

Presbyterian & Reformed Pub. Co. v. Commissioner, 79 T. C. 1070 (1982)

A nonprofit organization's tax-exempt status can be revoked if its operations shift toward a substantial commercial purpose.

Summary

Presbyterian & Reformed Publishing Co. was granted tax-exempt status in 1939 for publishing religious materials. By the 1970s, it had transitioned from a volunteer-driven operation to a more commercial enterprise, evidenced by significant profits, paid staff, and book sales practices. The IRS retroactively revoked its exemption to 1969, but the Tax Court adjusted this to 1975, finding that the organization's operations had materially changed by that year, driven by a substantial commercial purpose, while still recognizing its religious mission.

Facts

Presbyterian & Reformed Publishing Co. (petitioner) was incorporated in 1931 and granted tax-exempt status in 1939 for publishing a religious journal. By the mid-1970s, its operations had evolved significantly: it began paying royalties, hired paid staff, engaged in book sales with other publishers, and adopted a more commercial approach to pricing and operations. Its profits increased dramatically, with net profits from book sales reaching \$106,180 in 1975. The IRS initiated a review in 1978, leading to a final revocation letter in 1980.

Procedural History

The IRS issued a determination letter granting tax-exempt status in 1939. In 1978, the District Director informed the petitioner of a possible revocation. The final revocation letter was issued in 1980, effective from 1969. The petitioner sought a declaratory judgment from the U. S. Tax Court, which upheld the revocation but adjusted the effective date to 1975.

Issue(s)

1. Whether the petitioner was operated exclusively for an exempt purpose under section 501(c)(3) of the Internal Revenue Code.
2. Whether the Commissioner abused his discretion in making the revocation retroactive to January 1, 1969.

Holding

1. No, because the petitioner's operations had shifted toward a substantial commercial purpose by 1975, evidenced by significant profits, pricing strategies, and competition with commercial publishers.
2. Yes, because the material change in operations justifying revocation did not occur until 1975; thus, the retroactive revocation to 1969 was an abuse of discretion.

Court's Reasoning

The court examined the operational test under section 501(c)(3), focusing on whether the organization's activities were directed toward an exempt purpose. It found that the petitioner's transition to a commercial enterprise, characterized by substantial profits, pricing to break even on sales, competition with other publishers, and increased commercial practices, indicated a primary commercial purpose. The court cited cases like *Scripture Press Foundation v. United States* and *Inc. Trustees of Gospel Wkr. Soc. v. United States* to support its view that substantial profits and commercial competition were strong indicators of a nonexempt purpose. Regarding retroactivity, the court applied Revenue Procedure 80-25, which limits retroactivity to the date of material change, concluding that this occurred in 1975, not 1969.

Practical Implications

This decision underscores the importance of maintaining a clear focus on exempt purposes in nonprofit operations. Organizations must be cautious about adopting commercial practices that could suggest a shift toward nonexempt purposes. The case also highlights the IRS's ability to revoke exempt status retroactively, subject to procedural limits, which impacts how nonprofits should manage and report changes in their operations. Subsequent cases may reference this decision when evaluating the balance between nonprofit missions and commercial activities, particularly in the publishing sector.