



**DEPARTMENT OF THE TREASURY**  
INTERNAL REVENUE SERVICE  
1100 Commerce Street, MC 4920DAL  
Dallas, TX 75242

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Number: **202052026**  
Release Date: 12/24/2020

UIL: 501.03-00

**Date:** August 6, 2020

**Taxpayer ID Number:**

**Form:**

**Tax Period(s) Ending:**

**Person to Contact:**

**Identification Number:**

**Telephone Number:**

**Fax Number:**

**CERTIFIED MAIL – Return Receipt Requested**  
**LAST DAY FOR FILING A PETITION WITH THE TAX COURT:**

Dear :

This is a final determination that you do not qualify for exemption from federal income tax under Internal Revenue Code (IRC) Section 501(a) as an organization described in IRC Section 501(c)(3), effective January 1, 20XX. Your determination letter dated November 19XX is revoked.

Our adverse determination as to your exempt status was made for the following reason(s):

Organizations described in IRC Section 501(c)(3) and exempt under Section 501(a) must be both organized and operated exclusively for exempt purposes, and no part of their net earnings may inure to the benefit of private shareholders or individuals. The transfer of money to

, the sole trustee of the Foundation, constituted inurement.

As such, you failed to meet the requirements of IRC Section 501(c)(3) and Treasury Regulations Section 1.501(c)(3)-1(a), in that you have not established that you were organized and operated exclusively for exempt purposes, and that no part of your net earnings inured to the benefit of private shareholders or individuals.

Organizations that are not exempt under IRC Section 501 generally are required to file federal income tax returns and pay tax, where applicable. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

Because you were a private foundation as of the effective date of the adverse determination, you are considered to be a taxable private foundation until you terminate your private foundation status under section 507 of the Internal Revenue Code. In addition to your income tax return, you must also continue to file Form 990-PF, Return of Private Foundation or Section 4941(a)(1) Trust Treated as a Private Foundation, by the 15<sup>th</sup> day of the fifth month after the end of your annual accounting period.

Contributions to your organization are no longer deductible under IRC Section 170.

If you decide to contest this determination, you may file an action for declaratory judgment under the provisions of IRC Section 7428 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 was mailed to you. Please contact the clerk of the appropriate court for rules and the appropriate forms for filing petitions for declaratory judgment by referring to the enclosed Publication 892. You may write to the courts at the following addresses:

United States Tax Court  
400 Second Street, NW  
Washington, DC 20217

U. S. Court of Federal Claims  
717 Madison Place, NW  
Washington, DC 20439

U. S. District Court for the District of Columbia  
333 Constitution Ave., N.W.  
Washington, DC 20001

Processing of income tax returns and assessments of any taxes due will not be delayed if you file a petition for declaratory judgment under section 7428 of the Internal Revenue Code.

We'll notify the appropriate state officials (as permitted by law) of our determination that you aren't an organization described in IRC Section 501(c)(3).

You may be eligible for help from the Taxpayer Advocate Service (TAS). 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 [www.taxpayeradvocate.irs.gov](http://www.taxpayeradvocate.irs.gov) or call 1-877-777-4778.

Taxpayer Advocate assistance can't be used as substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determination, nor extend the time fixed by law that you have to file a petition in 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.

Organizations that are not exempt under IRC Section 501 generally are required to file federal income tax returns and pay tax, where applicable. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

You can get any of the forms or publications mentioned in this letter by calling 800-TAX-FORM (800-829-3676) or visiting our website at [www.irs.gov/forms-pubs](http://www.irs.gov/forms-pubs).

If you have questions you can contact the person listed at the top of this letter.

Sincerely,



Sean E. O'Reilly  
Director, EO Examinations

Enclosures:  
Publication 892



Department of the Treasury  
Internal Revenue Service  
Tax Exempt and Government Entities

Date:  
March 25, 2020  
Taxpayer ID number:

Form:

Tax periods ended:

Person to contact:

ID number:  
Telephone:  
Fax:  
Address:

Manager's contact information:

Name:  
ID number:  
Telephone:  
Response due date:

**CERTIFIED MAIL - Return Receipt Requested**

Dear :

**Why you're receiving this letter**

We enclosed a copy of our audit report, Form 886-A, Explanation of Items, explaining that we propose to revoke your tax-exempt status as an organization described in Internal Revenue Code (IRC) Section 501(c)(3).

