

Internal Revenue Service
Appeals Office
Attn:
Royal Palm One, Suite 350
1000 South Pine Island Road
Plantation, FL 33324

Department of the Treasury

Person to Contact:

Employee ID Number:
Tel:
Fax:

Refer Reply to:
AP:FE:FLL:GRP

In Re:
EO Revocation

EIN:
C = EIN

Form Required to be Filed:
1120

Tax Period(s) Ending:
20 , 20 , 20

**Last Day to File a Petition with the
United States Tax Court:**

JUN 08 2009

Release Number: **200932059**
Release Date: 8/7/09
Date: May 10, 2009
UIL Code: 7428.00-00

A= Org. Name
B= Org. Address

Certified Mail

Dear

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code (IRC). It is determined that you do not qualify as exempt from Federal income tax under IRC Section 501(c)(3) effective January 1, 2003.

Our adverse determination was made for the following reason(s): A substantial part of your activities consists of providing down payment assistance to home buyers. To finance the assistance, you rely on home sellers and other real-estate related businesses that stand to benefit from these down payment assistance transactions. Your receipt of a payment from the home seller corresponds to the amount of the down payment assistance provided in substantially all of your down payment assistance transactions. The manner in which you operate demonstrates you are operated primarily to further your insiders' business interests. Therefore, you are operated for a substantial nonexempt purpose. In addition, your operations further the private interests of the persons that finance your activities. Accordingly, you are not operated exclusively for exempt purposes described in section 501(c)(3).

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

You are required to file Federal income tax returns on the form indicated above. You should file these returns within 30 days from the date of this letter, unless a request for an extension of time is granted. File the returns in accordance with their instructions, and do not send them to this office. Processing of income tax returns and assessment

of any taxes due will not be delayed because you have filed a petition for declaratory judgment under Code section 7428.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia must be filed within 90 days from the date this determination was mailed to you. Contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.

We will notify the appropriate State officials of this action, as required by Code section 6104(c). 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, please contact the person whose name and telephone number are shown in the heading of this letter.

Sincerely,

CHARLES FISHER
TEAM MANAGER



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
9350 Flair Dr., 2nd Floor
El Monte, CA 91732-2828

ORG
ADDRESS

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 361E
Catalog Number

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,

Marsha A. Ramirez
Director, Exempt Organizations Exam

Enclosures:
Publications 892 & 3498
Report of Examination
Form 6018

EXPLANATION OF ITEMS

Name of Organization/Taxpayer

Tax Identification Number

Year/Period ended
12/31/20XX, 20XX
and 20XX

ORG

LEGEND
ORG = Organization name XX = Date City = city XYZ = State President = president EMP-1 = 1st employee V-P/CO-4
= Vice President/CO-4 CO-1, CO-2, CO-3, CO-4, CO-5, CO-6, CO-7 & CO-8 = 1st, 2nd, 3rd, 4th, 5th, 6th, 7th & 8th
COMPANIES

ISSUE

Whether the activities of ORG (hereinafter "ORG") are in compliance with the rules and regulations under Internal Revenue Code (hereinafter "the Code" or "IRC") §501(c)(3) during its existence.

FACTS

Organizational Information:

ORG was incorporated on April 28, 19XX, in the State of XYZ. The specific purpose of the organization, as originally stated in its articles of incorporation is "to provide downpayment assistance for home buyers." In order to meet the organizational test during the application process, the purpose statement was changed, on April 5, 19XX, to "This corporation is organized exclusively for charitable and educational purposes within the meaning of section 501(c)(3) of the Internal Revenue Code."

The IRS received Form 1023, *Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code*, on or around January 6, 19XX. The form was signed by President, the president of ORG. Its stated purposes in the application are as follows:

(a) ORG educates prospective home buyers in the importance of meetings one's obligations in the ownership of a home. Educational material in the amount of \$\$ value was donated by CO-1 for this purpose. As we help more prospective buyers, additional materials will hopefully be donated by CO-1, CO-2, or other concerned private organizations.

(b) The donation of books and educational material was made in November, 19XX.

(c) These educational materials will be sent to Realtors and Escrow closing agents as they will donate their time proctoring the course and examination.

During the application process, in response to the IRS's inquiry regarding ORG's activities, President responded as follows:

There are NO restrictions or requirements for participation. ANY person may attend the homebuyer course.

There is NO fee associated with the course. The course is administered by registered Real Estate agents and Mortgage Loan agents. NO one may charge for attendance, reservation, or completion of the course. It is FREE.

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No person is directed to a Lender, a Real Estate agent, or institution of any kind. Real Estate Agents and Lending Institutions may benefit from offering this course to the general public by offering the course in their community rooms and gathering a group of interested home buyers.

ORG requires a prospective homebuyer to complete either the CO-1 "A GUIDE TO HOME OWNERSHIP" or the "CO-3" study guide. Community does not publish or generate its own course or agenda.

The educational course is publicized by Broadcast Faxing a flyer to real estate agents through the United States (copy attached). The Real Estate agents determine how to best use the course material."

A determination letter was issued by the IRS on April 12, 19XX recognizing the tax exempt status of ORG under the Code §501(c)(3) and as an organization that is not a private foundation as described under the Code §§509(a)(1) and 170(b)(1)(A)(vi).

Operational Information:

During the years under exemption, the only activity ORG engaged in, other than fundraising, is the down payment assistance program (DPA) for homebuyers and homesellers. According to the general ledger provided by President, there were 978 DPA's provided in 20XX with the total assisted funds of \$\$ from home sellers. The following table displays a summary of the transactions by state:

State	Amount of DPA by State	Amount DPA by State in %	# of DPA by State	# of DPA by State in %
XYZ				0.31%
XYZ				0.20%
XYZ				0.10%
XYZ				2.56%
XYZ				68.40%
XYZ				7.46%
XYZ				1.23%
XYZ				0.31%
XYZ				15.95%
XYZ				0.41%
XYZ				0.61%
XYZ				0.10%
XYZ				1.84%
XYZ				0.20%
XYZ				0.10%
XYZ				0.10%
XYZ				0.10%

EXPLANATION OF ITEMS

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and 20XX

Total all states

100.00%

President explains that the DPA program is obtaining clients from realtors who will recommend buyers to participate in DPA program. The buyer then goes on the website, submits an application, completes the education (see further discussion below) and then prints out the certificate. ORG then faxes the approval to the lender or the escrow company.

A sample of 84 cases reviewed indicate the process of the DPA program as the 4-step process as follows:

Step 1 – A gift of funds to be used for the downpayment of a house is requested primarily via internet by completing the online application at responsiblehome.com by anyone involved in the real estate transactions.

Step 2 – After the request is received, ORG will fax 8 documents within a couple of hours to the closing agent involved with the real estate transaction. They are:

1. Priority Fax – a fax cover of ORG with the following statement in its body:

“Note: The credit to the **buyer** on Line 206 of the CO-2-1 for the Gift Funds should read: “**ORG GIFT FUNDS**”. The debit to the **Seller** on Line 1305 of the CO-2-1 for the Service Fee should read: “**ORG SERVICE FEE**”. Thank you!” [Emphasis added]

2. Closing Agent Instructions and Disbursement Authorization Form – this document summarizes the application information, spell out the fees due to ORG and instructs the closing agent to collect and submit/maintain certain documents.

3. Final Disbursement Instructions – using ORG’s letterhead, this letter instructs the closing agent to pay the fee to CO-4 (CO-4). (See below for further discussion about CO-4.)

4. ORG Escrow Draft – President explains the Escrow Draft as ORG’s authorization to the escrow/closing agent to take the funds that should be going to ORG from the seller’s account and to credit them to the buyer for the real estate transaction in question. The gift funds never leave the escrow accounts, and the general ledger transactions of gift funds are not a reflection of the transactions within the ORG’s bank account. In other words, the contribution from the seller of the property goes directly to the buyer of the same property. It can also be stated as the contributions don’t get “circulated” in the pool of funds for future buyers.

This document looks similar to a business check. One primary difference is that the draft has no banking information such as bank name, bank number, account number or check number. A standard copy of this draft looks similar to the following:

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(ORG logo)	ORG TIN	ESCROW DRAFT	(draft #)
			(date)
PAY TO THE ORDER OF	(closing agent's name)		\$
		DOLLARS	
Closing agent is authorized to draft ORG funds, you will receive upon completion of all contingencies, for credit to: (buyer's name and ORG case #)			(President's stamped signature)

5. Participating Home Agreement – using ORG letterhead this document is prepared for the seller to sign. The agreement requires a seller to agree to a certain amount of service fee and to provide a qualified buyer with a standard 1-year home protection plan including Central Air and Heating, and pest inspection report.

The document gives the appearance that ORG is watching out for the buyer's interest. In reality, if the parties involved don't want to comply with the requirement, they only need to request a waiver. There are 4 waivers among the 84 samples.

6. ORG Grant – ORG generates a certificate to each buyer as an indication of its commitment to provide down payment assistance for the purchase of a residence. No grant amount is indicated on this form.

7. Grant Funds Application – the information received via online application are transcribed onto this form with the following additional information:

“Buyer hereby applies for a Grant of Gift Funds for Down Payment and Closing cost Assistance as a “Qualified Buyer”. A Qualified Buyer must satisfy the following criteria:

1. Purchase a Participating Home.
2. Complete an Approved Home Ownership counseling course.
3. Participate in and be credit approved for an Eligible Loan Program.”

8. Buyer's acknowledgement of Property Value – using ORG letterhead, this document is produced for the buyer to sign under the following statement:

“I (We) the Buyers of a home located at: ...

Have been awarded a Grant of Gift Funds from ORG in the amount of: ...

I (We) acknowledge that I (We) have received and reviewed a current appraisal of this property and I (We) am familiar with the location and understand the values of similar properties adjacent to this property. I (We) am aware this property may have been purchased by the current Seller at a lower price within the past 12 months. I (We) understand that I (We) am under no obligation whatsoever to repay this gift from ORG”

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It is not clear why there is a requirement to sign this document when the parties involved can adjust the sale price.

Step 3 – As soon as step 2 is completed, ORG will fax 4 of the documents to the mortgage company. These four documents are (1) Participating Home Agreement, (2) ORG Grant, (3) Grant Funds Application, and (4) ORG Draft.

Step 4 – If there are changes to original amount, the changed information will be submitted via internet and steps 2 and 3 will be repeated. Otherwise ORG will wait for the closing agent to issue a check to CO-4 in the amount of the service fee charged.

CO-4 solely markets and administers the DPA program. ORG has an agreement with CO-4 that after ORG's "outside fundraising activities, they make up any shortfall needed for down payment assistance." The agreement isn't available for our review. In a letter dated July 24, 20XX, President stated that CO-4 was not a related entity. However, other records indicate CO-4 is a for-profit entity under President's control. He is the President of CO-4 and V-P/CO-4 is the Vice President. As explained above, all fees related to DPA are paid to CO-4. CO-4 in turn hires several employees to handle the work related to DPA and pays for all the related expenses. CO-4 also compensates President and V-P/CO-4.

Educational Activity:

In regards to the educational aspect of the DPA, ORG only provides on-line educational materials on its website at communityhousingdevelopment.org. The "Homebuyer Education" link at the website leads to the "How to Buy a Home with a Low Down Payment" document. A visitor, not necessary a homebuyer, can scroll straight down to the bottom of this document, fills out the requested information and prints out the certificate. In other words, ORG has no knowledge or control over whether a buyer actually reads the material and understand it.

Smoke Free Housing Activity:

ORG tried to explain to us that it has other charitable activities. The first one is smoke free housing activity. In a letter dated May 17, 20XX, ORG provides printouts of its website regarding "smoke free environment." One of the statement is "Recipients of Down Payment Grant Funds are requested to pledge that their home will be "Smoke Free"." To support this statement, ORG provides a copy of the application for a grant in 20XX for a portion of the Tobacco Fund to "educate homebuyers on the importance of maintaining their health and protecting their children from the harmful effects of second hand smoke." ORG stated in the application that it would require the homebuyers to enter into No Tobacco Tolerance Home agreement in order to receive the "free" Gift Funds to purchase their home and follow up with monthly monitoring. ORG talked about \$\$ matching funds coming from CO-4. It further stated that administrative and non-administrative responsibilities and their related cost would be handled and incurred by CO-4.

In response to our follow-up question, in a letter dated August 21, 20XX, ORG explains that no funds were received. Other records indicate ORG did not do anything related to smoke free housing. ORG's website back in 20XX also did not have any information regarding this activity.

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Clean-up of Contaminated Properties:

The second purported charitable activity is clean-up of contaminated properties. In a letter dated May 17, 20XX, ORG provides printouts from its Contaminated Properties website. ORG explains that "This is a fundraising activity that serves the greater public need by remediation of contaminated and City properties. Within this section is our "Police Partnership" program. ORG partners with law enforcement agencies to clean and make habitable property that was seized for methamphetamine production. We remediate these properties, sell them and share the proceeds with that police department."

In response to our follow-up questions, ORG states that "We are in negotiation states with these law enforcement agencies. To date, nothing has yet been finalized. These are confidential negotiations with propriety information. We prefer not to disclose the details at this time. Contaminated Property is a new venture that has not yet completed a project."

Fundraising Activities:

In a letter dated May 17, 20XX, ORG talks about its broad based fundraising activities which includes "but are not limited to Timeshare donations, Car Donations, Memorial Donations, Charitable Remainder Trusts, Gift Annuities, Real Estate donations, and cash donations." It also provides a copy of the "Virtual Donor Wall" which lists the "people who have made direct donations to ORG, none of which are sellers of homes that buyers received assistance nor do they have anything whatsoever to do with the down payment assistance program."

In response to our follow-up questions, ORG indicates it has only received timeshare donations which began in early 20XX and provides documents related to these donations. These documents indicate all timeshare donations went through CO-5, another for-profit entity under President's control. CO-5 will auction the donated timeshares on CO-6. When proceeds come in, CO-5 will make a check out to ORG net of service fee for itself. The service fees were at the rate of 20% from February 20XX through January 20XX. Beginning on January 29, 20XX, the service fees went up to 50%. However, there are no contracts or service agreements between ORG and CO-5.

Accounting of Financial Transactions:

Each year, ORG timely filed Forms 990. It reported the total funds received from home sellers that are used to pay the closing cost of the home buyers as income and expense. It also reported a small amount of cash balance as its asset. For the years 20XX through 20XX, ORG reported its financial information on its Forms 990 as follows:

Description	20XX12	20XX12	20XX12	20XX12	20XX12
Income: Direct public support					
Expense: Grants & allocations					
Net Income					
Year end Balance Sheet: Cash					

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Since the proceeds from the donations are not reported on the Form 990 filed for the year ending December 31, 20XX, we expanded the examination to include 20XX and 20XX years. The general ledgers provided only had the total amount for the DPA related transactions. The transactions related to timeshare donations were a summary of the documents provided earlier.

We requested copies of bank statements and cancelled checks from February 20XX through January 20XX, but only received the ones for February through August in 20XX and July and August in 20XX. None of the bank transactions are accounted for in the general ledgers. The checks issued in 20XX and 20XX are all signed by EMP-1, an employee of CO-4.

The bank information also doesn't match the amounts shown on Forms 990, which implies that the funds are not accounted for, monitored or reviewed by anyone.

Minutes of Meetings:

President provides four minutes of annual directors' meetings. Other than the date of the meeting the four annual minutes were identical and contain no substantive discussion of their meetings.

LAW

The Code §501(c)(3) provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided no part of the net earnings inures to the benefit of any private shareholder or individual.

The Income Tax Regulations ("the Regulations") §1.501(c)(3)-1(c)(1) provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in § 501(c)(3) of the Code. An organization must not engage in substantial activities that fail to further an exempt purpose.

The Regulations §1.501(c)(3)-1(d)(1)(ii) of provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. To meet this requirement it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests.

The Regulations §1.501(c)(3)-1(d)(2) provides that the term "charitable" includes relief of the poor and distressed or underprivileged, lessening of the burdens of government, and promotion of social welfare by conducting programs to combat community deterioration and juvenile delinquency.

The Regulations §1.501(c)(3)-1(d)(3) defines the term "educational" for the purposes of §501(c)(3) of the Code as including the instruction of the public on subjects useful to the individual and beneficial to the community.

The Regulations §1.501(c)(3)-1(d)(1) provides that an organization may be exempt as an organization described in §501(c)(3) of the Code if it is organized and operated exclusively for one or more of the following purposes:

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(a) religious, (b) charitable, (c) scientific, (d) testing for public safety, (e) literary, (f) educational, or (g) prevention of cruelty to children or animals.

The Regulations §1.501(c)(3)-1(e) provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of §501(c)(3) of the Code if the trade or business furthers an exempt purpose, and provided the organization's primary purpose does not consist of carrying on an unrelated trade or business.

In *Better Business Bureau of Washington, D.C. v. U.S.*, 326 U.S. 279, 283 (1945), the Supreme Court held that the "presence of a single... (nonexempt) purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly... (exempt) purposes."

In *Easter House v. U.S.*, 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F.2d 78 (Fed.Cir.) cert. denied, 488 U.S. 907 (1988), the court found an organization that operated an adoption agency was not exempt under § 501(c)(3) of the Code because a substantial purpose of the agency was a nonexempt commercial purpose. The court concluded that the organization did not qualify for exemption under § 501(c)(3) of the Code because the primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization's argument that the adoption services merely complemented the health related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff's adoption service is its primary goal" and held that the organization was not operated exclusively for purposes described in §501(c)(3) of the Code. *Easter House*, 12 Cl. Ct. at 485-486.

