24 T.C. 15 (1955)

A charitable foundation, otherwise qualifying for tax exemption, does not lose its exemption because it engages in a profitable activity, such as the sale of whiskey, if that activity is incidental to its charitable purpose and arises from its status as a stockholder.

Summary

The Alan Levin Foundation, a non-profit corporation, was established to engage in charitable activities. The foundation purchased stock in American Distilling Company, which offered its stockholders the opportunity to purchase whiskey at cost. The foundation acquired the whiskey and resold it at a profit. The Commissioner of Internal Revenue argued that the foundation was primarily engaged in a wholesale liquor business and thus did not qualify for tax-exempt status. The Tax Court held in favor of the foundation, concluding that the whiskey sales were incidental to the foundation's charitable purpose and its status as a stockholder, not its primary business activity. The Court emphasized that the foundation's actions were temporary, limited and that its primary purpose was to generate funds for charitable endeavors.

Facts

Maurice Levin, along with his family, purchased shares of American Distilling Company (American) stock before February 1944. American's board of directors decided in November 1943 to allow its stockholders to buy whiskey at cost. The Alan Levin Foundation (the Foundation) was incorporated on February 28, 1944, as a non-profit organization, and then purchased American stock from Levin and his family. The Foundation subsequently exercised its right as a stockholder to purchase whiskey and resold it at a profit. The Foundation had no other significant business activities. The Foundation used the proceeds, including those from the whiskey sales, for charitable purposes.

Procedural History

The Commissioner of Internal Revenue determined deficiencies in the Foundation's income tax for fiscal years 1945 and 1946, arguing that the Foundation did not qualify for tax-exempt status under Section 101(6) of the 1939 Internal Revenue Code. The Foundation appealed to the United States Tax Court.

Issue(s)

Whether the Alan Levin Foundation, a non-profit corporation, was exempt from income tax under Section 101(6) of the Internal Revenue Code during the fiscal years ending February 28, 1945 and 1946, despite its activities in purchasing and selling whiskey.

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Holding

Yes, because the Tax Court held that the Foundation qualified for tax-exempt status, as its whiskey sales were incidental to its charitable purpose, and the Foundation's activities did not constitute the primary purpose of its operations.

Court's Reasoning

The court referenced the statutory requirements for exemption under section 101(6), stating that the petitioner "was a foundation organized and operated exclusively for charitable purposes." The court considered that the Foundation's primary purpose was charitable, as evidenced by its certificate of incorporation and the use of its income, and its activities in the whiskey business were only an incidental means of generating funds. The court focused on the fact that the liquor sales were limited, temporary, and incidental to the Foundation's stock ownership and did not represent an ongoing business. The court found that the Foundation was not organized and operated primarily for the purpose of carrying on a wholesale liquor business for profit. The court distinguished the facts from cases where the non-exempt activities were the primary focus. The court also emphasized that the Foundation took advantage of an opportunity offered to all stockholders. The court stated, "The petitioner took advantage of the opportunity…which American gave its stockholders…but…had no regularly established place of business, did not purchase whiskey in the market for resale, did not handle the whiskey, and was not engaged in the operation for profit of a continuing business."

Practical Implications

This case is significant because it clarifies the boundaries of tax-exempt status for charitable foundations that engage in activities that generate profit. It indicates that a charitable foundation can engage in profitable activities without losing its tax exemption, provided those activities are incidental to its primary purpose. The case highlights that the nature of an activity and its connection to the exempt purpose are paramount. Lawyers advising charitable foundations should consider:

1. Assessing the extent and nature of any business activity to ensure it is truly incidental.
2. Documenting the primary charitable purpose and how the business activity supports that purpose.
3. Monitoring the level of business activity to ensure it does not become the primary focus.

This case offers guidance for foundations, allowing them to generate income for charitable purposes without being automatically disqualified for tax exemptions due to incidental business activities. This case has been cited in subsequent cases involving the interpretation of the scope of permitted activities for tax-exempt organizations, providing a useful precedent in analyzing similar situations.

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