



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service  
1100 Commerce Street  
Dallas, TX 75242

Release Number: **200732017**  
Release Date: 8/10/2007

June 12, 2006

UIL: 501.03-01

ORG

Taxpayer Identification Number:

Form:

990-PF

Tax Year(s) Ended:

December 31, 20xx

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:

Internal Revenue Service  
Taxpayer Advocate

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



## DEPARTMENT OF THE TREASURY

Internal Revenue Service  
TE/GE EO Examinations  
1100 Commerce Street  
Dallas, TX 75424

**TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION**

UIL: 501.03-01

Name = ORG

Person to Contact:  
Identification Number:  
Contact Telephone Number:  
In Reply Refer to: TE/GE Review Staff  
EIN:

LAST DATE FOR FILING A PETITION  
WITH THE TAX COURT: \_\_\_\_\_

Dear Sir:

This is a Final Adverse Determination Letter as to your exempt status under section 501(c)(3) of the Internal Revenue Code. Your exemption from Federal income tax under section 501(c)(3) of the code is hereby revoked effective January 1, 20XX.

Our adverse determination was made for the following reasons:

1. You are not operated exclusively for a charitable or nay other exempt purpose, as required under IRC section 501(c)(3).
2. Your net earnings have inured to the benefit of private shareholders or individuals, which is prohibited under IRC section 501(c)(3).
3. You are operated for a substantial private purpose and are not operated for an exclusively public purpose, which is prohibited under IRC section 501(c)(3).

You failed to meet the requirements of IRC section 501(c)(3) and Treas. Reg. section 1.501(c)(3)-1(d) in that you failed to establish that you were operated exclusively for an exempt purpose. Rather, you were operated for the benefit of private interests and a part of your net earnings inured to the benefit of your founder and board members.

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 1041. These returns should be filed with the appropriate Service Center for the year ending December 31, , and for all years thereafter.

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 initiate a suit for declaratory judgment in the United States Tax Court, the United States Claim Court or the District Court of the United States for the District of Columbia before the 91<sup>st</sup> day after the date this determination was mailed to you. Contact the clerk of the appropriate court for the rules for initiating suits for declaratory judgment.

You also have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers.

You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling or writing.

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States 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.

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

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

Sincerely yours,

Marsha A. Ramirez  
Director, EO Examinations

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer		Year/Period Ended December 31, 20xx December 31, 20xx
ORG		

**LEGEND:**

Name = Org

Co-Founder = Name of Co-Founder

Founder = Name of Founder

**Issue:**

Should the above named Private Non-Operating Foundation exempt under IRC section 501(c)(3) retain their exempt status?

**Facts:**

The ORG was recognized as Private Non-Operating Foundation, exempt under IRC section 501(c)(3), on January 22, 20XX and effective for year ending December 31, 20XX. Per their Form 1023, Application for Recognition of Exemption, which was filed in December of 2002, the organization activities would consist of making grants to other 501(c)(3) organizations classified as public charities for religious, charitable, educational, scientific and literary purposes. The organization's Form 1023 also states that the organization would develop operating procedures to ensure that it adheres to the rules of IRC Sections 4941, 4942, 4943, 4944 and 4945 as applicable to private non-operating foundations. The Form 1023 also states that the foundation will be funded primarily by its founders, Founder, trustee and Co-Founder, trustee.

The organization's Forms 990-PF for years ending December 31, 20XX and December 31, 20XX were selected for examination based on information obtained from a promoter in regards to abusive trusts.

**Funding Analysis**

Analysis of organization's books and records determined that a majority of the organization's total revenue, for both years under review, was generated from contributions made by its Executive Trustees, Founder and Co-Founder, with the remainder being derived from investment income. The figures are as follows:

	<u>20XX</u>	<u>20XX</u>
Trustee Contributions	\$14,794	\$ 17,689
Investment	<u>\$ 580</u>	<u>\$ 659</u>
Total	\$15,374	\$ 18,348

**Expenditure Analysis**

The following figures represent the organization's expenditure activity for years ending December 31, 20XX and 20XX.

<u>Credit Card Transactions</u>	<u>20XX</u>	<u>20XX</u>
• Travel	\$2,726	\$ 5,873
• Lodging	\$ 850	\$ 1,365
• Dining/Entertainment	\$ 621	\$ 691
• Vehicle	\$ 13	\$ 0

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ORG		December 31, 20xx December 31, 20xx

• Office Services	\$ 256	\$ 2,033
• Other	<u>\$ 508</u>	<u>\$ 2,980</u>
Total	\$4,974	\$12,942
	<u>20XX</u>	<u>20XX</u>

Store Credit Transactions

• Furniture	\$ 3,286	
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Cash Disbursements

• Credit Payments	\$ 8,053	\$13,282
• Grants (Organizations)	\$ 3,486	\$ 810
• Grants (Individuals)	\$ 465	\$ 0
• Scholarships	\$ 1,000	\$ 3,000
• Payments to Relatives	\$ 2,891	\$ 2,450
• Personal Services	\$ 0	\$ 120
• Cash Withdrawals	\$ 45	\$ 0
• Investments	<u>\$10,000</u>	<u>\$ 0</u>
Total	\$25,940	\$19,662

During the course of the examination, it was concluded that a substantial percentage of the organization's total expenditures were of a personal nature and conducted for the personal benefit of its trustees, disqualified persons and individuals.

The expenditures in question included a majority of the credit transactions, payments for personal services, disbursements to relatives and all individual awarded during both 20XX and 20XX.

The total amount of expenditures determined to be personal in nature totaled \$10,407 for 20XX and \$14,940 for 20XX. (See Attachment)

The largest percentage of these transactions was related to the organization's credit transactions. The majority of these credit transactions were associated with the purchase of personal items and the payment of travel expenses relating to family vacations taken by the trustees. The purchases were made utilizing credit cards issued in the name of the organization and provided for use by each of the Executive Trustees. Of the total credit transactions conducted during the two years under review, 85% of the transactions conducted during 20XX and 90% of those conducted during 20XX, were deemed to be transacted for the personal benefit of the trustees. (See attachment for specific transactions)

During both 20XX and 20XX, the organization also made regular, monthly disbursements to the mother of Executive Trustee, Founder. According to Executive Trustee, Co-Founder, these disbursements were issued as a form of reward for her involvement in conducting a genealogy study of the Founders Family. The monthly disbursements made to this individual totaled \$2,296 during 20XX and \$2,450 during 20XX. In addition, a cash disbursement of \$195 was made to Associate

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ORG		

Trustee, for payment of expenses related to a field trip. These activities and disbursements were conducted for the personal benefit of the trustees and their family members rather than the exempt purposes of the organization. (See Attachment)

A cash disbursement made during 20XX was also determined to be a personal expense and conducted for the benefit of a trustee. This disbursement involved a payment made by Executive Trustee, Founder for payment of professional services received during 20XX. No substantiation for this expense was provided by the organization.

During 20XX, the organization activities included making grants to seven individuals which totaled \$1,465. These individuals were all associated with the Trustees through personal relations and/or membership in the church in which the Trustees attended. The individuals were granted these funds as gifts or to assist them with some form of personal finance need. As a result, these disbursements were determined to be of a personal rather than a charitable nature (See Attachment)

It was also determined that this organization does not have any established procedures for issuing grants to individuals nor has it sought prior approval of its grant-making procedures from the Internal Revenue Service.

**Applicable Law:**

IRC Section 501(c)(3) provides tax exemption for corporations and foundations that are operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

Treasury Regulation Section 1.501(c)(3)-1(a)(1) states that in order to be exempt as an organization described in IRC 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.

Treasury Regulation Section 1.501(c)(3)-1(c)(1) states 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.

Treasury Regulation Section 1.501(c)(3)-1(c)(2) states 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 or private shareholders or individuals.

Treasury Regulation Section 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized or operated exclusively for one or more of the purposes specified in IRC Section 501(c)(3) unless it

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ORG		

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.

**Taxpayer's Position:**

The organization agreed to the proposed revocation of its exempt status under I.R.C. section 501(c)(3) by executing a Form 6018.

**Government's Position:**

The organization has failed to meet the operational test described in Treasury Regulation Section 1.501(c)(3)-1(c)(1), above.

A substantial percentage of the organization's total expenditures from 20XX through 20XX were clearly personal in nature. These personal expenditures included credit transactions and cash disbursements for the benefit of the trustees and their relatives, as well as grants being provided to individuals for personal reasons.

As stated in Treasury Regulation Section 1.501(c)(3)-1(c)(1), "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)." Since the majority of the organization's expenditures were used for personal purposes, the organization is clearly not engaging primarily in activities that accomplish exempt purposes under IRC Section 501(c)(3).

Further, as indicated in Treasury Regulation Section 1.501(c)(3)-1(c)(2), the organization is not operated exclusively for exempt purposes, because a substantial amount of its net earnings are inuring to trustees of the foundation.

The organization is also being operated for private rather than public interests since the majority of its total expenditures were personal in nature. As stated in Treasury Regulation Section 1.501(c)(3)-1(d)(1)(ii), an organization is not operated for exempt purposes if it is being operated for private interests.

Based on the above precedent, it is our position that the organization's exemption under IRC Section 501(c)(3) should be revoked.

**Conclusion:**

Since the organization does not meet the operational test under IRC Section 501(c)(3), we are proposing that its tax exemption be revoked.