



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Release Number: **201235023**
Release Date: 8/31/2012
Date: 6/5/2012
UIL Code: 501.31-00

Contact Person:
Identification Number:
Contact Number:
Employer Identification Number:
Form Required To Be Filed:
Tax Years:

Dear

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

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

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

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

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

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



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

TAX EXEMPT AND

GOVERNMENT ENTITIES

Date: April 17, 2012

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend

B= State
C= Date
D= Name
E= Name
F= Name
G= Website
H= Website

UIL

501.03-00

Dear:

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

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

Issues

Do you qualify for tax exemption under section 501(c)(3) of the Code?

No, for the reasons stated below.

Facts

You were incorporated under the not for profit corporation laws in the state of B on date C. Your Articles of Incorporation state your purposes are to retrain and find homes for abandoned dogs and cats. Your activities consist of rescuing abandoned animals and providing them shelter, food and medical care. You have an extensive website displaying your animals and describing their backgrounds and health issues. These animals may also be available for adoption for a fee and adopting families must complete a contract as well as a detailed questionnaire.

You have not adopted bylaws that establish operating procedures or internal policies. Your board of directors is made up of three individuals D, E, and F. D and E are husband and wife and they have held the same positions since you were formed. Moreover, you operate out of the home of D and E but no rent is paid. E conducts the majority of the day-to-day operations including making essentially all expenditures. You do not have a formal process for approving the payment of expenses. Your application for exemption included a Conflict of Interest Policy to be used when you enter into a transaction or arrangement with an officer or director.

Your application for exemption states that your officers are elected by the majority vote by members attending your annual meeting. The minutes to your meetings report only D and E in attendance. Consequently, these individuals were the only officers available to vote on all decisions made at these meetings. You claim that families adopting your animals are automatically considered your members. However, there has been nothing in writing that informs adopting families that they are considered your members or that there are meetings where they can participate and contribute to the decision making. You later represented that these adopting families are told informally they are members and this provision will be added to your adoption contract.

You do not solicit donations from the public and receive some funds from animal adoptions. The majority of your funds are from the sales proceeds of merchandise E sold on H. E used her personal credit card to purchase this merchandise. Over the past three-year period, these sales exceeded \$475,000. The proceeds from these sales were deposited into E's individual PayPal account. Most of these proceeds were then deposited into your checking account. You subsequently made several payments to her personal credit card account.

Because you were unable to provide accurate income statement reports, you provided copies of bank statements. Your bank statements indicated over \$100,000 in deposits and withdrawals from 2005 until 2008. Approximately one-half of these withdrawals (Over \$50,000) during this period were electronic payments to E's personal credit card. You were unable to obtain copies of the credit card statements for this time period and could not confirm nor deny that you paid your expenses and the personal expenses of E.

You were able to provide credit card statements for a more recent 15-month period that reported over \$60,000 in charges. Approximately \$30,000 of these charges was to purchase merchandise that E sold on the internet. About \$18,000 of the credit card charges were for the personal use of E indicated by purchases made at such places as bookstores, restaurants, department stores, and a gym membership. The balance of the charges was attributable to your operations.

Although you provided bank statements, credit card statements and internet sales reports, it was not a complete accounting of your sales and financial transactions. You also included copies of cancelled checks with your bank statements. Several of the checks, which were written to cash or directly to D and E, were described as loan repayments. These loans were not documented or reported in the balance sheet submitted with your application for exemption. You also clarified that you have not yet prepared any tax returns or reported your receipts and expenses for tax or for information return purposes.

Your bank statements also show you received deposits from G, which is H's charitable partner. You wrote that you were registered with G to receive proceeds or donations from H sales and that "No agreement or application is completed" and "The only requirement is to send a letter on the Organization's letter head stating the activity." The website of G states an organization must register with it and provide it a copy of its 501(c)(3) letter or other proof of deductibility in order to participate in its programs. In addition, the organization must complete the nonprofit user agreement.

Tax Law

Section 501(c)(3) of the Internal Revenue Code ("Code") provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable, educational and other purposes, including the prevention of cruelty to children or animals provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the regulations provides that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the regulations provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Section 1.501(a)-1(c) defines the words "private shareholder or individual" to mean persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations states that an organization is not operated exclusively for one or more exempt purpose unless it serves a public rather than a private interest. It must not be operated for the benefit of designated individuals or the persons who created it.

Rev. Proc. 2011-9, 2011-2 I.R.B. 283, in section 4.03 provides that exempt status may be recognized in advance of the organization's operations if its proposed operations are described

in sufficient detail to permit a conclusion that it will clearly meet the particular requirements for exemption pursuant to the section of the Code under which exemption is claimed. Section 4.03(2) states that the organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279, (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy a claim for exemption regardless of the number or importance of truly exempt purposes.

In Bubbling Well Church of Universal Love, Inc. v. Commissioner, 74 T.C. 531 (1980), in an action for declaratory judgment pursuant to section 7428(a), the Tax Court considered an adverse ruling by the IRS on an application for exempt status as a church. The applicant had declined to furnish some information, and made answers to other inquiries that were vague and uninformative. Based on the record, the Court held that the applicant had not shown that no part of its net earnings inure to the benefit of the family or that petitioner was not operated for the private benefit of its founders.

In New Dynamics Foundation v. United States, 70 Fed. Cl. 782 (2006), there was an action for declaratory judgment that the petitioner brought to challenge the denial of his application for exempt status. The court, in finding that the actual purposes displayed in the administrative record supported the Service's denial, stated, "It is well-accepted that, in initial qualification cases such as this, gaps in the administrative record are resolved against the applicant." The court noted that if the petitioner had evidence that contradicted these findings, it should have submitted it as part of the administrative process. The court also highlighted the principle that exemptions from income tax are matters of legislative grace.

In Ramese School of San Antonio, Texas v. Commissioner, T.C. Memo. 2007-85; No. 23228-04X (10 Apr 2007) the court held that the IRS properly revoked the tax exempt status under section 501(c)(3) of the code of a school on the grounds that its earnings inured to the benefit of its founder, who also served as its executive director, president, and CEO.

Due to the school's failure to maintain adequate financial and academic records and a lack of compliance with Texas requirements, the State Board of Education revoked its charter on November 14, 2000. Subsequently, the IRS revoked the exempt status of Ramese School in 2004.

In this case, the founder did not have a functioning board with regular meetings. There were numerous examples of distributions of funds for personal purposes. The record showed that the founder wrote checks to herself or cash for which the record showed no documented business purpose. The record also contained thousands of dollars of expenditures directed to retail stores, credit card companies, financial institutions and other businesses for which there was no evidence of a business purpose or board authorization. Neither did the organization's records show that there was any documented system for either loans to or repayments by the founder.

A charitable organization must serve the public interest and will lose exempt status if it violates the "private benefit" test. Reg. 1.501(c)(3)-1(b)(1)(i). The founder clearly received public charity

benefits that had been redirected to her private purposes. Because the Rameses School failed the private benefit test, its tax-exempt status was revoked.

Application of Tax Law

You are not as described in section 501(c)(3) of the Code and section 501(c)(3)-1(a)(1) of the regulations because you do not satisfy the operational requirements of the Code and regulations. You are not operated exclusively for exempt purposes due to net earnings inuring in whole or in part to E.

You are not described in Section 1.501(c)(3)-1(c)(1) of the regulations because more than an insubstantial part of your activities are devoted to a non-exempt purpose.

You are not described in Section 1.501(c)(3)-1(c)(2) of the regulations because, you are not operated exclusively for exempt purposes. Your net earnings inure to the benefit of E because you have paid her personal expenses.

You do not meet the provisions of Section 1.501(c)(3)-1(d)(1)(ii) because you are not operating exclusively for public purposes. You have no operational or financial controls in place. Furthermore, the fact that you have a small-related board and E has had essentially exclusive control over your daily operations and your finances indicates you are operating for private interests.

You are like the organization in Better Business Bureau v. Commissioner. Although operating an animal rescue may be exempt under 501(c)(3), the fact that you have a small-related board, and that there are neither organizational policies nor financial controls in place indicates you have a substantial non-exempt purpose.

You have operated similar to the organization described in the court case Ramese School of San Antonio, TX v. Commissioner. You have not kept adequate financial records. Moreover, you do not have a functioning board with a formal process for approving the payment of expenses. For instance, E is responsible for paying essentially all your expenditures. In addition you provided copies of cancelled checks of which many were written to cash or directly to D and E. These were described as loan repayments. However, these loans were not documented or reported in the balance sheet submitted with your application for exemption. Like the organization in the court case, your earnings have inured to D and E. Finally, consistent with the organization in the court case you have failed the private benefit test and do not qualify for exemption.

You are similar to Bubbling Well Church of Universal Love, Inc. v. Commissioner. You have not provided an open candid disclosure of facts. You have given answers to our inquiries that were vague, and uninformative. For example, you were unable to provide any documents showing how you formally registered with G even though G clearly requires registration and proof of exempt status before an organization can register on this web site.

You are like the organization in New Dynamics Foundation v. United States because the information through inference shows you are operating for the private benefit of E. For example, you paid more than \$50,000 to E's credit card account during and were unable to provide copies of those credit card statements and you could not confirm nor deny that you paid the expenses

of both you and the personal expenses of E. The 15-month sample of credit card statements you provided did report expenses for both you and E. Therefore, since we have evidence that you made payments of over \$50,000 to E' credit card account we can presume that you paid E's personal expenses during this period.

You have not met the requirements of Revenue Procedure 2011-9 , because you were unable to provide a complete accounting of your sales and financial transactions to conclude that you are in compliance with the operational requirements of section 501(c)(3). Furthermore, you received funds from G but the information concerning how to register with G contradicted what you provided.

Applicant's Position

You wrote that you have made changes to your operations. You held an annual meeting in January 2011 that was attended by a number of people. You elected a new secretary because the previous one could not be located and has been inactive in your operations. Moreover, you are currently searching for a treasurer. You have also discontinued the sale of merchandise over the internet. Finally, you wrote that you are willing and eager to make any changes that are necessary to obtain non-profit status.

Our Response to Applicant's Position

You failed to provide any additional information from which it can be concluded that your activities exclusively further or advance a purpose described in Section 501(c)(3). Although you are willing to make changes in order to qualify for exemption you have been operating for the benefit of your officers since you were formed. You have operated out of the home of D and E who have approved all expenditures without any oversight. Moreover, you have not provided a complete accounting of your sales and expense activities. Although you state that you are no longer selling merchandise over the internet, as of January 2012, there is merchandise listed under E's user name, which was listed on the internet sales reports you provided. In addition, the page states under "Why buy from E", that these proceeds will fund E's animal rescue.

Conclusion

Based on the information submitted, you are not organized and operated exclusively for exempt purposes as described in section 1.501(c)(3)-1(a)(1) of the regulations. You do not have organizational policies or financial controls in place to insure that you are operating exclusively for charitable purposes. Furthermore, you have a small-related board indicating that you have a substantial non-exempt purpose. Finally, you have paid E's personal expenses resulting in inurement. Accordingly, we conclude you do not qualify for exemption under section 501(c)(3) of the Code.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to appeal as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848, and any supporting documents to the applicable address:

Mail to:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Deliver to:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You may fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations