

**Internal Revenue Service**  
Appeals Office  
Royal Palm One, Suite 350  
1000 South Pine Island Road  
Plantation, FL 33324

**Department of the Treasury**

**Employer Identification  
Number:**

**Person to Contact:**

**Date:** FEB 06 2015

**Number:** 201518020

**Release Date:** 5/1/2015

**Employee ID Number:**

**Tel:**

**Fax:**

**UIL:** 7428.02-00

ORG

**Certified Mail**

Dear :

This is a final adverse determination regarding your exempt status under section 501(c)(3) of the Internal Revenue Code (the "Code"). It is determined that you do not qualify as exempt from Federal income tax under section 501(c)(3) of the Code effective January 1, 2012.

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

Organizations exempt from Federal income tax under section §501(c)(3) of the Internal Revenue Code are required to operate exclusively for charitable, education, or other exempt purposes. Organizations are not operated exclusively for exempt purposes if the net earnings of the organization inure in whole or in part to the benefit of private shareholders or individuals of the organization. See Treas. Reg. §1.501(c)(3)-1(c)(2). We have determined that your net earnings inured to the benefit of private individuals due to the distribution of your organization's primary asset to the trustees in 2012. As such, you have not operated exclusively for exempt purposes and have operated for the benefit of private interests of individuals in contravention of the requirements of Treas. Reg. §1.501(c)(3)-1(d)(1)(ii).

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

You are required to file Federal income tax returns on Forms 1041. File your return with the appropriate Internal Revenue Service Center per the instructions of the return. For further instructions, forms, and information please visit [www.irs.gov](http://www.irs.gov).

If you were a private foundation as of the effective date of revocation, you are considered to be taxable private foundation until you terminate your private foundation status under section 507 of the Code. In addition to your income tax return, you must also continue to file Form 990-PF by the 15th Day of the fifth month after the end of your annual accounting period.

We will make this letter and the proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. We have provided to you, in a separate mailing, Notice 437, *Notice of Intention to Disclose*. Please review the Notice 437 and the documents attached that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437.

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

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

Sincerely Yours,

Timothy D. Jarvis  
Appeals Team Manager

Enclosure: Publication 892



Department of the Treasury  
Internal Revenue Service  
Tax Exempt and Government Entities Division

UIL: 501.03.00

ORG

Date:

NOVEMBER 15, 2013

Taxpayer Identification Number:

Form:

Tax year(s) ended:

Person to contact / ID number:

Contact numbers:

Phone Number:

Fax Number

Manager's name / ID number:

Manager's contact number:

Phone Number:

Response due date:

**Certified Mail - Return Receipt Requested**

Dear

**Why you are receiving this letter**

We propose to revoke your status as an organization described in section 501(c)(3) of the Internal Revenue Code (Code). Enclosed is our report of examination explaining the proposed action.

**What you need to do if you agree**

If you agree with our proposal, please sign the enclosed Form 6018, *Consent to Proposed Action – Section 7428*, and return it to the contact person at the address listed above (unless you have already provided us a signed Form 6018). We'll issue a final revocation letter determining that you aren't an organization described in section 501(c)(3).

After we issue the final revocation letter, we'll announce that your organization is no longer eligible for contributions deductible under section 170 of the Code.

**If we don't hear from you**

If you don't respond to this proposal within 30 calendar days from the date of this letter, we'll issue a final revocation letter. Failing to respond to this proposal will adversely impact your legal standing to seek a declaratory judgment because you failed to exhaust your administrative remedies.

**Effect of revocation status**

If you receive a final revocation letter, you'll be required to file federal income tax returns for the tax year(s) shown above as well as for subsequent tax years.

**What you need to do if you disagree with the proposed revocation**

If you disagree with our proposed revocation, you may request a meeting or telephone conference with the supervisor of the IRS contact identified in the heading of this letter. You also may file a protest with the

Letter 3618 (Rev. 6-2012)  
Catalog Number 34809F

IRS Appeals office by submitting a written request to the contact person at the address listed above within 30 calendar days from the date of this letter. The Appeals office is independent of the Exempt Organizations division and resolves most disputes informally.

For your protest to be valid, it must contain certain specific information including a statement of the facts, the applicable law, and arguments in support of your position. For specific information needed for a valid protest, please refer to page one of the enclosed Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*, and page six of the enclosed Publication 3498, *The Examination Process*. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process. Please note that Fast Track Mediation referred to in Publication 3498 generally doesn't apply after we issue this letter.

You also may request that we refer this matter for technical advice as explained in Publication 892. 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 Exempt Organizations Rulings and Agreements office, no further IRS administrative appeal will be available to you.

**Contacting the Taxpayer Advocate Office is a taxpayer right**

You have the right to contact the office of the Taxpayer Advocate. Their assistance isn't a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate can't reverse a legally correct tax determination or extend the time you have (fixed by law) to file a petition in a United States court. They can, however, see that a tax matter that hasn't 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

**For additional information**

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:  
Report of Examination  
Form 6018  
Publication 892  
Publication 3498

Letter 3618 (Rev. 6-2012)  
Catalog Number 34809F

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
<b>Explanation of Items</b>		
Name of Taxpayer		Year/Period Ended
ORG		12/31/20XX

**LEGEND**

ORG - Organization name      XX - Date      Address - address      City - city  
 State - state      County - county      Trustee-1 to 6 - Trustee-1 to 6

**ISSUE**

1. Did the transfer of the personal residence, to the ORG, owned by the trustees of the ORG benefit private persons resulting in inurement and/or private benefit and result in the potential revocation of the 501(c)(3) Foundation exempt status?
2. Did the ORG transfer of 112.65 acres of land located in City, State on or about December 12, 20XX to Trustee-1 and Trustee-6 (both disqualified persons) via General Warranty Deed filed with the office of Recorder of County County, State result in inurement and/or private benefit and in the potential revocation of the 501(c)(3) Foundation exempt status?

**FACTS FOR ISSUE 1 TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION**

The ORG filed a Trust Agreement in City, State on March 18, 20XX. The purpose of the Trust Agreement was to create the Foundation exclusively for charitable, religious, scientific, literary 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.

Trustees of the ORG, at the date of inception, were Trustee-1 and Trustee-2, husband and wife.

On or about June 21, 20XX, The ORG received Letter 1076 from the Internal Revenue Service granting the Foundation exemption from Federal income tax under Internal Revenue Code Section 509(a) as a charitable organization as described in section 501(c)(3) of the Code, effective date of the exemption was April 10, 20XX.

On April 15, 20XX, The ORG held an Annual Trustee Meeting. Those present at the meeting were Trustee-1, Ph.D., Trustee, Trustee-2, Trustee; Trustee-3; Trustee-4; Trustee-5. At this meeting a discussion was conducted centering on the donation of the residence to the foundation. Additional discussions were conducted concerning the purchase of land and/or a building for the Foundation's future school. It was decided that by the end of 20XX, the ORG would purchase property in City, State

On or about December 6, 20XX, Trustee-1 and Trustee-2 transferred their personal residence, located at Address, City, State, to the ORG. An appraisal was conducted this date by Appraiser of Appraiser Appraisal for the purpose of determining the fair market value of the property located at Address, City, State Zipcode. The fair market value as determined by the appraiser as \$0.

The Form 990-PF filed for the period ended December 31, 20XX, reported Real Property on the Asset schedule at \$0 and Liabilities at \$0. These amounts were corrected on the Form 990-PF filed for the period ended December 31, 20XX, the residence cost/basis was correct to \$0 and two bank loans were reported for the residence:

Bank loan dated 11/      loan amount      \$0  
 loan dated 11/20XX loan amount      \$0

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
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ORG		12/31/20XX

On or about March 15, 20XX, the ORG sold the residence at Address, City, State to a third party and reported a loss on the sale on the Form 990-PF filed for the period ended December 31, 20XX.

On or about August 21, 20XX, Trustee-2 died.

Sometime in 20XX, Trustee-1 remarried and his current wife, Trustee-6 was added as a trustee of the ORG.

On or about May 20, 20XX in reference to United States Tax Court in the matter of Trustee-1 v Commissioner of Internal Revenue Service Document No. 1 a judgment was entered into by all parties in agreement that it was determined that under the law the home was not actually contributed to the ORG and the donation of the home to the Foundation did not meet the requirements of the law

#### **FACTS FOR ISSUE 2 TRANSFER OF CITY LAND FROM THE FOUNDATION TO THE DISQUALIFIED PERSONS**

On or about April 2, 20XX, The ORG purchased 112.65 acres of land located on Address, City, State at a contract price of \$0. The Form 990-PF filed for the period ended December 31, 20XX, reported the property purchase on its Balance Sheet as Real Property Acquisition at \$0 with liabilities of \$0. These amounts were corrected on the Form 990-PF filed for the period ended December 31, 20XX with the assets value being corrected to \$0 and liabilities being added for Bank loan dated 03/20XX loan amount \$0.

On or about December 12, 20XX the ORG transferred 112.65 acres of land located in City, State to Trustee-1 and Trustee-6 via General Warranty Deed filed with the office of Recorder of County County, State.

On or about January 18, 20XX, the 112.65 acres of land was listed with local City, State realtors for sale at an asking price of \$0.

On or about February 15, 20XX, Trustee-1 and Trustee-6 sold the 112.65 acres to Third Party.

The ORG filed Form 990-PF with the Internal Revenue Service for the periods ended December 31, 20XX, 20XX, 20XX, 20XX, 20XX and 20XX.

#### **LAW.**

Internal Revenue Code Section 501(c)(3) states "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, ..." (emphasis added)

Section 501(c)(3) of the Code forbids inurement of any part of the net earnings of a qualifying organization to the benefit of any private shareholder or individual. "Any part" literally means any part. The smallest amount of inurement will result in the organization's failure to meet the requirements for exempt status.

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer  <b>ORG</b>		Year/Period Ended  <b>12/31/20XX</b>

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

Treasury Regulation section 1.501(a)-1(c) defines a private shareholder or individual for section 501 purposes as those persons having a personal and private interest in the activities of the organization.

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

Treasury Regulation section 1.501(c)(3)-1(c)(1) states 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.

Treasury Regulation section 1.501(c)(3)-1(c)(2) states, in part, that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

Internal Revenue Code Section § 4941(d)(1)(A) provides that any sale or exchange of property between a disqualified person and a private foundation is self-dealing. As with most of the defined categories of self-dealing, sales or exchanges of property are flatly prohibited, rather than being judged by an arm's-length standard or eligible for a de-minimis exception.

Reg. § 4941(d)-2(a)(2) provides that the transfer of property by a disqualified person to a private foundation is treated as a sale or exchange if the private foundation assumes a mortgage, or takes subject to a mortgage that was placed on the property, within the 10-year period ending on the date of the transfer of the property to the private foundation.

#### **ARGUMENT AND RATIONALE FOR ISSUE 1 TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION**

The trustees for the Foundation formed the Foundation and transferred their personal residence to the Foundation. The Personal Residence had a mortgage associated with it as described above. As addressed in Internal Revenue Code Section § 4941(d)(1)(A), above, this is an act of self-dealing and is prohibited under Internal Revenue Code Section 501(c)(3) and would cause the revocation of the exempt status of the Foundation.

As stated above, on or about May 20, 20XX in reference to United States Tax Court in the matter of Trustee-1 v Commissioner of Internal Revenue Service Document No. 1 a judgment was entered into by all parties in agreement that it was determined that under the law the home was not actually contributed to the ORG and the donation of the home to the Foundation did not meet the requirements of the law. There was no charitable purpose for the contribution of this residence to the Foundation.

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
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ORG		12/31/20XX

**ARGUMENT AND RATIONALE FOR ISSUE 2 TRANSFER OF CITY LAND FROM THE FOUNDATION TO THE DISQUALIFIED PERSONS**

On or about December 12, 20XX the ORG transferred 112.65 acres of land located in City, State to Trustee-1 and Trustee-6 via General Warranty Deed filed with the office of Recorder of County County, State. This was an act prohibited by 501(c)(3) and Internal Revenue Code Section § 4941(d)(1)(A) and Reg. § 4941(d)-2(a)(2).

**TAXPAYERS POSITION**

**FIRST ISSUE (TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION).** In response to your question as to the personal benefit received by the transfer of the personal residence owned by the Trustees to the Foundation in the calendar year 20XX.

- a. This issue was settled in the U S Tax Court Case as set forth above and the related tax assessment was personally paid by the trustees as an integral part of that settlement.
- b. This property was sold and disposed of prior to January 1, 20XX and should not be an issue in this examination as the statute of limitation has now expired on this transaction.
- c. The exempt status of the Foundation was not disallowed as a part of this settlement with the U. S. Tax Court and therefore your claim for personal benefits to the trustees does not in fact exist as there was no benefit to the related parties following the action of the U.S. Tax Court.
- d. The settlement of this issue effective for the calendar years 20XX, 20XX, and 20XX resulted in the elimination of any possible "inurement and/or private benefit" to the trustees of the Foundation. In fact the reality of the circumstances and following settlement by the U. S. Tax Court resulted in a definite significant economic loss to e trustees.
- e. One of the trustee involved in your proposed adjustment passed away on August 21, 20XX, which as several months prior to the beginning of the fiscal year you have under examination. There is no way she benefitted from this transaction during the calendar year 20XX as you have asserted.
- f. Trustee-6 (now Trustee-6) did not become involved in the Foundation operation until her marriage to Trustee-1 on May 19, 20XX, which was almost 5 months past the fiscal year end of December 31, 20XX. Therefore there is also no way she benefitted from your proposed claim during the calendar year 20XX.

**SECOND ISSUE (TRANSFER OF CITY LAND FROM THE FOUNDATION TO THE DISQUALIFIED PERSONS).** The response to this issue requires it be broken down into two parts, one for which we agree and one for which we disagree.

- a. We acknowledge and agree that the City Property was purchased in 20XX and the purchase was accompanied with the creation of a debt to Bank. Numerous transactions involving the payment of this debt from 20XX thru December 31, 20XX were included in Exhibits A thru T submitted on January 6, 20XX. The debt was clearly a vital part of the purchase and was not debt added at a later date.
- b. We acknowledge and agree that the City Property was indeed tentatively transferred into the personal names of Trustee-1 and Trustee-6. The deed was recorded on December 17, 20XX which under State Law is the actual date of the transfer as deeds are not recognized as official until they are properly recorded.



Form 886A	Department of the Treasury - Internal Revenue Service	Schedule No. or Exhibit
Explanation of Items		
Name of Taxpayer		Year/Period Ended
ORG		12/31/20XX

c. We disagree that Trustee-1 and Trustee-6 received any benefit from this transaction during the calendar year 20XX. In fact they incurred a liability as a result of the deed due to the fact that they were then required to make a mortgage payment on the property's mortgage.

They received no benefit of any kind on the payment of the mortgage as they did not deduct the interest paid, neither did they attempt to deduct the principal paid as a charitable contribution.

d. Our conclusion is that the mere recording of the deed prior to 1-1-20XX did not result in "inurement and/or private benefit" to Trustee-1 and Trustee-6 for the calendar year 20XX.

e We accept the fact that the law prohibits the following: "no part of the net earnings of which inures to the benefit of any private shareholder or individual."

The deed to the property was not recorded until December 17, 20XX and there was absolutely no earnings from this date thru December 31, 20XX, therefore there was literally "no amount of earnings" or economic benefit received by any individual during 20XX.

f. We accept your statement that the MLS Listing of said property for sale as being officially listed on January 28, 20XX. However we do not accept your position that the listing price is the market value of the property. Support of the actual sale was for net proceeds of \$0 per copy of the HUD closing statement dated 2-15-20XX attached hereto. It will prove the value of the property to and be only \$0. This is the sales price of \$0 less the cost they had to incur to dispose of the property.

g. It is our position that Treasury Regulation section 1.501(c)(3)-1 (d)(1)(ii) has been complied with. This position was supported with the numerous exhibits attached to our letter of January 6, 20XX. The Foundation was organized for the purposes permitted by law and was definitely 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.

It is our understanding that the U.S. Tax Court agreed with our position.

h. The requirements of section 501(c)(3) were met by the ORG:

1). As supported by the Exhibits attached to our letter of January 6, 20XX, it was organized for the charitable purposes so stated.

2). Numerous attempts were made during the calendar years 20XX thru the years 20XX to secure grants with which to fund the Foundation for which it was organized. These attempts were unsuccessful but the lack of success does not detract from the efforts to comply with the original purpose.

3). This lack of funding resulted in the necessity to liquidate the corporate debt and this could only be done by disposing of the only asset the Foundation owned, which was the City Property.

4). The net proceeds from the sale in the amount of \$0 was temporally held in the personal bank account of Trustee-1 and Trustee-6 however it was transferred to the Foundation from this same personal bank account during the same fiscal year. See EXHIBITS AA, BB, & CC.

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5). This action is permitted under Section 4941 (b)(1) which allows for a disqualified person to correct any disqualifying act within the same taxable period without penalty. The transfer back to the Foundation in the amount of \$0 within the same fiscal year of the sale, as reflected in Exhibits C & DD, which supports our position that the error was corrected in the same fiscal year as permitted under the law.

I. Section 1.501(c)(3)-1(c)(i) requires an exempt organization to operated exclusively for the exempt purpose for which it was organized. We contend that extensive time an effort and personal expenditures were incurred by the Trustees in their attempt to accomplish this purpose. Thru no fault of their own, the requested grants to fund the proposed educational institution did not materialize which forced the liquidation of the only asset owned by the foundation. This was done at a loss to the trustees who received no salary or other expense reimbursement for the large amount of time and funds spent for the benefit of the Foundation.

