

EIN:

REDACTION LEGEND

Final Revocation Letter

A = Name of Organization
B = Address of Organization
NUM = Employer ID Number
Date 1 = Last Day for Filing a Petition w/Tax Court
Date 2 = Effective Date
Date 3 = Tax Year ended
TPA-A = Taxpayer Advocate – Location
TPA-B = Taxpayer Advocate - Address

Ltr 3618 – 30 Day Letter

A = Name of Organization
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NUM = Employer ID Number
Date 1 = Tax Year ended
TPA-A = Taxpayer Advocate – Location
TPA-B = Taxpayer Advocate – Address

Revenue Agent's Report – Explanation of Items.

A = Name of Organization
B = Address of Organization
C = Address of Related Entity
NUM = Employer ID Number
Date 1 = Tax Year ended
Date 2 = Date of Incorporation
Reg. A = Registered Agent
Dr 1 = Director 1
Dr 2 = Director 2
Dr 3 = Director 3
X = Name of State
Dr1A = Director 1 Address
Dr2A = Director 2 Address
Dr3A = Director 3 Address
Sec = Secretary
Sec A = Secretary's Address.
ED = Executive Director
ED = Executive Director's Address
Date 3 = Exemption Ltr. Mailed
Date 4 = Beginning of Advance Ruling Period
Date 5 = End of Advance Ruling Period
IRS = Name of Revenue Agent
Web A = Organization's Website
Web B = Related Entity's Website

EIN:
REDACTION LEGEND

Revenue Agent's Report – Explanation of Items.

Rel = Related Entity
Grants = Grants and Allocations
Date 6 = Date of Incorporation of Related Entity
Date 7 = Effective Date of Revocation.
Date 8 = Date of Exemption Letter



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

1100 Commerce Street, MS 4920-DAL

Dallas, Texas 75242

Number: 200736034

May 15, 2007

Release Date: 9/7/2007

UIL: 501.03-01

A
Attn: A
B
B

Person to Contact: Employee
Identification Number: XX-XXXXXXX
Contact Telephone Number: (xxx)xxx-xxxx
In Reply Refer to: TE/GE Review Staff
EIN: N

**LAST DATE FOR FILING A PETITION
WITH THE TAX COURT: Date 1**

Dear :

This is a Final Adverse Determination Letter as to the **A, Inc.** exempt status under section 501(c) (3) of the Internal Revenue Code.

Our adverse determination was made for the following reasons:

A, Inc. has not been operating exclusively for exempt purposes within the meaning of Internal Revenue Code section 501(c) (3). **A, Inc.** also is not a charitable organization within the meaning of Treasury Regulations section 1.501(c) (3)-1(d). You are not an organization which operates exclusively for one or more of the exempt purposes which would qualify it as an exempt organization. You operate substantially for a non-exempt purpose, for private benefit, and your earnings inure to the benefit of a related for profit entity..

Based upon these reasons, we are retroactively revoking your IRC section 501(c) (3) tax exempt status to **Date 2**

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

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending **Date 3** and for all years thereafter.

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

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

You also have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers.

You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling (xxx) xxx-xxxx, or writing to: Internal Revenue Service, Taxpayer Advocates Office, TPA -A, TPA-B .

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

We will notify the appropriate State Officials of this action, as required by section 6104(c) of the Internal Revenue Code.

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

Sincerely yours,

Marsha Ramirez



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
300 N. Los Angeles Street, MS 7300
Los Angeles, CA 90012

November 15, 2006

Taxpayer Identification Number:
Num.
Form:

Tax Year(s) Ended:
Date 1
Person to Contact/ID Number:
Employee
Contact Numbers:
Telephone: (xxx) xxx-xxxx
Fax: (xxx) xxx-xxxx

A
B
B

Certified Mail - Return Receipt Requested

Dear :

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

Letter 3618 (04-2002)
Catalog Number 34809F

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

TPA - A

TPA - B

Telephone: (xxx) xxx-xxxx

Fax: (xxx) xxx-xxxx

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO E xaminations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer	Tax Identification Number	Year/Period ended
A, Inc.	NUM	Date 1

ISSUE

Whether **A, Inc.** operated exclusively for exempt purposes within meaning of Internal Revenue Code § 501(c) (3) and the Regulations thereunder?

FACTS

Organizational Information:

A, Inc. was incorporated as an **X** not-for-profit corporation on **Date 2**. **Reg Agent** was the registered agent and signed the Articles of Incorporation as the Sole Incorporator. The three directors listed in the articles were Dr 1, Dr 2 and Dr 3.

On December 12, 2002 applied for recognition as a tax-exempt organization under Internal Revenue Code (IRC or the Code) § 501(c) (3) on Form 1023, *Application for Recognition of Exemption Under Section 501(c) (3) of the Internal Revenue Code*. **Reg Agent** signed the Form 1023 under the penalties of perjury and described **A, Inc.** purposes as follows:

A, Inc. has not been actively operated since its date of incorporation. One of the two activities that **A, Inc.** intends to conduct is to assist youth organizations that reach out to young people through outdoor activities, including those organizations that reach out to handicapped and troubled youth. First Equity will assist such organizations by providing time, fundraising and coordination of events and financial support.

...

The activity will be conducted by the directors and officers of **A, Inc.** **A, Inc.** will devote approximately 70% of its time and other resources to this activity.

In addition, First Equity will try to influence local media outlets to avoid placing programming on the public airwaves that is not appropriate for family viewing, and to seek programming that is positive and educational. **A, Inc.** will devote approximately 20% of its time to this activity.

A, Inc. will also provide free legal advice and services to youth and non-profit organizations on an ad hoc basis. This service will be provided by **Reg. Agent** who is member of good standing of the **X** State Bar. **A, Inc.** will devote approximately 10% of its time to this activity.

Regarding its sources of financial support, **Reg. Agent** stated as follows:

Funding will come from general and targeted solicitations for gifts through fundraising solicitations, mailings, etc. It is estimated that approximately 50% of funds will come from corporations and 50% of funds will come from the general public.

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer A, Inc.	Tax Identification Number NUM	Year/Period ended Date 1

Regarding its fundraising program, **Reg Agent** stated as follows:

Fundraising efforts will occur primarily through local community events and through electronic solicitations via website and email.

The following individuals were listed as the governing body of **A, Inc**:

<u>Name</u>	<u>Address</u>	<u>Title</u>
Dr 1	Dr1A	Director
Dr 2	Dr2A	Director
Sec	Sec A	Secretary
ED	ED A	Executive Director

(Emphasis added)

The list above indicated **Sec** shared the address with **ED** and according to the Service's records they filed joint tax returns for years and .

On April 8, 2003, in response to the Determination Agent's inquiry, **ED** expanded the description of **A, Inc.** purposes and activities as follows:

Activity I [in regards to assisting youth organization]

One of the primary goals of the Company is to provide a medium through which like-minded individuals and groups can participate to take advantage of synergies that exist among them. Another goal is to raise the level of interest and awareness of groups in our community that serve important needs... The Company will devote approximately 40% of its time and other resources to this activity...

Activity II [in regards to influencing local media]

The purpose and function of this activity is to promote programming that is educational and appropriate and does not expose children and youth to destructive and inappropriate violence, sex, profanity etc. ... The Company will devote approximately 50% of its time to this activity...

Activity III [in regards to providing free legal advices]

This service will be provided by **ED** who is [a] member of good standing of the **X** State Bar. **ED** is consistently approached about legal questions that organizations are facing. Any legal advice that he dispenses will be under the auspices of the Company in order to provide limited liability for such activities. Such legal advice will be limited to the areas of expertise and knowledge that **ED** possesses and there will be no fees or requirements imposed to limit to whom such assistance will be given. This service will be limited based on the time and resources of **ED**. The Company will devote approximately 10% of its time to this activity.

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer	Tax Identification Number	Year/Period ended
A, Inc.	NUM	Date 1

A determination letter was issued on **Date 3** granting exemption status under Code §501(c) (3) as an organization that is not a private foundation because it is described under Code §509(a) (1) and 170(b) (1) (A) (vi), with an advanced ruling period from **Date 4 to Date 5**.

Proposed change in activities:

On July 24, 2003, **70 days after** the issuance of the determination letter, **A, Inc.** faxed a letter to the Customer Service of IRS regarding its change in activities. **Reg. Agent** signed the letter and stated following:

We called your Customer Service department and were informed that we should notify you via facsimile to _____ of new activities we engage in.

We will have a new website focusing on the family. The website provides content and links designed to provide educational material, suggestions and resources for families to help them with common problems such as troubled children and finances as well as helping families avoid these troubles.

The emphasis is on helping families to be more successful. Part of this is helping families find a place that in conduc[t]ive to their success-such as moving families from apartments to homes. As part of this we will also seek to assist families with financing by helping with down payments.

The Customer Service Specialist responded by asking **A, Inc.** to request a private letter ruling from the National Office of the IRS. Instead of submitting the approval for changes in the operation to the National Office, **A, Inc.** re-submitted a similar letter to the Customer Service on August 18, 2003. The Customer Service Department again directed **A, Inc.** to the National Office. **A, Inc.** never submitted the request to the National Office.

Operational Information:

In response to the Service's current inquiry about its activities, **Reg Agent** stated the following:

“A buyer who qualifies for a loan that will allow down payment assistance, typically a Federal Housing Authority (FHA) loan, may apply to **A, Inc.** for down payment assistance. **A, Inc.** wires the down payment for the borrower to the title company prior to closing. The seller is asked to contribute to our program the amount of the down payment that we provide to the buyer, plus our fee.

The source of gross receipts reported on our Form 990 is the contributions made by sellers to our program.”

The 3 activities described during the application for exemption process were not mentioned during the current examination of the organization.

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
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IRS Agent analyzed the Forms 990 for fiscal years ended **Date 1** and **Date 6**. A side-by-side comparison of the financial information is displayed in the table below:

	Date 1	Date 5
Revenue		
Homebuyer Participation	\$ x,xxx.xxx	\$ x,xxx,xxx
Total revenue	\$ x,xxx,xxx	\$ x,xxx,xxx
Expenses		
Grants and allocations	(\$ xx,xxx)	(\$ x,xxx)
Down Payment Assistance for Home Buyers	(\$ x,xxx.xx)	(\$ x,xxx,xxx)
Accounting fees		(\$ xxx)
Postage and shipping		(\$ x,xxx)
Marketing fees	(\$ xxx,xxx)	(\$ xxx,xxx)
Wire fees	(\$ xx,xxx)	(\$ xx,xxx)
Total expenses	(\$ x,xxx,xxx)	(\$ x,xxx,xxx)
Net Income	\$ xx,xxx	\$ xxx,xxx

	Date 1	Percentage	Date 6	Percentage
Revenue - Homebuyer Participation	x,xxx,xxx	100%	x,xxx,xxx	100%
Grants and allocations	x,xxx	0.37%	X,xxx	0.12%
Down Payment Assistance for Home Buyers	X,xxx,xxx	94.50%	X,xxx,xxx	94.06%
Accounting fees	0	0%	xxx	0.01%
Postage and shipping	0	0%	X,xxx	0.02%
Marketing fees	Xxx,xxx	4.70%	Xxx,xxx	5.59%
Wire fees	Xx,xxx	0.43%	Xx,xxx	0.20%
Total expenses	X,xxx,xxx	100.00%	X,xxx,xxx	100.00%
Net Income	Xx,xxx		Xxx,xxx	

In addition, in regards to its statement of program service accomplishments, **A, Inc.** stated the following in its Form 990 for the year ending **Date 1**:

"To provide financial aid to qualified home buyers.

a. **A, Inc.** provided financial assistance to low income home buyers. Approximately 700 families and individuals were assisted. The program service expenses were \$2,970,235.

b. **A, Inc.** began developing a website for parental guidance regarding media consumption by juveniles. The program service expenses were \$1,000."

IRS Agent also observed that **A, Inc.** did not have any other activities other than down

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
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A, Inc.	NUM	Date 1

payment assistance (DPA), no paid employees, no office or rental expenses, etc. This indicates that **A, Inc.** did not handle the operation. This setup will be addressed under the related party section below.

IRS Agent visited **A, Inc.** website (**web address**) which promotes its DPA program to builders, lenders, realtors, buyers, and sellers. The website explains the procedures of down payment assistance program as follows.

1. A Real Estate Purchase Contract is executed by buyer and seller. Language similar to the following should be inserted into the purchase contract: "*Seller agrees to contribute \$----- to **A, Inc. (Rel)** upon closing*" (the amount indicated should be equal to the grant plus the processing fee).
2. The loan officer submits a Grant Application to **A, Inc.**.
3. We will contact the escrow company indicated on the Grant Application 2-3 days prior to closing and provide them with simple, one-page closing instructions. These instructions must be signed and returned to us before funds can be wired.
4. Prior to closing, we will wire the requested funds to the closing agent, ensuring the money is there before funding.
5. When the transaction closes, the closing agent wire us the gift amount plus our processing fee from the seller's proceeds as instructed.

Through **A, Inc.** DPA program, buyers receive a "gift" of the funds that they use for the down payment. A house buyer was eligible to participate in **A, Inc.** DPA program when they qualify for financing from a lender. According to **A, Inc.** financial records, **A, Inc.** provided down payment assistance to 686 buyers in 2003. **A, Inc.** charged for processing fees from the sellers up to \$xxx per transaction.

According to the procedures listed above, we understood that

A, Inc. would advance the funds to the buyer for the down payment. Upon closing of the escrow, the seller would pay **A, Inc.** the advanced funds plus the processing fees. The gift funds to the buyer might not have been directly paid by the seller, but indirectly the funds came from the sellers. In essence, these transactions result in a circular flow of the money with **A, Inc.** as the intermediary.

A, Inc. does not have any income limitations for its DPA program and did not screen applicants for down payment assistance based on income. **A, Inc.** explains how a buyer qualifies for its down payment assistance program in its promotional materials as, "Our program does not impose any credit or other restrictions on a buyer in order for them to receive down payment assistance. A buyer is automatically qualified for a gift from **A, Inc.** if they are eligible for a qualifying loan." On its website for lenders, **A, Inc.** stated the buyer qualifications as, "Homebuyers

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer A, Inc.	Tax Identification Number NUM	Year/Period ended Date 1

must qualify for a loan which allows gift money for the down payment and purchase a home in which the seller agrees to participate. **A, Inc.** has no income or asset restrictions for the homebuyer. Homebuyers do not need to be first-time homebuyers.”

The parties to the down payment assisted real estate transactions, including the sellers, lenders, realtors and builders, benefited from **A, Inc.** DPA. The references below, from **A, Inc.** website, demonstrate these benefits.

Sellers **A, Inc.** promotes its down payment assistance program to sellers as follows:

Down payment assistance has become a key tool for sellers who wish to qualify the highest number of buyers possible to purchase their home. By increasing the pool of buyers who are able to purchase their home by as much as 30%, sellers benefit from down payment assistance programs by selling their home up to 25% faster and possibly at a higher return to them than they otherwise could. Less time on the market can mean substantial savings in interest and other expenses. In addition, sellers will often net an amount comparable to a typical transaction – or even higher – because they will likely not have to reduce their price several times in order to sell their home.

Lenders **A, Inc.** promotes itself as a qualified grantor to conduct down payment assistance program as follows:

The grantor qualifies as a public charity and satisfies the requirements of the current guidelines found in HUD Handbook 4155. 1 Rev 4, Section 2-10, for FHA insured loans. This means we can provide grants for homebuyers who qualify for FHA loans.

Realtors **A, Inc.** promotes its down payment assistance program to realtors as follows:

Down payment assistance is a powerful tool for the real estate industry. We work with the best lenders in the business and can help you to close more sales by increasing the number of potential buyers for any seller willing to participate in our program. By offering grant funds on the homes you are listing, you get yourself apart from your competition and provide a valuable service to you clients.

Builders **A, Inc.** promotes its down payment assistance program to builders as following:

Let us help you close more deals with our down payment assistance programs. New home buyers are often looking for a way to get into a home with little money for down payment or closing costs. They may ask you for work they can do on their home to obtain “sweat equity” to meet their needs. **A, Inc.** provides gifted money for buyers to use toward down payment and/or closing costs. As you make potential customers aware of this service you will be increasing your pool of buyers and get great referrals.

Other Activities: **A, Inc.** website provides the following information to help with some common family problems:

1. Family: helping families understand the importance of homeownership in relation to child

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Name of Organization/Taxpayer A, Inc.	Tax Identification Number NUM	Year/Period ended Date 1

development. Education and finances.

2. Media: **A, Inc.** promotes sensible media for the improvement of children and family.

3. Youth: important information related to youth and teens. Internet Safety, Youth Group.

Under each section, there is a link for more information.

The additional information under the section of Family explained that the advantages to have a homeownership through child development and financial aspects.

The additional information under the section of Media explained how our children are affected by the media and why our parents can help our children avoid the effect from the inappropriate media.

The additional information under the section of Youth provides resources to help parents or guardians to deal with internet safety issues faced to their children.

A review of its financial records and the correspondence received from **A, Inc.** does not indicate the organization conducted the family related activities besides merely posting the information on its website. All its financial activities are the DPA besides the following cash grants. The cash grants and allocations reported on the Form 990 were the payments to the following:

- Grant \$
- Grant \$
- Grant \$
- Gtant \$

Minutes

A, Inc. provided a Summary of Minutes from February 2003 till to April 2004. The summary of minutes stated as follows:

2003

February: There was a discussion regarding the Company's application for non-profit status with the IRS. There is significant mutual interest in youth groups among the board of directors.

March: Discussed what would be done with **A, Inc.**.

June: There was discussion regarding down payment assistance. An explanation was made as to the nature of down payment assistance. Mention was made of the fact that many other charities are participating in down payment assistance.

July: Discuss Credit Agreement and Independent Contractor Agreement with **Rel. Housing**. There was discussion as to the use of **Rel, LLC** to market the down payment assistance and manage and perform the processing, and the fee paid to **Rel. Housing** and the duties of **Rel. Housing**. There was discussion regarding the line of credit from **Rel. Housing** to **A, Inc.** to be used to provide down payment assistance.

2004

February: Discussed officer positions and duties. Updates on business and progress of the Company.

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer A, Inc.	Tax Identification Number NUM	Year/Period ended Date 1

April: Updated on business and progress of the Company.

Related party: Housing, LLC

Rel. Housing, LLC was an independent contractor of **A, Inc.** to provide marketing services to **A, Inc.** in 2003 and after. **A, Inc.** stated the related party transaction at Statement number 4 of the Form 990 return.

Schedule A, Part III, Line 2 – Transactions with Trustees, Directors, Etc.: were fees paid to a related for-profit corporation, **Rel. Housing, Inc.**, in which an **A, Inc.** officer/director is an owner. The marketing firm's responsibility is to spread the name of **A, Inc.** with real estate agents, escrow officers and potential buyers throughout the country. In addition, it provides web site services and database management.

The summary of research of the corporate records indicates the following:

Company Name	A, Inc..	Rel. Housing, LLC
Mailing Address	B	C
Incorporated Date	Date 2	Date 6
Business Type	Corporation	LLC
Registered Agent	Reg. Agent	Reg. Agent

A, Inc. and **Rel.** signed an Independent Contractor's Agreement (Agreement) dated as of July 5, 2003. **A, Inc.** provided a copy of the contract, but did not attach the Schedule A which stated the services **Rel. Housing, LLC** agreed to perform and the terms and conditions. Even though the Schedule A is not provided, the facts indicated most, if not all, matters related to DPA were handled by **Rel.** The Agreement states **A, Inc.** I "shall pay to Contractor [**Rel.**] \$xxx for each grant opportunity brought to Company [**A, Inc.**] by Contractor, except that in no case shall Company be obligated to pay Contractor any amount in excess of the amount actually collected by Company in total in excess of the amount sent granted by company in total."

Rel's website (**Web 2**) promotes down payment assistance program, which is similar with the material at **A, Inc.** website. At this website, **Rel** states that it works with **A Inc.**, a qualified 501(c)(3) organization. The grant application on its website states that the seller service fee is \$xxx for new or resold homes, regardless of the grant amount. For sub prime or conventional, the fee is \$xxx for the first \$xx,xxx of grant amount, an additional \$xxx for the next \$xx,xxx of grant amount, and \$xxx for each \$xx,xxx of grant amount after that.

For the fiscal year end June 30, 2004, **A, Inc.** received a \$xxx,xxx service fees from sellers and paid **Rel. Housing** \$xxx,xxx for marketing fees, which was 68% of the service fees **A, Inc.** received.

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The above facts indicate that **Reg. Agent** incorporated **Rel.** about nine months before he incorporated **A, Inc.** July 2003, two months after **A, Inc.** was granted its exemption status, **Rel.** signed the DPA service contract with **A, Inc.** It was also the time **Reg Agent** notified the Service for the changes of **A, Inc.** activities. Based on **Rel.** website, **Rel.** primary activity is to conduct DPA through **A, Inc.**, there were no other apparent activities. It is apparent that **Reg. Agent** appeared to have knowledge of the DPA operation during **A, Inc.** application process. According to Mr. and Mrs. **Reg Agent** individual tax returns filed for and , they received k-1 income from **Rel.** Housing LLC.

APPLICABLE LEGAL PRINCIPLES

Section 501(c)(3) of the Code provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided that no part of the net earnings of such corporations inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in the Code § 501(c)(3). An organization must not engage in substantial activities that fail to further an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) the Regulations provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. To meet this requirement, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests.

Section 1.501(c)(3)-1(d)(2) the Regulations defines the term "charitable" as including the relief of the poor and distressed or of the underprivileged, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration. The term "charitable" also includes the advancement of education.

Section 1.501(c)(3)-1(d)(3)(i) the Regulations provides, in part, that the term "educational" relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e) the Regulations provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of the Code § 501(c)(3) if the trade or business furthers an exempt purpose, and if the organization's primary purpose does not consist of carrying on an unrelated trade or business.

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In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283 (1945), the Supreme Court held that the “presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes.”

In Easter House v. U.S., 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.), the U.S. Court of Federal Claims considered whether an organization that provided prenatal care and other health-related services to pregnant women, including delivery room assistance, and placed children with adoptive parents qualified for exemption under § 501(c)(3). The court concluded that the organization did not qualify for exemption under § 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization’s argument that the adoption services merely complemented the health-related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization’s operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization’s sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. In addition, although the organization provided health care to indigent pregnant women, it only did so when a family willing to adopt a woman’s child sponsored the care financially. Accordingly, the court found that the “business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff’s adoption service is its primary goal” and held that the organization was not operated exclusively for purposes described in § 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in § 501(c)(3) because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with entities of a particular political party and that most of the organization’s graduates worked in campaigns for the party’s candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting the party’s candidates and entities. Although the candidates and entities benefited were not organization “insiders,” the court stated that the conferral of benefits on disinterested persons who are not members of a charitable class may cause an organization to serve a private interest within the meaning of § 1.501(c)(3)-1(d)(1)(ii). The court concluded by stating that even if the political party’s candidates and entities did “comprise a charitable class, [the organization] would bear the burden of proving that its activities benefited members of the class in a non-select manner.” American Campaign Academy, 92 T.C. at 1077.

In Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), the court held that an organization that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops operated for exclusively charitable purposes within the meaning of § 501(c)(3). The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence collected by the Bureau of Indian Affairs or other government agencies. The organization

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marketed only handicrafts it purchased in bulk from communities of craftsmen. The organization did not market the kind of products produced by studio craftsmen, nor did it market the handicrafts of artisans who were not disadvantaged. The court concluded that the overall purpose of the organization's activity was to benefit disadvantaged communities. The organization's commercial activity was not an end in itself but the means through which the organization pursued its charitable goals. The method the organization used to achieve its purpose did not cause it to serve primarily private interests because the disadvantaged artisans directly benefited by the activity constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans. Therefore, the court held that the organization operated exclusively for exempt purposes described in § 501(c)(3).

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the court relied on the commerciality doctrine in applying the operational test. Because of the commercial manner in which the organization conducted its activities, the court found that it was operated for a nonexempt commercial purpose, rather than for a tax-exempt purpose. As the court stated:

Among the major factors courts have considered in assessing commerciality are competition with for-profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, inter alia, whether the organization uses commercial promotional methods (e.g. advertising) and the extent to which the organization receives charitable donations.

See also, Living Faith Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991) (holding that a religious organization which ran restaurants and health food stores in furtherance of its health ministry did not qualify for tax-exempt status because it was operated for substantial commercial purposes and not for exclusively exempt purposes).

Rev. Rul. 67-138, 1967-1 C.B. 129, held that helping low-income persons obtain adequate and affordable housing is a "charitable" activity because it relieves the poor and distressed or underprivileged. In Rev. Rul. 67-138, the organization carried on several activities directed to assisting low-income families obtain improved housing, including (1) conducting a training course on various aspects of homebuilding and homeownership, (2) coordinating and supervising joint construction projects, (3) purchasing building sites for resale at cost, and (4) lending aid in obtaining home construction loans.

Rev. Rul. 2006-27 discusses three examples of organizations providing down payment assistance and whether each qualified as an organization described in section 501(c)(3) of the Code.

Situation 1 describes X, a non-profit corporation, that helps low-income individuals and families purchase decent, safe and sanitary homes throughout the metropolitan area in which it is located. As a substantial part of its activities, X makes assistance available exclusively to low-income individuals and families to provide part or all of the funds they need to make a down payment on the purchase of a home. Individuals are eligible to receive assistance from the downpayment assistance program if they are low-income individuals, have the employment history and financial history necessary to

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qualify for a mortgage, and would so qualify but for the lack of a down payment. To fund its down payment assistance program and other activities, the organization conducts a broad based fundraising program that attracts gifts, grants and contributions from several foundations, businesses and the general public.

In Situation 1, X's grantmaking process is structured to ensure that its staff awarding grants does not know the identity of the party selling the home to the grant applicant or the identities of any other parties, such as real estate agents or developers, who may receive a financial benefit from the sale. The staff also does not know whether any of the interested parties to the transaction have been solicited for contributions to the organization or have made pledges or actual contributions to the organization. Further, the organization does not accept any contributions contingent on the sale of a particular property or properties.

In Situation 1, the revenue ruling held the organization qualifies for exemption because its purposes and activities relieve the poor, distressed and underprivileged by enabling low-income individuals and families to obtain decent, safe and sanitary homes. The way the organization conducts its down payment assistance program establishes that its primary purpose is to address the needs of its low-income grantees. The organization conducts a broad based fundraising program, and receives support from a wide array of sources. Their policies of ensuring that its grantmaking staff does not know the identity or contributor status of the party selling the home to the grant applicant (or any other party who may receive a financial benefit from the sale), and of not accepting contributions contingent on the sale of any particular properties, ensure that it is not beholden to any particular donors or other supporters whose interest may conflict with that of the low-income buyers the organization is working to help.

In Situation 2, Y is a nonprofit corporation that is like X in all respects as set forth in Situation 1, except as follows. Under Y's grantmaking procedures, Y's staff considering a particular applicant's application knows the identity of the party selling the home to the grant applicant and may also know the identities of other parties, such as real estate agents and developers, who may receive a financial benefit from the sale. Moreover, in substantially all of the cases in which Y provides down payment assistance to a home buyer, Y receives a payment from the home seller. Further, there is a direct correlation between the amount of the down payment assistance provided by Y in connection with each of these transactions and the amount of the home seller's payment to Y. Finally, Y does not conduct a broad based fundraising campaign to attract financial support. Rather, most of Y's support comes from home sellers and real estate-related businesses that may benefit from the sale of homes to buyers who receive Y's down payment assistance.

In Situation 2, the revenue ruling held Y does not qualify as an organization described in § 501(c)(3). To finance its down payment assistance activities, Y relies on sellers and other real-estate related businesses that stand to benefit from the transactions Y facilitates. Furthermore, in deciding whether to provide assistance to a low-income applicant, Y's grantmaking staff knows the identity of the home seller and may also know the identities of other interested parties and is able to take into account whether the home seller or another interested party is willing to make a payment to Y. Y's receipt of a payment from the home seller corresponding to the amount of the down payment

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assistance in substantially all of the transactions, and Y's reliance on these contributions for most of its funding indicate that the benefit to the home seller is a critical aspect of Y's operations. In this respect, Y is like the organization considered in Easter House, which received all of its support from fees charged to adoptive parents, so that the business purpose of the adoption service became its primary goal and overshadowed any educational or charitable purpose. Like the organization considered in American Campaign Academy, Y is structured and operated to assist private parties who are affiliated with its funders. Like the organizations considered in American Campaign Academy, Easter House, and Columbia Park Recreation Association, Y also serves an exempt purpose, but because Y is not operated exclusively for exempt purposes, Y does not qualify for exemption from federal income tax as an organization described in § 501(c)(3).

In Situation 3, Z is a nonprofit corporation formed to combat community deterioration in an economically depressed area that has suffered a major loss of population and jobs. Studies have shown that the average income in the area is below the median level for the State. Z cooperates with government agencies and community groups to develop an overall plan to attract new businesses to the area and to provide stable sources of decent, safe and sanitary housing for the area residents without relocating them outside the area. As part of the renewal project, Z receives funding from government agencies to build affordable housing units for sale to low and moderate-income families. As a substantial part of its activities, Z makes down payment assistance available to eligible home buyers who wish to purchase the newly-constructed units from Z. Z also offers financial counseling seminars and conducts other educational activities to help prepare potential low and moderate-income home buyers for the responsibility of home ownership. To fund its down payment assistance program and other activities, Z conducts a broad based fundraising program that attracts gifts, grants and contributions from several foundations, businesses and the general public.

In Situation 3, the revenue ruling held that although Z does not limit its down payment assistance program to low-income recipients, Z's down payment assistance program still serves a charitable purpose described in § 501(c)(3) because it combats community deterioration in a specific, economically depressed area that has suffered a major loss of population and jobs. Through a combination of counseling and financial assistance, Z helps low and moderate-income families in that area to acquire decent, safe and sanitary housing and to prepare for the responsibilities of home ownership. In this respect, Z is like the organization described in Situation 3 of Rev. Rul. 70-585. Because Z is operated exclusively for charitable purposes, Z qualifies for exemption from federal taxation as an organization described in § 501(c)(3).

The revenue ruling concluded that down payment assistance payments for home buyers in Situations 1 and 3 are made by those organizations out of a detached and disinterested generosity and from charitable or like impulse, rather than to fulfill any moral or legal duty, and thus qualify for exclusion from such home buyers' gross incomes as "gifts" under § 102. The benefits provided to the home buyers in these circumstances are sufficiently removed from the interests of any home sellers or sales agents that they proceed from a detached and disinterested generosity on the part of the donor organization, and such grants lack the indicia of a rebate, price adjustment, or *quid pro quo* incident to a sale. In Situation 2, the organization is not operated exclusively for charitable purposes,

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and consequently, does not qualify for exemption from federal income tax as an organization described in § 501(c)(3).

Benefiting Private Interests

Even if an organization's activities serve a charitable class or are otherwise charitable within the meaning of § 501(c)(3), it must demonstrate that its activities serve a public rather than a private interest within the meaning of Reg. § 1.501(c)(3)-1(d)(1).

Rev. Rul. 72-147, 1972-1 C.B. 147, held that an organization that provided housing to low income families did not qualify for exemption under § 501(c)(3) because it gave preference to employees of business operated by the individual who also controlled the organization. The ruling reasoned that, although providing housing for low-income families furthers charitable purposes, doing so in a manner that gives preference to employees of the founder's business primarily serves the private interest of the founder rather than a public interest.

In KJ's Fund Raisers v. Commissioner, T.C. Memo 1997-424 (1997), aff'd, 1998 U.S. App. LEXIS 27982 (2d Cir. 1998), the Tax Court held, and the Second Circuit affirmed, that an organization formed to raise funds for distribution to charitable causes did not qualify for exemption under § 501(c)(3) because its activities resulted in a substantial private benefit to its founders. The founders of the organization were the sole owners of KJ's Place, a lounge at which alcoholic beverages were served. The founders served as officers of the organization and, at times, also controlled the organization's board. The Tax Court found, and the Second Circuit agreed, that the founders exercised substantial influence over the affairs of the organization. The organization's business consisted of selling "Lucky 7" or similar instant win lottery tickets to patrons of KJ's Place. The organization derived most of its funds from its lottery ticket sales. The organization solicited no public donations. The lottery tickets were sold during regular business hours by the owners of the lounge and their employees. From the proceeds of the sales of the lottery tickets, the organization made grants to a variety of charitable organizations. Although supporting charitable organizations may be a charitable activity, the Tax Court nevertheless upheld the Commissioner's denial of exemption to the organization on the ground that the organization's operation resulted in more than incidental private benefit. The Tax Court held, and the Second Circuit affirmed, that a substantial purpose of KJ's activities was to benefit KJ's place and its owners by attracting new patrons, by way of lottery ticket sales, to KJ's Place, and by discouraging existing customers from abandoning KJ's Place in favor of other lounges where such tickets were available. Thus, the organization was not operated exclusively for exempt purposes within the meaning of § 501(c)(3).

An organization does not serve a public rather than a private interest within the meaning of Reg. 1.501(c)(3)-1(d)(1) if any of its assets or earnings inure to the benefit of any insiders (or disqualified persons). Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii). Inurement is any transfer of charitable assets to the organization's insiders for which the organization does not receive adequate consideration. Inurement can take many forms.

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Excessive compensation for services is a form of inurement. For example, in Mabee Petroleum Corp. v. U.S., 203 F. 2d 872, 875 (5th Cir. 1953), the Fifth Circuit held that the organization's payment of a full-time salary for part-time work was inurement.

The use by insiders of the organization's property for which the organization does not receive adequate consideration is a form of inurement. See, e.g., The Founding Church of Scientology v. U.S., 412 F.2d 1197, 1201 (Ct. Cl. 1969) (holding that the insiders' use of organization-owned automobiles and housing constituted inurement); Spokane Motorcycle Club v. U.S., 222 F.Supp. 151 (E.D. Wash. 1963) (holding that the organization's provision of goods, services and refreshments to its members constituted inurement).

Loans that are financially advantageous to insiders from the organization's funds (particularly unexplained, undocumented loans) are a form of inurement. For example, in The Founding Church of Scientology, 412 F.2d at 1200-01, the Claims Court listed unexplained loans to and from insiders among the examples of inurement. In Church of Scientology v. Commissioner, 823 F.2d 1310, 1314-15, 1318 (9th Cir., 1987), the Ninth Circuit held that "debt repayments" in the form of 10 percent of the organization's income made to the organization's founder, allegedly to compensate the founder for the organization's past use of his personal income and capital, constituted inurement. In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the court held that forgiveness of interest was a form of inurement.

Leasing arrangements that favor disqualified persons to the detriment of the organization are a form of inurement. In The Founding Church of Scientology, 412 F.2d at 1201-02, the Claims Court treated the organization's payment of rent to the founder's wife as inurement in the absence of any showing that the rental was reasonable or that the arrangement was beneficial to the organization. See also Texas Trade School v. Commissioner, 272 F.2d 168 (5th Cir. 1959) (holding that inflated rental prices constitute inurement).

Payment to one person for services performed by another (or for services presumed to be performed, without any proof of performance) is a form of inurement. In Church of Scientology, 823 F.2d at 1314, 1317-18, the court listed royalties received by the organization's founder on the sale of publications written by others among the improper benefits received by the founder from the organization. In The Founding Church of Scientology, 412 F.2d at 1202, the court held that the payment of salary to the founder's daughter without any proof that she actually performed any services for the organization constituted inurement.

A number of courts have held that unaccounted for diversions of a charitable organization's resources by one who has complete and unfettered control can constitute inurement. Parker v. Commissioner, 365 F.2d 792, 799 (8th Cir. 1966); Kenner v. Commissioner, 318 F.2d 632 (7th Cir. 1963); Church of Scientology, 823 F.2d at 1316-17, 1319.

The provision of inurement can be direct or indirect. In Church of Scientology, 823 F.2d at 1315, the organization transferred in excess of \$3.5 million to a for-profit corporation incorporated by the organization's founder and his wife. The directors of the corporation were high-ranking members

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of the Church of Scientology. The directors approved the founder's decision to transfer \$2 million from the corporation's account to the ship *Apollo* aboard which the founder and his family lived. The Ninth Circuit held that the funds funneled through the for-profit corporation constituted inurement to the founder and his family. Church of Scientology, 823 F.2d at 1318.

In Church by Mail, Inc. v. Commissioner, 765 F.2d 1387 (9th Cir. 1985), the Ninth Circuit held that a church that conducted its activities by mail did not qualify for exemption under § 501(c)(3) because a substantial purpose of its activities was to benefit a for-profit corporation controlled by the church's insiders. The church employed an advertising agency controlled by its insiders to provide all of the printing and mailing services for the church's mass mailings. The advertising agency devoted approximately two-thirds of its time to the work for the church. The majority of the church's income was paid to the advertising agency. Although the advertising agency claimed to have clients unrelated to the church, it did not advertise its services and refused to identify its other clients. The Ninth Circuit held that the church was operated for the substantial non-exempt purpose of "providing a market for [the advertising agency's] services" and, thus, primarily served the private interests of the advertising agency and its owners rather than a public purpose. In so holding the Ninth Circuit rejected the church's argument that the income paid by the advertising agency should not be included in the determination of reasonableness and treated this income as indirect inurement of the church's earnings to the church's insiders.

The prohibition on inurement in § 501(c)(3) is absolute. The Service has the authority to revoke an organization's exempt status for inurement regardless of the amount of inurement.

Effective date of revocation

An organization may ordinarily rely on a favorable determination letter received from the Internal Revenue Service. Treas. Reg. §1.501(a)-1(a)(2); Rev. Proc. 2003-4, §14.01 (cross-referencing §13.01 et seq.), 2003-1 C.B. 123. An organization may not rely on a favorable determination letter, however, if the organization omitted or misstated a material fact in its application or in supporting documents. In addition, an organization may not rely on a favorable determination if there is a material change, inconsistent with exemption, in the organization's character, purposes, or methods of operation after the determination letter is issued. Treas. Reg. § 601.201(n)(3)(ii); Rev. Proc. 90-27, §13.02, 1990-1 C.B. 514.

The Commissioner may revoke a favorable determination letter for good cause. Treas. Reg. § 1.501(a)-1(a)(2). Revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 2003-4, § 14.01 (cross-referencing § 13.01 et seq.).

HUD Directive 4155.1 REV-5, 2-10 issued in October 2003, describes about "Gift Funds" as follows:

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C. Gift Funds. An outright gift of the cash investment is acceptable if the donor is the borrower's relative, the borrower's employer or labor union, a charitable organization, a governmental agency or public entity that has a program to provide homeownership assistance to low- and moderate-income families or first-time homebuyers, or a close friend with a clearly defined and documented interest in the borrower. The gift donor may not be a person or entity with an interest in the sale of the property, such as the seller, real estate agent or broker, builder, or any entity associated with them. Gifts from these sources are considered inducements to purchase and must be subtracted from the sales price. No repayment of the gift may be expected or implied. ...

FHA deems the payment of consumer debt by third parties to be an inducement to purchase. ... When someone other than a family member has paid off debts, the funds used to pay off the debt must be treated as an inducement to purchase and the sales price must be reduced by a dollar-for-dollar amount in calculating the maximum insurable mortgage.

Documentation Requirements. The lender must document the gift funds by obtaining a gift letter, signed by the donor and borrower, that specifies the dollar amount of the gift, states that no repayment is required, shows the donor's name, address, and telephone number and states the nature of the donor's relationship to the borrower...

Regardless of when the gift funds are made available to the homebuyer, the lender must be able to determine that the gift funds ultimately were not provided from an unacceptable source and were indeed the donor's own funds. When the transfer occurs at closing, the lender remains responsible for obtaining verification that the closing agent received funds from the donor for the amount of the purported gift and that those funds came from an acceptable source.

NOTE: FHA does not "approve" down payment assistance programs in the form of gifts administered by charitable organizations (i.e., nonprofits). Mortgage lenders are responsible for assuring that the gift to the homebuyer from the charitable organization meets the appropriate FHA requirements and the transfer of funds is properly documented. In addition, FHA does not allow nonprofit entities to provide gifts to homebuyers for the purpose of paying off installment loans, credit cards, collections, judgments, and similar debts.

The Directive 4155.1 Rev.4, issued in September 1995 has similar wordings for the "Gift Funds" description and nonprofit organization requirements.

On March 3, 2000, HUD issued Mortgagee Letter 00-8 for "Nonprofit Agency Participation in Single Family FHA Activities" stating:

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Approval of Downpayment Assistance Programs in the Form of Gifts: There has been widespread confusion regarding the Department's role in approving downpayment assistance programs in the form of gifts. FHA does not "approve" down payment assistance programs in the form of gifts administered by charitable organizations. Mortgage lenders are responsible for assuring that the gift to the homebuyer from the charitable organization meets the instructions described in HUD Handbook 4155.1, REV-4, Change 1 (e.g., no repayment implied, etc.). Thus, while FHA will issue approval letters to nonprofit agencies for their participation as mortgagors, providers of secondary financing, and as purchasers of HUD homes at a discount, such letters are not to be construed as approval of the nonprofit agency's down payment assistance gift programs. FHA will not issue approval letters for down payment assistance gift programs.

On August 7, , HUD issued Mortgagee Letter 00-28 for "Gift Documentation, Mortgage Forms and other Credit Policy and Appraisal Issues" revising HUD procedures for verifying the transfer of gift funds from private individual donors to homebuyers, as well as the required contents of the gift letter itself. The letter states:

... These reforms are intended to ensure to the greatest extent possible that the gift funds were in fact the donor's own and are not derived from an unacceptable source. The donor must be able to furnish conclusive evidence that the funds given to the homebuyer came from the donor's own funds and thus, were not provided directly or indirectly by the seller, real estate agent, builder, or any other entity with an interest in the sales transaction.

The gift letter, ... now must also contain language asserting that the funds given to the homebuyer were not made available to the donor from any person or entity with an interest in the sale of the property including seller, real estate agent or broker, builder, loan officer or any entity associated with them. ...

Regardless of when the gift funds are made available to the homebuyer, the lender must be able to determine that the gift funds were not ultimately provided from an unacceptable source and were indeed the donor's own funds. When the transfer occurs at closing, the lender remains responsible for obtaining verification the closing agent received funds from the donor for the amount of the purported gift.

GOVERNMENT'S POSITION:

In order for an organization to retain its exempt status it must demonstrate to the Internal Revenue Service that it meets both the organizational and the operational tests. The facts stated above indicate that **A, Inc.** failed the operational test.

When the organization filed an application form to apply for its exempt status in December 2002, it stated that it will devote approximately 70% of its time and other resources to assist youth organizations. On **Date 8**, the Service issued a determination letter to recognize the organization

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exempt from federal income tax under section 501(a) of the Code. No education activities were conducted by **A, Inc.** Two months after the issuance of the determination letter, the organization faxed a letter to IRS Customer Service to propose changes in its activities, mainly engaging in down payment assistance activities. Instead of following the instructions from IRS Customer Service to submit its proposed changes in activities to the National Office, the organization sent another letter to the IRS Customer Service.

The organization did not provide any documents to prove that it conducted any activities as stated on the application Form 1023 for the year under examination. They merely posted educational material on the website.

Charitable purposes include relief of the poor and distressed. See section 1.501(c)(3)-1(d)(2) of the regulations. **A, Inc's** down payment assistance program does not operate in a manner that establishes that its primary purpose is to address the needs of low-income people by enabling low-income individuals and families to obtain decent, safe housing. See Rev. Rul. 2006-27, Situation 2. The down payment assistance program did not serve exclusively low-income persons. **A, Inc** does not have any income limitations for participation in its DPA program. The program is open to every homebuyer, without any income limitations, who otherwise qualified for financing from a lender.

A, Inc's DPA program does not limit assistance to certain geographic areas or target those areas experiencing deterioration or neighborhood tensions. See Rev. Rul. 2006-27, Situation 3. Down payment assistance is available for any property that is otherwise able to qualify for a mortgage. Arranging or facilitating the purchase of homes in a broadly defined geographic area does not combat community deterioration or serve other social welfare objectives within the meaning of section 501(c)(3) of the Code.

A, Inc promotes itself as a qualified grantor to conduct down payment assistance program according to the current guidelines in HUD Handbook 4155. 1 Rev 4, Section 2-10, for FHA insured loans. **IRS Agent** quoted the HUD Handbook 4155.1 Rev 5, 2-10 under the Applicable Legal Principles below. The Rev 5 was effective October 2003. The handbook stated that "**the gift donor may not be a person or entity with an interest in the sale of the property, such as the seller, real estate agent or broker, builder, or any entity associated with them.**" It means **A, Inc's** DPA did not meet the requirement of the guidelines in HUD because the gift donor are the sellers.

Also **A, Inc's** DPA program provided a private benefit to various parties. Like the organization considered in American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), **A, Inc.** is structured and operated to assist the private parties who fund it and give it business. Sellers who participate in **A, Inc's** DPA program benefit from achieving access to a wider pool of buyers, thereby decreasing their risk and the length of time the home is on the market. They also benefit by being able to sell their home at the home's full listed price or by being able to reduce the amount of the negotiated discount on their homes. Buyers who participate in **A, Inc's** DPA program benefit by being able to purchase a home without having to commit more of their own funds. It is evident from the foregoing that **A, Inc's** DPA program provides ample private benefit to the various parties in each home sale.

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The manner in which **A, Inc.** operated its DPA program shows that the private benefit to the various participants in **A, Inc's** activities was the intended outcome of **A, Inc's** operations. **A, Inc's** down payment assistance procedures are designed to channel funds in a circular manner from the sellers to the buyers and back to the sellers in the form of increased home prices. To finance its down payment assistance activities, **A, Inc** relies exclusively on sellers. **A, Inc** neither solicits nor receives funds from other sources. **A, Inc.** requires the home seller to reimburse it, dollar-for-dollar, for the amount of funds expended to provide down payment assistance on the seller's home, plus an administrative fee of several hundred dollars per home sale. **A, Inc.** receipt of a payment from the home seller corresponding to the amount of the down payment assistance in virtually every transaction indicates that the benefit to the home seller (and others involved in the transaction) is not a mere accident but rather an intended outcome of **A, Inc.** operations. In this respect, **A, Inc.** is like the organization considered in Easter House which provided health care to indigent pregnant women, but only when a family willing to adopt a woman's child sponsored the care financially.

A, Inc's receipt of a payment from the home seller corresponding to the amount of the down payment assistance in virtually every transaction and **A, Inc's** reliance on these payments for most of its funding indicate that the benefit to the home seller is a critical aspect of **A, Inc's** operations. The sellers got the benefit of having their property sold quicker (due to greater number of potential home buyers) without actually incurring any costs. Because the amount that home buyers received from **A, Inc.** was incorporated into the sale price of a home, the purported beneficiaries in fact did not receive anything from **A, Inc.**. Further, because the transaction fees charged by **A, Inc** could be based on a percentage of the home's sale price, **A, Inc** benefited from the transactions by maximizing its fees. The circular cash flow indicates that the Corporation's primary goal was to facilitate transactions for the benefit of private parties involved or connected to these transactions, i.e., buyers (who were not necessarily members of a charitable class), sellers, real estate professionals, etc. In this respect, **A, Inc.** is like the organization considered in Easter House which provided health care to indigent pregnant women only when a family willing to adopt a woman's child sponsored the care financially.

A, Inc.'s promotional material and its marketing activities show that **A, Inc.** operated in a manner consistent with a commercial firm seeking to maximize sales of services, rather than in a manner that would be consistent with a charitable or educational organization seeking to serve one or more of the charitable purposes enumerated in § 501(c)(3). The manner in which **A, Inc.** operated its DPA program shows that **A, Inc.** was in the business of facilitating the sales of homes in a manner indistinguishable from an ordinary trade or business. In this respect **A, Inc.'s** operations were similar to an organization which was denied exemption because it operated a conference center for commercial purposes. See Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003).

Operating a trade or business of facilitating home sales is not an inherently charitable activity. Unlike the trade or business in Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), **A, Inc.'s** trade or business was not utilized as a mere instrument of furthering charitable purposes but was an end in itself. **A, Inc.** provided services to home sellers for which it charged a market rate fee. **A, Inc.** did not market its services primarily to persons within a charitable class. **A, Inc.** did not solicit or receive any funds from parties that did not have interest in the down payment transactions. Like the organizations considered in American Campaign Academy, supra, and Easter House v. U.S., 12 Cl.

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer	Tax Identification Number	Year/Period ended
A, Inc.	NUM	Date 1

Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.) a substantial part of **A, Inc.'s** activities furthered commercial rather than exempt purposes.

Furthermore, **A, Inc.'s** activities were structured to provide substantial private benefit to **A, Inc.'s** related for-profit organization, **Rel. Housing, LLC**. **A, Inc.** entered into a marketing agreement with **Rel.**, a for-profit entity owned by the director of **A.Inc.**. For the agreed upon services, **A, Inc.** agreed to pay **\$xxx** of the fees generated for each transaction closed. **A, Inc.** normally charges **\$xxx** service fee for each home transaction. For the year end Date 1, **A, Inc.** made payments total **\$xxx,xxx** to **Rel.** for marketing fees, which was % of the service fees **A, Inc.** received.

A, Inc. does not qualify as an organization described in I.R.C. § 501(c)(3) because it operates a program that does not exclusively serve an exempt purpose described in section 501(c)(3), and provides substantial private benefit to its related for-profit corporations.

TAXPAYER'S POSITION:

A, Inc. hasn't provided its position.

CONCLUSION:

In order to qualify for exemption under IRC § 501(c)(3) an organization must be both organized and operated to achieve a purpose that is described under that Code section. **A, Inc.'s** DPA program is not operated in accordance with Internal Revenue Code § 501(c)(3) and the regulations governing qualification for tax exemption under Code. **A, Inc.** offers its down payment assistance to interested buyers regardless of the buyers' income levels or need. **A, Inc.'s** DPA activities do not target neighborhoods in need of rehabilitations or other relief such as lessening neighborhood tensions or eliminating prejudice and discrimination.

A, Inc. operates in a manner indistinguishable from a commercial enterprise. **A, Inc.'s** primary activity is brokering transactions to facilitate the selling of homes. **A, Inc.'s** primary goal is to maximize the fees from these transactions and benefit its related parties. **A, Inc.'s** brokering services are marketed to homebuyers, sellers, realtors, lenders, and builders regardless of the buyers' income level or need and regardless of the condition of the community in which the home is located. Because **A, Inc.'s** primary activity is not conducted in a manner designed to further § 501(c)(3) purposes, **A, Inc** is not operated exclusively for exempt purposes within the meaning of § 501(c)(3).

In addition, **A, Inc.'s** activities were operated for the purpose of serving a private benefit rather than public interest, and a part of the net earnings were benefit of a related for-profit corporation. Accordingly, it is determined that **A, Inc.** is not an organization described in section 501(c)(3), and is not exempt from income tax under section 501, effective **Date 7**.