

November 10, 1960

Commissioner of Internal Revenue
Washington 25, D. C.

Attention: T:R:PEO:4
WEL

Re: Iowa State College Research Foundation, Inc.

Sir:

The undersigned, Iowa State College Research Foundation, Inc., an Iowa corporation with its principal place of business in Ames, Story County, Iowa, hereby protests against and excepts and objects to the proposed denial of its application for exemption from Federal income tax as an organization described in Section 501(c)(3) of the 1954 Internal Revenue Code and the determinations and tax consequences resulting therefrom as set forth in your communications of September 13, 1960, for the grounds and reasons and upon the facts and subject to the terms, conditions and reservations hereinafter more particularly set forth:

1. The name of the taxpayer is the Iowa State College Research Foundation, Inc., 109 Morrill Hall, Iowa State College Campus, Ames, Iowa.
2. The date of your communication proposing said denial of exemption is September 13, 1960 (Extension of time within which to file protest having been previously granted).
3. Your communications of September 13, 1960, directs the Iowa State College Research Foundation, Inc. to file Federal income tax returns with the District Director of Internal Revenue for Iowa. This protest therefore covers any and all years in which the proposed denial of exemption would result in the Iowa State College Research Foundation, Inc. being required to file Federal income tax returns and pay any Federal income tax resulting therefrom.

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4. The Iowa State College Research Foundation, Inc. takes exception to, objects to and protests against the proposed recommendations, findings and determinations as set forth in your communications of September 13, 1960, as follows:

(a) The proposed determination that the Iowa State College Research Foundation, Inc. is not organized exclusively for one or more of the purposes specified in Section 501(c)(3) of the Internal Revenue Code or the Income Tax Regulations applicable thereto.

(b) The proposed determination that the Iowa State College Research Foundation, Inc. is not operated exclusively for one or more of the exempt purposes specified in Section 501(c)(3) of the 1954 Code.

(c) The determination set forth in your communications of September 13, 1960, whereby it is held that the only activity conducted by the Iowa State College Research Foundation, Inc. which may be in furtherance of an exempt purpose is the making of grants-in-aid to be used for research.

(d) The proposed denial of exemption under Section 501(c)(3) because of your proposed determination that the Iowa State College Research Foundation, Inc. has not clearly established that it does not receive patents, inventions or other valuable rights in return for any grants-in-aid for research purposes.

(e) The determination by you that the Iowa State College Research Foundation, Inc. is engaged primarily in processing patents, inventions and other rights for the purpose of receiving the income therefrom which the Iowa State College Research Foundation, Inc. is accumulating in a reserve for the purpose of continuing such activities and for making grants-in-aid.

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(f) The recommended denial by you of the exemption application of the Iowa State College Research Foundation, Inc. and your proposed determination that the Iowa State College Research Foundation, Inc. does not qualify for exemption from Federal income tax as an organization described in Section 501(c)(3) of the 1954 Internal Revenue Code.

(g) The proposed recommendation and finding that the Iowa State College Research Foundation, Inc. is required to file Federal income tax returns with the District Director of Internal Revenue for Iowa.

(h) The proposed recommendations and findings made by you in your communications of September 13, 1960, whereby contributions made by other parties to the Iowa State College Research Foundation, Inc. are not deductible by the donors as charitable contributions defined in Section 170(c) of the 1954 Internal Revenue Code.

5. The summary statement of grounds upon which the Iowa State College Research Foundation, Inc. relies is hereinafter set forth:

(a) The Iowa State College Research Foundation, Inc. is an Iowa corporation organized under the laws of the State of Iowa as a corporation not for pecuniary profit under the provisions of Chapter 504 of the Iowa Code. The objects of the corporation are to furnish grants-in-aid in support of educational, scientific and literary research at Iowa State University (formerly Iowa State College) at Ames, Iowa. The purposes of the corporation are exclusively scientific, educational and literary and such purposes must be accompanied by encouraging, aiding and promoting scientific investigation and research at Iowa State University in all departments thereof by the members of the faculty, staff, alumni and students of said university and their associates and by encouraging and aiding in the education and training of men and women to engage in research work at the University.

(b) The corporation, by its articles of incorporation, is given power to receive donations, gifts and bequests. The corporation is also given power to participate in the usual transactions required of any nonprofit corporation to further its charitable and scientific purposes. Under the laws of the State of Iowa it is customary to list in the articles of incorporation of all charitable corporations numerous so-called "business" powers which are inserted for the sole and only purpose of enabling the corporation to continue its charitable purposes. In numerous other states, these powers frequently exist by statute but in Iowa it is customary to place them in the articles of incorporation of all charitable corporations whether a church, college, hospital or similar organization. Any so-called "business" powers contained in the articles of incorporation are purely incidental and inserted for the sole and only purpose to enable the corporation to carry out its primary charitable and educational purposes. The so-called "business" powers are no more extensive than those found in the articles of incorporation of almost every church and other charitable organization organized under the laws of the State of Iowa. Under the Uniform Non-Profit Business Corporation Act which has been adopted by many states and, in fact, which is now being considered for adoption by the State of Iowa, the powers therein contained are much broader than the powers provided for in the articles of incorporation of the Iowa State College Research Foundation, Inc. Under the Uniform Act the articles themselves are drafted in an extremely short form and would not refer to the broad powers that the corporation would in fact have by virtue of the statutes, and it is submitted that a submission of the articles to the Commissioner of Internal Revenue which were adopted under the Uniform Act would raise no issue and would not be questioned, and yet a corporation so organized would have all of the powers specified in the articles of incorporation of the Iowa State College Research Foundation, Inc., as well as many others. Certainly it cannot be

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that one corporation which, by virtue of statute, has unlimited powers is exempt, and another identical corporation, because of situs in a state that does not provide the powers by statute and must, therefore, place those powers in its articles would thereby be non-exempt. It is not believed this is the position of the Internal Revenue Service, namely, that it will look to form rather than substance, and if it is the position of the Internal Revenue Service then the regulations expressing that position as referred to in the ruling of September 13, 1960, filed herein, are invalid.

(c) In the communications of the Commissioner dated September 13, 1960, great length is devoted to the listing of the powers of incorporation of this organization. The conclusion is then reached that because the powers are broad that that fact in and of itself prevents the corporation from being organized solely for exempt purposes. The corporation was in truth and fact organized solely for charitable, scientific and educational purposes, and has been solely operated in pursuance of these same purposes since the date of its organization. Any powers listed are incidental to the primary objects of the corporation and were inserted for the sole and only purpose of enabling the corporation to carry out its charitable, scientific and educational purposes in a business-like and efficient manner, and in conformity with the requirements of the laws of the State of Iowa.

(d) The membership of the corporation is limited to eleven persons, of whom one shall be the president of Iowa State University while occupying said office, one shall be a member of the Iowa State Board of Education, six shall be members of the faculty or staff on active duty at Iowa State University and the remaining members shall be alumni of Iowa State University

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not connected with the faculty or governing body thereof. This board of trustees is charged with the management, direction and control of the affairs of the corporation in the same manner as the board of trustees of any college, hospital or church.

(e) The corporation has endeavored to provide workable machinery for the management of patents as a service to Iowa State University. Any income received from patent royalty agreements has been used to pay the necessary operating expenses of the corporation with the balance dedicated to the primary objects of the corporation and used exclusively for scientific, educational and literary purposes. Grants-in-aid in furtherance of research have been made and any retained income has been dedicated for future grants-in-aid when appropriate personnel and opportunities are available. No effort has been made to retain income solely for the purpose of conserving operating income in future years. Any accumulation of income has resulted solely from the fact that the trustees in their discretion did not feel that appropriate personnel and projects were available at a specific time to award grants-in-aid, and further it was the attitude of the board of trustees that there should be a sufficient reserve in order to produce sufficient income for administration expenses, in that if the said reserve was so established that all future income could then be used solely for grants-in-aid in toto.

(f) Each and all of the receipts and income items received by the corporation have been properly accounted for and disbursed in accordance with the objects and purposes of the corporation and in accordance with sound business judgment.

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(g) In some instances the corporation has worked out arrangements whereby a percentage of the royalty receipts is retained by the inventor. The percentage of payment to the individual was in all instances a small percentage so that the corporation receives a valuable gift and donation from the arrangement. The manner in which said individuals received their royalty percentage was on a fixed basis whereby the Foundation would retain eighty-five per cent (85%) of all royalties for its further grants-in-aid work and the individual inventor would receive fifteen per cent (15%) of said royalties. For bookkeeping purposes this was the most convenient manner by which its distribution could be made, but it had the same effect and result as if the particular inventor had merely agreed to donate eighty-five per cent (85%) of the royalties to the Foundation and retained fifteen per cent (15%) for his own income, which was in fact the arrangement. It would be no different than the situation where a building owner wished to contribute to the Foundation and did so by donating to the Foundation each year eighty-five per cent (85%) of the rent from a particular building owned by him. Certainly it would not be suggested that the Foundation was giving him fifteen per cent (15%) of the building income. In the instant situation likewise the Foundation is certainly not giving to the inventor fifteen per cent (15%) of its income from a particular royalty. Rather, the inventor is giving to the Foundation eighty-five per cent (85%) of the royalty, but it is handled, as above noted, through the books of the Foundation for purposes of convenience to all parties.

(h) The records of the Foundation reflect that the average cost of each patent acquired by it is approximately Three to Five Hundred Dollars, which is expended solely for filing fees and attorneys' fees. There are no sums spent for further perfecting the invention nor for developing its use, nor for marketing the invention, nor for selling licenses thereon. The sole and only funds

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expended with reference to the patent is for the strictly clerical and administrative work done in obtaining the patent. This could all be done by the individual inventor, each in his own time and in his own way, with the same resultant income ultimately to the Foundation. Because it was merely put on an orderly basis by use of the Foundation office to process the paper work in connection with the patent, this, it would appear from the September 13, 1960, ruling, becomes objectionable as far as the exempt status of the Foundation is concerned. This is clearly an objection to form rather than substance and, it is submitted, is not a tenable objection.

(i) It is suggested in the letter of September 13, 1960, and in particular on page 4 thereof, that the Foundation makes its grants-in-aid in return for patentable inventions and other valuable rights. Your attention is directed to the application for exemption submitted hereto, and in particular to page 3 with reference to the 1957-58 grants-in-aid. Not only did not one of those grants-in-aid produce a patentable invention but also not one of those grants-in-aid could have conceivably produced a patentable invention, nor could any of such grants-in-aid have returned any patents or other valuable rights to the Foundation. They were each of such a nature that no return could be expected from them.

(j) The purpose of the grants-in-aid is to alleviate certain problems, both for the public as well as intra-university problems, either by direct financial assistance, such as in the purchase of needed equipment, or by research, such as in the instances where it is attempted to determine the cause of or the cure for a particular farm, commercial or public problem. Additionally, the grants-in-aid help to further the higher education of various individuals who are awarded fellowships in the particular areas offered by the Iowa State University. In some instances, due to

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the nature of the work, patentable inventions are developed, but only coincidentally to the purpose of the research, and in those instances those patents, if developed by a staff member of the University, are turned over to the Foundation in such a manner so that the Foundation may retain eighty-five per cent (85%) of the royalties for the purpose of using that money in furtherance of the above objectives. The purpose of the Foundation is now and has always been the alleviation of certain problems of the public and the University, as above noted, and the furtherance of advanced education, and the return of patents to the Foundation has always been only an incidental side benefit.

(a) For each and all of the grounds and reasons heretofore stated the proposed ruling is void and illegal and the application for exemption heretofore filed should be granted.

5. The taxpayer desires a conference on this protest.

6. This protest and all matters submitted in connection therewith are submitted and filed without waiver of or prejudice to the rights of the taxpayer, and the taxpayer reserves the right to assert any other, further or additional grounds of objection, exception and protest to the proposed ruling or to any proposed deficiency resulting therefrom or any additional tax, and the right to rely on all or any of the grounds and facts hereinbefore set forth, and the taxpayer further reserves the right to submit any other, further or additional facts or brief in support thereof or of any protest, exceptions or objections.

Respectfully submitted,

IOWA STATE COLLEGE RESEARCH FOUNDATION, INC.

By George R. Town
President

By Quincy C. Ayres
Secretary

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STATE OF IOWA)
) SS.
COUNTY OF STORY)

George R. Town and
Wmncy C. Ayres, being first duly sworn, on
oath depose and state that George R. Town
is President and Wmncy C. Ayres is Secretary
of the taxpayer corporation above named, and as such are duly
authorized to execute this protest; that they have read the foregoing
protest and are familiar with the statements therein contained, and
that the facts and statements are true and correct, to the best of
their knowledge, information and belief.

George R. Town
Wmncy C. Ayres

Subscribed and sworn to before me this 21st day of
November, A. D. 1960.

Roberta Fritchman
Notary Public in and for Story County, Iowa
My Commission Expires July 4, 1963

CERTIFICATE OF COUNSEL

The above and foregoing protest was prepared by the undersigned, Thomas M. Collins, counsel for the above and within named taxpayer, who is informed and believes that the facts contained therein are true, although he does not know the facts of his own knowledge.

Thomas M. Collins