

INTERNAL REVENUE SERVICE
District Director
2 Cupania Circle
Monterey Park, CA 91755

DEPARTMENT OF THE TREASURY
Western Key District

CERTIFIED MAIL

Date SEP 15 1998

Employer Identification Number:
[REDACTED]

Case Number:
[REDACTED]

Person To Contact:
[REDACTED]

Telephone Number:
[REDACTED]

Refer Reply to:
[REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code (Code).

FACTS:

The information submitted with your application discloses that you were incorporated [REDACTED]. Prior to incorporating you were an unincorporated organization governed by a set of by-laws.

Your Articles of Incorporation state the purposes of your organization in part, as follows:

"To create, form, and establish a club for those interested in the collection of casino chips and gaming tokens; to stimulate, encourage and promote public interest in the collection of casino chips and gaming tokens; to organize, sponsor and arrange fairs, shows, and exhibitions of such collectibles; to encourage the creation of social clubs for those interested in collecting casino chips and gaming tokens, to advance the appreciation of collecting casino chips and gaming tokens by conducting meetings, discussions, seminars and workshops on issues related to collection practices; to [REDACTED] public concerning the value, and gaming tokens..."

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10-23-98

- 2) Monthly newsletter which provides local information regarding old and current casino chips and gaming tokens. The newsletter is free to dues paying members.
- 3) The organization provides copies of [REDACTED] free to dues paying members.

In response to our letter dated [REDACTED] requesting a breakdown of your activities and the time spent on each activity, you provided the following:

- 1) General business meeting - approximately [REDACTED] minutes
- 2) Educational - guest speakers, new and future releases - approximately [REDACTED] minutes to [REDACTED] hours.
- 3) Auction - members consign approximately [REDACTED] chips per meeting. Members who consign chips are paid [REDACTED] percent of the proceeds from the auction, the organization retains only [REDACTED] percent. Approximately [REDACTED] minutes is spent on this activity.
- 4) Social - includes a 50-50 drawing. At each meeting, tickets are sold for \$[REDACTED] each towards a drawing. The winner and the organization split the proceeds. Approximately 15 minutes is spent on this activity.

In addition to your monthly meeting, your members participate in collectible shows that are held in malls or convention facilities. These collectible shows are organized and promoted by other entities.

You have recruited a historian who will develop and maintain exhibits and a gaming related library which will be available to anyone interested in the subject.

You provided financial information in your application for tax year 1997 which was before you were incorporated as a non-profit organization. You provide projected budgets for 1998 and 1999.

Your sources of income are as follows:

<u>INCOME:</u>	<u>1997</u>			
		1	[REDACTED]	[REDACTED]
Member Dues	\$[REDACTED]	\$	[REDACTED]	[REDACTED]
(1) Chip Auction	[REDACTED]	\$	[REDACTED]	[REDACTED]
50-50 Drawing	[REDACTED]		[REDACTED]	[REDACTED]
(2) Our Bar Promotion	[REDACTED]		[REDACTED]	[REDACTED]
Donations	[REDACTED]		[REDACTED]	[REDACTED]
<u>TOTAL</u>	<u>\$[REDACTED]</u>			
(1) Auction Consignments	(\$[REDACTED])	(\$	[REDACTED]	[REDACTED]
(amount of Chip Auction			[REDACTED]	[REDACTED]
revenue paid to members			[REDACTED]	[REDACTED]
whose chips were auctioned)			[REDACTED]	[REDACTED]

- (2) Our Bar Promotion was a one time event. A member secured the casino chips of a dissolved casino. Th chips were sold to members and the organization retained all the proceeds.

The financial information shown above indicates that approximately [redacted] percent of the organization's income for 1997 (not including the income from Our Bar Promotion which was an unusual event) was generated from the Chip Auction activity. The projected budgets for 1998 and 1999 show that [redacted] percent and [redacted] percent respectively will be generated from the Chip Auction activity.

ISSUE:

Is the organization organized and operated exclusively for Code section 501(c)(3) purposes or are they operated primarily for the benefit of their members?

LAW:

Section 501(c)(3) of the Code describes certain organizations exempt from income tax under section 501(a) and reads in part as follows:

..."(3) Corporation, and any community chest, fund or foundation 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 (but only if no part of its activities involve the provision of athletic facilities or equipment), 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, no substantial part of the activities of which is carrying on legislation, (except as otherwise provided in subsection h), and which does not participate in, or intervene in (including the publishing or distribution of statements), any political campaign on behalf of any candidate for public office."

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

Section 1.501(c)(3)-1(c)(1) of the Regs 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 exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities are not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the Regs 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 Regs defines "private shareholders or individuals" as an individual having a personal and private interest in the activity of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regs provides that an organization is not organized and operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirements of this subdivision, 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 creators, shareholders of an organization or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-1(d)(3) of the Regs defines the term "educational" as relating to (a) the instruction or training of the individual for the purpose of improving or developing his capabilities or (b) the instruction of the public on subjects useful to the individual and beneficial to the community."

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279 (1945), the Supreme Court interpreted the requirement in section 501(c)(3) that an organization be "operated exclusively" by indicating that in order to fall within the claimed exemption, an organization must be devoted exclusively to exempt purposes. The Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

In Retreat in Motion v. Commissioner, TC Memo 1984-315, the Court held an organization, created by a group of local churches to operate a bus ministry for church youth in which the youth would learn about their belief through travel and adventure, was not operated "exclusively" for educational purposes. The Court held that the "recreational activities" appear(ed) so extensive that we cannot consider them insubstantial and incidental to the religious purpose of the trip."

In Puritan Church of America v. Comm., (1953, Dist Col) 209 F2d 3-6, 53-2 USTC section 9601, 45 AFTR 119 cert den (1954) 347 US 975, 9898 L ED 1115, the court found that an organization is disqualified if it serves private rather than a public interest. It must therefore establish that it is not organized or operated for the benefit of private interest such as designated individuals, the creator of the organization or his family, shareholders, or persons controlled (directly or indirectly) by such private interest, and the accomplishment of the exempt purpose must not be accompanied by personal, private or selfish consideration.

In Human Engineering Institute, TC Memo 1978-145, affd (1980, CA6) 629 F2d 1160, 90-2 USTC section 9600, 46 AFTR 2d 80-5479; Kenner Williams v. Comm., (1963-CA7) 318 F2d 632 63-2 USTC section 9519, 11

AFTR 2d 1596; and Gondia Corp. TC Memo 1982-422 all affirm that an organization is not organized and 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.

Revenue Ruling 67-139, 1967-1 C.B. 129, discusses how an organization whose membership consists primarily of amateurs and hobbyists interested in geological, mineralogical, and lapidary activities, qualifies for exemption under section 501(c)(3) of the Code. The activities of the organization were primarily educational: lectures, discussions, field trips, and shows to which the general public are invited. The income of the society was from member dues and from a gem and mineral show. Disbursements were for office and club expenses. None of the net earnings of the organization inured to the benefit of any of the members. The ruling holds that the organization is organized and operated exclusively for educational purposes.

In Revenue Ruling 69-175, 1969-1 C.B. 149, held that an organization formed by parents of pupils attending a private school that provides school bus transportation for its members' children served a private rather than a public interest. Revenue Ruling 69-175 states in pertinent part, as follows;

"When a group of individuals associate to provide a cooperative service for themselves, they are serving a private interest."

Revenue Ruling 71-395, 1971-2 C.B. 228, held that an organization formed by a group of artists for the purpose of exhibiting and selling their works served a private rather than a public interest. Revenue Ruling 71-395 states in part as follows:

"The cooperative gallery in this case is engaged in showing and selling only the works of its own members and is a vehicle for advancing their careers and promoting the sale of their work. It serves private purposes of its members, even though the exhibition and sale of paintings may be an educational activity in other respects."

ANALYSIS:

All of the preceding Code sections, Regulation sections, Revenue Rulings, and Court cases describe the criteria under which an organization may be exempt under section 501(c)(3) of the Code. They also describe the basis for which organizations were denied exemption because of private benefit to members and because the organizations were not organized and operated exclusively for educational purposes.

Our analysis of your application indicates that you may have some educational activities within the meaning of Code section 501(c)(3), such as having a guest speaker at your monthly meetings and maintaining exhibits we find that more than an insubstantial amount of your activities are directly inuring to the benefit of your members and are not "educational."

Your business meetings, auctions, social portions of your meetings and your newsletters are not educational under Code section 501(c)(3). You give no breakdown of your newsletter, library, etc. but both activities are for the private benefit of your members. Your newsletters are full of information for your members and your library has never been publicized to the general public. You did not submit the number of members in your organization but judging from income and the amount of dues you have at least [REDACTED] and maybe more members. You show only [REDACTED] nonmembers present at any given meeting and those that are present cannot participate in all activities. You are not operated for the benefit of the public but for the benefit of your members.

Because you have a substantial non-exempt purpose of assisting members in the sale of their gaming tokens you are operated for more than an insubstantial purpose of serving the private interests of your members. The amount of your organization's time and resources spent on the auction of member's coins indicates that you are not organized and operated exclusively for an exempt purpose pursuant to section 1.501(c)(3)-1(c) and 1.501(c)(3)-1(d)(1)(ii) of the Regs. By failing to meet the operational test for exemption, you are not exempt under section 501(c)(3) of the Code. You refused consideration as an organization described in Code section 501(c)(7).

CONCLUSION:

To be considered for tax exempt status under Code section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in that Code section. Also, its activities must be restricted to those permitted a section 501(c)(3) organization. Based on the information submitted, it is the position of the Internal Revenue Service that you are not entitled to exemption from Federal income tax as an organization described in Code section 501(c)(3), inasmuch as you are not organized and operated exclusively for any of the specified purposes within that Code section but are operated exclusively for the private benefit of your members. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with this proposed determination, we request that you sign and return the enclosed Form 6018. Please note the instructions for signing on the reverse side of the form.

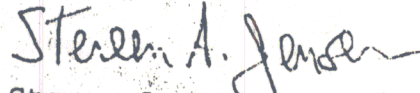
If you are not in agreement with this proposed determination, we recommend that you request a hearing with our office of Regional Director of Appeals. Your request for a hearing should include a written appeal giving the facts, law, and any other information to support your position as explained in the enclosed Publication 892. You will then be contacted to arrange a date for a hearing. The hearing may be held at the office of Regional Director of Appeals, or, if you request, at a mutually convenient District office.

If we do not hear from you within 30 days from the date of this letter, and you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service

as a failure to exhaust available administrative remedies and will then become our final determination. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that, "A declaratory judgement or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If you have any questions, please contact the per whose name appears on the heading of this letter.

Sincerely,



Steven A. Jensen
District Director

Enclosure(s):
Form 6018
Publication 892

Department of the Treasury-Internal Revenue Service
Consent to Proposed Adverse Action
(All references are to the Internal Revenue Code)

Prepare In
Duplicate

Case Number [REDACTED] Date of Latest Determination Letter

Employer Identification Number [REDACTED] Date of Proposed Adverse Action Letter

Name and Address of Organization
[REDACTED]
[REDACTED]
[REDACTED]
[REDACTED]

I consent to the proposed adverse action relative to the above organization as shown by the box(es) checked below. I understand that if Section 7428, Declaratory Judgments Relating to Status and Classification of Organizations under Section 501(c)(3), etc. applies, I have the right to protest the proposed adverse action.

NATURE OF ADVERSE ACTION

- Denial of exemption as an organization described in Internal Revenue Code Section 501(c)(3).
- Revocation of exemption, effective
- Modification of exempt status from section 501(c)() to 501(c)(), effective
- Classification as a private foundation (section 509(a)), effective
- Classification as a non-operating foundation (section 4942(j)(3)), effective
- Classification as an organization described in section 509(a)(), effective
- Classification as an organization described in section 170(b)(1)(A)(), effective

If you agree to the adverse action shown above, please sign and return this consent. You should keep a copy for your records.

If you sign this consent before you have exhausted your administrative appeal rights, you may lose your rights to a declaratory judgment under section 7428.

(Signatures instructions are on the back of this form.)

Name of Organization

Signature and Title Date

Signature and Title Date