

B. S. W. Group, Inc. v. Commissioner, 70 T. C. 352 (1978)

To qualify for tax-exempt status under Section 501(c)(3), an organization must be operated exclusively for exempt purposes, not primarily for commercial business.

Summary

B. S. W. Group, Inc. sought tax-exempt status under Section 501(c)(3) for providing consulting services to nonprofit organizations. The IRS denied the exemption, arguing that B. S. W. 's operations resembled a commercial business. The Tax Court upheld the denial, emphasizing that B. S. W. 's activities were not exclusively for charitable, educational, or scientific purposes but were primarily commercial. The court noted the lack of evidence that B. S. W. 's services were not in competition with for-profit businesses and that its fee structure aimed to produce a profit, indicating a commercial purpose.

Facts

B. S. W. Group, Inc. was formed to provide consulting services to nonprofit organizations involved in rural policy and program development. These services included connecting clients with independent consultants for research projects. B. S. W. intended to charge fees at or close to cost, but not less than cost, aiming to generate a small profit. The IRS denied B. S. W. 's application for tax-exempt status under Section 501(c)(3), citing that B. S. W. 's operations were primarily commercial in nature.

Procedural History

B. S. W. Group, Inc. applied for tax-exempt status under Section 501(c)(3) on April 5, 1976. The IRS issued a final adverse ruling on July 8, 1976, which was reissued on April 5, 1977. B. S. W. then sought a declaratory judgment from the U. S. Tax Court, which upheld the IRS's determination on May 30, 1978.

Issue(s)

1. Whether B. S. W. Group, Inc. is operated exclusively for charitable, educational, or scientific purposes within the meaning of Section 501(c)(3).

Holding

1. No, because B. S. W. Group, Inc. 's primary purpose is commercial, not charitable, educational, or scientific, as evidenced by its fee structure, profit motive, and potential competition with for-profit businesses.

Court's Reasoning

The court applied the operational test under Section 501(c)(3), which requires that

an organization be operated exclusively for exempt purposes. B. S. W. 's activities were deemed commercial because they were similar to those of for-profit consulting firms, including charging fees designed to cover costs and generate profit. The court emphasized the lack of evidence showing that B. S. W. 's services were not in competition with commercial businesses. Furthermore, B. S. W. did not limit its services to Section 501(c)(3) organizations, and its fee structure did not include provisions for below-cost services, which are often required for charitable status. The court referenced Revenue Ruling 72-369, which denies exemption to organizations providing services at cost to exempt organizations if those services resemble a commercial trade or business.

Practical Implications

This decision clarifies that organizations seeking tax-exempt status under Section 501(c)(3) must ensure their operations are exclusively for exempt purposes, not primarily for commercial gain. Legal practitioners advising clients on nonprofit formation should emphasize the importance of demonstrating that the organization's activities are not in competition with for-profit entities and that any fees charged are not designed to generate profit. This ruling may impact similar cases by reinforcing the need for clear delineation between commercial and charitable activities. Organizations providing services to nonprofits should consider how their fee structures and client bases align with the requirements for tax-exempt status.