



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **200913068**
Release Date: 3/27/2009

Date: December 31, 2008

XXXXXX
XXXXXX
XXXXXX

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Uniform Issue List:
501.03-20

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)(3). 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.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. 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.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

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 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,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements

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



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: October 30, 2008

Contact Person:

XXXXXX
XXXXXX
XXXXXX

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

A = XXXXX

M = XXXXX

r = XXXXX

s = XXXXX

t = XXXXX

u = XXXXX

v = XXXXX

Dear _____ :

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

You were incorporated in M on r. You have five directors and one executive director. The executive director is the only person not also a director of A, a foreign non-profit that supplies you with materials for distribution in _____. The executive director is the only compensated director.

You state that you will sell mainly bibles, cards, engagement books, movies, T-shirts, and school products. Your purpose in selling these materials is bringing people closer to God by distributing religious products. In order to facilitate the sales of these materials, you maintain catalogs of merchandise. Those catalogs contain activities books, address books, bookmarks, car stickers, coloring books, finger puppets, greeting cards, interactive books, journals, minibooks, pocket cards, school labels, stickers, t-shirts, videos, DVD's, and writing papers. All of your catalog products are based around a cast of characters created by A. The catalogs do not contain bibles.

You will pay A seven percent of the billing of products whose rights belong to A. You also plan to make international licensing contracts claiming fifty percent of royalties paid thereunder for yourself and transferring the other fifty percent to A.

Your projected finances for _____ anticipate s out of t in total income will be from sales of your religious products. For _____ you expect that u out of y in total income will be from sales of your religious products. Your most recent financial statement shows that around 33 percent of your total income will go towards the cost of goods sold. You estimate that between four and ten percent of your gross profits will be reinvested in the organization. You also plan to donate about five percent of your religious materials to certain religious organizations. The remainder of your income will go towards salaries and other expenses.

Section 501(c)(3) of the Internal Revenue Code provides an exemption from taxation for organizations organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

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

Section 1.501(c)(3)-1(c)(1) of the regulations 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 activities 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.

Section 1.501(c)(3)-1(c)(2) of the regulations provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Section 1.501(a)-1(c) of the regulations defines private shareholder or individual as a person having a personal and private interest in the activities of the organization.

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

Better Business Bureau of Washington D.C., Inc. v. U.S., 326 U.S. 279 (1945) holds that the presence of a single non-exempt purpose, if substantial in nature, will preclude exemption, regardless of the number or importance of statutorily exempt purposes.

In Scripture Press Foundation v. United States, 285 F.2d 800 (1961), the Court of Claims considered whether the sale of religious literature was incidental to the stated purpose of stimulating growth in Sunday schools in the United States or vice versa. The organization in that case consistently spent between three and five percent of its yearly accumulated profit on actual

religious education. The court found that the organization was primarily engaged in the sale of religious literature and that its purpose of stimulating Sunday school growth was incidental to that commercial activity. As a result, the court held that the organization was not entitled to exemption.

In Christian Manner International, Inc. v. Commissioner, 71 T.C. 661 (1979), the Tax Court considered whether an organization whose stated purposes were, *inter alia*, to teach and promulgate the gospel of Jesus Christ, to develop and maintain a Christian seminar center and international headquarters, to make direct application of the corporation's funds in the aid and assistance of those considered to be in need or infirm, to contribute to institutions which seek to evangelize and disciple, to provide scholarships or other assistance for worthy and indigent students, to share by media presentation the claims of the gospel of Jesus Christ was exempt for income tax under section 501(c)(3) of the Code. The organization sold religious materials and conducted ministries based on those materials, but the ministries were only conducted by request of interested parties and more emphasis was placed on the creation of materials. The court found that the organization's primary activity was the publication and sale of books written by its founder which were religiously inspired and oriented but were sold commercially. The court concluded that the organization was not exempt under section 501(c)(3) of the Code because it engaged in impermissible private benefit to its founder.

In Rev. Rul. 68-306, 1968-1 C.B. 257, an organization that primarily published a newspaper containing news, articles, and editorials relating to religion was held to qualify for exemption. The organization in question was not operated in a commercial manner. The newspaper was distributed on a subscription basis, but the income from subscription sales did not cover the cost of the newspaper. As such, the organization relied on contributions for its continued operation. Furthermore, none of the organization's earnings inured to the benefit of any private shareholder or individual.

You are operated in a manner similar to that of the organization in Scripture Press. You donate only five percent of your religious materials. The remaining 95 percent are sold at a profit. You do not conduct any other activities. Therefore, although the religious material that you sell may incidentally promote spirituality, your primary activity is the sale of these materials. Such sales cannot be meaningfully distinguished from commercial sales of religious materials and do not constitute an exempt function.

You are also operated in a manner similar to the organization in Christian Manner. The organization in that case focused primarily on the sale of literature and materials created by its founder. This resulted in impermissible private benefit to the founder. Similarly, your catalogs offer items for sale that are the creations of A and A receives payments from you based directly on the amount of those items that you sell. Thus, this arrangement results in impermissible private benefit to A. Accordingly, you have failed to demonstrate that you are operated exclusively for exempt purposes. See Better Business Bureau, *supra*.

Your operations are distinguishable from the organization described in Rev. Rul. 68-306. That organization is not operated in a commercial manner. In contrast, you sell items at a profit and you reinvest four to ten percent of your profit in your business. That organization depended on contributions to maintain operations. But, you need only the profit from the items that you sell to remain viable. Finally, none of that organization's earnings inured to the benefit of any private shareholder or individual. Your net earnings may not inure to the benefit of any private

shareholder or individual, however, your sales of A's intellectual property and the royalty payments resulting from those sales amount to impermissible private benefit. In this way, you do not fit within the description of an exempt organization that conducts religious publishing provided by Rev. Rul. 68-306.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

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.

Your protest statement should be accompanied by the following declaration:

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

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 file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

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:

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.

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

Sincerely,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements