

**Internal Revenue Service
Appeals**

Department of the Treasury

Address any reply to:
Office of Appeals
One Cleveland Center-Suite 815
1375 East Ninth Street
Cleveland, OH 44114-1739

Employer Identification Number:

C *****

Person to Contact:

Identification Number:

Contact Telephone Number:

Fax Number:

**Last Day to File a Petition with the United States
Tax Court JUN 09 2008**

Date: **MAR 11 2008**

A *****

B*****

Number: **200825046**
Release Date: 6/20/2008

UIL: 9999.98-00

Certified Mail

Dear :

This is our final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code ("Code"). Your tax-exempt status is revoked effective July 1, 2002.

It has been determined that the (A) is not operating as an organization exempt under IRC section 501(a) and described in IRC section 501(c)(3) for the following reasons:

- A substantial part of your activities (operation of the bingo games) is not in furtherance of an exempt purpose, and therefore, you are not operated exclusively for an exempt purpose pursuant to section 501(c)(3) of the Internal Revenue Code and Treas. Reg. section 1.501(c)(3)-1(c)(1), and
- By engaging in substantial activities that serve private rather than public interests (the private interests of the bingo operator), you are not operated exclusively for one of more exempt purposes pursuant to Treas. Reg. section 1.501(c)(3)-1(d)(1)(ii).

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

You are required to file Federal income tax returns on form 1120 for any years, which are still open under the statute of limitations. Based on the information you furnished, it appears that returns should be filed beginning with the year ending June 30, . You should file any returns due for these years or later years with the Internal Revenue Service Center, Cincinnati, Ohio 45999-0012. Processing of income tax returns will not be delayed because you have filed a petition for a declaratory judgment under section 7428 of the Code.

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

You have waived your right to contest this determination under the declaratory judgment provisions of Section 7428 of the Code by your execution of Form 906, Closing Agreement Concerning Specific Matters.

If you have questions about this letter, you may write to or call the contact person whose name, telephone number, and IRS address are shown on the first page of this letter. If you write, please include your telephone number, the best time for us to call you if we need more information, and a copy of this letter to help us identify your account. Keep the original letter for your records. If you prefer to call and the telephone number is outside your local calling area, there will be a long distance charge to you.

The contact person identified on the front of this letter can access your tax information and help you get answers. You also have the right to contact the office of the Taxpayer Advocate. You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate for the IRS office that issued this notice of deficiency by calling or writing to 550 Main Street, Room 7010, Cincinnati, OH 45202. Taxpayer Advocate assistance is not a substitute for established IRS procedures such as the formal appeals process. The Taxpayer Advocate is not able to reverse legally correct tax determinations, nor extend the time fixed by law that you have to file a petition in the U.S. 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.

Sincerely yours,

Linda E. Stiff
Acting Commissioner

By



Charles F. Fisher
Appeals Team Manager

Enclosures:

Notice 1214 Helpful Contacts for Your "Deficiency Notice"

cc:



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
1835 Assembly St., MDP 046
Columbia, SC 29201

October 6, 2006

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

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:

Taxpayer Advocate
1835 Assembly St., Rm. 466, MDP 03
Columbia, SC 29201
Phone: 803-253-3029
FAX: 803-253-3910

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 Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Legend:

A -
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ISSUE:

Whether the A, a B Corporation, continues to meet the requirements of Internal Revenue Code section 501(c)(3), and therein continues to qualify for exemption from Federal income tax.

FACTS:

Governing Documents

The A was incorporated as a non-profit corporation under the laws of B to promote the arts by putting on ballet performances.

In C, D was granted exemption under section 501(c)(3) of the Internal Revenue Code as an organization that is not a private foundation because it is described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the Code. On E, the IRS issued a letter acknowledging the change in the corporate name to A. That letter indicated that A continued to qualify as an organization exempt under section 501(c)(3) of the Code as an organization that is not a private foundation because it is described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the Code.

On F, you entered into a contract with G to promote bingo games in order to raise funds for your organization. Under the terms of the contract, G is the Promoter and A is the Sponsor.

The Promoter's contact with G requires the Promoter to: "perform general management and operating services in the operation of the bingo business located at H, to do business as I with all authority, subject to the limitations and conditions herein set forth, to direct, supervise and manage the operation of the business."

Article 2 of the contract provides, in part, that: "The promoter shall perform the following duties:

- a. Supervise and direct the general operations of the business;
- b. Operate the business efficiently and with proper economy;
- c. Develop policies with respect to publicity and advertising for the purpose of creating the greatest possible net income for the Sponsor;
- d. Supervise and manage the day-by-day operations of the bingo;
- e. Employ as necessary such individuals as may be required to staff and manage the bingo;
- f. Keep the bingo and all furniture, furnishings and other equipment therein and appurtenant thereto in repair and arrange for the necessary replacement improvements and changes in the bingo as may be required;
- g. Promoter has sole and exclusive responsibility of maintaining the bingo license issued to Sponsor and insuring that said license continue in good standing with the State licensing authority;
- h. Promoter shall be responsible for paying all bills, charges, costs, and debts of any kind relating to the operation of the bingo, including, but not limited to, bingo paper, payroll expenses, payroll taxes, and any and all other taxes, utilities, building maintenance, and insurance;
- i. Prepare and file all reports required for operation of the bingo, including but not limited to, Quarterly Financial Bingo Report, paper inventory, and State and Federal employer forms; the Promoter shall also furnish Sponsor with accounting summaries to enable Sponsor to report the income and net profits from special events on line 9 Part 1 of Sponsor's Form 990;

- j. Promoter shall provide all furniture, fixtures and equipment required for the operation of the bingo, including but not limited to, camera and sound system, bingo machine, approximately six (6) television monitors, tables and chairs necessary to comfortably seat a minimum of seventy-five (75) bingo players."

Article 4 of the contract provides for Compensation. "Promoter shall be paid on a monthly basis an amount equal to J% of the net profit and Sponsor is guaranteed to receive J% of the net profit or \$K each month, whichever is greater. The sufficiency of said compensation is hereby acknowledged by the parties hereto in consideration for the agreement of the parties hereto. All payments shall be made no later than the tenth (10th) of the month for the preceding month. Promoter shall receive any and all income from the sale of tangible items such as concession items, snacks, dabbers, etc."

On L, you entered into a new contract with your promoter, G. The contract has an expiration date of M, and will be automatically renewed for one (1) year terms thereafter, beginning on N.

The duties and responsibilities of the promoter listed in Article 2 a-j remained essentially the same as the original contract. The relevant changes are reflected below.

Changes to Article 2 of the Bingo Promoter's contract are shown in ***bold italics*** below:

- c. Develop policies with respect to publicity and advertising for the purpose of creating the greatest possible net income for the ***Licensee***;
- g. Promoter has sole and exclusive responsibility of maintaining the bingo license issued to ***Licensee*** and insuring that said license continue in good standing with the State licensing authority;
- h. Promoter shall be responsible for insuring payment of all bills, charges, costs, and debts of any kind relating to the operation of the bingo [***defined as "necessary and reasonable bona fide expenses incurred and paid in connection with the conduct of bingo" pursuant to § 12-21-4090(F), Code of Laws of B, 1976 (as amended)***], including, but not limited to, bingo paper, payroll expenses, payroll taxes, and any and all other taxes, utilities, building maintenance, and insurance;
- i. Prepare and file all reports required for operation of the bingo, including but not limited to, Quarterly Financial Bingo Report, paper inventory, and State and Federal employer forms; the Promoter shall also furnish ***Licensee*** with accounting summaries to enable ***Licensee*** to report the income and net profits from special events on line 9 Part 1 of ***Licensee's*** Form 990 ***return, should Licensee file such a return***;

Article 4 of the current contract provides for the following compensation. "Promoter shall receive 0% of the gross revenue (all revenue prior to player payouts) of the bingo on a monthly basis as the compensation for operating and promoting the bingo. All expenses (paragraph 2h, above) shall be paid from the bingo account. Any surplus funds after all expenses are paid shall be paid to the Licensee on a monthly basis, with a guaranteed minimum to the Licensee of \$K. The reasonableness and sufficiency of said compensation is hereby acknowledged by the parties hereto in consideration for the agreement of the parties. All payments shall be made no later than the tenth (10th) of the month for the preceding month. Promoter shall receive any and all income from the sale of tangible items such as concession items, snacks, dabbers, etc."

Activities & Income for the year ended P

During our examination we requested documentation showing the amount of time devoted to your exempt activities and to your bingo activities for the year ended P. No actual records were kept of the volunteer hours devoted to your exempt activities. You submitted an estimate which showed that volunteers devoted approximately 12,545 hours to your exempt function activities in the year ended P.

Payroll records indicate that paid bingo employees devoted a total of 3320 hours to bingo activities in the fiscal year ended P.

This does not include any time G devotes to the bingo operation. When asked, G was unable to provide any records showing the number of hours that he worked.

The percentage of time devoted to your bingo activities for the year ended P, has been computed as follows:

Exempt Function Time	+	Bingo Time	=	Total Time
12,545		+ 3,320		= 15,865

<u>Bingo Time</u>	=	<u>3,320</u>	=	20.9%
<u>Total Time</u>		<u>15,865</u>		

Our examination also showed that you received gross income of \$87,729 from exempt function activities and you received gross income of \$242,046 from your bingo games for the year ended P. Total gross income from all sources for the year ended P, was \$329,775.

Gross bingo income for the period constituted 73% of your total gross income for the year ended June 30, , and is computed as follows:

Bingo Gross Income	=	\$242,046	=	73%
<u>Exempt Function Income</u>	=	<u>\$87,729</u>	=	<u>27%</u>

Total Gross Income = \$329,775 = 100%

Although records for the bingo account showed two checks for \$500 were written to the charity account, they did not clear the bank and no deposits were recorded in the charity account for payments from the bingo account for the year ended P.

Therefore, 0% of the gross bingo proceeds went to A. for charitable or other IRC 501(c)(3) purposes for the year ended P.

Activities & Income for the year ended Q

During our examination we requested documentation showing the amount of time devoted to your exempt activities and to your bingo activities for the year ended Q. No actual records were kept of the volunteer hours devoted to your exempt activities. You submitted an estimate which showed that volunteers devoted approximately 12,431 hours to your exempt function activities in the year ended Q.

Payroll records indicate that paid bingo employees devoted a total of 15,033 hours to bingo activities in the fiscal year ended Q

This does not include any time G devotes to the bingo operation. When asked, was unable to provide any records showing the number of hours that he worked.

The percentage of time devoted to your bingo activities for the year ended Q, has been computed as follows:

Exempt Function Time + Bingo Time = Total Time
12,431 + 15,033 = 27,464

$$\frac{\text{Bingo Time}}{\text{Total Time}} = \frac{15,033}{27,464} = 54.7\%$$

Our examination showed that you received gross income of \$97,815 from exempt function activities and you received gross income of \$1,090,048 from your bingo games for the year ended Q. Total gross income from all sources for the year ended Q, was \$1,187,863.

Gross bingo income for the period constituted 92% of your total gross income for the year and is computed as follows:

Bingo Gross Income = \$1,090,048 = 92%
Exempt Function Income = 97,815 = 8%
Total Gross Income = \$1,187,863 = 100%

Records for the year ended Q, showed that A received \$DD from the bingo account. The percentage of gross bingo receipts distributed to A for charitable or other IRC 501(c)(3) purposes for the year ended Q, amounts to .34% of the gross bingo income and is computed as follows:

$$\frac{\text{Amount Distributed to Charity}}{\text{Gross Bingo Income}} = \frac{3,725}{\$1,090,048} = .34\%$$

Delinquent Returns

Our records show that proper Forms 990 have not been filed for the years ended P, Q, or R.

Prior to the start of our examination on S, a Revenue Officer from the Internal Revenue Service contacted you regarding the collection of penalties related to your failure to timely file Form 990 for the year ended T and P.

You provided Form 990EZ to the Revenue Officer on or about U. Since Form 990EZ may only be filed by organizations that received less than \$100,000 in gross receipts, you do not meet the requirements to file Form 990EZ. Consequently, that return has not been accepted and your Form 990 for the year ended P, remains delinquent and penalties and interest continue to accrue up to the maximum allowed by law.

There is no record that any Forms 990 were filed for the years ended Q and R. Delinquency penalties and interest continue to accrue for those returns up to the maximum allowed by law.

During our examination, we noted that the Form W-2 issued to your Office Manager for the calendar year ended V, was not filed with the Social Security Administration as required.

In a notice dated W, you were assessed a penalty of \$X for failure to file Forms W-2 and W-3. A subsequent notice increased that penalty to \$Y. There is no record showing that you paid the penalties or filed the Forms W-2 and W-3. Penalties and interest continue to accrue up to the maximum allowed by law.

Our records also show that you were sent a notice dated Z, showing that you owe \$AA for failure to timely file your Form 990 for the year ended T. There is no record that you paid the penalty or furnished reasonable cause as to why the Form 990 for T, was filed late. Therefore, penalties and interest continue to accrue up to the maximum allowed by law.

LAW:

Section 501(a) of the Internal Revenue Code exempts from taxation organizations described in subsection (c) or (d) under this subtitle unless such exemption is denied under section 502 or 503.

Section 501(c) (3) of the Code exempts from taxation: "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 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."

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

Treasury Regulation 1.501(c) (3) - (a) (1) provides, in part, 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 purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt."

Section 1.501(c) (3) - 1 of the Income Tax Regulations provides:
(c) Operational test - (1) Primary activities. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of such exempt purposes specified in section 501(c) (3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

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

Section 1.501(c) (3) - 1(d) (1) (ii) provides that the burden of proof is on the organization to establish that it is not organized and operated for the benefit of private interests.

Church in Boston v. Commissioner, 71 T.C. 102, 107 (1978), provides, in part, that the word "exclusively" does not mean "solely" or "without exception." An organization which engages in nonexempt activities can obtain and maintain exempt status so long as such activities are only incidental and insubstantial. (World Family Corp. v. Commissioner, 81 T.C. 958, 963 (1983) Neither the Internal Revenue Code, the regulations nor the case law provide a general definition of "insubstantial" for purposes of 501(c)(3). This is an issue of fact to be determined under the facts and circumstances of each particular case. (World Family Corp. v. Commissioner, supra at 967.)

In Help The Children, Inc. v. Commissioner 28 TC 1128 (1957), the court held that an organization engaged in fund-raising activities through operation of bingo games and whose actual charitable contributions consisted of contributions to charitable institutions of insubstantial amounts when compared to its gross receipts from operation of bingo games, did not qualify for exemption under section 501(c)(3) of the Code.

Petitioner's fund-raising activities consisted of the operation of bingo games at the Lodge of the Fraternal Order of the Eagles. It also operated a soda bar, and miscellaneous activities. Income from the soda bar and miscellaneous activities was reported on the returns as \$2,843.25 for 1953 and \$3,672.64 for 1954. The gross receipts from the fixed charge or donation for the use of the bingo cards were \$313,802.20 for 1953 and \$306,309.85 for 1954.

Petitioner did not operate any charitable institutions and its actual charitable function consisted of contributions to various individual doctors and institutions. These contributions totaled \$2,880 in 1953 and \$3,873.20 in 1954. Its principal activity was the profitable operation of bingo games on a business or commercial basis. The principal source of gross receipts was from the fixed charge or donation assessed against each player for the use of the bingo cards.

Therefore, the court held that the petitioner failed to establish that it is entitled to a tax-exempt status in the taxable years in question.

In Make a Joyful Noise, Inc. v. Commissioner, 56 TCM 1003 (1989), the court held that operating regularly scheduled bingo games on behalf of other exempt organizations was a trade or business unrelated to the organization's exempt purposes.

In that case, the court concluded that the petitioner failed to carry its burden of proving that its participation in bingo games was an insubstantial part of its activities.

In P.L.L. Scholarship Fund, v. Commissioner, 82 TC 196 (1984) the Tax Court held that petitioner was not operated exclusively for exempt purposes under the provisions of section 501(c)(3), I.R.C. 1954, and

section 1.501(c)(3)-1(c)(1), Income Tax Regs. Therefore, the Tax Court held that it was not exempt from Federal income tax.

Petitioner was incorporated as a nonprofit corporation for the purpose of raising money to be used for providing college scholarships. The money was raised from the operation of bingo games on the premises of a commercial establishment.

The court stated that: "After careful consideration of the entire record, this Court finds that the petitioner has not carried its burden of showing that it was operated exclusively for an exempt purpose under the required standards."

The court further stated that: "Since the record in this case does not show that the petitioner was operated exclusively for exempt purposes, but rather indicates that it benefited private interests, exemption was properly denied."

In People of God Community v. Commissioner, 75 TC 127 (1980), the court held, that part of petitioner's net earnings inured to the benefit of private shareholders or individuals and that petitioner was not exempt as an organization described in section 501(c)(3), of the Internal Revenue Code of 1954.

The court stated that the burden falls upon petitioner to establish the reasonableness of the compensation. The court indicated that by basing compensation upon a percentage of petitioner's gross receipts, apparently subject to no upper limit, a portion of petitioner's earnings was being passed on to an individual. The court stated that: "The statute specifically denies tax exemption where a portion of net earnings is paid to private shareholders or individuals. We hold here that paying over a portion of gross earnings to those vested with the control of a charitable organization constitutes private inurement as well. All in all, taking a slice off the top should be no less prohibited than a slice out of net."

Revenue Ruling 69-383, 1969-2 CB 113, (Jan. 01, 1969) provides in part that, under certain circumstances, the use of a method of compensation based upon a percentage of the income of an exempt organization can constitute inurement of net earnings to private individuals. For example, the presence of a percentage compensation agreement will destroy the organization's exemption under section 501(c)(3) of the Code where such arrangement transforms the principal activity of the organization into a joint venture between it and a group of physicians (Lorain Avenue Clinic v. Commissioner, 31 T.C. 141 (1958)), or is merely a device for distributing profits to persons in control (Birmingham Business College v. Commissioner, 276 F. 2d 476 (1960)).

Revenue Ruling 64-182, 1964-1 (Part 1) C.B. 186, concluded that an organization qualified for exemption under section 501(c)(3) of the

Code where it used the proceeds from a business activity to conduct a charitable, program, "commensurate in scope" with its financial resources, of making grants to other charitable organizations. Thus, an organization whose principal activity is operating games of chance may nevertheless qualify for exemption, provided it uses the proceeds of that business activity in a real and substantial charitable program (such as charitable grant making) commensurate in scope with its financial resources, and other wise meets the requirements of exemption.

Christian Echoes National Ministry, Inc. v. United States, 470 F2d 849 (1972), held, in part, that "tax exemption is a privilege, a matter of grace rather than right".

IRC section 6033 (a) (1) provides: IN GENERAL. "Except as provided in paragraph (2), every organization exempt from taxation under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe;"

IRC 6033(a) (2) EXCEPTIONS FROM FILING

"(A) (ii) any organization (other than a private foundation, as defined in section 509(a)) described in subparagraph (C), the gross receipts of which in each taxable year are normally not more than \$5,000,..."

In Announcement 82-88, 1982-25 I.R.B. 23, the Commissioner announced that he had exercised his discretionary authority and enlarged a category of exempt organizations that are not required to file Form 990. Exempt Organizations described in section 501(c) of the Code (other than private foundations) the gross receipts of which in each taxable year are normally not more than \$25,000, are excused from filing the annual information return for tax years ending on or after December 31, 1982.

Treasury Regulation 1.6001-1(c) requires that an exempt organization must maintain records sufficient to demonstrate that it is entitled to tax-exempt status.

Treasury Regulation 1.6033-2(h) (2) holds that an organization which is exempt from tax, whether or not it is required to file an annual information return, shall submit such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into its exempt status.

Revenue Ruling 59-95, Cumulative Bulletin 1959-1, page 627, prescribes that failure to comply with the provisions of section 6033

of the Code and regulations which implement it, may result in the termination of the exempt status of an organization on the grounds that the organization has not established that it is observing the conditions required for the continuation of its exempt status.

Section 6652 of the Internal Revenue Code provides penalties for failure to file certain information returns.

6652(c) RETURNS BY EXEMPT ORGANIZATIONS AND BY CERTAIN TRUSTS -

6652(c) (1) Annual returns under section 6033 or 6012(a) (6) -

6652(c) (1) (A) Penalty on organization - In the case of -

(i) a failure to file a return required under section 6033 (relating to returns by exempt organizations) or section 6012(a) (6) (relating to returns by political organizations) on the date and in the manner prescribed therefor (determined with regard to any extension of time for filing), or

(ii) a failure to include any of the information required to be shown on a return filed under section 6033 or section 6012(a) (6) or to show the correct information, there shall be paid by the exempt organization \$20 for each day during which such failure continues. The maximum penalty under this subparagraph on failures with respect to any 1 return shall not exceed the lesser of \$10,000 or 5 percent of the gross receipts of the organization for the year. In the case of an organization having gross receipts exceeding \$1,000,000 for any year, with respect to the return required under section 6033 or section 6012(a) (6) for such year, the first sentence of this subparagraph shall be applied by substituting "\$100" for "\$20" and, in lieu of applying the second sentence of this subparagraph, the maximum penalty under this subparagraph shall not exceed \$50,000.

6652(c) (1) (B) Managers -

6652(c) (1) (B) (i) In general - The Secretary may make a written demand on any organization subject to penalty under subparagraph (A) specifying therein a reasonable future date by which the return shall be filed (or the information furnished) for purposes of this subparagraph.

6652(c) (1) (B) (ii) Failure to comply with demand - If any person fails to comply with any demand under clause (i) on or before the date specified in such demand, there shall be paid by the person failing to so comply \$10 for each day after the expiration of the time specified in such demand during which such failure continues. The maximum penalty imposed under this subparagraph on all persons for failures with respect to any 1 return shall not exceed \$5,000.

GOVERNMENT'S POSITION:

In C, D was granted exemption under section 501(c)(3) of the Internal Revenue Code as an organization that is not a private foundation because it is described in IRC 509(a)(1) and 170(b)(1)(A)(vi). On E, the IRS issued a letter acknowledging the change in the corporate name to A. That letter indicated that A continued to qualify as an organization exempt under section 501(c)(3) of the Code as an organization that is not a private foundation because it is described in IRC 509(a)(1) and 170(b)(1)(A)(vi).

In order to comply with the provisions of IRC 501(c)(3) and to maintain its exemption from taxation, an organization must be able to demonstrate that it is operated exclusively for exempt purposes, that its income has not inured to the benefit of officers or others, that it has not been involved in any substantial way in legislative activities and that it has not intervened in any political campaign in support of or in opposition to any political candidate.

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

Regardless of the organization's requirement to file an information return, it is required to maintain adequate books and records to substantiate its claims regarding its level of income and the expenditures and to provide such additional information as may be required by the Internal Revenue Service for the purpose of inquiring into its exempt status.

Our examination showed that you conduct bingo games to raise funds to support your charitable and educational purposes. You conduct the bingo games under a contract with G who is the bingo promoter. Under the contract, G is responsible for conducting the bingo games. G set the terms of the agreement and determines the amount of bingo prizes, bingo expenses and the amount that you receive. This amount is generally the minimum \$K per month required to be distributed to you under the terms of the contract.

However, our examination revealed that the bingo promoter failed to distribute the required minimum of \$K per month. Under the terms of the contract, you should have received at least \$BB from the bingo operation for the year ended P, and you should have received at least \$CC from the bingo operation for the year ended Q. No records were provided to show that any bingo proceeds were deposited into the

charity's bank account for the year ended P, and only \$DD was deposited in the year ended Q.

Information furnished to us regarding the amount of time devoted to your bingo activities shows that approximately 20.9% of your time was devoted to bingo activities in the year ended P. Similar information furnished to us regarding the amount of time devoted to your bingo activities in the subsequent year shows that approximately 54.7% of your time was devoted to bingo activities for the year ended Q.

The bingo records showed that the bingo grossed \$242,046 in the year ended P, and the bingo grossed \$1,090,048 in the year ended Q.

Gross income from your exempt function activities was \$87,729 for the year ended P, and gross income from your exempt function activities was \$97,815 for the year ended Q.

Total gross income for the year ended P was \$329,775 and gross income for the year ended Q was \$1,187,863.

Seventy three percent (73%) of your gross income for the year ended P, and ninety two percent (92%) of your gross income for the year ended Q, came from your bingo games.

Based on our analysis, the operation of the bingo games constitutes a substantial nonexempt purpose and activity.

You are operated similar to the organizations described in Make a Joyful Noise v. Commissioner; Help the Children v. Commissioner; and P.L.L. Scholarship Fund, v. Commissioner. Those cases involved organizations engaged primarily in fund raising activities through bingo games. The courts held that neither organization qualified for exemption under section 501(c)(3) of the Internal Revenue Code because they were not operated exclusively for exempt purposes.

Because a substantial part of your activities is not in furtherance of an exempt purpose, we have determined that you are not operated exclusively for an exempt purpose pursuant to section 501(c)(3) of the Internal Revenue Code and section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations.

We have also determined that income from your bingo operation inures to the private benefit of your bingo promoter. The percentage method of compensation constitutes inurement of net earnings to private individuals which is strictly prohibited under section 501(c)(3) of the Code. The statute specifically denies tax exemption where a portion of net earnings is paid to private shareholders or individuals. (See People of God Community v. Commissioner.)

In addition, by engaging in substantial activities that serve private rather than public interests, you are not operated exclusively for one or more exempt purposes pursuant to section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations. (See Church in Boston v. Commissioner and World Family Corp. v. Commissioner.)

The total amount of income distributed to the charity from the bingo account in the years ended P, and Q, was \$0 and \$DD, respectively. The percentage of gross bingo income distributed to the charity was 0% for the year ended P, and approximately .34% of the gross bingo receipts in the years ended Q.

Based on the amount of gross bingo income that was distributed for charitable purposes, we have concluded that the amount of the proceeds received from your bingo activities to conduct charitable and educational programs is not "commensurate in scope" with the financial resources of your bingo operation. (See Revenue Ruling 64-182, 1964-1 (Part 1) C.B. 186)

Our examination also revealed that you filed Form 990 for the year ended T, late and you improperly filed Form 990EZ for the year ended P, when gross receipts exceeded \$100,000.

There is no record that any Forms 990 were filed for the years ended Q or R. Delinquency penalties and interest continue to accrue, up to the maximum allowed by law, for delinquent filing of Forms 990 for the years ended T, P, Q, or R.

During our examination, we also noted that the Form W-2 issued to your Office Manager for the calendar year ended T, was not filed with the Social Security Administration as required. There is no record showing that you paid the penalties or filed the Forms W-2 and W-3. Penalties and interest continue to accrue up to the maximum allowed by law.

Based on the multiple delinquencies, we have determined that you have failed to satisfy the conditions required for the continuation of your exempt status as required under section 6033 of the Internal Revenue Code and Revenue Ruling 59-95, Cumulative Bulletin 1959-1, page 627.

TAXPAYER'S POSITION:

Current officers maintain that they are a voluntary board and that they were not aware that all of the requirements necessary for maintaining their exempt status had not been met.

CONCLUSION:

Based on the analysis of your activities and the sources and amounts of your gross income and expenses, it has been determined that the operation of the bingo games constitutes a substantial nonexempt purpose and activity.

You are operated similar to the organizations described in Make a Joyful Noise v. Commissioner; Help the Children v. Commissioner; and P.L.L. Scholarship Fund, v. Commissioner. Those cases involved organizations engaged primarily in fund raising activities through bingo games. The courts held that neither organization qualified for exemption under section 501(c)(3) of the Internal Revenue Code because they were not operated exclusively for exempt purposes.

Based on the amount of gross bingo income that was distributed for charitable purposes, we have concluded that the amount of the proceeds received from your bingo activities to conduct charitable and educational programs is not "commensurate in scope" with the financial resources of your bingo operation. (See Revenue Ruling 64-182, 1964-1 (Part 1) C.B. 186)

Because a substantial part of your activities is not in furtherance of an exempt purpose, we have determined that you are not operated exclusively for an exempt purpose pursuant to section 501(c)(3) of the Internal Revenue Code and section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations.

We have also determined that income from your bingo operation inures to the private benefit of your bingo promoter. The percentage method of compensation constitutes inurement of net earnings to private individuals which is strictly prohibited under section 501(c)(3) of the Code. The statute specifically denies tax exemption where a portion of net earnings is paid to private shareholders or individuals. (See People of God Community v. Commissioner.)

In addition, by engaging in substantial activities that serve private rather than public interests, you are not operated exclusively for one or more exempt purposes pursuant to section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations. (See Church in Boston v. Commissioner and World Family Corp. v. Commissioner.)

Since you have not timely filed Forms 990 for the years ended T, P, Q, R, and you have not filed Form W-2 for the calendar year ended V, we have determined that you have failed to satisfy the conditions required for the continuation of your exempt status as required under section 6033 of the Internal Revenue Code and Revenue Ruling 59-95, Cumulative Bulletin 1959-1, page 627.

Based on the facts, law and conclusions cited above, we have determined that you no longer qualify for exemption under section 501(c)(3) of the Internal Revenue Code.

Therefore, your exemption under section 501(c)(3) of the Internal Revenue Code is revoked effective EE, the first day of the year that we determined that you are not operated exclusively for exempt purposes and you failed to satisfy the conditions required for the continuation of your exempt status as required under section 6033 of the Internal Revenue Code.

Contributions made to you after EE, are not deductible under section 170 of the Internal Revenue Code.

You are required to file Forms 1120 and pay Federal income tax for all years beginning after EE.