

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

NO PROTEST RECEIVED
Release copies to District
Date [REDACTED]
Surname [REDACTED]

Date: OCT 24 2000

Contact Person: [REDACTED]

ID Number: [REDACTED]

Contact Number: [REDACTED]

[REDACTED]

Employer Identification Number: [REDACTED]

Dear Applicant:

This is in reply to your application for recognition of exemption under section 501(c)(3) of the Internal Revenue Code.

We have considered the information you have submitted and have concluded you do not qualify for recognition of exemption under section 501(c)(3) of the Code because you are not operating exclusively for exempt purposes.

You are affiliated with the [REDACTED]. You were established to provide social services to the public in the local area which are beyond those services provided by [REDACTED]. These charitable services include care and activities for children and adults, education and support for parents, housing, and services to families or providing funding for such services. In your letter of [REDACTED] you indicate that you expect to make contributions to various charitable causes. However, you note that many of your giving programs are not yet operational and that as of the date of that letter, although you had received some income from the sale of housing units, you had not expended anything to accomplish these charitable purposes.

As a part of your activities and as a major source of your income you work with [REDACTED] a for-profit corporation (hereinafter referred to as [REDACTED]), to provide independent housing for individuals who are over 55. [REDACTED] has developed a housing complex for the elderly which includes several apartment units. These units will be transferred to you by the developer to be sold to the elderly for limited lifetime estates. You have represented that during the term of the life estates of the purchaser you are the legal owner of the units. At the end of the lifetime estate the properties will be repurchased by the developer for subsequent transfer and resale of a new limited lifetime estate to another qualified purchaser. For your role in this transaction you will retain \$[REDACTED] from the sales prices. You also are entitled upon the reconveyance of a lifetime estate to a subsequent occupant to .5% of the gross purchase price paid by the new occupant. The remainder of sales price goes to [REDACTED] for the cost of the unit and for an anticipated profit. The repurchase price as set in the Purchase Agreement is 90 percent of the initial purchase price and does not include the value of any optional items or extras which were purchased at the time the interest was acquired. Any outstanding debts, such as waived service fees, will be deducted by [REDACTED] from the amount needed to repurchase the unit.

[REDACTED]

You have submitted copies of several agreements you expect to enter into with [REDACTED] and the individual purchaser of the unit. As noted above the Provider Agreement states that [REDACTED] is the owner of the property. This agreement also indicates that if you terminate this arrangement you are required to convey all of your right, title and interest in and to this agreement to either the residents, [REDACTED] or another third party as directed by [REDACTED]. In addition, the Provider Agreement establishes that the housing unit shall revert to [REDACTED] upon termination of the Limited Life Estate. The Purchase Agreement gives [REDACTED] the right to repurchase the unit at the end of the limited life estate. The Grant of Limited Life Estate provides that that agreement is subject to and limited by the other agreements between you and [REDACTED].

The apartment units and the entire complex, has been specially designed and constructed with the needs of the elderly in mind. Services will be provided to the residents by [REDACTED] for a set monthly fee which varies as to the services provided. You have represented that the housing has been priced at the fair market value of a lifetime estate and that the service fees have been set at fair market value. You have also represented that the costs involved are within the financial reach of a significant segment of the elderly in the local community. You have proposed to amend your purchase agreements to ensure that you will retain residents in their housing units even if they become unable to pay the monthly service fee. However, the outstanding debts will be deducted from the repurchase price that [REDACTED] will pay for the unit.

You are affiliated with [REDACTED]. All of your directors serve at the pleasure of [REDACTED]. At least one of your directors is required to be a representative of any organization that provides social services or community services to members of the public who reside in or the area. Another is required to have an involvement in the local school district. You have represented that you are not related to the individuals who control [REDACTED].

Section 501(c)(3) of the Code describes organizations organized and operated exclusively for religious, charitable and educational purposes, no part of the net earnings of which inures to the benefit of any private shareholder or individual.

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 purposes specified in that section. If an organization does not meet either the organizational or the operational test, it is not exempt.

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) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(i) of the regulations provides that an organization is not organized or operated exclusively for one or more of the purposes specified in section 501(c)(3) unless it serves a public rather than a private interest. Thus, to meet these requirements, 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.

Section 1.501(c)(3)-1(d)(2) of the regulations provides that the term "charitable" is used in section 501(c)(3) in its generally accepted legal sense. It includes relief of the poor and distressed, the advancement of religion, the advancement of education and lessening the burdens of government.

[REDACTED]

In certain instances providing housing to the elderly is considered a charitable purpose.

In Better Business Bureau of Washington, D.C., Inc. v. United States, 326 U.S. 279 (1945), Ct.D. 1650, C.B. 1945, 375, the Supreme Court of the United States held that the presence of a nonexempt purpose, if more than insubstantial, would destroy tax exempt status as a charitable organization.

In United States v. Wells Fargo Bank, 485 U.S. 351, 108 S. Ct. 1179, 99 L.Ed. 2d 368 (1988), the Supreme Court held that an organization must prove unambiguously that it qualifies for a tax exemption.

Harding Hospital, Inc. v. United States, 505 F.2d 1068 (1974), holds that an organization seeking a ruling as to recognition of its tax exempt status has the burden of proving that it satisfies the requirements of the particular exemption statute. Whether an organization has satisfied the operational test is a question of fact.

In Old Dominion Box Co. v. United States, 477 F.2d 344 (4th Cir. 1973) cert. Denied 413 U.S. 910 (1973), the court held that operating for the benefit of private parties constitutes a substantial non-exempt purpose.

In Stevens Bros. Foundation, Inc. v. Commissioner, 324 F.2d 633 (10th Cir. 1963), affirming 39 T.C. 93 (1962), an organization's exemption was revoked for failure to operate exclusively for charitable purposes where it entered into a partnership with and advanced funds to a for-profit entity owned and controlled by the organization's directors. The for-profit entity needed the funds to obtain construction contracts, which ultimately proved profitable. The court reasoned that the organization engaged in the transactions substantially for the purpose of benefiting its founders.

In P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), a nonprofit organization's regularly scheduled bingo games were held on the premises of a for-profit business which sold food and beverages, the games were conducted by the owners of the for-profit, and the directors of the for-profit controlled the nonprofit's board. Under these circumstances, the court held that the nonprofit had a substantial non-exempt purpose to enhance the profits of the for-profit.

In Housing Pioneers, Inc. v. Commissioner, T.C.M. 1993-120, aff'd 58 F.3d 401 (9th Cir. 1995) the court held that an organization's participation as a general partner in a limited partnership precludes exemption where the investors privately benefit from the arrangement. The court noted that the activities performed as co-general partner in for-profit limited partnerships substantially furthered non-exempt purposes and private interests were served by its activities.

Rev. Rul. 79-18, 1979-1 C.B. 194 holds 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 operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Code.

Whether an organization has satisfied the operational test is a question of fact. See Harding Hospital, Inc. v. United States, *supra*. In addition, the existence of more than an substantial nonexempt purpose will preclude exemption. See Better Business Bureau of Washington, D.C., Inc. v. United States, *supra*. As emphasized by the Supreme Court in United States v. Wells Fargo Bank, *supra*, qualification must be proven unambiguously.

The information you have submitted establishes that you envision carrying on a program of charitable giving. However, it is also clear that your charitable giving endeavors are only a portion of your activities. The submitted information establishes that the major source of your funding and a substantial activity involves your participation in the housing program operated by [REDACTED]. Under this program a

[REDACTED]

qualified purchaser buys a limited life estate in the property developed by [REDACTED] and the funds, minus your share, are then transferred to [REDACTED] a for-profit corporation. At the termination of the life estate in the unit it will be repurchased by [REDACTED] for 90 percent of the original purchase price less any outstanding service fees. In addition, to being the developer of the project, [REDACTED] also provides services to the residents for set fees. You indicate that your role in this endeavor is to hold title to the property after the limited life estate has been sold to a qualifying individual and, at least once, characterize [REDACTED]'s role as that of your agent.

Providing housing for the elderly may be a section 501(c)(3) charitable activity. The information you have submitted establishes that your role in this endeavor falls short of directly providing housing for the elderly. However, for the purposes of this letter we will presume that the housing provided by Parkside would satisfy the requirements of the various revenue rulings describing qualifying section 501(c)(3) facilities for the elderly and that your supporting role is a qualifying charitable activity. Still, even if we presume that your activities are directed to accomplish this charitable purpose, the submitted information indicates that you have a substantial nonexempt purpose to benefit [REDACTED]. See Old Dominion Box Co. v. United States, *supra*, which holds that operating for the private benefit of individuals is a substantial nonexempt purpose.

[REDACTED] is a for-profit company. Although there is no information establishing that it controls your board of directors, the various agreements you have submitted establish that it has absolute control over this project and runs it for its own economic benefit. We recognize that there are various clauses in the agreements indicating your ownership rights and that you characterize [REDACTED] as your agent. However, as noted above the agreements clearly establish [REDACTED]'s dominate role in the operations of this program. It is also clear that, except for the small payments you receive, almost all of the profits flow to [REDACTED]. Even on repurchase, it only has to pay 90 percent of the original purchase price and it can then resell the property for fair market value. Furthermore, any amenities a property holder might have added to the property, such as upgrades at the initial time of purchase, are transferred to [REDACTED] without cost. These facts establish that this entire program is being operated for the financial benefit of [REDACTED]. The Courts have often denied exemption where a small group of individuals control a nonprofit organization and use it to steer business towards their own for-profit enterprise. See for example Stevens Bros. Foundation, Inc. v. Commissioner, *supra*, where an exempt organization invested in a for profit owned by its directors and P.L.L. Scholarship Fund v. Commissioner, *supra* where a nonprofit organization's regularly scheduled bingo games were held on the premises of a for-profit business, which was established and controlled by the for profit's board. Therefore, we have concluded that this arrangement is similar to the situation in Housing Pioneers v. Commissioner, *supra*, where exemption was denied because the organization's activities benefited the private business interests of its investors.

Accordingly, we have concluded that you have not established that you qualify for recognition of exemption under section 501(c)(3) of the Code. Contributions to you are not deductible under section 170 and you are required to file Federal income tax returns.

In this proposed adverse determination we have not made an determination as to whether you would qualify as a supporting organization described in section 509(a)(3) of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views, with a full explanation of your reasoning. This statement, signed by one of your principal officers, must be submitted within 30 days from the date of this letter. You also have the right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your principal officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practice Procedures.

[REDACTED]

If you do not protest this proposed ruling in a timely manner, it will be considered by the Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgement or decree under this section shall not be issued in any proceeding unless the United States Tax Court, the U.S. Court of Federal Claims, 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.

Sincerely yours,

Joseph Chasin

Joseph Chasin
Acting Manager,
Exempt Organizations
Technical Group 2

cc: [REDACTED]

qa [REDACTED]

act [REDACTED]

[REDACTED]