



**DEPARTMENT OF THE TREASURY**

Internal Revenue Service  
TE/GE EO Examinations  
1100 Commerce Street  
Dallas, TX 75242

**TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION**

Number: **200903083**  
Release Date: 1/16/2009

October 1, 2008

**Uil:501.03-01**

LEGEND

ORG = Organization name      XX = Date      Address = address

ORG  
ADDRESS

Person to Contact:  
Identification Number:  
Contact Telephone Number:  
In Reply Refer to: TE/GE Review Staff  
EIN

**CERTIFIED MAIL-RETURN RECEIPT REQUESTED**

LAST DATE FOR FILING A PETITION WITH  
THE TAX COURT: December 30, 20XX

Dear                    :

This is a Final Adverse Determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code.

Our adverse determination was made for the following reasons:

Exemption from income tax is a matter of legislative grace and taxpayers have the burden of establishing their entitlement to exemptions. Section 6033 requires organizations exempt from tax to keep such records and render such statements as are required by such rules and regulations as the Secretary may prescribe. Treasury Regulations section 1.6033-2 (h)(2) requires organizations exempt from tax to submit such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into the organization's exempt status.

You have not established that you have been operated exclusively for exempt purposes within the meaning of Internal Revenue Code section 501(c)(3). You are not a charitable organization within the meaning of Treasury Regulations 1.501 (c)(3)-1(d) in that you failed to establish that you were operated exclusively for an exempt purpose. You failed to establish that you were engaged in exempt activities, that your expenditures were for exempt purposes, and that your assets did not inure to private shareholder or individuals.

Based upon the above, we are revoking your organization's exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code retroactively to January 1, 20XX.

Contributions to your organization are no longer deductible under section 170 of the Internal Revenue Code.

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending December 31, 20XX, and for all years thereafter.

Processing of income tax returns and assessment of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination in court, you must initiate a suit for declaratory judgment in the United States Tax Court, the United States Claim Court or the District Court of the United States for the District of Columbia before the 91<sup>st</sup> day after the date this determination was mailed to you. Contact the clerk of the appropriate court for the rules for initiating suits for declaratory judgment.

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 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by writing to: Internal Revenue Service, Taxpayer Advocates Office. 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 the United States Tax 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 section 6104(c) of the Internal Revenue Code.

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

Sincerely yours,

Vicki L. Hansen  
Acting Director, EO Examinations



TAX EXEMPT AND  
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**DEPARTMENT OF THE TREASURY**

Internal Revenue Service  
TEGE EO Examination  
31 Hopkins Plaza - Room 1400  
Baltimore, MD 21201

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.

Letter 3618 (04-2002)  
Catalog Number 34809F

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 <b>886-A</b> (Rev. January 1994)	<b>EXPLANATIONS OF ITEMS</b>	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number	Year/Period ended 31/ 0/20XX

**LEGEND**

ORG = Organization name      XX = Date      XYZ = State      Address = address      City = city  
 BM-1 = 1<sup>st</sup> Board member

**ISSUE**

Whether the organization known as ORG has operated exclusively for §501(c)(3) purposes and if not, whether their exempt status should be revoked?

**FACTS**

The organization, ORG was incorporated in the State of XYZ on September 3, 20XX.

A letter (Letter 1045) dated April 14, 20XX granted ORG tax-exempt status as an organization exempt from income tax under Internal Revenue Code (hereinafter referred to as "IRC" or "Code") section 501(a) as an organization described in section 501(c)(3).

Because ORG was a newly created organization, the Internal Revenue Service ("IRS") did not make a final determination of the organization's foundation status under section 509(a) of the Code. Instead, they were granted an advance ruling period in which they would be treated as a publicly supported organization, and not as a private foundation. The advance ruling period began October 9, 20XX and ended December 31, 20XX.

After several attempts were made to contact the organization by telephone, Letter 3611 informing the organization of the examination was mailed to the last known address of ORG identified as Address, City, XYZ. This correspondence was returned by the United States Post Office ("USPS") as "Unclaimed" on April 20, 20XX. Several more attempts were made to contact the organization via Certified Mail but were not successful.

Research was performed to locate BM-1 who is listed as the Registered Agent for ORG and was also the initial president of the organization. BM-1 (nee BM-1) was located on July 20, 20XX. Internal Revenue Agent ("IRA") discussed the current status of the organization with BM-1 who informed RA that the organization ceased operations not long after exemption was granted (20XX). She stated the organization has never operated as an exempt organization (no exempt activities) due to their inability to obtain grants to support the activities detailed on the Application for Exemption, Form 1023. They did not file Articles of Dissolution with the State of XYZ as they did not own any assets at that time.

The XYZ Department of Taxation website lists the current status of ORG as "Forfeit" due to failure to file Personal Property Tax Returns. According to the XYZ Department of Taxation, an organization is considered "Forfeit" if they fail to file any required return(s) and/or pay any outstanding fees/penalties. Once an organization is classified as "Forfeit" they can only be reclassified as "Active" after filing any delinquent returns and/or paying outstanding fees/penalties *and* resubmitting the articles of incorporation.

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According to internal IRS documents, the organization has never filed Form 990 or any other federal returns since exemption was granted. BM-1 concurred that they have never filed any returns as they received no income nor made any disbursements. No documentation could be obtained that would evidence any exempt function activities engaged in since exemption was granted.

## LAW

IRC 501(c)(3) exempts from Federal income tax: corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting to influence legislation (except as otherwise provided in subsection (i)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.

### The Dual Test: Organized and Operated

IRC 501(c)(3) requires an organization to be both "organized" and "operated" exclusively for one or more IRC 501(c)(3) purposes. If the organization fails either the organizational test *or* the operational test, it is not exempt. Reg. 1.501(c)(3)-1(a)(1). Church of Visible Intelligence That Governs The Universe v. U.S., 4 Cl.Ct. 55

The organizational test concerns the organization's articles of organization or comparable governing document. The operational test concerns the organization's activities. A deficiency in an organization's governing document cannot be cured by the organization's actual operations. Likewise, an organization whose activities are not within the statute will not qualify for exemption by virtue of a well written charter. Reg. 1.501(c)(3)-1(b)(1)(iv).

### Operational Test

1. Section 1.501(c)(3)-1(d)(i) defines appropriate exempt purposes. An organization may be exempt as an organization described in section 501(c)(3) if it is organized and operated *exclusively* for one or more of the following purposes:

- religious
- charitable
- scientific
- testing for public safety
- literary
- educational

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- fostering national or international sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment) prevention of cruelty to children or animals
2. Reg. 1.501(c)(3)-1(c)(1) provide that an organization is *operated exclusively* for charitable purposes only if it engages *primarily* in activities that accomplish those purposes in (1) above. It is not so operated if more than an insubstantial part of its activities do not further those purposes.

### Meaning of "Operated Exclusively"

The meaning of the term 'exclusively' as used in the statutes is no longer open to debate. In Better Business Bureau of Wash., D.C. v. United States, 326 U.S. 279, 66 S.Ct. 112, 90 L.Ed. 67 (1945), the Supreme Court, in giving effect to § 811(b)(8) of the Social Security Act (in terms substantially the same as § 501(c)(3) of Int.Rev.Code), made this pronouncement:

"In this instance, in order to fall within the claimed exemption, an organization must be devoted to educational purposes exclusively. This plainly means that the presence of a single noneducational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes." 326 U.S. at 283, 66 S.Ct. at 114, 90 L.Ed. 67. See also, Duffy v. Birmingham, 8 Cir., 190 F.2d 738 (1951); American Institute for Economic Research v. United States, Ct.Cl., 302 F.2d 934 (1962), cert. denied, 372 U.S. 976, 83 S.Ct. 1109, 10 L.Ed.2d 141 (1963); Scripture Press Foundation v. United States, Ct.Cl., 285 F.2d 800 (1961), cert. denied.

The most liberal of constructions does not mean that statutory words and phrases are to be given unusual or tortured meanings unjustified by legislative intent or that express limitations on exemption are to be ignored. See Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279, 66 S.Ct. 112.

Furthermore, Section 1.501(c)(3)-1(c)(2) provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

### Public v. Private Purposes

Reg. 1.501(c)(3)-1(d)(1)(ii) provide that to meet the operational test, an organization must be engaged in activities furthering "public" purposes rather than private interests. It must not be operated for the benefit of designated individuals or the persons who created it. The purposes specified in IRC 501(c)(3), pertaining to this particular organization, which are all "public" purposes, are separately analyzed below.

In order to establish that it meets the first criterion of the operational test for tax-exempt status, i.e., that it is "operated exclusively" for exempt purposes, an organization must prove that it is operated for a public purpose rather than for benefit of private interests, such as those of its creator or his family, shareholders, or designated individuals; presence of a single nonexempt purpose, if substantial in nature, will destroy the exemption. Church By Mail, Inc. v. C.I.R., 765 F.2d 1387 C.A.9, 1985.

### Charitable Organizations

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Reg. 1.501(c)(3)-1(d)(2) provide that the term "charitable" is used in IRC 501(c)(3) in its generally accepted legal sense and includes relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of government; promotion of social welfare.

### Educational Purposes

1. An organization that is organized and operated exclusively for educational purposes qualifies for exemption under IRC 501(c)(3).

2. The regulations under Reg. 1.501(c)(3)-1(d)(3)(i) define education as:

- "the instruction or training of the individual for the purpose of improving or developing his capabilities"
- "the instruction of the public on subjects useful to the individual and beneficial to the community."

### Burden of Proof

The court in Church of Spiritual Technology v. United States, 510 U.S. 870, 114 S.Ct. 197 (Mem) U.S.,1993, cited a long line of authority holding that the applicant bears the burden of showing it is entitled to exemption. In Harding Hospital, Inc. v. United States, 505 F.2d 1068, 1071 (6th Cir. 1974), the court stated that "[i]ncome tax exemption must be strictly construed, with any doubts to be resolved in favor of the taxing entity. Consequently, determinations of the Commissioner are presumed correct."

Similarly, the court cited Welch v. Helvering, 190 U.S. 111, 115 (1933), and modern cases following its stricture that "[P]laintiff thus bears the burden of proving its entitlement to an exemption." See also, Bubbling Well Church of Universal Love, Inc. v. Commissioner, 670 F.2d 104, 106 (9th Cir. 1981); Freedom Church of Revelation v. United States, 588 F. Supp. 693, 696 (D.D.C. 1984).

The Tax Court has **consistently** stated that a statute creating an exemption must be strictly construed and any doubt must be resolved in favor of the taxing power. Harding Hospital, Inc. v. United States of America, 505 F.2d. 1068, 34 A.F.T.R.2d 74-6174, 74-2 USTC.

### TAXPAYER'S POSITION

BM-1 stated the organization ceased operations not long after they were granted exemption as they were unable to secure funding for activities described in the Application for Exemption, Form 1023. BM-1 has concurred that: the organization has never had any exempt activities; and made the decision to cease operations in 20XX. Per a conversation with BM-1 on July 20<sup>th</sup> and 23<sup>rd</sup>, 20XX, she has agreed with the proposed revocation.

### SERVICE POSITION



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The issues affecting tax exempt status of ORG center on:

1. Operational Test

Exempt status under §501(c)(3) is a privilege as opposed to a right. An organization granted tax-exempt status under §501(c)(3) maintains the responsibility for substantiating continued eligibility for recognition thereunder. Organizations seeking to obtain *or* maintain tax-exempt status under §501(c)(3) must meet two basic tests. Such organizations must be *both* organized *and* operated for §501(c)(3) purposes.

