



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE: EO Examinations

1100 Commerce Street, MC 4920 DAL

Dallas, TX 75242

501.03-00

**TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION**

December 3, 2012

Number: **201338049**
Release Date: 9/20/2013

LEGEND

ORG - Organization name

XX - Date Address - address

Taxpayer Identification Number:

Person to Contact:

Identification Number:

Contact Telephone Number:

ORG

ADDRESS

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

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 February, 20XX is hereby revoked and you are no longer exempt under section 501(a) of the Code effective January 1, 20XX.

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

You are not operating exclusively for any charitable purpose, educational purpose, or any other exempt purpose. Our examination reveals that you are not engaged primarily in activities which accomplish charitable, educational or other exempt purposes as required by Treas. Reg. 1.501(c)(3)-1(c)(1). Your activities, including your financial transactions, more than insubstantially furthered non-exempt purposes. Moreover, you failed to establish that you were not operated for the benefit of private interest of your executive director as required for continued recognition of exemption pursuant to Treas. Reg. 1.501(c)(3)-1(d)(1)(ii). Your income inured to the benefit of private shareholders and individuals.

Contributions to your organization are no longer deductible under IRC §170 after January 1, 20XX.

You are required to file Form 1120 U. S. Corporation Income Tax Return. You have filed Form 1120 U. S. Corporation Income Tax Return for the years ended December 31, 20XX, December 31, 20XX and December 31, 20XX with us. In addition, for future

periods, you are required to file Form 1120 with the appropriate service center indicated in the instructions for 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:

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:

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



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE

TE/GE EO Examinations

4330 Watt Ave; Stop# 6209

Sacramento, CA 95821

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

May 4, 2012

ORG
ADDRESS

Taxpayer Identification Number:

Form Number:

Tax Year Ended:

Person to Contact/ID Number:

Employee Telephone Number:

Phone:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear _____ :

We propose to revoke our recognition of your exempt status as an organization described in section 501(c)(3) of the Internal Revenue Code (the Code). We enclose our report of examination explaining why we are proposing this action.

If you accept our proposal, please sign and return the enclosed Form 6018, *Consent to Proposed Action - Section 7428*, unless you have already provided us a signed Form 6018. We will issue a final revocation letter determining you are not an organization described in section 501(c)(3). After the issuance of the final revocation letter we will publish an announcement that you have been deleted from the cumulative list of organizations contributions to which are deductible under section 170 of the Code. If you do not respond to this proposal, we will similarly issue a final revocation letter. Failing to respond to this proposal may adversely impact your legal standing to seek a declaratory judgment because you may be deemed to have failed to exhaust administrative remedies.

If you do not agree with our proposed revocation and wish to protest our proposed revocation to the Appeals Office of the Internal Revenue Service, then 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. This written request is called a protest. For your protest to be valid it needs to contain certain specific information which generally includes a statement of the facts, the applicable law, and arguments in support of your position. For the specific information needed for a valid protest, please refer to page 6 of the enclosed Publication 3498, *The Examination Process*, and page 1 of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

Modified Letter 3618

If you do submit a valid protest, then 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 and Publication 892 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. Please note that Fast Track Mediation Services referred to in Publication 3498, generally do not apply after issuance of this letter.

You may also request that we refer this matter for Technical Advice as explained in Publication 892 and an annual revenue procedure. Please contact the individual identified on the first page of this letter if you are considering requesting Technical Advice. If we issue a determination letter to you based on a Technical Advice Memorandum issued by the EO Rulings and Agreements function, then no further administrative appeal will be available to you within the IRS on the matter.

If you receive a final revocation letter, you will be required to file Federal income tax returns for the tax period(s) shown above as well as for subsequent years.

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

Enclosure:
Publication 892,
Publication 3498,
Form 6018,
Report of Examination

Modified Letter 3618

Form 886-A (Rev. January 1994)	EXPLANATIONS OF ITEMS	Schedule number or exhibit
Name of taxpayer ORG	Tax Identification Number EIN	Year/Period ended 12/31/20XX

LEGEND

ORG - Organization name XX - Date DIR-1 - 1st DIR CO-1 through CO-12 - 1st through 12th COMPANIES

Issue

Whether ORG("ORG") qualifies for exemption under Internal Revenue Code ("IRC") Section 501(c)(3).

Facts

The organization was granted exemption under section 501(c)(3) in February, 20XX. To this date, this determination has not been changed. ORG is a small organization which rescues dogs and cats and puts them in foster homes. The organization uses various resources such as www.petfinder.com and the newspaper to find people to adopt the animals. When someone adopts the animals they sign an adoption contract and pay a fee which ranges from \$-\$.

The organization filed Form 990-N, *e-Postcard* for the periods ended December 31, 20XX through December 31, 20XX and has not filed a return for the 20XX period.

An appointment letter (L3613) and information document request, Form 4564 (IDR) was sent to ORG on April 10, 20XX requesting information needed to determine whether the organization was organized and operating for exempt purposes. Items requested in the IDR included:

- Governing Instruments: (Articles of Incorporation, Bylaws, etc.)
- Minutes of Meetings
- Books and records of assets, liabilities, receipts and disbursements
- Records showing the dates and amounts of all adoption fees received
- Records of Contributions, and Donations (cash and noncash) received
- Source documents kept for Jan 1, 20XX- Dec 31, 20XX such as: receipts, bills, invoices, vouchers
- Check register, bank statements, bank reconciliations, returned checks, canceled checks
- Contracts/Leases/Rental Agreements in effect during period under examination (including any adoption contracts from 20XX)

On May 1, 20XX the Assigned Agent began the examination at the representative's office. The organization did not have any meeting minutes because no formal meetings were held. The bank statements and adoption contracts were provided. The bank statements show \$ was deposited into the checking account at CO-12. Most of the organization's funds came from adoption fees. Adoption fees were paid via check, cash, and credit card; however the organization currently only accepts cash. According to the adoption contracts provided, the organization received \$ in fees for 153 dogs and 210 cats that were adopted in 20XX.

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There was \$ in withdrawals from the organization's checking account. Besides some of the veterinarian bills, the organization did not have any other receipts, invoices, or reimbursement vouchers for their expenses. There were numerous questionable expenditures noted in the bank statements which were unsubstantiated such as:

- Gas Station (CO-1)
- Supermarket (CO-2)
- Restaurants
- Coffee Shop (CO-3)
- Clothing Store (CO-4, CO-5, CO-6, CO-7)
- Cell Phone, Cable, Internet bills (CO-8, CO-9, CO-10)
- CO-11

Source documents were needed to determine how funds were used and whether they were used for charitable purposes. The organization has not kept adequate books and records.

The Assigned Agent determined DIR-1, Executive Director, was responsible for caring for and finding people to adopt the cats; and three volunteers were responsible for caring for and finding people to adopt the dogs. The organization did not maintain an accountable plan for reimbursements. The three volunteers kept a portion of the adoption fees to cover their expenses and did not provide any substantiation showing how the money was used. There wasn't any contemporaneous documentation showing the organization approved this practice. The organizations funds were used to purchase gasoline on a regular basis and none of the officers or volunteers kept mileage logs.

DIR-1 has signature authority on the organization's bank account and makes the decisions on the direction and policy of ORG. There are other officers, but they did not appear to be actively involved in the organization.

Law

IRC § 501(c)(3) provides for exemption of organizations organized and operated exclusively for charitable purposes, 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 the IRC, or for the collection thereof, shall keep adequate records as the Secretary of the Treasury or his delegate may from time to time prescribe.

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IRC § 6033(a)(1) provides, except as provided in IRC § 6033(a)(3), 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.

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

Treas. Reg. § 1.501(c)(3)-1(b) **Organizational test**--(1) In general. (i) An organization is organized exclusively for one or more exempt purposes only if its articles of organization:

- (a) Limit the purposes of such organization to one or more exempt purposes; and
- (b) Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities, which in themselves are not in furtherance of one or more exempt purposes.

Treas. Reg. § 1.501(c)(3)-1(c) **Operational test**--(1) Primary activities. 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.

Treas. Reg. § 1.501(c)(3)-1(c)(2) Distribution of earnings. 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.

Treas. Reg. § 1.501(c)(3)-1(d)(i) **Exempt purposes**-- An organization may be exempt as an organization described in section 501(c)(3) if it is organized and operated exclusively for one or more of the following purposes:

- (a) Religious,
- (b) Charitable,
- (c) Scientific,
- (d) Testing for public safety,

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(e) Literary,

(f) Educational, or

(g) Prevention of cruelty to children or animals.

Treas. Reg. § 1.501(c)(3)-1(d)(ii) 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.

Treas. Reg. § 1.6001-1(a) in conjunction with Treas. Reg. § 1.6001-1(c) provides that every organization exempt from tax under IRC § 501(a) and subject to the tax imposed by IRC § 511 on its unrelated business income must keep such permanent books or accounts or records, including inventories, as are sufficient to establish the amount of gross income, deduction, credits, or other matters required to be shown by such person in any return of such tax. Such organization shall also keep such books and records as are required to substantiate the information required by IRC § 6033.

Treas. Reg. § 1.6001-1(e) states that the books or records required by this section shall be kept at all times available for inspection by authorized internal revenue officers or employees, and shall be retained as long as the contents thereof may be material in the administration of any internal revenue law.

Treas. Reg. § 1.6033-1(h)(2) provides that every organization which has established its right to exemption from tax, whether or not it is required to file an annual return of information, shall submit such additional information as may be required by the district director for the purpose of enabling him to inquire further into its exempt status and to administer the provisions of subchapter F (section 501 and the following), chapter 1 of the Code and IRC § 6033.

Rev. Rul. 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

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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.

Taxpayer's Position

The issue was presented and the representative expressed agreement with the government's position.

Government's Position

Based on the cited law, it is the government's position that ORG failed to meet its reporting/recordkeeping requirements and has not demonstrated it meets the requirements under section 501(c)(3). Section 6033 requires organizations exempt from tax to keep records and render statements as are required by rules and regulations prescribed by the Secretary. Treasury Regulation section 1.6033-2(i)(2) requires organizations exempt from tax to submit such additional information as the Internal Revenue Service may require for the purpose of inquiring into the organization's exempt status.

The organization failed to demonstrate it met the operational test for a section 501(c)(3) organization. In order to meet the operational test, ORG must demonstrate it engages primarily in activities which accomplish one or more exempt purposes specified in section 501(c)(3). See *Treas. Reg. section 1.501(c)(3)-1(d)(ii)*. An organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. Information was obtained which shows ORG has not operated exclusively for charitable purposes because part of its net earnings inured to the benefit of the officers and volunteers that run the organization.

Using the organizations funds to buy groceries, coffee, food at restaurants, clothes, and pay for cell phone, cable and/or Internet bills are not necessary for ORG's tax-exempt purpose and is inurement. A substantial amount of the organization's funds was used to pay for gasoline. There wasn't corroborative information such as mileage logs, and the Assigned Agent could not determine if these expenses served the organizations interests or private interests. The organization did not have any internal controls and there was no accountability for how funds were used. The organization does not require substantiation of expenses and there is no board oversight of how funds are used.

This situation is similar to the case in Revenue Ruling 59-95. In that case, tax-exempt status was revoked for failure to establish that it was observing the required conditions for exempt status, namely, providing financial statements.

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In addition to the aforementioned issues ORG filed Form 990-N instead of an annual information return. ORG's gross receipts were over \$ and the organization was required to file Form 990-EZ or Form 990.

Conclusion

It is the Service's position that ORG failed to meet the reporting requirements under IRC section 6001 and 6033 to be recognized as exempt from federal income tax under IRC section 501(c)(3). The organization did not provide information or demonstrate that it was organized and operating exclusively for exempt purposes and no part of net earnings inured to the benefit of any private shareholder or individual.

Accordingly, the organization's exempt status should be revoked effective January 1, 20XX. Contributions will no longer be deductible under section 170 of the Internal Revenue Code. Form 1120 returns should be filed for all tax periods ending on or after December 31, 20XX.