



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **200847019**
Release Date: 11/21/2008

Date: August 26, 2008

UIL: 501.03-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

SE:T:EO:RA:T:2

Dear _____:

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. 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 about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: July 2, 2008

Contact Person:

Identification Number:

Contact Number:

501.03-00

Employer Identification Number:

Legend:

B =

C =

M =

N =

O =

P =

Q =

R =

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.

FACTS:

You were incorporated on April 2, 2002, under the State M, Not For Profit Corporation Act. Article III of your incorporating document states that you are organized exclusively for charitable and other exempt purposes within the meaning of section 501(c)(3) of the Code. Further, you will not carry on any activities which are impermissible for an organization which is tax exempt under section 501(c)(3) of the Code. Your specific purposes, as stated in Article III, are "(t)he acquisition, financing, ownership and operation of dormitory and other ancillary facilities at institutions of higher learning in the State of M and elsewhere in the United States."

Article IV of your incorporating instrument provides that no part of your net earnings shall inure to the benefit of any private individual. Article VI provides that upon your dissolution, remaining assets shall be distributed for one or more exempt purposes within the meaning of Code section 501(c)(3) or to a federal, State, or local government organization for public purposes, in conformity with the purposes stated in Article III.

In response to Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code concerning your present and proposed activities, you restate the language from Article III above. You then state that the student housing facilities will be located on campus and will be available only to students enrolled at the institution and their dependents (if married student housing is made available).

Initially, you reported discussions with two colleges in the State of M. At the time that you submitted your exemption application, you were unable to determine whether either of the two institutions might ultimately utilize your services. You stated the "intention is to be available to the educational institutions to the extent that they find it necessary to provide 'privatized' student housing for their students and do not have access to any other viable not for profit corporation. The corporation will not take any fees, disbursements will be solely for operating expenses and debt retirement, and once debt on the facilities is retired the ownership of the facilities will be transferred to the educational institution." Your intention is that such institution be closely involved with the operations of the student housing.

You have indicated that no member of your Board of Directors will be an owner or employee of any developer involved with any of your projects.

You anticipate that your financial support will be from student housing rents. You indicated that all revenues will be applied to servicing the debt, operational expenses, and for a reserve to be used to improve or replace existing housing facilities. If there is a surplus, you plan to return it to the educational institution where the student housing is located.

In conjunction with the educational institutions, you will begin activity by hiring a developer and/or contractor for the construction of the student housing. If any of the facilities are managed by someone other than the educational institution, then you will adhere to the procedures for management contracts set forth in Rev. Proc. 2001-39, 2001 - 2 C.B. 38.

You have also indicated that you will enter into a ground lease with the institution in which the housing is to be constructed. The rentals charged to students will be at rates designed to pay your expenses and will be approved by the particular college or university. The financing for the acquisition and development of college housing will be done with tax exempt debt, "the specifics of which are not yet determined."

Your President, B, has stated, that he was contacted by representatives of Two M Universities "regarding their desire for privatized student housing and asking if a not-for-profit corporation could be formed in order to assist them with this desire. To the extent that either of them moves forward with their plans for development of student housing, (you) would be available to them as a potential financing vehicle."

You state that the contract that you will have with the university will be the ground lease agreement. "The ground lease will be the nexus between the university and (your organization) and will provide all of the requirements that the university has for us to construct on their property." You have stated that no ground lease presently exists and "If the university is unwilling to sign a ground lease, (you) will not participate in the financing."

You have stated that no payments will be made to any of your officers or members of your Board of Directors.

We inquired how you will determine that an educational institution does not have adequate housing for its students. You responded that that is a determination to be made by the

university on the basis of such factors as current utilization of existing facilities, waiting lists, and anticipated increases in enrollment. "Additionally, before we agree to act as the issuer for the bonds, we would require that a needs assessment be conducted by an independent third party addressing the housing demand, the type of facilities that should be constructed and the amenities that should be included. Also, since the construction of these facilities will be accomplished through the use of tax-exempt bonds, the underwriters for those bonds, together with any rating agencies or banks that might be involved, will need to be comfortable that, in fact, the facilities will be able to be rented at rates that will provide for payment of the bonds."

Your President, B, explained why the rental rate for the proposed student housing facility will be comparable to the existing market, as follows: "All of the universities with whom I have ever had conversation require that new facilities not only be competitive with other existing facilities but also with the surrounding marketplace. The needs assessment discussed in question 7 will also address competitive facilities in the surrounding areas and the rental rates being charged."

You have stated that "The developer will be an entity that is selected by the university. These facilities are being built for the university and it is our desire that they get exactly what they need and bargain for. The university will select the developer and will have the right of approval on all plans, however, since the facilities will actually be owned by (you), the contract will be between the developer and (you), subject to the approval of the university."

We inquired as to who has the expertise to issue the tax exempt bonds and why specifics have not been provided about the bond financing needed to build the student housing. In response, you state that your President, B, has a background in the issuance of tax exempt bonds, having worked as bond counsel on the issuance of bonds worth in excess of three billion dollars in his career. In addition, your Vice President, C, had a long career with N, a well known financial services firm, as both an underwriter and a trader. However, "Whoever is selected as the underwriter for the bonds will largely control the manner in which they are issued." Even though the bonds will be issued by you, "the success of this issue and the specifics of the issue will be dependent, at least in large part, on the university for whom the bonds are being issued." Because the student housing will need to be self liquidating, and as it will be your only asset, "the term of the bonds will probably be relatively long, 25-30 years, in order that the rents may be kept down to the competitive levels..."

We inquired as to whether you will operate "below cost" and, if so, how. You responded that you will operate at "virtually no cost." The housing project will be self sustaining and the debt on it will be self liquidating. You also indicated that your officers and directors will not receive any compensation and you will have no employees. All of your services "will be accomplished through contracts with third party vendors."

You have stated that you are not going to market or design student housing facilities. "That will be done through contracts entered into with third party providers, subject to the approval of the university. Our goal is to be of assistance to educational institutions and to provide them with an additional method of financing their student housing needs."

In a letter dated August 27, 2003, responding to our inquiry dated July 7, 2003, you state that your President, B, has on occasion been contacted by a developer, O, "where they have had discussions with a college that is looking to do tax-exempt financing and would like to use an unrelated 501(c)(3). This has happened on two occasions prior to this one. And on each of these occasions, (B) created a 501(c)(3) corporation and financings were completed for the colleges."

You state that you will own a student housing facility once such facility is completed. The revenue from the facility will be used to retire the debt and to pay whatever operating expenses you incur. Once the debt is retired, the facility will be transferred to the college. The set up fees and administrative fees, which have been minimized to date, have been paid out of B's pocket. B will represent you during the bond financing, will review the bond documents, and will render the required opinion as it relates to you. For these services, B will receive compensation from bond proceeds.

You have indicated that to complete the construction and management of a student housing facility, you will enter into contractual arrangements with a number of entities, none of which have been identified to date. However, each of such entities will be paid either from the proceeds of a bond issue or from the revenues of the project itself.

You have stated that B will not be acting as bond counsel on any student housing project. He will represent only you as the borrowing entity and will be paid a fee for such services.

However, you state, "As a bond counsel with 20 years of experience, (B) has been involved in financing a few student housing projects and... has utilized a similar 501(c)(3) structure on two previous occasions. Additionally, (B), while with a larger national law firm, represented the P Housing Authority and was involved in a few low cost housing projects."

In addition, you have indicated that "For the most part, all service providers will be selected by the college. They will select bond counsel and underwriters. Although (your organization) will be a separate legal entity from the college, all things are being done for the benefit of the college and the college would remain very closely involved in all decisions. As to competitive bidding, (you) assume that the colleges will utilize whatever structure they normally utilize for the selection of their service providers."

In a letter dated August 20, 2004, you stated that, as indicated in your previous letter, you intend to be a sole purpose entity. You were originally created pursuant to requests made by the Q campus of University of R. "However, since we originally filed over two years ago, R utilized other avenues for their tax-exempt financing. If we receive our determination, we would potentially be available for their next phase or possibly some other project."

You state that bond proceeds would be utilized for construction, debt service, a reserve fund, capitalized interest, and up to 2% to pay for the costs of bond issuance.

We asked whether any of your officers or directors will provide goods or services (directly or indirectly) to any facility which you will own or operate. You responded that, "The only service provided by an officer would be the legal representation of the corporate entity (you) in the issuance process."

LAW:

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

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense and includes the advancement of education

Section 1.501(c)(3)-1(c)(1) of the regulations provides, in part, 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 exempt purposes as specified in section 501(c)(3) of the Code, but will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for any of the purposes specified in section 501(c)(3) of the Code unless it serves a public rather than a private interest. Thus, to qualify under section 501(c)(3) of the Code, an organization must establish that it is not organized and operated for the benefit of private interests such as designated individuals, the creator or the creator's family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

In general, an organization which applies for recognition has the burden of proving that it clearly meets all the requirements of the particular Code section under which it has applied. See Kenner v. Commissioner, 318 F. 2d 632, 635 (7th Cir. 1963), and Cleveland Chiropractic College v. Commissioner, 312 F. 2d 203, 206 (8th Cir. 1963).

Rev. Proc. 2008-9, 2008-2 IRB 258, states in Sec. 4.03 that,

Exempt status may be recognized in advance of the organization's operations if proposed activities are described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements for exemption mere restatement of exempt purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement... The organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures... Where the organization cannot demonstrate to the satisfaction of the Service that it qualifies for exemption pursuant to the section of the Internal Revenue Code under which exemption is claimed, the Service will generally issue a proposed adverse determination letter or ruling.

Rev. Rul. 63-220, 1963-2 C.B. 208, describes a corporation that was organized primarily for the purpose of extending loans to needy students of a college to enable them to complete their educational programs. Certain loans were granted on an unsecured basis, while others required a type of security. Both types of loans were made at the same nominal rate of interest which was substantially lower than commercial interest rates, thereby representing a substantial saving to the students. The ruling holds that such activity serves a charitable purpose by making loans available to students at substantially less than commercial rates. The fact that under certain circumstances security is required before a loan may be granted is not sufficient to destroy the charitable aspect of the organization's purposes and activities

Rev. Rul. 64-274, 1964-2 C.B. 141, describes an organization that provides free housing, scholarships, and books, to students who could not otherwise attend college because of a lack of funds. The Service ruled that under these circumstances, the organization was exempt because it was advancing education by relieving the poverty of the students.

Rev. Rul. 67-217, 1967- 2 C.B. 181, recognizes an organization formed to provide housing and food service exclusively for students and faculty of a specific university lacking such facilities as exempt under section 501(c)(3) of the Code. The housing facility was constructed by the

organization on land near the university and made available to the students of the university at rates comparable to those offered by the university in its own facilities. While the facility was run by a commercial management company, any surplus from operations was donated to the university and the university had an option to purchase the facility at any time for an amount equal to the outstanding indebtedness. Providing the housing under these circumstances served to advance education.

Rev. Rul. 76-336, 1976-2 C.B. 143, describes an organization formed by community leaders to provide housing for students of a particular college in response to studies by staff members of the college showing that the college lacked suitable housing to meet the needs of students. The college was financially unable to provide housing. Additionally, many of the students in its primary service area live at such a distance that daily commuting is not reasonably possible. The organization operates a housing facility for students adjacent to the college campus. All students of the college are eligible to apply for the housing. Applications for housing are accepted on a first come-first served basis. Charges to students for the housing approximate costs, including debt retirement. The organization is not controlled by the student residents or by the college. However, the college and the organization consult and cooperate to ensure that the needs of the college and its students are served by the operation of the housing facility. The organization is governed by a board of directors composed of community leaders. The organization's income is from rentals of the housing facilities and from contributions. Its disbursements are for operating expenses and debt retirement. The ruling holds that the organization provides needed student housing that is not otherwise available. All students who attend the college are eligible to apply for residence. Under these circumstances, the organization is both helping the college, which is unable to provide adequate student housing, to fulfill its educational purposes, and aiding the students to attain an education. Therefore, the activities of the organization are advancing education.

In Better Business Bureau of Washington, D.C. v. U. S., 326 U.S. 279 (1945), the court held that an organization was not organized and operated exclusively for charitable purposes. The court reasoned that the presence of a single nonexempt purpose, if substantial in nature, would destroy the exemption regardless of the number or importance of truly exempt purposes.

Analysis and Conclusion:

You have failed to establish that your operations will further a charitable purpose and that you will not be operated for a substantial nonexempt private purpose. Providing housing for students in the manner you have described, absent special facts and circumstances, is a trade or business that is not a charitable activity.

An organization providing student housing may qualify for exemption if certain facts and circumstances are present. For example, serving a class of students recognized as a charitable class. However, you do not restrict your services to a charitable class of students such as low-income. Nor do you provide free housing or below cost services. Providing services at cost and solely for exempt organizations is not sufficient to characterize the activity as charitable. See Rev. Ruls. 63-220 and 64-274, *supra*. In addition, you have also failed to establish that you will provide any other charitable activities to the affiliated educational institutions.

Unlike Rev. Ruls. 67-217 and 76-336, *supra* where exemption was based primarily on the element of control by or on behalf of an exempt organization and providing assistance to specific colleges, your primary purpose is to provide financing and housing services to a number of colleges and universities. This structure prevents you from being controlled by any one educational institution or by any one community. Instead, you are an independent organization

not created by the community or in conjunction with the educational institutions that you intend to become "affiliated" with. While you plan to include members of the community and the university on the board, there is no evidence that members of the local community or directors of the educational institutions will have any significant involvement in, contribute to, or otherwise participate in your actual operations.

Finally, your role is primarily that of developer. You are operated for the substantial nonexempt purpose of marketing and designing projects and to act as a vehicle for financing the projects through tax-exempt bonds. The essential facts and circumstances of both Rev. Rul. 67-217 and 76-336, community control, college involvement and below cost operations are absent from your structure and operations. Your overall structure is designed to be self-supporting without regard to the educational institutions you are servicing. Such activity is not an exempt activity, but a trade or business.

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.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree 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 all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
TE/GE (SE:T:EO:RA:T:2)

1111 Constitution Ave, N.W.
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements