

Internal Revenue Service
Appeals Office

Number: **201306028**
Release Date: 2/8/2013

Date: November 15, 2012

Department of the Treasury

Taxpayer Identification
Number:

Person to Contact:

Tax Period(s) Ended:

UIL: 0501.03-30

Certified Mail

Dear _____:

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code effective January 1, 2006.

The revocation of your exempt status was made for the following reason(s):

A substantial amount of your organization's assets inured to the private benefit of your founders. Because a substantial amount of your charitable assets were used for private purposes, the organization is not operated exclusively for exempt purposes described in section 501(c)(3) of the Code.

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

You are required to file Federal income tax returns on Forms **** for the tax periods stated in the heading of this letter and for all tax years thereafter. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit www.irs.gov.

You have waived your right to contest this determination under the declaratory judgment provisions of Section 7428 of the Code.

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

Sincerely Yours,

/s/
Appeals Team Manager

DEPARTMENT OF THE TREASURY

Internal Revenue Service
1100 Commerce Street
Dallas, TX 75242

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

February 18, 2011

LEGEND

ORG - Organization name
XX - Date Address - address

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.

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,

Nanette M. Downing
Director, EO Examinations

Enclosures: Publication
892 Publication 3498
Report of Examination

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

LEGEND

ORG - Organization name XX - Date EIN - EIN Address - address
City - city State - state Country - country DIR-1 & DIR-2 - 1st &
2nd DIR CO-1, CO-2, CO-3, CO-4, CO-5, CO-6, CO-7, CO-8, CO-9, CO-10, CO-11,
CO-12, CO-13, CO-14, CO-15, CO-16, CO-17, & CO-18 - 1st, 2nd, 3rd, 4th, 5th, 6th,
7th, 8th, 9th, 10th, 11th, 12th, 13th, 14th, 15th, 16th, 17th & 18th COMPANIES

ISSUE:

Is ORG operating exclusively for charitable and educational purposes as described in Internal Revenue Code (IRC) Section 501 (c)(3)?

FACTS:

ORG, whose Employer Identification Number is EIN, was incorporated on October 21, 19XX. In a letter dated September 26, 20XX, ORG was granted exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501 (c)(3), with a foundation status of 509(a)(1) during the advanced ruling period which ended on December 31, 20XX. Another letter dated May 24, 20XX, stated that with the information submitted by ORG, the Organization will continue to be classified as a public charity with a status of 170(b)(1)(A)(vi). The mission of the Organization as stated on Form is "to preserve play for future generations of children and parents." In furtherance of its mission, ORG will: (1) work to educate adults as to the value of constructive play in the lives of children and adults; (2) provide venues for education regarding and development of insightful play experiences among adults and children; (3) research and report for educational purposes on the effects of play, and the lack thereof, on children and adults; and (4) establish a center for research and education on the benefits of constructive play and the ability to participate in the same.

ORG began operations in City, State in 20XX. DIR-1, the Director, holds an Associates Degree in Business and a Bachelor of Science Degree in Education. ORG has deviated from their original purpose, as stated on Form , to the helping of autistic persons by taking them on hiking trips and other outings. This change in mission was not reported to the IRS. During their interview, the stated they moved to City to be in the country of State, which provided more opportunity for hiking and other outdoor activities.

ORG has three main sources of income: monetary contributions, money from an annual fundraiser that the Organization holds every November, and advertising income. Their income is used for client incentives, meals, meeting costs, uniforms, transportation expenses for taking children on outings, travel and entertainment, equipment and repairs, and vehicle and equipment rental. The Organization does not receive any funding from the city, county, or the State of State.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

Bank statements for ORG were reviewed on Tuesday, November 18, 20XX. There were recurring transactions at liquor stores, grocery stores, fast food restaurants, full service restaurants, CO-1, CO-2, and hair salons, all located within close proximity of their former residence in City, State, (see exhibits A -L for monthly debit card transactions). Another set of exhibits (exhibits 1 -7) categorizes the different types of transactions and how many transactions were made for each category. The final set of exhibits (Q-1 -Q-2) is a list of the checks written from the Organization's checking account. There are no copies of the cancelled checks, just the check numbers and the amounts stated on their bank statement. The information on Information Document Request #1 was requested on April 21, 20XX, and due to the agent by May 21, 20XX.

The following responses to Information Document Request #1 were received on May 19, 20XX, and a duplicate copy with an original signature on May 24,20XX. For exhibits R-1 -R-2 the Officer created a spreadsheet to show how the Organization received their revenue for the calendar year 20XX. The revenue was divided into five categories: CO-3 Bank Error, Contribution, CO-4 (advertising income), Event Income, and Class Programming.

- The Officer explained that the CO-3 bank error was an error on the side of CO-3 when someone else's deposit was mistakenly credited to ORG's account.
- The Officer stated that copies of where the contributions came from are attached. However, only the proof of one contributor was attached. See exhibits S-16 & S-17.
- The Officer stated that the cost of generating the publication CO-4 was supported by low cost advertising from local businesses and organizations that provide services for children and their parents. This was not entirely true, as many of the advertisements were from businesses that did not provide services that either helped overcome learning differences or helped with motor skill development. The Organization did not report their advertising income on Form
- The deposits in the "Paid Class Programming" column were comprised of class programming sessions conducted by ORG. It was also stated that DIR-1 conducted these classes to further his research of play and its benefit to children. He also was providing a service of monetary value to the children and their parents. The Officer also stated that the amounts were not donations or tax deductible.

For exhibits Q-1 through Q-2, the Organization provided only partial information. This was attributed to a computer problem, and the Officer stated, "*That the cost of ordering these checks through CO-3 will cost \$ a piece.*" The expenses that were explained in exhibits Q-1 and Q-2 were for an apartment that was rented at CO-5 in City, State. There were also payments to CO-6, CO-7, CO-8 payment, CO-9, and CO-10. No explanation was provided as to how these expenses furthered their exempt purpose, or if any of these accounts were in the name of the Organization.

The debit card transactions were broken down into eight separate categories, (See exhibits 1 8). For their explanation of exhibit 1, concerning the 123 liquor store transactions paid in the calendar year 20XX, the Officer stated, "*that the transactions were for wine purchases that we*

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

needed to purchase a little at a time to increase inventory, so that we have wine to pour at our annual food and wine events. It relieves the financial burden of having to purchase it all at once to conduct our event, and wine was also purchased as client incentives for the parents. Many times DIR-1 would be invited to sit down over dinner with parents to discuss ORG's programming and how it could benefit their children. This was the cost of doing business to further ORG's mission." The Organization did not provide documentation as to the times, dates, and topics discussed for these dinner meetings.

For their explanation of exhibit 2, the 307 grocery store purchases, the Officer stated, *"these grocery store purchases were food purchases so that we could provide picnic, lunches, snacks, candy and drinks to the children while we were on recreational play outings. In addition to these expenses we would purchase food to prepare if we were hosting a lunch or dinner meeting to discuss ORG's mission and goals with potential supporters, volunteers, or program participants."* Again, the Organization did not provide documentation as to the times, dates, places where the play outings took place, or when lunch or dinner meetings took place.

For their explanation of exhibit 3, the 17 rental car and car payments, the Officer stated, *"the car payments to either CO-8 or CO-11 were for DIR-1's vehicle that he used for carrying out ORG's programming going to and from recreational location, transporting the children, and meeting potential clients. We had another vehicle we used for non-business related activities and transportation. The payment to CO-12 was to fix a small rock chip in the windshield of the business vehicle that occurred during programming. Small amounts to CO-13 and CO-14 were for oil changes in the business vehicle for maintenance. The payments to CO-6 were for auto insurance on the business vehicle in the event of an accident. The rental car and truck expenses were in conjunction with trips to and from City to assess possibly moving the Organization, and then for the expenses associated with the actual move. This was a small portion of the actual move. We personally incurred most of the expense to move the Organization."* The Organization did not provide documentation that the vehicles used for the Organization were used exclusively for the Organization and not for personal use such as a log book which would notate the date, destination, purpose, and mileage. No document was submitted that identified the windshield repair and vehicle maintenance as that of the Organization's vehicle or personal vehicle such as a receipt for the make and model of the car. As far as the rental car and truck expenses are concerned, no distinction was made as to what part of the move to City constituted Organizational expenses versus personal expenses.

For their explanation of exhibit 4, the 29 salon, health care, and clothing store transactions, the Officer stated, *"these transactions are the result of obtaining uniforms and equipment to carry out the programming and client incentives for the kids. Often times children would be rewarded for working hard, participating, paying attention or following directions well during a recreational outing."* No explanation was received as to how the trips to the beauty salons, cleaners, jewelry stores, and medical clinics were in furtherance of the Organization's exempt purpose, or rewards for the children.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

For their explanation of exhibit 5, the 30 various utility payments, the Officer stated, *"These were the utility costs associated with ORG's office space and one cell phone for DIR-1 and internet service for the computers."* No supporting documentation was provided by the Organization such as a lease agreement for the office space, or copies of the bills with an address of the office space location. This was requested in the IDR..

For their explanation of exhibit 6, the 84 various purchases in City, State, the Officer stated, *"These City transactions were in conjunction with the Organization's relocation such as gas expense to and from City, research, on-site recreational mapping of locations for programming, meals and programming equipment."* No documentation was provided to support these claims, such as, where they went for on-site recreational mapping, how the meals supported their exempt purpose, what types of programming equipment was purchased, where it was purchased, and what was purchased. Again no log book or any other type of receipt was submitted for their gas expenses.

For their explanation of exhibit 7, the 13 purchases made in State, State, and State, the Officer stated, *"The charges outlined in this exhibit were also in conjunction with moving ORG. These transactions are only a portion of the expenses incurred for a trip to State to pick up some office furniture that was being stored there. We personally paid for a majority of the moving cost."* No documentation was provided as to how the purchases at CO-15 # 3573, CO-16 # 0207, or CO-17, all in City, State, related to the acquisition of their office furniture.

For their explanation of exhibit 8, the 210 restaurant and beverage purchases made in City, State, the Officer stated, *"These transactions are associated with various formal business meetings over lunch and dinner, meetings organized and conducted at a local coffee shop as opposed to ORG's office to discuss furthering ORG's mission, organize recreational outings with volunteers of the Organization as well as to entertain potential donors, grant writing advisors, non-profit consultants, and potential program participants. Many professional services were donated to keep ORG's cost low so that the Organization could continue to operate on a very limited "shoestring" budget while getting the help needed to operate. In return for the generous help of many professionals and volunteers we would treat them to a cup of coffee, lunch or dinner as a thank you for their service. Often times a trip to CO-1 was also made to treat the kids to an after session treat for validation of their good work and good behavior. In addition to the expenses that ORG incurred, CO-1 would also donate some drinks to match a portion of what we were spending. As a result we were consistent in going there as an after program location. This may have happened multiple times in one day if there were multiple classes conducted."* Once again no supporting documentation was provided. No dates, times, who attended, and what was discussed was provided. Most of the purchases made at CO-1 appear to be for single purchases.

IDR # 3 was sent via certified mail on June 3, 20XX. This request asked for additional information to clarify the responses given to the Service in IDR # 1, sent on April 21, 20XX for

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

exhibits 1 -8. The Officer noted on the reply that not all of the questions were answered, and that the additional information will be faxed at a later date. The following questions and answers are as follows:

1(a). Where is the food and wine event held specifically? Such as a park, hall rental, etc. Please provide the Service with a copy of the permit(s), and/or rental contracts for the event in 20XX. Their reply was, "*CO-18 in City, State No service contract as catering was donated.*" No correspondence between ORG and CO-18 was provided. 1(b). What activities are held at this event? Is this a one day event, or is it longer? Their reply was, "*Wine tasting paired with food. It was a one evening event.*" 1(c). How do the annual food and wine events further ORG's exempt purpose? Their reply was, "*Helped raise sustaining funds.*"

1(d). How many people attend this event, and do you keep attendance rosters? Their reply was, "*75 people. We have attendance roster.*" No attendance roster was provided.

1(e). How many bottles of wine, and what kind of food is offered by ORG at this event? Their reply was, "*Wine poured by the glass paired with "Tapas" (small appetizer portions).*" No documentation was submitted as to how many bottles of wine were poured, or who provided the wine.

1(f). Do you sell tickets to the annual event? Their reply was, "*Charged for admission or sometimes offered opportunity to make donations when events were free.*"

1(g). If so, how much are they? Their reply was, "*Admission was based on venue's capacity.*" Since this event was already held no price was given, or the capacity of CO-18 facility.

1(h). If tickets are sold, does part of the cost of the ticket price go towards your wine and food costs? Their reply was, "*All upfront costs were normally very minimal as venue, food, wine, linens, etc., were donated. Ticket sales proceeds did not go to cover any of these costs.*" This statement is contradictory to their response from IDR # 1, exhibit 1, the liquor store purchases, "*that the transactions were for wine purchases that we needed to purchase a little at a time to increase inventory, so that we have wine to pour at our annual food and wine events. It relieves the financial burden of having to purchase it all at once to conduct our event.*"

1(i). If some of the money is used to cover food and wine costs, are the attendees given a statement that tells them how much of the proceeds qualify as a charitable deduction, and that only the amount over and above the cost of food and wine is deductible? Their reply was, "*In 20XX everything was donated.*"

For exhibit 2, questions a -e, the following questions and answers are as follows: 2(a). Did you keep a log in 20XX, of each outing ORG participated in? Their reply was, "*Outings can be accounted for.*" No supporting documentation was provided as to when, where, how many children and/or adults attended, and what activities took place.

2(b). If so, how many children went on each trip, and where did you go on each trip? Their reply was, "*4-5 kids going to outdoor parks, trails, lakes, etc.*" No supporting documentation was provided.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

2(c). Please provide receipts, a list of each outing's activities, and insurance/medical release forms from the parent's of the children for each outing. Their reply was, "*Outdoor play and recreation/no release forms required.*" Once again no supporting documentation was provided to support the expenses.

2(d). When ORG hosted a lunch or dinner meeting did you keep the receipts, write down the date and time of the meeting, and who attended the meeting? Their reply was, "*Yes, via bank statements.*" The bank statements do not provide any information that the expenses were related to the Organization's exempt purpose.

2(e). When ORG hosted the lunch and dinner meetings, how did you decide to invite? Their reply was, "*Mailings to parents in our area.*" No supporting documentation of the mailings was sent with these responses.

For exhibit 3, questions a -g, the following questions and answers are as follows:

3(a). We will need a copy of the loan agreement for DIR-1's vehicle that is used for ORG's activities. Their reply to this was, "*We no longer have this vehicle.*"

3(b). We will need a copy of the mortgage contract for the residence on Address, City, State. Their reply to this was, "*This mortgage contract was signed until 12/6/XX.*" No mortgage contract was provided. .

3(c). Was a record kept of the dates and mileage for each time DIR-1's vehicle was used for ORG's activities? If so, please provide the Service a copy. Their reply to this was, "*Will confirm.*" As of December 8, 20XX no records have been sent.

3(d). Were receipts from CO-13 and CO-14 for oil changes in the business vehicles maintenance retained for the year 20XX? If so, please provide the Service a copy. Their reply to this was, "*Will send.*" As of the date of this writing, December 8, 20XX no records have been sent.

3(e). Please provide proof of insurance for the business vehicle from CO-6 for 20XX. Also, were your personal vehicles insured with a different insurance company or with CO-6 in 20XX? Please provide the Service with proof of insurance on your personal vehicles for 20XX. Their reply to this was, "*Working on this.*" As of December 8, 20XX no records have been sent.

3(f). Why did you rent car and trucks for trips to City instead of using your personal vehicles? Their reply to this was, "*Moved here for business reasons.*" ORG both lives and runs the Organization out of their home, so the move was not exclusively for business reasons.

3(g). Do you have receipts for the total moving costs from City to City? If so, please provide the Service with a copy. Their reply to this was, "*Will find and submit.*" As of December 8, 20XX no records have been sent.

For exhibit 4, questions a & b, the following questions and answers are as follows:

4(a). You told the Service that the transactions in exhibit 4 were to obtain uniforms and equipment to carry out programming and client incentives for the kids, so how does beauty supply stores, jewelry stores, cleaners, and doctor visits further the Organization's exempt purpose? Their reply to this was, "*Beauty supplies for girls, will find receipts for the other and explain.*" For the beauty supplies no documentation was provided as to what was bought, and for

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

whom. As of December 8, 20XX, no supporting documents have been sent for the other expenses inquired about.

4(b). Please send copies of the medical visits incurred on exhibit 4. Their reply to this was, "Okay, will find and submit." As of December 8, 20XX no records have been sent.

For exhibit 5, questions a -d, the following questions and answers are as follows:

5(a). What was the physical address of your residence in City in 20XX? Their reply was, "Address, City, State." This coincides with the checks written from ORGs checking account. The Officer of the Organization stated that in 20XX, the Organization leased office space at a different location from their residence. The following check numbers, dates written, amounts written, and who to are as follows:

- #, Thursday, April 20, 20XX, \$, The CO-5
- #, Tuesday, May 9, 20XX, \$, The CO-5
- #, Thursday, June 15, 20XX, \$, The CO-5
- #, Wednesday, July 12, 20XX, \$, The CO-5
- #, Tuesday, August 15, 20XX, \$, The CO-5

5(b). What was the physical address of the office, if different from your personal residence? Their reply was, "Same." No supporting documentation was provided that the utility expenses and rental payments were either for personal or organizational use.

5(c). If the office was at a different location please send a copy of the lease or rental agreement. Their reply to this was, "N/A." It appears the Officer's personal residence and ORG's office is at the same location, and no distinction can be made as to what expenses that were paid by ORG were for personal or organizational use.

5(d). Please send copies of the utility bills listed on exhibit 5. Their reply was, "Coming." As of December 8, 20XX no records have been sent.

For exhibit 6, questions a -c, the following questions and answers are as follows:

6(a). Did ORG keep a log book or any other records to record the mileage, transactions, and explain how these expenses furthered ORG's exempt purpose? If so, please provide the copies. Their reply was, "Answered in exhibit 3(c)." As of December 8, 20XX no records have been sent.

6(b). Did you record what types of research was performed during your trips to City, TX.? If so, please provide the Service with copies. Their reply to this was, "Research was on best areas for play/outdoor recreational activities." The Organization did not record the types of research conducted such as, why they picked the place they did, if they did any internet research, or the dates they visited each location.

6(c). Provide a list of on-site recreational locations you mapped for programming. Their reply was, "City, City, City, City, City, City."

For exhibit 7, questions a -c, the following questions and answers are as follows:

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

7(a). Provide a copy of the storage agreement for the office furniture in State. Their reply was, "Coming." As of December 8, 20XX no records have been sent.

7(b). Does the office furniture belong to ORG? Their reply was, "Yes. "

7(c). What was the total cost incurred to move the furniture from State to State? Please provide the receipts for the cost of the move. Their reply was, "Coming." As of December 8, 20XX no records have been sent.

For exhibit 8, questions a -c, the following questions and answers are as follows:

8(a). Please provide receipts to substantiate the business meeting over lunch and dinner. Their response was, "Coming." As of December 8, 20XX no records have been sent.

8(b). How does entertaining potential donors, grant writing advisors, non-profit consultants, and potential program participants classify as a charitable or educational activity? Their reply was, "This was "the cost of doing business" expense as we further ORG. "

8(c). Provide documentation that shows CO-1 donates drinks to match a portion of ORG's spending. Their reply was, "Will do." As of December 8, 20XX no records have been sent.

IDR # 4 was sent via certified mail on September 7, 20XX. This request asked for responses and/or documentation that ORG still has not provided. This was the last Information Document Request that was sent. The following entries are follow-up responses from Information Document Request # 3, which have been requested on Information Document Request # 4.

Exhibit 1(a) -Question and response to 1(a) on IDR # 3. Where is the food and wine event held specifically? Such as a park, hall rental, etc. Please provide the Service with a copy of the permit(s), and/or rental contracts for the event in 20XX. Their reply from IDR # 3 was, "No service contract as catering was donated." IDR # 4 requested that if they provide the company with a thank you letter, or something else, so they could prove the services and/or catering was a donation, please provide the Service with a copy. Their reply was, "Called and thanked personally so there is no letter or other documentation. "

Exhibit 1(c) -Question and response to 1(c) on IDR # 3. How do the annual food and wine events further ORG's exempt purpose? Their reply from IDR # 3 was, "Helped raise sustaining funds." IDR # 4 requested the Organization to provide the Service with a detailed summary such as follows: Date, fundraising event, location, & amount received. Their reply to this was, "Date: April 6, 20XX

*Fundraising Event: Fall Fundraiser
Location: CO-18 - City*

Exhibit 1(d) -Question and response to 1(d) on IDR # 3. How many people attend this event, and do you keep attendance records? Their reply from IDR # 3 was, "75 people. We have an attendance roster." IDR # 4, requested the Organization to provide the Service with a copy of the attendance roster, and the date and time held. Their reply was, "Cannot retrieve from inaccessible computer hard drive in time for deadline.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

Exhibit 1(i) -Question and response to 1(i) on IDR # 3. If some of the money is used to cover food and wine costs, are the attendees given a statement that tells them how much of the proceeds qualify as a charitable deduction, and that only the amount over and above the cost of food and wine is deductible? Their reply from IDR # 3 was, *"20XX everything was donated. See (H)."* In IDR # 4, the Organization was asked to provide a copy of any written documentation given to donors during 20XX. Their reply was, *"None of the money raised was used for food costs because, as previously stated, the "passed food" (small quantities) was donated in full. Also, we did not charge in excess of\$."*

Exhibit 2(a) -Question and response to 2(a) on IDR # 3. Did you keep a log book in 20XX, of each outing ORG participated in? Their reply was, *"That the outings can be accounted/or."* But no records were sent. IDR # 4, asked them to please provide the date(s), time, purpose, how many children went, the cost to the parent(s), and a detailed description of the outing(s). Their reply was, *"Cannot retrieve from inaccessible computer hard drive for deadline."*

Exhibit 2(d) -Question and response to 2(d) on IDR # 3. When ORG hosted a lunch or dinner did you keep the receipts, write down the date and time of the meeting, and who attended the meeting? Their reply to this request was, *"Yes, via bank statement."* As of December 8, 20XX no bank statements have been provided. IDR # 4 asked to provide the date and time of the lunch and dinner meetings, the place where the meeting was held, what business purpose that meeting had, such as, what was discussed, how it was presented, and how long it took ORG's relation to those who attended, and especially, who attended. Their reply to IDR # 4 was, *Copies of all bank statements have previously been provided to you.*

Exhibit 3 -Request and response to question 3(b), from IDR # 3. We will need a copy of the mortgage contract for the residence on Address, City, State. Their reply was, *"This mortgage contract wasn't signed until 12/6/XX."* As of December 8, 20XX, a copy of the mortgage has yet to be submitted. In IDR # 4, the Organization was asked to please provide the Service with a copy of the mortgage contract for the address stated in Exhibit 3(b). Their reply was, *"The closing documents for Address were executed at the title company on 12/6/20XX, and no mortgage payments were made until the following year, 20XX."*

Exhibit 3(c) -Question and response to question 3(c), from IDR # 3. Was a record kept of the dates and mileage for each time DIR-1's vehicle was used for ORG's activities? If so, please provide the Service a copy. Their reply was, *"Will confirm."* As of December 8, 20XX no documents have been submitted. IDR # 4 asked them to please provide the Service with a copy of these records. Their reply was, *"1 can now confirm that we did not keep a mileage log."*

Exhibit 3(d) -Question and response to question 3(d), from IDR # 3. Were receipts from CO-13 and CO-14 for oil changes in the business vehicles maintenance retained for the year 20XX? If so, please provide the Service a copy. Their reply was, *"Will send."* As of December 8, 20XX no documents have been submitted. Please provide the Service with copies of these receipts. Their reply to IDR # 4 was, *"No."*

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

Exhibit 3(e)-Request and response to 3(e), from IDR #3. Please provide proof of insurance for the business vehicle from CO-6 for 20XX. Also, were your personal vehicles insured with a different insurance company or with CO-6 in 20XX? Their reply was, "*Working on this.*" As of December 8, 20XX no documents have been submitted. IDR # 4 again requested the documentation. Their reply was, "*Can 't find in time for deadline.*"

Exhibit 3(f) -Question and response to question 3(f), from IDR # 3. Why did you rent cars and trucks for trips to City instead of using your personal vehicles? Their response to this was, "*Moved here for business reasons.*" In IDR # 4 the Organization was asked to please provide an explicit explanation of "business reasons." Their reply was, "*As stated in our initial interview/audit in City, State and is stated in our Organization's charter we moved to City to research and establish a "center for promoting the value of play for kids and adults.*"

Exhibit 3(g) -Question and response to question 3(g), from IDR # 3. Do you have receipts for the total moving costs from City to City? If so, please provide the Service with a copy. Their reply was, "*Will find and submit.*" As of the December 8, 20XX no documents have been submitted. IDR # 4 asked the Organization again to please send copies of these receipts. Their reply was, "*Can 't find in time for deadline.*"

Exhibit 4

Exhibit 4(a) -Question and response to question 3(a), from IDR # 3. How do the beauty supply stores, jewelry stores, cleaners, and doctor visits further the Organization's exempt purpose? Their reply was, "*Beauty supplies for girls, will find receipts for other and explain.*" In IDR # 4, the Organization was asked to provide a list of the girls ORG provided beauty supplies for, and the receipts and explanation of the other expenses listed on Exhibit 4(a). Their reply to IDR # 4 was, "*No separate list exists other than the list that was kept on the computer hard drive that can no longer be accessed, and the receipts were presented during the initial interview.*"

Exhibit 4(b) -Request and response to 4(b), from IDR # 3. Please send copies of the medical visits incurred on exhibit 4. Their reply was, "*Okay, will find and submit.*" As of December 8, 20XX no documents have been submitted. In IDR # 4, we asked the Organization to please send the Service copies of the medical visits. Their reply was, "*Can't find in time for deadline.*"

Exhibit 5

Exhibit 5(d) -Request and response to item 5(d) from IDR # 3. Please send copies of the utility bills listed on exhibit 5. Their reply was, "*Coming.*" As of December 8, 20XX no documents have been submitted. In IDR # 4, we asked the Organization to please provide the Service with the requested information. Their reply was, "*Can't find in time for deadline.*"

Exhibit 6

Exhibit 6(a) -Question and response to question 6(a) from IDR # 3. Did ORG keep a log book, or any other records to record the mileage, transactions, and explanations of how these expenses furthered ORG's exempt purpose? Their reply was, "*Answered in Exhibit 3(c).*" As of December 8, 20XX, no documentation has been received. In IDR # 4, we asked the Organization to please provide the Service with the amount of each separate expense for transportation and lodging, the

