

Internal Revenue Service
Appeals Office
1352 Marrows Road, Suite 104
Newark, DE 19711-5445

Release Number: **201009018**
Release Date: 3-5-10
Date: 12-9-09
UIL Code: 501.03-05

A

B

Department of the Treasury

Person to Contact:

Employee ID Number:

Tel:

Fax:

Refer Reply to:

AP:FE:SAC:SKP

In Re:

EO Revocation

Tax Period(s) Ended:

Form Number

1120

Employer Identification Number

C

CERTIFIED MAIL

Last Day to File a Petition with the

United States Tax Court: MAR 05 2010

Dear

This is a final adverse determination as to your exempt status under section 501(c)(3) of the Internal Revenue Code. It is determined that you are no longer recognized as exempt from Federal income tax under Section 501(c)(3) of the Internal Revenue Code, effective January 1, 2003. Your application for exemption (Form 1023) and associated materials misstated material fact, and you operated in a manner materially different than originally represented.

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.

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 before the 91st (ninety-first) day after 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 from the United States Tax Court, write to United States Tax Court, 400 Second Street, NW, Washington, D.C. 20217.

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

You also 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 is not able to reverse legally correct tax determinations, nor extend the time fixed by law that you have to file a petition in the U.S. Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. If you want Taxpayer Advocate assistance, please contact the Taxpayer Advocate for the IRS office that issued this notice of deficiency. See the enclosed Notice 1214, *Helpful Contacts for Your "Notice of Deficiency"*, for Taxpayer Advocate telephone numbers and addresses.

Thank you for your cooperation.

Sincerely,


CHARLES FISHER
TEAM MANAGER

Enclosures:

Notice 1214 Helpful Contacts for your 'Deficiency Notice'



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
Internal Revenue Service
300 N. Los Angeles Street, MS 7300
Los Angeles, CA 90012

SEP 13 2007

Taxpayer Identification Number:
EIN

Form:
990

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:
Telephone:
Fax:

ORG

Certified Mail - Return Receipt Requested

Dear

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

Letter 3618 (04-2002)
Catalog Number 34809F


If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,



Marsha A. Ramirez
Director, EO E xaminations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer	Tax Identification Number	Year/Period ended
ORG	EIN	12/31/200X & 12/31/200X

Legend

ORG =Final Name of organization
ORG1=Original Name of organization
NN=Name of individual
RR=Related organization
UR=Unrelated organization

x=Amount
X=Year
EIN=EIN of the organization
EINR=EIN of the Related organization
FN=Family Name

ISSUE:

Whether **ORG** operated exclusively for exempt purposes within the meaning of Internal Revenue Code § 501(c) (3) and the Regulations?

FACTS:

Organizational Information:

ORG1 (EIN:) was incorporated as a not-for-profit corporation on September 03, 199X. **NN** signed the Articles of Incorporation as the Incorporator.

The specific and primary purpose of the corporation was for charitable and educational purposes in connection with the following:

- (a) *To support and promote positive family values as the basis for improving society as a whole.*
- (b) *To promote the importance of "family" and the family unit as the groundwork for the development of today's youth.*
- (c) *To provide education and guidance to individuals and families on moral and religious values, including meetings and seminars designed to bring families close together.*
- (d) *To assist other charitable, educational and social welfare organizations in the conduct of similar activities.*
- (e) *To establish a main office or offices for the conduct of the activities necessary to carry out the purposes of this corporation.*
- (f) *To engage in any and all lawful activities incidental to the foregoing purposes, except as restricted herein.*

On October 23, 199X the organization applied for recognition as a tax-exempt organization under Internal Revenue Code (IRC) § 501(c) (3) on Form 1023, *Application for Recognition of Exemption Under Section 501(c) (3) of the Internal Revenue Code*. **NN** signed the Form 1023 as the president and described the organization's activities as follows:

ORG1 has been organized and will be operated as a charitable organization to provide and promote guiding principles designed to unite families and society through faith, courage, love, commitment and integrity. The organization shall also assist federal, state

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and local governments and agencies as well as other 501(c)(3) organizations in lessening their burdens and facilitating the education and services they provide in general assistance to families and in bringing families and people together.

To those ends, the organization will provide educational and promotional materials through written media (and secondarily through other media) designed to provide guiding principles to individuals and families for a positive, moral and united existence. The organization will also provide programs and seminars for the same purposes, as well as to encourage faith in a Supreme Being; acknowledge and release the unlimited potential of the individual; share knowledge and understanding; promote unselfish service to each other and families, and to build integrity and strength and morals into values.

These purposes will be accomplished largely through the promotion and production of live events carrying these principles and themes and using the influence and talents of NN and his associates. The organization will also set up an internet site to identify and promote the values described herein.

The sources of financial support stated as follows:

- (i) grants and contributions from individuals, organizational and corporate donors, and*
- (ii) investment income.*

A determination Letter 1045 was issued on February 14, 199X granting exemption status under Code §501(c) (3) as an organization that is not a private foundation because it is described under Code §509(a) (1) and 170(b) (1) (A) (vi), with an advanced ruling period from September 23, 199X through December 31, 200X.

On August 03, 200X, **ORG1** filed Articles of Amendment with the State of (c) change its name to **ORG** and added the following provision under its specific and primary purposes:

To act as a charitable and educational organization to assist persons, financially or otherwise, who are not able to meet the financial burdens of purchasing or otherwise owning their own home and to provide services and programs designed to improve and revitalize single family neighborhoods throughout the country.

The amended Articles signed by **NN** Chairman of the Board, on May 08, 200X. The organization sent its amended Articles to the IRS to update its records.

A classification Letter 1050 was issued on December 19, 200X classifying organization as a public charity under Code 170(b) (1) (A) (vi).

A new entity named **RR** was organized with **EINR** by **NN** in 200X and it filed Forms 990 for

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years 200X through 200X.

Operational Information:

ORG conducted a down payment assistance (DPA) program since 200X and the program was introduced by **NN** of **UR** Mortgage. **ORG** conducted this program with **UR** Mortgage and received a fee of \$x and decreased to below \$x for each down payment assistance transaction that took place. Since July 200X, the **ORG** conducted no other programs besides the down payment assistance program.

Agreement with UR Mortgage Company

In the agreement, the **ORG** was referred to as _____ and the **UR** Mortgage Company was referred to as **UR**. The agreement is as follows:

I. Background. _____ desires to create a nationwide homebuyer down payment assistance program, wherein qualified first time homebuyers will apply for and receive a grant for the purchase of a home. The homebuyer assistance program essentially operates as follows: A homebuyer applies for a grant from _____ for the purchase of a home. The real estate contract is negotiated between the qualified homebuyer and the seller of a home and includes the seller's agreement to pay _____ the amount of the grant plus a service fee of \$x. At closing of the home purchase, _____ wires the grant to the title company and applies it toward the homebuyer's purchase of the home. Following closing, the title agent wires the amount of the grant and \$x of the service fee to _____ and \$x of the service fee to **UR**.

- II. Services Provided by UR In consideration of an administrative fee of \$x paid to **UR** by _____ on each homebuyer transaction, **UR** will provide the following services:
- A. Create underwriting guidelines for qualification in the homebuyer assistance program, including homebuyer education courses;
 - B. Draft contract clause regarding the homebuyer assistance program to be inserted in the purchase contract between the buyer and seller, draft the homebuyer application for participation in homebuyer assistance program and draft gift letter, with all necessary title instructions;
 - C. Accept and process borrower and seller applications to participate in the homebuyer assistance program, including review of purchase contracts and automated underwriting approval of the borrower;
 - D. Issue grant approval to participating lender and/or title company in the form of a gift letter; and
 - E. Coordination of money wire transfers to and from **UR** and the applicable title company.

