



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **201452020**
Release Date: 12/26/2014

Date: October 2, 2014

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

UIL: 501.03-00

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.

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.

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,

Michael Seto
Manager, Exempt Organizations
Technical

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



Department of the Treasury
Internal Revenue Service
1111 Constitution Ave. NW
Washington, DC 20224

Date: August 11, 2014

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

Website =

Company =

Dear :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(3) of the Code. This letter explains the basis for our conclusion. Please, keep it for your records.

Issue

Whether you qualify for exemption as an organization described in § 501(c)(3).

Facts

Your Articles state that you will "provide funding to domestic and international nonprofit organizations whose missions are to provide humanitarian, wildlife, or educational aid around the globe." Your narrative statement on your Form 1023 provides that you will not perform any fundraising, rather you will raise funds by "selling travel through the use of [the internet] on Website."

You describe three different activities that you will perform: sale of travel, marketing of Website, and distribution of funds to selected non-profits. You state that you will contract an affiliate internet travel partner to provide the booking engine for your website, Website. The website indicates that you have partnered with Company, a for-profit company that operates a travel

website. A user of your website can search for and purchase travel related services. Your website will be available anytime of any day. You also anticipate marketing your website through social media and other sources in order to increase traffic to your website.

While there is no membership fee for your services, individuals will have to pay on a per service basis incurring a fee based upon the item purchased through you. The fee charged to the user will be determined by Company. Part of the fee charged will be retained by Company as its fee for services. The remainder of the fee will be retained by you. You will then distribute your earnings to preselected non-profits. You will distribute funds to organizations that are recognized as being described in § 501(c)(3). You will select organizations that meet your philanthropic goals. Users of your website will then be able to select to which of the selected organizations he/she would like to send funds. If the user does not select from your list of organizations you will determine the distribution amount on your own. You do not have any grant approval process or application. You merely state that you will distribute funds to organizations that provide humanitarian, wildlife, or educational aid around the globe. Your website currently lists twenty-four different organizations from which a user might select for this distribution of the portion of the fees generated by that user's transaction.

You have three directors. Two of your directors are married to each other. None of your directors are compensated.

Law

I.R.C. § 501(c)(3) provides that organizations may be exempted from tax if they are organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes and "no part of the net earnings of which inures to the benefit of any private shareholder or individual."

I.R.C. § 502(a) provides the general rule that an organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt from taxation under I.R.C. § 501 on the ground that all of its profits are payable to one or more organizations exempt from taxation under I.R.C. § 501.

I.R.C. § 502(b)(1) excludes from the definition of trade or business for the purposes of § 502 the production of income through rents which would be excluded under § 512(b)(3) if § 512 were to apply to that organization.

I.R.C. § 512(b)(1) excludes all dividends, interest, payments with respect to securities, and annuities from "unrelated business income."

I.R.C. § 512(b)(3) provides that all rents, with certain exceptions not relevant here, shall be excluded from unrelated taxable income.

I.R.C. § 513(a) defines the term "unrelated trade or business" to include 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 purpose or function constituting the basis for its exemption under I.R.C. § 501. The term "trade or business" as used in I.R.C. § 512 and I.R.C. § 513 has the same meaning given the term in other sections of the Internal Revenue Code.

Treas. Reg. § 1.501(c)(3)-1(a)(1) provides that in order to be exempt under section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the exempt purposes specified in that section.

Treas. Reg. § 1.501(c)(3)-1(c)(1) states 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 the exempt purposes specified in I.R.C. § 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.

Treas. Reg. § 1.501(c)(3)-1(d)(2) defines charitable as it is used in its generally accepted legal sense. The term includes the relief of the poor and distressed, advancement of religion, lessening the burdens of government, and the promotion of social welfare by eliminating prejudice and discrimination or by defending human and civil rights secured by law.

Treas. Reg. § 1.501(c)(3)-1(e)(1) states that, "an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513." An organization operated primarily for an unrelated trade or business is not exempt under 501(c)(3).

Revenue Ruling 64-182, 1964-1 C.B. 186, provides that corporation organized exclusively for charitable purposes derives its income principally from the rental of space in a large commercial office building which it owns, maintains, and operates. The charitable purposes of the corporation are carried out by aiding other charitable organizations, selected in the discretion of its governing body, through contributions and grants to such organizations for charitable purposes. The ruling holds that the corporation is deemed to meet the primary purpose test of section 1.501(c)(3)-1(e)(1) of the regulations, and to be entitled to exemption under section 501(c)(3) of the Code, where it is shown to be carrying on through such contributions and grants a charitable program commensurate in scope with its financial resources.

Revenue Ruling 67-149, 1967-1 C.B. 133, holds that an organization formed for the purpose of providing financial assistance to several different types of organizations which are exempt under section 501(c)(3) of the Code is itself exempt under that section. It carries on no operations other than to receive contributions and incidental investment income and to make distributions of income to such exempt organizations at periodic intervals. The organization does not accumulate its investment income.

Revenue Ruling 76-442, 1976-2 C.B. 148, discusses an organization that provides free legal services for personal tax and estate planning to individuals who wish to make current and deferred gifts to charity. The revenue ruling states that aiding individuals in their tax and estate planning is not a charitable activity in the generally accepted legal sense. The organization is providing commercially available services to individuals who can afford them. The revenue ruling concludes that although funds may ultimately be made available to charity as a result of the organization's planning assistance to individuals, the benefits to the public are tenuous in view of the predominantly private purpose served by arranging individuals' tax and estate plans. The fact that gifts to charity are contemplated in the plans do not convert the organization's assistance into a charitable activity or one that promotes social welfare within the meaning of the regulations.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279, 283 (1945), the court determines 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 Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991) *aff'd* 70 T.C. 352 (1978), the court determined that a nonprofit organization established by the Seventh Day Adventist Church to operate restaurants and health food stores to carry out its "health ministry" was not exempt under section 501(c)(3) as a religious organization. The court of appeals affirmed the tax court's finding that "Living Faith's religious purposes, although sincere, did not sufficiently mitigate the 'clear commercial purpose' of its operations." The court noted that the organization was in competition with other restaurants, advertised, charged market rates and generally operated in a manner similar to commercial businesses.

In Easter House v. U.S. 12 Cl. Ct. 476 (1987), *aff'd in an unpub. opinion*, 846 F. 2d 78 (Fed. Cir. 1988), *cert. den.*, 488 U.S. 907 (1988), the organization, in exchange for a fee, provided adoption services to parents seeking to adopt a child, including services to pregnant women who intended to place their newborns for adoption. The Claims Court concluded that the organization's business purpose of operating an adoption service, not the advancement of educational and charitable activities, was its primary goal. It competed with other commercial organizations providing similar services. Thus, "[p]laintiff's competition provides its activities with a commercial hue." 12 Cl. Ct. at 486. Accordingly, the organization did not qualify for exemption under I.R. C. § 501(c)(3).

In Airlie Foundation v. IRS, 283 F. Supp. 2d 58, 63, 65 (D.D.C. 2003), the court states that, "Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, *inter alia*, whether the organization uses commercial promotional methods (e.g., advertising) and the extent to which the organization receives charitable donations." With respect to the organization in question, the court found that, "While certain factors-including plaintiff's fee structure and subsidization practice-are indicative of non-commercial characteristics, others-such as the nature of its clients and competition, its advertising expenditures and the substantial revenues derived from weddings and special events on the premises, strongly

suggest that the agency was correct in revoking the foundation's tax exempt status.”

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the court found that a corporation formed to provide consulting services did not satisfy the operational test under I.R.C. § 501(c)(3) because its activities constituted the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. In addition, the court found that the organization had not solicited, nor had it received, voluntary contributions from the public. Its only source of income was from fees from services, and those fees were set high enough to recoup all projected costs and to produce a profit. Moreover, it did not appear that the corporation ever planned to charge a fee less than “cost.”

In Zagfly, Inc. v. Commissioner, T.C. Memo 2013-29, an applicant proposed to sell flowers over the internet, allowing purchasers to direct a portion of their payment to recognized exempt organizations and to the applicant for its operating costs. The applicant argued that it was not a business as it planned to direct the profit to contributions and that giving the opportunity to contribute to its customers was a charitable purpose. The court held that selling flowers at market prices over the internet was a business, and not substantially related to an exempt activity.

Application of law

To be an exempt organization described in § 501(c)(3) an organization must be both organized and operated exclusively for religious, charitable, scientific, educational, or other specified exempt purpose. Section 1.501(c)(3)-1(a)(1). In order to be operated exclusively for one or more exempt purposes an organization must engage primarily in activities that accomplish one or more of the exempt purposes specified in § 501(c)(3). Section 1.501(c)(3)-1(c)(1). Such an organization will not be so regarded if more than an insubstantial portion of its activities is not in furtherance of an exempt purpose. *Id.* An organization may be described under § 501(c)(3) even though it operates a trade or business as a substantial part of its activities, however, as long as such trade or business is in furtherance of the organization’s exempt purpose and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in § 513. Section 1.501(c)(3)-1(e)(1).

Section 513(a) defines the term “unrelated trade or business” to include “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 purpose or function constituting the basis for its exemption under § 501.” The term “trade or business” has the same meaning within §§ 512 and 513 as that term has been given in other sections of the Code.

You are not engaged primarily in activities that accomplish one or more exempt purposes as more than an insubstantial portion of your activities is not in furtherance of an exempt activity. You primarily run a travel website where individuals can search for and purchase travel related services. This activity is not substantially related to any exempt purpose other than the production of income. Since your online booking engine does not further your

exempt purpose (other than through the production of income) it is an unrelated trade or business as defined in § 513 therefore it cannot be a substantial part of your activities under § 1.501(c)(3)-1(e)(1). Your online booking activities are conducted twenty-four hours a day and 365 days a year, therefore your unrelated trade or business is a substantial part of your activities.

Furthermore, courts have determined that organizations that operate with a substantial commercial purpose are not exempt organizations as described in § 501(c)(3). Two recent cases have substantially defined the factors to consider when determining whether an organization is operated for a substantial commercial purpose. The earlier case, Living Faith, 950 F.2d 365, considered whether the organization sold goods or services to the public, whether the organization was in direct competition with commercial organizations, whether the prices were set in a commercial manner, whether the organization used promotional materials similar to those of a commercial enterprise, whether the organization utilized volunteers, and whether the organization received charitable contributions. More recently, Airlie Foundation, 283 F. Supp. 2d at 63, reiterated these factors adding that the reasonableness of financial reserves was also to be considered. Also, the court noted that the organization need not fall on the commercial side of all of the factors in order to be operated for a non-exempt purpose. Id. at 68; see also, B.S.W. Group, 70 T.C. 352.

Using the factors listed in these cases your activities serve primarily to further a commercial purpose. You sell the service of flight, car rental, and hotel searches and bookings to individuals for a fee based on the overall price of the item purchased. This fee is set by a for profit company thus your prices are similar to the commercial rates offered by for profit organizations with which you compete. You also stated that you will market your website in order to drive increased traffic there. Finally, while you do use the volunteer labor of your founders and directors you do not receive any charitable contributions. Thus you fall on the commercial side of each of the factors provided. Additionally, your activities are similar to the organizations described in Zagfly, T.C. Memo 2013-29, and Rev. Rul. 76-442, supra. Both of these organizations performed unrelated commercial activities that ultimately directed funds toward charitable organizations. It was determined that the destination of these funds was not sufficient to make the otherwise commercial activity a charitable purpose. The factors used by the courts indicate that you are formed primarily for a commercial purpose, which is confirmed by your similarity to two prior organizations the exemption of which has been denied.

You are not like the organizations described in Rev. Rul. 64-182, supra, and Rev. Rul. 67-149, supra. While both of these organizations were determined to be exempt as organizations that exclusively provided distributions to recognized charitable organizations, neither of the organizations performed other activities that were considered an unrelated trade or business. The organization in Rev. Rul. 64-182, supra, earned income through contributions and the rental of property, which is excluded from unrelated business income under § 512(b)(3). See also, § 502(b)(1) (excluding renting as described in § 512(b)(3) as a trade or business for § 502 purposes). The organization in Rev. Rul. 67-149, supra, earned income from contributions and investments, which are excluded from unrelated business income under § 512(b)(1). Unlike these organizations your income is derived from the active

conduct of an unrelated trade or business as discussed above. The destination of your income does not convert your activity into a charitable one. Section 502.

Section 502 provides that an organization operated for the primary purpose of carrying on a trade or business for profit shall not be exempt from taxation under § 501 on the grounds that all of its profits are payable to one or more organizations exempt from taxation under § 501. Here, you are conducting a trade or business since you are providing a service for a commercially set fee. Also, you are in competition with other for-profit organizations that perform the same service for a fee. The only charitable activity you perform is the provision of funds to organizations recognized as exempt from taxation. Section 502 precludes your exemption based on the destination of your funds earned through the provision of your service.

Conclusion

You are not operated exclusively for an exempt purpose. You provide a service for a fee in competition with commercial organizations and otherwise act as a commercial organization. You are also a "feeder organization" as described in § 502. You are not exempt under § 501(c)(3).

If you don't agree

You have a right to file a protest if you don't agree with our proposed adverse determination. To do so, you must send us a statement within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A copy of this letter highlighting the findings you disagree with
- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

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

For an authorized representative:

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

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. You also have a right to a conference after you submit your statement. If you want a conference, you must request it when you file your protest statement.

You can also ask the Office of Appeals to review your application for tax-exempt status. Your right to request Appeals review is in addition to your right to a conference, as outlined in Revenue Procedure (Rev. Proc.) 2014-4 and Rev. Proc. 2014-9. You must notify us in writing if you want us to forward your case to the Appeals Office. You can find more information about the process and the role of the Appeals Office in Section 7 of Rev. Proc. 2014-9 and Publication 4227, *Overview of the Appeals Process*.

If the person representing you in this process is not an officer, director, trustee, or other official who is authorized to sign for the organization, he or she must file Form 2848, as explained above, and otherwise meet the requirements in Publication 216, *Conference and Practice Requirements*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

Where to send your protest

Please send your protest statement, any request for consideration by the Office of Appeals, Form 2848, if needed, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
TE/GE (SE:T:EO:RA:T:2)
NCA - 557-09
1111 Constitution Ave, N.W.
Washington, DC 20224

Street address for delivery service:

Internal Revenue Service
TE/GE (SE:T:EO:RA:T:2)
NCA - 557-09
1111 Constitution Ave, N.W.
Washington, DC 20224

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at www.irs.gov/formspubs. If you have questions, you can contact the person listed at the top of this letter.

Sincerely,

Michael Seto
Manager, Exempt Organizations
Technical

Enclosure: Publication 892