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

date you left and returned on each outing, who attended each outing, and the name and location of each outing. Their reply was, *"Cannot retrieve from inaccessible computer hard drive in time for deadline."*

Exhibit 6(b) -Question and response to question 6(b) from IDR # 3. Did you record what types of research was performed during your trips to City, TX.? Their reply was, *"Research was on best areas for play/outdoor recreational activities."* In IDR # 4, we asked the Organization to please provide the Service with a list of what sources was used for research. Their reply was, *"Research was done by visiting and researching what areas of the Country would offer the best options for play/outdoor recreation such as hills, water, and abundance of outdoor activity."*

Exhibit 7

Exhibit 7(a) -Request and response to exhibit 7(a) from IDR # 3. Provide a copy of the storage agreement for the office furniture in State. Their reply was, *"Coming."* As of December 8, 20XX no documents have been submitted. In IDR # 4, we asked the Organization to please provide the Service the requested documentation. Their reply was, *"There was no storage agreement."*

Exhibit 7(b) -Question and response to question 6(b) from IDR # 3. Does the office furniture belong to ORG? Their reply was, *"Yes."* IDR # 4 asked for copies of receipts or cancelled checks for the furniture. Their reply was, *"Cannot retrieve from inaccessible computer hard drive in time for deadline."*

Exhibit 7(c) -Question and response to question 7(c) from IDR # 3. What was the total incurred to move the furniture from State to State? Please provide the receipts for the cost of the move. Their reply was, *"Coming."* As of December 8, 20XX no documents have been submitted. IDR # 4 asked the Organization to provide the Service the requested information. Their reply was, *"Cannot retrieve from inaccessible computer hard drive in time for deadline."*

Exhibit 8

Exhibit 8(a) -Request and response from item 8(a) from IDR # 3. Please provide receipts to substantiate the business meetings over lunch and dinner. Their reply was, *"Coming."* As of December 8, 20XX no documents have been submitted. IDR # 4 asked the Organization to please provide the Service the requested information. Their reply was, *"Actual transactions are listed on the copies of the bank statements."*

Exhibit 8(c) -Request and response from item 8(c) from IDR # 3. Provide documentation that shows CO-1 donates drinks to match a portion of ORG's spending. Their reply was, *"Coming."* As of December 8, 20XX no documents have been submitted. IDR # 4 we asked the Organization to please provide the Service the requested information. Their reply was, *"Cannot retrieve from inaccessible computer hard drive in time for deadline."*

IDR # 3 asked about the \$ in assets reported on the 20XX Form 990-EZ, but no response was given. IDR # 4 asked for a list of the assets along with copies of receipts and cancelled checks. Their reply was, *"On the 20XX Form 990-E2 the \$ in assets listed would have been outstanding accounts receivable due to ORG at the time the return was filed."*

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

LAW:

IRC 501(a) provides, in part, that organizations described in section 501(c) are exempt from federal income tax. Section 501(c)(3) provides in pertinent part, that an organization must be organized and operated exclusively for religious, charitable, or educational purposes and no part of its net earnings may inure to the benefit of any private shareholder or individual.

IRC 501(c)(3) are corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, and no part of the net earnings of which inures to the benefit of any private shareholder or individual.

IRC 6001 provides that every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the Secretary it is necessary, he may require any person, by notice served upon such person or by regulations, to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not such person is liable for tax under this title.

IRC 6033(a)(1) provides, except as provided in IRC §6033(a)(2), every organization exempt from tax under Section 501(a) shall file an annual return, stating specifically the items of gross income, receipts and disbursements, and such other information for the purposes of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe.

Treasury Regulation §1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that in order for an organization to be exempt under section 501(c)(3) of the Code it 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 or operational test, it is not exempt.

Treasury Regulation §1.501(a)-1(b)(3)(c) states that the words "private shareholder or individual" in section 501 refer to persons having a personal and private interest in the activities of the organization. The word "shareholder," as used here, does not have the same meaning as it does in a for-profit corporation. An exempt organization cannot have shareholders, or it would not meet the organizational test. However, these are terms that Congress gave us.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

Treasury Regulation §1.501(c)(3)-1(b)(4) provides that an organization is not organized exclusively for one or more exempt purposes unless its assets are dedicated to an exempt purpose. Further, it provides that an organization does not meet the organizational test if its articles or the law of the State in which it was created provide that its assets would, upon dissolution, be distributed to its members or shareholders.

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

Treasury Regulation §1.501(c)(3)-1(c)(2) states 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.

Treasury Regulation §1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests. This group of individuals is generally referred to as "*insiders*." This regulation places the burden of proof on the organization to demonstrate that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled directly or indirectly by such private interests.

The Operational Test must meet the following three requirements:

1. Engage primarily (>50%) in activities which accomplish one or more of the exempt purposes specified in IRC section 501(c)(3) and (Treas. Reg. Section 1.501 (c)(3)-1(c)(1)),
2. Not allow its net earnings to inure to the benefit of private shareholders or individuals (Treas. Reg. Section 1.501(c)(3)-1(c)(2)),
3. Not engage in substantial (>5%) lobbying activity (Treas. Reg. Section 1.501(c)(3)-1(c)(3)), and not engage in any political activity (Treas. Reg. Section 1.501 (c)(3)-1 (c)(3)).

If an organization fails to comply with any of these requirements, it will fail the operational test and lose its IRC section 501(c)(3) exemption.

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

Rev. Rut. 59-95, 1959-1 C.B. 627, concerns an exempt organization that was requested to produce a financial statement and statement of its operations for a certain year. However, its records were so incomplete that the organization was unable to furnish such statements. The Service held that the failure or inability to file the required information return or otherwise to comply with the provisions of IRC § 6033 and the regulations which implement it, may result in the termination of the exempt status of an organization previously held exempt, on the grounds that the organization has not established that it is observing the conditions required for the continuation of exempt status.

In accordance with the above cited provisions of the Code and regulations under IRC § 6001 and 6033, organizations recognized as exempt from federal income tax must meet certain reporting requirements. These requirements relate to the filing of a complete and accurate annual information (and other required federal tax forms) and the retention of records sufficient to determine whether such entity is operated for the purposes for which it was granted tax-exempt status and to determine its liability for any unrelated business income tax.

Revenue Ruling 78-232, 1978-1, C.B.69 explains that in the instant case the money deposited by the taxpayer in the ABC church account was used or available for use for the taxpayer's benefit. The taxpayer had complete control and enjoyment of the money and it was used to maintain the taxpayer's accustomed standard of living. Under the circumstances no portion of the amounts deposited by the taxpayer in the ABC church account can be identified as for the exclusive benefit of the organization.

Church by Mail, Inc. v. Commissioner of Internal Revenue 1985, 765 F.2d 1387,56 A.F.T.R.2d 85-5483, 85-2 USTC P 9549. The dispositive issue in this case is whether the Church meets the "operational" test imposed by I.R.C. § 501 (c)(3). The Treasury Regulations specify three criteria for this requirement. First, the organization must be primarily engaged in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3), so that it is "operated exclusively" for exempt purposes. Treas. Reg. § 1.501(c)(3)-(1)(c)(1). Second, the organization's net earnings must not be distributed in whole or in part to the benefit of private shareholders or individuals.

The tax court upheld the Commissioner's determination, holding that (1) the Church was operated for the non-exempt purpose of providing a market for Twentieth's services, and (2) a substantial, if not principal, purpose of the Church's operations was to generate income for the private benefit of Reverend Ewing and Reverend McElrath and their respective families.

In **Church of Gospel Ministry, Inc. v. United States, 640 F. Supp. 96, 1986 U.S. Dist.**, due to the taxpayer's failure to keep adequate records, the court held that the taxpayer failed to sustain its burden to show that it was qualified for federal tax exemption as a corporation organized and operated exclusively for religious and charitable purposes, as required under IRC §501 (c)(3), and

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

that it was further qualified to receive deductible charitable contributions under IRC §170(c)(2). The court found that as a prerequisite to an IRC §6033 filing exemption, it was necessary for the taxpayer to show it qualified as an IRC §501 (c)(3) organization, which it could not.

John Marshall Law School v. U.S. 1981 WL 11168,48 A.F.T.R.2d 81-5340, 81-2 USTC P 9514 (Ct.Cl. Trial Div. Jun 24,1981) (NO. 27-78, 28-78)

In its determination letter, the IRS stated that it had considered numerous items pertaining to the fiscal years ended August 31, 1967 to August 31, 1973, including, but not limited to, payments by John Marshall Law School (JMLS) for Fenster family: automobiles, education, and travel expenses, insurance policies, basketball and hockey tickets, membership in a private eating establishment, membership in a health spa, interest-free loans, home repairs, personal household furnishings and appliances, and golfing equipment. John Marshall Law School hereinafter (Plaintiff) argued that all the expenses incurred by the organization were ordinary and necessary in furtherance of their exempt purpose. The term 'net earnings' in the inurement-of-benefit clause of § 501(c)(3) has been construed to permit an organization to incur ordinary and necessary expenses in the course of its operations without losing its tax-exempt status. The issue, therefore, is whether or not the expenditures Plaintiff paid to or on behalf of the Fenster family were ordinary and necessary to Plaintiff operations. Also, the burden of proof was on Plaintiff to establish that the grounds set forth in determination letter and the resulting revocation of notice of exemption was erroneous.

Ultimately, the court decided that their jurisdiction was limited to a review of error for the Service's revocation of Plaintiffs favorable tax-exempt ruling. The burden of establishing whether the Plaintiff is an organization described in section 501(c)(3), furthermore, rests with the Plaintiff. It is the courts decision that the Commissioner of Internal Revenue's revocation of Plaintiffs notices of exemption for the years 1966 through 1973 was correct.

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 purposes, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. Also, the existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. The Court found that the trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

GOVERNMENTS POSITION:

Based on the facts shown above, ORG has been involved in numerous transactions that without further detail indicates the Organization is not operating within scope of IRC 501(c)(3).

ORG, a corporation recognized by the Internal Revenue Service as being exempt from federal income tax under Internal Revenue Code section 501 (c)(3) and having a foundation status of

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

170(b)(1)(A)(vi), must pass two tests in order to continue its exempt status. The first test, an organizational test, relates to the organizational documents. This test can only be satisfied if the written documents prepared at the time of the organization's formation meets the requirements of the regulations. An organizational document must meet requirements in both form and language. ORG satisfied the organizational requirement by having their Articles of Incorporation formed under the State of State' non-profit corporation law. Their Articles of Incorporation were stamped received by the Secretary of State of State. ORG also satisfied the language requirement by having an acceptable purpose clause, powers clause, and although not needed in the State of State, a dissolution clause.

The second test relates to the organization's activities. To establish that ORG operates primarily in activities which accomplish its exempt purposes, the Organization must establish that no more than an insubstantial part of its activities does not further an exempt purpose. Section 1.501(c)(3)-1 (c)(1), Income Tax Regulations. The presence of a single substantial nonexempt purpose destroys the exemption regardless of the number or importance of the exempt purposes. *Better Business Bureau v. United States*. While ORG is not an action organization, it has failed to comply with the first two conditions of the operational test because of the egregious usage of the Organization's assets for private benefit.

A Section 501(c)(3)'s assets are required to be irrevocably dedicated to their exempt purpose(s). Treasury Regulations Section 1.501(c)(3)-1 (b)(4). The inurement prohibition serves to prevent the individuals who operate the organization from siphoning off any of a 501(c)(3) organization's income or assets for personal use.

An organization is described in Section 501(c)(3) only if no part of its net earnings inures to the benefit of any private shareholder. The inurement prohibition is designed to insure that organization's assets are dedicated to exclusively furthering public purposes. ORG is not operated exclusively for exempt purposes because its net earnings inure to the benefit of DIR-1 & DIR-2. Inurement can take the form of questionable transactions that have no causal relationship to the organization's exempt purpose(s) but result in some benefit to an insider. The insiders, DIR-1 & DIR-2, are in a position to exercise control over the organization's net earnings as if they were their own by using them at will rather than within the limitations of a fiduciary capacity. In effect, the Booth's are using the public's "net earnings" for their own benefit by using the Organization's assets to further their own interests. ORG has breached the private inurement prohibition.

Although the requirements for finding inurement or private benefit are similar, inurement and private benefit differ in two key respects. The first is that even a minimal amount of inurement results in disqualification for exempt status, whereas private benefit must be more than quantitatively or qualitatively incidental in order to jeopardize tax exempt status. The second is that inurement only applies to "insiders" (individuals whose relationship with an organization offers them an opportunity to make use of the organization's income or assets for personal gain),

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

whereas private benefit may accrue to anyone. ORG has failed the operational requirement (inurement), in using a substantial amount of the Organization's assets for personal gain as discussed in Treasury Regulation Section 1.501(c)(3)-1(d)(1)(ii). Inurement can take the form of any transaction. The transaction results in inurement because it provides a disproportionate benefit to an insider. Both DIR-1 & DIR-2 are considered insiders. Private inurement may be as straightforward as a cash payment to an insider when the Organization has no obligation to pay. Put simply, *inurement* is the use of an exempt organization's assets to benefit an individual(s) connected to it on a personal level. As a result, such use means the organization does not exclusively serve the public. Note, that the payment of personal expenses of an insider that the organization did not characterize as compensation at the time of payment may constitute inurement even when, if added to compensation, the total amount of compensation would be reasonable.

As in the case of *John Marshall Law School v. U.S.*, the assets of ORG inured to the private benefit of DIR-1 & DIR-2, Officers of ORG. The Internal Revenue Code and Regulations provide that an organization exempt under IRC Section 501(c)(3) cannot allow its assets to benefit private interests; an organization that allows their assets to benefit private interests is not exempt.

The "not more than an insubstantial part of its activities" standard of Section 1.501(c)(3)I(c)(1) of the Regulations can be understood by reference to *Better Business Bureau v. United States*, 316 U.S. 279 (1945) which held that an organization which engaged in some educational activity but pursued nonprofit goals outside the scope of the statute was not exempt under Section 501(c)(3) of the Code. The Court stated that an organization is not operated exclusively for charitable purposes if it has a single non charitable purpose that is substantial in nature. This is true regardless of the number or importance of the organization's charitable purposes. Thus, the operational test standard prohibiting a substantial nonexempt purpose is broad enough to include inurement, private benefit, and operations which further goals outside the scope of Section 501(c)(3).

DIR-1 & DIR-2 used ORGs debit card everyday of the 20XX calendar year except for a total of 35 days. No debit card statements were available for review for the month of September 20XX. While the number of days the card was used is not the issue, the types of transactions are. There was no calendar of events, no client listings, no billing information, and no log books were kept as to where and when the outings took place, and how many individuals participated. IRC 6001 requires that every person liable for any tax imposed by the Code shall keep adequate records. ORG failed to keep such records as required by this Code section. Also, IRC 6033(a)(1) requires every organization exempt from tax under Section 501 (a) shall file an annual return stating specifically the items of gross income, receipts and disbursements. In the 20XX Form 990-EZ the Organization filed stated that they had \$ in Accounts Receivable, but there was no explanation as to what it involved. In IDR # 3 & 4, we asked to list the \$ in assets. We did not get a response to this question in IDR # 3. In IDR # 4, we again asked as to the nature of the \$ in assets, and their

Name of Taxpayer
ORG

Year/Period Ended

December 31, 20XX

response was, "On the 20XX Form 990-EZ the \$ in assets listed would have been outstanding accounts receivable due to ORG at the time the return was filed." This was not specifically explained, nor was the client incentives, such as who the clients were, when they met, and what was discussed.

CONCLUSION:

In the case of ORG, the primary activity is to use the assets of the Organization for personal gain. ORG does not qualify for exemption from Federal Income Tax as an organization described in Section 501 (c)(3) of the Code because of the egregious nature as to which the assets of the Organization were used for personal gain.

Consequently, we are proposing ORG's exemption from federal income tax be revoked as of January 1, 20XX. Please file U.S. Corporation income tax return Form for tax periods ending December 31, 20XX, December 31, 20XX, December 31, 20XX, December 31, 20XX, and December 31, 20XX. Contributions to your organization are not deductible under IRC Code Section 170.

If you agree with our decision please sign and return Form in the enclosed envelope.

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. Please refer to the attached letter and Publications enclosed for specific details of this process.