

Internal Revenue Service
Appeals Office

Department of the Treasury

Release Number: 201321040

Release Date: 5/24/2013

Date: MAR - 1 2013

Taxpayer Identification Number:

Person to Contact:

Employee ID:

Tel:

Fax:

Contact Hours:

Tax Period(s) Ended:

UIL: UIL Code: 501.09-03

Certified Mail

Dear Taxpayer:

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code effective January 01, 2007.

The revocation of your exempt status was made for the following reason(s):

- You did not meet the recordkeeping requirements to maintain your exempt status as required under section 6033 of the Code.
- A substantial amount of your assets inured to the private benefit of your founder and president. Because a substantial amount of your charitable assets were used for private purposes, you are not operated exclusively for exempt purposes described in section 501(c)(3) of the Code.

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

You are required to file Federal income tax returns on Forms 1120 for the tax period stated in the heading of this letter and for all tax years thereafter. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit www.irs.gov.

If you were a private foundation as of the effective date of revocation, you are considered to be taxable private foundation until you terminate your private foundation status under section 507 of the Code. In addition to your income tax return, you must also continue to file Form 990-PF by the 15th Day of the fifth month after the end of your annual accounting period.

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

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of section 7428 of the Code in one of the following three venues: 1) United States Tax Court, 2) the United States Court of Federal Claims, or 3) the United States District Court for the District of Columbia. A petition or complaint in one of these three courts must be filed within 90 days from the date this determination letter was mailed to you. Please 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. See also Publication 892.

You also 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 matters that may not have been resolved through normal channels get prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this letter. You may call toll-free, 1-877-777-4778, for the Taxpayer Advocate or visit www.irs.gov/advocate for more information.

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

Sincerely Yours,

Appeals Team Manager

Enclosure: Publication 892



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE EO Examinations

4330 Watt Ave; Stop# 6209

Sacramento, CA 95821

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

January 6, 20XX

LEGEND

ORG - Organization name

XX - Date Address - address

ORG

ADDRESS

Taxpayer Identification Number:

Form Number:

Tax Year Ended:

Person to Contact:

Employee Identification Number:

Employee Telephone Number:

Phone:

Fax:

**CERTIFIED MAIL - RETURN RECEIPT
REQUESTED**

Dear President

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, please sign and return the enclosed Form 6018, *Consent to Proposed Action - Section 7428*. If you have already given us a signed Form 6018, you need not repeat this process. 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.

in lieu of Letter 3618

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.

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,

Nanette M. Downing
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

in lieu of Letter 3618

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number EIN	Year/Period ended 12/31/20XX

LEGEND

ORG - Organization name XX - Date President - president motto - motto
 RA-1, RA-2 & RA-3 - 1ST, 2ND & 3RD RA CO-1, CO-2, CO-3, CO-4, CO-5, CO-6 & CO-7 -
 1ST, 2ND, 3RD, 4TH, 5TH, 6TH & 7TH COMPANIES

Issue

Whether ORG (ORG) qualifies for exemption under section 501(c)(3) of the Internal Revenue Code?

Whether any part of ORG net earnings inured to the benefit of any private shareholder or individual?

Should 501(c)(3) tax-exempt status be revoked, effective January 1, 20XX, for failure to operate exclusively for exempt purposes and for violating the prohibition on inurement as set forth in Internal Revenue Code section 501(c)(3)?

Facts

The organization was granted exemption under section 501(c)(3) with foundation code 170(b)(1)(A)(vi) on May 25, 20XX. To this date, this determination has not been changed. The purpose of ORG is to promote and support humane education in our nation's schools. It is the intent of this corporation to operate exclusively for charitable purposes, including but not limited to: speaking for non-human species from what is imagined to be their point of view and not to endorse their use for purposes that would be deemed detrimental to them on an individual or species basis as determined by the society. According to the articles of incorporation the organization was formed for the purpose of rendering humane and charitable services to animals and for all other legal purposes. No substantial part of the activities of the corporation shall inure to the benefit of, or be distributable to, its contributors, directors, officer, or other private persons. The organization was founded by President. He has been the President of the organization since it was created.

