E. IRC 501(c)(3) ORGANIZATIONS AND PUBLISHING ACTIVITIES

1. Introduction

Publishing activities may be a means of attaining an exempt purpose or an ordinary commercial venture. The purpose of this article is to explain how exempt publishing activities may be distinguished from commercial publishing operations.

2. Background

Religious and educational organizations have traditionally relied on publications as one of the primary means of accomplishing their exempt purposes. The permissible range of publishing activity encompasses publications that further the specific religious, educational, literary, or scientific endeavors of an exempt organization. Income from publications not furthering these exempt purposes is subject to unrelated business income tax. If the unrelated publishing becomes a primary purpose, then exemption is denied. For additional publishing standards applicable to scientific research organizations, see the 1986 CPE Book at Topic O, Scientific Research Under IRC 501(c)(3), beginning at page 195.

When the publishing activity is large, considerations apart from exempt organizations tax law may make it advantageous for an exempt organization to set up a separately incorporated publishing operation rather than to operate the activity as an integral part of its activities. Thus, the publishing activity may be conducted through a separately incorporated for profit subsidiary. In such cases, there is a significant legal barrier to overcome before the commercial activities of a separately incorporated subsidiary may be attributed to its parent as noted in the 1986 CPE Book at Topic E, For-Profit Subsidiaries of Tax-Exempt Organizations, on pages 33 through 35.

If the subsidiary a nonprofit corporation, then it may establish its own exemption as explained in Rev. Rul. 54-243, 1954-1 C.B. 92. Under exempt organizations tax law, the same tests apply whether the publishing is carried on by a separately incorporated subsidiary or as an unincorporated activity of an exempt organization. If the publishing activity is unrelated business, it is taxed under IRC 513(c) even if carried on within a larger aggregate of endeavors which may be related to the organization's exempt purposes. However, if the primary purpose for engaging in publishing is the nonexempt one of operating a trade or business for

profit, with no other significant charitable or educational activities, an organization does not qualify for exemption under IRC 501(a) as being described in IRC 501(c)(3). For example, the foreign language magazine described in Rev. Rul. 60-351, 1960-2 C.B. 169, was not qualified under IRC 501(c)(3) because it was operated to conduct activities which were indistinguishable from those of an ordinary commercial publishing enterprise.

The IRC 502 regulations also provide that a subsidiary of an exempt organization will not be exempt if it is operated for the primary purpose of carrying on activities that would be unrelated business if carried on directly by its parent. For example, Rev. Rul. 73-164, 1973-1 C.B. 223, concluded that a church-controlled commercial printing corporation whose business earnings are paid periodically to the church, but which has no other significant charitable activity, is a feeder organization as described in IRC 502 and does not qualify for exemption under IRC 501(a) as an organization described in IRC 501(c)(3).

In trying to decide whether publishing primarily furthers exempt purposes, the analysis employed is a highly factual one and the resolution of one case often provides little guidance for the next. The need for objective criteria in this area was addressed by the publication of Rev. Rul. 67-4, 1967-1 C.B. 121.

3. Rev. Rul. 67-4

A. Criteria

In order to be described in IRC 501(c)(3), a publishing organization must be operated exclusively for charitable purposes. These include religious or educational purposes. Often times, educational activities may also include literary and scientific publishing. In Rev. Rul. 67-4, 1967-1 C.B. 121, the Service recognized four criteria indicating that publishing activities are directed to the attainment of purposes specified in IRC 501(c)(3). These criteria are: (1) The content of the publication must be "educational"; (2) The preparation of materials must follow methods generally accepted as "educational" in character; (3) The distribution of the materials must be necessary or valuable in achieving the organization's exempt purposes; and (4) The manner in which the distribution is accomplished must be distinguishable from ordinary commercial publishing practices. Under this standard, it is not sufficient that a particular publication be educational, since books generally have this attribute to a greater or lesser degree. Also, while the revenue ruling speaks only in terms of educational purposes, similar reasoning is applicable to religious publishing activities. However,

religious publishing activities do not have to satisfy the methodology test, the second criterion.

B. Application

The organization described in Rev. Rul. 67-4 was formed to encourage basic research in specific types of physical and mental disorders, to improve educational procedures for teaching those afflicted with such disorders, and to disseminate educational information about such disorders by the publication of a journal containing current technical literature relating to these disorders. The revenue ruling states that the organization would have to meet the four criteria set forth above in order to be described in IRC 501(c)(3). The organization was found to qualify under under IRC 501(c)(3) because the methods used in preparing and presenting the research information conformed to methods traditionally accepted as "educational" in character. The organization provided a reference to literature on the research undertaken in the area, and enabled the afflicted to receive improved instruction and treatment. The distribution of the abstracts was carried out essentially in a "charitable" manner, in the sense that there was a public benefit derived from the distribution. The charges for the publication recovered only a portion of the costs.

C. Educational Content and Methodology

The first two of the four criteria relate to educational content and educational methodology. The term "educational" is defined in Reg. 1.501(c)(3)-1(d)(3) as relating to (a) the instruction or training of the individual for the purpose of improving or developing his capabilities; or (b) the instruction of the public on subjects useful to the individual and beneficial to the community. The regulation goes on to state that an organization may be educational even though it advocates a particular position or viewpoint, so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

The definition of the term "educational" contained in Reg. 1.501(c)(3)-1(d)(3) was found to be unconstitutionally vague in Big Mama Rag, Inc. v. U.S., 631 F.2d 1030 (D.C. Cir. 1980). The case involved the Service's denial of exemption recognition to a feminist organization that published a monthly newspaper. The court noted that the guidelines in Rev. Rul. 67-4 "use the same

conclusory terms as the regulation and are not helpful in clarifying [the meaning of 'educational' as set forth in the regulations]." The decision, therefore, called into question the validity of the standards set forth in Rev. Rul. 67-4.

In National Alliance v. U.S., 710 F.2d 868 (D.C. Cir. 1983), the court upheld the Service's position that the organization in that case was not educational. Although no question as to the constitutionality of Reg. 1.501(c)(3)-1(d)(3) was presented, the court did note that the methodology test used by the Service when applying the regulation "tends toward ensuring that the educational exemption be restricted to material which substantially helps a reader or listener in a learning process." The court also noted that the application of this test reduced the vagueness found in the earlier Big Mama Rag decision.

The methodology test cited with approval by the court in the National Alliance case was set forth in Section 3 of Rev. Proc. 86-43, 1986-2 C.B. 729. The revenue procedure, reproduced at page 76, notes that the formal publication of the methodology test represents no change either to existing procedures or to the substantive position of the Service. Therefore, Rev. Rul. 67-4 continues to be an accurate statement of the Service's position on exempt publishing activities.

The methodology test focuses on the techniques used by an organization in advocating a position on controversial subjects rather than on the position or viewpoint itself. The techniques used will not be considered to be educational if they fail to provide a factual foundation for the viewpoint or position being advanced or fail to provide relevant facts that would materially aid a listener or reader in a learning process. Rev. Proc. 86-43 thus provides additional authority for testing the qualification of organizations claiming exemption as educational organizations based on their publishing activities.

4. Conversion of a For Profit Publication

Although the G.C.M. discussed below cannot be used or cited as precedent, it illustrates the type of analysis employed in applying the Rev. Rul. 67-4 standard to distinguish exempt publishing activities.

G.C.M. 38845 (January 21, 1982) provides an example of a commercial magazine that changed its operation and qualified for exemption under IRC 501(c)(3). It should be noted that the reorganization did not serve the private interests of individuals associated with the commercial publisher. This is important to keep in mind, since an otherwise exempt activity will not support a favorable

determination if the organization's operations result in proscribed benefit to private interests. For example, Rev. Rul. 76-441, 1976-2 C.B. 147, and Hancock Academy of Savannah v. C.I.R., 69 T.C. 488 (1978), concerned the disqualification under IRC 501(c)(3) of for-profit schools attempting to convert into exempt organizations because private rather than public interests were served.

In G.C.M. 38845 a for profit newspaper had been publishing a magazine. The magazine had first been published in 1850 and had come to be generally recognized as a magazine of literary distinction. The magazine was not profitable and the for profit corporation was about to cease its publication. An exempt private foundation purchased the magazine from the for profit corporation. The foundation established an independent nonprofit corporation to publish the magazine. The publishing foundation sought exemption under IRC 501(c)(3).

The publishing foundation planned to take a number of steps designed to assure that the magazine would maintain high standards of literary quality. Its board of directors consisted of independent persons selected for their acknowledged stature in journalism and the literary arts. The foundation planned to form an advisory board of distinguished writers to assist its board of directors in promoting literary excellence. The foundation planned to expand the magazine's editorial content to include articles on linguistics, the English language, and literary traditions. It also planned to conduct a writing competition for young people and to provide summer internships for college students. In addition, the foundation planned to publish public service pamphlets for distribution through libraries and schools and expected to conduct public seminars at colleges and universities to educate students in literary techniques and journalism methods.

The publishing foundation received its financial support from magazine sales, subscriptions, and advertising; contributions from two private foundations in amounts equal to the magazine's operating losses up to a specified maximum amount; and gross investment income which constituted less than one-third of its financial support. For the first year of its operations the publishing foundation had a substantial loss. The prospect of future profits was considered to be remote so that it would continue to be dependent on contributions.

Chief Counsel analyzed the organization's activities in terms of the four criteria contained in Rev. Rul. 67-4, supra, as follows.

A. The first criterion, that the content of the publications be educational, was satisfied because the content of the magazine was educational in that it would

educate the public by adding to the sum total of knowledge on standards of literary excellence and on substantive issues of public policy, the arts and the humanities. The foundation would serve educational goals both through publication of the magazine and its ancillary activities. The foundation instructed the public in methods of obtaining knowledge through clear expression and analysis as well as by imparting substantive knowledge on the arts and humanities.

B. The second criterion, that the publication be prepared in accordance with methods traditionally accepted as educational in character, was also found satisfied. Of importance was that selection of articles would be chosen for literary merit rather than commercial appeal; the focus of articles would be on serious fiction, poetry and issues of public policy rather than on articles of popular mass appeal; many articles would be written by leading authors, journalists, professors of English and educators; and the foundation would be encouraging new writers through its ancillary activities. (In this context, the methodology criteria developed in Rev. Proc. 86-43, supra, would also be satisfied since the activities of this publishing foundation show that it seeks to promote writing that would develop facts that would materially aid a reader in a learning process or in understanding a viewpoint being advocated.)

C. The third criterion, that the distribution of the publication be necessary to achieve the organization's purpose, was found present since without publication and distribution of the magazine the foundation could not achieve its stated purpose of promoting literary excellence nor could it function as a forum for articles and writers unlikely to be published in profit-oriented magazines.

The foundation was distinguished from the foreign language magazine described in Rev. Rul. 60-351, supra, which publication could not be shown as necessary to the achievement of any charitable or educational purpose, but rather was published and sold to the general public as a business enterprise.

D. Chief Counsel, in analyzing the fourth criterion, summarized the factors which the Service and the courts have relied on in deciding whether an organization's publishing activities are "sufficiently distinguishable from ordinary commercial practices so as to be conducted primarily as a means of carrying out some exempt purpose" as follows:

(1) Conducting as its sole activity publishing activities using standard commercial techniques which generate ongoing profits.

(2) Pricing its materials "competitively" with other commercial publications or to return a profit.

(3) Conducting an enterprise in a manner in which all participants expect to receive a monetary return.

(4) Publishing its materials almost exclusively for sale, with only a de minimis amount of material donated to charity.

(5) Creating or accumulating large profits and accumulating profits from sales activities which are greatly in excess of the amounts expended for educational purposes.

Chief Counsel further noted that the primary factor relied on to demonstrate an exempt purpose is that the foundation distributes its literature without regard to the realization of net profits. Thus, in Rev. Rul. 67-4 the organization's method of distributing its medical journal, by charging amounts for the publication which allowed only recovery of a portion of the costs, was the primary factor relied upon in distinguishing that organization's activities from ordinary commercial practices.

Chief Counsel noted that the magazine under consideration contained a much lower percentage of space devoted to advertising than was common among for profit magazines. In fact, the percentage of advertising was lower than that contained in many nonprofit publications. Further, the magazine contained no articles at all on certain subjects of popular appeal such as sports, fashion, food, drink, popular music and movies. The foundation did not engage in competitive pricing, did not emphasize monetary return, and was not accumulating profits--rather, it was operating at a loss.

After summarizing the operational characteristics of the publication activities, Chief Counsel completed the analysis by showing how other facts in the case related to attainment of the magazine's overall objective of promoting literary quality. The independent governing body, the advisory board, and the activities undertaken in association with colleges and universities were recognized as evidence of an intent to operate in a manner different from the normal operations of a commercial publishing enterprise. Chief Counsel concluded as follows:

> The [foundation's] scholarly selection of topics, their treatment and the magazine's low percentage of advertising content lead to the conclusion that [the

> foundation's] publishing procedures are not those of ordinary commercial publishers. Rather, the [foundation] has provided sufficient evidence to establish that its purpose in publishing [the] magazine is to further section 501(c)(3) literary and educational purposes by promoting literary excellence for the educational benefit of the public. In short, the [foundation] has established its right to recognition of exemption by satisfying the test of Rev. Rul. 67-4.

5. Commercial Publishing Activities

Both religious and educational publishing organizations must meet the fourth requirement of Rev. Rul. 67-4; that is, their activities must be distinguishable from the activities of an ordinary commercial publishing operation. Rev. Rul. 77-4, 1977-1 C.B. 141, provides an example of an ordinary commercial publishing operation.

The organization described in Rev. Rul. 77-4 was a nonprofit corporation which published a weekly newspaper. The newspaper contained local, national, and world news, editorials and paid advertising. The newspaper's editorial content focused on matters of interest to members of a particular ethnic group. Although the organization had been in existence for several years, it had never realized a profit from its operations. The organization was supported by charges for advertising and payments for subscriptions. Its primary expenses were for employee wages and printing costs. The revenue ruling notes that the newspaper's employees did not have any particular qualifications which would serve to distinguish them from the employees of other newspapers generally. The revenue ruling concludes that the ethnic newspaper was operated in a manner indistinguishable from that of an ordinary commercial publishing enterprise. Therefore, the organization was not exempt under IRC 501(c)(3) of the Code.

6. The Primary Purpose Test

Factual situations which fall somewhere between the two poles represented by Rev. Ruls. 67-4 and 77-4 turn on interpretations of fact. The legal issue to be resolved in such cases is whether the organization's primary purpose is a commercial purpose or an exempt purpose. If the organization's primary purpose is an exempt purpose, publishing activities substantially related to the attainment of that purpose will not be ordinary commercial operations.

A A review of the older court cases in this area is contained in Pulpit Resource v. C.I.R., 70 T.C. 594, (1979). The case involved the publication of a monthly journal devoted to advancing the art of preaching. Each issue of the journal contained "at least six highly crafted sermons." The journal was sold on a subscription basis to clergy of various religious faiths.

The Service denied Pulpit Resource's application for recognition of exemption under IRC 501(a) as being described in IRC 501(c)(3) on the ground that the operations of the organization "closely resembled a commercial enterprise organized for profit." The Service characterized the organization as "a profitmaking publisher of specialized literature operated for a business purpose." The organization filed a declaratory judgment petition in the Tax Court.

The court noted that the Service's denial of exempt status to Pulpit Resource rested on the theory that an organization operated for a commercial purpose was not "operated exclusively" for any of the purposes specified in IRC 501(c)(3). Since Pulpit Resource had only one activity, the publication of a monthly journal, this must mean that a single activity could serve both an exempt and a commercial purpose. The problem before the court was, therefore, to determine which purpose was the primary purpose of Pulpit Resource. While decided cases could offer some guidance, the court noted that "it is apparent that the relevant facts in each individual case must be strained through those principals to arrive at a decision on the particular case."

The court stated that Pulpit Resource's activities "had a commercial or business hue--it was selling religious literature to clergy." It had made a small net profit after paying a reasonable salary to its founder and only employee, a United Methodist minister. The presence of net profits suggested that the organization had a commercial rather than a charitable purpose.

On the other hand, the court noted that the presence of a profit was not fatal to exemption. Further, the actual market for the organization's journal seemed to be so limited that it would not attract a truly commercial enterprise. Also, no royalties were being paid to the founder/employee who authored the sermons that appeared in the organization's journal. Weighing these facts and circumstances against one another, the court concluded that Pulpit Resource was operated exclusively for religious and charitable purposes.

B. A more recent case, The Incorporated Trustees of the Gospel Worker v. U.S., 510 F. Supp. 374 (D.D.C. 1981), applied a similar analysis and affirmed the Service's revocation of a religious publishing house's exempt status. In that case, the organization had formerly been engaged in the operation of missions and had conducted a variety of public evangelizing efforts over a period of many years. However, these activities had ceased by 1962. Since that time the organization's activities had consisted of operating a home for its aging members and operating a religious publishing house unaffiliated with any denomination. Although some of its publications were published at a loss, the organization had shown increasing profits since the 1960's and had accumulated profits of over 5.3 million dollars by 1978. The salaries of the officials of the publishing house had similarly increased during the same time period. The policies and practices of the organization in regard to content, payment of royalties, wholesale pricing and broad marketing programs were the same as those employed by a number of nonexempt commercial publishers of fundamentalist Christian literature.

The court noted the pattern of accumulation of profits, escalating salaries for top officials, and the similarity of the organization's publishing activities to those of a commercial religious publisher. The court stated that—

> taken together [these factors] present a picture of a publishing enterprise the primary purpose of which is profits, not salvation. To put it another way, to find the primary purpose behind the activities of the Gospel Worker Society at the present time is religious rather than commercial would be "to avoid reality."

In its analysis the court noted the presence of an additional consideration in cases presenting a fact pattern that involves an organization conducting religious activities while also carrying on a trade or business for profit. The court stated that the main inquiry in such a situation is whether the profit-producing activity is merely incidental to and in furtherance of the religious activities and their exempt purpose:

> See e.g., Scripture Press Foundation v. United States, 285 F. 2d 800 (Ct. Cl. 1961) (organization's door-to-door evangelism and religious instructional activities incidental to sale of religious literature for profit); Saint Germain Foundation v. Commissioner, 26 T.C. 648 (1956) (organization's sale of religious publications

producing income incidental to its religious purposes as manifested through the conduct of religious classes and conclaves).

C. Although the courts have accepted the view that exempt publishing activities are distinguishable from similar activities conducted for commercial purposes, questions still arise as to the weight to be accorded specific facts in actual cases. In Presbyterian & Reformed Publishing Co. v. C.I.R., 79 T.C. 1070 (1982), the Tax Court found that the manner in which the organization conducted its publishing activities revealed a nonexempt commercial purpose that was substantial in nature. In making this determination, the court noted that whether an organization satisfies the operational test is essentially a question of fact. The court noted that where a nonexempt purpose is not an expressed goal of the organization, courts have nonetheless focused on the manner in which the organization conducts its activities, implicitly reasoning that an end can be inferred from the means chosen to attain it. If, for example, an organization's management decisions replicate those of commercial enterprises, it is fair to infer that at least one purpose of the organization is commercial. Among the factors and cases to which the court looked in deciding what ends the organization's activities furthered were the following.

(1) The presence of substantial profits and accumulations, while not determinative, constitutes evidence indicative of a commercial character. (Scripture Press Foundation, supra; B.S.W. Group v. C.I.R. 70 T.C. 352 (1978)).

(2) The method of pricing books, whether at break even or below cost, to encourage readership rather than to generate profits (Peoples Translation Service v. C.I.R., 72 T.C. 42 (1979)).

