

Internal Revenue Service

Department of the Treasury

Employer Identification Number:

Release Number: **201643025**
Release Date: 10/21/2016
Date: July 25, 2016
UIL Code: 501.03-05

Person to Contact:

Employee ID Number:
Tel:
Fax:

Certified Mail

Dear :

This is a final adverse determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code (the "Code") section 501(a) as an organization described in section 501(c)(3) .

The favorable determination letter to you dated December 2007 is hereby revoked and you are no longer exempt under section 501(a) of the Code effective January 1, 2008.

The adverse determination was made for the following reason(s):

You are not operated exclusively for charitable purposes.

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. 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.

You have agreed to waive your right to contest this determination under the declaratory judgment provisions of Section 7428 of the 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,

Appeals Team Manager

Enclosure: Publication 892

Internal Revenue Service
Tax Exempt and Government Entities Division
Exempt Organizations: Examinations

Department of the Treasury

Date: May 27, 2015

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Manager's Name/ID Number:

Manager's Contact Number:

Response due date:

Certified Mail – Return Receipt Requested

Dear :

Why you are receiving this letter

We propose to revoke your status as an organization described in section 501(c)(3) of the Internal Revenue Code (Code). Enclosed is our report of examination explaining the proposed action.

What you need to do if you agree

If you agree with our proposal, please sign the enclosed Form 6018, *Consent to Proposed Action – Section 7428*, and return it to the contact person at the address listed above (unless you have already provided us a signed Form 6018). We'll issue a final revocation letter determining that you aren't an organization described in section 501(c)(3).

After we issue the final revocation letter, we'll announce that your organization is no longer eligible for contributions deductible under section 170 of the Code.

If we don't hear from you

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final revocation letter. Failing to respond to this proposal will adversely impact your legal standing to seek a declaratory judgment because you failed to exhaust your administrative remedies.

Effect of revocation status

If you receive a final revocation letter, you'll be required to file federal income tax returns for the tax year(s) shown above as well as for subsequent tax years.

What you need to do if you disagree with the proposed revocation

If you disagree with our proposed revocation, you may request a meeting or telephone conference with the supervisor of the IRS contact identified in the heading of this letter. You also may file a protest with the IRS Appeals office by submitting a written request to the contact person at the address listed above within 30 calendar days from the date of this letter.

The Appeals office is independent of the Exempt Organizations division and resolves most disputes informally.

For your protest to be valid, it must contain certain specific information including a statement of the facts, the applicable law, and arguments in support of your position. For specific information needed for a valid protest, please refer to page one of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*, and page six of the enclosed Publication 3498, *The Examination Process*. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process. Please note that Fast Track Mediation referred to in Publication 3498 generally doesn't apply after we issue this letter.

You also may request that we refer this matter for technical advice as explained in Publication 892. Please contact the individual identified on the first page of this letter if you are considering requesting technical advice. If we issue a determination letter to you based on a technical advice memorandum issued by the Exempt Organizations Rulings and Agreements office, no further IRS administrative appeal will be available to you.

Contacting the Taxpayer Advocate Office is a taxpayer right

You have the right to contact the office of the Taxpayer Advocate. Their assistance isn't a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate can't reverse a legally correct tax determination or extend the time you have (fixed by law) to file a petition in a United States court. They can, however, see that a tax matter that hasn't 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:

Internal Revenue Service
Office of the Taxpayer Advocate

For additional information

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.

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

Issues:

- 1) Whether the _____ is operated exclusively for exempt purposes within the scope of Internal Revenue Code section 501(c)(3).
- 2) Whether there is a substantial nonexempt commercial purpose served by the organization in that the organization is also providing significant private benefit to the organization's insiders and contributors?

Facts:

_____ was incorporated on _____, as a _____ non-profit corporation, having previously operated as a for-profit organization. In December _____, the IRS recognized _____ as tax-exempt under IRC section 501(c)(3) and not as a private foundation as described in IRC §170(b)(1)(A)(vi).

The _____ Articles of Incorporation state the purpose(s) of the organization as follows:

"to promote and operate a school and ranch program in _____ for children with emotional and behavioral problems; to provide an environment where troubled youth can develop socially, intellectually, emotionally, spiritually and physically so that they can find themselves and be able to manage their personal lives to become successful well adjusted citizens; and to transact any other lawful charitable activity".

The preamble to the _____ bylaws states that _____ was primarily staffed by the _____ and his wife, _____, own the _____ (_____), on which _____ is located and operates. Listed _____ assets are the _____ cabin with cook house, vehicles, corrals, livestock, farmland, and crops—corn, alfalfa, oats.

programs/activities:

_____ was a licensed group home located on a _____ and _____ in _____ served boys ages _____ years old and promoted its program as offering behavior modification, equine therapy, and experiential education to at-risk boys. _____ served boys exhibiting ADD, ADHD, depression, low self-esteem, emotionally-troubled, narcissistic behavior, and underachievement. It was not, however, a treatment facility.

The number of boys _____ was licensed to house at its facility was _____ and _____ and _____ for _____. The increase in the latter years was due to the creation of _____ which allowed _____ to apply for a second license. The following table shows the estimated

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number of youth attending _____ per month for each of the four years. This information is an estimate compiled using primarily payments logs as many of the records were destroyed in a flood.

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.

s programs comprised the following

The boys were placed in the _____ before entering any long term program. This program was offered year round and generally lasted from _____ days to _____, although some would stay up to _____. The program is described as a Christian-based wilderness intervention and therapy program located in the _____. The program was based on an 1 _____.

Work by the boys included horse care, feeding baby calves, participating in cattle drives, building fences and mechanics. The knowledge gained by the boys included survival skills, conservation principles, range management, biology and plant identification, ecology, animal behavior and orientation and safe travel in the wilderness. In _____ the _____ was replaced with the _____, sometimes referred to as _____.

The _____ offered vocational training and horsemanship. The boys were not paid for their work and did not receive allowances.

The boys were also offered a home school program. Every year _____ would graduate _____ boys.

Tuition rate and fees:

In _____ and _____, tuition for the _____ was \$ _____ per day, plus a one-time, non-refundable, admission fee of \$ _____ to \$ _____. Tuition for the long term program was \$ _____ per month, plus a one-time, non-refundable admission fee of \$ _____. Fees covered counseling; tutoring; 24 hour supervision; room and board; academic classes; personal hygiene products; use of horse, saddle and all tack used; all bedding and laundry facilities; and use of all outdoor,

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camping gear. In tuition was increased to \$ per month, and the one-time, non-refundable, admission fee to \$

did not ask boys to leave the program in the event their parent(s) did not or were unable to pay for the tuition. would work with the parent(s) to agree to a discounted rate and/or a payment plan in line with what the family could afford. In instances where the parent(s) did not pay, the boy would participate in the program for free and would write off the unpaid portion.

did not provide records showing when or how often this happened during the period.

Facility:

assets consist of a , and a . The and were constructed in with funds provided by the . The is a square foot facility with three bedrooms containing four bunk beds each. Capacity was limited to boys per rules of . There was also a staff bedroom, classroom space, administrative offices, storage rooms, furnace room, washer/dryer room, two bedrooms for staff, living room, dining room, and kitchen. One full-time counselor and a mentor stayed with the youth around the clock.

The is a square foot steel frame building with a basketball court, gymnasium, boxing ring, free weights and exercise equipment, and was used daily by students.

The is a square foot pole barn. The center was used to conduct vocational and equestrian training for the students in the areas of equine therapy, horse training, reining and roping classes, basic cattle management, veterinarian skills, branding, and calving.

Officers/Board members:

The articles of incorporation states that the affairs and management of would be vested in the board of directors consisting of four persons--President, Vice President, Secretary, and Treasurer. In operation, the board of directors also served as officers of

The bylaws state that the board of directors consisted of three members and that the third member must be the executive director of . The executive director oversees and is responsible for all youth care. Additionally, the board of directors could only approve the appointment of an executive director from among the . The bylaws also state that the officers of consisted of a President, Secretary, and Treasurer. The officers would hold a one-year term. The bylaws state that the officers' duties consisted of the following:

- o President: will act as a liaison between the and the board of directors
- o Secretary: will keep record of all meetings
- o Treasurer: will maintain all financial dealings of

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..., founder of I ..., served as a director of the organization through at least ... and served as an advisor to the board through ... Prior to ... was the Vice President, Director, and house parent of I ... A review of ... day-to-day operations revealed that ... was still very much involved with running

Following are some of the members of the ... All reside on the ... acre parcel owned by ... and/or the family trusts.

1) ... is co-founder and the wife of (... In previous years, ... served as house parent of

2) ... and ... are the daughter and son-in-law of ... In addition to other, for-profit businesses, they own and operate the ... which started in ... taught the credited ... course every Friday at ... and handled the admission process at the ... She is also a certified marriage mentor, a certified Christian counselor, family life and abstinence educator, a PSSP certified breakthrough parenting instructor, and a home schooling mother of ... children. ... stated that ... teaching position was paid for by ... not by

... stated that he was the ... project manager in ... and the executive director of ... in subsequent years. His duties and responsibilities included facilitating the ... , and working with boys and their families. He did not draw compensation from ... but rather was paid from ... is also a certified marriage mentor, and a family life coach. He has a Master of Arts Degree in education with a focus on religious studies, and a Bachelor of Arts Degree in Physiology.

3) ... ran the ... as ... manager. He is ... and occasional employee of ... He is the owner/operator of ... and has a ... % interest in the

4) ... also ran the : ... He is ... and was executive director of ... In previous years, he served as counselor, ranch manager, and vocational director. He has a ... % interest in the

5) ... is ... He worked at the teen boot camp and

6) ... is ... She did the bookkeeping, general help, ran errands, and answered phones. Her compensation was about \$... per year.

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7) _____ is _____ in _____, she was brought in to be the business manager and bookkeeper of _____.

Minutes of the Board:

The board members of _____ also served as the organization's officers. The minutes show that officers/board members consist of three board/officers and three advisors from the _____. The _____ members were not listed as officers or board members of _____.

Contracts:

Contracts between _____ and _____

The lease agreement between _____, dated July _____ states that the _____ agreed to lease to _____ the premises located at _____. The premises includes the main ranch residence and any subsequent dwellings, all outbuildings, all lands titled to the _____, all equipment and vehicles, all interior furnishings, all recreational equipment, together with all appurtenances, for a _____ year term to commence on _____ and end on _____. The rental fee was \$ _____ per month.

Per an "Agreement" dated _____, between _____, certain agreements and statements by the parties were set forth in the document. The document, in its entirety, outlines the understanding that _____ had a duty and responsibility to pay for and operate cattle ranching operations on behalf of _____ and for the benefit of the _____.

2. Consideration. In consideration of this Agreement, the net proceeds of sale (determined as sales price less expenses to ship and sell) of all _____ and _____ intended for slaughter raised from the ranching operation, upon the premises during the term of this Agreement shall be divided to the _____ based on _____ and to _____ based on _____. In addition to its obligation to maintain _____ numbers as herein required, _____ shall during the term hereof have the continuing duty _____.

3. Operating Costs. _____ shall have the duty to pay and discharge all charges either directly or by reimbursement to _____ upon demand, for (1) all repairs and maintenance charges to any farm equipment and machinery and (2) all charges of any kind made by any public or private utility or other for gas, electric power, or other services furnished to or placed upon the premises during the term hereof, including charges made for livestock feed delivered to the premises by third parties and charges for gasoline and diesel fuels used in the ranching operation.

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5. Purpose. The purpose of this agreement is to allow [redacted] continued use of the properties in order to achieve its charitable non-profit purpose in helping the troubled youth accepted into its program with vocational experience, outdoor activities, animal care and training and involvement in ranch operations. . . .

8. Net Agreement. It is the intention of [redacted] that the consideration payable to [redacted] pursuant to this Agreement shall be net to [redacted] and that all costs, expenses, obligations, taxes and assessments, utilities and charges of every kind or nature relating to the properties (except as may be otherwise specifically provided in this Agreement) and the ranching operation which arise or become due during the term of this Agreement, including the cost to register, record and maintain the [redacted] upon the premises, shall be paid by [redacted] directly, or by reimbursement to [redacted] upon demand, and that [redacted] are hereby indemnified by [redacted] against all of such costs, expenses and obligations.

9. Repair and Maintenance. [redacted] shall be responsible for all necessary costs of maintenance and repair of the properties, including, without limitation, all farm equipment and the improvements to the deeded real estate listed in Exhibit "A" during the term of this Agreement. In this regard, and without limiting the generality of the foregoing, [redacted] shall, at its own expense, pay or provide for all necessary [redacted] services on [redacted], control the c [redacted], maintain fences and water sources, maintain facilities and equipment, including tack, herd and trail all cattle and protect livestock from predators.

Contrary to the agreements entered into, and based upon all available information, it appears that [redacted] never reaped the benefit of income from the [redacted] set forth in the Consideration section of the [redacted] Agreement. It does appear, however, that [redacted] bore all of the expenses outlined in the other sections of the Agreement. [redacted] was able to fund the expenses through tuition charged for youths attending the program.

Additionally, the contract states that the [redacted] and [redacted] can continue to reside on the [redacted] and to engage in the family livestock and agricultural business. family members may also at any time be hired as staff members of [redacted]

In a proposed Long Term Lease Agreement provided to the examining agent in this case in [redacted] the family enterprise is described as follows.

WHEREAS, THE [redacted] operates a [redacted] located outside [redacted] [redacted] is operated on approximately [redacted] [redacted] which are owned, or leased, by the [redacted] by and through the [redacted] The property is used for various purposes including [redacted] operations,

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the families' primary residences, and for the charitable and educational programs conducted by _____ and described below in greater detail. The area is a rugged and remote wilderness region in _____ near the _____

In the next paragraph of the document, it states the following about the students.

... During their two to twelve month stay at _____, the students matriculate through an intensive four-phase curriculum that combines the daily life and work activities of a traditional ranch cowboy with ... life skills and vocational training opportunities.

Contracts between _____ and _____ of clients:

Examination of the financial contract between _____ and the _____ of participating boys revealed a dual contract between _____ and _____ (hereinto known as the '_____ or' _____) and the _____ of participating boys. The contract shows what costs the _____ would be responsible for in addition to tuition. For example:

- _____ % of cost incurred for finding the student when the student runs away from the _____
- Responsible for all medical and hospital expenses of the boys.
- _____ needs to repurchase equipment if student's equipment was destroyed through neglect or abuse.
- Financially responsible for replacing or repairing _____ property if the boys destroys or damages the property.
- Responsible for cost of transporting the boys to _____ from _____ I _____. The cost is \$ _____ during business hours and \$ _____ for non-business hours. There was no charge if the transport was from (_____ during business hours.
- Responsible for any additional costs incurred for staffing, medical, mental health treatment and consultation that may not be covered by insurance.
- Responsible for payment of tuition. Interest would be assessed on any balance overdue by 30 days each month until balance is paid in full. There's no refund if the boys are to withdraw early.