**If you agree**

If you haven't already, please sign the enclosed Form 6018, Consent to Proposed Action, and return it to the contact person shown at the top of this letter. We'll issue a final adverse letter determining that you aren't an organization described in IRC Section 501(c)(3) for the periods above.

After we issue the final adverse determination letter, we'll announce that your organization is no longer eligible to receive tax deductible contributions under IRC Section 170.

**If you disagree**

1. Request a meeting or telephone conference with the manager shown at the top of this letter.
2. Send any information you want us to consider.
3. File a protest with the IRS Appeals Office. If you request a meeting with the manager or send additional information as stated in 1 and 2, above, you'll still be able to file a protest with IRS Appeals Office after the meeting or after we consider the information.

The IRS Appeals Office is independent of the Exempt Organizations division and resolves most disputes informally. If you file a protest, the auditing agent may ask you to sign a consent to extend the period of limitations for assessing tax. This is to allow the

IRS Appeals Office enough time to consider your case. For your protest to be valid, it must contain certain specific information, including a statement of the facts, applicable law, and arguments in support of your position. For specific information needed for a valid protest, refer to Publication 892, How to Appeal an IRS Determination on Tax-Exempt Status.

Fast Track Mediation (FTM) referred to in Publication 3498, The Examination Process, generally doesn't apply now that we've issued this letter.

4. Request technical advice from the Office of Associate Chief Counsel (Tax Exempt Government Entities) if you feel the issue hasn't been addressed in published precedent or has been treated inconsistently by the IRS.

If you're considering requesting technical advice, contact the person shown at the top of this letter. If you disagree with the technical advice decision, you will be able to appeal to the IRS Appeals Office, as explained above. A decision made in a technical advice memorandum, however, generally is final and binding on Appeals.

**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 adverse determination letter.

**Contacting the Taxpayer Advocate Office is a taxpayer right**

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 [www.taxpayeradvocate.irs.gov](http://www.taxpayeradvocate.irs.gov) or call 877-777-4778.

**For additional information**

You can get any of the forms and publications mentioned in this letter by visiting our website at [www.irs.gov/forms-pubs](http://www.irs.gov/forms-pubs) or by calling 800-TAX-FORM (800-829-3676).

If you have questions, you can contact the person shown at the top of this letter.

Sincerely,

Christopher M. Holmes

Digitally signed by Christopher M. Holmes  
Date: 2020.03.25 10:35:40 -07'00'

for Maria Hooke  
Director, EO Examinations

Enclosures:  
Form 886-A  
Form 6018

|                                 |   |                                  |
|---------------------------------|---|----------------------------------|
| Form <b>886-A</b><br>(May 2017) | Department of the Treasury – Internal Revenue Service<br><b>Explanations of Items</b> | Schedule number<br>or exhibit    |
| Name of taxpayer                | Tax Identification Number ( <i>last 4 digits</i> )                                    | Year/Period ended<br>20XX – 20XX |

**ISSUE**

Whether the transfer of money from \_\_\_\_\_ (“Foundation”) to \_\_\_\_\_, the sole trustee of the Foundation, constituted inurement. As such, revocation of the Foundation’s exempt status is warranted.

**FACTS**

**Foundation’s Background, Activities and Financial Information**

The Foundation is a trust created by the Last Will and Testament (Will) dated January 21, 19XX, of \_\_\_\_\_. See section 8(c) of the Will. The Foundation’s purposes are supporting the arts and providing scholarship to creative and original musicians, composers and lyricists. Following the death of \_\_\_\_\_, the Foundation was formed on March 22, 19XX. In May 19XX, the Foundation applied and was recognized as a private non-operating foundation under Internal Revenue Code (IRC) Section 501(c)(3) and 509(a) in November 19XX. The Foundation is operated on a calendar year basis. The Foundation has made no distributions since \_\_\_\_\_. Per \_\_\_\_\_, the Foundation had few activities in the last few years. \_\_\_\_\_ was looking into fundraising programs and building a web site to promote the Foundation’s profile. Due to the high cost, \_\_\_\_\_ did not go through with the plan.

The Foundation reports the following financial information on its Form 990-PF.

| Income                | 20XX        | 20XX        | 20XX        |
|-----------------------|-------------|-------------|-------------|
| Royalty income        | 0           | 0           | 0           |
| <b>Expense</b>        |             |             |             |
| Trustee fee ( _____ ) | 0           | 0           | 0           |
| Accounting            | 0           | 0           | 0           |
| Professional fee      | 0           | -           | -           |
| Tax                   | 0           | 0           | 0           |
| Storage               | 0           | 0           | 0           |
| Office supplies       | 0           | 0           | 0           |
| Website hosting       | -           | 0           | 0           |
| Internet & phone      | -           | -           | 0           |
| Total expense         | 0           | 0           | 0           |
| <b>Net income</b>     | <b>0</b>    | <b>0</b>    | <b>0</b>    |
| <br>                  |             |             |             |
| <b>Assets</b>         | <b>20XX</b> | <b>20XX</b> | <b>20XX</b> |
| Cash                  | 0           | 0           | 0           |
| Loan to               | 0           | 0           | 0           |
| Total                 | 0           | 0           | 0           |

|                                 |   |                                      |
|---------------------------------|---|--------------------------------------|
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| Name of taxpayer                | Tax Identification Number (last 4<br>digits)  | Year/Period ended<br><br>20XX – 20XX |

In the years under audit, the Foundation did not have separate accounting records. The Foundation maintains a bank account at . The Foundation relied on receipts and disbursements reported on its annual statement to prepare the Form 990-PF. The annual statement reveals the following transfers to and from the bank account.

| Date       | Description                   | Amount     |
|------------|-------------------------------|------------|
| 2/3/XX     | Online transfer to checking   | (0)        |
| 4/27/XX    | Online transfer to checking   | (0)        |
| 7/27/XX    | Online transfer to checking   | (0)        |
| 8/9/XX     | Online transfer to checking   | (0)        |
| 9/6/XX     | Online transfer to checking   | (0)        |
| 9/12/XX    | Online transfer to checking   | (0)        |
| 9/12/XX    | Online transfer to checking   | (0)        |
| 10/6/XX    | Online transfer to checking   | (0)        |
| 10/11/XX   | Online transfer to checking   | (0)        |
|            |                               | (0)        |
| 7/27/XX    | Online transfer from checking | 0          |
| 8/11/XX    | Online transfer from checking | 0          |
| 9/15/XX    | Online transfer from checking | 0          |
| 10/17/XX   | Online transfer from checking | 0          |
|            |                               | 0          |
| Net amount |                               | <u>(0)</u> |

then treated \$0 of the \$0 as his salary. The remaining \$0 was for reimbursement of expenses. The Foundation did not furnish or file a Form W-2 or 1099-MISC to report the salary.

#### About

In his Will, named , his friend, as the sole trustee of the Foundation. has been the sole trustee of the Foundation since inception.

Article 8, Section (c)(8), of the Will provides, *"I authorize and empower , by instrument in writing duly acknowledged, or by will duly admitted to probate, to appoint any citizen of the United States or any corporation having fiduciary powers to be successor to him as Trustee of the Foundation, and to revoke any such appointment prior to the time such successor has undertaken his duties and to appoint a different successor."*

Although his wife is not a trustee, she also has access to the Foundation's bank account. states that she is the one paying the bills and transferring money to the ' bank account.

Transfers of Money from the Foundation to

|                                 |   |                                  |
|---------------------------------|---|----------------------------------|
| Form <b>886-A</b><br>(May 2017) | Department of the Treasury – Internal Revenue Service<br><b>Explanations of Items</b> | Schedule number<br>or exhibit    |
| Name of taxpayer                | Tax Identification Number (last 4<br>digits)  | Year/Period ended<br>20XX – 20XX |

During the meeting on February 4, 20XX, stated that in 20XX, they experienced financial hardship. began drawing fund from the Foundation for salary. Per , the Foundation's outside accountant later advised to treat the amounts withdrew in excess of trustee salary as loan. recalls hearing the accountant verbally advising that he could draw amounts equaled to 0 to 0 percent of the Foundation assets for salary. The salary could increase if the Foundation generates more revenue.