(3) Competition with commercial publishers as the exclusive vendor of the books sold in terms of whether the scope of the enterprise would attract a truly commercial enterprise (B.S.W. Group, Inc. v. C.I.R., supra; American Institute for Economic Research v. U.S., 302 F. 2d 934 (Ct. Cl. 1962); Christian Manner International v. C.I.R. 71 T.C. 661 (1979); Pulpit Resource v. C.I.R., supra.).

(4) Other factors weighing against the organization were aggressive commercial practices resembling those undertaken by commercial publishers.

(5) Favorable factors indicating a nonprofit-oriented approach included past reliance on volunteers and modest wages paid, sale of some books that were

not profitable, loans to its printer to ensure viability, and donations of books and funds to distributors of Presbyterian literature. However, these factors were outweighed by the commercial practices.

The publishing company appealed the Tax Court's decision to the United States Court of Appeals for the Third Circuit. The Circuit Court concluded that the Tax Court had applied the proper principles to the case, but had failed to give adequate weight to two important facts bearing on the organization's purpose in accumulating profits. One fact was the origin of the profits. The second fact was the intended purpose of their accumulation.

The Circuit Court noted that the organization had relied on donations to offset operating losses from its founding in 1931 until 1969. Beginning in 1969, books written by Jay Adams, a member of the faculty at Westminster Theological Seminary, were published by the organization. The popularity of Adams' books caused a sudden and unexpected escalation in the organization's profits. It was accumulating some of the profits in order to construct and equip a combined warehouse and office building to serve its publishing needs. According to the Circuit Court, the Tax Court focused too narrowly on the accumulations. In addition, the Tax Court failed to temper its conclusions concerning the nonexempt purpose of the accumulations in light of the fact that no evidence was presented which would suggest that the profits of the activity inured to the benefit of any private individual. When these considerations were given proper weight, the Tax Court's decision could not be sustained. Therefore, the organization was entitled to continuation of its exempt status. Presbyterian and Reformed Publishing Company v. C.I.R., 743 F. 2d 148 (3rd Cir. 1984).

The Presbyterian and Reformed case stands for the proposition that a denial of exemption to a nonprofit publishing house cannot be sustained solely on the ground that the organization realizes a profit from its operations. However, a pricing policy which is not designed to produce profits still carries considerable weight in favor of exemption. See Peoples Translation Service v. C.I.R., supra; Rev. Rul. 68-306, 1968-1 C.B. 257; Rev. Rul. 68-307, 1968-1 C.B. 258; Rev. Rul. 67-4, supra; Rev. Rul. 66-147, 1966-1 C.B. 137.

7. Conclusion

If an organization's primary purpose in conducting publishing, which represents its sole or primary activity, is to operate a commercial business producing net profits, the organization is not exempt under IRC 501(a) as an

organization described in IRC 501(c)(3). The decision as to what an organization's primary purpose is must be made in light of all of the relevant facts and circumstances in a particular case. Among the factors that should be considered are the organization's methods of pricing, presence of substantial profits from its operations, and the intended purpose of any accumulated profits. The mere presence of operating profits is not, by itself, a bar to exemption of a publishing organization.

At the same time, profits are the objective of commercial operations. Therefore, the presence of profits suggests that the organization's purpose is commercial. The presence of profits thus invites further inquiry as to how the profits were produced, for what purposes, and for whose benefit. Many successful denominational publishing houses have chosen to avoid the necessity of justifying their profits by organizing their publishing departments as for profit corporations.

Exempt publishers that do make a profit are often charged by their critics with competing unfairly with commercial publishers. In June, 1987 the Oversight Subcommittee of the House Ways and Means Committee heard testimony to this effect from commercial cartographers who complained that they were unable to compete effectively within a consumer market dominated by an exempt organization whose activities include producing magazines and maps.

26 CFR 601.201: Rulings and determination letters. (Also Part I, Section 501; 1.501(c)(3)-1.)

Rev. Proc. 86-43

SECTION 1. PURPOSE

The purpose of this revenue procedure is to publish the criteria used by the Internal Revenue Service to determine the circumstances under which advocacy of a particular viewpoint or position by an organization is considered educational within the meaning of section 501(c)(3) of the Internal Revenue Code, and within the meaning of section 1.501(c)(3)-1(d)(3) of the Income Tax Regulations.

SEC. 2. BACKGROUND

.01 Section 501(c)(3) of the Code provides for exemption from federal income tax for organizations that are organized and operated exclusively for purposes specified in that section, including educational purposes. Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term "educational" relates to a) the instruction or training of the individual for the purpose of improving or developing his capabilities; or b) the instruction of the public on subjects useful to the individual and beneficial to the community. Under this regulation, an organization may be educational even though it advocates a particular position or viewpoint, so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

.02 In applying section 1.501(c)(3)-1(d)(3) of the regulations, the Service has attempted to eliminate or minimize the potential for any public official to impose his or her preconceptions or beliefs in determining whether the particular viewpoint or position is educational. It has been, and it remains, the policy of the Service to maintain a position of disinterested neutrality with respect to the beliefs advocated by an organization. The focus of section 1.501(c)(3)-1(d)(3), and of the Service's application of this regulation, is not upon the viewpoint or position, but instead upon the method used by the organization to communicate its viewpoint or positions to others.

.03 Two recent court decisions have considered challenges to the constitutionality of section 1.501(c)(3)-1(d)(3) of the regulations. One decision held that the regulation was unconstitutionally vague. Big Mama Rag, Inc. v. United States, 631 F. 2d. 1030 (D.C. Cir. 1980). However, in National Alliance v. United States, 710 F. 2d 868 (D.C. Cir. 1983), the court upheld the Service's position that the organization in question was not educational. Although the latter

decision did not reach the question of the constitutionality of section 1.501(c)(3)-1(d)(3), it did note that the methodology test used by the Service when applying the regulation "tend[s] toward ensuring that the educational exemption be restricted to material which substantially helps a reader or listener in a learning process." The court also noted that the application of this test reduced the vagueness found in the earlier Big Mama Rag decision.

.04 The methodology test cited by the court in National Alliance reflects the long-standing Service position that the method used by an organization in advocating its position, rather than the position itself, is the standard for determining whether an organization has educational purposes. This methodology test is set forth in Section 3 of this revenue procedure, and is used in all situations where the educational purposes of an organization that advocates a particular viewpoint or position are in question. Publication of this test represents no change either to existing procedures or to the substantive position of the Service.

SEC. 3. CRITERIA USED TO DETERMINE WHETHER ADVOCACY BY AN ORGANIZATION IS EDUCATIONAL

.01 The Service recognizes that the advocacy of particular viewpoints or positions may serve an educational purpose even if the viewpoints or positions being advocated are unpopular or are not generally accepted.

.02 Although the Service renders no judgment as to the viewpoint or position of the organization, the Service will look to the method used by the organization to develop and present its views. The method used by the organization will not be considered educational if it fails to provide a factual foundation for the viewpoint or position being advocated, or if it fails to provide a development from the relevant facts that would materially aid a listener or reader in a learning process.

.03 The presence of any of the following factors in the presentations made by an organization is indicative that the method used by the organization to advocate its viewpoints or positions is not educational.

1 The presentation of viewpoints or positions unsupported by facts is a significant portion of the organization's communications.

2 The facts that purport to support the viewpoints or positions are distorted.

3 The organization's presentations make substantial use of inflammatory and disparaging terms and express conclusions more on the basis of strong emotional feelings than of objective evaluations.

4 The approach used in the organization's presentations is not aimed at developing an understanding on the part of the intended audience or readership because it does not consider their background or training in the subject matter.

.04 There may be exceptional circumstances, however, where an organization's advocacy may be educational even if one or more of the factors listed in section 3.03 are present. The Service will look to all the facts and circumstances to determine whether an organization may be considered educational despite the presence of one or more of such factors.

SEC. 4. OTHER REQUIREMENTS

Even if the advocacy undertaken by an organization is determined to be educational under the above criteria, the organization must still meet all other requirements for exemption under section 501(c)(3), including the restrictions on influencing legislation and political campaigning contained therein.

1986-2 C.B. 729