



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **200644043**

Release Date: 11/3/2006

Date: 05/26/06

U.I.L. 501.06-01

501.06-02

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear _____ :

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(5). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, 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 Notice 437. If you agree with our deletions, you do not need to take any further action.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at

Information letter

1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely yours,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



tion letter

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**DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224**

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: 04/19/06

U.I.L. 501.06-01
501.06-02

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

B =

M =

N =

O =

m =

n =

Dear :

We have considered your application for recognition of exemption from Federal income tax under section 501(a) of the Internal Revenue Code. Based on the information provided, we have concluded that you do not qualify for exemption under section 501(c)(5) of the Code. The basis for our conclusion is set forth below.

The information submitted indicates that you were incorporated under the laws of the State of O on December 10, 2002. Your Articles of Incorporation state that your purpose shall be to assist in the education, development, and promotion of natural m and natural m products for the healthy use and consumption by members of the general public. You also will coordinate with natural m producers, packers, and distribution agents on a farm to market basis.

Your bylaws state that your initial Board of Directors shall be comprised of one member from M, a research and development n breeder and producer, one member from the m producers group, and one member from the m processors group, currently the Chief Executive Officer of N. N is a small full-line packer with extensive experience in the development and marketing of high-

quality m products, and is the sole representative from the processors group. N has a 25% interest in M. N has a contract through you to purchase n from M.

In your application, you state that your goals are to establish and enhance the profitability, competitiveness, and sustainability of member m producers. You state that these goals will be met through your formal establishment and, subsequently, through the development of a United States Department of Agriculture (USDA) process verified quality certification and marketing program for high-quality, branded, value-added m products produced by you. You state that you are unique in that each member producer remains completely independent – each being responsible for management, production, and marketing decisions. You also state that, specifically, a line of branded m products will be developed by you using the M Natural m label. The m used for the program will be produced according to your strict production regimen adopted by all your members. You state that you will obtain guaranteed price protection, significant and guaranteed price enhancement and market access for member producers via formal marketing contracts with N. In your letter dated December 23, 2004, you state that N has a 25% interest in M, and that N has a contract through you to purchase n from M. You also state that you do not have any material used to solicit members or explain your benefits. Potential members are identified as producers producing or with an interest in producing natural m. You state that, currently, no new producers have been solicited for membership in you.

You state in your application that feasibility and demand for the preliminary product has been effectively demonstrated through in-store product trials.

You state that your member producers were enrolled in your Certification Program. After enrollment, each of your member producers will be certified for production of live n. You state that certified producers will be guaranteed price support and enhancement, as well as market access. You also state that your President, B, (the representative from and managing partner of M) and your Vice-President (the representative from the producers group) will present each member producer with educational materials outlining the program specifications, after which B and an Extension Educator from the University of O with a Masters Degree in Agricultural Education, will conduct one-on-one sessions at each producer's farm. The Livestock Procurement Manager for N will coordinate the evaluation of carcasses for residues, cutability, and muscle quality for the certification process.

You state that your next activity will be to complete the product and to structure the marketing packages for primary market initiation. You have enlisted the assistance of the Marketing Director of N, in cooperation with marketing specialists from the University of O Department of Agriculture Economics. You state that N will manufacture all of the "Natural m" products for you. N will also be assisting with the development of further markets for the products, providing a portion of the marketing and advertising budgets.

You state that once the product has been test-marketed and a value has been established, sales presentations will be made to potential customers, both foreign and domestic. Those responsible will be your members, as well as B and your Vice-President, the Chief Executive Officer of N.

You state that the entire scope of the production of M “Natural m” will be documented and submitted to auditors at the Quality System Verification Program, a user-fee service provided by the USDA. B will be in charge of this verification audit which will verify genetic complement of the m, specifications for m quality, freedom from all artificial hormones, enhancers and antibiotics, ration specifications, and basic acceptable animal husbandry practices for each of your members. You state that the University of O is providing consulting personnel, marketing, and resource assistance.

In your letter dated December 23, 2004, you state that M is no longer a financial contributor to you and is in the process of being liquidated. The managing partner of M, B, no longer works for you. You also state that, previously, you focused most of your effort on genetic selection and carcass quality improvement, and that these efforts have been extremely successful. You state that your future time and resources will be directed toward the marketing of the final product, which is extremely important for your members. You state that, presently, marketing accounts for 60% of your time and 44% of your resources. Further, you state that your logo was derived from the M logo; your name was also derived from the M, which is near a physical location from which it took its name; currently, no licensing or branding agreements exist between M and you for the use of the name and/or logo.

Section 501(c)(5) of the Code provides for the exemption from federal income tax of labor, agricultural, or horticultural organizations.

Section 1.501(c)(5)-1(a) of the Income Tax Regulations provides that the organizations contemplated by section 501(c)(5) of the Code as entitled to exemption from income taxation are those which have no net earnings inuring to the benefit of any member, and have as their objects the betterment of the conditions of those engaged in such pursuits, the improvement of the grade of their products, and the development of a higher degree of efficiency in their respective occupations.

Rev. Rul. 56-245, 1956-1 C.B. 204, holds that an organization formed to encourage better and more economical methods of raising fur bearing animals, to provide an orderly system for marketing the pelts of its members, and to create a public demand for their products, and which carries out its purposes by furnishing members educational materials on the breeding and raising of fur bearing animals and the marketing of pelts, procuring agreements from auction companies to market the products of its members and furnish them certain beneficial services in connection therewith, and conducting advertising to encourage the use of fur products, is exempt under section 501(c)(5) of the Code.

Rev. Rul. 66-105, 1966-1 C.B. 145, discusses whether an organization composed of agricultural producers, whose principal activity is marketing livestock for its members, qualifies for exemption under section 501(c)(5) of the Code. The revenue ruling holds that the sale of members' products with the return to them of the sale proceeds, less expenses and reserves, is neither an object nor an activity within the ambit of section 501(c)(5). The principal purpose of the organization is to act as a sales agent for its members. Therefore, the organization does not meet the requirements under section 501(c) (5).

Rev. Rul. 70-372, 1970-2 C.B. 118, holds that an organization of agricultural producers formed to process individual farmer's milk production records for use in improving milk production does not qualify for exemption under section 501(c)(5) of the Code. The revenue ruling states that the processing of production and test records for individual farmers does not of itself better the conditions of those engaged in agricultural pursuits, improve the grade of their products, or develop a higher degree of efficiency in their operations. The services provided simply relieve the individual farmer of work that he would either have to perform himself or have performed for him.

Rev. Rul. 74-518, 1974-2 C.B. 166, clarifies and distinguishes Rev. Rul. 70-372, supra, and holds that a nonprofit organization of dairy farmers, a member of the National Cooperative Dairy Herd Improvement Program sponsored by the U.S. Department of Agriculture, that derives its income from testing fees and membership assessments and that weighs and tests milk of members' cows and makes statistical information based on the tests available to members, nonmembers, and governmental agencies for use in improving milk production is exempt as an agricultural organization under section 501(c)(5) of the Code. The organization described in Rev. Rul. 70-372 benefited only its own members and not dairymen in general.

Rev. Rul. 76-399, 1976-2 C.B. 152, holds that an organization of growers and producers of a particular agricultural commodity formed principally to negotiate with processors for the price to be paid to members of their crops and not act as a sales agent for its members is exempt under section 501(c)(5) of the Code.

Rev. Rul. 77-153, 1977-1 C.B. 147, holds that a nonprofit organization that owns and operates a livestock facility and leases it to local members of a nonexempt national association of farmers for use in implementing the association's collective bargaining program with processors does not qualify for exemption as an agricultural organization under section 501(c)(5) of the Code. The revenue ruling states that the operation and leasing of a facility for collecting, weighing, sorting, grading, and shipping of livestock, the organization's principal activity, is the providing of a business service to those members who make use of the national association's collective bargaining program. This service merely relieves the members of the organization of work they would either have to perform themselves or have performed for them.

The information you have submitted establishes that your primary activities center on the marketing of your members' agricultural product. This activity is relieving your members of work they would either have to perform themselves or have performed for them. See Rev. Rul. 77-153, supra. Where a service merely relieves members of work they would either have to perform themselves or have performed for them, an organization providing that service will not qualify for exemption as an agricultural organization under section 501(c)(5) of the Code. However, where individual benefits are incidental to the objectives of the program as a whole and the industry as a whole benefits, such incidental benefit will not preclude exemption. You are not similar to the organization described in Rev. Rul. 56-245, supra, because you are benefiting only your own members and not m producers in general, as discussed in Rev. Rul. 70-372, supra. Although you are working under a USDA process verified quality certification and marketing program for high-quality, branded, value-added products, you are not described in Rev. Rul. 74-518, supra, because you are engaged in the program solely for your own members, producers of a natural m product.

You state that your future time and resources will be directed toward the marketing of the final product. Sales activities can provide a unique direct benefit to members. Where the principal purpose of the organization is to act as a sales agent for its members, an organization will not qualify as an organization described in section 501(c)(5) of the Code. On the other hand, where the organization limits its activities to negotiating a price that is satisfactory to its members, exemption under section 501(c)(5) is available. You are not merely negotiating satisfactory prices for m, but rather you are acting as a sales agent for your members. Rev. Rul. 66-105, supra, holds that such an activity does not meet the requirements under section 501(c)(5) of the Code. The organization discussed in Rev. Rul. 76-399, supra, is recognized as exempt under section 501(c)(5) precisely because the organization is not acting as a sales agent for its members.

Accordingly, you do not qualify for exemption as an agricultural organization described in section 501(c)(5) of the Code and you must file federal income tax returns.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to this address:

Internal Revenue Service
TE/GE
1111 Constitution Ave, N.W.
Washington, D.C. 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely yours,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437