

[REDACTED]

[REDACTED]

[REDACTED]

[REDACTED]

NOV 15 1993

Employer Identification Number: [REDACTED]
Key District: Cincinnati

Dear Applicant:

We have considered your application for recognition of exemption as an organization described in section 501(c)(3) of the Internal Revenue Code. Based on the information submitted, we have concluded that you do not qualify for exemption under that section.

FACTS

You were formed on [REDACTED], pursuant to the laws of the State of [REDACTED]. [REDACTED]'s father owned farm land containing a house, barns, and a dairy farm. He died and the heirs sold a portion of the property, but not the dairy farm, to unrelated third parties. [REDACTED] became the sole owner of the dairy farm, which she operates as a sole proprietorship.

After the third parties had purchased the land formerly owned by her father, [REDACTED] obtained an option to purchase the property. She formed you and gave you the option. You purchased the property from the third parties for \$[REDACTED] plus two years back taxes in [REDACTED]. The property was valued by an independent appraiser in [REDACTED] and found to be worth \$[REDACTED]. You plan to operate the property as an 1890s historical farm catering primarily to tourists and children on elementary school field trips.

Most of the your activities will be carried out on the parcel of property purchased by you. However, you have also entered into a lease for the use of certain of the adjacent property owned by [REDACTED]. The property was leased for \$[REDACTED] per acre. This price is represented to be equal to the lowest price charged in the area for use of farm land, although no independent rental appraisal was done. You also represented that in your area you do not make rental appraisals. The use of this property is necessary to afford the applicant access to woods and ponds on the dairy farm property. These woods and ponds will form part of the tour of the Family Farm. It appears that a project to demonstrate proper land

management will also be carried out on the dairy farm property and will comprise a stop on the tour of the Family Farm.

you will present [REDACTED] half-hour programs designed to focus on math, science, language arts, and history. Afterward attending the programs visitors will be able to put the acquired knowledge to work. Area school teachers are designing your educational programs according to the Core Curriculum of the [REDACTED] Department of Education. The programs will have a three year span to enable the schools to come back year after year. In addition to the educational programs, the farm will have a cider press, a dehydrator, an ice house, a blacksmith shop, quilting, churning of butter, spinning wool, making of soap and candles. Buggy rides or covered wagon rides pulled by oxen will be provided through the farm lane to the pond or woods. In the woods there will be [REDACTED] acre wood lots, one cleared and managed, the other one not. The idea behind these [REDACTED] lots is to show the importance of forestry. The woods will have paths planted with wild flowers that will be identified.

[REDACTED] has formed a separate Subchapter S corporation, [REDACTED], which will operate a restaurant and gift shop on the dairy farm property immediately adjacent to the Family Farm. Due to the layout of the Family Farm, the restaurant and gift shop will function as an integral part of the Family Farm. For example, admission tickets will be purchased at the restaurant/gift shop for the Family Farm tour. The gift shop will also sell craft items made on the Family Farm. It was originally intended that [REDACTED] would be a for profit concession located in a barn on the Family Farm property. However, the intended location created public health issues and the Eatery was sited for a location on the dairy farm property to resolve the public health issues.

The letterhead stationery used by the applicant, and the information furnished in support of the application, indicate that the [REDACTED] is presented to the public as a collective entity, the [REDACTED], consisting of the applicant proper, the [REDACTED], and the dairy farm (to the extent the dairy farm is used to demonstrate modern and turn of the century dairy practices, land use projects, various species of plant life, or other educational activities).

A business plan submitted in support of the application indicates that the applicant plans to devote approximately \$[REDACTED], amounting to [REDACTED]% of its projected annual gross income, to advertising its attractions to the general public. This promotional campaign is expected to continue for three years, by which time the applicant expects to have established a sufficient

██████████.

level of public awareness to assure its continued successful operation.

The business plan envisions that the project will include a bed and breakfast inn. It is not clear who will be the owner of the bed and breakfast inn. Projected income and expenses are combined for the dairy farm, historical farm, and restaurant.

██████████ is expected to be employed as the applicant's manager. ██████████, ██████████'s brother, is expected to be employed to handle sales and promotion. ██████████, ██████████'s sister, is to be employed to help with restoration of the farm house and purchase of furniture and "props" for educational programs. ██████████ and her brother and sister serve on the organization's ██████████ member Board of Directors. ██████████ is your President. The remaining ██████████ directors are not related to ██████████. The Board meets once a year. Non-family Board members are paid \$██████████ per year for their services. It is anticipated that all of the family board members will continue to pursue other employment while employed part time by the applicant.

Your principal source of financial support will be the sale of admission tickets. You will also receive financial support from grants and contributions, as well as from the sale of milk, electricity, and craft items made at your facilities.

LAW AND ANALYSIS

Section 501(a) of the Internal Revenue Code exempts from taxation organizations described in subsection (c)(3), which includes corporations organized and operated exclusively for charitable and educational purposes. Furthermore, the aforementioned subsection requires that no part of the organization's net earnings inure to the benefit of any private shareholder or individual, that no substantial part of its activities is to influence legislation and that it does not participate in any political campaign on behalf of or in opposition to any candidate for public office.

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(b)(2) defines the words "private shareholder or individual" as persons 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 exempt purposes 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.

Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term "educational" as used in section 501(c)(3) of the Code 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 513(a) of the Code defines the term "unrelated trade or business" as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501.

RATIONALE

are a composite entity comprised of two for-profit corporations and one nonprofit corporation, each dominated or controlled by . Transactions among the organizations are not based on arm's length standards.

For example, you were willing to pay in excess of appraised fair market value for land adjoining 's property. Further, some of the land you use is rented from , but no rent appraisal was made by an independent appraiser. Although the Service requested an appraisal of the rental property, you stated that you did not make such appraisals in that part of the country, making it impossible for us to determine whether the rental price is at fair market value. Thus, you have failed to provide information necessary to establish that you are not organized or operated for the benefit of as required by section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

████████████████████.

Further, if you carry out your plan of creating an historical farm/tourist attraction on the property which ██████████ optioned for you, the adjacent property belonging to ██████████ will increase in value from being mere farm land to being property with a significant potential for business use. That potential for business use will be exploited by ██████████ through the operation of a for-profit restaurant and gift shop whose clientele will be generated as a result of your activities. Thus, even though some of your activities may be educational, the private interests of ██████████ are intertwined with your operations in such a way that, to the extent you are successful in attracting visitors, ██████████ will also be enriched. This constitutes a benefit to her private interests within the meaning of section 1.501(c)(3)-1(d)(1)(ii) of the regulations. Moreover, since it involves the use of your income or assets in such a way as to benefit your President as a private individual, this activity also violates the prohibition against private inurement contained in section 501(c)(3) of the Code.

Accordingly, you do not qualify for exemption from federal income tax under 501(c)(3) of the Internal Revenue Code. Contributions to you are not deductible under section 170 of the Code. You must file federal income tax returns.

You have the right to protest this ruling if you believe that it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your principal officers, must be submitted in duplicate within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under the Conference and Practice Requirements.

If you do not protest this ruling 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 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 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 administrative remedies available to it within the Internal Revenue Service."

If we do not hear from you within 30 days, this ruling will become final and copies will be forwarded to the District Director,

[REDACTED]

Cincinnati, Ohio, which is your key district for exempt organization matters. Thereafter, any questions about your federal tax status or the filing of returns should be addressed to that office. If you want the matter reopened at a later time, you must pay a new user fee as provided in Rev. Proc. 93-23, 1993-19 I.R.B. 6. Also, the appropriate State officials will be notified of this action in accordance with section 6104(c) of the Code.

Sincerely yours,

[REDACTED]
[REDACTED]
Chief, Exempt Organizations
Rulings Branch 1

cc: [REDACTED]
[REDACTED]