The organization's gross receipts are normally less than \$. The only return that has been filed by the organization was Form 990-N for the 20XX period (to prevent automatic revocation).

The organization has been operating out of President's residence. Its activities consisted of rescuing motto, providing the motto' food and shelter on President's property, finding homes for the rescued motto, conducting outreach and educational activities related to pets in the community.

President was contacted on November 15, 20XX and the initial appointment was scheduled on December 14, 20XX. An appointment letter (L3613) and information document request, Form 4564 (IDR) was sent to ORG requesting information needed to conduct the examination and

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determine whether the organization was organized and operating for exempt purposes. Important items requested in IDR#1 were:

- Governing Instruments: (Articles of Incorporation, Bylaws, etc.)
- Minutes of Meetings for the 20XX period
- IRS Determination Letter
- Original application for exemption (Form 1023)
- Copies of any other Federal tax/information returns filed
- Copies of literature printed/distributed
- Chart of Accounts
- Books and records of assets, liabilities, receipts, disbursements: general ledger/income statement/balance sheet/etc.
- Sample of source documents for January 20XX- December 20XX such as: receipts, bills, invoices, vouchers
- Records of Grants, Contributions, and Donation received during 20XX
- PayPal records
- Check Register, bank statements, and canceled checks
- Contracts/Leases/Rental Agreements used by the organization

On November 17, 20XX, President called to explain the organization was not active in 20XX and he did not keep any records. After his mobile home was condemned a lot of information was thrown out because he didn't think it was important. President was asked what books and records he does have. There was no information for 20XX as well as 20XX and 20XX.

On November 30, 20XX, IDR#2 was sent to President requesting documents he could obtain from third parties. IDR#2 requested:

- All bank statements, and canceled checks for period under examination.
- PayPal records.
- A sample of source documents for January 20XX- December 20XX such as receipts, bills, invoices, vouchers.
- Records of Grants, Contributions, and Donations received.

The only documents provided were the bank statements (no copies of checks). On April 29, 20XX, the organization's bank records and PayPal records were summonsed. The PayPal account was locked and had not been used in 20XX.

The bank statements showed that \$ was deposited into the organization's business checking account at CO-1. Most of the organization's funds came from donations. President also received \$ cash-back throughout the year when donation checks were deposited into the account (the \$ was not included in total deposits). There was \$ in withdrawals from the checking account.

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On November 7, 20XX, IDR#3 was sent to President requesting substantiation for a sample of transactions listed in the summonsed bank records. The following transactions were obtained from the organizations monthly bank statements, cancelled checks, deposit slips, and records for all debit and credit memos.



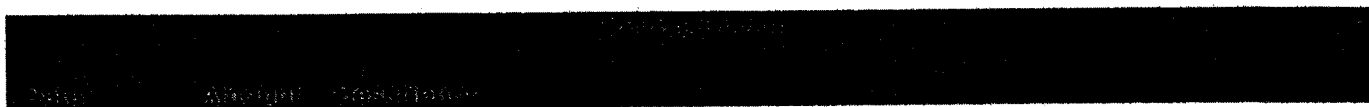
4/2/20XX
4/30/20XX
5/17/20XX
8/9/20XX
10/18/20XX
10/16/20XX
11/1/20XX
11/13/20XX
12/13/20XX