J. No individual received any net earnings from the activity of the Foundation in whole or in part therefore Section 1.501(c)(3)-1(c)(2) was followed as the Foundation's only operation was their attempt to exclusively accomplish this exempt purpose.

k. In response to your question about Section 4941(d)(1)(A). All proceeds from the net sale of the property in 20XX were properly held in the bank account of the Foundation as of the 12-31-20XX. No sale was made to a disqualified person as our position was that the made the sale for the benefit of the Foundation even though the sale was erroneously made in their name. They received no benefit from the proceeds and they were deposited into the Foundation's bank account as of the end of the fiscal year.

I. We fail to see the relative aspect of Reg 4941(d)-2(a)(2). The mortgage taken out by the Foundation to purchase the land is not applicable. The mortgage was incurred as part of the purchase price of the City Property and this property was purchased at an arms length from a non related third party.

#### **TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION**

9. This transaction was agreed to by the U. S. Tax Court in that they ruled that the property was never in reality transferred to the Foundation. This was a settled issue and should not be an item of this examination.

#### **RESPONSE TO TAXPAYERS PROTEST**

The following constitutes the Agent's rebuttal to The ORG's protest (numbered in same order as protest above):

#### **FIRST ISSUE ( TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION).**

- a. The referred to Tax Court Case is United States Tax Court V Trustee-1 Docket Number 1 and can be found at Index 10 of the Administrative file. The decision of the court was that additional individual Federal Income Tax was owed by the Foundation Founder(s) for 20XX, 20XX and 20XX based on an examination of their individual income tax form 1040. There was no examination conducted of the ORG's Form 990 and there was no decision entered as to the exempt status of the Foundation, at that time. The tax court case was the result of a Form 1040, Individual Income Tax, examination conducted by Small Business Self-Employed (SBSE). This division has no authority over the examination of Exempt Organizations. The conclusion of the Tax Court, and agreed to by all parties,

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was that the donation of the home to the Foundation did not meet the requirements of the law and as such, no contribution is allowable as it pertains to the home.

- b. This section of the protest is referring to the personal residence of the Foundations Founder(s) being sold in 20XX and statutes being barred for that sale. This examination is not questioning the proper tax treatment of the sale of the property. This examination is questioning whether or not the transfer of the personal residence to the Foundation on December 6, 20XX resulted in a prohibitive transaction, thus causing the revocation of the exempt status of the Foundation. The examination conclusion as stated above concludes that the prohibited transaction does cause the revocation of the Foundations exempt status and therefore is retroactive to that December 6, 20XX date.

When IRC 501(c)(3) exemption is revoked, the revocation is retroactive unless IRC 7805(b) relief is warranted. Such relief will not be warranted if the organization omitted or misstated a material fact in seeking exemption, or operated in a manner materially different from that originally represented. IRC 7805(b) relief is discussed in Rev. Proc. 90-4, 1990-2 I.R.B. 10, 20. Although a retroactively revoked organization is a taxable entity for the entire period for which the revocation is effective, the charitable deductions of contributors to the organization are protected until public announcement of the revocation is made. However, an exception may be made if a contributor knew of the actual or imminent revocation, or was responsible for or aware of the activities that resulted in the revocation. See Rev. Proc. 82-39, 1982-2 C.B. 759, 760.

- c. The protest refers to Tax Court Case United States Tax Court V Trustee-1 Docket Number 1 and can be found at Index 10 of the Administrative file and involves the Internal Revenue Service examination of Individual Income Tax Deductions, it does not encompass the examination of the ORG. The current examination is questioning whether or not the transfer of the personal residence to the Foundation on December 6, 20XX resulted in a prohibitive transaction, thus causing the revocation of the exempt status of the Foundation. The examination conclusion as stated above concludes that the prohibited transaction does cause the revocation of the Foundations exempt status and therefore is retroactive to that December 6, 20XX date.
- d. The Internal Revenue Service disagrees with the protests conclusion that the disallowance of the tax deduction for federal individual income tax purposes is governing in the determination of inurement or private benefit. This examination is questioning whether or not the transfer of the personal residence to the Foundation on December 6, 20XX resulted in a prohibitive transaction, thus causing the revocation of the exempt status of the Foundation. The examination conclusion as stated above concludes that the prohibited transaction does cause the revocation of the Foundations exempt status and therefore is retroactive to that December 6, 20XX date. The fact that Internal Revenue Service income tax examiners and the Tax Court found that the donation of the home to the Foundation did not meet the requirements of the law only supports the conclusion that the transaction was prohibitive.
- e. This examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees. Who the trustees are is not as important as the fact that both transactions involved disqualified persons and both transaction in and of themselves violate the prohibitions of Internal Revenue Code Section 501(c)(3) and 4941 resulting in the revocation of the exempt status of the ORG
- f. As stated in response to protest "e": above: This examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the

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Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees. Who the trustees are is not as important as the fact that both transactions involved disqualified persons and both transaction in and of themselves violate the prohibitions of Internal Revenue Code Section 501(c)(3) and 4941 resulting in the revocation of the exempt status of the ORG

**SECOND ISSUE( TRANSFER OF CITY LAND FROM THE FOUNDATION TO THE DISQUALIFIED PERSONS).**

- a. The Internal Revenue Service also agrees with this statement.
- b. The Internal Revenue Service also agrees with this statement
- c. The essence of the inurement proscription is found in the language of Internal Revenue Code Section 501(c)(3), which provides that no part of a 501(c)(3) organization's net earnings can inure to the benefit of any private shareholder or individual. Although this would clearly prohibit the distribution of dividends to those in control of the organization, the inurement prohibition is much broader than that in application.

The goal of the inurement prohibition is to prevent siphoning off of an exempt organization's assets by insiders – those in control of the organization. In this context, "control" may be direct (as in the case of formal directors) or indirect (such as control over others who are officers or directors). Any time assets of the organization flow through to benefit the organization's insiders, whether directly or indirectly, inurement is an issue.

The inurement restriction is absolute: An organization that violates this prohibition will not qualify (or will cease to qualify) for tax exemption regardless of whether it otherwise meets the appropriate statutory requirements for exemption.

The IRS contends that there were two violations of this inurement prohibition. The first violation was on or about December 6, 20XX, when the Foundations Founder(s)/Trustee(s) transferred their personal residence to the Foundation and the second violation was on or about December 12, 20XX when the ORG transferred 112.65 acres of land located in City, State to the Foundations Founder/Trustee(s)

- d. The essence of the inurement proscription is found in the language of Code § 501(c)(3), which provides that no part of a 501(c)(3) organization's net earnings can inure to the benefit of any private shareholder or individual. Although this would clearly prohibit the distribution of dividends to those in control of the organization, the inurement prohibition is much broader than that in application.

The goal of the inurement prohibition is to prevent siphoning off of an exempt organization's assets by insiders – those in control of the organization. In this context, "control" may be direct (as in the case of formal directors) or indirect (such as control over others who are officers or directors). Any time assets of the organization flow through to benefit the organization's insiders, whether directly or indirectly, inurement is an issue.

The inurement restriction is absolute: An organization that violates this prohibition will not qualify (or will cease to qualify) for tax exemption regardless of whether it otherwise meets the appropriate statutory requirements for exemption.

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Explanation of Items		
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ORG		12/31/20XX

The IRS contends that there were two violations of this prohibition. The first violation was on or about December 6, 20XX, when the Foundations Founder(s) transferred their personal residence to the Foundation and the second violation was on or about December 12, 20XX when the ORG transferred 112.65 acres of land located in City, State to the Foundations Founder

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f. The Internal Revenue Service issue herein is whether the two transactions discussed in this examination report result in inurement to the ORG Trustee(s) as disqualified persons and thus the disallowance of the Foundations exempt status. The determination of the sales price of the land or its fair market value is not material to that conclusion and is therefore not discussed here.

g. The referred to Tax Court Case is United States Tax Court V Trustee-1 Docket Number 1 and can be found at Index 10 of the Administrative file. The decision of the court was that additional individual Federal Income Tax was owed by the Foundation Founder(s) for 20XX, 20XX and 20XX based on an examination of their individual income tax form 1040. There was no examination conducted of the ORG's Form 990 and there was no decision entered as to the exempt status of the Foundation, at that time. The tax court case was the result of a Form 1040, Individual Income Tax, examination conducted by Small Business Self-Employed (SBSE). This division has no authority over the examination of Exempt Organizations. The conclusion of the Tax Court, and agreed to by all parties, was that the donation of the home to the Foundation did not meet the requirements of the law and as such, no contribution is allowable as it pertains to the home.

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the organization flow through to benefit the organization's insiders, whether directly or indirectly, inurement is an issue.

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The IRS contends that there were two violations of this prohibition. The first violation was on or about December 6, 20XX, when the Foundations Founder(s) transferred their personal residence to the Foundation and the second violation was on or about December 12, 20XX when the ORG transferred 112.65 acres of land located in City, State to the Foundations Founder.

- h.
- 1) This examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees. Both of these transaction in and of themselves violate the prohibitions of Internal Revenue Code Section 501(c)(3) and 4941 resulting in the revocation of the exempt status of the ORG
  - 2). This examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees. Both of these transaction in and of themselves violate the prohibitions of Internal Revenue Code Section 501(c)(3) and 4941 resulting in the revocation of the exempt status of the ORG
  - 3 ). This examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees. Both of these transaction in and of themselves violate the prohibitions of Internal Revenue Code Section 501(c)(3) and 4941 resulting in the revocation of the exempt status of the ORG
  - 4 ). Reference the response included under "5" below, both section "4" and "5" are responded together.
  - 5). The protest is responding to excise tax for self-dealing and as assessed upon the Foundation's Disqualified persons. However, this examination has addressed two events that call into question the exempt status of the ORG, the first event occurred on December 6, 20XX, when the Foundation Trustees transferred a personal residence to The Foundation and the second event occurred on December 12, 20XX when the Foundation transferred City Land to the Foundation Trustees.

The Internal Revenue Service concedes that the "second tier tax" under Internal Revenue Code section 4941(b)(1) does not apply to the Foundation Trustees (disqualified person(s)) due to the fact that the error was corrected in the taxable period.

The discussion of Internal Revenue Code Section 4941 has been reserved for another report



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Internal Revenue Code Section **4941**. Taxes on self-dealing.

(a) Initial taxes.

(1) On self-dealer. There is hereby imposed a tax on each act of self-dealing between a disqualified person and a private foundation. The rate of tax shall be equal to 10 percent of the amount involved with respect to the act of self-dealing for each year (or part thereof) in the taxable period. The tax imposed by this paragraph shall be paid by any disqualified person (other than a foundation manager acting only as such) who participates in the act of self-dealing. In the case of a government official (as defined in section **4946(c)** [IRC Sec. **4946(c)**]), a tax shall be imposed by this paragraph only if such disqualified person participates in the act of self-dealing knowing that it is such an act.

(b) Additional taxes.

(1) On self-dealer. In any case in which an initial tax is imposed by subsection (a)(1) on an act of self-dealing by a disqualified person with a private foundation and the act is not corrected within the taxable period, there is hereby imposed a tax equal to 200 percent of the amount involved. The tax imposed by this paragraph shall be paid by any disqualified person (other than a foundation manager acting only as such) who participated in the act of self-dealing.

I. The IRS has determined that, based upon the documentation presented by the Foundation, there has been no charitable activity conducted by the Foundation for the five years prior to December 31, 20XX. The IRS has further determined that the protest argument is an immaterial argument in that the requirements of Treasury Regulation section 1.501(c)(3)-1(d)(1)(ii), which provides that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest, since its inception. This examination has determined that the ORG benefited a private interest since its inception due to the transfer of the Trustee(s) private residence to the Foundation.

J. The IRS disagrees with this statement in that funds may not have been exchanged between the Foundation and the Founder(s)/Trustee(s). The essence of the inurement proscription is found in the language of Code § 501(c)(3), which provides that no part of a 501(c)(3) organization's net earnings can inure to the benefit of any private shareholder or individual. Although this would clearly prohibit the distribution of dividends to those in control of the organization, the inurement prohibition is much broader than that in application.

The goal of the inurement prohibition is to prevent siphoning off of an exempt organization's assets by insiders – those in control of the organization. In this context, "control" may be direct (as in the case of formal directors) or indirect (such as control over others who are officers or directors). Any time assets of the organization flow through to benefit the organization's insiders, whether directly or indirectly, inurement is an issue.

The inurement restriction is absolute: An organization that violates this prohibition will not qualify (or will cease to qualify) for tax exemption regardless of whether it otherwise meets the appropriate statutory requirements for exemption.

The IRS contends that there were two violations of this prohibition. The first violation was on or about December 6, 20XX, when the Foundations Founder(s) transferred their personal residence to the Foundation and the second violation was on or about December 12, 20XX when the ORG transferred 112.65 acres of land located in City, State to the Foundations Founder.

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k. The IRS agrees that the proceeds of the sale of the City Property were held in the Foundations bank account on December 31, 20XX. The IRS further accepts that this is evidence that this demonstrates that there was a correction of an error as defined in Code Section 4941(b)(1) which allows for a disqualified person to correct any disqualifying act within the same taxable period without penalty.

However, this is not an indication that there was not a violation of the prohibition of self-dealing when the personal residence of the Foundations Founder was transferred to the Foundation on December 6, 20XX.

Internal Revenue Code Section § 4941(d)(1)(A) provides that any sale or exchange of property between a disqualified person and a private foundation is self-dealing. As with most of the defined categories of self-dealing, sales or exchanges of property are flatly prohibited, rather than being judged by an arm's-length standard or eligible for a de-minimis exception

l. The relative aspect of Reg 4941(d)-2(a)(2). has to do with the transfer of the personal residence to the foundation in 20XX, thus causing the exempt status to be revoked at that date. Reg. § 4941(d)-2(a)(2) provides that the transfer of property by a disqualified person to a private foundation is treated as a sale or exchange if the private foundation assumes a mortgage, or takes subject to a mortgage that was placed on the property, within the 10-year period ending on the date of the transfer of the property to the private foundation.

The ORG accepted the personal residence of Trustee-1 on December 6, 20XX, this property was subject to a mortgage which was assumed by the Foundation thus causing Reg. § 4941(d)-2(a)(2) to be relevant, thus violating Internal Revenue Code Section § 4941(d)(1)(A) which provides that any sale or exchange of property between a disqualified person and a private foundation is self-dealing. Treasury Regulation section 1.501(c)(3)-1(c)(2) states, in part, that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.

#### **TRANSFER OF THE PERSONAL RESIDENCE TO THE FOUNDATION**

The referred to Tax Court Case is United States Tax Court V Trustee-1 Docket Number 1 and can be found at Index 10 of the Administrative file. The decision of the court was that additional individual Federal Income Tax was owed by the Foundation Founder(s) for 20XX, 20XX and 20XX based on an examination of their individual income tax form 1040. There was no examination conducted of the ORG's Form 990 and there was no decision entered as to the exempt status of the Foundation, at that time. The tax court case was the result of a Form 1040, Individual Income Tax, examination conducted by Small Business Self-Employed (SBSE). This division has no authority over the examination of Exempt Organizations. The conclusion of the Tax Court, and agreed to by all parties, was that the donation of the home to the Foundation did not meet the requirements of the law and as such, no contribution is allowable as it pertains to the home.

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the organization flow through to benefit the organization's insiders, whether directly or indirectly, inurement is an issue.

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The IRS contends that there were two violations of this prohibition. The first violation was on or about December 6, 20XX, when the Foundations Founder(s) transferred their personal residence to the Foundation and the second violation was on or about December 12, 20XX when the ORG transferred 112.65 acres of land located in City, State to the Foundations Founder.

The examination conclusion as stated above concludes that the prohibited transaction does cause the revocation of the Foundations exempt status and therefore is retroactive to that December 6, 20XX date. The fact that Internal Revenue Service income tax examiners and the Tax Court found that the donation of the home to the Foundation did not meet the requirements of the law only supports the conclusion that the transaction was prohibitive.

When IRC 501(c)(3) exemption is revoked, the revocation is retroactive unless IRC 7805(b) relief is warranted. Such relief will not be warranted if the organization omitted or misstated a material fact in seeking exemption, or operated in a manner materially different from that originally represented. IRC 7805(b) relief is discussed in Rev. Proc. 90-4, 1990-2 I.R.B. 10, 20. Although a retroactively revoked organization is a taxable entity for the entire period for which the revocation is effective, the charitable deductions of contributors to the organization are protected until public announcement of the revocation is made. However, an exception may be made if a contributor knew of the actual or imminent revocation, or was responsible for or aware of the activities that resulted in the revocation. See Rev. Proc. 82-39, 1982-2 C.B. 759, 760.

#### CONCLUSION

Based on the facts and circumstances, The ORG does not qualify for exemption under IRC 501(c)(3) and should be revoked effective April 10, 20XX because the trustees of The Foundation received a prohibited benefit know as inurement. This inurement occurred in violation of IRC 501(c)(3) and Treasury Regulations 1.501(c)(3)-1(d)(1)(ii). Further, based on the EO agent's analysis of the factors in Treas. Reg. § 1.501(c)(3)-1(f) revocation is appropriate.

Please file US Corporate income tax return Form 1120 for the tax periods ending December 31, 20XX, December 31, 20XX, and all periods subsequent to these dates

Contributions to The Organization are not deductible under IRC 170.