



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE: EO Examinations

1100 Commerce Street, MC 4920 DAL

Dallas, TX 75242

Uil: 501.03-01

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

May 16, 2016

Release Number: 201409014

Release Date: 2/28/2014

Taxpayer Identification Number:

Person to Contact:

LEGEND:

ORG = Name of Organization

Identification Number:

Contact Telephone Number:

ADDRESS = Address of Organization

Year = xx

ORG

ADDRESS

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). Our favorable determination letter to you dated August 6, 19xx is hereby revoked and you are no longer exempt under section 501(a) of the Code effective July 1, 20xx.

You have failed to establish that you are operated exclusively for exempt purposes within the meaning of Internal Revenue Code section 501(c)(3), and that no part of your net earnings inure to the benefit of private shareholders or individuals. You failed to respond to repeated reasonable requests to allow the Internal Revenue Service to examine your records regarding your receipts, expenditures, or activities as required by I.R.C. sections 6001 and 6033(a)(1).

Contributions to your organization are no longer deductible under IRC §170.

You are required to file income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the tax year ending June 30, 20xx and for all tax years thereafter in accordance with the instructions of the return.

Processing of income tax returns and assessments of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination under the declaratory judgment provisions of section 7428 of the Code, a petition to the United States Tax Court, the United States Claims Court, or the district court of the United States for the District of Columbia must be filed before the 91st Day after the date this determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing petitions for declaratory judgments by referring to the enclosed Publication 892. You may write to these courts at the following addresses:

United States Tax Court
400 Second Street, NW
Washington, D.C. 20217

United States Court of Federal Claims
717 Madison Place, NW
Washington, D.C. 20005

United States District Court for the District of Columbia
333 Constitution Avenue, NW
Washington, D.C. 20001

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 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:

Internal Revenue Service

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

Sincerely,

Nanette M. Downing
Director, EO Examinations

Enclosure:
Publication 892

Internal Revenue Service
Tax Exempt and Government Entities Division
Exempt Organizations: Examinations

Department of the Treasury

Date: January 13, 2012

Taxpayer Identification Number:

Legend:

ORG = Name of Organization
ADDRESS= Address of Organization

ORG
Address

Form:

990

Tax Year(s) Ended:

June 30, 20xx

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:

Internal Revenue Service
Office of the Taxpayer Advocate

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

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number	Year/Period ended June 30, 20xx

LEGEND:

ORG = Name of Organization
 Director = Name of Executive Director
 Date = xx
 State = Name of State

Issues:

Whether ORG, . is organized and operating to further tax-exempt purposes as described under Section 501(c)(3) of the Internal Revenue Code?

Facts:

On December 6, 19xx, the organization's Director, filed Articles of Incorporation with the State establishing ORG, . The purpose of the corporation is to present multi-media performances of art in motion, through the interaction of visual and performing arts, using sculptured form, music, lighting and film; to create and present abstractions of the human body and humanizations of abstract sculptured ideas; to educate and promote public awareness of this multi-media form of art through workshops; installations, slide and video shows, seminars and discussions groups.

The corporation is organized exclusively for charitable and educational purposes, including, for such purposes, the making of distributions to organizations that qualify as exempt organizations under Section 501(c)(3) of the Internal Revenue Code. No part of the net earnings of the corporation shall inure to the benefit of, or be distributable to, its members, directors, officers, or other private persons, except that the corporation shall be authorized and empowered to pay reasonable compensation for services rendered. Upon the dissolution of the corporation, the board of directors shall, after payment of all of the liabilities of the corporation, dispose of all of the assets of the corporation to other organizations organized and operated exclusively for charitable, educational, religious or scientific purposes as described under Section 501(c)(3) of the Internal Revenue Code.

On February 19, 19xx, the Internal Revenue Service received Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, from ORG, . Form 1023 Part III states that the organization is devoted to the promotion of live performance of multi-media art in motion. The performances include kinetic sculptures using dances to physically move the sculpture presented. In addition to performances, the organization also gives slide shows and demonstrations. The organization's principal sources of support will be from grants from private foundations, schools, and state art councils to enable it to give free performances and workshops. ORG, secondary source of support will be from receipts from performances to which tickets are sold. On August 6, 19xx, ORG, . was granted exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number	Year/Period ended June 30, 20xx

On April 29, 20xx a letter was received by the Internal Revenue Service from the Office of the Attorney General regarding the operations of ORG, . The letter states that ORG, articles provide for the use of the same name as a for-profit created on March 10, 19xx by Director. The for-profit ORG, . was created for the following purposes:

- (a) To engage in the business of marketing designs, developing designs and manufacturing products from developed designs.
- (b) To carry on any business or other activity which may be lawfully carried on by a corporation organized under the Business Corporation Law of the State.

The letter states that the for-profit ORG . was involuntarily dissolved on December 31, 19xx. The letter states that the majority of information that is publicly available about ORG, activities relate to the rental of an exhibition space and the creation of fabric structures for commercial purposes. The following discrepancies were noted by the Attorney General's Office from ORG, 20xx Form 990:

- 1) The organization's website www. .org immediately goes to www. .com which contains no reference to the non-profit, its charitable mission or activity. The website describes ORG, activities as event marketing, architecture and retail, exhibits and conferences, hotels and other venues and lists clients.
- 2) \$ million reported in revenue for "rentals and other income" and describes it as "income from furnishing facilities below fair market value to organizations whose activities are in furtherance of ORG, tax exempt purpose," but it would seem that the revenue predominantly comes from creating signs and marketing for commercial purposes;
- 3) That more than million in expenses is for "enrich[ing] the public with performance and visual fabric art by putting on performances and offering below market ticket prices," but the performances appear to be commercial in nature, comprised largely of marketing events and trade shows;
- 4) That the entity made significant revenue over the last several years, \$1 in 20xx, \$1 in 20xx, \$2 in 20xx, and \$3 in 20xx, but how that revenue was used for charitable purposes is unclear; and,
- 5) Creator and President signed the Form 990 identifying herself as its owner.

A comparative analysis of ORG, revenues and expenses as reported on Forms 990 for tax years 20xx, 20xx, and 20xx is detailed below.

Revenue	20xx Form 990	20xx Form 990	20xx Form 990
Rentals and Other Income	\$1	\$2	\$1
Total Revenue	\$1	\$2	\$1

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
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Expenses	20xx Form 990	20xx Form 990	20xx Form 990
Production Supply Expenses			
Salaries and Wages of Employees			
Office Expenses			
Compensation of Officers and Directors			
Postage and Shipping			
Advertising and Promotion			
Occupancy			
Employee Benefits			
Travel			
Miscellaneous Expense			
Payroll Taxes			
Accounting Fees			
Bank Charges			
Trade Show Entry Fees			
Professional Fees			
Fees for Services - Other			
Legal Fees			
Supplies			
Insurance			
Conferences and Conventions			
Commissions			
Payroll Fees			
Service Charges			
Office Expenses			
Interest			
Information Technology			
Computer Expense			
Automobile Expense			
Utilities			
Depreciation and Depletion			
Telephone			
Equipment Rental and Maintenance			
All Other Expenses			
Total Expenses	(1)	(2)	(1)
Net Income (Loss)	\$1	(1)	\$1

ORG, . was notified by the Internal Revenue Service on December 13, 20xx of a pending examination of its books and records to be conducted on March 23, 20xx of the Form 990 for the tax year ended June 30, 20xx. The Executive Director listed on the organization's Form 990 is Director Director appointed CPA, to act as Power of Attorney for the organization. The examination was conducted at the accounting firm.

On March 23, 20xx, an initial interview was conducted with the organization's Power of Attorney, . CPA, to obtain an understanding of the organization's activities during the year under examination. CPA stated that ORG, . generated income from performance fees and renting its art. He stated that the non-profit organization never received any contributions or ever solicited donations. CPA stated that ORG, . was leasing space in State to create its art in an apartment owned by an unrelated 3rd party. .

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number	Year/Period ended June 30, 20xx

State. The reason provided by the postal service for returning the letter to the Internal Revenue Service was because the mail forwarding service had expired.

On September 20, 20xx, the organization's Power of Attorney, CPA, was contacted because no response was provided to the Information Document Request mailed to him on August 19, 20xx. CPA advised the Service that he would no longer be representing ORG,

During the year under examination, ORG received % of its revenue from sales and rentals of its art. The organization did not receive any contributions from the general public. The Internal Revenue Service sampled the organization's expenses and discovered that 0% of ORG, total expenses incurred for the year were used to further for-profit commercial activities. During the year under examination, ORG, activities and resources were directed to benefit a for-profit business, rather than exclusively to accomplish Section 501(c)(3) purposes. Therefore, ORG, does not qualify for exemption from federal income tax under Section 501(c)(3) of the Internal Revenue Code.

Law:

Internal Revenue Code

Section 501(c)(3) of the Internal Revenue Code provides for the exemption from taxation 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, no part of the net earnings of which inures to the benefit of any private shareholder or individual, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 6001 of the Code states 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.

Federal Tax Regulations

Section 1.501(c)(3)-1(a)(1) of the Federal Tax Regulations states in order to be exempt as an organization described in Section 501(c)(3) of the Internal Revenue Code, 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(d)(2) of the regulations states that the term "charitable" is used in Section 501(c)(3) of the Code in its generally accepted legal sense. Such term includes relieving the poor and distressed or the underprivileged, advancement of education or science, lessening of the burdens of government, combating community deterioration, lessening neighborhood tensions, and eliminating prejudice and discrimination.

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Section 1.501(c)(3)-1(d)(3)(b) of the regulations states that the term "educational" as used in Section 501(c)(3) of the Code relates to the instruction of the public on subjects useful to the individual and beneficial to the community.

Court Cases

In the case of Airlie Foundation v. Internal Revenue Service, 283 F.Supp.2d 58, the United States District Court upheld the Service's position to revoke the organization's tax-exempt status under Section 501(c)(3) of the Code. The grounds for revocation included the organization's earnings inuring to the benefit of its founder and the organization's operation of a conference center in a commercial manner. The Court stated that in cases where the organization's activities could be carried out for either exempt or non-exempt purposes, the manner in which the activities are carried out must be examined in order to determine their true purpose. In assessing an organization's claim for tax-exempt status under the operational test, the court considers competition with for-profit commercial entities; extent and degree of below cost services provided; pricing policies; reasonableness of financial reserves; whether the organization uses commercial promotional methods; and the extent to which the organization receives charitable donations.

In the case of B.S.W. Group, Incorporated v. Commissioner of Internal Revenue, 70 T.C. 352, the United States Tax Court upheld the Service's position to deny the organization's application for recognition of exemption under Section 501(c)(3) of the Code for failing to meet the operational test by primarily engaging in a trade or business. The Court stated that under the operational test, the purpose towards which an organization's activities are directed, and not the nature of the activities themselves, ultimately determines the organization's right to be classified as a Section 501(c)(3) organization. The fact that the organization's activities may constitute a trade or business does not, of itself, disqualify it from classification under Section 501(c)(3), provided the activity furthers or accomplishes an exempt purpose. Rather, the critical inquiry is whether the organization's primary purpose for engaging in the activities is an exempt purpose, or whether its primary purpose is the non-exempt purpose of operating a commercial business. Factors such as the particular manner in which an organization's activities are conducted, the commercial hue of those activities, and the existence and amount of annual or accumulated profits are relevant evidence of a non-exempt purpose.

In the case of the Better Business Bureau of Washington, D.C., v. United States, 326 U.S. 279, 66 S.Ct.112, the Supreme Court of the United States determined that for the Better Business Bureau of Washington, D.C. to fall within exemption from taxation, the organization must be devoted exclusively to educational purposes, and the presence of a single non-educational purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly educational purposes. The Court stated that it is apparent beyond dispute that an important, if not primary, pursuit of the Better Business Bureau of Washington, D.C. is to promote not only an ethical but also a profitable business community.

The Court stated that the commercial hue permeating the organization is reflected in its corporate title and in the charter provisions dedicating the organization to the promotion of the 'mutual welfare, protection and improvement of business methods among merchants' and others and to the securing of the 'educational and scientific advancements of business methods' so that merchants might 'successfully and profitably conduct their business.' The Court stated that the organization's activities are largely animated by this commercial purpose. Unethical business practices and fraudulent merchandising schemes are investigated, exposed and destroyed. The Court stated that such efforts to cleanse the business system of dishonest practices are highly commendable and may even serve incidentally to educate certain persons

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but that they are directed fundamentally to ends other than that of education. The Court stated that any claim that education is the sole aim of the organization is thereby destroyed.

Revenue Rulings

Revenue Ruling 71-529, 1971-2 C.B. 234, considered whether an organization that provides assistance in the management of participating colleges and university's endowment fund substantially below cost qualifies for exemption under Section 501(c)(3) of the Code. Membership in the organization is restricted to colleges and universities exempt under Section 501(c)(3) of the Code. The organization will not make its services available to anyone other than the exempt organizations controlling it. Most of the operating expenses of the organization, including the costs of the services of the investment counselors and the custodian banks, are paid for by grants from independent charitable organizations. The member organizations pay a nominal fee for the services performed. By performing this function for the organization for a charge that is substantially below cost, the organization is performing a charitable activity within the meaning of Section 501(c)(3) of the Code. Accordingly, it is held that the organization qualifies for exemption from federal income tax under Section 501(c)(3) of the Code.

Revenue Ruling 72-369, 1972-2 C.B. 245, considered whether an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations qualifies for exemption under Section 501(c)(3) of the Code. The services consist of writing job descriptions and training manuals, recruiting personnel, constructing organizational charts, and advising organizations on specific methods of operation. To satisfy the operational test the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of Section 501(c)(3) of the Code. An organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. Providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The fact that the services are provided at cost and solely for exempt organizations is not sufficient to characterize the activity as charitable within the meaning of Section 501(c)(3) of the Code. Accordingly, it is held that the organization's activities are not charitable and therefore the organization does not qualify for exemption from federal income tax under Section 501(c)(3) of the Code.

Taxpayer's Position:

ORG, position with respect to the issues, facts, applicable law, and government's position as discussed in this report is unknown. The organization will be allowed 30-days to review this report and respond with a rebuttal if considered necessary.

Government's Position:

In order to qualify for exemption under Internal Revenue Code Section 501(c)(3), an organization must be both organized and operated exclusively for charitable or educational purposes, provided that no part of the net earnings of such corporation inures to the benefit of any private shareholder or individual. The purpose of ORG, as provided in its Articles of Incorporation is to present multi-media performances of art in motion, through the interaction of visual and performing arts, using sculptured form, music, lighting and film; to create and present abstractions of the human body and humanizations of abstract sculptured ideas; to educate and promote public awareness of this multi-media form of art through workshops; installations, slide and video shows, seminars and discussion groups. However, there has been no

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
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evidence provided in the record to demonstrate that ORG, . has provided any form of education, public awareness seminars or discussion groups to benefit the general public.

During the year under examination, ORG, . operated in a manner similar to the for-profit corporation considered in Airlie Foundation v. Internal Revenue Service., 283 F.Supp.2d 58 in which the United States District Court upheld the Service's position to revoke the organization's tax-exempt status under Section 501(c)(3) of the Code. The Court ruled that Airlie Foundation operated in a commercial manner and did not further tax-exempt purposes as described under Section 501(c)(3) of the Code. Similarly, ORG, . sold its products in a commercial manner and competed with for-profit entities providing similar services. During the year under examination, ORG, . did not operate to further tax-exempt purposes as described under Section 501(c)(3) of the Code.

In the case of B.S.W. Group, Incorporated v. Commissioner of Internal Revenue., 70 T.C. 352, the United States Tax Court upheld the Service's position to deny the organization's application for recognition of exemption under Section 501(c)(3) of the Code for failing to meet the operational test by primarily engaging in a trade or business. The Court stated that factors such as the particular manner in which an organization's activities are conducted, the commercial hue of those activities, and the existence and amount of annual or accumulated profits are relevant evidence of a non-exempt purpose. During the year under examination, ORG, . operated solely in a manner indistinguishable from a for-profit business. The organization maintained a website similar to a for-profit business advertising its products for sale or rent. The website also listed for-profit companies as its clients and there is no mention on the website of any charitable or educational services provided by the organization.

In the case of the Better Business Bureau of Washington, D.C., v. United States., 326 U.S. 279, 66 S.Ct.112, the United States Supreme Court ruled that to obtain exemption from taxation, an organization must be devoted exclusively to exempt purposes, and the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. It is clearly evident that the primary purpose of ORG, . is to sell or rent its fabric structures rather than to accomplish exclusively Section 501(c)(3) purposes. ORG, . has not provided records to demonstrate that the organization is furthering tax-exempt purposes. During the year under examination, ORG, . did not engage in any educational activities as described in the regulations. ORG, . did not instruct the public on subjects useful to the individual or beneficial to the community.

Conclusion:

The exempt status of ORG, . is to be revoked effective July 1, 20xx, for failing to operate in accordance with the requirements under Section 501(c)(3) of the Internal Revenue Code. For the tax year ended June 30, 20xx, the organization is required to file Form 1120. ORG, . is required to file Form 1120 for all subsequent tax periods. Per Internal Revenue Code Section 6020(b)(2), the Internal Revenue Service has the authority to file substitute for returns, and assess the correct amount of tax in situations where the taxpayer fails to file the required returns.