

Internal Revenue Service
Director, Exempt Organizations
Rulings and Agreements

Department of the Treasury
P.O. Box 2508 - RM 7008
Cincinnati, OH 45201

Date: [REDACTED]

Employer Identification Number:
[REDACTED]

Person to Contact - I.D. Number:
[REDACTED]

Contact Telephone Numbers:
[REDACTED] Phone
[REDACTED] FAX

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1120. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that:

A declaratory judgement 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 administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely,

[REDACTED]
[REDACTED]

Director, Exempt Organizations
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Enclosures: 3

ISSUES:

1. The organization was formed to provide a Christian retreat house. The retreats will be unsupervised. Does significant unsupervised time available at a Christian retreat constitute a religious activity that would qualify for exemption under section 501(c)(3) of the IRC?
2. The organization will use the property of the Board of Directors of the organization. This property will be maintained with the organization's income. The property will be expanded with additional houses at the organization's expense. Since the property is not owned by the organization, the property and all improvements will revert back to the incorporators when the organization terminates. Does the improvement of a related party's property constitute inurement and therefore prohibit exemption under section 501(c)(3) of the IRC?
3. The organization will pay the Board of Directors for services rendered to the organization. These salaries will be set by the Board of Directors, which is comprised of related parties. Does setting salaries by the related Board of Directors constitute inurement and therefore prohibit exemption under section 501(c)(3) of the IRC?

FACTS:

Purpose of the Organization

The organization was incorporated on [REDACTED] under the laws of the state of [REDACTED]

The organization's objective and purpose is:

- (1) The operation of a non-profit Christian retreat.

Membership

The organization shall have no members.

Activities and Additional Facts

Activities:

The activities of the organization as stated in the application for exemption include:

- (1) Inviting people to come for a day, 3 day, or 7 day stay in a cabin.
- (2) Participants will not be chaperoned during the course of their

stay and are allowed to do what they want to do.

Additional facts:

- (1) The Board of Directors is made up of three individuals. They are [REDACTED], [REDACTED] and [REDACTED]. [REDACTED] and [REDACTED] are married. [REDACTED] is a neighbor and the individual who ordained both [REDACTED] and [REDACTED]. [REDACTED] and [REDACTED] are also the owners of the property being used by the organization.
- (2) The organization will make improvements to the property owned by [REDACTED] and [REDACTED]. This includes repairs and improvements to the current building along with adding several additional buildings and recreational items to the property.
- (3) The organization will pay the Board of Directors for work performed for the organization. The organization states that [REDACTED] and [REDACTED] are currently uncompensated and that they will never be compensated for ministerial services. Eventually they will be compensated for services such as maintenance, grounds keeping, janitorial and bookkeeping. The amount of compensation will be \$[REDACTED] per hour. The related parties will set their own compensation package.
- (4) The organization was requested to amend the Articles of Incorporation to include appropriate language for Section 501(c)(3) exemption. The organization stated that they would amend the Articles of Incorporation. The Amended Articles of Incorporation filed with the state on [REDACTED] did not include appropriate language for Section 501(c)(3). Article III, the purposes for which the corporation is organized is "To minister the Gospel of Jesus Christ in order to produce disciples and increase a believers level of intimacy with our Lord and to help discover God's purpose in their life." Article VII, any provisions which the incorporators elect to set forth for the regulation of the internal affairs of the corporation, including any provision for the distribution of assets on dissolution or final liquidation is "The assets would revert back to the donors, [REDACTED] and [REDACTED] if this entity ceases to continue its ministry, in addition the [REDACTED] will continue it's public service until our Lord returns and will be operated by [REDACTED] and [REDACTED] or their de(s)cendants and and no liquidations of assets will take place before the second coming of our Lord Jesus Christ."
- (5) The organization was requested to expand the Board of Directors to include additional unrelated individuals. The

organization declined to expand the Board of Directors.

- (6) The organization was requested to sign a conflict of interest policy. The organization submitted a signed copy of the Ten Commandments as its conflict of interest policy.
- (7) The organization was requested to provide a lease agreement between the organization and the owners of the property being used. A lease was submitted. The lease calls for all expenses and improvements to be "paid by the [REDACTED] as contributions are given and future buildings."
- (8) It is also indicated that the source of funding for the organization will be donations from individuals that use the facility.
- (9) If the organization ceases to exist, all property and improvements will revert back to the owners of the property.
- (10) As previously mentioned, there is no structure to the religious retreat. The participants have religious books and videos at their disposal. Based on the response to the letter dated [REDACTED] "the only scheduled association will be the delivery of a light lunch and a(n) evening meal, otherwise the guest will be unchaperoned during the course of their stay." Therefore, participants are unsupervised for a significant part of the day.

LAW:

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

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states that, in order to be exempt as an organization described in section 501(c)(3) of the Code, an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Regulations provides that 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(b)(1)(iv) of the Regulations provides that in no case shall an organization be considered to be organized exclusively for one or more exempt purposes, if, by the terms of its articles, the purposes for which such organization is created are broader than the purposes specified in section 501(c)(3).

Section 1.501(c)(3)-1(b)(4) of the Regulations provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will be considered dedicated to an exempt purpose, for example, if, upon dissolution, such assets would, by reason of a provision in the organization's articles or by operation of law, be distributed for one or more exempt purposes, or to a State or local government, for a public purpose, or to the Federal government, or to a State or local government, for a public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgement of the court will best accomplish the general purposes for which the dissolved organization was organized.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations states that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(a)-1(c) of the Regulations states that the words "private shareholder or individual" means an individual having a personal and private interest in the activities of the organization.

In general, an organization that applies for recognition of exemption has the burden of proving that it clearly meets all the requirements of the particular section of the Code under which it has applied. See Kenner vs. Commissioner, 318 F. 2d 632 (7th Cir. 1963), and Cleveland Coral Practical College vs. Commissioner, 312 F. 2d 203, 206 (8th Cir. 1963).

Revenue Ruling 77-366 holds that a nonprofit organization that arranges and conducts winter-time ocean cruises during which activities to further religious and educational purposes are provided in addition to extensive social and recreational activities is not operated exclusively for exempt purposes and does not qualify for exemption.

Leon A. Beeghly v. Commissioner, 35 T.C. 490 (1960), provided that

where an exempt organization engages in a transaction with a related interest and there is a purpose to benefit the private interest rather than the organization, exemption may be lost even though the transaction ultimately proves profitable for the exempt organization.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 179, the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purpose.

In The Schoger Foundation v. Commissioner, 76 T.C. 380 (1981), an organization operating a religious retreat facility did not qualify for exemption under IRC 501(c)(3) because it failed to show that the retreat facility was operated exclusively for religious purposes. Although the organization's mountain lodge offered guests religious, recreational, and social activities; however, none were regularly scheduled or required. The court concluded that the organization had not met its burden of proof to show that the lodge was operated primarily for an exempt religious purpose and that the recreational and social activities at the lodge were only incidental to a religious purpose.

In Airlie Foundation, Inc v. United States of America, 312 U.S. App. D.C. 119; 55 F.3d 684; 1995 U.S. App., it was held that to be eligible for exempt status, "no part of an organization's net earnings may inure to the benefit of any private shareholder or individual." See Freedom Church of Revelation v. United States, 588 F. Supp. 693, 698 (D.D.C. 1984) (the amount or extent of the inurement or benefit is not relevant). "Private shareholder or individual" is broadly defined as any person "having a personal and private interest in the activities of the organization" and it includes the creator of the organization and his family. See Presbyterian and Reformed Publishing Co. v. Commissioner, 743 F.2d 148, 153 (3rd Cir. 1984), citing 26 C.F.R. § 1.501(a)-1(c) (1984). In addition, an organization is not operated exclusively for exempt purposes if it serves a private rather than a public interest. Easter House v. United States, 12 Cl. Ct. 476, 487 (1987), citing Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii), aff'd. without opinion, 846 F.2d 78 (Fed. Cir. 1988).

To be considered exempt under 501(c)(3), an organization must be operated for public rather than private interests. In addition, no part of the earnings of the organization can inure to the benefit of any private individual. Since the organization is improving the personal property of the incorporators, it is not operating exclusively for an exempt purpose and its activities constitute inurement. In addition, the related Board of Directors will set the salaries that they will receive for services provided to the organization. With no basis and no outside controls to confirm that salary payments will be commensurate with the work provided, there

is inurement. This will preclude exemption under section 501(c)(3) of the Code.

APPLICATION OF LAW:

Section 1.501(c)(3)-1(b)(1)(iv) of the Regulations provides that in no case shall an organization be considered to be organized exclusively for one or more exempt purposes, if, by the terms of its articles, the purposes for which such organization is created are broader than the purposes specified in section 501(c)(3). The organization's Articles of Incorporation do not state that it is organized exclusively for one or more exempt purposes.

Section 1.501(c)(3)-1(b)(4) of the Regulations provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will be considered dedicated to an exempt purpose, for example, if, upon dissolution, such assets would, by reason of a provision in the organization's articles or by operation of law, be distributed for one or more exempt purposes, or to a State or local government, for a public purpose, or to the Federal government, or to a State or local government, for a public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgement of the court will best accomplish the general purposes for which the dissolved organization was organized. The Articles of Incorporation state that the assets of the organization will revert back to the donors.

Section 501(c)(3) of the Code states that no part of the net earning of a charitable organization can inure to the benefit of any private shareholder or individual. By having the organization pay for all expenses, including improvements to a facility that is owned by the incorporators of the organization, the incorporators are benefiting substantially from the organization's funds invested in to the facility. The facilities, including all improvements will revert back to the owners if the organization ceases to exist as stated in the Articles of Incorporation.

In addition, the organization will be paying the board of directors for work performed around the facility. The board of directors will decide on their own salaries. Two out of three members of the board of directors are related.

There is a strict prohibition against inurement and private benefit under IRC 501(c)(3). Burden of proof is upon the taxpayer to prove that the organization is operating for a public rather than a private interest and that no inurement or private benefit exists. The organization has clearly not done this.

[REDACTED]

In The Schoger Foundation v. Commissioner, 76 T.C. 380 (1981), an organization operating a religious retreat facility did not qualify for exemption under IRC 501(c)(3) because it failed to show that the retreat facility was operated exclusively for religious purposes.

Revenue Ruling 77-366 discusses a religious organization which operated a retreat. This organization, similar to your organization, allows its participants significant unsupervised time. This spare time can be used, at the discretion of the participant, to do as the participant desires. Your organization has no structured religious activities. The participants in the retreat are unsupervised for the entire time that they are at the facility.

APPLICANT'S POSITION:

The organization has responded to the fact of significant unsupervised time available by stating that there is no unsupervised time. The organization stated "our guests are chaperoned 24 hours a day either by [REDACTED] and myself or the Holy Spirit of God." In addition, the organization stated that no social or recreational activities are scheduled into its functions.

The organization has responded to the inurement issue by stating "the [REDACTED] is our Inheritance given to us by God and to our descendants to be caretakers of the [REDACTED]. As the functions of this facility is solely to benefit the public at large."

SERVICE RESPONSE TO APPLICANT'S POSITION:

The organization has not met the organizational test for exemption under section 501(c)(3). Section 1.501(c)(3)-1(b)(1)(iv) of the Regulations provides that in no case shall an organization be considered to be organized exclusively for one or more exempt purposes, if, by the terms of its articles, the purposes for which such organization is created are broader than the purposes specified in section 501(c)(3).

Section 1.501(c)(3)-1(b)(4) of the Regulations provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. An organization's assets will be considered dedicated to an exempt purpose, for example, if, upon dissolution, such assets would, by reason of a provision in the organization's articles or by operation of law, be distributed for one or more exempt purposes, or to a State or local government, for a public purpose, or to the Federal government, or to a State or local government, for a public purpose, or would be distributed by a court to another organization to be used in such manner as in the judgement of the court will best accomplish the general purposes for which the dissolved organization

was organized. The organization's dissolution clause in its Articles of Incorporation state that assets will revert back to the donors, [REDACTED] and [REDACTED].

As stated in the response of [REDACTED], item 6, the organization stated "The [REDACTED] will operate on a on-call basis, as a guest requests spiritual guidance as we share the same premises. The only scheduled association will be the delivery of a light lunch and a evening meal, otherwise the guest will be unchaperoned during the course of their stay." The organization has not satisfied the problem of unsupervised time of the participants. The organization stated that no social or recreational activities are scheduled. As much as this is true, there are no religious activities scheduled either. The participants time is significantly unsupervised. The participants are able to do the activities, whether religious, social or recreational, as they wish.

The organization's response to the inurement issue does not respond to the issue. The property that the organization will maintain and improve is still owned by two of the organization's related board of directors. All improvements made to the property will revert back to the owners upon the dissolution of the organization. Based on the organizations response of [REDACTED] the organization plans to build 7 additional guesthouses, plus shelters, basketball and tennis courts.

CONCLUSION:

In view of the foregoing, we conclude that the principal benefits arising from your activity of providing a retreat house accrue to the Board of Directors. In addition, the requirement that an organization providing religious retreat activities must solely be related to a religious activity has not been fulfilled. Therefore the requirement of section 1.501(c)(3)-1(d)(1)(ii) of the regulations that an exempt organization must serve a public rather than a private interest is not satisfied.