In the fax transmittal dated March 12, 20XX, recanted the disclosure above and stated that business manager advised that could borrow from the Foundation. The amounts withdrawn were documented as a loan not as salary by and then given to for official accounting by . did not provide written records to support the above disclosure. passed away in 20XX.

The examining agent requested a written loan agreement in Information Document Request #1 and #2. During the meeting on February 4, 20XX, stated that there was no written loan agreement and unable to provide the agreement. In the fax transmittal dated March 12, 20XX, recanted the above statement and stated that cannot confirm whether there was a written loan agreement.

put up no collaterals for the loan. confirmed neither the Foundation nor established a fixed schedule of repayments. Since 20XX, neither accrued nor paid interest on the loans. stated that made repayments when financially able. The Form 990-PF shows the following year-end loan balances.

| End of year balance |      |                    |      |                    |      |                    |     |
|---------------------|------|--------------------|------|--------------------|------|--------------------|-----|
| 20XX                | 20XX | Increase from 20XX | 20XX | Decrease from 20XX | 20XX | Decrease from 20XX | 20X |
| 0                   | 0    | 0                  | 0    | (0)                | 0    | (0)                | 0   |

| End of year balance |                    |      |                    |      |                    |      |      |
|---------------------|--------------------|------|--------------------|------|--------------------|------|------|
| 20XX                | Increase from 20XX | 20XX | Increase from 20XX | 20XX | Decrease from 20XX | 20XX | 20XX |
| 0                   | 0                  | 0    | 0                  | 0    | (0)                | 0    | 0    |

Separately, provided a schedule showing loan balance dating back to 20XX. The schedule is reproduced below.

20XX Beginning balance: \$0  
20XX Loan to date: \$0



|                                 |   |                                  |
|---------------------------------|---|----------------------------------|
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| Name of taxpayer                | Tax Identification Number (last 4<br>digits)  | Year/Period ended<br>20XX – 20XX |

| Repayments and additions |                                    | Year-end balance |
|--------------------------|------------------------------------|------------------|
| 20XX                     | \$0 repayment                      | 0                |
| 20XX                     | \$0 trustee salary applied to loan | 0                |
| 20XX                     | No repayment                       | 0                |
| 20XX                     | \$0 additional loan taken          | 0                |
| 20XX                     | \$0 additional loan taken          | 0                |
| 20XX                     | \$0 trustee salary applied to loan | 0                |
| 20XX                     | No repayment                       | 0                |
| 20XX                     | No repayment                       | 0                |
| 20XX                     | \$0 trustee salary applied to loan | 0                |

Below were additional money transferred from the Foundation to \_\_\_\_\_ in 20XX and 20XX.

| Date     | Amount |
|----------|--------|
| 10/20/XX | 0      |
| 12/18/XX | 0      |
|          | 0      |

| Date    | Amount | Date     | Amount |
|---------|--------|----------|--------|
| 1/6/XX  | 0      | 7/21/XX  | 0      |
| 1/16/XX | 0      | 8/3/XX   | 0      |
| 3/10/XX | 0      | 8/17/XX  | 0      |
| 3/13/XX | 0      | 8/28/XX  | 0      |
| 5/5/XX  | 0      | 9/1/XX   | 0      |
| 5/27/XX | 0      | 12/1/XX  | 0      |
| 6/5/XX  | 0      | 12/31/XX | 0      |
| 6/18/XX | 0      |          |        |
|         | 0      |          | 0      |
|         |        |          | 0      |

**LAW**

IRC Section 501(c)(3) provides for exemption from Income Tax for corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which

|                                 |   |                                      |
|---------------------------------|---|--------------------------------------|
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| Name of taxpayer                | Tax Identification Number ( <i>last 4 digits</i> )                                    | Year/Period ended<br><br>20XX – 20XX |

does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Treasury Regulations (Regs.) Section 1.501(c)(3)-1(a)(1) provides 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.

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

Regs. Section 1.501(a)-1(c) defines the words private shareholder or individual in section 501 as persons having a personal and private interest in the activities of the organization.

The courts have broadly construed the term net earnings to include more than gross receipts minus disbursements as shown on the organization's books and records.

Founding Church of Scientology v. U.S., 412 F.2d 1197 (Ct. Cl. 1969), involved a classic across-the-board channeling of an organization's funds to those in control of the organization. In that case, a wide variety of devices were employed, including fees, commissions, excessive rental payments, loans and excessive salaries, to divert the organization's funds to its founder, L. Ron Hubbard, and his immediate family. The principle of inurement was neatly summarized when the Court stated, "what emerges from these facts is the inference that the Hubbard family was entitled to make ready personal use of the corporate earnings."

In John Marshall Law School v. U.S., 228 Ct. Cl. 902 (1981), the Court ruled that interest-free and unsecured loans to insiders constituted inurement. The Court detailed with particularity each of a series of interest-free and unsecured loans used by the Fensters to purchase a home and furnish it. Although one of the loans was evidenced by a promissory note, the note made no provision for a definite repayment schedule.

#### TAXPAYER'S POSITION

The Foundation's position is not known.

#### GOVERNMENT'S POSITION

Regs. Section 1.501(c)(3)-1(a)(1) provides that an organization must be both organized and operated exclusively for one or more of the purposes. If an organization fails to meet either the organizational test or the operational test, it is not exempt. 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. Regs. Section 1.501(c)(3)-1(c)(2). See also Founding Church of Scientology v. U.S. and John Marshall Law School v. U.S.

|                                 |   |                                      |
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| Name of taxpayer                | Tax Identification Number ( <i>last 4 digits</i> )                                    | Year/Period ended<br><br>20XX – 20XX |

The facts of this case are similar to those of *Founding Church of Scientology v. U.S.* In *Founding Church of Scientology v. U.S.*, the Court noted, "what emerges from these facts is the inference that the Hubbard family was entitled to make ready personal use of the corporate earnings." The Court ruled that the use of the corporate earnings constituted inurement.

In this case, the \_\_\_\_\_ readily and conveniently used the Foundation's bank account as if it was theirs. They withdraw money from the Foundation's bank account as needed. While the \_\_\_\_\_ repaid some of the money, the unpaid amount remain substantial. As of the end of 20XX, the unpaid amount totaled \$0. The forms, amounts, and infrequency of repayments raise doubt whether \_\_\_\_\_ is able to make future repayments.

The \_\_\_\_\_ personal uses of the Foundation's money derived the Foundation of the ability to generate income on the money. The Foundation could have invested the \$ \_\_\_\_\_ in certificate of deposit (CD) to generate interest income. The Foundation was not able to do that because it no longer has that \$ \_\_\_\_\_. All the while, the \_\_\_\_\_ paid zero interest to the Foundation for using the \$ \_\_\_\_\_.

The facts of this case are also similar to those of *John Marshall Law School v. U.S.* The Court detailed with particularity each of a series of interest-free and unsecured loans used by the Fensters to purchase a home and furnish it. The Court ruled the interest-free and unsecured loans to the Fensters constituted inurement.

In this case, the \_\_\_\_\_ treated the money they withdrew from the Foundation as loans. Yet, they accrued and paid zero interest on the loans since \_\_\_\_\_. They also put up no collaterals to secure the loans. The Foundation has little recourses in the event the \_\_\_\_\_ decided not to repay the loans.

### CONCLUSION

Based on the above facts, it is concluded that the Foundation' net earnings have inured to the benefits of its insiders, the \_\_\_\_\_. The Foundation's tax-exempt status should be revoked. Since the Foundation is a trust, it is required to file a Form 1041, *Income Tax Return of Estates and Trusts*, for all future years. In addition to the Form 1041, the Foundation is required to file the Form 990-PF as a taxable private foundation for all future years.