

INTERNAL REVENUE SERVICE

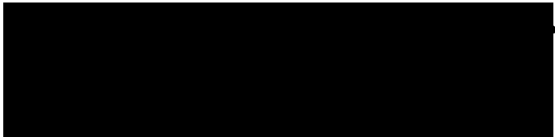
DEPARTMENT OF THE TREASURY

Southwest Region



Date: 18 FEB 1987

CERTIFIED MAIL



Form Number:
1023

EIN:

Person to Contact:

Telephone Number:

Refer Reply to:

Dear Sir/Madam:

This is a final adverse determination with respect to your exempt status under Section 501(c) (3) of the Internal Revenue Code.

The primary purpose and function of your organization is to provide childcare for the benefit of shoppers and merchants at the . While some of your activities may be educational in nature, a substantial amount of the activities are not educational. You do not qualify for exemption under IRC 501(a) as an educational organization described in IRC 501(c) (3).

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

You are required to file Federal Income Tax returns with your Key District Director for exempt organization matters for taxable years for which the filing date of the appropriate return has passed. These returns should be filed within 30 days of the date of this letter, unless a request for extension of time is granted. Please send them to the attention of the EP/EO Division, attach a copy of this letter, and address any requests for time extensions to the EP/EO Division. Processing of an income tax return and assessing any taxes due will not be delayed because a petition for a declaratory judgement has been filed under Section 7428 of the Internal Revenue Code.

We will notify the appropriate State officials, as required by Section 6104(c) of the Code, that based on the information we have available, we are unable to recognize you as an organization described in Section 501(c) (3) of the Internal Revenue Code for the period mentioned.

If you decide to contest this determination in court, a petition for a declaratory judgement proceeding in the United States Tax Court, the United States Court of Claims, or the United States District Court for the District of Columbia must be filed within 90 days from the date this determination was mailed to you. Contact the Clerk of the appropriate court for rules for filing petitions for declaratory judgement section of the enclosed Publication 892.

[REDACTED]

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

Thank you for your cooperation.

Sincerely yours,

[REDACTED]
Associate Chief, Appeals

Enclosure:
Publication 892

JUN 18 1985

[REDACTED]
[REDACTED]
[REDACTED]

July 23, 1985

[REDACTED]

Ladies and Gentlemen:

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

A review of the information submitted reveals that you incorporated under the [REDACTED] Nonprofit Corporation Act on [REDACTED]. You are organized exclusively for educational purposes. Your stated purpose and function is to work with childcare professionals, nonprofit organizations and local governments to initiate programs which will address the unmet needs for quality childcare services in the [REDACTED] community.

In your application, you indicate that you have targeted areas of child care need which you plan to fulfill. These are sick care for children whose parents are unavailable by reason of work or school, infant and toddler learning and care, part-time learning and care, drop-in learning and care, learning and care facilities for the periods before and after school, and support services for the so called "latch-key" children. You state that your only operation at this time is your day care center which offers part-time and drop-in care and is located at the [REDACTED] in [REDACTED], and is known as the [REDACTED] ([REDACTED]).

[REDACTED] provides an experiential learning facility for children from the ages of one and one-half to eight years. It began operations in [REDACTED]. [REDACTED] is run as a part-time care facility, in that it is the policy of the Center to accept a child for care in the Center no more than [REDACTED] hours per week. Of the spaces available for toddlers (to age two and one-half), [REDACTED] percent are available to parents on a contract (pre-arranged basis), and [REDACTED] percent of the total hours per week for pre-school children are available by reservation.

