



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce Street
Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: 11/27/2007

Number: **200809038**

Release Date: 2/29/2008

UIL: 501.03-01

LEGEND

ORG = Organization name Address = address XX = Date

ORG
Address

Certified Mail

Employer Identification Number:

Person to Contact

Employee ID Number

Tel:

Fax:

Form Required to be Filed

990 PF & 1120

Tax Years:

June 30, 20XX and subsequent

Dear _____ :

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). It is determined that you are no longer recognized as exempt from Federal income tax under IRC section 501(c)(3), effective July 1, 20XX, for the following reason(s):

You do not qualify as an organization described in I.R.C. § 501(c)(3) because you operate programs that do not exclusively serve an exempt purpose described in section 501(c)(3). You do not have a charitable activity and you operate a political action fund (PAC), contrary to the express prohibition as outlined in IRC 501(c)(3).

Contributions to your organization are not deductible under IRC section 170.

You are required to file Federal income tax returns on the form indicated above. You should file these returns within 30 days from the date of this letter, unless a request for an extension of time is granted. File the returns in accordance with their instructions, and do not send them to this office. Processing of income tax returns and assessment of any taxes due will not be delayed because you have filed a petition for declaratory judgment under IRC section 7428.

If you decide to contest this determination under the declaratory judgment provisions of IRC section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the

district court of the United States for the District of Columbia must be filed within 90 days from the date this determination letter was mailed to you. Contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

You also have the right to contact the Office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance or you can contact your nearest Advocate's office, in this case by calling () or writing to:

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

We will notify the appropriate State officials of this action, as required by IRC section 6104(c). You should contact your state officials if you have any questions about how this determination may affect your state responsibilities and requirements.

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Attachments:
Publication 892



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service
230 S Dearborn, Room 1720, MC4929CHI
Chicago, IL 60606

August 22, 2007

ORG
Address

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear _____,

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886A	Department of the Treasury - Internal Revenue Service Explanation of Items	Schedule No. or Exhibit
Name of Taxpayer The ORG		Year/Period Ended 20XX06

LEGEND

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ISSUE

Whether The ORG (ORG) operated exclusively for exempt purposes within the meaning of Internal Revenue Code (IRC) § 501(c)(3)? If not, should the exemption be modified to IRC 501(c)(5) or should the organization exemption be revoked?

EXPLANATION OF FACTS

The organization applied for an exempt status in 19XX and received exemption as a 501(c)(3) organization in August 22, 19XX. In order to meet recognition under IRC 501(c)(3), the EO was asked to sign a declaration that they will not make any contribution to Political Action Council (PAC) fund. This declaration was signed on August 16, 19XX.

During the year 19XX, the organization requested that we examine their activities to determine if exemption under IRC 501(c)(3) was appropriate. A closing letter dated August 31, 19XX determined that an adjustment of the organization's exempt status was necessary. Taxpayer signed Form 6018 – Consent to Proposed Action on December 30, 19XX and agreed to modify exempt status from IRC 501(c)(3) to IRC 501(c)(5). A letter dated August 31, 19XX was issued to taxpayer with a copy of examination report explaining why the adjustment in exemption code was necessary.

A revised letter 948 (Recognition of Exemption) was issued to taxpayer on October 19XX to inform the organization that the exempt status has been modified from IRC 501(c)(3) to IRC 501(c)(5). However, the modification process was not completed.

Response to a routine request to inquire about exempt status prepared by Internal Revenue Service (IRS) Customer Service, dated October 22, 20XX, stated that "In December 19XX, we issued a determination letter that recognized your organization as exempt from federal income tax. Our records indicate that your organization is currently exempt under section 501(c)(5) of the Internal Revenue Code."

Another letter was received from the Internal Revenue Service dated April 21, 20XX regarding exempt status. The Letter stated that "our records indicate that your organization is recognized as exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code. At the time your organization received its initial determination letter, it was given an advance ruling period of five years to determine the actual sources of income...."

Taxpayer failed to respond to notice issued to provide a completed Form 8474 (Support Schedule for Advance Ruling Period). Taxpayer's status was modified from "Public Charity" to "Private Foundation" due to inability to assess the revenue sources during the advance ruling period. Thus, the organization filing requirement was modified from "990 requirement" to "990PF requirement"

Activity Description:

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ORG is an organization working on behalf of Principals, Assistant Principals, and administrators of the XYZ Public Schools. The goal of this organization is to improve educational and administrative leadership in schools and to elevate the status and morale of members.

Activities conducted during the year include:

- 1) Legislative Activities: Lobbyist pursues issues and bills germane to interest of members.
- 2) Political Activities: Funds are provided to support candidates for election or reelection.
- 3) ORG Monthly Calendar: Monthly Calendar is distributed to members for planning purposes.
- 4) : A monthly newsletter with ample information regarding membership activities and school information is published monthly and distributed to members.
- 5) The Directory: The association publishes a directory of schools and members.
- 6) Professional Development of members through various trainings and educational activities.
- 7) Conferences:
- 8) Negotiation of salaries for members.
- 9) Legal Assistance for members.
- 10) Training & Conferences

Economic Benefits for members includes:

- 1) Accidental Death Benefit
- 2) Buying Service
Credit Union

Sources of Income:

The major sources of income are as described below:

- 1) Membership Dues %
- 2) Program Services Revenue %
- 3) Dividend & Interest %
- 4) Payment from Affiliates %
- 5) PAC Revenue %

Federal Returns Filed:

The organization filed Form 990 return until 20XX year end. Since 20XX, taxpayer has not filed a return.

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A delinquent return Form 990 for 20XX06 and 20XX06 was filed with the service center before the examination began, but after notice of examination of 20XX06 Form 990PF return, was issued.

LAW

Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual. The term charitable includes relief of the poor and distressed. Section 1.501(c)(3)-1(d)(2), Income Tax Regulations.

The term educational includes (a) instruction or training of the individual for the purpose of improving or developing his capabilities and (b) instruction of the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3). In other words, the two components of education are public education and individual training.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that, in order to be exempt as an organization described in section 501(c)(3), an organization 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 test or the 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 that 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. The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279 (1945).

Educational purposes include instruction or training of the individual for the purpose of improving or developing his capabilities and instruction of the public on useful and beneficial subjects. An organization must establish that it serves a public rather than a private interest and “that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.”

Section 501(c)(5) of the Internal Revenue Code provides for the exemption of labor, agricultural, or horticulture organizations, which have no net earnings inuring to the benefit of any member and have as their objects the betterment of the conditions of persons engaged in the pursuits of labor, agriculture, or horticulture, the improvements of the grade of their products, and the development of a higher degree of efficiency in their respective occupations.

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Section 1.501(c)(5)-1(a) of the Income Tax Regulations provides that labor organizations contemplated by section 501(c)(5) of the Code include those which have as their objects the betterment of the conditions of those engaged in labor, and the development of a higher degree of efficiency in their respective occupations.

Revenue Ruling 76-31, 1976-1 CB 157, (Jan. 01, 1976)

The organization is an association of teachers who are employed by the school system of a certain city and teach in that city's public schools. The organization was formed to improve the professional abilities of its members and to secure for them better salaries and working conditions. To accomplish these purposes, the organization sponsors seminars and courses for its members, participates in state and national conventions of teachers, and bargains collectively and processes grievances on behalf of its members pursuant to a labor contract with the local school board. To keep its members informed of these activities, the organization sends out a monthly newsletter and conducts regular meetings.

The organization, by bargaining collectively and processing grievances on behalf of its members, has as its object the betterment of the conditions of those engaged in labor. By sponsoring seminars and courses and by participating in conventions of teachers, the organization has as its object the development of a higher degree of efficiency in the teaching profession. By keeping its members informed of these activities, through its newsletters and meetings, the organization furthers both of these objects.

Accordingly, since the organization's activities and objects are those of a labor organization, it qualifies for exemption from Federal income tax under section 501(c)(5) of the Code.

Regulation §601.201.(n)(3) Rulings and determination letters

- (i) A ruling or determination letter recognizing exemption is usually effective as of the date of formation of an organization, if its purposes and activities during the period prior to the date of the ruling or determination letter were consistent with the requirements for exemption.
- (ii) A ruling or determination letter recognizing exemption may not be relied upon if there is a material change inconsistent with exemption in the character, the purpose, or the method of operation of the organization.

Regulation §601.201. (n)(6)(1) Rulings and determination letters

(6) Revocation or modification of rulings or determination letters on exemption:

An exemption ruling or determination letter may be revoked or modified by a ruling or determination letter addressed to the organization, or by a revenue ruling or other statement published in the Internal Revenue Bulletin. The revocation or modification may be retroactive if the organization omitted or misstated a material fact, operated in a manner

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materially different from that originally represented, or engaged in a prohibited transaction of the type described in subdivision (vii) of this subparagraph. In any event, revocation or modification will ordinarily take effect no later than the time at which the organization received written notice that its exemption ruling or determination letter might be revoked or modified.

GOVERNMENT'S POSITION:

ORG does not qualify as an organization described in I.R.C. § 501(c)(3) because it operates programs that does not exclusively serve an exempt purpose described in section 501(c)(3), does not have a charitable activity and operates political action fund (PAC), contrary to agreement signed during the determination process.

The primary activity of this organization is to better the working conditions of members, negotiate wages, provide legal representation to settle disputes between members and the XYZ Public School, and provide other similar benefits for their members.

Organizations recognized under IRC 501(c)(5) strive to provide betterment of the working conditions of those engaged in the pursuits of a particular labor. Similar to the organization described in Revenue Ruling 76-31, 1976-1, ORG's goal is to better the working conditions of those directly involved in educating students. To accomplish the exempt purpose, ORG organize trainings, seminars, bargain collectively for raises/salary increment beneficial to the members, and promote the general interest of all members.

This contradicts the purpose of exemption under IRC 501(c)(3). Benefits from organization recognized under IRC 501(c)(3) must accrue to the general public rather than individual members of an organization.

For the foregoing reasons, ORG activities are not charitable activities and the organization cannot be recognized under IRC 501(c)(3).

Although, the organization have an exempt purpose and functions similar to exemption under IRC 501(c)(5), but, exemption under IRC 501(c)(3) cannot be modified to another code section.

In order to establish exemption under section 501(c)(5) of the Code, the organization must file an application on Form 1024, Exemption Application, with the Internal Revenue Service.

CONCLUSION:

In order to qualify for exemption under I.R.C. § 501(c)(3) an organization must be both organized and operated to achieve a purpose that is described under that Code section. ORG are not organized or

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operated in accordance with Internal Revenue Code § 501(c)(3), and the regulations there-under governing qualification for tax exemption under the Code.

Although, the service tried to modify the organization's exemption in 19XX, but the modification did not go through because exemption under IRC 501(c)(3) CANNOT BE MODIFIED.

Therefore, revocation of exempt status is proposed. The proposed revocation will be effective July 01, 20XX.

TAXPAYER'S POSITION:

Taxpayer agreed with the conclusion as the best way to resolve the issue. We agreed that no penalties will be imposed on failure to file Form 990 return because the returns were filed but unpostable due to incorrect filling requirement. We also agreed that Form 1120 will not be required because the organization will apply for IRC 501(c)(5) as soon as possible.