not operating per Treas. Reg. Section 1.501(c)(3)-1(c)(1) because you operate for a substantial nonexempt purpose because more than an insubstantial part of your activities is not in furtherance of an exempt purpose.

You are like the organization described in Rev. Rul. 72-369, 1972-2 C.B. 245 because you are operating in a commercial manner. The organization described in the revenue ruling was conducting commercial services only for organizations exempt under Section 501(c)(3) Your activities consists of the provision of consulting services primarily to any individual or organization who is able to pay your fees. The fact that your consulting services may be provided in the range of x percent below market rate does not characterize your activities as charitable. Furthermore, the fact that your clients are fighting against rare diseases by providing new cures and requesting your assistance is not sufficient to characterize the activity as charitable.

In Better Business Bureau of Washington, D.C., Inc., the United States Supreme Court provided that “the presence of a single [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly [exempt] purposes.” Since your primary purpose is the conduct of an unrelated trade or business for profit, by operating as a consulting business, you serve a substantial nonexempt purpose, which precludes tax exemption under Section 501(c)(3) of the Code.

You are operated for a substantial nonexempt purpose similar to the organization described in Airlie Foundation v. Internal Revenue Service, supra. Applying the factors stated in Airlie Foundation as demonstrating a substantial nonexempt commercial purpose, your provision of consulting services to clients primarily for a fee directly competes with other providers of similar consulting services. Like a commercial business, your services are generally available to any individual or organization willing to pay your fees.

Furthermore, you stated that when establishing your fees for your various services, you take into consideration general project based factors in determining hourly rates such as salaries, benefits and overhead (rent, equipment usage, research time etc.) and then you ensure your fees are generally below market rates by collecting pertinent information on competitors through market research.

In addition, like the organization in Arlie, you do not limit your clients to organizations that are described under Section 501(c)(3) of the Code. Another factor considered in assessing a commercial manner of operations is the extent and degree of below cost services provided. You indicated that you provide services to clients who may not be able to pay your fees through a variety of methods including a complete review of their clinical data and conference calls with employees in which technical guidance is provided positioning the client to move forward on their own as well as offering a reduced fee for those firms which may be financially challenged; however, you still primarily operate in commercial manner. Moreover, based on your financial data, your revenues will come exclusively from consulting fees resulting from the provision of consulting services. Thus, you meet most of the factors indicated by the courts as operating for a substantial nonexempt purpose.

You are like the organization described in Living Faith, Inc. v. Commissioner, supra, where the court of appeals upheld a Tax Court decision stating that the organization operated its restaurants and health food stores for a substantial commercial purpose. You also meet most of the factors provided by the appellate court in Living Faith, Inc. as exhibiting a substantial nonexempt commercial purpose. Your provision of consulting to clients for a fee is in direct competition with other for-profit providers of similar services. The fact that you ensure the fees you charge through market research are less also illustrated you that you are in direct competition to similar entities. You did not substantiate that you offer below-cost services to your clients. The financial data you submitted showed that all of your income is from fees for services rendered. You are not supported by gifts, grants and charitable contributions from the general public. You are also using your website to market and promote your services which is characteristic of a commercial business. You are operated in a manner indistinguishable from a commercial enterprise. By operating in the manner described, you are furthering a substantial nonexempt purpose.

You are like the organization described in Easter House v. United States, supra, where the court determined that the organization was not exempt because its conduct of adoption services activity was in furtherance of a nonexempt commercial purpose. Similar to adoption services, your provision of consulting services to clients for a fee do not in and of themselves constitute an exempt purpose. Your sole activity is to render consulting

services to your clients in exchange for a fee. Your activities are not carried out to accomplish a tax-exempt purpose under Section 501(c)(3) of the Code.

You are comparable to the organization described in B.S.W. Group, Inc. v. Commissioner, supra, where the court indicated that the provision of managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. Your activities constitute the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. Like a for-profit business, all your revenues are from fees paid by your clients for consulting services. While charitable institutions often do provide services to individuals, the cost is generally subsidized by contributors who do not receive anything in return. Your fees however, are set high enough to recoup all projected costs and to produce a profit. Thus, based on the totality of the facts and circumstances, you are operated for the substantial nonexempt purpose.

Conclusion

Based on the facts, we conclude that you are not in compliance with the above stated laws and precedence. You do not meet the operational test under Section 501(c)(3) of the Code because the manner in which you operate is commercial. Accordingly, you do not qualify for exemption as an organization described in Section 501(c)(3) of the Code. 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.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

Enclosure:
Publication 892

cc: