



**Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities**

Date:
03/10/2025
Employer ID number:

Form you must file:
1120

Tax years:
All

Person to contact:

Release Number: 202523005
Release Date: 6/6/2025
UIL Code: 501.35-00, 501.36-01

Dear :

This letter is our final determination that you don't qualify for exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in IRC Section 501(c)(3). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

Because you don't qualify as a tax-exempt organization under IRC Section 501(c)(3), donors generally can't deduct contributions to you under IRC Section 170.

We may notify the appropriate state officials of our determination, as required by IRC Section 6104(c), by sending them a copy of this final letter along with the proposed determination letter.

You must file the federal income tax forms for the tax years shown above within **30 days** from the date of this letter unless you request an extension of time to file. For further instructions, forms, and information, visit www.irs.gov.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection after deleting certain identifying information, as required by IRC Section 6110. Read the enclosed Letter 437, Notice of Intention to Disclose - Rulings, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Letter 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

If you have questions about this letter, you can call the contact person shown above. If you have questions about your federal income tax status and responsibilities, call our customer service number at 800-829-1040 (TTY 800-829-4933 for deaf or hard of hearing) or customer service for businesses at 800-829-4933.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements

Enclosures:
Letter 437
Redacted Letter 4034
Redacted Letter 4038

cc:



Department of the Treasury
Internal Revenue Service
PO Box 2508
Cincinnati, OH 45201

Date: 01/21/2025

Employer ID number:

Person to contact:

Name:

ID number:

Telephone:

Fax:

Legend:

B = Date of formation

C = State

D = Number

E = Number

UIL:

501.35-00

501.36-01

Dear :

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

Issues

Do you qualify for exemption under IRC Section 501(c)(3)? No, for the reasons stated below.

Facts

You incorporated on B, in the state of C. You are a veterans' organization with D members, all members holding military discharge papers.

You operate a restaurant and bar that is open to the public every day. You serve alcoholic beverages, breakfast, lunch, dinner, Sunday brunch, and you have daily specials. You have take-out, individual and group dining, entertainment, karaoke, country and western dance music, bingo, etc. For special holidays you have free breakfast, lunch, and dinner for veterans and military personnel. Your restaurant and bar are family friendly and capable of providing motorcoach parking. Your restaurant's hours of operation are 7 a.m. to 9 p.m. and is open every day of the year. Your internet advertising states that your restaurant and bar are open to the public and the prices are comparable to other restaurants.

You hold fundraising events to provide services for veterans seeking help and to support various causes. For example, you raised funds to support the Sea Cadets, for a trip to Hawaii for the ceremonies of USS Arizona, the reconstruction of the Marine Air Force Base benches and statues, veterans who lost their homes to fire, veterans and veterans' spouses to pay medical expenses, and veterans' trips to VA hospital appointments.

You do not have an application form for a veteran to request assistance from you. Instead:

- You will interview the veteran that is seeking assistance.
- Your officers and members will decide what kind of help can be provided.
- Your officers and members will select the recipient for the fundraising event.
- The selection of the recipient will be made before the fundraising event.
- The recipient's identity will be made public before the fundraising event.
- The recipient generally is not present at the fundraising event.

Other proposed future programs include:

- The development of a veterans' village, with micro mini homes for low income or homeless veterans.
- Celebrating veterans' birthdays every month.
- Applying for medical benefits for veterans and their families.
Helping veterans and their families transition into civilian life.
- Providing a space for veterans and their families.
- Providing honor guard ceremonies for those who have fallen.

Your revenue sources include (in order from most to least substantial) restaurant and bar receipts, contributions, bingo/gaming activities, and membership fees. The vast majority of your revenue is from the operation of the restaurant and bar. A substantial portion of your expenses are for cost of goods sold, occupancy, and other operating expenses related to the restaurant and bar.

Law

IRC Section 501(c)(3) provides for the exemption of corporation and foundations organized and operated exclusively for charitable or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholders or individuals.

IRC Section 513(a) defines the term 'unrelated trade or business' as any trade or business of an organization subject to tax under Section 511 the conduct of which is not substantially related (aside of 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 exempt functions. Such term does not include any trade or business 1) in which substantially all the work in carrying on such trade or business is performed for the organization without compensation, or 2) which is carried on by the organization primarily for the convenience of its members, students, patients, officers, or employees, or 3) which is the selling of merchandise, substantially all of which has been received by the organization as gifts or contributions.

Treasury Regulation Section 1.501(c)(3)-1(a)(1) states 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 such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Treas. Reg. Section 1.501(c)(3)-1(c)(1) 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.

Treas. Reg. Section 1.501(c)(3)-1(d)(2) defines the term charitable as including the relief of the poor and distressed or of the underprivileged, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration. The term "charitable" also includes lessening of the burdens of government.

Treas. Reg. Section 1.501(c)(3)-1(e)(1) provides that an organization may meet the requirements of IRC 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.

Rev. Rul. 79-360, 1979-2 C.B. 236, held the operation of health club facilities in a commercial manner by an exempt organization whose purpose is to provide for the welfare of young people, constitutes unrelated trade or business. It also held that the operation of the health club program did not contribute importantly to the accomplishment of the organization's exempt purposes.

In Better Business Bureau of Washington, D.C. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will prevent exemption regardless of the number or importance of truly exempt purposes. The Court found that the trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court determined that an organization that sold consulting services to nonprofit and exempt organizations interested in rural-related policy and program development operated a trade or business ordinarily carried on for profit. Furthermore, the petitioner did not conduct other substantial charitable activities. Other factors that counted against petitioner included the fact that the petitioner's financing did not resemble that of a typical IRC Section 501(c)(3) organization and that the petitioner failed to limit its services to Section 501(c)(3) organizations. Therefore, the court determined that petitioner failed to qualify for recognition under Section 501(c)(3).

In Federation Pharmacy Services, Inc. v. Commissioner, 72 T.C. 687 (1979) aff'd 625 F.2d 804 (8th Cir. 1980), the Tax Court stated that the sale of prescription drugs to senior citizens and handicapped persons is a trade or business normally carried on for profit. The court also ruled that sales of prescription drugs to the elderly and the handicapped even at a discount is not, without more, in furtherance of a charitable purpose. The court said it was clear that petitioner's exclusive purpose for being was to sell drugs, an activity that is normally carried on by commercial profit-making enterprises. The court also stated that in regard to the promotion of health "We do not believe that the law requires that any organization whose purpose is to benefit health, however remotely, is automatically entitled, without more, to the desired exemption. We have been cited no evidence that Congress intended to exercise its grace in such an expansive manner."

In Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), the court wrote that the activities were conducted as a business and the organization was in direct competition with other restaurants and health food stores; thus, it did not qualify for exemption under IRC Section 501(c)(3). The appellate court stated the factors that the court relied on to find commerciality and thus offered the best contemporary explanation of the commerciality doctrine. These factors include:

- a) The organization sold goods and services to the public.

- b) The organization was in direct competition with for profit businesses (food stores and restaurants).
- c) The prices set by the organization were based on pricing formulas common to retail food businesses.
- d) The organization utilized promotional materials and "commercial catch phrases" to enhance sales.
- e) The organization advertised its services and food.
- f) The organization did not receive any charitable contributions.

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the District Court relied on the "commerciality" doctrine in applying the operational test. Because of the commercial manner in which the organization conducted its activities, the court found that it was operated for a non-exempt commercial purpose, rather than for a tax-exempt purpose. "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 received charitable donations."

Application of law

IRC Section 501(c)(3) sets forth two main tests for qualification for exempt status. As stated in Treas. Reg. Section 1.501(c)(3)-1(a)(1), an organization must be both organized and operated exclusively for purposes described in Section 501(c)(3).

You are not operating exclusively for exempt purposes consistent with IRC Section 501(c)(3). Your primary activity is operating a restaurant and bar for the general public, which is an unrelated trade or business as defined in Section 513(a). You state that volunteers work at the restaurant and bar, but they not truly volunteers because they receive compensation through tips. Additionally, the restaurant isn't just for the convenience of members because you are open to the public and the food and drinks you sell aren't donated. The revenue from these activities comprise the majority of your income. The operation of the restaurant and bar is your primary activity and it is unrelated to, and not in furtherance of, any charitable or educational activities.

You are not described in Treas. Reg. Section 1.501(c)(3)-1(c)(1) because a substantial part of your activities, the operation of a restaurant and bar, are devoted to non-exempt purposes. You operate in a manner consistent with, and in competition with, other similar for-profit restaurants. While you plan to use some of the profits from your operations for charitable purposes, your primary activity is the operation of a restaurant for the public. As the court found in Better Business Bureau, the presence of a single, substantial non-exempt purpose will preclude exemption regardless of the number of other exempt activities.

You are similar to the organization described in Rev. Rul. 79-360 because the operation of the restaurant and bar do not contribute importantly to the accomplishment of your exempt purposes. Therefore, you are not primarily operating exclusively for charitable purposes as described in Treas. Reg. Section 1.501(c)(3)-1(d)(2).

You do not meet the requirements of Treas. Reg. Section 1.501(c)(3)-1(e)(1) for recognition of tax exemption under IRC Section 501(c)(3) because you are operated for the primary purpose of carrying on an unrelated trade or business as defined in Section 513. You have established a business where customers purchase food that competes with other similar commercial businesses. Your primary source of revenue is from your restaurant and your expenses are mainly related to operating the restaurant. As stated in Living Faith, Inc., the fact that an organization's primary activity may constitute a trade or business does not, of itself, disqualify it from classification under IRC Section 501(c)(3), provided the trade or business furthers or accomplishes an exempt

purpose. If one of the activity's purposes, however, is substantial and nonexempt, the organization will be denied exempt status under Section 501(c)(3), even if its activity also furthers an exempt purpose.

You are like the organizations described in B.S.W. Group, Inc., Federation Pharmacy Services, Inc., and Airlie Foundation because you are operating for a substantial non-exempt purpose rather than for a tax-exempt purpose. You are in competition with other restaurants and you advertise your restaurant and bar on the internet. You are open to the general public during regular business hours. Your prices are comparable to other restaurants, and you will be funded primarily restaurant receipts. Your largest expenses are for operation of the restaurant and bar. These factors indicate that you are precluded from exemption under IRC Section 501(c)(3) because you are operated for the substantial nonexempt purpose of operating an unrelated trade or business.

Your position

You emphasize that you do much more than operate a restaurant. You said there are an estimated E volunteer hours per year toward the following activities:

- Providing free assistance for VA applications and appeals.
- Providing nutritional, financial, emotional, transportation, and social support for veterans.
- In the future to provide affordable housing, tiny houses, at the veterans' village.

Your restaurant is essential to get funding for your activities. The restaurant, operated solely by volunteers, provides low-cost meals to the veteran community. It provides free food to home-bound members and those with food challenges. It serves as a focal point and gathering place for members that is paramount to their emotional and social wellbeing.

Our response to your position

Your restaurant and bar are open to the public, not just veterans. Most of your time and funds are spent to operate the restaurant and bar. While you state that your restaurant employees are volunteers, they receive tips as compensation.

While you have some charitable and educational activities, in order to qualify for exemption under IRC Section 501(c)(3), you have to be operated exclusively for exempt purposes. You are not operating exclusively to provide charitable and educational services to veterans. Rather, you have a substantial activity of operating a restaurant and bar for the public, which does not fulfill a charitable or educational purpose.

Conclusion

You fail the operational test because you have a substantial nonexempt purpose of operating a restaurant and bar for the general public, which is a unrelated trade or business. Therefore, you are precluded from exemption under Section 501(c)(3).

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.

If you don't agree

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

- Your name, address, employer identification number (EIN), and a daytime phone number
- A statement of the facts, law, and arguments supporting your position
- A statement indicating whether you are requesting an Appeals Office conference
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization or your authorized representative
- The following declaration:

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

Under penalties of perjury, I declare that I have examined this request, or this modification to the request, including accompanying documents, and to the best of my knowledge and belief, the request or the modification contains all relevant facts relating to the request, 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 they haven'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 gave us a basis to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't given us a basis for reconsideration, we'll send your case to the Appeals Office and notify you. You can find more information in Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

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

Where to send your protest

Send your protest, Form 2848, if applicable, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Mail Stop 6403
PO Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Mail Stop 6403
Cincinnati, OH 45202

You can also fax your protest 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 they received it.

You can get the forms and publications mentioned in this letter by visiting our website at www.irs.gov/forms-pubs or by calling 800-TAX-FORM (800-829-3676). If you have questions, you can contact the person listed at the top of this letter.

Contacting the Taxpayer Advocate Service

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or if you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit www.taxpayeradvocate.irs.gov or call 877-777-4778.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Stephen A. Martin
Director, Exempt Organizations
Rulings and Agreements