Total

	1/4/20XX	Cash		Food/Lumber	1/3/20XX	President
	1/10/20XX	Cash		Lumber/Pizza	1/10/20XX	President
	1/17/20XX	RA-1		Plumbing	1/17/20XX	RA-1
	1/17/20XX	RA-1		Labor	1/17/20XX	RA-1
	1/31/20XX	Cash			1/31/20XX	President
	1/31/20XX	RA-1		Food Run t	2/1/20XX	RA-1
	12/27/20XX	CO-2		Food President	1/30/20XX	CO-3
	12/29/20XX	RA-1		Dogfood/Tarp/Plumbing	1/2/20XX	RA-1
	1/31/20XX	RA-1		Gas	2/9/20XX	RA-1
	2/9/20XX	RA-1		Food	2/9/20XX	RA-1
	2/5/20XX	CO-3		Cert Copy of Birth Certificate	2/27/20XX	CO-4
	2/23/20XX	RA-1			2/26/20XX	RA-1
	2/23/20XX	RA-1			2/26/20XX	RA-1
	3/8/20XX	CO-4			3/12/20XX	CO-4
	4/10/20XX	RA-2			4/16/20XX	RA-3
	5/8/20XX	Cash			5/8/20XX	President
	5/3/20XX	RA-1		Satellite, Lumber, Fabric	5/10/20XX	RA-1
	5/10/20XX	RA-1			5/10/20XX	RA-1
	5/14/20XX	RA-1		Trench, Hook-up	5/14/20XX	RA-1
	5/10/20XX	RA-1		Bonus	5/10/20XX	RA-1
	5/25/20XX	Cash			5/25/20XX	President
	6/2/20XX	RA-1		Landfill, Concrete, Trench	6/4/20XX	RA-1

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	5/31/20XX	CO-4			6/6/20XX	CO-4
	6/12/20XX	Cash			6/12/20XX	President
	6/16/20XX	CO-4			6/18/20XX	CO-4
	6/25/20XX	Cash			6/25/20XX	
	7/16/20XX	Cash			7/16/20XX	
	6/28/20XX	CO-4			7/3/20XX	CO-4
	6/27/20XX	CO-4			7/3/20XX	CO-4
	7/8/20XX	CO-5			7/17/20XX	
	7/9/20XX	Cash			7/9/20XX	
	7/12/20XX	CO-4			7/17/20XX	CO-4
	7/20/20XX	Cash			7/20/20XX	President
	7/24/20XX	Cash			7/24/20XX	
	7/25/20XX	CO-4			7/31/20XX	CO-4
	7/26/20XX	Cash			7/27/20XX	
	8/11/20XX	Cash			8/16/20XX	
	8/22/20XX	Cash			8/22/20XX	
	9/6/20XX	CO-4			9/6/20XX	CO-4
	9/7/20XX	Cash			9/7/20XX	
	9/20/20XX	CO-4			9/25/20XX	CO-4
	10/4/20XX	CO-4			10/9/20XX	CO-4
	10/23/20XX	CO-4			10/23/20XX	CO-4
	11/1/20XX	CO-4			11/6/20XX	CO-4
	11/15/20XX	CO-4			11/20/20XX	CO-4
	11/16/20XX	Cash			11/16/20XX	
	11/27/20XX	Cash			11/27/20XX	President
	12/12/20XX	CO-4			12/18/20XX	CO-4
Total						



1/23/20XX CO-6
 2/22/20XX CO-6
 3/30/20XX CO-6
 4/6/20XX CO-6
 5/9/20XX CO-7

President did not provide any contemporaneous substantiation for the aforementioned transactions. A handwritten response was provided in which President wrote an explanation for the transactions he recalled. He also typed an attachment which stated:

"Knowing all along that I'm not the best at keeping financial records and receipts, I've always gone with the option of others just paying my bills for me. Found volunteers that were willing to pick up my mortgage payments, gas, electric, phone and internet bills on a monthly basis.

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I even had those who would send money to me specifically for certain financial obligations such as my food and ongoing improvements around the facility to ensure the safety and comfort of all the motto in my care.

One couple paid for my well to be dug, another donated a nice SUV for me to use. Most of these never had the opportunity to 'write off' their contribution to ORG since they simply paid the bills directly. A gentleman in OC pays my home and car insurance. Currently the dog food is being provided at no cost to myself or the organization, utilities are still be paid by others and the purchase of cd's and mailing charges to get them to schools with humane education is also paid by interested parties."

