Internal Revenue Service
Director, Exempt Organizations
Rulings and Agreements

Department of the Treasury
P.O. Box 2508 - EP/EO
Cincinnati, OH 45201

Date: NOV 0 8 2002

[redacted]

Employer Identification Number:
[redacted]

Person to Contact - I.D. Number:
[redacted]

Contact Telephone Numbers:
[redacted] Phone
[redacted] FAX

Dear Sir:

We have considered your application for recognition of exemption from Federal income tax under the provisions of section 501(c)(3) of the Internal Revenue Code of 1986 and its applicable Income Tax Regulations. Based on the available information, we have determined that you do not qualify for the reasons set forth on Enclosure I.

Consideration was given to whether you qualify for exemption under other subsections of section 501(c) of the Code. However, we have concluded that you do not qualify under another subsection.

As your organization has not established exemption from Federal income tax, it will be necessary for you to file an annual income tax return on Form 1041 if you are a Trust, or Form 1120 if you are a corporation or an unincorporated association. Contributions to you are not deductible under section 170 of the Code.

If you are in agreement with our proposed denial, please sign and return one copy of the enclosed Form 6018, Consent to Proposed Adverse Action.

You have the right to protest this proposed determination if you believe it is incorrect. To protest, you should submit a written appeal giving the facts, law and other information to support your position as explained in the enclosed Publication 892, "Exempt Organizations Appeal Procedures for Unagreed Issues." The appeal must be submitted within 30 days from the date of this letter and must be signed by one of your principal officers. You may request a hearing with a member of the office of the Regional Director of Appeals when you file your appeal. If a hearing is requested, you will be contacted to arrange a date for it. The hearing may be held at the Regional Office or, if you request, at any mutually convenient District Office. If you are to be represented by someone who is not one of your principal officers, he or she must file a proper power of attorney and otherwise qualify under our Conference and Practice Requirements as set forth in Section 601.502 of the Statement of Procedural Rules. See Treasury Department Circular No. 230.

[redacted]

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides, in part, that:

> A declaratory judgement 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 administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within the time specified, this will become our final determination. In that event, appropriate State officials will be notified of this action in accordance with the provisions of section 6104(c) of the Code.

Sincerely,

Lois G. Lerner

Lois G. Lerner
Director, Exempt Organizations
Rulings and Agreements

Enclosures: 3

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[redacted]

Facts

A review of your Articles of Incorporation, which do not bear the State filed or approved date stamp, show that you are organized exclusively to develop, on a non-profit basis, a housing project at [redacted], for low-income persons.

Page 2 of Form 1023 states that the project is targeted to lease to very-low-income families who, without this program, could not afford to live in this type of housing. Page 2 of Form 1023 also refers to the [redacted] (the "Plan"). The Plan, however, describes the activities of the [redacted] ("[redacted]") rather than your own activities.

You state that you are organized by and through the auspices of [redacted] to act as a shield to protect [redacted] a section 501(c)(3) organization, from liabilities that could be imposed upon the sponsor of the low-income housing project for which the sponsor is the guarantor of various obligations.

You are governed by [redacted], and [redacted]. In your [redacted] letter, you state that all three are employees of [redacted], a social service agency that acquires, develops, and manages the [redacted]. The letter states that [redacted] is the [redacted] of all housing activities of [redacted]; [redacted] is [redacted]; and [redacted] is the [redacted]. The [redacted] letter from [redacted] to [redacted] shows that [redacted] is also the [redacted] and that [redacted] is the [redacted].

You submitted an Amended and Restated Agreement of Limited Partnership that was executed on [redacted] (the "Partnership Agreement") showing you as the General Partner with .[redacted]% interest, [redacted] as the Investment Partnership with [redacted]% interest, and [redacted]., as the Special Limited Partner with .[redacted]% interest in the project of [redacted] units. The Investment Partnership and the Special Limited Partner are collectively referred to as the Limited Partners.

The Partnership Agreement shows you, as the General Partner, represent, warrant, covenant, and guarantee the tax credit

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[redacted]

shortfall and recapture for each year during the credit period, the timing reduction amount (delay in receipt of tax credits), the repurchase of the Investment Partnership's interest, if actual credit for any year is less than [redacted]% of certified credit as a return of capital to the Investment Partnership, the development fee, the development cost overruns, the operating deficits, etc. (refer to [redacted], and other affected provisions). Section [redacted] also states that you indemnify the Investment Partnership against any breach of representations, warrants, and covenants.

Section 8.15 of the Partnership Agreement provides, in part:

> The General Partner hereby collaterally assigns, pledges, and grants a security interest to the Investment Partnership in all right, title and interest the General Partner has in its Interest hereunder and in the right to receive any distributions and payments under this Agreement, including without limitation, any payments with respect to Operating Deficit Loans and GP Loans and distributions of Net Cash Flow and Cash from Capital Event ("GP Pledged Payments"). The General Partner irrevocably directs the Partnership to pay to the Investment Partnership any GP Pledged Payments at any time that there is an unsatisfied obligation secured by the GP Pledged Payments.

The Pledge and Security Agreement, which you pledge to the Investment Partnership, defines "collateral" as:

(i) All of Debtor's right, title and interest in the Partnership, whether now owned or hereafter acquired, including, without limitation, its general partner's interest in the Partnership and its right to receive distributions, allocations and payments under the Partnership Agreement, as such Partnership Agreement may be modified from time to time with consent of the Secured Party;

(ii) All fees and charges to be paid by e Partnership to the Debtor, whether now owned or hereafter acquired, whether arising under the Partnership Agreement or otherwise;

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[redacted]

(iii) All indebtedness of the Partnership to Debtor of any kind or description; and

(iv) All products and proceeds whether cash proceeds or noncash proceeds, and products of any and all of the foregoing.

You state that [redacted] contracts [redacted] to develop the property and that [redacted] assigns its position in the contracts to you upon your creation. You state that, as the sponsor and the owner, you secure the loans for the project. In the [redacted] Unanimous Written Consent of the Board of Directors, you were authorized to borrow $[redacted] from [redacted] (the "[redacted]") and an [redacted] loan of $[redacted] from [redacted] ("[redacted]"). The loan documents show you secured a $[redacted] loan from [redacted], a [redacted] loan of $[redacted] from the [redacted], and a mortgage from [redacted], [redacted]. for $[redacted]. The Unconditional Guaranty signed by the Developer, [redacted], on [redacted] states that the Investment Partnership made a loan for $[redacted] and that [redacted] ("[redacted]") made a loan for $[redacted] you, which resulted in the [redacted] Note and the Construction Loan Note, respectively. You state that, upon completion of the construction, you contributed the property to the Partnership subject to and pursuant to the consent of [redacted] and the [redacted]. You state that, at the time of the transfer of the building, the loans were terminated either by contributions from the investors or transfer of the [redacted] grants. You state that all loans from the [redacted] and its agents became part of the Investment Partnership's capital and were used for construction costs and related expenses such as legal fees, title insurance, filing fees, etc. in connection with the closing. You state that the loan from [redacted] became a grant to you for payment of the rehabilitation.

[redacted] of the Partnership Agreement defines "Land" as the tract of land currently owned by the General Partner, to be transferred and contributed to the Partnership upon which the apartment complex is located. [redacted] states that you agree to contribute the apartment complex to the Partnership upon receipts of all consents of the authority. [redacted] of the Partnership Agreement states that the General Partner shall transfer and assign to the Partnership all of its rights, title, and interest in and to the apartment complex. The court document shows that you transferred the project to the Partnership for a

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[redacted]

sum of $[redacted] and the Partnership became an additional obligee on all Notes and Regulatory Agreements.

[redacted] of the Partnership Agreement states that, upon transfer of the title to the apartment complex to the Partnership following the completion of its rehabilitation, the General Partner shall assign and transfer all of its interest as a general partner to a wholly owned for-profit subsidiary of [redacted]. You submitted a copy of the [redacted] of the [redacted] filed wi[redacted] on [redacted] which shows [redacted]. is the substitute General Partner.

The Assignment and Assumption Agreement signed between you and the wholly owned for-profit subsidiary of [redacted]. shows that you transfer all interests, obligations, rights and duties to [redacted]. However, you are designated as the Guarantor by definition of the Partnership Agreement and as the Debtor by definition of the Pledge and Security Agreement. You state that the Investment Partnership agrees with the transfer of guarantees by allowing [redacted]. to replace you as the [redacted]. The [redacted]. is hereafter referred to as the General Partner.

You currently do not own any interest in the Partnership. You state that your primary role is to oversee the operation of the apartments and to make certain that it continues to operate solely for the low-income residents of the community. However, the Partnership Agreement provides no charitable purpose. Section 3.01 of the Partnership Agreement states:

> Purpose of the Partnership. The Partnership has been organized exclusively to acquire the Apartment Complex and to develop, rehabilitate, finance, construct, own, maintain, operate and sell or otherwise dispose of the Apartment Complex, in order to obtain long-term appreciation, cash income, Tax Credits and tax losses.

By definition of the Partnership Agreement, the Special Limited Partner must consent to the selection and removal of the Accountants ([redacted]). The Special Limited Partner must also consent to the withdrawals from the reserve for replacements ([redacted]). [redacted] of the Partnership Agreement provides that the Special Limited Partner has the right to remove the General Partner when the General Partner violates its guaranties pursuant to Section [redacted], [redacted] and/or [redacted], and when the

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[redacted]

amount of actual credits for any year are, or are projected by the Accountants after the State Designation to be, less than [redacted]% of the certified credits for that year.

In your [redacted] letter, you state that each reason given in Redlands Surgical Services, Inc. v. Commissioner, 113 T.C. 47 (1999) must be answered positively in your case, i.e. charitable purposes must be followed pursuant to the Partnership Agreement, the Regulatory, and other agreements with t[redacted], and the control over day-to-day operations of the Partnership are vested in a corporation, controlled and owned by you, which in turn is owned by [redacted]. Your letter further states that your oversight function is accomplished because the General Partner is owned and controlled by you and managed by [redacted]. You state that [redacted] and you have the same board members; therefore, the control and direction of the operations of the Partnership effectively remain with non-profit entities. You also state that the management has contracted with a section 501(c)(3) organization to operate the project; therefore, there is no competitive commercial market for low-income housing.

In your [redacted] letter, you also indicate that, unless the court permits a piercing of the corporate shields and allows a party to sue [redacted] or you, neither [redacted] nor you are responsible for the obligations of the General Partner in the Partnership, because [redacted] is not a party of the agreement, and your only assets are your interest in the project through the ownership of the [redacted].

You state that the Partnership itself is subject to the Partnership Agreement which sets forth the authority of the Partnership in [redacted] and pursuant to subsection [redacted] thereunder to provide housing subject to the Minimum Set Aside Test and the Rent Restriction Test and consistent with the Requirements of the Extended Use Agreement, the Regulatory Agreement and the Loan Agreement. You further state that the Partnership is subject to the Regulatory Agreement with [redacted], which requires [redacted] occupancy by low-income families (an acceptable charitable function). You state that sponsoring housing for low-income residents who could not otherwise afford decent housing clearly is an activity in furtherance of an exempt purpose. You cite Regulations 1.501(c)(3)-(1)(d)(2), Revenue Rulings 70-585, 79-18, and 79-19, Notice 93-1, and Private Letter Ruling ("PLR") 199929049.

When asked for a budget for 2002 and 2003, you stated in the [redacted] letter "there is no proposed budget for 2002 or

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[redacted]

[redacted] the entity being a mere shell without any current activity."

Law

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable purposes.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states that, in order to be exempt as an organization described in section 501(c)(3) of the 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(a)-1(c) of the Regulations states that the words "private shareholder or individual" mean an individual having a personal and private interest in the activities of the organization.

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 which 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(d)(1) of the Regulations provides, in part, that an organization may be exempt under section 501(c)(3) of the Code if it is organized for charitable purposes. However, it is not organized or operated exclusively for a charitable purpose unless it serves a public rather than a private interest. Thus, an organization must establish that it is not organized or operated for the benefit of designated individuals.

Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations states that an organization is not organized or operated exclusively for one or more exempt purposes 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

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[redacted]

interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Section 1.501(c)(3)-(1)(d)(2) of the Regulations states the term 'charitable' is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of 'charity' as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency. The fact that an organization which is organized and operated for the relief of indigent persons may receive voluntary contributions from the persons intended to be relieved will not necessarily prevent such organization from being exempt as an organization organized and operated exclusively for charitable purposes. The fact that an organization, in carrying out its primary purpose, advocates social or civic changes or presents opinion on controversial issues with the intention of molding public opinion or creating public sentiment to an acceptance of its views does not preclude such organization from qualifying under section 501(c)(3) so long as it is not an 'action' organization of any one of the types described in paragraph (c)(3) of this section.

Section 6110(k)(3) of the Code states, unless the Secretary otherwise establishes by regulations, a written determination may not be used or cited as precedent.

Application of Law

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279, 283 (1945) the Supreme Court holds that the presence of a single non-exempt purpose, if substantial in nature, destroys a claim for exemption regardless of the number or importance of truly exempt purposes.

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[redacted]

In Plumstead Theatre Society, Inc. v. Commissioner, 74 T.C. 1324 (1980). 675 F.2d 244 (9th Cir. 1982), the Court holds that an organization's participation as a general partner in a limited partnership will not adversely affect its tax-exempt status under section 501(c)(3) of the Code. Important to the holding is that (a) the transaction is at arm's length, (b) the general partner is not obligated to return capital to the investors out of its own funds, and (c) the limited partners have no control over the way the organization managed its affairs.

In Redlands Surgical Services, v. Commissioner, 113 T.C. 47 (1999), the Tax Court holds that a nonprofit wholly owned subsidiary of Redlands Health Systems (a section 501(c)(3) organization) operates for impermissible private benefit when it cedes effective control over partnership operations to private parties. The organization's sole activity is participating as a co-general partner with a for-profit corporation in a partnership that owns and operates an ambulatory surgery center. An affiliate of the for-profit partner is the manager of the surgical center. It receives a [redacted]% management fee under the management agreement. The court closely examines the structure of the relationships among the parties and states:

> Clearly, there is something in common between the structure of petitioner's sole activity and the nature of petitioner's purpose in engaging in it. An organization's purposes may be inferred from its manner of operations; its "activities provide a useful indicia of the organization's purpose or purposes." Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), affd. T.C. Memo. 1990-84. The binding commitments that petitioner has entered into and that govern its participation in the partnerships are indicative of petitioner's purposes. To the extent that petitioner cedes control over its sole activity to for-profit parties having an independent economic interest in the same activity and having no obligation to put charitable purposes ahead of profit-making objectives, petitioner cannot be assured that the partnerships will in fact be operated in furtherance of charitable purposes. In such a circumstance, we are led to the conclusion that petitioner is not operated exclusively for charitable purposes...nothing in the General Partnership agreement, or in any of the other binding commitments relating to the operation of

[redacted]

> the Surgery Center, establishes any obligation that charitable purposes be put ahead of economic objectives in the Surgery Center's operations. The General Partnership agreement does not expressly state any mutually agreed-upon charitable purposes or objective of the partnership.

After a thorough analysis of the all of the operating agreements entered into by the petitioner, the Court reaches the following conclusions:

> Based on all of the facts and circumstances, we hold that petitioner has not established that it operates exclusively for exempt purposes within the meaning of section 501(c)(3). In reaching this holding, we do not view any one factor as crucial, but we have considered these factors in their totality: The lack of any express or implied obligation of the for-profit interests involved in petitioner's sole activity to put charitable objectives ahead of non charitable objectives, petitioner's lack of voting control over the General Partnership; petitioner's lack of other formal or informal control sufficient to insure furtherance of charitable purposes; the long-term contract giving SCA Management control over day-to-day operations as well as a profit-maximizing incentive; and the market advantages and competitive benefits secured by the SCA affiliates as the result of this arrangement with petitioner. Taken in their totality, these factors compel the conclusion that by ceding effective control over its operations to for-profit parties, petitioner impermissibly serves private interests.

In Moline Properties, Inc. v. Commissioner, 319 U.S. 436, 438 (1943), the Court holds that for federal income tax purposes, a parent corporation and its subsidiary are separate taxable entities so long as the purposes for which the subsidiary is incorporated are the equivalent of business activities or the subsidiary subsequently carries on business activities.

In Britt v. United States, 431 F. 2d 227, 234 (5th Cir. 1970), the Court emphasizes that where a corporation is organized with the bona fide intention that it will have some real and substantial business function, its existence may not generally be disregarded for tax purposes.

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[redacted]

In Krivo Industrial Supply Company; Morgan Precision Parts, Inc. v. National Distillers and Chemical Corporation, 483 F.2d 1098, 1106(5th Cir. 1973), the Court holds only where the parent corporation so controls the affairs of the subsidiary that it is merely an instrumentality of the parent may the corporate entity of the subsidiary be disregarded.

Notice 93-1, 1993-1 I.R.B. 172, publishes a safe harbor guideline for processing applications for exemption of organizations that provide low-income housing. This notice provides that an organization will meet the safe harbor guideline if it establishes that at least 75 percent of the units for a given project will be made available for families earning 60 percent or less of the area's median income, as adjusted for family size. Concerning the remaining 25 percent of the units, if any, the organization must adopt a general policy which states that the remaining units will be made available to persons on the lower end of the economic spectrum, yet who may not necessarily be members of a charitable class. It also states that even if an organization satisfies the safe harbor guideline, it may fail to qualify for exemption because private interests of individuals with a financial stake in the project are furthered.

In Rev. Proc. 96-32, section 3, which supersedes Notice 93-1, the Service publishes guidance on the qualification under section 501(c)(3) for organizations engage in low-income housing. The Rev. Proc. states an organization will be considered to relieve the poor and distressed if it establishes that (a) at least 75 percent of the units are occupied by residents that qualify as low-income; and (b) either at least 20 percent of the units are occupied by residents that also meet the very low-income limit for the area or 40 percent of the units are occupied by residents that also do not exceed 120 percent of the area's very low-income limit. Up to 25 percent of the units may be provided at market rates to persons who have incomes in excess of the low-income limit.

Rev. Proc. 96-32, section 7, states if an organization furthers a charitable purpose such as relieving the poor and distressed, it nevertheless may fail to qualify for exemption because private interests of individuals with a financial stake in the project are furthered. For example, the role of a private developer or management company in the organization's activities must be carefully scrutinized to ensure the absence of inurement or impermissible private benefit resulting from real property sales, development fees, or management contracts.

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[redacted]

Rev. Rul. 70-585, 1970-2 C.B. 115, describes four situations in which an organization assists individuals or families to obtain housing. In Situation 1, the organization assists low-income families obtain housing who cannot qualify for loans under a federal loan program and who cannot otherwise afford any housing. In this example, the Service concludes by providing homes for low-income families, who cannot otherwise afford them, the organization relieves the poor and distressed, which is charitable. Situation 1 concludes by noting that the determination of what constitutes low income is a factual question based on all of the surrounding circumstances. In Situation 2, the organization provides low- and moderate-income housing to ease the housing problems of minority groups. The housing units are located to reduce racial imbalance in the community and are designed to eliminate prejudice and discrimination, and lessen neighborhood tension. As such, the organization is held charitable within the meaning of section 501(c)(3) of the Code. In Situation 3, the organization has a purpose to rehabilitate housing in an area that is generally old and badly deteriorated where the median income is lower than other parts of the city. It then rents the units at cost to low- and moderate-income families. Those activities combat community deterioration and are charitable within the meaning of section 501(c)(3) of the Code. In Situation 4, the organization assists moderate-income families to obtain affordable housing in an area where, because of high land costs, increased interest rates, and growing population, there is a shortage of housing for moderate-income families. The organization in Situation 4 does not provide relief to the poor or carry out any other charitable purpose within the meaning of section 501(c)(3) of the Code. Accordingly, it is not exempt under section 501(a).

Rev. Rul. 79-18, 1979-1 C.B. 194 provides that a nonprofit organization that provides specially designed housing to elderly persons at the lowest feasible cost and maintains in residence those tenants who subsequently become unable to pay its monthly fees is an organization operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code.

Rev. Rul. 79-19, 1979-1 C.B. 195 provides a nonprofit organization that provides specially designed housing to physically handicapped persons at the lowest feasible cost and maintains in residence those tenants who subsequently become unable to pay its monthly fees is operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code.

Rev. Rul. 98-15, situation 2, describes an LLC that enters into a

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[redacted]

long-term agreement with a wholly owned subsidiary of the for profit member to provide the day-to-day management services to the LLC. It is essentially a perpetual contract in that it is renewable at the discretion of the manager. The lack of structural control is worsened by the contractual control vested in the for-profit or its affiliate. The perpetual duration of the management arrangement makes the arrangement in essence a non-arm's length contract by virtue of ceding control over renewals to the for-profit. Such organization does not qualify for exemption because the control over hospital operations has substantially shifted to the for-profit party.

Discussion

Section 501(c)(3) of the Code sets forth two main tests for qualification for exempt status. An organization must be both organized and operated exclusively for purposes described in section 501(c)(3). With respect to the organizational test, your Articles of Incorporation contain section 501(c)(3) provisions; however, the document does not contain the filed or approved stamp [redacted]. You must also satisfy the operational test. The key requirement is that an organization be operated exclusively for one or more exempt purposes. An organization is not operated exclusively to further exempt purposes unless it serves a public rather than a private interest.

Historically, the Service did not recognize general partners in limited partnerships as exempt from federal income tax under section 501(c)(3), because of the inherent conflict with operating for the benefit of investors and operating exclusively for charitable purposes. Following the case of Plumstead Theatre Society, the Service loosened its approach to the exemption of organizations acting as general partners in limited partnerships. Our guidelines require that we scrutinize the relationships of the partners to assure that the exempt general partner can operate exclusively for charitable purposes.

Housing Pioneers, Redland Surgical Services, and Rev. Rul. 98-15 indicate that where a charity's primary activity is conducted through a partnership, then the charity must control the partnership to ensure that operations are conducted in furtherance of charitable purposes. See also Plumstead Theatre Society.

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[redacted]

You state that your primary role is to oversee the project and make certain that it continues to operate for the benefit of the low-income residents. You state that sponsoring housing for low-income residents who could not otherwise afford decent housing clearly is an activity in furtherance of an exempt purpose. You cite Regulations 1.501(c)(3)-(1)(d)(2), Revenue Rulings 70-585, 79-18, and 79-19, Notice 93-1, and PLR 199929049 in supporting your position. A private letter ruling is issued under section 6110(k)(3) for a particular organization and is not intended to be used as an authority. Furthermore, the exempt organizations discussed in the subject authorities or non-authorities and you differ factually.

Regulations 1.501(c)(3)-(1)(d)(2) provides the definition of the term "charitable" and states that an organization organized and operated to relieve the poor and the distressed is charitable. However, Regulations 1.501(c)(3)-1(d)(1)(ii) provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. By sponsoring a low-income housing that meets the requirements under section 42 or the Minimum Set Aside Test and the Rent Restriction Test alone does not necessarily satisfy section 501(c)(3) of the Code. Not all low-income housing projects qualify for exemption under section 501(c)(3) of the Code.

Furthermore, you are organized for a single housing project. Initially, you owned the general partner interest but you subsequently transferred your interest to a for-profit corporation, which you claim sometimes as your own subsidiary and other times, as that of [redacted]. You state that your goal is to oversee the housing project and to make certain it continues to operate solely for low-income residents. However, you have no ownership interest in and have no managing authority over the affair of the Partnership. Under these circumstances, you are not in a position to claim that you cause the Partnership to carry out your charitable purpose. With respect to your goal, you have not demonstrated that you conduct a charitable activity because you are merely a shell with no activities, no employees, and no operating budgets of your own. You do not have a charitable activity. When asked of your financial statements, you even state that you are "a mere shell without any current activity." Therefore, you have not established you are operated exclusively for charitable purposes as defined in Regulations 1.501(c)(3)-(1)(d)(2).

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[redacted]

In Rev. Ruls. 70-585 (Situations 1, 2, and 3), 79-18, and 79-19, the Service rules that these organizations are exempt under section 501(c)(3) because, not only do they provide affordable housing directly to low-income families, physically handicapped persons, and elderly persons, but there is also no evidence that they serve private interests. An organization described in Situation 4 of Rev. Rul. 70-585 is held not be exempt because it serves a non-charitable class of people. These revenue rulings do not apply to you because the organizations described in these rulings directly own and operate the housing projects and there are no private investors involved. You, on the other hand, do not own or operate any housing project. You claim your activity is to oversee the operation of a housing project and to make certain it continues to operate solely for low-income residents in the community; however, the project is owned and operated by for profit parties and you are not a partner and have no managing authority over the Partnership. A for-profit entity is not in any way obligated to perform within the meaning of section 501(c)(3).

The organization described in PRL 199929049 provides loans and credit enhancement service to organizations that develop affordable housing projects at the rates below commercial market rates. That organization serves as a "lender of last resort" to enable the development of affordable housing when federal, state or local government funding is not available and when under writing standards cause commercial lenders to decline such loans. That organization limits its services to various low-income housing organizations, which qualify for tax-exempt status. Such organization differs from you because it conducts a charitable activity by continually providing below market rate loans to exempt organizations that otherwise would not be able to obtain through conventional loans. You, on the other hand, secure loans for only one housing project that is owned and operated by a for-profit entity (the Partnership) in which you are not a partner.

A corporation is a separate entity, a legal being having an existence separate and distinct from that of its owner. Whether [redacted] or you are the owner of the General Partner, the activity of [redacted] or the General Partner cannot be attributed to you because [redacted] and the General Partner are separate legal corporations. Since you have no charitable activity of your own, you may not use activities of the General Partner, the Partnership, or the [redacted] to solely establish your basis of exemption as indicated in Moline Properties and Pittt. Even if the General Partner is wholly owned by [redacted] and is treated as disregarded for tax purposes of [redacted] as ruled in Krivo

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[redacted]

Industrial Supply, the activity of the General Partner still cannot be attributed to you because [redacted] and you are two separate legal entities. This is so even though [redacted] and you have an identical governing board. Even if the General Partner is wholly owned by you and is treated as disregarded for your tax purposes as ruled in Krivo Industrial Supply, the housing project is still not considered charitable, because of a guarantee of return on investment to the Investment Partnership and the control given to the Limited Partners.

In this regard, Plumstead Theatre Society provides guidance. In that case, the general partner is not obligated to return capital out of its own funds and the limited partners have no control over the general partner in the management of its affairs. In sum, the limited partnership does not intrude into the exemption operations.

One problem with the Partnership Agreement is the lack of any obligation of the for-profit partners of the Partnership to place any charitable purpose ahead of their commercial objectives, which is a key factor in Redlands Surgical Services and Rev. Rul. 98-15. The Partnership Agreement is silent with respect to any charitable purpose. The Partnership's purpose is to maximize and protect the economic interests of the Investment Partnership. As for-profit entities (the Partnership, the General Partner, and the Limited Partners), they are not obligated to operate within the parameter of section 501(c)(3). The for-profit entities that own and operate the project have economic goals strikingly different from, and often in conflict with, the charitable goal of providing low-income housing. To qualify for exemption under section 501(c)(3), an organization must not serve private interests in carrying out its low-income housing project. Since you do not have an ownership in the Partnership, you have no authority to direct the Partnership in its operation.

Regardless of the Minimum Set Aside Test, the Rent Restriction Test, the Extended Use Agreement, the Regulatory Agreement, the Loan Agreement(s), and the safe harbor described in Rev. Proc. 96-32, section 7 of Rev. Proc. 96-32 states that an organization, which meets the safe harbor, can very well fail to meet the qualifications of section 501(c)(3) because of private interests. As demonstrated in Better Business Bureau, a single function may actually achieve more than one purpose. If one purpose is non-exempt and substantial in nature, it destroys the exemption regardless of the number and importance of the exempt purposes. Thus, regardless of the fact that you may cause the Partnership to provide housing to persons regarded as poor and distressed,

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[redacted].

you do not qualify for exemption if the substantial purpose of yours is to benefit the Investment Partnership via a guarantee of return on investment.

You state that you transfer your interests, rights, and obligations to the wholly owned subsidiary of an affiliated section 501(c)(3) organization. This includes tax credit shortfalls and recaptures and any other guarantees and obligations described in the Partnership Agreement and in the Pledge and Security Agreement. You state that the Limited Partners agree with the transfer of guarantees by allowing [redacted]. to replace you as the General Partner. However, there is no indication that the Investment Partnership agrees to the transfer of guarantees of return on investment. [redacted] of the Partnership only states that you assign and transfer all of your interests as a general partner in the Partnership to [redacted]. Furthermore, the Partnership Agreement and the Pledge and Security Agreement indicate that such obligations are irrevocable and that you are obligated to assign what is "now owned and hereafter acquired."

When the Investment Partnership invests in the Partnership, its capital is at risk and it is uncertain whether the Investment Partnership will get a return on the investment. By guaranteeing the difference between the projected tax credits and the actual tax credits, you, as the Debtor of the Pledge and Security Agreement, operate to remove the risk of the Investment Partnership and indemnify the Investment Partnership's speculation that its investment will pay-off as projected. As stated in Notice 93-1 and Rev. Proc. 96-32, even if an organization satisfies the safe harbor guideline, it may very well fail to qualify for exemption because private interests of individuals with a financial stake in the project are further. The arrangement privately benefits the Investment Partnership, which results in violation of section 1.501(c)(3)-1(d)(1) of the Regulations.

Conclusion

Under the facts presented, the Service concludes that you are not operated exclusively for charitable purposes because you do not have a charitable activity. In addition, your existence serves private benefits to the Investment Partnership because the partnership in which you claim to be the sponsor does not place

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[redacted]

charitable objectives ahead of profitable objectives and has a substantial purpose to obtain tax credits and other benefits for the Investment Partnership.

Accordingly, based on all the facts and circumstances, the Service concludes that you do not qualify for recognition of exemption from federal income tax as an organization described in section 501(c)(3) of the Code.