



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

Number: **200450043**
Release Date: 12/10/04
SIN – 501.03-30

Date: September 14, 2004

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend

X =

Entity 1 =

Entity 2 =

Entity 3 =

Entity 4 =

A =

B =

C =

D =

E =

M =

d =

r =

s =

t =

u =

v =

w =

x =

Y =

Dear _____ :

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

The information submitted indicates that you were incorporated on d under the General Corporation Law of M. Article IV of your Certificate of Incorporation states the following:

"Said corporation is organized exclusively for charitable, religious, education, and/or scientific purposes, including for such purposes, the distribution to organizations that qualify as exempt organizations under Section 501(c)(3) of the Internal Revenue Code of 1954..."

You are one of the five related corporations formed by X. Simultaneously formed with you on d by X were Entity 2, Entity 3 and Entity 4. The submissions refer to them as A, B and C, respectively. You are referred to as D. Four years earlier, X had formed Entity 1.

A and B have each filed an application for recognition of exemption under section 501(c)(3) of the Code. C filed an application for recognition of exemption under section 501(c)(25) of the Code. Entity 1 is currently exempt under section 501(c)(3).

X is the sole officer holding the position of president of the five corporations (the Related Corporations). You indicated that the recent formation of the four corporations is the expansion of the work for the public good into a cooperative arrangement between all five corporations.

You indicated that in year _____, X gave y dollars to Entity 1 with the intention that it be used as a loan, be invested in a program of high interest return, the interest earned be kept by Entity 1, and the principal be returned to X. However, the person who had control of the fund embezzled the fund. Entity 1 has written off the amount in its books and treated it as a "donation" by X to allow him to deduct the amount on his personal income tax return.

You state the following information relating to the Related Organizations---

"We would like to use A as our 501(c)(3) Charitable Foundation to accept large donations, invest them and distribute specific amounts to B, a non-operating 501(c)(3) foundation, after B has solicited, received, reviewed and approved grant applications that fit the vision and mission of our system.

B will function as our non-operating 501(c)(3) pass-through organization. Grant and service proposals will be directed to this organization from other operating 501(c)(3) non-

profit organizations. B will thus handle the year to year distribution of funds as requested and received from A.

D and Entity1 will be two of the many operating 501(c)(3) non-profit organizations that will be eligible to receive grants from B.

C will function as section 501(c)(25)(A) through (G) holding corporation for real assets that can be best purchased by C and then leased to other 501(c)(3) non-profit organizations within the system. This will maximize the use of assets that can be time-shared by grantees, instead of being purchased and then only be used part-time. It will also simplify the change over from one non-profit to the next, if a grantee decides to "close its doors."

Our vision and mission is to provide the following:

1. Workshops and training that teach how to be successful at obtaining B grants, matching funds and/or sponsorships.
2. Workshops that teach how to share one's wealth that is above and beyond immediate needs in a way that benefits others and still protect the future needs of the philanthropist.
3. Workshops and training that teach how to improve one's spiritual, mental, physical, and emotional approaches to life.
4. Workshops on personal, business and relationship development.
5. Workshops on developing talents in any of the fine arts.

The financial data submitted in your application shows "zero" income and expenses for tax years _____ and _____. You indicated that while services were provided in year _____, no income was received until _____.

You state that your activities will include providing counseling services on u and related subjects, and the receiving of grants from the A System. You also call yourself E. You applied with the state for a designation of a r care center for x reimbursement. You did not obtain the designation, and you stated that the state "has decided NOT to fund our type of agency. They have limited r Services for s and their ancillaries."

You will provide counseling services for a fee. You indicate only t will provide the service. Your service fee is \$ _____ per hour. You indicate the rate is negotiated with v companies as well as w so patients' responsibility is only the required deductibles and co-pay. If the patient does not have insurance or has exceeded insurance benefits, you have a negotiable discount fee that ranges from \$ _____ for a single person's annual income from \$ _____, to \$ _____ for a single person's annual income of over \$ _____. There is no fee for income below \$ _____.

You will rely for financial support from service revenues and will use funds for payment of salaries, office and other operating expenses. You will pay X based on a percentage of your income but not to exceed the usual and customary rate for an organization of your size and a t.

You also indicated that for prior years X has not been compensated, as you have not received income.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable and other exempt purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order for an organization to be exempt under section 501(c)(3) of the Code it must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(2) of the regulations provides the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense and includes the relief of the poor and distressed or of the underprivileged. The term "charitable" has been interpreted to include the promotion of health.

In *People of God Community v. Commissioner*, 75 T.C. 127 (1980), the organization paid its minister, also a director who controls the organization, with a compensation based on a percentage of the organization's gross receipts. The Court found that with such compensation arrangement, a portion of the organization's earnings is being passed to the minister, and paying over a portion of gross earning to those vested with control of an organization constitutes private inurement. Accordingly, the Court held that the organization is not exempt under section 501 (c)(3) of the Code.

The courts have likewise found inurement of income in favor of private individuals and serving their private interests as grounds for disqualification for exemption under section 501 (c)(3) of the Code in the following cases: *Beth-El Ministries, Inc. v. U.S.*, 79-2 U.S.T.C., 9412 (payment of living expenses of members); *Church of Modern Enlightenment v. Commissioner*, T.C. Memo 1988-312 (July 25, 1988) (payment of the principal officer's living expenses and taxes); *Good Friendship Temple v. Commissioner*, T.C. Memo 1988-313 (July 25, 1988) (payment of officers' personal expenses) ; and *New Life Tabernacle v. Commissioner*, T.C. Memo 1982-367 (payment of members' living expenses).

It is clear that an organization will not be considered "operated exclusively" for an exempt purpose and, thus, not meet the "operational test" unless it is operated for public, rather than private interests. See section 1.501 (c)(3)-1(d)(1)(ii) of the regulations. An organization will likewise not be considered "operated exclusively" for an exempt purpose and, thus, not meet the "operational test" if its net earnings inure in whole or in part to the benefit of private individuals. See section 1.501 (c)(3)-1 (c)(2) of the regulations. These are separate

requirements within the "operational test" and failure to meet either one precludes an organization from qualifying for exemption under section 501 (c)(3).

Our analysis indicates that you have been formed for more than 2 years and have yet to operate. When you become operational you will engage in the activities of providing counseling services on u for a fee. Your fee will be derived from clients' third party payors, co-payments or your discounted fees for those without insurance or have exceeded their insurance benefits. In your operation, you pay your officer compensation based on a percentage of your income. The court in *People of God's Community, supra*, ruled that paying over a portion of gross earning to those vested with control of an organization constitutes private inurement.

Because your net earnings inure in whole or in part to the benefit of private shareholders or individuals, you are not operated exclusively for one or more exempt purposes. See section 1.501 (c)(3)-1 (c)(2) of the regulations. Therefore, you are not exempt under section 501 (c)(3) of the Code.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

Contributions to you are not deductible under section 170 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

In the event this ruling becomes final, it will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

If you decide to protest this ruling, your protest statement should be sent to the address shown below. If it is convenient, you may fax your reply using the fax number shown in the heading of this letter.

Internal Revenue Service
TEGE, SE:T:EO:RA:T:3

1111 Constitution Ave, NW
Washington, D.C. 20224

If you do not intend to protest this ruling, and if you agree with our proposed deletions as shown in the letter attached to Notice 437, you do not need to take any further action.

If you have any questions, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

Ronald J. Shoemaker

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437