



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

Number: **202015021**
Release Date: 4/10/2020

Date:
January 14, 2020

Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

UIL Code: 501.35-00, 501.36-01

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*

cc:



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

Date:
November 12, 2019
Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

B = Formation date
C = State of formation
D = LLC name
F = Supermarket
g = Number of inhabitants
h = Number of households
k dollars = Household income comparison point
m dollars = Median household income

UIL:

501.35-00
501.36-01

Dear _____ :

We considered your application for recognition of exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a). We determined that you don't qualify for exemption under IRC Section 501(c)(3). This letter explains the reasons 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

Formation:

You were incorporated on B in the State of C, exclusively for charitable or other exempt purposes within the meaning of Section 501(c)(3) of the Internal Revenue Code of 1986, as amended.

Governance:

You are governed by _____ board members, _____ of whom are married to each other. None of your board members are compensated at this time. Your _____ board members own D LLC.

Activities

You plan to operate a grocery store in a blighted low-income census tract which is a food desert as defined by the USDA, a low-income community in an urban area in which there is no grocery store within a mile. The store will provide residents with walkable access to affordable and nutritious foodstuffs, including staples such as milk, eggs, cheese fruits and vegetables, which would otherwise be hard to obtain or overpriced for low income members of the community within reasonable walking distance.

The neighborhood includes g people in h households with a median age of years. The residents are percent African American and percent Latino with percent of households making less than k dollars per year and a median income of m dollars. In this zip code there are corner stores, dollar stores and no grocery stores. The nearest full grocery store, F, is to miles from the residents in this neighborhood. Access to that grocery requires residents to cross major state and interstate highways.

You stated that several for-profit grocery stores had rejected offers to locate in the area you will serve. You did not provide the requested documentation to this effect.

The property that you will use for your market is owned by two board members, a married couple, through their D LLC. They purchased the property with the sole intent of making it available to you to operate as a grocery store. You will lease the facility from the LLC; the rent will be limited to the landlord's cost of real estate taxes, insurance, utilities and maintenance. The landlords have assumed the costs of renovations to the building, which will not be passed on to you. Asked why D LLC does not transfer the property to you, you respond that you currently lack resources for operating the facility.

You will purchase grocery items which you will sell at discounted prices "to meet the economic level of the neighborhood." You will also accept donated grocery items. You will donate surplus groceries to other charities. You are applying for SNAP and WIC service.

Revenue and Expense

You are seeking grant funding and donations for start-up expenditures. Sixty-eight percent of your projected income comes from sales in your market. The balance is from donations. Your expenses are for occupancy expenses, salaries and wages, and other expenses. We asked you to provide a breakdown of your other expenses. You stated your other expenses are projections based on your review of another non-profit food market in the area, but you did not provide categorized expenses as requested. We asked you to provide a list of your grocery items which include your purchase price and your proposed sale price. You provided a list of estimated sales prices only, based on the other non-profit's current prices.

Law

Section 501(c)(3) of the Code provides for the recognition of exemption of organizations that are organized and operated exclusively for religious, charitable or other purposes as specified in the statute. No part of the net earnings may inure to the benefit of any private shareholder or individual.

Section 6110(k)(3) of the Code states unless the Secretary otherwise establishes by regulations, a written determination may not be used or cited as precedent. Section 6110(b)(1)(A) provides that in general, the term "written determination" means a ruling, determination letter, technical advice memorandum, or Chief Counsel advice.

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. 1.501(c)(3)-1(d)(2) provide that the term "charitable" is used in IRC 501(c)(3) in its generally accepted legal sense and includes relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of government; promotion of social welfare. It expressly provides that relief of the poor, distressed, or underprivileged is a charitable purpose.

Revenue Ruling 73-127, 1973-1 C.B. 221 describes a nonprofit organization that operates a discount grocery store and allocates a small portion of its earnings to provide on-the-job training to the hard-core unemployed. The organization operates in a poverty area, selling food at prices substantially lower than those charged by competing grocery stores, providing free grocery delivery service to customers needing, participating in the Federal food stamp program, and providing job training for unemployed residents. The organization's purpose of operating a retail grocery store where food is sold to residents of a poverty area at low prices is not recognized as a charitable purpose under the basic common law concept of charity and within the meaning of Section 501(c)(3) of the Code and Section 1.501(c)(3)-1(d)(2) of the regulations.

Revenue Procedure 2019-5, 2019-1 I.R.B. 230 provides that we apply statutes, tax treaties, court opinions and guidance published in the Internal Revenue Bulletin when issuing our determination letters.

In Universal Life Church v. United States, 372 F. Supp. 770 (E.D. Cal. 1974), the court concluded that "one seeking a tax exemption has the burden of establishing his right to a tax-exempt status."

Pius XII Academy v. Commissioner, T.C. Memo. 1982-97 provides that an organization must establish through the administrative record that it operates as an exempt organization. Denial of exemption may be based solely upon failure to provide information describing in adequate detail how the operational test will be met.