During examination of the organization books and records, the examining agent obtained a copy of the _____ profit and loss statement. The profit and loss statement shows that in _____ the _____ reported receiving income of \$ _____

Related for-profit entities:

During the examination, _____ disclosed the following related for profit entities:

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- 1.
- 2.
- 3.
- 4.
- 5.
- 6.
- 7.
- 8.
- 9.
- 10.

_____ advertises itself as raising high quality registered ,
for-profit commercial operation. The ranch contains the primary residences of the
families.

It is a
and

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_____ are trustees of the _____ and the _____. These two revocable trusts own the approximately _____ of property upon which many of the following entities are operated.

_____ was the founder of _____. _____ are named as Directors of _____. _____ owns a _____ % interest, _____ owns a _____ % interest and _____ owns a _____ % interest in _____. _____ shares facilities with _____ and uses _____ assets to conduct its business.

_____ is a young adult program for men aged _____ to _____ years old. The program is for young men overcoming substance abuse, anger issues, and negative and potentially destructive behavior patterns. The _____ handbook states that _____ will help young men in their school work, but that parents will have to cover the cost of curriculum and credits. All other educational materials are included in enrollment cost and covered under the admission fee. Rules for _____ are the same rules as for _____.

Occasionally, _____ young men would be mixed with the younger boys, but under heavy supervision (i.e., _____). _____ workdays and all other activities are separate from the younger boys program--housing, meals, etc.

The _____ is the sole proprietorship of _____ (i.e., _____). In response to Information Document Request (IDR) dated _____, the POA stated that _____ owns the cattle. The cattle were purchased in _____ and are used in the operations of the _____ as well as by _____, and the _____ entities in conducting their activities. _____ youth participate in cattle drives and work with the cows several times a year when they are brought into corrals.

_____ is also a cattle business and the sole proprietorship of _____ of _____.

_____ owned _____ from _____. The _____ activity held two, _____ leases and a _____ lease permit for the _____ (referred to as the _____). The lease permits were transferred to _____ and _____. The leases permit a total of _____ to be held on the land. _____ youth participated in cattle drives on the _____.

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properties while working with _____ and _____. Additionally, _____ organized outings to the _____ where the youth participated in recreational activities.

_____ owns a _____ of property near the _____ and operates a seed business. It is owned _____ % by _____ and _____ % by _____.

_____ was owned _____ % by _____ and _____ % by _____ from _____ through part of _____. The corporation was administratively dissolved in _____. It operated a _____ program in which the _____ youth were initially enrolled. During _____, the activities were taken over by _____, a subsidiary of _____.

_____ is a subsidiary of _____ created to act as a second group home under the direction of _____. It was created in order to provide services to _____ additional youth as the _____ was unable to license two group homes to the same entity.

_____ is a for-profit corporation that was formed by _____. The corporation has taken over all operations of _____ beginning in _____. _____ is the Director and Incorporator.

Youth participation in for-profit entities

POA, _____, provided the following description of youth activities in the for-profit activities.

_____ youth participated in the farming and ranching activities of the above entities based upon seasonal demands. In general, _____ youths spent an average of three to four hours per day outside in the summer, and one to two hours in the winter. No records were kept to substantiate time spent by _____ youths or the paid employees of these activities. Employees were paid wages to assist with the following activities; however, the _____ were not compensated for labor performed in carrying out any of the following activities.

From _____ (: _____), _____ youths participated in the following:

Horsemanship: Youths were taught basic horsemanship skills including grooming, saddling, riding, feeding, and appropriate comportment around horses. Since leisure time is also spent riding, it is difficult to quantify the time spent on this activity, but was estimated at three to ten hours per week. _____ paid all wages relating to this activity except for _____ who were compensated by the _____ and _____ was not compensated for _____.

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this activity from any entity. The horses, horse related equipment and land were owned by the use of assets is governed by the agreements between and the

Fence Building: youths participated in repairing fence as needed on the property. Estimated time was three to five hours per week. paid all wages relating to this Activity except for who were paid by the and did not receive any compensation for this activity from any entity.

The POA claimed that for every hour of work youths put in, one to two hours of additional work was often performed to undo and redo the work. This time was not compensated for by ; the costs were absorbed by the also paid for repairs and replacement costs of entity-owned equipment pursuant to the Agreement. did not compensate the entities for time lost due to equipment repairs. According to the POA, all materials used in this activity were paid for by the

The POA stated that fence building provided by ; youths was not a benefit to any of the related entities. While over time some of the youths became more proficient, the men who trained and supervised youth could have done the job in a fraction of the time. As a result, fence repair came at a cost of workers (specifically , and) spending more time on fence building than would have been otherwise needed, and a general loss in productivity to the for-profit entities.

Farming: youth participated in farming activities by learning to use tractors and various farming implements including levels, roller harrows, and discs to prepare the fields for planting. Because these activities involve heavy machinery posing significant safety risks, farming activities are used as an incentive and reward for good behavior.

A trainer would spend a minimum of two days (one to two hours per day) in a tractor teaching how to safely operate the equipment, how to ensure that proper levels of oil, etc., were maintained, and how to correctly prepare the land. When the trainer felt the youth was ready, the youth would be allowed to drive the tractor with the trainer in the cab. This direct supervision went on for several days. During the entire time that was in operation, only five boys were allowed to operate the machinery totally on their own. paid all wages relating to this activity except for who were compensated by the did not receive compensation for this activity from any entity.

According to the POA, did not receive compensation from the for-profit entities for the work conducted by the youth, nor did or the receive any compensation for the use of equipment. did pay for repairs and replacement of equipment pursuant to the agreement between and the

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Irrigation: youth participated in cutting troughs from ditches out into a field. This usually required between 30 to 45 minutes of work per field. The estimated time spent by youths was approximately one hour per day. paid all wages relating to this activity except for who were compensated by the did not receive any compensation for this activity from any entity. According to the POA, by allowing youth to participate in this activity it decreased the productivity of the because of faulty and sub-par work that had to be redone by employees.

Working with Cows: Several times a year, the cattle were brought to the corrals and moved through loading chutes for general management tasks. This included administering medication, treatment for parasites, and basic doctoring. youths participated by helping to ring the animals to the corrals and push them through the loading chutes; but did not directly treat the cows. This was done three to five times each summer. and lasted from a few hours to a full day. paid all wages relating to this activity except for who were compensated by the did not receive any compensation for this activity from any entity.

According to the POA, jobs were created for the youths so they could participate even though their help was not needed. This resulted in wasted time and facility repairs. The activity involved about cows and could have been completed by four to five skilled adult men but with youth, ten to fifteen workers were needed.

Cattle Drives: Once or twice per Summer, the cattle owned by were moved from the to the . Moving cattle covers miles and requires the oversight of four adult skilled men. When youth participated in the cattle drive, the operation took a full two days (much longer than if the youth were not involved) and did not decrease the number of skilled cowboys required. paid all wages relating to this activity except for who were compensated by the did not receive any compensation for this activity from any entity.

Mechanic Work: youth assisted in working on tractors, vehicles and other equipment. Generally, they worked on equipment/vehicles, and occasionally worked on machinery owned by the or other entities. In general, youth observed and provided very basic assistance. paid all wages relating to the training and supervision of this activity. did not receive any compensation for this activity from any other entity.

Feeding: Feeding ranch animals was the primary outside activity engaged in by youths during the winter. Feeding the animals involved using a tractor with a feed wagon attached. One boy operated the tractor while the other operated the loader and dumped hay, beet tailings, and corn silage into the wagon that mixed the feed. The boys then drove the tractor to the corral to feed the animals. Estimated time spent was one hour per day. paid all wages relating to this activity except for who were compensated

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by the _____ did not receive any compensation for this activity from any other entity.

Form 990, Return of Organization Exempt From Income Tax:

_____ signed the Form 990 in _____ signed the Form 990 in
and _____ signed the return in _____

On the _____ Form 990, Part II, Schedule L, _____ reported a loan from _____ (a for-profit entity). The Form 990 reported that the loan was to meet payroll expense needs. The loan amount was \$ _____ and was not documented in a written agreement. Schedule L also shows two other loans. One from _____ of \$ _____ and _____ . The return indicated that both of the loans had no written agreements and were approved by the board. Part IV of Schedule L indicated that business transactions involving interested persons were "still under review".

Form 4562, *Depreciation and Amortization*, did not reflect any vehicles owned by _____

The organization's Form 990 reported its primary revenue source deriving from program service revenues and grants. The primary revenues for _____ are shown below:

	TY	TY	TY	TY
Contributions, gifts, grants:	\$	\$	\$	\$
Program service revenue:	\$	\$	\$	\$
TOTAL REVENUE	\$	\$	\$	\$

The organization's program service revenues consisted solely of tuition fees. The primary grant donor in _____ was from the _____ of \$ _____ of \$ _____ and from _____ of \$ _____ are the parents of one of the participating boys in the _____ program.

The organization's Form 990 listed its primary expense items as follows:

	TY	TY	TY	TY
Other salaries/wages	\$	\$	\$	\$
Payroll taxes	\$	\$	\$	\$
Occupancy		\$	\$	
Student housing/util				\$
Student food				\$
Operations & rent				\$
Occupancy	\$			

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Bad debts	\$			
Fees for service: other		\$		
Benefits paid to/for members			\$	
Supplies	\$	\$	\$	\$
Depreciation	\$			\$
Insurance	\$	\$	\$	\$
Fuel	\$	\$	\$	
Repair	\$	\$	\$	
Vet expense	\$			
Tax/license		\$	\$	
Chemicals	\$			
Freight	\$			
Seed	\$			
Other expenses		\$	\$	\$

Financial Information:

Examination of source documents indicates expenses were either authorized by [redacted]. The source documents also show that [redacted] and [redacted] signed for all of [redacted] expenses.

The following are examples of expenses that were paid by [redacted] for use of the assets:

1) Sampling of fuel expenses shows that primarily [redacted] signed the checks for fuel expenses. The payments were for diesel for semi/truck/trailing cattle. Payments were also made for gas to fill the [redacted] mini van, Datson, white van, and blue van, etc.

2) Sampling of seed expenses reveal that the expenses were for the agricultural business. The seed expenses were charged to [redacted] account. Review of the [redacted] account invoices and monthly/yearly statements revealed that the purchases and payments were made for machine parts, shop work, labor, and others. Review of invoices and cancelled checks show that the checks were signed by [redacted] and the funds were coming from [redacted] main checking account.

[redacted] received no income from the sale of the seeds and did not use these seeds.

3) Sampling of repair and maintenance expenses reveal that the expenditures were for parts, labor, saddle repairs, shop work for the [redacted]!

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4) Sampling of veterinary expenses shows payments for horses, cattle, dogs, cats, etc. owned by the

5) Review of the billing statements shows that the services provided by Attorney of \$ was for services related to s for-profit partnership business,

6) In , there were payments going to the owned vehicles. The following are examples of those expense items:

- general ledger reported ; paying its related organization, Ascent, \$ for accounting and legal fees, on , check #
- Taxes and license expenses associated with the vehicle fees and property taxes.
- paid for telephone and utility expenses of the personal residences.
- charged a monthly lease for use of . The lease payments were \$

7) paid for insurance. The insurance was for liability (for commercial use) and commercial auto insurance from Under the it was a package policy for and

A review of the Certificate of Insurance named the insured as: and and the certificate holder name was shown for: . Sometimes the certificate holder was shown for and as the additional insurer.

A review of auto insurance policies shows coverage for the following vehicles which were not listed as assets of

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8) Review of books and records shows that has been paying \$ and \$ per month for auto loan.

The table below is a summary schedule showing total expenses paid by for use of the

	TY	TY	TY	TY
Insurance	\$	\$	\$	\$
Fuel	\$	\$	\$	\$
Repair & maintenance	\$	\$	\$	\$
Vet expense	\$	\$	\$	\$
Occupancy	\$	\$	\$	\$
Tax/license	\$	\$	\$	\$
Legal	\$	\$	\$	\$
Owner's draw	\$	\$	\$	\$
Utilities	\$	\$	\$	\$
Freight	\$	\$	\$	\$
Chemicals	\$	\$	\$	\$
Supplies	\$	\$	\$	\$
Advertising&promo	\$	\$	\$	\$
Telephone/telecommunication	\$	\$	\$	\$
Farm & supply	\$	\$	\$	\$
Ranch lease	(\$	(\$	(\$	\$
Ranch equipment	\$	\$	\$	\$
Personal loan	\$	\$	\$	\$
Property taxes	\$	\$	\$	\$
Loan	\$	\$	\$	\$
Total	\$	\$	\$	\$

In addition to the direct payment of ranching expenses of the various enterprises, an analysis of labor costs for the various family enterprises show that it incurred a very small percentage of labor costs for its ranching operations, as opposed to whose labor costs were generally in excess of % each year. Combining all family operations, their labor costs as a percentage of receipts were generally less than % each year.

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Further, given the fact that a number of _____ paid staff was unrelated to ranching activities (i.e. administrative, teaching or housekeeping and food preparation), we can only surmise that a great deal of the labor needed to work the _____ ranching operations came from the youths themselves. This was all accomplished under the auspices of teaching of life skills and vocational training by combining the daily life and work activities of a traditional ranch cowboy.

Law:

IRC section 501(c)(3) describes certain organizations exempt from taxation under section 501(a) of the Code and reads as follows:

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 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, 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.

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) of the Code, the organization must be one that is both organized and operated exclusively for one or more of the purposes specified in that section. If an organization fails to meet either the organizational or operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that an organization will not be regarded as operated exclusively for exempt purposes if more than an insubstantial part of its activities is not in furtherance of exempt purposes. The organization will not qualify for exemption if a nonexempt activity is more than an insubstantial part of its activities, or if an activity of the organization has more than an insubstantial nonexempt purpose.

Section 1.501(c)(3)-1(c)(2) of the Regulations 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. Section 1.501(a)-1(c) states that the word "private shareholder or individual" refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a

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private interest. Thus, 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.

Section 1.501(c)-1(d)(3) of the regulations defines the term "educational" as including the instruction or training of the individual for the purpose of improving or developing his capabilities, or the instruction of the public on subjects useful to the individual and beneficial to the community.

In Better Business Bureau v. United States, 326 U.S. 279 (1945), the court held that regardless of the number of truly exempt purposes, the presence of a single substantial non-exempt purpose will preclude exemption under section 501(c)(3).

In Living Faith, Inc v. Commissioner, 950 F. 2d 365, a nonprofit organization which operated restaurants and health food stores in accordance with the doctrines of the Seventh-day Adventist Church. The court found that Living Faith conducted its operations with a substantial commercial purpose, and therefore does not qualify as a tax-exempt organization.

Harding Hospital, Inc. v. United States, 505 F.2d 1068, 1072 (6th Cir. 1974), the court holds that the transfer of funds directly to the disqualified persons and to their business served the financial interests of the disqualified persons and/or their business.

Church by Mail, Inc. v. Commissioner, 769 F .2d 1387 (9th Cir. 1985) and est of Hawaii v. Commissioner, 71 T.C. 1067 (1979) states that an organization has a substantial commercial purpose that serves a private rather public interests, it will not be recognized as exempt.

Taxpayer's Position:

POA, stated in a letter dated _____ that _____ was willing to agree to revocation and properly dispose of its assets in order to prevent additional excess benefit transactions under IRC section 4958.

However, _____; will not agree to a retroactive revocation to _____ as this is believed to be doubly punitive and based on misunderstandings between _____ and the examining agents. The taxpayer has requested relief from retroactive revocation.

Government's Position:

Based on the facts and circumstances described above, it is the government's position that _____ does not qualify as an organization exempt from tax because _____ did not operate exclusively for purposes described under IRC 501(c)(3). Therefore, the government is proposing the revocation of the organization's tax-exempt status under IRC section 501(c)(3).

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The facts show that _____ was paying for the expenses of the _____ assets and that the youths were indirectly being used for their services for the benefit of the privately owned _____ business. Reg. 1.501(c)(3)-1(c)(2) states that an organization is not operated exclusively for exempt purposes if its net earnings inured to the benefit of private individuals.

The organization's website and handbook advertised the _____ to the parents and guardians of participating youth and to the general public as the _____ and the assets used in the ranch were advertised as belonging to _____. For example, the _____ handbook gave the appearance that the ranch equipment and vehicles were _____. In actual operation, the ranch equipments and vehicles belonged to the _____.

The _____ is actually made up of five or more for-profit entities. The examining agent discovered several other for-profit family ranches within the _____ which _____ then disclosed. The assets used in conducting _____ activities belonged to the _____.

_____ has no assets other than the _____, and _____ center. All three assets are improvements to the land owned by _____.

During the second visitation to _____, it was discovered that the _____ farm equipment, supplies, livestock, and _____ assets were also used by participating boys from the _____ or-profit businesses. For example, sampling of fuel expenses disclosed that _____ has been paying _____ for the _____ business. _____ signed the checks for fuel expenses used to pay for diesel for semi/truck/trailing cattle.

Review of the parent/guardian financial contract between _____ and the _____ indicate that the parents/guardian of participating youths had already paid for the use of the _____ assets through its tuition costs. In addition, the contracts primarily benefitted _____ for-profit businesses rather than the _____, as the youth were to initially enroll in the _____ first and then migrate over to the _____ program.

In the years under examination, it was revealed that _____ earnings have inured to the benefit of its insiders. The insider is in a position to exercise control over the organization's earnings as if they were his/her own by using them at will rather than within limitations. The facts show that _____ and other _____ members were able to use the organization's funds as if they were their own. _____ and _____ controlled operations and financial affairs. The board members listed on the Form 990 were mere figureheads with no authorities. _____ founded _____ and he made decisions for _____ The governing body was not required to approve the expenditures of _____.

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The examination determined that a substantial amount of the expenditures were for the personal use of _____, and their commercial businesses. The family members wrote and signed all the checks. There were no signatures by the officers/board members. The officers/board members did not authorize any expense vouchers. _____ and _____ signed all returns, checks, and controlled all bank accounts.

Furthermore, the labor services provided by the youths benefited the _____ as well as the _____ for-profit commercial agricultural businesses.

When an organization operates for the benefit of private interests, such as designated individuals, the creator or his family, or persons directly or indirectly controlled by such private interest, the organization by definition does not operate exclusively for exempt purposes. Section 1.501(c)(3)-1(d)(1)(ii).

Treas. Reg. section 1.501(c)(3)-1(f)(2) application

Following is a discussion of the five factors contemplated in §1.501(c)(3)-1(f)(2)(ii) of the Treasury Regulations for revoking 501(c)(3) status on the grounds of inurement when the inurement also constitutes excess benefit transactions ("EBTs"):

Factor #1: Size and scope of activities furthering exempt purposes before and after EBTs

_____ has engaged in regular and ongoing activities that further exempt purposes until _____ has continuously provided a home for troubled boys prior to and during the EBTs explained in this report. During _____ ceased operating and the founder, _____ started a for profit entity, _____, which took over all activities previously conducted by _____ is currently using all assets owned by _____

_____ estimated, based on their records that it served _____ boys in _____, in _____; in _____ and _____ in _____ was allowed to have _____ boys at a time during _____ and _____; In _____ and _____, the number was increased to _____ by adding a second license under the _____ subsidiary. Based on _____ available records, the table below estimates how many boys _____ served each month.

	Jan.	Feb.	Mar.	Apr.	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.

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While the number of boys allowed to attend the ranch at any given time is limited by the State licenses, the cost of attendance is also a hindrance for the families of many troubled youth in our society. To attend the _____, the family was expected to pay tuition, room and board of \$ _____ per month. This limits attendance to families that have the means and ability to pay the fees.

During the four year's under examination, _____ served approximately _____ boys for the entire period. Given the number of boys that received services by _____ over the years, the well-being of our society will not unreasonably suffer if _____ is not operating as a tax-exempt organization in the future. Additionally, in light of the fact that _____ activities have been taken over by a for-profit corporation, which provides the same services to troubled boys, consideration of this first factor weighs in favor of revocation.

Factor #2: Size and scope of the EBTs in relation to the size and scope of activities furthering exempt purposes

As explained in the facts, the boys worked in the for profit entities owned by the founder, as part of their rehabilitation, which provided a benefit to the entities. Therefore, even though the boys were being provided rehabilitation, there was still private benefit being provided to the for profit entities in addition to the EBTs. _____'s activities of providing a home for troubled boys do not lessen the instances of inurement detailed in this report.

The number and amount of EBTs is significant in relationship to the organization's exempt activities. As you can see from the table below, the EBT transactions were substantial in comparison to the total expenses of _____. We note that the percentage of transactions decreased in _____, which is when our examination of _____ began. In all years, the size of the EBTs is comparison to the other expense is substantial.

						<u>4-year Total</u>
EBT Transactions	\$	\$	\$	\$		\$
Total Revenue	\$	\$	\$	\$		\$
Percentage of Revenue		%	%	%	%	%

As shown above, the EBTs from _____ through _____, is approximately _____% of exempt revenue. This is a substantial level of EBTs, and does not account for any other private benefit that may have been received by the for profit entities from labor provided by the boys. Therefore, consideration of this second factor weighs in favor of revocation.

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Factor #3: Whether there were multiple EBTs

engaged in multiple EBTs with _____ and his for profit entities continuously over multiple years, as you can see from the facts of this report. _____ entered into two contracts with _____ since its inception in _____. The contracts entered into between _____ and _____ outlined the understanding that _____ had a duty and responsibility to pay for and operate the cattle ranching operations on behalf of and for the benefit of the _____. While we are only examining the years _____ through _____, we assume that the EBTs were ongoing since the initial contract was enter into on _____

_____s activities and operations were integrated with the for-profit operations in such a way that the EBT's and inurement have happened on a day-to-day basis. During the initial visit at _____ facilities, the IRS was unaware of the for-profit entities and was under the impression that the activities of the for-profit entities were part of _____s operations. It wasn't until after the first visit that the IRS became aware of the for-profit entities and their role in the activities of _____. No clear separation between these entities and _____ has been shown.

Due to the continual and frequent nature of the EBTs, consideration of factor three weighs heavily in favor of revocation.

Factor #4: Whether safeguards have been implemented by the organization

The organization has not implemented any safeguards to prevent excess benefit transactions in the future. While _____ considered revising the contract between the organization and the _____, the revisions were never completed. Oversight of _____s activities and financial transactions were the sole responsibility of _____ or one of his family members. Board members only visited _____ periodically and held sporadic board meetings. All of the day-to-day operations were conducted by _____ and his family members.

As discussed above, _____ ceased operations in _____ and the _____ began operating the activities as a for profit entity called _____. _____ is a for profit entity owned by _____. It is operating as a for profit home for troubled boys and is using the assets owned by _____ in its operations with no compensation to _____. Therefore, inurement to _____ is continuing even after _____ has ceases operations.

Due to the lack of safeguards being implemented by _____ consideration of Factor four weighs greatly in favor or revocation.

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Factor #5: Whether the EBTs have been corrected or the organization has made a good faith effort to seek correction

To date, _____ has not received correction of the EBTs nor have they sought correction of the transactions. For this reason, consideration of factor five weighs in favor of revocation.

As explained in factors 1 through 5, consideration weighs heavily in favor or revocation of exempt status. s

Conclusion:

The _____ does not qualify as an organization exempt from tax because _____ did not operate exclusively for purposes described in IRC 501(c)(3), _____ earnings and assets inured to the benefit of private individuals, and more than an insubstantial part of its activities furthered private purposes rather than exempt purposes when _____ paid for the expenses of the _____ for profit ranch and related for-profit businesses.

The inurement detailed in this report is a substantial amount of inurement compared to _____ revenue. This puts _____ in violation of §1.501(c)(3)-1(c)(2) of the Treasury Regulations, and warrants revocation of its exempt status under Code §501(c)(3). Given the frequent and continuous nature of the inurement from _____ through _____, revocation is proposed effective _____.

Therefore, _____ is liable for filing Forms 1120 for the tax year ended _____ as well as each subsequent tax year.