

Refer. Reply to:

CERTIFIED

Section 501(c)(3) of the Code provides for the exemption from Federal Income Tax of corporations organized and operated exclusively for religious, charitable, literary, scientific, and educational purposes; no part of the net earnings of which inures to any private shareholder or individual.

Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
	9/18/85	9/4/85	10-7-85	10-10-85		

For Approval and Clearance Department of the Treasury Internal Revenue Service

Section 1.501(c)(3)-1 of the Tax Regulations relates to the definition of the organization and operation of organizations described in Section 501(c)(3). It is quoted, in part, as follows:

"(a) Organizational and operational tests. (1) 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 such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt. (2) The term "exempt purpose or purposes", as used in this section, means any purpose or purposes specified in Section 501(c)(3)...."

"(b) Operational test. (1) Primary activities. 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). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. (2) Distribution of earnings. 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(c)(3)-1(a) of the Income Tax Regulations provides that in order to be exempt as an organization described in Section 501(c)(3), the organization must be one that is 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 or the operational test it is not exempt.

Section 1.501(c)(3)-1(a)(1) of the Income Tax 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 purposes specified in 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."

Section 1.501(c)(3)-1(d)(1)(i) of the Income Tax Regulations provides that an organization is not organized and operated exclusively for exempt purposes unless it serves a public rather than a private interest. Thus, it is necessary for an organization seeking exemption under Section 501(c)(3) 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.

An organization formed to purchase groceries for its membership at the lowest possible prices on a cooperative basis was held not exempt as a social welfare organization under Section 501(c)(4) of the Code. (Revenue Ruling 75-349, 1975-2 C.B. 179)

Your organization does not meet the operational test of Section 501(c)(3) of the Code because you are operated for the benefit of your members.

The holding of the aforementioned revenue ruling was based on the conclusion that the organization in question was operated primarily for the private benefit of its members and any benefits to the community were deemed not sufficient to meet the requirements of the regulations under Section 501(c)(4) of the Code that the organization be operated primarily for the common good and general welfare of the community.

Even though the subject of the revenue ruling was an organization who applied under 501(c)(4) rather than 501(c)(3) of the Code, the rationale for the denial is appropriate for both Code sections.

The community as a whole does not benefit. This is true even if the membership is open to anyone. Obtaining food on a cooperative basis in order to reduce cost to your membership is not an acceptable activity under Section 501(c)(3) of the Code because it serves the private interests of your membership.

Accordingly, we have concluded that you are not entitled to recognition of exemption from Federal Income Tax under Section 501(c)(3) of the Code, since you are not organized and operated exclusively for charitable, religious, or other exempt purposes within the meaning of Section 501(c)(3).

You are required to file Federal Income Tax Returns.

Contributions made to you are not deductible by the donors as charitable contributions as defined in Section 170(c) of the Code.

If you do not agree with these conclusions, you may within thirty days from the date of this letter, file a brief of the facts, law and arguments (in duplicate) which clearly sets forth your position. In the event you desire an oral discussion of the issues, you should so indicate in your submission.

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A conference will be arranged in the Regional Office after you have submitted your brief to the Chicago District Office and we have had an opportunity to consider the brief and it appears that the conclusions reached are still unfavorable to you. Any submission must be signed by one of your principal officers. If the matter is to be handled by a representative, the Conference and Practice Requirements regarding the filing of a power of attorney and evidence of enrollment to practice must be met. We have enclosed Publication 892, Exempt Organization Appeal Procedures for Adverse Determinations, which explains in detail your rights and procedures.

If 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. Section 7425(b)(2) of the Internal Revenue Code provides in part that "A declaratory judgment 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."

Please keep this determination letter in your permanent records.

If you agree with this determination, please sign and return the enclosed Form 6018.

Sincerely yours,

[REDACTED]
District Director

Enclosures:
Publication 892
Form 6018