In La Verdad v. Commissioner, 82 T.C. 215 (1984), the administrative record did not demonstrate that the organization would operate exclusively in furtherance of an exempt purpose. Therefore, denial of organization's request for tax-exempt status was reasonable.

In New Dynamics Foundation v. United States, 70 Fed. Cl. 782 (2006), the organization failed to establish an administrative record that showed it was operated for exclusively exempt purposes. The court held that exemption from federal income tax is not a right; it is a strictly interpreted matter of legislative grace and the burden rests with the applicant to prove that it is entitled to exempt status.

In Better Business Bureau v. United States, 326 U.S. 279, 283 (1945) the court held that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

Application of law

You do not meet the operational test under Section 501(c)(3) of the Code because you are not operating exclusively for charitable purposes as required under Treas. Reg. Section 1.501(c)(3)-1(c)(1). You plan to

operate a community grocery store where you will sell items at a discount. You are like the grocery store in Revenue Ruling 73-127, which sold grocery items in a poverty area at below market prices. Operating a grocery store – even one that sells food to residents of a poverty area at low prices -- is not a recognized charitable purpose under the basic common law concept of charity and within the meaning of Section 501(c)(3) of the Code and Section 1.501(c)(3)-1(d)(2) of the regulations.

You distinguish your activities from those of the grocery store in the revenue ruling, stating that you are operated for the charitable purpose of relief of the poor and distressed and of the underprivileged, by providing low income residents of a food desert with walkable access to affordable and nutritious foodstuffs, including staples such as milk, eggs, cheese fruits and vegetables, which would otherwise be hard or prohibitively expensive for them to obtain. However, this purpose is in addition to, rather than the unique purpose of your activities. You are clearly organized and operated for a substantial non-exempt purpose, operation a retail grocery store where food is sold to residents of a poverty area at low prices. It is therefore unnecessary to consider whether your additional purpose of alleviating conditions in a food desert is a charitable purpose within the meaning of Treas. Reg. 1.501(c)(3)-1(d)(2), as you are not operated exclusively for exempt purposes. See Better Business Bureau v. United States. However, even if that were your exclusive purpose, you have not carried your burden to establish that you are operated for an exempt purpose within the meaning of Section 501(c)(3) and Treas. Reg. 1.501(c)(3)-1(d)(2), because you have not cited any clear precedent for recognition of alleviation of conditions in a food desert as a charitable purpose; see our response to your position, below, and Universal Life Church v. United States, Pius XII Academy v. Commissioner, La Verdad v. Commissioner, New Dynamics Foundation v. United States.

Your position

You are organized and operated exclusively for the charitable purpose of relief of the poor and distressed and of the underprivileged in accordance with Treas. Reg. 1.501(c)(3)-1(d)(2). Increasing the poor's access to quality fruits and vegetables and other nutritious ingredients at affordable prices relieves the poor and distressed by reducing health issues caused by poor nutrition. Modern research has established a connection between the lack of access to fresh and nutritious food and significant health issues that are more prevalent in under-privileged neighborhoods. The U.S. Department of Agriculture created the designation of "food desert" to draw attention to the impact on the health and well-being of residents who lack access to affordable nutritious food. The Food, Conservation, and Energy Act of 2008 directed the U.S. Department of Agriculture to conduct a 1-year study of public issues related to "areas with limited access to affordable and nutritious food" - now referred to as "food deserts." The report, "Access to Affordable and Nutritious Food: Measuring and Understanding Food Deserts and Their Consequences," presented to Congress in June 2009, found that 11.5 million low-income people, or 4.1 percent of the total U.S. population, live in low-income areas more than 1 mile from a supermarket where access to affordable and nutritious food is limited. The report reviewed studies finding in general, "that better access to a supermarket is associated with reduced risk of obesity and better access to convenience stores is associated with increased risk of obesity." The report continues with a look at the Supplemental Nutrition Assistance Program (SNAP), the foundation of America's national nutrition safety net for low income families. "Access to a variety of high quality and affordable foods is essential to meet the program's mission of improving food security, reducing hunger, and providing access to a healthful diet and nutrition education." Of particular concern are households in "low-income urban neighborhoods where access to stores that offer such quality and variety at reasonable cost may be limited." Studies reported that households that did not shop mainly at a supermarket tended to purchase significantly smaller amounts of fruits, vegetables, and milk, which is a major dietary deficiency facing Americans, especially low-income Americans. The report pointed out that the price of nutritious food is also a factor in the quality of the diet in low income neighborhoods.

Exemption under Section 501(c)(3) is indispensable if you are to address the health and nutrition needs of the under-privileged residents and to meet the need for equitable access to healthy food. The grocery industry is highly competitive and operates with low gross margins and requires significant cash flow and debt burden. As a result, they must rely upon large volume sales or charge significantly higher prices to be profitable. Low-cost, high-volume supermarket stores average 43,000 square footage. The enormous facilities are necessary to generate the large revenue stream needed to maintain a profitable margin. Those stores serve a large number of customers in neighborhoods with high density that include moderate to higher income individuals. Nonprofit grocery stores like you are most often less than 7,000 square footage. They seek to serve a low-income clientele. The operators frequently lack grocery sector expertise and do not have ready access to investors and capital markets. Because non-profit markets serve impoverished neighborhoods and sell goods at below market value, their viability is dependent on donations and grants which will only occur if the non-profit entity has a 501(c)(3) designation. In some industries, business that buy and sell at discounted prices can still operate at a profit. The grocery industry is not one that can. The prices charged for items will not be set based upon a desire to make money. Instead, prices will be set to make the healthy items affordable. This will necessarily result in a shortfall in revenues necessary to cover the cost of operations. You cannot therefore sustain your operations without receiving grant funding, not even by keeping costs as low as possible, as you intend to do, by obtaining imperfect or surplus food items, using volunteers as part of the workforce, paying less than a fair market value rent (paying property taxes, insurance, utilities, etc., only, and not having to service the debt on your facility.

You believe that Rev. Rul. 73-127 is not an appropriate basis for concern in approving your application. This revenue ruling was issued in an era before "food desert" designations and before many of the grocery stores in indigent areas closed for lack of sustainability due to the declining economies in the areas and the slim profit margins caused by increased competition from large discount stores. You state that the revenue ruling is not law. It is simply a ruling by the IRS based upon circumstances and conditions as they existed in 1973. In 1973, obesity and diabetes were not national health issues costing our nation hundreds of millions of dollars. Since 1973, modern research and our understanding of human behavior, health issues and the impact of generational poverty, racial segregation and wealth disparity has evolved. Providing affordable and accessible healthy food options, along with nutrition education, can help to address the issues faced by the poor and underprivileged. You assert that your research of Guide Star indicates that since 2000, the IRS has approved 501(c)(3) applications for many smaller grocery markets with the charitable purpose of serving underprivileged areas in order to address health and well-being issues of low-income individuals living in food deserts with limited access to affordable nutritious foods. This awarding of 501(c)(3) status to many inner-city grocery stores serves as precedent and is more in line with current activities and purposes in the charitable arena than Rev. Rul. 73-127.

Our response to your position

You argued that Rev. Rul. 73-127's finding that that selling groceries at discount prices in a low income neighborhood does not serve a charitable purpose should be set aside in this case and a rash of determinations recognizing organizations engaged in food desert amelioration by such means should be preferred as precedents. Revenue Procedure 2019-5, 2019-1 I.R.B. 230 provides that we apply statutes, tax treaties, court opinions and guidance published in the Internal Revenue Bulletin when issuing our determination letters. Revenue Ruling 73-127 is a part of the guidance published in the Internal Revenue Bulletin. Further, IRC Section 6110(k)(3) of the Code states unless the Secretary otherwise establishes by regulations, a written determination may not be used or cited as precedent. Section 6110(b)(1)(A) provides that in general, the term "written determination" means a ruling, determination letter, technical advice memorandum, or Chief Counsel

advice. Therefore, your argument that other determinations should be treated as precedents rather than a revenue ruling is inconsistent with the statutory authority we must follow. Thus, Revenue Ruling 73-127 is controlling authority for purposes of our determination. Furthermore, your statement that its decision was based on situations occurring in 1973 is erroneous; it is based rather upon a historical review of the application of charitable law. The Revenue Ruling states clearly that “operating a grocery store is not recognized as a charitable purpose under the basic common law concept of charity and within the meaning of Section 501(c)(3) of the Code and Section 1.501(c)(3)-1(d)(2) of the regulations.”

Since you have been unable to adduce any legal precedent supporting your contention that alleviating conditions in a food desert is charitable as relieving poverty and distress, you have failed to carry your burden of establishing that your operations exclusively further purposes described in IRC Section 501(c)(3).

Conclusion

Because you do not meet the operational test of Treas. Reg. Section 1.501(c)(3)-1(c)(1), you do not qualify for exemption from federal income tax under Section 501(c)(3) of the Code.

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.

If you don't agree

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

- Your name, address, employer identification number (EIN), and a daytime phone number
- A statement of the facts, law, and arguments supporting your position
- A statement indicating whether you are requesting an Appeals Office conference
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization or your authorized representative
- The following declaration:

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

Under penalties of perjury, I declare that I have examined this request, or this modification to the request, including accompanying documents, and to the best of my knowledge and belief, the request or the modification contains all relevant facts relating to the request, 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 they haven'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 gave us a basis to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't given us a basis for reconsideration, we'll send your case to the Appeals Office and notify you. You can find more information 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 later because the law requires that you use the IRC administrative process first (IRC Section 7428(b)(2)).

Where to send your protest

Send your protest, Form 2848, if applicable, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Mail Stop 6403
P.O. Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Mail Stop 6403
Cincinnati, OH 45202

You can also fax your protest 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 they received it.

You can get the forms and publications mentioned in this letter by visiting our website at www.irs.gov/forms-pubs or by calling 800-TAX-FORM (800-829-3676). If you have questions, you can contact the person listed at the top of this letter.

Contacting the Taxpayer Advocate Service

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or if you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit www.taxpayeradvocate.irs.gov or call 877-777-4778.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements