

Internal Revenue Service  
Director, Exempt Organizations

Department of the Treasury  
P.O. Box 2508 - Room 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 1041 if you are a Trust, or Form 1120 if you are a corporation or an unincorporated association. 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.

[REDACTED]

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 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 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]

Director, Exempt Organizations

Enclosures:

Enclosure I  
Form 6018  
Publication 892

## ENCLOSURE I

### Facts

The evidence presented shows that it appears that you were incorporated in the State of [REDACTED]; however no official filing receipt stamp on the articles was submitted. The articles you have submitted were also not signed. Your incorporator is [REDACTED]. You did submit a declaration that the copy of your articles you submitted was filed with the State of [REDACTED].

You also submitted amended articles that indicate the organization filed a Business Entity Amendment Filing in the name of [REDACTED]. The certificate indicates the organization was formed as a Domestic Non-Profit Corp in the State of [REDACTED].

The purpose of which this organization was formed is exclusively for charitable, religious, educational and scientific purposes.

The organization is formed as a membership organization open to the public.

You indicated in your application that you would "repair homes, acquire mortgages and/or notes and in turn would sell the notes.

In your reply to our letter of [REDACTED] you indicated you may do repair to dwellings with a serviced fee determined by the Applicant's income, credit history, cost associated with their current living expense. Additional services include a Data Entry Service, Credit Counseling and Tax Preparation Service.

Under Exhibit A, Part 2, you listed Owner Financing, conducted by the Administrator.

In this same reply, your Flyers indicate purchase criteria, and advertisements. One flyer indicates "Purchase Your Dream Home", "use my money", "just pay me back". Your advertisement goes on to end "Sincerely, Private Investor".

One brochure indicates an individual may submit a Residential Application and receive up to \$[REDACTED] in down payment and/or closing cost assistance is available.

In our letter of [REDACTED] we asked if the organization was providing down payment assistance and how you were operating in a charitable manner.

In your reply of [REDACTED] you indicated you are exempt because your clients are either of low income, handicapped or of moderate income facing stressors such as homelessness due to fire or illness. In addition, repair assistance must be limited to owner occupants or clients seeking to achieve ownership or tenancy.

FIN: [REDACTED]

You stated your housing stock will be obtained from townships or municipalities with abandoned or distressed unites or from Federal Housing Listings (HUD,VA USDA) or at below market rate on Multiple Listing Services or from Owners wishing to dispose of homes.

You also indicated they may be no down payment assistance however, seller concession may be available per banking guidelines which allows [REDACTED] % seller's concession toward Buyers closing cost on conventional mortgages or [REDACTED] % seller's concession towards Buyers closing cost on FHA or Fannie Mac approved financing.

Down Payment or closing cost assistance is available for buyers up to \$ [REDACTED] per non-profit organizations.

Mortgages will be sold at settlement to allow immediate cash flow. Notes are sold once legally matured and marketed through a network or registered investors with a multitude of financial cost then sold at [REDACTED] % of face value depending on interest rate of mortgage usually to realize immediate case.

You indicated that you would provide Credit Repair Assistance/Counseling by Board Members or its officers. Mainly to run credit reports with counseling preformed by your President, [REDACTED] to purchase a residence. That is your hope to place individuals for purchase or rental properties.

Other fees charged (credit reports, data entry and tax preparation) are determined by the cost to perform the service. The credit counseling will be included in the housing search, which will generate a commission to the individual commercial licensee. You indicate [REDACTED] % of time will be devoted to credit repair in hopes of securing a transaction, [REDACTED] % of time will be spent on Data Entry, Work Processing and Tax preparation Services.

Also in your statement of proposed activities, you state the criteria that a home buyer must meet to qualify for assistance from you as follows:

- "1. Selected Habitat must be within Borrower's budget;
- "2. Combined Credit Score must be 500 or higher;
- "3. Credit Report Fee \$ [REDACTED] to be "Paid" prior to application process is executed;
- "4. Purchase Price Range: No lower than \$ [REDACTED] and no higher than \$ [REDACTED] (No Exceptions) based on Income & Debt Ratio.
- "5. Owner Occupants Only. (Purchaser must reside in unite for a minimum of 60 months);

FIN: [REDACTED]

"6. 30-Day Settlement upon executed Agreement to Purchase unless seller or purchases defaults or a cash transaction.

"7. At least 2 active trade Lines (Rent is an acceptable trade line).

"8. All properties must be appraised by a State: Bonded: Licensed Appraiser (Should consideration exceed \$ [REDACTED] a second State Bonded Appraisal must be allowed)

9" Debt Ration [REDACTED] % or less

10" Compliance with Federal, State and Local Laws.

The organization currently has one employee, [REDACTED], in addition to board members who volunteer services "at this time". In the future, you indicated it may be necessary to utilize board members or relatives for staff duties if no other employee can be retained with the limited amount of funds

You also indicate the organization has had gross receipts under \$ [REDACTED]. In your reply of [REDACTED] you indicated an additional user fee of \$ [REDACTED] is not due and have reported the income from the organization on [REDACTED] tax return. Although a budget was submitted, a revised budget was requested based on the activities the organization would conduct. You stated it is impossible to project a future budget for [REDACTED] and [REDACTED]. However, you included a breakdown of fees charged for tax preparation \$ [REDACTED] an hour, data entry \$ [REDACTED] per hour, Word Processing Service \$ [REDACTED].

We also requested sample contracts the organization would use. Blank forms were submitted that are used for purchasing and selling of property. One blank form was for the real estate broker to use in buying, selling the property.

Based upon your proposed sources of support, you claim status as an organization described in sections 509(a)(1) and 170(b)(1)(A)(vi) of the Code.

Your biographical information indicates the [REDACTED] is a licensed Realtor and active Salesperson at [REDACTED].

In your reply of [REDACTED] you submitted [REDACTED] Income tax return. You indicated an Internal Revenue Code employee advised you to report the income from this organization on your Personal Income Tax Return. Your Schedule C showed the business name as [REDACTED].

#### Law

Section 501(a) of the Internal Revenue Code of 1986 provides for the exemption from federal income tax for organizations described in Section 501(c)(3). Such organizations are recognized as exempt if

FIN: [REDACTED]

they are organized and operated exclusively for religious, charitable, and educational purposes.

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) of the Code. 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(d)(2) of 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 lessening of the burdens of government.

Section 1.501(c)(3)-1(e) of the regulations provides that an organization may meet the requirements of section 501(c)(3) if it operates a trade or business that is in furtherance of its exempt purposes but not if it is operated for the primary purpose of carrying on an unrelated trade of business as defined in section 513 of the Code.

In International Postgraduate Medical Foundation v. Commissioner, TCM 1989-36, the Tax Court considered the qualification for exemption under section 501(c)(3) of the Code of a nonprofit corporation that conducted continuing medical education tours. Michael Helin, trustee and executive director of the nonprofit corporation, was also a shareholder and president of H & C Tours, a travel agency. The foundation used H & C Tours exclusively for all travel arrangements. The foundation did not solicit competitive bids from any entity other than H & C Tours. In holding, the foundation not to be exempt, the court stated:

When a for profit organization benefits substantially from the manner in which the activities of a related organization are carried on, the latter organization is not operated exclusively for exempt purposes within the meaning of section 501(c)(3), even if it furthers other exempt purposes.

In Church By Mail Inc v. Commissioner, 765, F2d 1387 (9<sup>th</sup> Cir, 1985) the court determined that an organization whose board members had interrelationships with related for-profit entities had the potential for abuse through manipulation of the arrangements between those

FIN: [REDACTED]

entities and were operated in furtherance of the board members. On these bases, the Court concluded that the organization could not qualify for exemption under section 501(c)(3) of the code. In deciding for the government, the Court made the following statement:

There is ample evidence in the record to support the Tax Court's finding that the Church was operated for the substantial non-exempt purpose of providing a market for Twentieth's services. The employees of Twentieth spend two-thirds of their time working on the services provided to the Church. The majority of the Church's income is paid to Twentieth to cover repayments on loan principal, interest, and commissions. Finally, the potential for abuse created by the ministers' control of the Church requires open and candid disclosure of facts bearing upon the exemption application. Moreover, the ministers' dual control of both the Church and Twentieth enable them to profit from the affiliation of the two entities through increased compensation.

In est of Hawaii v. Commissioner, 71 T.C. 1067 (1979), several for-profit est organizations exerted significant indirect control over est of Hawaii, a nonprofit entity, through contractual arrangements. The Tax Court concluded that the for-profits were able to use the nonprofit as an "instrument" to further their for-profit purposes. Neither the fact that the for-profits lacked structural control over the organization nor the fact that amounts paid to the for-profit organizations under the contracts were reasonable affected the court's conclusion that est of Hawaii did not qualify as an organization described in section 501(c)(3) of the Code.

In 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.

Revenue Ruling 70-585, 1970-2 C.B. 115 provides advice whether nonprofit organizations created to provide housing for low or moderate income families under federal and State programs qualify for exemption from federal income tax as charitable organizations described in section 501(c)(3) of the Code. In situation 1 in that ruling, an organization was held to be exempt under section 501(c)(3) where it limited its housing activities to low income families. The organization in that situation obtained operating funds from federal loans and contributions from the general public, and used volunteer help for some of its housing activities. Conversely, in situation 4 of that ruling, an organization operated to assist families with moderate income erect and occupy affordable homes did not qualify since its activities were not designed to provide relief to the poor or to carry out any other charitable purpose within the meaning of section 501(c)(3). The organization in situation 4 was financed by federal and State programs and contributions from the general public.

FIN: [REDACTED]

Revenue Ruling 61-170, 1961-1 C.B. 112, holds that an association composed of professional private duty nurses and practical nurses which supported and operated a nurses' registry primarily to afford greater employment opportunities for its members was not entitled to exemption under section 501(c)(3) of the Code. Although the public received some benefit from the organization's activities, the primary benefit of these activities was to the organization's members.

Revenue Ruling 76-206, 1976-1 C.B. 154 described an organization formed for the purpose of promoting the broadcasting of classical music in a particular community. The organization accomplished its purpose by engaging in a variety of activities designed to stimulate public interest in the classical music programs of a for-profit station. These activities included soliciting sponsors, soliciting subscriptions to the station's program guide, and distributing pamphlets and bumper stickers encouraging people to listen to the station. The organization's board of directors represented the community at large and did not include any representatives of the for-profit radio station. The ruling concluded that the organization's activities enabled the radio station to increase its total revenues and therefore benefited the for-profit radio station in more than an incidental way. Therefore, the organization was serving a private rather than a public interest and did not qualify for exemption.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 179 (1945), 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 purposes.

In United States v. Wells Fargo Bank, 485 U.S. 351, 108 S. Ct. 1179, 99 L. Ed. 2d 368 (1900) the Supreme Court held that an organization must prove unambiguously that it qualifies for a tax exemption.

In Harding Hospital, Inc. v. United States, 505 F2d 1068 (1974), the court held that an organization seeking a ruling as to recognition of its tax exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute. Whether an organization has satisfied the operational test is a question of fact.

In Old Dominion Box Co. v. United States, 477 F2d 344 (4<sup>th</sup> Cir. 1973) cert. denied 413 U.S. 910 (1973), the court held that operating for the benefit of private parties constitutes a substantial non-exempt purpose.

In Christian Stewardship Assistance, Inc. v. Commissioner, 70 T.C. 1037, the organization's sole purpose was to assist religious, educational and/or other nonprofit organizations in the application of Christian stewardship principles. In furtherance of these purposes, the organization was engaged in financial counseling by providing a financial planning service to wealthy individuals whose net worth exceeded one-half million dollars. These financial planning services were also performed for the directors and major officers of the Christian organizations. The organization prepared a financial plan



FIN: [REDACTED]

for a contributor that took into account his personal goals and the applicable tax savings. The financial plan was developed to permit increased current or deferred donations by rearranging the *inter vivos* or testamentary disposition of the individuals' assets to family members. The rearrangement also resulted in a reduction of Federal income and estate taxes.

The Court concluded that the organization failed the operational test because the financial advice to contributors was a nonexempt purpose that was greater than the exempt purpose:

"The activity of the organization consists of advice on income and estate tax planning to reduce the individual's liability for taxes to a minimum. Regardless of how this advice is characterized, it is advice which assists wealthy individuals in reducing their tax burden. This is the primary effect of the advice given. This serves the private interests of individuals rather than a broad public interest."

Similarly, the Court concluded in American Campaign Academy v. Commissioner, 92 T.C. 1053, that the petitioner was operated for the benefit of private interests and consequently, not entitled to exemption. The organization was incorporated by the General Counsel of the National Republican Congressional Committee. Funding for the school's activities had been provided exclusively by the National Republican Congressional Trust, an organization that collected political contributions approved by the Federal Election Commission.

As its primary activity, the organization operated a school to train individuals for careers as political campaign professionals. A campaign professional worked for a candidate and typically occupied such strategic campaign positions as communications director, finance director, or campaign manager. To the "best" that the organization could determine, these graduates served on campaigns of candidates who were predominantly affiliated with the Republican party. No specific example of a graduate working for a Democratic Senatorial or Congressional candidate was offered. The Court concluded that the organization's activities benefited Republican Party entities and candidates more than incidentally.

#### Application OF Law

The facts in this case indicate that [REDACTED] is the driving force behind the project and that the remainder of your board of directors is only passively involved.

It appears you were created to allow [REDACTED] to provide herself compensation. Your operations result in substantial private benefit to her and are not incidental to the operation of a charitable organization. In this regard, you are similar to the organizations discussed in Leon A. Beeghly and est of Hawaii, supra.

FIN: [REDACTED]

Like the organization in International Postgraduate Medical Foundation v. Commissioner, supra, and Church by Mail, supra, you have contracted for services with individuals who directly controls your operations. You are similar to the organization in International Postgraduate Medical Foundation v. Commissioner because [REDACTED] benefit substantially from the manner in which your activities are carried on.

In order for private benefit to be present, it is not required that payments services to [REDACTED] be unreasonable or exceed fair market value. In est of Hawaii, the Tax Court stated:

"nor can we agree with petitioner that the critical inquiry is whether the payments made to International were reasonable or excessive. Regardless of whether the payments made by petitioner to International were excessive, International and Est, Inc., benefited substantially from the operation of petitioner."

Also, in Church by Mail, supra, the Church argued that the compensation to the for-profit was reasonable. The Court's statement on the subject is very significant.

The Church exaggerates the importance of the contracts. The critical inquiry is not whether particular contractual payments to a related for-profit organization are reasonable or excessive, but instead whether the entire enterprise is carried on in such a manner that the for-profit benefits substantially from the operation.

In est of Hawaii, supra, and Church by Mail, supra, the organization procured services from for-profit entities. Although there was no structural relationship between the entities, the Court inferred from the totality of benefits flowing from the exempt organizations to the for-profit organizations that they had substantial influence over the nonprofit organizations operations. Your situation is more egregious in that there is a direct relationship between you and your President, [REDACTED]. She would benefit substantially from your operations.

While you meet the organizational test of section 501(c)(3), you are operated for the "substantial" purpose of benefiting [REDACTED]. The presence of a single non-exempt purpose, if "substantial" in nature, will destroy a claim for exemption regardless of the number of importance of truly exempt purposes. Better Business Bureau of Washington, supra.

You indicate you intend to pay income to your officer, [REDACTED] and whom is your incorporator, for services they may earn as your employees. Also, you have not indicated that commissions will be paid; however, you have claimed income from the organization on [REDACTED] Form 1040, Schedule C. While an organization may pay reasonable compensation for services rendered to it, it appears that one of the purposes for your incorporation was to provide employment and income opportunities for particular individuals. [REDACTED] would be paid as staff, may receive commissions and receives fees for

FIN: [REDACTED]

services for providing services for homebuyers. Providing benefits to private persons not members of a charitable class is not a charitable activity and you are therefore not operated exclusively for charitable purposes.

### Conclusion

To determine whether the operational test is satisfied, section 1.503(c)(3)-1(c)(1) of the Regulations directs the Service to determine if the organization engages primarily in activities which accomplish one or more exempt purposes. Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations expands on the "operated exclusively" concept by providing that an organization is not operated exclusively to further exempt purposes unless it serves a public rather than a private interest.

Based on the facts and circumstances provided to date, it appears that you are not operated exclusively for public rather for private purposes. Your activities clearly further the private interests of [REDACTED]. The fact that your activities may further some truly charitable purposes (i.e., provisions of low-income housing, repair to homes owned by a charitable class) does not detract from the existence of the "substantial non-exempt purpose" of benefiting [REDACTED].

In addition, buying and selling mortgages on the open market does not serve a charitable purpose but is conducting a regular business and is not an exempt purpose. As in Better Business Bureau of Washington, supra, 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 purposes.

Because you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

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