In your letter of [REDACTED], you provided the following information. For the period between [REDACTED], and [REDACTED], you served [REDACTED] children from [REDACTED] families for a total of [REDACTED] visits totaling [REDACTED] hours. [REDACTED] percent of the children were from families in which both parents were

Code	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
		[REDACTED]	[REDACTED]				
Surname		[REDACTED]	[REDACTED]				

employed. [REDACTED] visits were made in order that the parents might keep appointments (medical, dental, job interviews, etc.) or to attend meetings. [REDACTED] visits were made to go shopping. [REDACTED] visits were for "other" purposes (such as time-off, job search efforts, housing securement, etc.). The parents are required to specify their destinations on the drop-in form for drop-in visits. You did not provide the purposes of the remaining [REDACTED] visits.

Your educational philosophy is that children can have learning experiences at any time, and sustained, repeated instruction is not necessarily required for every learning experience. Your curriculum is designed to meet the educational philosophy of the program which stresses the developmental needs of children, i.e., physical, mental, emotional, and social needs. The daily schedule allows for indoor and outdoor physical activities such as climbing, digging, swinging and skipping, dancing and obstacle courses. Group time activities provide opportunities for language and listening skills to develop through such activities as story telling, book reading, singing, and rhyming games. You regularly schedule visits from the pet store. That the care of the plants and animals in the room are scheduled into the science portion of the curriculum.

You believe that each hour of the day will provide a learning experience for the children. Although some of the care given at [REDACTED] is referred to as "drop-in" the mere fact that the care has not been pre-arranged or is not on a regular basis does not mean that the time spent in the Center is any less educational or learning related. Your [REDACTED] Center is open to all children in the [REDACTED] area. You have a regular faculty comprised of college educated individuals with backgrounds in child care and child development. You are licensed by the State of [REDACTED].

You estimate that [REDACTED] to [REDACTED] of the parents who use the [REDACTED] Center use it for day care which thereby enables them to have part-time employment. Other parents use the [REDACTED] Center not as a regular day care service which allows them to be gainfully employed, but rather as "fill-in" and contingent day care service which allows them to work their regular schedule and have day care when the regular day care providers are sick or unable to be there, or for Saturdays or holidays when regular day care may not be available. Also, the flexibility of the [REDACTED] Center allows both full and part-time students at the University of [REDACTED] to have day care for their children on a basis that coincides with their irregular schedules.

On [REDACTED], you entered into a contract with the City of [REDACTED] under which the City was to provide certain accounting and payroll services for you. The following statement appears in that contract:

[REDACTED] operates the [REDACTED] at [REDACTED] to provide "drop-in" child care for shoppers and related services.

On [REDACTED], you entered into a lease agreement with the City of [REDACTED], wherein you leased the facilities used for your [REDACTED]. The facilities are described as, "the building, playgrounds, and related facilities on the premises were constructed, and are operated and supplied partly with money provided by the landlord, and they were designed to be used to provide "drop-in" day care for children of shoppers at the [REDACTED], and on some occasions, of individuals employed at [REDACTED], in order to provide child care and support child care activities for the citizens of the City of [REDACTED]."

Another provision of the lease agreement states, "Landlord desires to lease to Tenant, and Tenant desires to lease from Landlord, the premises to be used to provide "drop-in" day care for the children of the shoppers at [REDACTED], and some related services, e.g., occasional care for the children of individuals employed at [REDACTED]."

Section 4.1 of the lease states, "Limitation on Use and Obligation of Use. Tenant shall use and occupy the premises only for the operation of a "drop-in" day care center for children of shoppers at [REDACTED] on a temporary basis while they are shopping or otherwise using the facilities at [REDACTED]. At the Tenant's discretion, care may also be provided to the children of individuals employed at [REDACTED]." Section 10.1 of the lease provides, "Defaults Defined. The following shall constitute defaults of Tenant hereunder....(g) Failure by Tenant to continuously provide "drop-in" day care from the premises as specified in Subparagraph 4.1."

In section 11 of the Lease Agreement, reference is made to Landlord's Lease With Owner which was entered into on [REDACTED]. The owner being [REDACTED], and the landlord being the city of [REDACTED]. On [REDACTED], we requested a copy of this lease. Your response indicated there was no lease in effect between the city of [REDACTED] and the Mall at that time.

In your letter of [REDACTED], you state, "The lease agreements dated [REDACTED] and [REDACTED], state that [REDACTED] must provide drop-in child care for the children of shoppers at the Mall and services for Mall employees. This wording was included to ensure the [REDACTED] that the Center would indeed benefit the entire Mall redevelopment effort. Because the funds provided for the building of the [REDACTED] were tied to the redevelopment of the Mall, the City Attorney felt it important to ensure in the lease that a portion of the Center's program would serve Mall interests. Minutes of [REDACTED] City Council meetings reflect the Council's interest in ensuring that the Center provide a high quality educational program for toddlers and preschoolers throughout the entire community.

[REDACTED] is distinguished from other facilities located in commercial shopping areas in a number of ways. As the only licensed, flexible-time educational program in existence in [REDACTED] County it offers a regularly scheduled curriculum of high quality taught by a regular faculty to both a student body of regularly enrolled children (utilizing over 50% of the current hours) and to the drop-in student. This curriculum is accessed by all children attending the Center regardless of the activities of their parents during their stay. In contrast to other facilities offering part-time flexible services, [REDACTED] maintains a developmentally oriented curriculum which focuses on various developmental areas to enhance each child's learning and growth rather than providing a mere custodial service. Although custodial care is implicit and necessary to ensure the safety and health of each child during their stay, it is not a substantial part of the Center's operations. As a licensed center employing only qualified and certified faculty, and meeting specific rigid physical environmental criteria mandated by the State of [REDACTED] licensing regulations, [REDACTED] is able to offer educational part-time programs to children throughout the community regardless of their parents destination during their child's stay. In contrast to other facilities offering part-time flexible services, [REDACTED] maintains a developmentally oriented curriculum which focuses on various developmental areas to enhance each child's learning and growth rather than providing a mere custodial service. Other childcare facilities operating as commercial non-licensed centers in shopping malls as a convenience to shoppers must restrict their attendance to children whose parents remain in the mall during their stay. They provide only custodial care with the parent or guardian on-site at all times."

You state that you offer high quality, educational day care to large segment of the local population that is unable to secure a part-time educational experience for their children elsewhere in the community. You have a regularly scheduled curriculum designed to enhance each child regardless of the activities of the parents while the child is enrolled. Your regular faculty is composed of highly trained professionals. You state that over [REDACTED]% of your daily operating hours are utilized by pupils enrolled in the permanent part-time program, and that these children constitute a regularly enrolled and attending student body. Your services are not dependent on the financial status of the parents of the children in your care.

[REDACTED] agreed to produce and provide to the public, tokens worth [REDACTED]¢ off of the fee for a visit to your Center. The Association reimburses you directly for every [REDACTED]¢ token submitted. The tokens are available to anyone, no purchase necessary, and they are not dated and may be used at any time. Patronizing the mall facilities and stores is not a requirement.

In your newsletter, "[REDACTED]", you advertise the various activities to be conducted at the Center for the month. Several days each month are noted as "Mall Discount Day" or "Grocery Discount Day". On the Mall Discount day,

parents present a receipt from the [redacted] merchant for the second hour of child care free. On the Grocery Discount Day, parents present a receipt from a grocery purchase for the second hour of child care free. In your [redacted] issue, you encourage readers to "bring your children in for special fun while you shop for outstanding savings in the Mall stores. Bring us a Mall merchant receipt (dated for day of [redacted] visit) and receive \$[redacted] off your total child care bill. "In the [redacted] issue, you state, "We are also planning to expand our services! Beginning Thanksgiving weekend ([redacted]) the [redacted] will be open on Sunday's to better accommodate holiday shoppers."

"Many special events have already been scheduled for [redacted] and [redacted]. Please check our attached calendar and plan now which events your children will most enjoy while you shop in peace, take a break from it all to have lunch with a friend, see a movie or treat yourself to some other type of "time-out".

"Gift Idea? Suggest a [redacted] Gift Certificate for your family. These gift certificates come in \$[redacted], \$[redacted] and \$[redacted] denominations and will give hours of fun for your children and hours of relaxation for you."

In the [redacted] issue, you state, "We hope that parents take advantage of our discount price specials. Plan your special activities around the calendar of events from the [redacted]. Take a leisurely lunch with a friend. See a favorite matinee movie. Keep a dental appointment. Or just use the time to read a good book. Enjoy! Your children will have fun playing with the other children at the [redacted] while you take time for yourself."

You also submitted several letters of recommendation from child care professionals and members of the community regarding the high quality of care and programs that you offer.

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

"(3) Corporations, *** fund, or foundation, organized and operated exclusively for religious, charitable, scientific, *** literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involved the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the

publishing or distributing of statements), any political campaign on behalf of any candidate for public office."

Section 1.501(c)(3)-1 of the regulations provides, in part, as follows:

"(a)(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."

"(c)(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."

"(d)(1)(ii) An organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. Thus, to meet the requirement 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 creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests."

"(d)(2) Charitable defined. The term "charitable" is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of "charity" as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency. "

"(d)(3)(i) In General. The term "educational", as used in section 501(c)(3), relates 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.

Section 501(k) of the Code states that for purposes of section 501(c)(3), the term "educational purposes" includes the providing of care of children away from their homes if 1) substantially all of the care provided by the organization is for purposes of enabling individuals to be gainfully employed, and 2) the services provided by the organization are available to the general public. This section applies to tax years beginning after July 18, 1984.

Section 1.170A-9(b)(1) of the Regulations states, "educational organization and organizations for the benefit of certain State and municipal colleges and universities - (1) Educational organization. An educational organization is described in section 170(b)(1)(A)(ii) if its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils or students in attendance at the place where its educational activities are regularly carried on. The term includes institutions such as primary, secondary, preparatory, or high schools, and colleges and universities. It includes Federal, State, and other public supported schools which otherwise come within the definition. It does not include organizations engaged in both educational and noneducational activities unless the latter are merely incidental to the educational activities".

In construing the meaning of the phrase "exclusively for educational purposes" in Better Business Bureau v. U.S., (326 U.S. 279 1945), the Supreme Court of the United States said, "This plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes."

Revenue Ruling 68-166, 1968-1 Cumulative Bulletin 255, provides that an organization providing purely custodial day-care for children from needy or low income families is exempt.

Revenue Ruling 73-430, 1973-2 Cumulative Bulletin 362, describes a pre-school children's day care center that meets the requirements relating to faculty, curriculum, and enrolled student body as described in section 170(b)(1)(A)(ii) of the Code as a "nonprofit educational organization".

Revenue Ruling 78-86, 1978-1 Cumulative Bulletin 152, stated that a parking arrangement whereby merchants join together to provide parking for their

customers at a reduced rate serves the merchants' private interests by encouraging the public to patronize their stores. Thus, although there may well be some public benefit derived from the construction and operation of the parking lot, it cannot be said to be operated exclusively for charitable purposes.

An exempt health and welfare fund that operated child day care centers for the pre-school children of union members was denied exempt status as a charitable organization under section 501(c)(3). The day care and other services it provided benefited the union members and not the public at large. (Baltimore Regional Joint Board Health & Welfare, Amalgamated Clothing & Textile Workers Union, 69 TK 554, Dec.)

In San Francisco Infant School, Inc., 69 TC 957, Dec. 35,046 (Acq.), the court held that a child care center met the operational test as a tax-exempt educational organization and the custodial care it provided was merely incidental to its primary purpose of providing education to infants and young children. The organization met the requirements of Section 170(b)(1)(A)(ii) of the Code, thus it qualified under section 501(c)(3).

Based on the information submitted, we have concluded that you are not operated exclusively for one or more purposes specified in section 501(c)(3) of the Code.

The provision of child care is not, in and of itself, an exempt purpose or activity under section 501(c)(3). An organization providing such care may qualify under that section if it is exclusively educational or charitable. In order to qualify as charitable, the organization must be operating in a manner similar to the organization described in Revenue Ruling 68-166. You have stated that the financial position of the parents utilizing your services has no bearing on whether you will accept their children. Thus you are not operated to serve the "needy" and are not charitable.

In order to qualify as exclusively educational, you must either qualify under section 501(k) of the Code, or as a school under section 170(b)(1)(A)(ii). You are not providing substantially all (at least 85%) of your services to enable individuals to be gainfully employed. You have no requirements regarding the purposes of the parents in seeking day-care for their children. From [redacted] to [redacted], only [redacted] percent of the children in your care were from families in which both parents worked. Thus you are not educational by reason of section 501(k) of the Code.


An organization cannot be classified as a school under section 170(b)(1)(A)(ii) unless its primary function is the presentation of formal instruction and it normally maintains a regular faculty and curriculum and normally has a regularly enrolled body of pupils in attendance. An organization that is

engaged in both educational and noneducational activities is not a school if the noneducational activities are more than incidental to the educational professionals. You provide a curriculum similar to the organization described in Revenue Ruling 73-430. However, your services are provided on a drop-in basis. Only [redacted] percent of the slots for pre-schoolers are available on a reservation basis. The remaining slots are drop-ins and cannot be considered regularly enrolled. Though these drop-in children may receive care that includes educational activities and guidance, they are not regular students and you do not meet the definition of a school. Furthermore, since the drop-in care is more than incidental to the educational activities, you are not a school as defined in section 1.170A-9(b)(1) of the Regulations. Thus you are not educational by reason of being a school.

Throughout your application, correspondence, and supplements, you refer to drop-in child care provided for the convenience of the shoppers of [redacted]. This drop-in service is mentioned in your newsletters and required by your lease agreement. The persons using your drop-in service are encouraged to shop at [redacted] in order to receive discounts on your rates (Discount Days and Grocery Discount Days). The merchants at the shopping center directly subsidize your fees through tokens available to the public. Thus you are serving the private interests of both the merchants who attract customers due to the availability of drop-in child care, and of the parents who can leave their children in your care for a portion of the day in order to shop, relax, or do whatever they wish. During the period from [redacted] to [redacted], at least [redacted] percent of the parents used your drop-in service in order to shop at the shopping center. Thus you are similar to the organization described in Revenue Ruling 78-86, and are not operated exclusively for educational purposes.

You have indicated that [redacted] is not intended to be your only activity and that the drop-in care for the convenience of the shoppers at the shopping center is not a substantial part of your program. However, you have operated since [redacted], and your only activity to date has been [redacted]. Furthermore, the drop-in care for the convenience of the shoppers is a substantial part of your activities as shown in the promotions to encourage your clients to use the shopping center and through the requirements in your lease that such services be provided. Thus, since you are providing child-care services for shoppers, you are serving the private interests of the shoppers and the merchants they patronize as a substantial part of your activities, and you are not exempt as an educational organization. Serving the private interests of individuals also precludes exemption under section 501(c)(3), regardless of the classification under that section.

Accordingly, even though you may provide some educational services, it is held that you are not entitled to exemption from Federal income tax under section 501(c)(3) of the Code.


It follows, therefore, that contributions to you are not deductible by donors under section 170 of the Code.

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.


If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

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 7428(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."

If this determination letter becomes a final determination, we will notify the appropriate State Officials, as required by section 6104(c) of the Code, that based on the information we have, we are unable to recognize you as an organization of the type described in Code section 501(c)(3).

Sincerely,


District Director

Enclosures:
Form 6018
Publication 892


cc: 