

Internal Revenue Service

Department of the Treasury

District
Director

31 Hopkins Plaza
Baltimore, MD 21201

Person to Contact:

Telephone Number:

Refer Reply to:

EP/EO:T
Date:

CERTIFIED MAIL

AUG 20 1990

Dear Applicant:

We have completed our review of the application for recognition of exemption from federal income tax under section 501(c)(3) and your request for classification as a "church" within the meaning of the Internal Revenue Code.

You indicated in your application and supporting documents that you were incorporated [REDACTED], under the laws of [REDACTED] to provide through the framework of your membership, hierarchy and other levels of organization opportunities which will enable you individual members to learn and apply the principles, teachings, doctrines, philosophy and beliefs of the [REDACTED].

On [REDACTED], you filed an amendment to your Articles of Incorporation that stated that your organization was organized exclusively for religious, educational and other stated purposes within the meaning of section 501(c)(3) of the Code and provided for the adequate distribution of your assets in the event your organization dissolved.

Your activities, as stated in your original application filed include Sunday worship, [REDACTED], Prayer meetings, bible study and outreach bible study.

Income to your organization comes from tithes and offerings. Expenses have been incurred for lease expenses, including building maintenance, utilities, renovations and repairs, contributions, advertising and furnishings.

In your original application filed on [REDACTED], you stated that you hold regular religious services in a facility that is jointly owned by your pastor and her spouse with one floor of the facility being leased to the church at no rental charge. The property consists of an apartment complex in which [REDACTED] units are rented to private individuals as residences. Rent is paid to the pastor and her spouse for these facilities. A separate portion of one unit is being leased to the [REDACTED] of which the pastor is the founder. Under the terms of the lease agreement, although no rent is paid to the founder, the Church is responsible for payment of repairs, renovations, utilities and upkeep of this property.

Membership in your organization consisted of [redacted] individuals representing [redacted] to [redacted] families in [redacted]. In [redacted] you state your membership is [redacted] members. You have not provided us with any detailed information on how you expect to expand your congregation within the near future other than by "word of mouth" and through "distribution of business cards" nor have you provided us with any criteria regarding how future compensation for the pastor will be determined once finances permit.

During the years [redacted], contributions were received from your pastor and spouse totalling \$[redacted]. For the period [redacted], an additional \$[redacted] was contributed by them.

You also state in your application that an oral agreement was made between the congregation and pastor in [redacted] to pay \$[redacted] per month rent for any vacant apartment within the building where your organization holds its services. During [redacted], these payments amounted to approximately \$[redacted]. No other data for [redacted] or [redacted] has been supplied.

Your financial statements also show that cash grants were made for mortgage payments, electricity and funeral expenses for members of your congregation. You have not provided the criteria used to determine who would receive this assistance or the reason for the grant other than for mortgage payments, electricity, and similar expenses.

Your [redacted] financial statement shows two loans made to your treasurer, [redacted]. These loans were in the amount of \$[redacted] and \$[redacted] and were to be repaid at [redacted]% interest. The purpose of these loans were primarily a business purpose of providing financial assistance for his bookstore. [redacted] serves as an officer of your organization and is also one of the two signature authorities of the church checking account.

During the period [redacted], your application states that [redacted] contributed \$[redacted] to [redacted]. During the period [redacted], a total of \$[redacted] was donated to your organization by [redacted] with \$[redacted] being returned to him in [redacted] in the form of loans at a below market favorable interest rate.

Section 501(c)(3) of the Internal Revenue Code provides for the exemption from Federal income tax of organizations organized and operated exclusively for religious, charitable and other stated purposes.

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

Regulations section 1.501(c)(3)-1(b)(1) specifies that an organization is organized exclusively for one or more exempt purposes only if its Articles of Organization limit the purposes of such organization to 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 purposes, unless its assets, upon dissolution, are dedicated to 501(c)(3) purposes.

Regulations section 1.501(c)(3)-1(c)(1) stipulates that an organization will be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish any of the activities 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(d)(1)(ii) of the regulations state that an organization is not organized or operated exclusively for exempt purposes unless it serves public rather than private interests. Thus, to meet the requirement of this section, it is necessary for the 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, or persons controlled directly or indirectly by such private interests.

Section 170(a) of the Internal Revenue Code allows as a deduction any "charitable contribution... payment of which is made within the taxable year. For purposes of this section, IRC 170(c) states that a charitable contribution is a contribution or gift to or for the use of a corporation, trust, community chest, fund or foundation, created or organized in the United States or in any possession thereof or under the law of the United States, any State, the District of Columbia, or any possession of the United States organized and operated exclusively for religious, charitable, educational and other state purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

The term charitable contribution as it is used generally in section 170 is largely synonymous with the term "gift". See *v. Commissioner*, 57 T.C. 265, 275 (1971). A gift is generally defined as a voluntary transfer of property to another without consideration.

In *Western Catholic Church v. Commissioner*, 73 T.C. 196, 211 (1979), the Tax Court reviewed an organization where a section 501(c)(3) entity made grants and loans to private individuals. The court examined the criteria used by the organization in determining the recipients of these disbursements and found that the organization had no established criteria for awarding the grants and loans. The court stated that grants made by an exempt organization on a personal basis without objective, non-discriminatory criteria constitutes inurement of benefit to private individuals.

[REDACTED]

In Church in Boston, 71 T.C., 102, (1978), an organization was organized as a religious entity and it used a substantial portion of its receipts for making grants of cash to individuals, including its officers and members, based upon no fixed criteria and with no provision for repayment. The Tax Court held in this case that the organization was not entitled to exempt status under section 501(c)(3). Although the organization stated that it furthered a charitable purpose to assist the poor who were in need of food, clothing, shelter and medical attention, the organization was unable to furnish any documented criteria which demonstrated the selection process of a deserving recipient, the reason for specific amounts given or the purpose of the grant. The only documentation contained in the file was a list of grants made which included the name of the recipient, the amount of the grant and the "reason" for the grant which was merely a list showing unemployment, medical expenses, food or other similar personal type items. Because of this lack of documented criteria for the selection process, the service was unable to determine whether the grants were made in an objective and non-discriminatory manner and whether the distribution of the grant was made in furtherance of an exempt purpose. The court also stated that the grants constituted inurement of benefits to private individuals.

In Founding Church of Scientology, supra, 188, Ct. Cl. at 499, 412F 2d at 1202, the court stated: "the very existence of a private source of loan credit from an organization's earnings may itself amount to inurement of benefit." And this is all the more true where the loans are without interest (or at rates more favorable than market). Lowry Hospital Association v. Commissioner, 66 T.C. 850, 858 (1959).

To qualify for exemption under section 501(c)(3), the applicant organization has the burden of showing, (1) that it is organized and operated exclusively for religious or other stated purposes, (2) that no part of its net earnings inured to the benefit of a private individual or shareholder, and (3) that no substantial part of its activities consisted of the dissemination of propaganda or otherwise attempting to influence legislation or engaging in political activity, National Association of American Churches v. Commissioner, 82 T.C. 18 (1984).

We have reviewed the activities of your organization and have determined that while some of your activities serve religious purposes, your organization has used substantial portions of the funds received for permanent improvements to

property legally owned by your pastor and spouse. During the years [REDACTED], your organization received contributions in the amount of \$[REDACTED]. Of this amount, approximately \$[REDACTED] was expended for lease expenses, \$[REDACTED] in [REDACTED], \$[REDACTED] in [REDACTED], \$[REDACTED] in [REDACTED] and \$[REDACTED] in [REDACTED]. Under the terms of the lease agreement submitted, this means that these funds were used for repairs and renovations to property that is legally owned by your pastor and spouse. In addition, during [REDACTED], you state that funds were allocated from church monies to pay rent for vacant apartments within the building whenever a vacancy occurred. You state in [REDACTED], this amounted to approximately \$[REDACTED].

[REDACTED]

The record also shows that personal loans were made to the treasurer of your organization, [REDACTED], for business purposes rather than for exclusively religious or charitable purposes. These funds were loaned to him at a rate of interest of [REDACTED]% which is less than he would have had to pay at a commercial lending institution. [REDACTED] is also one of the two signatories on the church checking account and maintains control over the funds collected. Under the circumstances of the financial arrangements made between the church and [REDACTED], any contributions he may have made to the organization could not be considered "charitable" contributions. While [REDACTED] donated funds to the [REDACTED], it appears that he did not relinquish control of these monies since he was in a position as treasurer and signatory on the church checking account to use these funds for any purpose he needed, including making a personal loan to himself. Your pastor has also received considerable benefit from the contributions made to [REDACTED] in the form of permanent improvements to privately owned property and rent subsidies for the vacant apartments.

Your grant program as described in your application where you made cash disbursements for personal type expenses for mortgage \$[REDACTED], electricity \$[REDACTED], and funeral expenses \$[REDACTED], does not show that you had established in advance any fixed criteria for determining who would be selected, the purposes for which grants would be made or any limitations on the grants upon which it could be determined that these grants were given on an objective and non-discriminatory basis.

While you also state that you expect to expand your membership, it appears that although you have been in existence since [REDACTED], you still have the same members and number of members after six years of operations with no apparent growth or expansion in your membership. This indicates that you are not operated for a public purpose.

Therefore, based on the information submitted, we have determined that while your organization's articles of incorporation meet the organizational test to be exempt, your activities are not exclusively religious and charitable and a significant portion of your financial support serves the private interests of your pastor, spouse, treasurer and other specified members. As a result of these arrangements, your net earnings inure to the benefit of private individuals and your organization serves private rather than public purposes.

You are not entitled to exemption under section 501(c)(3) and are a taxable entity. You are required to file federal income tax returns on Form 1120.

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

[REDACTED]

If you do not agree with our determination, you may request consideration of this matter by the Office of Regional Director of Appeals. To do this, you should file a written appeal as explained in the enclosed Publication 892. Your appeal should give the facts, law, and any other information to support your position. If you want a hearing, please request it when you file your appeal and you will be contacted to arrange a date. The hearing may be held at the regional office, or, if you request, at any mutually convenient district office. If you will be represented by someone who is not one of your principal officers, that person will need to file a power of attorney or tax information authorization with us.

If you do not appeal this determination within 30 days from the date of this letter, as explained in the enclosed Publication 892, this will become our final determination on this matter. In accordance with section 6104(c) of the Code, we are notifying the appropriate state officials of this determination. Further, if you do not appeal this determination within the time provided, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) 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."

Sincerely yours,

[REDACTED]
Acting District Director

Enclosure: Publication 892

cc: State Attorney General ([REDACTED])

cc: [REDACTED] (POA)