The organizational test is not being questioned at this juncture.

In **St. David's Health Care System v. U.S., 349 F.3d 232 C.A.5.Tex.,2003** to pass the "operational test" for tax-exempt status, purported charitable organization must show that: (1) it engages primarily in activities which accomplish its exempt purpose; (2) its net earnings do not inure to benefit of private shareholders or individuals; (3) it does not expend substantial part of its resources attempting to influence legislation or political campaigns; and (4) it serves valid purpose and confers public benefit. Failure to satisfy any one of these requirements will result in denial of tax exemption. **Church of Visible Intelligence That Governs The Universe v. U.S., 4 Cl.Ct. 55 Cl.Ct.,1983.**

According to internal IRS documents, the organization has never filed Form 990 or any other federal returns. No documentation could be obtained that would evidence any exempt function activities engaged in since exemption was granted. BM-1 concurred that they have never filed any returns as they received no income nor made any disbursements. In **Church By Mail, Inc. v. C.I.R., 765 F.2d 1387** the Court found that "purpose and objective to which income of an organization is devoted is ultimate test in determining whether it is operated exclusively for an exempt purpose.

Operationally, it would appear that ORG has never conducted any exempt function activities since they were granted tax exempt status beginning October 9, 20XX. There was no evidence of revenues or expenditures being made for activities that would support the conduct of any exempt activities.

An organization must carry on exempt function activities in order to be entitled to continued recognition of tax-exempt status under §501 (c)(3), i.e., dormant organizations are not entitled to such exempt status as they cannot meet the operational test.

In **Samuel Friedland Foundation v. United States, 144 F.Supp. 74**, the courts found an organization was not exempt due to the following:

- The exempt organization (Freidland) failed to formulate and design a meaningful charitable program, one having a definite functional objective;
- Ergo, the accumulation of profits during this time was deemed unreasonable as no charitable purpose was identified.

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In *Erie Endowment v. United States*, 3 Cir., 316 F.2d 151 (1963), the Third Circuit, confronted with the same problem, affirmed the district court's holding in *Friedland case*, supra, 144 F.Supp. at 92, and also made the following general pronouncement:

“Mindful of these principles, we are impelled to conclude that the Tax Court here correctly decided that the accumulations were unreasonable within the meaning of the statute. Several salient facts stand out. Foundation did not have a concrete or definite charitable program requiring the accumulation of a large percentage of its income. Under its corporate charter, Foundation possessed broad charitable powers, but the fact remains that it failed to formulate and design a meaningful charitable program, one having a definite functional objective. ..”

An exemption is an exception to the norm of taxation. An organization which seeks to obtain tax exempt status, therefore, bears a heavy burden to prove that it satisfies all the requirements of the exemption statute. The Supreme Court repeatedly has said that exemptions from taxation are not granted by implication. See, e.g., *Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 156, 93 S.Ct. 1267, 36 L.Ed.2d 114 (1973), and authorities therein cited. The Tax Court has stated consistently that ‘(a) statute creating an exemption must be strictly construed and any doubt must be resolved in favor of the taxing power.’ *American Automobile Association v. Commissioner*, 19 T.C. 1146, 1158 (1953); *Associated Industries of Cleveland v. Commissioner*, 7 T.C. 1449, 1464 (1946).

## CONCLUSION

Organizations seeking to obtain *or* maintain tax-exempt status under §501(c)(3) must meet two basic tests. These organizations must be *both* organized *and* operated for §501(c)(3) purposes. Due to the lack of exempt function activities, we have concluded that the organization known as ORG has failed the operational test. It is the Internal Revenue Service’s position that exemption under Internal Revenue Code §501(c)(3) should be revoked as of January 1, 20XX.

Form 1120 returns should be filed for the tax periods ending on or after January 1<sup>st</sup>, 20XX.