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III. Services Provided by Foundation. For good and valuable consideration, including the receipt of a \$x service fee on each homebuyer transaction, _____ agrees to fund the qualified homebuyer's grant. _____ further agrees to utilize its financial and administrative resources in marketing the homebuyer assistance program on a nationwide level to realtors, mortgage lenders and prospective homebuyers.

According to the response from the organization, **ORG** was not involved in any paperwork for documentation on the transactions. The money came in and went back out. **ORG** discontinued the program in 200X because **ORG** was not happy with how the program was working and not being able to get information and paperwork from **UR Mortgage**.

How the DPA program works:

ORG states how the DPA program works as follows:

*The Seller or Builder of the home being purchased pays a service fee to **ORG** for their services. The fee is a percentage of the sales price of the home based on the amount of cash the buyer needs to get into the home and then x% of the sales price or \$x, which ever is less and then added to the gift amount. For example, if the buyer needs a gift of x% for their down payment; the seller would pay a x% service fee to **ORG**. At closing, the buyer receives a "bona fide gift" from **ORG** for x% of the sales price. After closing, the seller pays the service fee to **ORG**, which comes from the Sellers net proceeds at the time of funding.*

ORG is available to any qualified homebuyer including first-time homebuyers. **ORG** offers funds in the form of a Gift, to homebuyers to be used for their down payment and / or closing costs.

Eligibility Requirements:

- Homebuyer must qualify and be approved for a single family 1-4 unit, FHA or Conventional loan through an automated underwriting system such as Loan Prospector, Desktop Underwriter, Desktop Originator or a Mortgage Investor specific underwriting system. Borrower's that do not meet the automated underwriting criteria, may still be eligible based on traditional underwriting on a case to case basis.
- The Homebuyer's must complete a homeownership education course, offered at any of the following agencies:

UR
UR
UR
UR
UR
UR

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UR

- *The Loan program the buyer is quailed for, must allow for gift funds to be used in conjunction with the purchase of their home.*
- **ORG reserves the right to approve or disapprove any loan program, homebuyer or seller.**

Step by Step Instructions:

- 1. The Real Estate Purchase Contract is negotiated between the buyer and the seller, where the seller agrees to pay a service fee to **ORG**. The contract should include the following: "Seller agrees to pay a service fee to **ORG** in the amount of \$_____ at closing." The Real Estate Purchase Contract and Seller Participation Letter should then be forwarded to the participating Lender and Title Company.*
- 2. The application should then be filled out by the lender, buyers and sellers. This form may be obtained by calling [#] or online at www. (no phone number of website address are listed under the instructions.)*
- 3. The application, Real Estate Purchase Contract and proof the borrowers have been pre-approved by an automated underwriting system or equivalent, and the Seller's Participation Letter should then be faxed to **ORG**. The Fax number is [#]. (no phone number is listed) Our staff then reviews them and the transaction is scheduled for future funding.*
- 4. The Gift Letter for the Buyer is prepared and faxed to the Lender, with instructions that the borrowers must attend a Homebuyer Counseling Program from the list of agencies listed under the Eligibility Requirements. Proof of the buyer's attendance must be provided to **ORG**, before closing.*
- 5. When the loan is approved, the Lender notifies **ORG** of the target closing date. Closing instructions are faxed to the Title Company and then the Gift Funds can be wired from **ORG** to the Title Company within 24 hours.*
- 6. Once the Closing occurs, another American Dream will have been achieved.*

From the above descriptions of how the DPA program works and who is eligible, we have learned that the **ORG's** DPA program has no income or asset restrictions for the homebuyer. Homebuyers do not need to be low or medium income and/or first-time homebuyers. Also, we discovered that the DPA transactions result in a circular flow of the money with **ORG** as the intermediary.

Financial Statement

ORG conducted x DPA transactions in 200X and x transactions in 200X. A side-by-side comparison of the Forms 990 information is displayed in the table below:

Form 886-A (Rev. January 1994)	EXPLANATION OF ITEMS	Schedule number or exhibit
Name of Organization/Taxpayer ORG	Tax Identification Number EIN	Year/Period ended 12/31/200X & 12/31/200X

	December 31, 200X	December 31, 200X
Revenue		
Direct public support		
Program service revenue		
Interest income		
Other revenue		
Total revenue		
Expenses		
Grants to RR		
Accounting fees		
Legal fees		
Supplies		
Telephone		
Postage and shipping		
Occupancy		
Printing and publication		
Travel		
Wire transfer fee		
Administration costs		
Automobile expense		
Bank service charges		
Credit card fees		
Miscellaneous		
Advertising		
Professional fees		
Production costs		
Down Payment Assistance		
Licenses and permits		
Total expenses		
Net Income		

ORG described its primary exempt purpose on the Forms 990 as follows:

ORG mission is to strengthen individuals by providing guiding principles that unite families and society through faith, courage, love, commitment, and integrity. ORG accomplishes its mission by producing, publishing, and distributing practical information from qualified experts in the areas of physical health, literacy and education, social-emotional, spiritual strength, finance and resource management, and self-reliance.

According to its financial records, the direct public support of \$x for 200X was revenues earned before **ORG** started the Down Payment Assistance program. The revenue included production fees and donations received. The program service revenue were fees received from the DPA program. In 200X, both direct public support and program service revenue were fees received from DPA program.

The reported grants of \$x paid in 200X and \$x paid in 200X were grants to **RR**.

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Bank Statement:

ORG had a checking account with UR Bank. The account was under ORG and it was closed on Dec. 19, 200X.

ORG opened a checking account with Bank UR on Nov. 10, 200X and the account is under NN and NN [spouse]. The account number is [#].

The transactions listed on the bank statements indicated that ORG started its DPA transactions on June 19, 200X. They received a \$x fee transferred from UR Title Corp. The last DPA transaction was on May 31, 200X.

After a review of the General Ledger and bank statements, we established that ORG received DPA funds first, then wire transferred the exact amount of the funds to the title or escrow companies. After the transaction, ORG received its fees from the title or escrow companies. For example, ORG received a wire transfer fund of \$x on Nov. 17, 200X, then it transferred the \$x to UR Title Co Escrow A. On Nov. 18, 200X, UR received a fee of \$x from the UR Title.

Advertising Material

ORG's pamphlet promotes its DPA program to buyers, sellers, builders, lenders, and real estate professionals as follows:

Buyers

.....
Our program is simple, fast, and easy. You can work with any real estate professional or lender. There is no extra qualifying, no asset or geographical restrictions, and no reserve requirements. We will even provide you with an online, homeowner's education program. All you need to do is be approved with your lender through an automated underwriting system for a mortgage that allows your down payment to come from gift funds and use a seller that will agree to pay ORG a service fee after the home closes.

Seller/Builder...

ORG provides sellers or builders with several advantages. By allowing more people to become qualified home buyers we increase a seller's pool of potential buyers by up to x%. Because of the increased qualified buyers, the seller can sell the home significantly faster. Your house will be on the market for less time. We also help the seller sell the home at full market value. Your chances of getting the price you want will be maximized.

We help sellers save money in two ways. First, we help them sell their homes faster. This means that they avoid the extra interest payments on their mortgage that they

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would otherwise be responsible for while they wait for their home to sell. Second, we help them maximize their net profit. In a typical transaction, negotiations will cause the seller to reduce the sales price on average by x%. By using our program the seller will sell his home at full market value.

Using our program is easy and rewarding. After the closing, the seller donates the grant amount plus a small fee (either \$x or x% whichever is less) to **ORG**. This replenishes our pre-existing gift funds and makes it possible for more buyers and seller to benefit from **ORG's** down payment assistance.

Lenders

ORG helps lenders close more loans and gets more families into homes. Our program provides lenders with a x% increase in the number of qualified home buyers. This in turn will increase the lender's originations and fundings. Our excellent service helps make this process fast and easy.

Buyers participating in this program need no additional qualifying. They simply need to be approved through an automated underwriting system for a mortgage loan that allows the down payment to come from gift funds from a non-profit organization. We also help minimize the risk of default by educating your borrowers with an online, homeowner's education program. Take advantage of the increase in potential home buyers by using **ORG**.

Real Estate Professionals

ORG benefits real estate professionals by bringing more qualified homebuyers means that real estate professionals will be able to increase their sales. By eliminating the up-front funds obstacle, we can increase your potential clients by x%.

Our program is designed to be easy, fast, and hassle free. By showing your buyers and sellers the advantages of using **ORG's** program, you can increase your listing opportunities.

APPLICABLE LEGAL PRINCIPLES:

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

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

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Section 1.501(c)(3)-1(d)(1)(ii) the Regulations 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.

Section 1.501(c)(3)-1(d)(2) the Regulations defines the term "charitable" as including the relief of the poor and distressed or of the underprivileged, and the promotion of social welfare by organizations designed to lessen neighborhood tensions, to eliminate prejudice and discrimination, or to combat community deterioration. The term "charitable" also includes the advancement of education.

Section 1.501(c)(3)-1(d)(3)(i) the Regulations provides, in part, that the term "educational" relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e) the Regulations provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of the Code § 501(c)(3) if the trade or business furthers an exempt purpose, and if 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.), the U.S. Court of Federal Claims considered whether an organization that provided prenatal care and other health-related services to pregnant women, including delivery room assistance, and placed children with adoptive parents qualified for exemption under § 501(c)(3). The court concluded that the organization did not qualify for exemption under § 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. 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. In addition, although the organization provided health care to indigent pregnant women, it only did so when a family willing to adopt a woman's child sponsored the care financially. 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).

In American Campaign Academy v. Commissioner, 92 T.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

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described in § 501(c)(3) because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with entities of a particular political party and that most of the organization's graduates worked in campaigns for the party's candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting the party's candidates and entities. Although the candidates and entities benefited were not organization "insiders," the court stated that 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)(1)(ii). The court concluded by stating that even if the political party's 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 that an organization that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops operated for exclusively charitable purposes within the meaning of § 501(c)(3). The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence collected by the Bureau of Indian Affairs or other government agencies. The organization marketed only handicrafts it purchased in bulk from communities of craftsmen. The organization did not market the kind 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 organization's activity was to benefit disadvantaged communities. The organization's commercial activity was not an end in itself but the means through which the organization pursued its charitable goals. The method the organization used to achieve its purpose did not cause it to serve primarily private interests 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 described in § 501(c)(3).

In Airlie Foundation v. Commissioner, 283 F. Supp. 2d 58 (D.D.C., 2003), the court relied on the commerciality doctrine in applying the operational test. Because of the commercial manner in which the organization conducted its activities, the court found that it was operated for a nonexempt commercial purpose, rather than for a tax-exempt purpose.

Rev. Rul. 67-138, 1967-1 C.B. 129, held that helping low-income persons obtain adequate and affordable housing is a "charitable" activity because it relieves the poor and distressed or underprivileged. In Rev. Rul. 67-138, the organization carried on several activities directed to assisting low-income families obtain improved housing, including (1) conducting a training course on various aspects of homebuilding and homeownership, (2) coordinating and supervising joint construction projects, (3) purchasing building sites for resale at cost, and (4) lending aid in obtaining home construction loans.

Rev. Rul. 2006-27 discusses three examples of organizations providing down payment assistance and whether each qualified as an organization described in section 501(c)(3) of the Code.

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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, 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.

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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 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

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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).

Effective date of revocation

An organization may ordinarily rely on a favorable determination letter received from the Internal Revenue Service. Treas. Reg. §1.501(a)-1(a)(2); Rev. Proc. 2003-4, §14.01 (cross-referencing §13.01 et seq.), 2003-1 C.B. 123. An organization may not rely on a favorable determination letter, however, if the organization omitted or misstated a material fact in its application or in supporting documents. In addition, an organization may not rely on a favorable determination if there is a material change, inconsistent with exemption, in the organization's character, purposes, or methods of operation after the determination letter is issued. Treas. Reg. § 601.201(n)(3)(ii); Rev. Proc. 90-27, §13.02, 1990-1 C.B. 514.

The Commissioner may revoke a favorable determination letter for good cause. Treas. Reg. § 1.501(a)-1(a)(2). Revocation of a determination letter may be retroactive if the organization omitted or misstated a material fact or operated in a manner materially different from that originally represented. Treas. Reg. § 601.201(n)(6)(i), § 14.01; Rev. Proc. 2003-4, § 14.01 (cross-referencing § 13.01 et seq.).

GOVERNMENT'S POSITION:

In order for an organization to retain its exempt status it must demonstrate to the Internal Revenue Service 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 section 1.501(c)(3)-1(d)(2) of the regulations. **ORG**'s down payment assistance 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 Rev. Rul. 2006-27, Situation 2. The down payment assistance program did not serve exclusively low-income persons. **ORG** did not establish that it has any income limitations for participation in its DPA program. Its program is open to every homebuyer, without any income limitations, who otherwise qualified for financing from a lender.

ORG's DPA program does not limit assistance to certain geographic areas or target those areas experiencing deterioration or neighborhood tensions. See Rev. Rul. 2006-27, Situation 3. Down payment assistance is available for any property that is otherwise able to qualify for a mortgage. Arranging or facilitating the purchase of homes in a broadly defined geographic area does

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not combat community deterioration or serve other social welfare objectives within the meaning of section 501(c)(3) of the Code.

Also **ORG's** DPA program provided a private benefit to various parties. Similar to 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 a DPA program benefit from achieving 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 home at the home's listed price or by being able to reduce the amount of the negotiated discount on their homes. Buyers who participate in DPA program benefit by being able to purchase a home without having to commit more of their own funds. The program also helps lenders to close more loans and helps real estate professional to close more deals. Because **ORG** contracted its service out to a mortgage company, the mortgage company also benefited to receive fees from each DPA transaction.

To finance its down payment assistance activities, **ORG** relies exclusively on sellers. **ORG** neither solicits nor receives funds from other sources. **ORG** requires the home seller to reimburse it, dollar-for-dollar, for the amount of funds expended to provide down payment assistance on the seller's home, plus an administrative fee of x% of home sales price. **ORG** receipt of a payment from the home seller corresponding to the amount of the down payment assistance in virtually every transaction indicates that the benefit to the home seller (and others involved in the transaction) is not a mere accident but rather an intended outcome of **ORG's** operations.

ORG's receipt of a payment from the home seller corresponding to the amount of the down payment assistance in almost every transaction and **ORG's** reliance on these payments for all its funding indicate that the benefit to the home seller is a critical aspect of **ORG's** operations. The sellers got the benefit of having their property sold quicker (due to greater number of potential home buyers) without actually incurring any costs. Because the amount that home buyers received from **ORG** was incorporated into the sale price of a home, the purported beneficiaries in fact did not receive anything from **ORG**. Further, because the transaction fees charged by **ORG** was based on a percentage of the sales price, **ORG** benefited from the transactions by maximizing its fees. The circular cash flow indicates that the Corporation's primary goal was to facilitate transactions for the benefit of private parties involved or connected to these transactions, i.e., buyers (who were not necessarily members of a charitable class), sellers, real estate professionals, the contracted mortgage company, etc. 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), [A] Foundation's trade or business was not utilized as a mere instrument of furthering charitable purposes but was an end in itself. **ORG** provided services to home sellers for which it charged a market rate fee. **ORG** did not limit its services primarily to persons within a charitable class. **ORG** did not solicit or receive any funds from parties that did not have interest in the down payment

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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.

ORG does not qualify as an organization described in I.R.C. § 501(c)(3) because it operates a program that does not exclusively serve an exempt purpose described in section 501(c)(3). Therefore, the exempt status granted **ORG** should be revoked and **ORG** is required to file Forms 1120 for the years 200X and after.