



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
TE/GE: EO Examinations
1100 Commerce Street, MC 4920 DAL
Dallas, TX 75242

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

August 22, 2016

Release Number: 201647008

Release Date: 11/18/2016

UIL Code: 501.03-00

Taxpayer Identification Number:

Person to Contact:

Identification Number:

Contact Telephone Number:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear :

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the Code). Our favorable determination letter to you dated July 7, 19XX is hereby revoked and you are no longer exempt under section 501(a) of the Code effective January 1, 20XX.

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

You are not operating exclusively for any charitable purpose, educational purpose, or any other exempt purpose. Our examination reveals that you are not engaged primarily in activities which accomplish charitable, educational or other exempt purposes as required by Treas. Reg. 1.501(c)(3)-1(c)(1). Your activities, including your financial transactions, more than insubstantially furthered non-exempt purposes. Moreover, you failed to establish that you were not operated for the benefit of private interest of your founder and president as required for continued recognition of exemption pursuant to Treas. Reg. 1.501(c)(3)-1(d)(1)(ii).

Contributions to your organization are no longer deductible under IRC §170 after January 1, 20XX.

You are required to file Form 1120 U. S. Corporation Income Tax Return. The return should be filed with the appropriate Service Center for tax years ended December 31, 20XX and December 31, 20XX and for all tax years thereafter in accordance with the instructions of the return.

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 Internal Revenue Code.

If you decide to contest this determination under the declaratory judgment provisions of section 7428 of the Code, a petition to the United States Tax Court, the United States Claims Court, or the district court of the United States for the District of Columbia must be filed before the 91st Day after the date this determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing petitions for declaratory judgments by referring to the enclosed Publication 892. You may write to these courts at the following addresses:

United States Tax Court
400 Second Street, NW
Washington, D.C. 20217

United States Court of Federal Claims
717 Madison Place, NW
Washington, D.C. 20005

United States District Court for the District of Columbia
333 Constitution Avenue, NW
Washington, D.C. 20001

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect your taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit taxpayeradvocate.irs.gov or call 1-877-777-4778.

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

Sincerely,

Margaret Von Lienen
Director, EO Examinations

Enclosure:
Publication 892



Department of the Treasury
Internal Revenue Service
Tax Exempt and Government Entities
Exempt Organizations Examinations
1100 Commerce Street MS 4900 DAL
Dallas, TX 75242-1100

Date:
April 20, 2016
Taxpayer Identification Number:

Form:

Tax Year(s) Ended:
December 31, 20XX
December 31, 20XX
Person to Contact/ID Number:

Contact Numbers:
Telephone:
Fax:
Manager's Name/ID Number:

Manager's Contact Number:

Response due date:
May 20, 20XX

CERTIFIED MAIL - RETURN RECEIPT REQUESTED

Dear

We propose to revoke our recognition of your exempt status as an organization described in section 501(c)(3) of the Internal Revenue Code (the Code). We enclose our report of examination explaining why we are proposing this action.

If you accept our proposal, please sign and return the enclosed Form 6018, *Consent to Proposed Action - Section 7428*, unless you have already provided us a signed Form 6018. We will issue a final revocation letter determining you are not an organization described in section 501(c)(3). After the issuance of the final revocation letter we will publish an announcement that you have been deleted from the cumulative list of organizations contributions to which are deductible under section 170 of the Code. If you do not respond to this proposal, we will similarly issue a final revocation letter. Failing to respond to this proposal may adversely impact your legal standing to seek a declaratory judgment because you may be deemed to have failed to exhaust administrative remedies.

If you do not agree with our proposed revocation and wish to protest our proposed revocation to the Appeals Office of the Internal Revenue Service, then 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. This written request is called a protest. For your protest to be valid it needs to contain certain specific information which generally includes a statement of the facts, the applicable law, and arguments in support of your

position. For the specific information needed for a valid protest, please refer to page 6 of the enclosed Publication 3498, *The Examination Process*, and page 1 of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

If you do submit a valid protest, then 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 and Publication 892 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. Please note that Fast Track Mediation Services referred to in Publication 3498, generally do not apply after issuance of this letter.

You may also request that we refer this matter for Technical Advice as explained in Publication 892 and an annual revenue procedure. 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 EO Rulings and Agreements function, then no further administrative appeal will be available to you within the IRS on the matter.

If you receive a final revocation letter, you will be required to file Federal income tax returns for the tax period(s) shown above as well as for subsequent years.

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:

Internal Revenue Service
Office of the Taxpayer Advocate

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,

Paul A. Marmolejo
Acting Director, Exempt Organizations
Examinations

Enclosure:
Publication 892,
Publication 3498,
Form 6018,
Report of Examination

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 1 of 6
Name of Taxpayer		Year Ended 20XX12 & 20XX12

Issue

Should the Organization's 501(c)(3) status be revoked on the grounds that it is not operating within the scope of Internal Revenue Code Section 501(c)(3)?

Facts

Per the Organization's filed Form 990 for tax year ending December 31, 20XX, their mission is to:

“ . . . ”

Per the Organization's Articles of Incorporation, filed August 5, 19XX, their purpose is:

“ . . . ”

The President, _____, advised that the Organization is no longer affiliated with the _____ in _____.

On July 28, 19XX, the Organization's Articles of Incorporation were amended to include the following paragraph, which states, in part:

“ . . . ”

Per the President, the Organization performs: _____, _____, _____, and they perform social services for individuals and families. At the time of the tour of the facilities, they were not providing any housing. They identify individuals and families in need and they network with different organizations and businesses in the community to find the resources to meet that need. The President advised that their activities have greatly been reduced since governmental agencies now provide the majority of the services they used to offer.

During 20XX, the Organization reported that they received a total of \$XXX,XXX in Fair Market Value from a combination of donated furniture, food and toys. The President advised that the majority of these items are donated to those in need throughout the year.

On the Filed Form 990 and calendar years ending 20XX and 20XX, the Organization reported that they own properties. The Organization reported “gross rents” (Part VIII of Form 990) related to this property, totaling \$XX,XXX. For tax year 20XX, the amount reported totaled \$XX,XXX. When asked about this property and the related rental income, the President _____, advised that this property and rental income was actually _____.

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hers, and it should not have been reported on the Forms 990 because the Organization does not own the property nor do they directly receive the rental income. She advised that she reports this rental income on her personal tax return. She advised that it was a mistake to have included it on the Forms 990.

Due to this, the President advised that the Forms 990 are incorrect and that most of the income and expenses reported on the returns are actually related to her and not the Organization. Therefore, the Forms 990 filed for 20XX and 20XX and materially incorrect.

The President advised that her personal checking account is also used as the Organization's bank account. The President advised that she makes all deposits into this account, which includes the rental income, her retirement pension, which is unrelated to the Organization, and all charitable contributions the Organization receives. Since the Organization's bank account is commingled with the President's personal funds, it is impossible to discern any purported Organization expense from the President's personal expenditures. The Organization's assets, i.e. its bank account, are readily available for the President's immediate and personal use. The majority of the expenditures were personal in nature or unexplained.

An Information Document Request (IDR) dated August 21, 20XX was provided to the Organization. This IDR requested source documentation pertaining to questionable transactions identified in the checking account, such as out of state and out of country ATM withdrawals and debit card transactions at casinos. A follow up IDR was provided to the Organization on September 14, 20XX. No response was provided by the organization to either IDRs.

The President is in complete control over the Organization's financial activities. The President does not have to substantiate or provide accounting for any expenditure made from the Organization's bank account. The audit reveals that the President never relinquishes control over the funds. There is a Board of Directors listed on the filed Forms 990 but there is no indication that they act as an independent body responsible for reviewing, approving, co-signing financial transactions, or, preventing Organizational assets (bank account) from inuring to its founder. Transactions are not recorded, there is no segregation of duties, there are no outside parties overseeing the Organization, there is no annual independent audit. The President is the sole controller of the Organization.

Law

Section 501(c)(3) of the Code exempts from federal income tax organizations organized and operated exclusively for charitable, educational, and other exempt purposes; provided that no part of the organization's net earnings inures to the benefit of any private shareholder or individual.

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. 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 existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. *Better Business Bureau of Washington, D.C., Inc. v. United States*, 326 U.S. 279 (1945).

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Regulation Section 1.501(c)(3)-1(c) defines the "Operational test". Regulation Section 1501(c)(3)-1(c)(1) "Primary activities" provides, in part "An organization will be regarded as 'operated exclusively' for one or more exempt purposes only if it engages primarily in activities which accomplish one or more 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."

Regulation Section 1.501(c)(3) 1(c)(2) "Distribution of earnings" expands on the definition of an activity that is not in furtherance of an exempt purpose. It states: "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. For the definition of the words 'private shareholder or individual', see paragraph (c) of Sec. 1.501(a)-1."

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 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. Prohibited private interests include those of unrelated third parties as well as insiders. *Christian Stewardship Assistance, Inc. v. Commissioner*, 70 T.C. 1037 (1978); *American Campaign Academy v. Commissioner*, 92 T.C. 1053 (1989). Private benefits include an "advantage; profit; privilege; gain; [or] interest." *Retired Teachers Legal Fund v. Commissioner*, 78 T.C. 280, 286 (1982).

Better Business Bureau v. United States, 316 U.S. 279 (1945), holds that the existence of a single non-exempt purpose, if substantial in nature, will destroy the exemption under section 501(c)(3). An organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such purposes.

In *Basic Bible Church v. Commissioner*, 74 T.C. 846 (1980), the court found that although the organization did serve charitable purposes, it existed to serve the private benefit of its founders, and thus failed the operational test of section 501(c)(3). Control over financial affairs by the founder created an opportunity for abuse and the need to be open and candid about financial matters; the applicant failed to provide information concerning financial affairs.

Taxpayer's Position

The organization's President advised that she disagrees with certain portions of this report. She stated that she has never misused the organization's funds. She stated that she has never personally benefited from her involvement with the organization and that the organization would not have existed without her financial support. She is very proud of the work the organization has done on the behalf of the community over the roughly XX years they have been in existence. She advised that any errors they might have made by not properly abiding by the laws governing charitable organizations were done in ignorance and were not intentional.

With a letter dated April 11, 20XX, the organization's President, _____, further explained her position concerning this report. See attached, Exhibit 1. Accompanying this letter was Form 6018 signed by her, also attached.

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Government's Position

Though some exempt purpose activity has occurred, the Organization does not appear to operate exclusively exempt purposes as required by section 501(c)(3) and Section 1.501(c)(3)-1(c)(1). Similar to the Organization in *Basic Bible Church v. Commissioner*, 74 T.C. 846 (1980), the Foundation appears to exist to serve the private benefit of its founder, and thus fails the operational test of section 501(c)(3) even though it may operate for some exempt purposes. As in that case, control over financial affairs by the founders creates an opportunity for abuse. More than an insubstantial part of the President's activities appear to benefit the President rather than the general public.

Since the Organization does not operate exclusively for exempt purposes and operates to the private benefit of the President to a more than insubstantial extent, the Organization is not described by section 501(c)(3).

Conclusion

The above facts demonstrate that the Foundation is not operated exclusively for exempt purposes described within Internal Revenue Code section 501(c)(3):

- a. The Organization is not engaged primarily in activities that accomplish an exempt purpose.
- b. More than an insubstantial part of the Organization's activities are in furtherance of a non-exempt purpose.
- c. The Organization was operated for the purpose of serving a private benefit rather than public interests.

Based on our audit, and in light of the applicable law, we have determined that you are not operated for exempt purposes. Rather, you are, primarily, operated for the non-exempt purpose, operating in furtherance of private interests, of the President. Accordingly, you do not qualify for exemption as an Organization described in section 501(c)(3) of the Code and you must file federal income tax returns. Contributions to you are not deductible under section 170 of the Code.

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Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No. Page 6 of 6
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