

Promoting business activity in economically deteriorated area. An organization formed to increase business patronage in a deteriorated area by providing information on the area's shopping opportunities, local transportation, and accommodations is not operated exclusively for charitable purposes and does not qualify for exemption under section 501(c)(3) of the Code. Similarly, an organization whose purpose is to revive retail sales in an area of economic decline by constructing a shopping center does not qualify for exemption.

'Advice has been requested whether the nonprofit organizations described below, which otherwise qualify for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954, are operated exclusively for charitable purposes.

Situation 1.

'The organization's purpose is to increase business patronage in a deteriorated area mainly inhabited by minority groups. It accomplishes this purpose by presenting television and radio advertisements describing the advantages of shopping in the area; by creating a speaker's bureau composed of local businessmen who discuss the shopping environment with various groups; by operating a telephone service providing information to prospective shoppers on transportation and accommodations in the area; and by informing the news media on the area's problems and potential.

Situation 2.

'The organization's purpose is to revive retail sales in an area suffering from continued economic decline. The organization proposes to limit further decline of retail sales within the area caused by competing, outlying shopping centers by constructing a center that would complement the area's existing retail facilities.

'It purchased land for the construction of a retail center that will include a department store and shopping mall. The land purchased by the organization was sold to the city at no economic benefit to the organization. Additional land for the project was acquired by the city through its use of eminent domain. The city rents all the land to the organization and to a private developer.

'The actual construction of the development project and the leasing of the buildings are carried out by the private developer. Throughout these various transactions, no financial gain accrued to the organization. In addition, the city requires that minorities be utilized in both the construction and the operation of the project. Stores located within the project are also required to employ a certain percentage of minority group employees.

'Section 501(c)(3) of the Code provides for the exemption from Federal income tax of organizations organized and operated exclusively for charitable or educational purposes.

'Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations states that the term 'charitable' is used in section 501(c)(3) of the Code in its generally accepted legal sense. Such term includes relieving the poor and distressed or the underprivileged, combatting community deterioration, lessening neighborhood tensions, and eliminating prejudice and discrimination.

'Section 1.501(c)(3)-1(d)(3) of the regulations states that the term 'educational,' as used in section 501(c)(3) of the Code, relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

In *Better Business Bureau v. U.S.*, 326 U.S. 279 (1945), 1945 C.B. 375, the Supreme Court determined that while some activities of the organization under consideration were educational, a substantial purpose of the organization was to promote business, and thus the organization was not operating exclusively for educational purposes.

'Rev. Rul. 74-587, 1974-2 C.B. 162, holds that a nonprofit organization providing low-cost financial assistance, either through loans or through purchase of equity interest in various business enterprises in economically depressed areas, qualifies for exemption under section 501(c)(3) of the Code. Loans and equity financing are granted only to those individuals or corporations who are unable to obtain funds from conventional sources because of the poor financial risks involved in operating businesses within the depressed area or because of operation or ownership of such businesses by members of a minority group. The Revenue Ruling states that this activity promotes the community in three ways that are designed to be 'charitable'. First, the activity lessens prejudice against minorities by demonstrating that with proper guidance and opportunity such groups can operate a business. Second, it eliminates poverty and lessens neighborhood tensions by assisting local businesses, thereby creating job opportunities. Third, it combats community deterioration by establishing new businesses and rehabilitating existing one.

'Although the organization's activities described in Situation 1 may contribute to the achievement of the purposes described in section 501(c)(3) of the Code, their overall thrust is to promote business rather than to accomplish exclusively 501(c)(3) objectives. Thus, the organization's activities lack the qualities of those that rendered the organization described in Rev. Rul. 74-587 exempt from Federal income tax under section 501(c)(3). The organization described in that Revenue Ruling provides funding only to businesses located in a deteriorated area whose owners could not obtain conventional financing. As the

Revenue Ruling notes, the end result of the provision of funds was the accomplishment of the charitable purpose of lessening prejudice, eliminating poverty, reducing neighborhood tensions, and combatting community deterioration. The organization described in Situation 1 does not limit its activities in this regard and provides assistance not only to businesses similar to those described in the Revenue Ruling, but also to businesses which are not owned by minority groups and which are not experiencing difficulty because of their location in a deteriorated section of the community.

'The activities of the organization described in Situation 2 result in major benefits accruing to the stores that will locate within the shopping center. The organization does not limit its aid to businesses that are owned by members of a minority group or to businesses that would only locate within the area because of the existence of the center. The end result is that this organization's activities are directed to benefit the businesses in the shopping center rather than exclusively to accomplish 501(c)(3) purposes.

'Accordingly, neither organization qualifies for exemption from Federal income tax under section 501(c)(3) of the Code.