



Department of the Treasury
Internal Revenue Service
Independent Office of Appeals

Number: **202144028**
Release Date: 11/5/2021

Date: **AUG 10 2021**

Person to contact:

Name:
Employee ID number:
Telephone:
Fax:
Hours:
Employer ID number:

Uniform Issue list (UIL):

501. 30-02
501. 35-00
501. 36-03

Certified

Mail :

This is a final adverse determination that you do not qualify for exemption from federal income tax under Internal Revenue Code (the "Code") Section 501(a) as an organization described in Section 501(c)(3) of the Code.

We made the adverse determination for the following reasons:

You have not demonstrated that you will be operated exclusively for charitable, educational or other exempt purposes as required by section 501(c)(3) of the Internal Revenue Code. Furthermore, you are organized and operated for the primary purpose of carrying on an unrelated trade or business. Additionally, your operations more than incidentally benefit the private interests of your founder and officer rather than public interests.

Contributions to your organization are not deductible under Section 170 of the Code.

You're required to file federal income tax returns on Forms 1120, U S Corporation Income Tax Return Mail your form to the appropriate Internal Revenue Service Center per the form's instructions. You can get forms and instructions by visiting our website at www.irs.gov/forms-pubs or by calling 800-TAX-FORM (800-829-3676).

We'll make this letter and the proposed adverse determination letter available for public inspection under Section 6110 of the Code after deleting certain identifying information We provided to you, in a separate mailing, Notice 437, Notice of Intention to Disclose. Please review the Notice 437 and the documents attached that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437.

If you decide to contest this determination, you can file an action for declaratory judgment under the provisions of Section 7428 of the Code in either:

- The United States Tax Court,
- The United States Court of Federal Claims, or
- The United States District Court for the District of Columbia

You must file a petition or complaint in one of these three courts within 90 days from the date we mailed this determination letter to you. Contact the clerk of the appropriate court for rules and the appropriate forms for filing petitions for declaratory judgment. You can write to the courts at the following addresses:

United States Tax Court	US Court of Federal Claims	US District Court for the District of Columbia
400 Second Street, NW	717 Madison Place, NW	333 Constitution Avenue, NW
Washington, DC 20217	Washington, DC 20005	Washington, DC 20001

Note: We will not delay processing income tax returns and assessing any taxes due even if you file a petition for declaratory judgment under Section 7428 of the Code.

You also have the right to contact the Taxpayer Advocate Service (TAS). 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 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 800-913-4688.

TAS assistance is not a substitute for established IRS procedures, such as the formal appeals process. TAS cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States Court.

If you have questions, contact the person at the top of this letter.

Sincerely,

Charles Rettig
Commissioner
By

Appeals Team Manager

Enclosures:

cc:



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

Date: September 15, 2020

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

X = State

Y = Date

Z = Individual

B = Title

C = Date

D = Date

F = Date

p dollars = Amount

q dollars = Amount

Ull :

501 30-02,

501 35-00

501.36-03

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 IRC Section 501(c)(3)? No, for the reasons stated below.

Facts

You were formed by a trust agreement in the state of X and funded on Y. Z is both your trustee and the donor.

The same day you were formed, Z granted you a Certain Exclusive Limited License for the film screenplay B which he wrote and copyrighted in his name. Specifically, you will hold certain license rights to B in order to raise funds to produce, promote and exhibit B. The initial term of the license ends on D; however this may be extended if you meet the following two key requirements:

- You must secure conditional charitable grants of q dollars to fund the production of B; and
- You must enter into an agreement with a Qualified Production Company. A Qualified Production Company is defined as a production company that has been the primary producer of at least two qualified films is defined as:

- a) A full length feature film of material historical accuracy;
- b) Having a budget of not less than _____ US Dollars (\$ _____), and
- c) Exhibited at more than one hundred theaters for a period of more than ten (10) consecutive weeks, measured from the date of wide release.

You plan to secure conditional grants to meet the requirements of the license by soliciting only very high net-worth individuals and large organizations, both for-profit and not-for-profit, to finance a highly professional production of B. In the event B is completed within the time period specified in the license, you will own the perpetual exclusive right to exhibit B. If these requirements are not met before the initial or any extended term, the license expires. The license does not apply to merchandising and soundtrack rights, which are reserved to be held by Z.

If B is made into a movie, the two key avenues of promoting it will be traditional broadcast and print media outlets. Your plan is to exhibit the movie to a mass audience on a broad and extended basis using multiple forms of distribution (theater, home video, etc.).

Any net proceeds from the movie will be used to provide financial support to soldier and/or youth charities. The support you will provide to charities is limited to the terms of an Exclusive Benefit Period which is defined in the trust agreement. This period begins at the commencement of the trust and ends on C. During the last year, you are required to donate a majority of your assets (no less than 80%) to charities. You will also install a member charity committee to determine to which charities donations are made.

Concerning adding more trustees, Z has the authority and ability to:

- Appoint one or more additional trustees;
- Reduce the number of trustees then serving, and
- Remove and replace any trustee, with or without cause.

You initially expect a majority of your revenue to come from donations. Expenditures are for producing and marketing B, professional fees, and Z's salary.

You finally wrote that Z commissioned reviews through a well-known film industry screenplay hosting site. B received positive reviews. Z also received strong positive comments from three nationally prominent historians who are experts in the area of history portrayed in B.

Law

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

Treasury Regulation (Treas. Reg.) Section 1.501(c)(3)-1(a)(1) states that, to be exempt as an organization described in IRC Section 501(c)(3), 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) 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 IRC Section 501(c)(3). 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 exempt purposes unless it serves a public rather than a private interest. It must not be operated for the benefit of designated individuals or the persons who created it.

In Revenue Ruling (Rev. Rul.) 60-351, 1960-2 CB 169, a corporation was organized and operated on a non-profit basis. It published a foreign language magazine containing fiction, poetry, book reviews and articles which it states was of a literary, scientific and educational character. The magazine was available to the general public through regular paid subscriptions. The corporation's income was derived mainly from subscriptions and sales of individual copies of the publication, and some was from advertising and contributions. Its expenditures consisted of fees paid to authors for their works, salaries, printing, advertising, shipping, packing, postage and other operating costs incurred in the publication of the magazine. It was devoted to publishing a magazine and selling it to the general public in accordance with ordinary commercial publishing practices. It was held that the corporation was not an exempt charitable, scientific, literary or educational organization within the meaning of IRC Section 501(c)(3).

In Rev. Rul. 77-4, an organization's only activities were preparing and publishing a weekly newspaper that presented local, national and world news, solicited advertising, and sold subscriptions. The Service held that the newspaper's activities were indistinguishable from ordinary commercial publishing practices.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U. S. 279 (1945), the Supreme Court concluded that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption under IRC Section 501(c)(3), regardless of the number and importance of truly exempt purposes.

In Fides Publishers Assoc. v. United States, 263 F. Supp. 924 (1967) the government retroactively revoked the taxpayer's exempt status, concluding that, for the previous five years, the taxpayer was engaged primarily, if not solely, in publishing activities. The court noted that, to qualify for IRC Section 501(c)(3) exemption, the taxpayer must be "organized and operated exclusively for" an exempt purpose. The court rejected the taxpayer's argument that, rather than its primary activity, the court should focus on the end to which that activity was taken, namely, religious education. The court pointed out that the taxpayer's sole activity and purpose was the carrying on of the publishing trade and held that the taxpayer's purpose, rather than its goals, were the focus of Section 501(c)(3).

In Harding Hospital, Inc. v. United States, 505 F.2d 1068 (6th Cir. 1974), the court held that an organization seeking a ruling as to recognition of its tax-exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute.

In Airlie Foundation v. IRS, 283 F. Supp. 2d 58 (D.D.C. 2003), the court laid out the factors for determining whether an organization's activity is of a commercial nature. These factors include competition with for-profit commercial entities; extent and degree of below cost services provided; pricing policies; reasonableness of financial reserves and use of promotional methods (e.g., advertising). Ultimately, it was determined that Airlie did not qualify for exemption under Section 501(c)(3) of the Code.

Application of law

You are not operated exclusively for one or more exempt purposes under IRC Section 501(c)(3) as described in Treas. Reg. Section 1.501(c)(3)-1(a)(1) because you fail the operational test.

You do not meet the provisions of Treas. Reg. Section 1.501(c)(3)-1(c)(1) because more than an insubstantial part of your activities is not in furtherance of an exempt purpose. For example, Z granted you a Certain Exclusive Limited License for the historical era film screenplay B which he wrote and copyrighted in his name in order to raise funds to produce it. The terms of the Certain Exclusive Limited License concerning the deadlines for raising funds as well as the fact that Z retains rights to merchandising shows you are operated for substantial nonexempt private purposes.

Furthermore, you are serving a substantial non exempt commercial purpose because of the manner in which you are planning to produce, distribute and promote the film if funding is obtained. This also causes you to fail the operational test under IRC Section 501(c)(3).

As required by Treas. Reg. Section 1.501(c)(3)-1(c)(2), you are not operated exclusively for exempt purposes because your net earnings inure to the benefit of Z. For example, you were formed by Z to raise money by soliciting donations to produce B into a movie and subsequently market it and distribute it. Z will retain rights for merchandising. In addition, your board consists of one person, Z, who controls all aspects of your operations and will benefit from your operations. This precludes exemption under IRC Section 501(c)(3).