In *American Campaign Academy v Commissioner*, 92T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in § 501(c)(3) of the Code because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with Republican Party entities and that most of the organization's graduates worked in campaigns for Republican candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting Republican candidates and entities. Although the candidates and entities benefited were not organization "insiders," the court stated the conferral of benefits on disinterested persons who are not members of a charitable class may cause an organization to serve a private interest within the meaning of §1.501(c)(3)-1(d)(ii) of the Regulations. The court concluded by stating that even if the Republican candidates and entities did "comprise a charitable class, the organization would bear the burden of proving that its activities benefited members of the class in a non-select manner."

In *Aid to Artisans, Inc. v. Commissioner*, 71 T.C. 202 (1978), the court held an organization that marketed handicrafts made by disadvantaged artisans through museums and other nonprofit organizations and shops was operated for exclusively charitable purposes within the meaning of §501(c)(3) of the Code. The organization, in

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ORG

cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence given by the Bureau of Indian Affairs or other government agencies. The organization marketed only handicrafts it purchased in bulk from a community of craftsmen. It did not market the kinds of products produced by studio craftsmen, nor did it market the handicrafts of artisans who were not disadvantaged. The court concluded that the overall purpose of the activity was to benefit disadvantaged communities. The method it used to achieve its purpose did not cause it to serve primarily private interest because the disadvantaged artisans directly benefited by the activity constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans. Therefore, the court held that the organization operated exclusively for exempt purposes.

Revenue Ruling 2006-27 discusses three examples of organizations providing downpayment assistance and whether each qualified as an organization described in § 501(c)(3) of the Code.

Situation 1 describes X, a non-profit corporation, that helps low-income individuals and families purchase decent, safe and sanitary homes throughout the metropolitan area in which it is located. As a substantial part of its activities, X makes assistance available exclusively to low-income individuals and families to provide part or all of the funds they need to make a down payment on the purchase of a home. Individuals are eligible to receive assistance from the downpayment assistance program if they are low-income individuals, have the employment history and financial history necessary to qualify for a mortgage, and would so qualify but for the lack of a down payment. To fund its down payment assistance program and other activities, the organization conducts a broad based fundraising program that attracts gifts, grants and contributions from several foundations, businesses and the general public.

In Situation 1, X's grantmaking process is structured to ensure that its staff awarding grants does not know the identity of the party selling the home to the grant applicant or the identities of any other parties, such as real estate agents or developers, who may receive a financial benefit from the sale. The staff also does not know whether any of the interested parties to the transaction have been solicited for contributions to the organization or have made pledges or actual contributions to the organization. Further, the organization does not accept any contributions contingent on the sale of a particular property or properties.

In Situation 1, the revenue ruling held the organization qualifies for exemption because its purposes and activities relieve the poor, distressed and underprivileged by enabling low-income individuals and families to obtain decent, safe and sanitary homes. The way the organization conducts its down payment assistance program establishes that its primary purpose is to address the needs of its low-income grantees. The organization conducts a broad based fundraising program, and receives support from a wide array of sources. Their policies of ensuring that its grantmaking staff does not know the identity or contributor status of the party selling the home to the grant applicant (or any other party who may receive a financial benefit from the sale), and of not accepting contributions contingent on the sale of any particular properties, ensure that it is not beholden to any particular donors or other supporters whose interest may conflict with that of the low-income buyers the organization is working to help.

In Situation 2, Y is a nonprofit corporation that is like X in all respects as set forth in Situation 1, except as follows. Under Y's grantmaking procedures, Y's staff considering a particular applicant's application knows the identity of the party selling the home to the grant applicant and may also know the identities of other parties,

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such as real estate agents and developers, who may receive a financial benefit from the sale. Moreover, in substantially all of the cases in which Y provides down payment assistance to a home buyer, Y receives a payment from the home seller. Further, there is a direct correlation between the amount of the down payment assistance provided by Y in connection with each of these transactions and the amount of the home seller's payment to Y. Finally, Y does not conduct a broad based fundraising campaign to attract financial support. Rather, most of Y's support comes from home sellers and real estate-related businesses that may benefit from the sale of homes to buyers who receive Y's down payment assistance.

In Situation 2, the revenue ruling held Y does not qualify as an organization described in § 501(c)(3). To finance its down payment assistance activities, Y relies on sellers and other real-estate related businesses that stand to benefit from the transactions Y facilitates. Furthermore, in deciding whether to provide assistance to a low-income applicant, Y's grantmaking staff knows the identity of the home seller and may also know the identities of other interested parties and is able to take into account whether the home seller or another interested party is willing to make a payment to Y. Y's receipt of a payment from the home seller corresponding to the amount of the down payment assistance in substantially all of the transactions, and Y's reliance on these contributions for most of its funding indicate that the benefit to the home seller is a critical aspect of Y's operations. In this respect, Y is like the organization considered in Easter House, which received all of its support from fees charged to adoptive parents, so that the business purpose of the adoption service became its primary goal and overshadowed any educational or charitable purpose. Like the organization considered in American Campaign Academy, Y is structured and operated to assist private parties who are affiliated with its funders. Like the organizations considered in American Campaign Academy, Easter House, and Columbia Park Recreation Association, Y also serves an exempt purpose, but because Y is not operated exclusively for exempt purposes, Y does not qualify for exemption from federal income tax as an organization described in § 501(c)(3).

In Situation 3, Z is a nonprofit corporation formed to combat community deterioration in an economically depressed area that has suffered a major loss of population and jobs. Studies have shown that the average income in the area is below the median level for the State. Z cooperates with government agencies and community groups to develop an overall plan to attract new businesses to the area and to provide stable sources of decent, safe and sanitary housing for the area residents without relocating them outside the area. As part of the renewal project, Z receives funding from government agencies to build affordable housing units for sale to low and moderate-income families. As a substantial part of its activities, Z makes down payment assistance available to eligible home buyers who wish to purchase the newly-constructed units from Z. Z also offers financial counseling seminars and conducts other educational activities to help prepare potential low and moderate-income home buyers for the responsibility of home ownership. To fund its down payment assistance program and other activities, Z conducts a broad based fundraising program that attracts gifts, grants and contributions from several foundations, businesses and the general public.

In Situation 3, the revenue ruling held that although Z does not limit its down payment assistance program to low-income recipients, Z's down payment assistance program still serves a charitable purpose described in § 501(c)(3) because it combats community deterioration in a specific, economically depressed area that has suffered a major loss of population and jobs. Through a combination of counseling and financial assistance, Z helps low and moderate-income families in that area to acquire decent, safe and sanitary housing and to prepare for the responsibilities of home ownership. In this respect, Z is like the organization described in Situation 3 of

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Rev. Rul. 70-585. Because Z is operated exclusively for charitable purposes, Z qualifies for exemption from federal taxation as an organization described in § 501(c)(3).

The revenue ruling concluded that down payment assistance payments for home buyers in Situations 1 and 3 are made by those organizations out of a detached and disinterested generosity and from charitable or like impulse, rather than to fulfill any moral or legal duty, and thus qualify for exclusion from such home buyers' gross incomes as "gifts" under § 102. The benefits provided to the home buyers in these circumstances are sufficiently removed from the interests of any home sellers or sales agents that they proceed from a detached and disinterested generosity on the part of the donor organization, and such grants lack the indicia of a rebate, price adjustment, or *quid pro quo* incident to a sale. In Situation 2, the organization is not operated exclusively for charitable purposes, and consequently, does not qualify for exemption from federal income tax as an organization described in § 501(c)(3).

Revenue Ruling 67-138, 1967-1 C.B. 129, holds that a nonprofit organization created to help low income persons obtain adequate and affordable housing may be exempt from Federal income tax under §501(c)(3) of the Code because it relieves the poor and distressed or underprivileged. It describes the organization's activities, which are directed toward assisting low-income families obtain improved housing, as "(1) conducting a training course relative to various aspects of housebuilding and homeownership, (2) coordinating and supervising joint construction endeavors, (3) purchasing building sites for resale at cost, and (4) lending aid in obtaining home construction loans. No charge is made for any of these services."

Revenue Ruling 70-585, 1970-2 C.B. 115, provides that nonprofit housing organizations created to aid low and moderate income families by lessening neighborhood tensions, eliminating prejudice and discrimination, and combating community deterioration may qualify for exemption under §501(c)(3) of the Code.

Revenue Ruling 85-1, 1985-1 C.B. 177, and Revenue Ruling 85-2, 1985-1 C.B. 178, provide that the criteria to be used to determine whether or not an activity is lessening the burdens of government are "first, whether the governmental unit considers the organization's activities to be its burden; and second, whether these activities actually lessen the burden of the governmental unit."

Revenue Ruling 68-17, 1968-1 C.B. 247 provides that a nonprofit organization formed to aid low-income families living in deteriorating neighborhoods in improving their homes may qualify for exemption from Federal income tax under §501(c)(3) of the Code. The organization's "membership consists of other nonprofit institutions, neighborhood groups, and individuals. To accomplish its purposes, a model demonstration housing program is conducted by the organization. It is financed in part by a grant from the Department of Housing and Urban Development under Section 207 of the Housing Act of 1961 (42 U.S.C.A. 1436). The objects of the demonstration program are to test the feasibility, cost, and procedural and financial aspects of providing housing for low-income families through the acquisition, rehabilitation, and resale or lease of residential structures in a deteriorating neighborhood."

"Homes rehabilitated by the organization in the model demonstration program are sold or leased to low-income or displaced families on a nonprofit basis. The organization does no new construction."

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HUD Directive 4155.1 REV-5, issued in October 2003, describes about "Gift Funds" in Chapter 2, Section 3 C as follows:

C. Gift Funds. An outright gift of the cash investment is acceptable if the donor is the borrower's relative, the borrower's employer or labor union, a charitable organization, a governmental agency or public entity that has a program to provide homeownership assistance to low- and moderate-income families or first-time homebuyers, or a close friend with a clearly defined and documented interest in the borrower. The gift donor may not be a person or entity with an interest in the sale of the property, such as the seller, real estate agent or broker, builder, or any entity associated with them. Gifts from these sources are considered inducements to purchase and must be subtracted from the sales price. No repayment of the gift may be expected or implied. ... [Emphasis added.]

The Directive 4155.1 Rev.4, issued in September 1995 has similar wordings for the "Gift Funds" description and nonprofit organization requirements.

Effective date of revocation

The Regulations §1.501(a)-1(a)(2) states that an organization may rely upon the IRS's determination of its exemption status so long as there are no substantial changes in the organization's character, purposes, or methods of operation. The IRS may revoke a favorable determination letter for good cause.

The Regulations § 601.201(n)(6) spells out how an exemption status can and will be revoked. The revocation or modification may be retroactive if the organization omitted or misstated a material fact, operated in a manner materially different from that originally represented, or engaged in a prohibited transaction.

GOVERNMENT POSITION

In order for an organization to retain its exempt status it must demonstrate to the IRS that it meets both the organizational and the operational tests. The facts stated above indicate that ORG failed the operational test.

Charitable purposes include relief of the poor and distressed. See §1.501(c)(3)-1(d)(2) of the Regulations. ORG's DPA program does not operate in a manner that establishes that its primary purpose is to address the needs of low-income people by enabling low-income individuals and families to obtain decent, safe housing. See Revenue Ruling 20XX-27, Situation 2. The DPA program did not exclusively serve low-income persons. ORG does not have any income limitations for a homebuyer to participate in its down payment assistance program, which means the program is open to every homebuyer.

ORG's DPA program does not limit assistance to certain geographic areas or target those areas experiencing deterioration or neighborhood tensions. See Revenue Ruling 20XX-27, Situation 3. Arranging or facilitating the purchase of homes in a broadly defined geographic area does not combat community deterioration or serve other social welfare objectives within the meaning of the Code §501(c)(3).

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ORG's DPA program provided a private benefit to various parties. Like the organization considered in American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), ORG is structured and operated to assist the private parties who fund it and give it business. Sellers who participate in DPA program benefit from having access to a wider pool of buyers, thereby decreasing their risk and the length of time the home is on the market. They also benefit by being able to sell their homes at the listed prices or by being able to reduce the amount of the negotiated discount on their homes. Buyers who participate in down payment assistance program benefit by being able to purchase a home without having to commit more of their own funds.

To finance its DPA activities, ORG relies exclusively on sellers. Using the "escrow draft," ORG requires the home seller to transfer the DPA amount directly to the buyer's escrow account. There was no limit on the amount of grant. However, the size of the grant would affect the amount of fee ORG/CO-4 would collect. Most of the fees collected were at the rate of 1% of the selling price. The closing agent of the seller would issue a check for the stated fee amount to ORG or CO-4.

ORG's assistance to a participating home buyer comes directly and solely from the participating seller of the same property. ORG's reliance on these payments for all its funding indicates that the benefit to the home seller is a critical aspect of ORG's operations. The sellers get the benefit of having their property sold quicker (due to greater number of potential home buyers) without actually incurring any costs. Since the amount that a home buyer receives from ORG is incorporated into the sale price of a home, the purported beneficiaries in fact does not receive anything from ORG. In this respect, ORG is like the organization considered in Easter House which provided health care to indigent pregnant women only when a family willing to adopt a woman's child sponsored the care financially.

Operating a trade or business of facilitating home sales is not an inherently charitable activity. Unlike the trade or business in Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), ORG's trade or business is not utilized as a mere instrument of furthering charitable purposes but is an end in itself. ORG provides services to home sellers for which it charges a market rate fee. ORG does not limit its services primarily to persons within a charitable class. ORG does not solicit or receive any funds from parties that do not have interest in the down payment transactions. Like the organizations considered in American Campaign Academy, supra, and Easter House v. U.S., 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.) a substantial part of ORG's activities furthered commercial rather than exempt purposes.

CO-2 rules and regulations also does not allow for an interested party such as the seller of the property to provide gifts to the buyer.

Other Charitable Activities:

In a letter dated May 17, 20XX, President points out several other activities ORG is involved in and stated "Thank you for this opportunity to clarify matters and to show that we are not just another down payment "scam". We serve a real purpose to the community. We have been asked in the past to mimic CO-7, CO-8 and other larger companies, but we feel that keeping our mission, our purpose and our integrity is more important than dollar volume." We reviewed the documents and made follow-up inquiries and found out the following:

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Educational Activity: Educating the homebuyers is the stated purpose within the application for exemption status. However, ORG does not conduct classroom type of training to homebuyers. ORG does not disseminate any training materials to potential homebuyers. ORG only posts its training materials on its website which can be accessed by anyone anytime. No testing is involved. To be certified as an "educated" homebuyer, a visitor only needs to complete personal information at the end of the webpage. ORG even shifts the responsibility of maintaining these certificates to the lenders and escrow companies. In other words, there is no assurance that a homebuyer reads through the material, understands it and is qualified to receive the certificate. Posting the educational material on the website and allowing a visitor to printout a personalized certification does not constitute educating the visitor.

Smoke Free Housing Activity: This activity is limited to completing a grant application on August 18, 20XX to receive Tobacco Funds. The grant, if received, will have been incorporated into the DPA program by having homebuyers enter into No Tobacco Tolerance Home agreement. ORG did not receive any grants and none of the homebuyers we reviewed entered into No Tobacco Tolerance Home agreement. An activity that did not take place can not be used as an exempt activity of ORG.

Clean-up of Contaminated Properties: ORG indicates the activity is still in a negotiation state. They are confidential negotiations with proprietary information. ORG prefers not to disclose the details. An activity that can't be disclosed in sufficient detail for us to determine whether it meets the operational test can't be used as an exempt activity of ORG.

Fundraising Activities: Fundraising activity by an exempt organization doesn't affect its exemption status. What will affect the exempt status is how the funds are being raised and how the proceeds are being used. In this case, all matters related to fundraising are handled by CO-5, an entity under President's control. There are no contracts between ORG and CO-5. The service fee changed from 20% to 50% without any explanation. The net proceed is over \$\$ in 20XX. However, ORG does not report this on its Form 990 and no accounting is made as to how the funds are being used.

Board Member Involvement: In addition to President and V-P/CO-4, ORG has 4 to 5 other board members. However none of these other board members are involved in any decision making process that will have required their involvement. In other words, President and V-P/CO-4 have full control over ORG.

ORG's primary activity, the DPA program, fails to pass the operational test, and it is not the activity described in the application for the exemption status. Other charitable activities ORG claims to be doing did not occur. Therefore, the ORG does not qualify as an organization described in the Code §501(c)(3) and its exemption status should be revoked effective April 28, 19XX.

CONCLUSION

Based on the information secured during the examination, we conclude that ORG is not operated for exempt purposes under §501(c)(3) of the Code. An organization can not be recognized as exempt under §501(c)(3) unless it shows that it is operated exclusively for charitable, education, or other exempt purposes. Among other things, ORG activities must demonstrate conclusively that it meets the operational test of §1.501(c)(3)-1(c) of the Regulations. The activities show that the primary purpose is to operate a down payment assistance program

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that does not exclusively serve a purpose described in §501(c)(3) of the Code. ORG operates its primary activity, DPA program, since its inception. However, ORG does not notify the service of its primary activity. Therefore, the exempt status granted to ORG should be revoked effective from the date of its inception: April 28, 19XX.

If the revocation is sustained, ORG is required to file Forms 1120 for the years 20XX and after.