



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE: EO Examination

625 Fulton Street, Room 503

Brooklyn, NY 11201

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Release Number: 200726032

Release Date: 6/29/07

UIL: 501.03-01

Date: 3/23/07

Taxpayer Identification Number:  
Person to Contact:

Identification Number

Contact Telephone Number:

LAST DATE FOR FILING A PLEADING  
WITH THE TAX COURT, THE CLAIMS  
COURT, OR THE UNITED STATES  
DISTRICT COURT FOR THE DISTRICT  
OF COLUMBIA:

Dear :

This is a final determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). Recognition of your exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3) is retroactively revoked to because it is determined that you are not operated exclusively for an exempt purpose.

IRC 501(c)(3) exempts from taxation organizations which are organized and operated exclusively for charitable or educational purposes, no part of the net earnings of which inure 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 and which do not participate in, or intervene in, any political campaign on behalf of (or in opposition to) any candidate for public office.

We have determined that you are not operating exclusively for charitable or educational purposes. Our examination reveals that you are not conducting charitable or educational activities pursuant IRC section 501(c)(3), and that you failed to meet the "operational test" under Treas. Regs. 1.501(c)(3)-1(d)(ii).

- 3 -

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

Sincerely Yours,

Enclosure:  
Publication 892

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
<b>Name of Taxpayer</b>		<b>Year/Period Ended</b>

Legend:

- A = Name of the Organization
- B = Taxpayer Identification Number
- BB = Taxpayer Identification Number
- C = Tax Year Ended
- D = Acronym (Organization's Name)
- E = State Name
- F = Date of Exemption Letter
- G = Date Advance Ruling Period Ended
- H = Date Reclassified to Private Foundation
- I = Founder and Manger
- J = Founder and Manager
- K = Founder's Friend
- L =
- M = Purchaser's Name
- N = Owner's Name
- O =
- P =
- Q = Checking Account Number
- R = Name of Bank
- S = IRS Agent's Name

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No.
Name of Taxpayer		Year Ended

**ISSUE:**

Has the A (D) met the requirements for tax exempt status under section 501(c) (3) of the Internal Revenue Code?

**FACTS:**

**Background of D**

A, Employer Identification Number ("EIN") BB, was incorporated in as a nonprofit corporation in the State of E. In its Articles of Incorporation, D stated its specific purpose as follows:

*"To provide food, shelter, job training & child care to battered women."*

D filed Form 1023, Application for Recognition of Exemption under Section 501(c) (3) of the Internal Revenue Code, on January 14, 1999. The activities and operational information as described in the Form 1023 were:

*"We plan to provide the following to Battered women & youth*

- 1. Food*
- 2. Clothing*
- 3. Shelter*
- 4. Childcare*
- 5. Job training*
- 6. Computer literacy training*
- 7. Habilitation-related services as counseling etc. and other youth services.*

*B. These activities were initiated in December 1997*

*C. The activities will be conducted in the city of to all women in the communities that need the services. The activity will be conducted by A."*

The Internal Revenue Service determined that D could be treated as a publicly supported organization described under Internal Revenue Code sections 509(a) (1) on F. The advance ruling period ended on G. On H, the Internal Revenue Service reclassified D as a private foundation because D did not provide support schedules indicating it received public support during its advance ruling period.

**Management**

Form 886-A	EXPLANATION OF ITEMS	Schedule or Exhibit No.
Name of Taxpayer		Year Ended

I founded and manages the organization. She received compensation in various amounts depending on the organization's financial abilities. According to the returns 990, J received \$ in year O and \$ in year P. A review of the financial records indicated that the organization paid \$ in year O. J explained that she paid over \$ worth of cell phone bill and other utilities from her personal money.

**Activities**

The primary activities engaged in by D during the year 2000 and thereafter were to purchase properties from the Department of Housing and Urban Development, rehabilitate, rent out, and sell the properties to the highest bidder at fair market value. Agent S conducted interview with , I on December 15, 2005. I described the organization's history and activities as follows:

*I founded the organization and planed to open a shelter in December 1997. Due to the financial difficulties to open and run a shelter, the organization has not opened a shelter. J learned about the L project from friend, K, a contractor. The organization applied for the L project in late 2000 and bought about eleven properties with the help from K in late year 2000 and early year of 2001. After the purchase, J obtained loans for the purchase and rehabilitation of the properties from financial institutions. Most of the loans were from All E Funding. The lending company used its own company, to inspect the properties and to determine the required rehabilitation. K and his workers rehabilitated the properties. Right after the organization purchased the properties, the project was terminated by L because it broke the L policy not to purchase more than three properties within six months.*

*After rehabilitation, the organization rented out the properties. The rental income was not enough to cover the mortgages because the initial interest rate was around 15 percent. The organization refinanced the mortgages at 10-11 percent.*

*J managed the properties by . Some properties were rented to Section 8 tenants and some were rented to the available applicants depending on the locations. It is better to rent to Section 8 tenants if the property is in bad areas because Section 8 paid at fair market value and the payments were certain. The organization applied for Section 8 for some properties. After approved by Section 8, the organization put the properties on the Section 8 list. The Section 8 tenants called J to rent the properties. After , J approved the application, Housing authority agency sent the application's package to J. Housing authority agency inspected the properties and checked the tenants annually. Section 8 paid major portion of the rents and the tenants paid around 10-15 percent of the rents.*

<b>Form 886-A</b>	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer</b>		<b>Year Ended</b>

*K helped the organization to sell two or three properties and evenly split the profit with the organization. The organization sold six properties in O. Currently, there is one property renting out. J received calls from potential buyers referred by the workers who rehabilitated the properties or learned the properties from the financial institutes. J sold the properties at the market values to the individual with highest bid. The profits from selling the properties were enough to cover the losses from renting of the properties.*

According to the records provided by J, D purchased seven properties from L and sold six properties in O; the summary of the property transactions was as follows:

Property Address	Purchase Day	Purchase Price	Sold Day	Sold Price	Buyer
		\$		\$	M
		\$		\$	M
		\$		\$	
		\$		\$	K
		\$		\$	K
		\$		\$	K
		\$			

According to the property deeds records from Accurint.com, the properties were purchase by M were owned by N., a for profit company owned by J. J stated that M was her friend and worked as an intermediary to earn \$ for the two properties transactions.

According to the property deeds records from Accurint.com, the organization purchased 11 properties from L and resold them. The 11 properties included the seven properties listed above. The other four properties sold in year 2001. The summary of the four property transactions was as follows:

<b>Form 886-A</b>	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer</b>		<b>Year Ended</b>

Property Address	Purchase Day	Purchase Price	Sold Day	Sold Price	Buyer
		\$		\$	
		\$		\$	
		\$		\$	
		\$		\$	

**Financial information**

D filed 990 returns for 2001 and 2002 and 990-PF for O and P. The summary of return 990-PF for years O and P as follows:

	O	P	Total
Net gain from sale of assets	\$	\$	\$
Rental Income	\$	\$	\$
Total revenue	\$	\$	\$
Compensation of officers	\$	\$	\$
Rental expenses	\$	\$	\$
Total Oper. & Admin exp.	\$	\$	\$
Excess or deficit for the year	(\$	\$	(\$

D did not have accounting software to record its financial transactions. J provided the summary of expenses and income, bank statements, checkbooks, and escrow documentation to the CPA to prepare the returns. The returns information did not reflect the actual financial activities. The return 990-PF for year O did not report the transactions from selling the properties. J stated that D did not have net loss and she was not aware how the CPA prepared the returns.

**Financial information from the bank statements of D**

D had a checking accounting (account number: Q) at R. According to the bank statements, the total deposits and withdraws were \$ and \$ respectively, for the year O. D spent major of its expenses on the mortgage, repair and maintenance, utilities, and compensations to Mrs. J.

**LAW:**

Section 501(c) of the Internal Revenue Code provides that an organization described in section 501(c) (3) is exempt from income tax. Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

<b>Form 886-A</b>	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer</b>		<b>Year Ended</b>

Section 1.501(c)(3)-1(a)(1) of the regulations provides 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 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) states, "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) 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. The words "private shareholder or individual" refer to persons having a personal and private interest in the activities of the organization. The term "private shareholder or individual" is defined in regulation section 1.503(a)-1(c).

An organization must establish that it serves a public rather than a private interest and "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." Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii). Prohibited private interests include those of unrelated third parties as well as insiders. Christian Stewardship Assistance, Inc. v. Commissioner, 70 T.C. 1037 (1978); American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989). Private benefits include an "advantage; profit; fruit; privilege; gain; [or] interest." Retired Teachers Legal Fund v. Commissioner, 78 T.C. 280, 286 (1982).

In Better Business Bureau v. United States, 326 U.S. 279 (1945) the court held that regardless of the number of truly exempt purposes, the presence of a single substantial non exempt purpose will preclude exemption under section 501(c)(3) of the code.

An organization formed to educate people in Hawaii in the theory and practice of "est" was determined by the Tax Court to a part of a "franchise system which is operated for private benefit," and, therefore, should not be recognized as exempt under section 501(c)(3) of the Code. est of Hawaii v. Commissioner, 71 T.C. 1067, 1080 (1979). Although the organization was not formally controlled by the same individuals who controlled the for-profit entity that owned the license to the "est" body of knowledge, publications, and methods, the for-profit entity exerted considerable control over the applicant's activities by setting pricing, the number and frequency of different kinds of seminars and training, and providing the trainers and management personnel who are responsible to it in addition to setting price for the training. The court stated that the fact that the organization's rights were dependent upon its tax-exempt status showed the likelihood that the for-profit entities were trading on that status.



<b>Form 886-A</b>	<b>EXPLANATION OF ITEMS</b>	<b>Schedule or Exhibit No.</b>
<b>Name of Taxpayer</b>		<b>Year Ended</b>

The question for the court was not whether the payments made to the for-profit were excessive, but whether the for-profit entity benefited substantially from the operation of the organization. The court determined that there was a substantial private benefit because the organization "was simply the instrument to subsidize the for-profit corporations and not vice versa and had no life independent of those corporations."

**GOVERNMENT POSITION:**

The Service contends that D has not operated exclusively for exempt purposes described within Internal Revenue Code section 501(C)(3).

D stated that its purpose is to provide food, shelter, job training & child care to battered women. On the contrary, the primary activity engaged in by D during the year 2000 and thereafter was engaging in real estate transactions. D purchased eleven properties from Department of Housing and Urban Development at 30 percent discount and sold them at market price to the individuals for profit. For the year under examination, D sold six properties including two properties to N, a for profit corporation owned by J, and sold three properties to K. D distributed its net earnings to its sole officer, J, as compensation.

The organization purchased properties at a discount from L and sold them for profit. This is not for charitable purposes.

**CONCLUSION:**

In summary, D has not operated exclusively for exempt purposes because it did not engage primarily in activities that accomplish an exempt purpose. Therefore, the Service determines that D does not qualify for exemption from Federal income tax under section 501(c) (3) of the code. D is liable to file corporate income tax return (Form 1120) for year O and years thereafter.



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

**DEPARTMENT OF THE TREASURY**

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

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:

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,

Enclosures:  
Publication 892  
Publication 3498  
Report of Examination

We are revoking your exemption from Federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code effective

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

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for all years beginning

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

If you decide to contest this determination in court, you must file a pleading seeking a declaratory judgment in the United States Tax Court, the United States Court of Federal Claims, or the United States District Court for the District of Columbia before the 91<sup>st</sup> day after the date this final determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing pleadings for declaratory judgments and refer to the enclosed Publication 892. You may write to these courts at the following addresses:

United States Tax Court  
400 Second Street, NW  
Washington, D.C. 20217

United States Court of Federal Claims  
717 Madison Place, NW  
Washington, D.C. 20005

United States District Court for the District of Columbia  
333 Constitution Avenue, NW  
Washington, D.C. 20001

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 too-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at: Internal Revenue Service,

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