You are not as defined in Treas. Reg. Section 1.501(c)(3)-1(d)(1)(ii) because you are operating for the private interests of Z. Z is the author of B, over which he has secured Federal Copyright protection. Z is using you as a vehicle to apply for grants to fund the production and associated costs with B. Further, the fact that Z is retaining rights to merchandising and the fact that licensing rights will revert back to Z if sufficient funding is not obtained, shows you are serving his private interests.

You are like the organizations denied exemption in Rev. Rul. 60-351 and 77-4 because if the funds are raised, you intend to produce and promote B in a manner similar to ordinary commercial filmmaking practices. B will be available to the general public for the cost of a movie ticket and advertised to the general public.

You are similar to the organization in Fides Publishers Assn. v. United States, which printed, published and sold products to promote religious culture. The organization argued, rather than focusing on its primary activity, the court should focus on the end to which that activity was conducted, namely religious education. You have indicated your purpose is to advance and promote history through funding, producing, promoting and distributing the movie based on B. Much like the organization in this case, you have a substantial nonexempt commercial purpose which precludes exemption under IRC Section 501(c)(3).

You are similar to the organization described in Better Business Bureau of Washington, D.C., Inc. v. United States. Although you may have some educational purposes, the presence of the non-exempt commercial and private purposes disqualify you from exemption under IRC Section 501(c)(3).

You are operated for a substantial nonexempt commercial purpose like the organization described in Airlie Foundation. For example, you sought reviews and comments from experts to determine if there would be a market for B. You plan to use broadcast and print media outlets to advertise B. You have not supplied any evidence of B being viewed free of charge but indicate you hope to distribute B through multiple means of

exhibition including regular for-profit theaters. This shows that you intend to compete with other films, regardless of their content.

Your position

You indicated that Z has extended the license agreement to date F. You also provided more details on how B is an educational endeavor because it is based on historical facts and dialogue as well as provided statements from renowned historical authors and experts praising the historical aspects of B. You also contend that the educational value of B outweighs any potential commerciality.

You addressed the commerciality factors that were expressed in Ailie. For example, your

- Indicated that there is no competition because films of this specific subgenre are nonexistent.
- Indicated that B would be financed by donations and not investments.

Additionally, your pricing policies as defined in the terms of the License, state that you are: (a) required to use your best efforts to facilitate viewing of B to high schools in the United States; and (b) encouraged but not required to exhibit B in theaters and open-air venues in the United States on or around the Fourth of July holiday, in perpetuity - in both cases at a discounted or preferably no fee.

You are required to use your best efforts to undertake an exclusive extended theatrical release of B as a completed film (exhibited in theaters) immediately upon B's completion. It is Z's firm belief that the completed film should be viewed by the citizenry in a communal setting.

You further stated that because at the time of this application, the film project is in its infancy, with no agreements for the production and distribution in place, you cannot in any meaningful way outline the terms of any theatrical release pricing policies. It is not certain that you will be in a position to control theatrical viewing pricing. However you are unlike (commercial) theatrical releases because any net profits resulting from the exhibition of B will ultimately be distributed to charities. All of these facts support and do not impair the case for exemption.

You went on to discuss the two-pronged test which consists of: 1) what is the purpose of the organization claiming tax-exempt status? and 2) to whose benefit does the activity inure?

Your operational goals are simple and finite: to (1) raise charitable funds sufficient to fully fund production of B; (2) make and exhibit B to as wide an audience as possible (including in American high schools); and (3) distribute substantially all of the revenues from B to designated charities within a reasonable time. This boils down to two benefits: education inuring to the people and financial support inuring to qualified soldier and youth charities. Any other claimed benefit must (a) be identified; (b) be real (not merely theoretical), and (c) be determined to be substantial, in order to render you undeserving of exemption.

Our response to your position

You have not provided any additional information from which it can be concluded that your activities exclusively further or advance a purpose described in IRC Section 501(c)(3). As previously described, you are operating for substantial nonexempt private and commercial purposes. Similar to the organization in Harding Hospital, Inc. v. United States, you have failed to provide sufficient information to prove to us that you are operating exclusively for purposes described in Section 501(c)(3).

Conclusion

Based on the information submitted, you are not operated exclusively for one or more purposes described in IRC Section 501(c)(3). You are operated for substantial nonexempt private and commercial purposes. Your net earnings also inure to the benefit of Z. Accordingly, you do not qualify for exemption under IRC Section 501(c)(3).

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 1428(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