Law

IRC §501(c)(3) provides for exemption of organizations organized and operated exclusively for charitable purposes, and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

IRC § 6001 provides that every person liable for any tax imposed by the IRC, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe.

IRC § 6033(a)(1) provides, except as provided in IRC § 6033(a)(3), every organization exempt from tax under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts and disbursements, and such other information for the purposes of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.

Treas. Reg. § 1.501(c)(3)-1(a) states 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.

Treas. Reg. § 1.501(c)(3)-1(b) **Organizational test--(1)** In general. (i) An organization is organized exclusively for one or more exempt purposes only if its articles of organization:

- (a) Limit the purposes of such organization to one or more exempt purposes; and
- (b) Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities, which in themselves are not in furtherance of one or more exempt purposes.

Treas. Reg. § 1.501(c)(3)-1(c) **Operational test--(1)** Primary activities. An organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily

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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.

Treas. Reg. § 1.501(c)(3)-1(c)(2) Distribution of earnings. 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.

Treas. Reg. § 1.501(c)(3)-1(d)(i) **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:

- (a) Religious,
- (b) Charitable,
- (c) Scientific,
- (d) Testing for public safety,
- (e) Literary,
- (f) Educational, or
- (g) Prevention of cruelty to children or animals.

Treas. Reg. § 1.501(c)(3)-1(d)(ii) An organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish 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.

Treas. Reg. § 1.6001-1(a) in conjunction with Treas. Reg. § 1.6001-1(c) provides that every organization exempt from tax under IRC § 501(a) and subject to the tax imposed by IRC § 511 on its unrelated business income must keep such permanent books or accounts or records, including inventories, as are sufficient to establish the amount of gross income, deduction, credits, or other matters required to be shown by such person in any return of such tax. Such organization shall also keep such books and records as are required to substantiate the information required by IRC § 6033.

Treas. Reg. § 1.6001-1(e) states that the books or records required by this section shall be kept at all times available for inspection by authorized internal revenue officers or employees, and

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shall be retained as long as the contents thereof may be material in the administration of any internal revenue law.

Treas. Reg. § 1.6033-1(h)(2) provides that every organization which has established its right to exemption from tax, whether or not it is required to file an annual return of information, shall submit such additional information as may be required by the district director for the purpose of enabling him to inquire further into its exempt status and to administer the provisions of subchapter F (section 501 and the following), chapter 1 of the Code and IRC § 6033.

Rev. Rul. 59-95, 1959-1 C.B. 627, concerns an exempt organization that was requested to produce a financial statement and statement of its operations for a certain year. However, its records were so incomplete that the organization was unable to furnish such statements. The Service held that the failure or inability to file the required information return or otherwise to comply with the provisions of IRC § 6033 and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of exempt status.

In accordance with the above cited provisions of the Code and regulations under IRC § 6001 and § 6033, organizations recognized as exempt from federal income tax must meet certain reporting requirements. These requirements relate to the filing of a complete and accurate annual information (and other required federal tax forms) and the retention of records sufficient to determine whether such entity is operated for the purposes for which it was granted tax-exempt status and to determine its liability for any unrelated business income tax.

Taxpayer's Position

The facts have been presented to the ORG and they disagree with the government's position. The organization believes they qualify for exemption under section 501(c)(3) and provided an explanation of some of the activities done to support their position. The organization mentions they filed Form 990N in 20XX and 20XX. The organization received a small amount of income and some of the funds were provided specifically to President. President lives in a remote area and does not have a vehicle. One of the supporters allotted \$ a month for the CO-4 deliver food service. The funds were deposited in the organizations account. President states he provided a written explanation for all of the expenses that the assigned agent requested substantiation for and some of his responses were misquoted. For example, none of the organizations money was used to pay for his mortgage because he never paid or owed rent on the property and in 20XX it was purchased and placed in his name. President also explains that RA-1 was a handyman that was hired on occasion for necessary repairs to the kennels and surrounding infrastructure. None of the work done by RA-1 was for personal benefit. *See Exhibit A for the complete written position provided by taxpayer.*

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Government's Position

Based on the above cited law, it is the government's position that ORG has failed to meet its reporting/recordkeeping requirements and has not demonstrated it meets the requirements under section 501(c)(3). Section 6033 requires organizations exempt from tax to keep records and render statements as are required by rules and regulations prescribed by the Secretary. Treasury Regulation section 1.6033-2(i)(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.

The organization failed to demonstrate it met the operational test for a § 501(c)(3) organization. In order to meet the operational test, ORG must show it engages primarily in activities which accomplish one or more of such exempt purposes specified in section § 501(c)(3). Further, information has been obtained which shows ORG has not operated exclusively for charitable purposes because part of the organizations net earnings inured to the benefit of its President, President.

Forms 4564 sent to ORG requested documents such as bylaws, minutes, and application for exemption which were needed to determine if organizational requirements were met. Forms 4564 requested documents such as copies of Federal tax/information returns filed, and prior Service audit reports/letters/correspondence which were needed to determine if ORG met all filing requirements. The Forms 4564 also requested documents such as books and records of assets, liabilities, receipts, disbursements, check register, bank statements, and a sample of source documents for expenses which were needed to determine how funds were used and whether they were used for charitable purposes. The organization was given an adequate opportunity to provide the information required to conduct the examination. The organization did not provide books and records for the period under examination (or subsequent years) and did not meet the recordkeeping requirements in IRC §§ 6001 and 6033.

The organization had over \$ in gross receipts and \$ in expense. Substantiation was requested for a sample of questionable transactions identified in the summonsed bank information. Contemporaneous substantiation was not provided for any of these expenses to demonstrate how they served a charitable purpose. President provided an explanation of the expenditures he remembered; however his explanation indicated the organizations earnings inured to the benefit of private shareholders or individuals. The organizations funds were used to pay for his personal expenses.

President has signature authority on the organization's bank account and makes the decisions on the direction and policy of ORG. He is the founder and President of the organization and is considered an insider.

As seen in the summonsed bank information and President's response to IDR#3, the organization's funds have been used to pay his mortgage payments, gas, electric, phone, and

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Internet bills. No information was provided to demonstrate the expenses were allocated to take into account personal use and exempt use. President benefits from the organization paying his portion of the aforementioned expenses. This is not necessary for ORG tax-exempt purpose and is inurement.

A substantial amount of the organization's checks were written out to "Cash" to pay for gasoline. Since there wasn't corroborative information such as mileage logs, the assigned agent could not determine if these expenses served the organizations interests or private interests.

RA-1, an individual that performed services for the organization, was paid \$ during the period under examination. RA-1 is a handyman that worked on various jobs on President's property. No substantiation was provided to show how these expenses served the organization's interests. The organization did not furnish or file RA-1 a Form 1099.

CO-4, an online supermarket and food delivery service, was paid \$ by the organization. CO-4 website was reviewed and the only item for motto was "doggie sundaes". The assigned agent could not determine how these expenses served the organization's exempt purpose. Using organization funds to pay for President's groceries is also inurement.

An organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. The organization has not established that it's 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. See *Treas. Reg. § 1.501(c)(3)-1(d)(ii)*

This situation is similar to the case in Revenue Ruling 59-95. In that case, tax-exempt status was revoked for failure to establish that it was observing the required conditions for exempt status, namely, providing financial statements.

Conclusion

It is the Service's position that ORG failed to meet the reporting requirements under IRC § 6001 and § 6033 to be recognized as exempt from federal income tax under IRC § 501(c)(3). The organization did not provide information or demonstrate that it was organized and operating exclusively for exempt purposes and no part of net earnings inured to the benefit of any private shareholder or individual.

Accordingly, the organization's exempt status should be revoked effective January 1, 20XX. Contributions will no longer be deductible under section 170 of the Internal Revenue Code.