



TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

Release Number: **200828029**

Release Date: 7/11/08

Date: April 18, 2008

UIL Code: 501.03-00

Dear

This is our final determination that you do not qualify for exemption from Federal income tax under Internal Revenue Code section 501(a) as an organization described in Code section 501(c)(3).

We made our determination based on the following reasons. You are not organized exclusively for purposes described in section 501(c)(3). You have not established that you are operated exclusively for exempt purposes described in section 501(c)(3). You have not established that your activities lessen the burdens of government, relieve the poor and distressed or underprivileged, or accomplish any other exempt purpose specified in section 1.501(c)(3)-1(d)(2) of the Federal Tax Regulations. You have not established that you are not operated for the private interests specified in section 1.501(c)(3)-1(d)(1)(ii) of the regulations. Nor have you established that your net earnings do not inure to the benefit of private shareholders or individuals as specified in section 1.501(c)(3)-1(c)(2) of the regulations. Finally, you have not established that you are not operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513 of the Code, pursuant to section 1.501(c)(3)-1(e)(1) of the regulations.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, you must initiate a suit in the United States Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia before the 91<sup>st</sup> day after the date that we mailed this letter to you. Contact the clerk of the appropriate

court for rules for initiating suits for declaratory judgment. Filing a declaratory judgment suit under Code section 7428 does not stay the requirement to file returns and pay taxes.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, you should follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Robert Choi  
Director, Exempt Organizations  
Rulings & Agreements

Enclosure  
Notice 437  
Redacted Proposed Adverse Determination Letter  
Redacted Final Adverse Determination Letter



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

Date: July 6, 2004

U.I.L. Nos.  
501.03-00

Employer Identification Number: \*\*\*\*\*

Dear :

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

According to your Amended Articles, your activities shall include, but shall not be limited to:

Provision of consulting services, development, acquisition by purchase and/or gift, improvement, operation, management, promotion, funding, sale and preservation of affordable rental housing and space, including in particular space of one or more manufactured home parks and interests therein located within the U.S. for persons of limited financial means, elderly persons, or other persons in need of safe and adequate housing consistent with and recognized as charitable the Internal Revenue Service in Revenue Ruling 70-585, Revenue Ruling 72-124 and Revenue Ruling 79-18 and similar federal and state regulatory guidance.

Your Bylaws provide that the board of directors may create one more limited liability companies (branches) for the purpose of acquiring, constructing, improving, renovating, and or holding title to real or personal property.

Under your Bylaws, the Founding Director is to serve a term of \*\*\*\*\* years, other initial directors or their successors are to serve a term of \*\*\*\*\* years, and the term of other directors is to be one year. There are no limits on the number of successive terms that a director can serve. Any Founding Director may be removed only for cause, while other directors may be removed with or without cause. \*\*\*\*\* is designated as the sole Founding Director.

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Your Board of Directors consists of \*\*\*\*\* and Mr. \*\*\*\*\*. The resumes that you provided for the board members contain the following information:

\*\*\*\*\* has been involved in real estate investment management related to the manufactured housing and recreational vehicle industry; business consulting, and commercial property management.

\*\*\*\*\* owns a company that builds \*\*\*\*\* and is a \*\*\*\*\* in mobile home parks.

\*\*\*\*\* was Vice President of \*\*\*\*\* and \*\*\*\*\* Properties. You were asked to describe in detail all of Mr. \*\*\*\*\*' past, present and future relationships with \*\*\*\*\* as well as any and all of its affiliates (not just those in the \*\*\*\*\* industry). Your response was that since August of \*\*\*\*\* he has been and is currently directly involved with every acquisition, refinance and disposition as an employee of \*\*\*\*\* and \*\*\*\*\* (collectively "Owner"). Since June of \*\*\*\*\* he has also held a profit participation interest in an entity that holds a limited partnership interest in each of the \*\*\*\*\* and \*\*\*\*\* . You further state that as of \*\*\*\*\* Mr. \*\*\*\*\* no longer maintains any economic interest in any of the \*\*\*\*\* or related management company owned by an affiliate of the Owner. You also state that after your acquisition of \*\*\*\*\* target properties from \*\*\*\*\* Mr. \*\*\*\*\* will resign his employment with the Owner and all of its affiliates but he will continue to maintain a profit participation interest in the \*\*\*\*\* portfolio. You explain that you see no conflict of interest in his maintaining an interest in the \*\*\*\*\* portfolio. When asked whether any of your officers or directors has a business or financial relationship with a principal in the \*\*\*\*\* Management Company such as a shared interest in a partnership, your response was "No. The only relationship of the Corporation (you) to \*\*\*\*\* Management Company (or any affiliate of \*\*\*\*\* Management Company) is as described in the Previously Submitted Materials." You state that you will not conduct business with \*\*\*\*\* , a business in which Mr. \*\*\*\*\* is a director.

You state that board members were chosen who were unrelated to \*\*\*\*\* and their business experience was cited. We asked whether you were willing to expand your board so that it is more representative of the community that it serves, and if so, to provide drafts of the Bylaws and Limited Liability Company (LLC) operating documents that would incorporate the changes. You responded that you would add additional board members with no financial interest in your affairs within the first 12 months of closing your first acquisition. You stated that you would diligently undertake to appoint such new board members consistent with your representations and our understanding. No change in the composition of your board has been made to date.

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Your Bylaws provide for two officers, president and secretary/treasurer. While other officers may be elected, you are not required to have any officers other than these. The president is authorized to sign documents on your behalf; enter into contracts or agreements; execute in your name, along with the secretary, any instrument or other writing; and, see that that the orders and resolutions of the board are carried into effect. He has the right to supervise and direct your management and operation. And, he makes all decisions as to policy and otherwise between board meetings, with all officers and employees being under his supervision and control during the interim period. The secretary/treasurer duties include attending all meetings; giving notice of meetings; keeping the corporate seal; having custody of corporate funds and securities; disbursing funds at the board's direction; and, preparing financial statements. Your proposed budget includes compensation of officers, directors, and trustees of \$ \_\_\_\_\_ per year with a notation that the only officer you anticipate paying will be your president. You state that when funds become available, the president's actual compensation will be determined. \*\*\*\*\* serves as your president.

You submitted a draft conflict of interest statement. In the draft, "Interest Party" is defined as any director, officer or employee or person with powers derived from the board of directors who has a direct or indirect financial interest. It also provides for minutes to be kept which contain the names of the persons who disclosed or otherwise were found to have a financial interest in connection with an actual or possible conflict of interest, the nature of the financial interest, any action taken to determine whether a conflict of interest was present, and the board's or committee's decision as to whether a conflict of interest in fact existed. In addition, the minutes are to include the names of the persons who were present for the discussion and votes, the content of the discussion, including any alternatives to the proposed transaction or arrangement, and a record of any votes taken in connection with the proposed arrangement or transaction. The section related to compensation requires you to endeavor to ensure that all compensation arrangements affecting interested persons are objectively reasonable, based on the relevant market for persons of comparable skills, training, education and experience and performing similar duties for comparable organizations under similar conditions and circumstances.

We asked whether you would be willing to amend your governing documents so that certain language related to possible conflicts of interests could be added. If you were willing to do so, you were to provide drafts of the proposed changes. In the suggested language, persons deemed to have a financial interest in your affairs include persons receiving compensation (other than the reimbursement of expense) from you; independent contractors for services with you; persons with a financial relationship with such an independent contract (such as owners or employees of the independent contractor); and, close family members of the foregoing. It further provides that a director, officer, or committee member who has a financial interest conflicting with your interest in any matter is to bring this to the attention of the other directors,

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officers, and committee members. In response, you submitted drafts of revisions to your Articles, Bylaws and LLC Articles of Organization and Regulations. You state that upon recognition of your exemption, your board will adopt the draft documents and the Articles will be filed.

You plan to engage in activities related to the acquisition, rehabilitation, repair, ownership and management of manufactured home parks. You will provide land and land improvements such as streets, community areas and structures, landscaping, laundry facilities and pads. The residents, who are responsible for the manufactured home or housing unit, will rent the land on which the homes are located (pads). The residents are responsible for all utilities (i.e., water, sewer, electric, gas, trash and cable television). You state that you will make certain supportive services available to the residents; i.e., computer training, English classes, after school programs and tutoring.

Your activities are to be funded by, in order, tax-exempt bonds; space rental income, utility pass-through income, and, other miscellaneous income from residents; and, asset management fees. You do not plan to participate in fundraising activities. You explain that each project will be set up as a separate Limited Liability Company (LLC). The LLC's will be responsible for acquiring properties, issuing bonds and entering into agreements with government agencies. The language used by the LLC's in their documents is to be that used for HUD contracts. Where there is a conflict with the LLC Articles of Organization, FHA loan documents will govern.

A letter dated July 24, \*\*\*\*\* from you to \*\*\*\*\* evidences your intent to acquire \*\*\*\*\* properties in \*\*\*\*\* as a portfolio from \*\*\*\*\* for \$\*\*\*\*\*. You state that principals of \*\*\*\*\* are also principals of \*\*\*\*\*. According to the letter, \*\*\*\*\* as seller is to pay \*\*\*\*\* % of the purchase price as a consulting fee, payable upon closing of escrow. The letter is addressed to \*\*\*\*\* at \*\*\*\*\* which is also your address as shown in your letterhead and the application that you submitted.

You provided draft documents related to your acquisition of the \*\*\*\*\* properties, including Articles of Organization for each LLC that is to be set up. You state that you have identified \*\*\*\*\* additional properties for acquisition, \*\*\*\*\* of which are owned by \*\*\*\*\* and/or its affiliates. The \*\*\*\*\* properties owned \*\*\*\*\* are located in the state of \*\*\*\*\*.

Among the documents furnished were appraisal documents for the \*\*\*\*\* properties (collectively, the "Projects"):

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<u>Project Name</u>	<u>Proposed Purchase Price</u>	<u>Approximate Appraised Value</u>
*****	\$*****	\$*****
*****	\$*****	\$*****
*****	\$*****	\$*****

The acquisition of the Projects is contingent upon certain conditions, including the issuance of tax-exempt bond by either the cities where the projects are located, the \*\*\*\*\* Finance Authority or another qualified issuer of tax-exempt bonds located in the state.

You submitted a copy of a consulting contract that you propose entering into with \*\*\*\*\*. \*\*\*\*\* is to be employed by you as an independent contractor responsible for asset identification and acquisition efforts on a project-by-project basis. The compensation structure set up under the contract for \*\*\*\*\* consulting services is as follows:

- \*\*\*\*\*% of the first \$\*\*\*\*\* of acquisition price;
- \*\*\*\*\*% on \$\*\*\*\*\*-\$\*\*\*\*\* of acquisition price; and,
- \*\*\*\*\*% in excess of \$\*\*\*\*\*

You state that the amounts will be determined by project pooling rather than per project, with related projects treated as single bond issuance.

You also submitted a copy of a Management Agreement that you propose entering into with \*\*\*\*\* making it property manager for the Projects. You state that \*\*\*\*\* was selected without competitive bidding based on its breadth of experience in managing manufactured home communities, and in the case of the Projects, its prior experience owning and operating such property. You further state that the arrangement was made at arm's length, and the manager's fees and terms of the agreement are competitive.

As property manager, \*\*\*\*\* is to be compensated in an amount equal to \*\*\*\*\*% of the gross income collected from the Project. The compensation will be modified prior to bond issuance to provide for a flat management fee of \*\*\*\*\*% of gross amounts of all income collected by property manager. In addition, for its construction management and oversight services, \*\*\*\*\* will be paid an amount equal to \*\*\*\*\*% of the hard costs incurred during rehabilitation of a Project. Prior to issuance of the bonds, the agreement will be modified to place a cap on any amounts due annually for construction supervision and oversight so that compensation for such services will not exceed the manager's compensation for management services.

You state several reasons why you believe that you qualify for exemption under section 501(c)(3) of the Code.

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You state that your efforts to acquire the first Projects, which are located in a state which imposes statutory duties on cities and similar political subdivisions of the State to provide affordable housing for very low, low and moderate-income families, lessens the burdens of local and state government.

You state that you expect "to operate the Projects in a manner ...which is consistent with the so-called 'safe harbor' guidelines, published by the Internal Revenue Service as Revenue Procedure 96-32."

You state that future acquisitions may include projects appealing to senior residents (age 55 and older) who would otherwise qualify as very low, low or moderate-income persons or couples.

You state that you will also satisfy the Facts and Circumstances test under Rev. Proc. 96-32 for the following reasons:

1. Participation in a government housing program designed to provide affordable housing.
2. Provision of social services affordable to poor residents.
3. Existence of affordability covenants or restrictions running with the land
4. Limitation on rents to ensure that they are affordable to low-income and very low-income residents.

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

Section 501(c)(3)-1(e) of the Code provides that an organization may meet the requirements of section 501(c)(3) of the Code although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose.

Section 1.501(c)(3)-1(c)(1) of the Income Tax 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(c)(2) of the regulations 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

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benefit of private shareholders or individuals. Section 1.501(a)-1(c) defines the words "private shareholder or individual" in Code section 501 as referring to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more exempt purposes under Code section 501(c)(3) unless it serves a public rather a private interest. Thus, 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(c)(3)-1(d)(2) of the regulations provides that the term charitable is used in section 501(c)(3) in its generally accepted legal sense. In the law of charity, the promotion of health and relief of the poor and distressed or the underprivileged are charitable purposes. Programs directed to relieving the distress of physically handicapped persons serve charitable purposes. Also included as a charitable purpose is the lessening of the burdens of government.

Section 53.4958-6 of the regulations creates a rebuttable presumption that compensation is reasonable if arrived at by a particular procedure. A decision will be entitled to the presumption if it is approved in advance by an authorized body composed entirely of individuals who do not have a conflict of interest, and which relied upon appropriate data when making the decision, and adequately documented the basis for the decision.

In Better Business Bureau v. United States, 316 U.S. 279 (1945), the Court held that the existence of a single non-exempt purpose, if substantial in nature, will destroy a charitable exemption.

In Leon A. Beechly Fund v. Commissioner, 35 T.C. 490 (1960), the Court held that where an exempt organization engages in a transaction with an insider and there is a purpose to benefit the insider rather than the organization, inurement occurs even though the transaction ultimately proves profitable for the exempt organization. The test is not ultimate profit or loss but whether, at every stage of the transaction, those controlling the organization guarded its interests and dealt with related parties at arm's-length.

In Old Dominion Box Co. v. United States, 477 F.2d. 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.

Harding Hospital, Inc. v. United States, 505 F.2d 1068 (1974), holds 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.

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B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), holds that the operation of a consulting service for exempt organizations is not itself entitled to exempt status under section 501(c)(3) of the Code. The critical inquiry is whether the activity is carried on for an exempt purpose or a commercial purpose. The commercial "hue" of the activity is relevant, as is competition with commercial enterprises.

In Christian Manner International, Inc. v. Commissioner, 71 T.C. 661 (1979), the Court held that both the actual as well as the stated purposes for the existence of an organization and the activities it engages in to accomplish those purposes must be considered. What those purposes are and what purposes the activity or activities engaged in support are questions of fact. See also Pulpit Resource v. Commissioner, 70 T.C. 594 (1978).

In Church by Mail v. Commissioner, 765 F.2d 1387 (9<sup>th</sup> Circ. 1985), aff'g TCM 1984-349 (1984), the court found that it was unnecessary to consider the reasonableness of payments made by the applicant to a business owned by its officers. The Court stated that "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 of the Church."

Federation Pharmacy Services, Inc. v. Commissioner, TC Memo 1986-348, holds that although the activity of the organization promoted health, which could be a charitable purpose, it operated in a commercial manner. The opinion notes that the organization relies upon the sale of drugs to the public and competes with commercial pharmacies. The slight discount offered, which does not reduce prices below cost, did not amount to a charitable purpose.

Living Faith, Inc. v. Commissioner, TCM 1990-484, holds that the operation of a restaurant and health food shop is not exempt under section 501(c)(3) of the Code. Although the establishments carried out religious rules about food, they were operated in a commercial manner. The court pointed out that they were in competition with commercial restaurants, and set prices, hours, and other characteristics to compete with those commercial restaurants.

Quality Auditing Co., Inc. v. C.I.R., 114 T.C. 498 (U.S. Tax Ct. \*\*\*\*\*), holds that an organization can be classified as having the charitable purpose of lessening the burdens of government only if two criteria are satisfied. First, the activities engaged in by the organization must be those which a governmental unit considers to be its burden. In other words, it must be shown that a governmental unit accepts as its responsibility the activities conducted by the organization and recognizes the organization as acting on the Government's behalf. Second, the organization's performance of the activities must actually lessen the burdens of Government. However, "The mere fact that such activities might improve the general economic well-being of the Nation or a State or reduce any adverse impact from the failure of Government to carry out such activities is not enough."

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Rev. Rul. 69-383, 1969-2 C.B. 113, provides an example of a reasonable compensation arrangement. It holds that under certain circumstances, the use of a method of compensation based upon a percentage of the income of an exempt organization can constitute inurement of net earnings to private individuals. For example, the presence of a percentage compensation agreement will destroy the organization's exemption under section 501(c)(3) of the Code where such arrangement transforms the principal activity of the organization into a joint venture between it and a group of physicians (Lorain Avenue Clinic v. Commissioner, 31 T.C. 141 (1958)), or is merely a device for distributing profits to persons in control (Birmingham Business College v. Commissioner, 276 F.2d 476 (1970)).

Rev. Rul. 79-18, 1979-1 C.B. 194, holds that an organization that provides specially designed housing to elderly persons at the lowest feasible cost and maintains in residence those tenants who subsequently become unable to pay its monthly fees is an organization operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code.

Rev. Rul. 79-19, 1979-1 C.B. 195, holds that an organization that provides specially designed housing to physically handicapped persons at the lowest feasible cost and maintains in residence those tenants who subsequently become unable to pay its monthly fees is operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code

Rev. Rul. 72-124, 1972-1 C.B. 145, sets forth requirements that homes for the aged must meet in order to qualify for exemption under section 501(c)(3) of the Code. The Revenue Ruling makes clear that a home for the aged will be deemed 'charitable' if it meets the special needs of the elderly such as the need for health care, financial security, and residential facilities designed to meet specific physical, social, and recreational requirements of the elderly.

Rev. Ruls. 85-1 and 85-2, 1985-1 C.B. 178, set forth a two-part test for determining whether an organization's activities lessen the burdens of government. First, it is necessary to determine whether the government unit considers the activities of the organization to be its burden. The second part of the test is whether these activities actually lessen the burdens of the government. An activity is a burden of the government if there is an objective manifestation by the governmental unit that it considers the activities of the organization to be its burden. The interrelationship between the governmental unit and the organization may provide evidence that the governmental unit considers the activity to be its burden. However, engaging in an activity sometimes undertaken by the government or an expression of approval by the government is insufficient to establish a burden of government. Whether the organization is actually lessening the burdens of government is determined by considering all relevant facts and circumstances.

Revenue Procedure 96-32, 1996 -1 C.B. 717, sets forth a safe harbor under which organizations that provide low-income housing will be considered charitable as described in

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section 501(c)(3) of the Internal Revenue Code because they relieve the poor and distressed. The revenue procedure also describes the facts and circumstances test that will apply to determine whether organizations that fall outside the safe harbor relieve the poor and distressed. An organization must establish that at least (a) 75 percent of its units are occupied by low-income families, and (b) either 20 percent of the units are also occupied by very low-income residents or 40 percent of the units are occupied by residents whose incomes do not exceed 120 percent of the area's very low income limit. In addition, the housing is affordable to beneficiaries. In the case of rental housing, this requirement will ordinarily be satisfied by the adoption of a rental policy that complies with government-imposed rental restrictions or otherwise provides for the limitation of the tenant's portion of the rent charged to ensure that the housing is affordable to low-income and very low-income residents. The organization may not further the private interests of individuals with a financial stake in the project resulting from real property sales, development fees or management contracts.

The facts and circumstances test considers all the surrounding facts and circumstances, including, but are not limited to, the following:

- (1) A substantially greater percentage of residents than required by the safe harbor with incomes up to 120 percent of the area's very low-income limit.
- (2) Limited degree of deviation from the safe harbor percentages.
- (3) Limitation of a resident's portion of rent or mortgage payment to ensure that the housing is affordable to low-income and very low-income residents.
- (4) Participation in a government housing program designed to provide affordable housing.
- (5) Operation through a community-based board of directors, particularly if the selection process demonstrates that community groups have input into the organization's operations.
- (6) The provision of additional social services affordable to the poor residents.
- (7) Relationship with an existing 501(c)(3) organization active in low-income housing for at least five years if the existing organization demonstrates control.
- (8) Acceptance of residents who, when considered individually, have unusual burdens such as extremely high medical costs which cause them to be in a condition similar to persons within the qualifying income limits in spite of their higher incomes.

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(9) Participation in a homeownership program designed to provide homeownership opportunities for families that cannot otherwise afford to purchase safe and decent housing.

(10) Existence of affordability covenants or restrictions running with the property.

In Example (1) under section 5.01 of the Rev. Proc., Organization N operates pursuant to a government program to provide low and moderate income housing projects. Seventy percent of N's residents have incomes that do not exceed the area's low-income limit. Fifty percent of N's residents have incomes that are at or below the area's very low-income limit. Under the program, N restricts rents charged to residents below the income limits to no more than 30 percent of the applicable low or very low-income limits for N's area. N is close to meeting the safe harbor. N has a substantially greater percentage of very low-income residents than required by the safe harbor; it participates in a federal housing program; and it restricts its rents pursuant to an established government program. Although N does not meet the safe harbor, the facts and circumstances demonstrate that N relieves the poor and distressed.

In Example (2), Organization O will finance a housing project using tax-exempt bonds pursuant to § 145(d). O will meet the 20-50 test under §142(d)(1)(A). Another 45 percent of the residents will have incomes at or below 80 percent of the area's median income. The final 35 percent of the residents will have incomes above 80 percent of the area's median income. O will restrict rents charged to residents below the income limits to no more than 30 percent of the residents' incomes. O will provide social services to project residents and to other low-income residents in the neighborhood. Also, O will purchase its project through a government program designed to retain low-income housing stock. O does not meet the safe harbor. However, the facts and circumstances demonstrate that O relieves the poor and distressed.

In Example (5), Organization V provides rental housing in a section of the city where income levels are well below the other parts of the city. All of V's residents are below the very low-income limits for the area, yet they pay rents that are above 50 percent of the area's very low-income limits. V has not otherwise demonstrated that the housing is affordable to its residents. Although the residents are all considered poor and distressed under the safe harbor, V does not relieve the poverty of the residents.

While providing low-income housing is a charitable purpose, you have failed to establish that you will do so in a manner that is consistent with section 501(c)(3) of the Code and Rev. Proc. 96-32, supra. In addition, you have failed to show that public rather than private purposes will be served by your operation as required by section 1.501(c)(3)-1(d)(1)(ii) of the regulations. Harding Hospital, supra.

You state that in providing low-income housing, your proposed activities would serve to lessen the burdens of government, which is recognized as a charitable purpose. Section 1.501(c)(3)-1(d)(2) of the regulations. As explained in Quality Auditing Co., supra, there are two criteria to be satisfied in order to show that you have the charitable purpose of lessening the burdens of government: (1) the activities engaged in by the organization must be those which a

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governmental unit considers to be its burden; and (2) the performance of the activities must actually lessen the burdens of Government. See also, Rev. Ruls. 85-1 and Rev. Rul. 85-2, supra. You have not established that your proposed activities are those that a governmental entity sees as its burden, and that your activities specifically serve to lessen such a burden.

In support of your claim of exemption on this basis, you explain that there is a general interest by the government in low-income housing, and that providing low-income housing is statutorily required of some governmental units where you plan to locate your projects. The fact that you undertake an activity that a governmental unit may be required to conduct does not in itself establish that you are furthering the charitable purpose of lessening government burden. An organization must show not only that the governmental unit accepts as its responsibility the activities the organization conducts, but it must also show that the governmental unit recognizes the organization as acting on the Government's behalf. There must be an objective manifestation of a jurisdiction's recognition of you as an entity that it has specifically designated to accomplish a goal on its behalf. Quality Auditing Co., supra; Rev. Rul. 85-2, supra.

You have identified some of the jurisdictions where you propose setting up your projects as being required by statute to provide low-income housing. To establish that you are recognized as acting on behalf of the governmental unit, it is not sufficient to state that by conducting the activities you will improve conditions or to provide statements by the governmental unit expressing its approval of what you are doing. You must provide evidence that a specific governmental unit has established a relationship with you that distinguishes you from other entities seeking assistance: i.e., you were created by a governmental unit, a governmental unit will directly provide a significant amount of your funding, key government employees sit on your board, and the governmental unit will be jointly involved in the housing project. See, Quality Auditing Co., supra; Rev. Rul. 85-1, supra; Rev. Rul. 85-2, supra. We find no evidence of this type of interrelationship with a governmental unit existing in your case. According to the information that you have provided, you will seek assistance from several governmental units. There is no indication that in order to receive the assistance, an organization must have an interrelationship with the governmental unit as described above. Therefore, you have failed to establish that you lessen the burdens of government.

Revenue Procedure 96-32 describes "units occupied" by residents. The Revenue Procedure requires the "housing [to be] affordable to the charitable beneficiaries." The terms "units" and "housing" are understood to be shelters with walls and ceilings that enclose the resident. The affordability criteria of the revenue procedure only make sense if compared to an entire dwelling. A unit can be a manufactured housing unit, but it must be the entire unit. The affordability criteria are designed to measure the complete expense of housing against the income of a resident. The 30% standard of Examples (1) and (2) refers to the rent for the entire unit.

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Rev. Proc. 96-32 requires that the housing be affordable. Housing is considered less affordable when the cost is well above 30% of the resident's income. See, e.g., Example 5.

On the issue of affordability, you provided several formulas for determining what percentage of a resident's income will be used for rent. You state that in connection with certain parks, and consistent with certain affordability restrictions applicable to manufactured housing parks in the state, rental rate limitations may be increased to 30% of the applicable resident income rather than 15% for residents who are not required to make monthly payments on a mortgage or chattel loan related to their manufactured home. We expressed our concern regarding the various factors affecting the determination of the rents to be paid on various properties, and regarding your exclusion of utilities from the costs considered in determining affordability, and how these would affect your ability to guarantee that all of your properties would satisfy the affordability requirement of Rev. Proc. 96-32. We sent you several publications related to the issue of affordable housing for renters.

You state that it is difficult, if not impossible, for you to select a fixed percentage to be used in determining rental payments that you could apply to every community you acquire, noting that your projects will be located from            to           . You state that you would be able and willing to agree, and commit to your business plan, that you will establish for every community a rental policy that limits rents to the lowest possible amount. What the lowest possible amount would be, how it is to be determined, and whether it satisfies the affordability requirement of the Rev. Proc. is not explained.

You will rent to residents the land (or "pads") beneath their manufactured units. You have failed to establish that rent for your properties will be set so as to ensure affordability of the housing within the guidelines of Rev. Proc. 96-32. In addition to the expense of renting the pads, residents will be required to bear the additional costs of paying for utilities (including electric, gas, sewer, trash and water). You have not treated this as part of the housing expense in addressing the issue of what percentage of the residents' income is to be used for rent. In some cases, the housing costs, including utilities, would exceed the 30% standard.

You distinguish very low and low-income families residing in manufactured home parks from "traditional renters", comparing their housing needs to those of the elderly. You state that like the elderly, they suffer from burdens and stress other than simple high housing costs. You further state that manufactured home owners are often "trapped" by their landlords and the supply and demand of sites that allow landlords to increase rents beyond a reasonable percentage of an individual's income. You also state that the rents will be fixed for a long period of time once you acquire a community. You conclude that whether the rents are set at 25%, 30% or 35%, your proposed charitable endeavors will address the problem of housing for this class of renters. However, you have not established that as in the case of the elderly and the disabled, renters in mobile home parks have special needs which have led to them being recognized as a charitable class within the meaning section 501(c)(3) of the Code. See, Rev. Rul. 79-18, supra; Rev. Rul. 79-19, supra.

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You indicate that you "may" provide housing to the elderly and the disabled, some of whom would qualify as low-income. Providing assistance to the elderly and the disabled is recognized as a charitable purpose within the meaning of section 1.501(c)(3)-1(d)(2) of the regulations. However, you have not furnished specific information regarding how you propose to satisfy the special needs of these groups so as to qualify for exemption under section 501(c)(3) on this basis. See Rev. Rul. 72-124, supra.

The presence of a single non-exempt purpose that is substantial in nature will destroy a charitable exemption. Better Business Bureau v. U.S., supra.

Providing inexpensive housing in a commercial manner is not a charitable activity. See, Federation Pharmacy Services, supra, and Example (5) of the Revenue Procedure. For-profit entities as well as exempt entities provide housing, including that for manufactured home residents. The properties that you propose purchasing are presently owned by a for-profit entity. In order to be recognized as exempt, an organization must operate in a non-commercial manner that makes it plain that it is exclusively advancing its charitable purpose, and does not have a substantial non-exempt purpose. B.S.W. Group, Inc., supra; Living Faith, Inc., supra. You propose managing the housing parks in much the same way that for-profit ones are managed, except that you will offer longer leases, and you will pass on certain tax savings to tenants. You do not offer other subsidies. Residents are responsible for utility costs for which there is no allowance in your determination of the rental price for the pads. And, while you discuss the problems encountered by manufactured home residents, including financial ones, you do not have any policy for maintaining in residence those who become unable to pay rent.

Finally, you cite several reasons why you should qualify for exemption under the facts-and-circumstances test of Rev. Proc. 96-32 for relieving the poor and distressed. In applying the Revenue Procedure, all of the surrounding facts and circumstances are to be considered.

1. You state that upon acquisition of any community, you intend to design and implement support service programs based on a particular community's needs. However, you qualify this in several ways by saying that the economics and feasibility of a program will be considered. In addition, you state that actual supportive services may vary from time to time without explaining why.
2. You state that there will be limitations on the rents. As discussed above, you have not shown that you will operate your facilities so that a limitation set for the percentage of a resident's income to be used for a rent or mortgage payment would ensure that the housing is affordable to low-income and very low-income residents.

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3. You have no relationship with an existing 501(c)(3) organization active in low-income housing for at least five years that would have control over you. Such a relationship would serve to further your stated charitable purposes.

4. You state that in areas where there is no rent control, you will negotiate with the jurisdiction to establish it. However, it is not shown what authority the jurisdiction would have under such circumstances.

5. You have not shown that you will accept residents who, when considered individually, have unusual burdens such as extremely high medical costs which cause them to be in a condition similar to persons within the qualifying income limits in spite of their higher incomes.

6. You have not shown that residents will participate in a homeownership program designed to provide homeownership opportunities for families that cannot otherwise afford to purchase safe and decent housing.

7. Existence of affordability covenants or restrictions running with the property can not be guaranteed by you for all of your properties.

8. You are not operated by through a community-based board of directors, and there is no indication that community groups have input into the your operations. Your board members have been selected based upon their business experience. You have made representations regarding your willingness to expand your board. However, you made the expansion contingent upon your receiving an exemption under section 501(c)(3). In addition, you have also made your present board's participation in decision making, including the adoption of changes in your conflict of interest policy, contingent upon your receiving an exemption, while \*\*\*\*\* has proceeded to make significant decisions concerning your organization and operation.

You state that \*\*\*\*\* created you for a limited purpose, and in the documents that you submitted you have identified that purpose as being to provide low-income housing for manufactured home residents. However, you have not established that you operate exclusively for exempt purposes. Section 1.501(c)(3)-1(c)(2) of the regulations. In reviewing the facts, in addition to the concerns expressed above, we have additional ones regarding whether you are organized and operated so as to further a charitable purpose within the meaning of section 501(c)(3) of the Code. See, Christian Manner International, Inc., supra.

You have not shown that you operate for public rather than private interests. We do not believe in this case that you have significant interests that can be distinguished from those of \*\*\*\*\* so as to establish that you are not being operated for the non-exempt purpose of benefiting him. Old Dominion Box Co., supra; Section 1.501(c)(3)-1(d)(1)(ii) of the regulations.

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Mr. \*\*\*\*\* exerts considerable influence over you. He was your sole incorporator and has financed your activities. Unlike the other directors, as the sole Founder, Mr. \*\*\*\*\* can only be removed for cause. His term of service on the board exceeds that of other directors, and since board members may serve unlimited successive terms, his term may be considered perpetual.

There are two officer positions, with the position of secretary/treasurer being administrative in nature. As President, Mr. \*\*\*\*\* holds the only paid position. There is no job description that details the specific duties and responsibilities for which he is to be compensated as president.

The authority that Mr. \*\*\*\*\* possesses as president, as set forth in the Bylaws, gives him significant control over your affairs. He is authorized to make major decisions concerning your day-to-day operations with little oversight. Other than the annual meeting, your Bylaws do not mandate that meetings be held on a regular basis. During the periods between meetings, Mr. \*\*\*\*\* as president has total control over you. Minutes of meeting and other information were requested to document the board's involvement in certain actions taken on your behalf. You stated that there were none because you are awaiting recognition of your exemption before going forward as a board.

Despite your hesitancy to engage the board in your operation at this stage, in advance of your receiving exemption, Mr. \*\*\*\*\* has proceeded to make major decisions on your behalf. You provided copies of correspondence involving a tax-exempt bond issuance you are seeking to finance the projects, Mr. \*\*\*\*\* has identified properties held by \*\*\*\*\* for acquisition, and he has entered into negotiation for the purchase of the properties. You have also prepared lease agreements, documents related to the LLC's organization and operation, a consulting contract with Mr. \*\*\*\*\* and, a management contract with \*\*\*\*\*.

We have expressed our concerns regarding the current composition of your board. Your board, which is comprised of Mr. \*\*\*\*\* and two individuals from the mobile home industry, lacks members who are representative of the community. You state that you will expand the board within the first 12 months of closing your first acquisition.

Major decisions, including those involving ongoing transactions such as the consulting contract with Mr. \*\*\*\*\* and the management contract with \*\*\*\*\* will be made in advance of your expansion of the board. You state that the board will approve changes to documents that we have requested once you receive your exemption. The two current board members are to review the \*\*\*\*\* portfolio purchase, and the consulting agreement with Mr. \*\*\*\*\*. You state that they may obtain comparative data for nonprofits and for profits in evaluating compensation paid to Mr. \*\*\*\*\*. In light of the degree of authority vested in Mr. \*\*\*\*\* and the absence of documentation of the board's participation in decision making to date, there is nothing to indicate that the other two directors have had or will have significant input. In addition, given the time and resources expended on your activities, it is questionable whether the other two board members will be able to objectively review decisions and arrangements made prior to the date

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of that any exemption may be granted to you.

An organization is not operated for exclusively for exempt purposes if its net earnings inure to the benefit of private shareholders or individuals. Section 1.501(c)(3)-1(c)(3). In addition to the general prohibition against inurement involving organizations exempt under section 501(c)(3), Section 7 of Rev. Proc. 96-32 provides that an organization providing low income housing may fail to qualify for exemption, even if it furthers a charitable purpose, because private interests of individuals with a financial stake in the project are furthered. Inurement can take many forms. Founding Church of Scientology v. United States, *supra*.

We are concerned about inurement of your earnings to Mr. \*\*\*\*\*. The manner in which the consulting agreement has been drafted, providing Mr. \*\*\*\*\* with a project-by-project percentage payment based upon the sales price of the properties that he locates for your acquisition, confers substantial financial benefit upon him in his position as an independent contractor. See, Leon A. Beehly Fund, *supra*; Church by Mail, *supra*; Rev. Rul. 69-383, *supra*.

The consulting contract with Mr. \*\*\*\*\* also appears to constitute excessive compensation. The contract was created without any contemporaneous documentation as to the basis for the compensation amount, involvement by your board in determining its terms, or consideration of Mr. \*\*\*\*\*' conflict of interest.

Section 7 of Rev. Proc. 96-32 identifies private developers and management companies as being subject to the prohibition against private benefit and inurement in providing low-income housing. It provides that their roles in an organization's activities must be carefully scrutinized to ensure the absence of inurement or impermissible private benefit resulting from real property sales, development fees, or management contracts.

The facts and circumstances surrounding your financial arrangements with \*\*\*\*\* leads to the question of whether the transactions have been conducted at arm's length. Significant financial benefit is conferred upon the company, for which Mr. \*\*\*\*\* works.

According to a letter dated November 19, 2003 from \*\*\*\*\* Management Company, the company worked with Mr. \*\*\*\*\* for over a year on the acquisition of the properties. The Amended Articles identifies your date of incorporation as being \*\*\*\*\*. The properties do not appear to have been actively marketed by \*\*\*\*\* to other parties. When asked why \*\*\*\*\* was selling the properties, you stated that the Seller had adopted a change in its overall business plan and strategy, and believed its investment capital was more effectively and profitably deployed in \*\*\*\*\* acquisition and financing rather than manufactured home park acquisition and ownership. It is noted that while Mr. \*\*\*\*\* has given up financial interests related to manufactured homes, he has retained his interest in his \*\*\*\*\* portfolio.

Mr. \*\*\*\*\* using space at \*\*\*\*\* and while employed by the company, has negotiated contracts on your behalf for the purchase of properties from the company at a price at or above

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market value. In addition, he negotiated a management contract with \*\*\*\*\* that provides it with a percentage of the gross from all rental income sources on the projects it manages for you, as well as fees associated with construction management and oversight services. The agreements were entered into without competitive bidding, and without any documentation as to how the board determined that they will be to your best benefit.

An organization has the burden of providing that it satisfies the requirements of a particular exemption statute. Harding Hospital, Inc., supra. You have failed to prove that you satisfy the requirements for exemption under section 501(c)(3) of the Code. Accordingly, 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.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling 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 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 United States Court of Federal Claims, 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 30 days, this ruling will become final and a copy will be forwarded to the Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, . The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

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When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service

1111 Constitution Ave, N.W.  
Washington, D.C. 20224

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

Sincerely,

Lois G. Lerner  
Director, Exempt Organizations  
Rulings & Agreements