



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **200623071**
Release Date: 6/9/2006

Date: March 15, 2006

SE:T:EO:RA:T:2

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear Applicant:

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

Information letter

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



tion letter

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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: January 19, 2006

Contact Person:

Uniform Issue List: 501.00-00

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

- M =
- N =
- R =
- A =
- B =
- C =
- State =
- Date =

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below. This letter supersedes our letter of July 30, 2001.

FACTS

You, M are a State non-profit corporation, formed on Date. Your Articles of Incorporation state that your specific purpose is "to act and operate as a charitable organization in lessening the burdens of government, to provide down payment assistance to individuals, couples,

families and groups in obtaining financing to purchase real property."

Subsequently, you amended and restated your Articles to state your purposes as "to act and operate exclusively for charitable purposes within the meaning of section 501(c)(3) of the Internal Revenue Code, including, but not limited to, the relief of poverty, lessening the burdens of government, community beautification and maintenance, providing donations and assistance in marketing, program management and fund raising for other 501(c)93) organizations."

Your application Form 1023 and subsequent correspondence indicates that your primary activity will be operating a downpayment assistance program in conjunction with N for persons, regardless of income level to purchase real property anywhere in the United States.

You state that your primary source of financial support for your downpayment assistance program is N. You state that you specifically established N, a related organization that has applied for tax exemption under section 501(c)(3) of the Code, to be the primary provider of downpayment funds. This is reiterated in your letters of August 29, 2001 and October 10, 2003.

You further state that you will utilize a marketing company, R to administer your downpayment assistance program. In your letter of August 29, 2001, you describe R, as a for-profit entity that provides various services to M and N. You state that R "acts as a central clearinghouse for overhead expenses of both" M and N "as well as providing management, administration and marketing services for both." In your letter of June 28, 2002, you state that R was established as a method of paying the management costs of operating M and N.

In your letter of March 20, 2001, you describe the basic operations of your program as follows: R solicits and markets the down payment assistance program on behalf of yourself and N. You provide downpayment funds to a particular homebuyer. At the conclusion of the transaction, the home seller whose property was purchased by the particular homebuyer makes a donation to N. N in turn, makes a contribution to your pool of funds. You then provide downpayment assistance to additional buyers using these funds from N. You state that R may refer a buyer to another organization for downpayment assistance; however the information you provided indicates that this actually does not occur.

The information packet describing your program indicates that to qualify, applicants do not need to be first-time home buyers and there are no income limitations. In your letter of August 29, 2001, you state that you "specifically target[s] to provide assistance to low to moderate income families as defined by HUD." In your letter of March 20, 2001, you state that the program will be available on a nationwide basis. In addition, you state that in order for a buyer to receive funds from you, a buyer must obtain pre-approval from a participating

lender; that is, you rely on the lender to determine which buyers need assistance. You state that such pre-approval will assist the buyer in determining the purchase amount for which the buyer qualifies. In addition, the sales price of the home must be appraised to meet the lender's terms and the seller must agree to the terms of the Seller Participation Letter.

The information packet also indicates that a buyer must purchase a participating property from a participating home seller. In your letter of March 21, 2001, you describe a participating property as a home being sold by a seller who has entered into agreement with you, located in any community in the United States. In addition, you describe the home as "usually, they (the homes) are in the lower-income areas."

You state that your program provides home sellers with a greater pool of qualified buyers and "helps the seller get the highest value for the home and may be instrumental in a quicker sale of the home." Sellers enter into an agreement with you and N to provide a donation to a "pre-determined charity" designated by R upon sale of the seller's property. The seller agrees to donate a percentage of the purchase price, which is withheld from the seller's proceeds and delivered to the designated charity the business day following the closing of the transaction. For example, if the gift provided to the homebuyer by you is five percent or less of the selling price, then the seller makes a contribution to N in an amount equal to the gift provided by you plus an additional amount as a service fee.

You further state that the seller is not obligated to give a donation if the closing/escrow is terminated. The donation is a fixed percentage of the purchase price of the property is not negotiable. Copies of your seller participation letter indicates that the "pre-determined charity" is N. The seller participation letter indicates that the seller's fee and corresponding contribution is only refundable if the buyer does not close on the property. In addition, the fee and contribution is only made if the seller has signed the agreement and the buyer receives funds from M.

In your letters of June 28, 2002 and October 10, 2003, you describe a typical transaction in your downpayment assistance program as follows:

1. A real estate agent writes a contract for the buyer with an addendum stating "[t]he contract is contingent upon the buyer receiving gift funds from a non-profit charitable organization."
2. The seller agrees to the terms and conditions of the seller participation letter and the terms and conditions are incorporated into the Real Estate Purchase Contract.

3. The buyer then applies for a loan with a mortgage company.
4. The loan officer sends M and N a gift funds request form.
5. Upon receiving the gift funds request form, M and N send a gift letter to the loan officer stating that they will provide gift funds to the buyer for the downpayment.
6. At the close of escrow or the day before, the title company will send M and N a copy of the settlement statement stating the amount of gift funds needed for the buyer from M and the amount of funds that are to be sent to N after the close of escrow.
7. M and N will verify that the gift funds are noted on the settlement statement and agree to the amount reflected on the gift letter.
8. Upon verification, the gift funds are wired from M to the title company's trust account.
9. After the title company receives the gift funds and the funds from the lender, the transaction is closed and recorded. At that time, the title company wires funds from the seller's proceeds to N.

In your letter of October 10, 2003, you state that neither you M, N or R has actual contact with either the buyer or the seller.

In your letter of October 10, 2003, you state that you do not have any paid staff members and that R provides the staff needed to operate your program. The staff members are A, B and C. Your Board of Director meeting minutes of June 22, 2001 indicates that you drafted an agreement between yourself, N and R regarding services to be provided. In your meeting minutes of August 9, 2001, you indicate that the service agreement between N and R was approved by board members and signed. However, you never provided us with a copy of this agreement as requested in our letter of July 7, 2003.

In your letter of March 20, 2001, you state that A, B, and C are all officers or trustees of M and N. A and B are husband and wife and C is their child. A is employed as a loan officer. B is a licensed real estate agent. C is also a licensed real estate agent and has worked as a loan officer. You also state that A, B, and C are all owners and employees of R. You state that you determined that you should use two nonprofit corporations: one to provide the downpayment gifts to homebuyers and the other to receive donations. In your letter of August 29, 2001, you stated that you expanded your Board of Directors to seven so that A, B, and C would be the minority board members. However, the day-to-day operations are run by A, B, and C as employees of R.

In your letter of January 18, 2002, you state that you have initiated a homebuyer education program. You further described your

education program in your letter of June 28, 2002. You state that you offer a homebuyer education program in conjunction with N. You state that the course covers a variety of topics ranging from the home buying process, grant programs to money management. You state that the programs are open to the general public and you are creating study materials. In your letter of October 10, 2003, you state that the course materials used in your homebuyer education program as those published by FHA. You did not provide any other information as to how you operate your homeownership program.

In addition, you state that the only services you provide to a buyer are the down payment funds. You state that you do not have any other programs or activities to ensure that the buyer is purchasing safe, decent, sanitary and affordable housing.

In your letter of March 20, 2002, you restated your purposes and activities to include the acquisition and rehabilitation of homes for rental, lease or sale as affordable housing. You state that you will make the renovated homes available to affordable housing families as defined by HUD. You further state that preference will be given to low-income, military, public safety and education related families. However, in your letter of June 28, 2002, you state that you may elect to contribute funds to other exempt organizations that conduct such activities. You did not provide any other information regarding this activity.

In your restated purposes and activities, you also indicate that you will be offering special needs housing for the elderly, handicapped and others. In your letter of June 28, 2002, you defined such persons as those with a "physical or mental disability which has a substantial and long-term adverse effect on an individual's ability to carry out normal day-to-day activities." You further state that M and N will use the Social Security Administration's definition of disability for these purposes. However, you did not provide any information regarding this activity.

The financial data that you submitted including your Form 990 indicates that you received approximately _____ in gross receipts from services during your first three years of operation. You made "gifts" of approximately _____ during that same period of time. In your letter of October 10, 2003, you indicate that seller contributions to N have been your only source of financial support.

You have represented that your program operates in a manner to lessen the burdens of government by providing housing opportunities.

In your letter of January 18, 2002, you represent that your program is part of the American Dream Downpayment Initiative operated through HUD's HOME program.

In your letter dated August 29, 2001, you represent that you operate in a manner similar to several specified organizations. The manner in which you and these organizations operate is referred to as "seller-funded downpayment assistance" in the Final Report, *An Examination of Downpayment Gift Programs Administered by Non-Profit Organizations*, commissioned by Office of Housing, United States Department of Housing and Urban Development, HUD Contract No: C-OPC-22550/M0001 (March 1, 2005). The report concludes that seller-funded downpayment assistance for mortgage downpayments has led to underwriting problems that require immediate attention. Furthermore, the report concludes that the effective costs of homeownership are increased even more by the processing fees charged by the seller-funded downpayment assistance providers which get passed through to borrowers in higher property prices. A copy of the report is enclosed with this determination letter.

LAW

Section 501(c)(3) of the Code provides for the exemption from federal income tax of corporations organized and operated exclusively for charitable or educational purposes, provided no part of the net earnings inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations provides that an organization operates exclusively for exempt purposes only if it engages primarily in activities that accomplish exempt purposes specified in section 501(c)(3) of the Code. An organization must not engage in substantial activities that fail to further an exempt purpose.

Section 1.501(c)(3)-1(c)(2) of the regulations provides 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.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for exempt purposes unless it serves a public rather than a private interest. To meet this requirement it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests.

Section 1.501(c)(3)-1(d)(2) of the regulations defines the term "charitable" as used in section 501(c)(3) of the Code as including the relief of the poor and distressed or of the underprivileged. The term "charitable" also includes the advancement of education.

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

Section 1.501(c)(3)-1(e) of the regulations provides that an organization that operates a trade or business as a substantial part of its activities may meet the requirements of section 501(c)(3) of the Code if the trade or business furthers an exempt purpose, and provided the organization's primary purpose does not consist of carrying on an unrelated trade or business.

In Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279, 283 (1945), the Supreme Court held that the "presence of a single . . . [nonexempt] purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly . . . [exempt] purposes."

In Easter House v. U.S., 12 Cl. Ct. 476, 486 (1987), aff'd, 846 F. 2d 78 (Fed. Cir.) cert. denied, 488 U.S. 907 (1988), the court found an organization that operated an adoption agency was not exempt under section 501(c)(3) of the Code because a substantial purpose of the agency was a nonexempt commercial purpose. The court concluded that the organization did not qualify for exemption under section 501(c)(3) because its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court rejected the organization's argument that the adoption services merely complemented the health related services to unwed mothers and their children. Rather, the court found that the health-related services were merely incident to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff's adoption service is its primary goal" and held that the organization was not operated exclusively for purposes described in section 501(c)(3). Easter House, 12 Cl. Ct. at 485-486.

In American Campaign Academy v. Commissioner, 92 T.C. 1053 (1989), the court held that an organization that operated a school to train individuals for careers as political campaign professionals, but that could not establish that it operated on a nonpartisan basis, did not exclusively serve purposes described in section 501(c)(3) of the Code because it also served private interests more than incidentally. The court found that the organization was created and funded by persons affiliated with Republican Party entities and that most of the organization's graduates worked in campaigns for Republican candidates. Consequently, the court concluded that the organization conducted its educational activities with the objective of benefiting Republican candidates and entities. Although the candidates and entities benefited were not organization "insiders," the court stated that the conferral of benefits on disinterested persons who are not members of a charitable class may cause an organization to serve a private interest within the meaning of section 1.501(c)(3)-1(d)(1)(ii) of the regulations. The court concluded by stating that even if the Republican candidates and entities did "comprise a charitable class, [the organization] would bear the burden of proving that its activities benefited members of the class in a non-select manner."

In Aid to Artisans, Inc. v. Commissioner, 71 T.C. 202 (1978), the court held an organization

that marketed handicrafts made by disadvantaged artisans through museums and other non-profit organizations and shops be operated for exclusively charitable purposes within the meaning of section 501(c)(3) of the Code. The organization, in cooperation with national craft agencies, selected the handicrafts it would market from craft cooperatives in communities identified as disadvantaged based on objective evidence the Bureau of Indian Affairs or other government agencies. The organization marketed only handicrafts it purchased in bulk from these communities of craftsmen. It did not select individual craftsmen based on the needs of the purchasers. The court concluded that the overall purpose of the activity was to benefit disadvantaged communities. The method it used to achieve its purpose did not cause it to serve primarily private interests because the disadvantaged artisans directly benefited by the activity constituted a charitable class and the organization showed no selectivity with regard to benefiting specific artisans. Therefore, the court held that the organization operated exclusively for exempt purposes.

In *Airlie Foundation v. Commissioner*, 283 F. Supp. 2d 58 (D.D.C., 2003), the court relied on the “commerciality” doctrine in applying the operational test. Because of the commercial manner in which this organization conducted its activities, the court found that it was operated for a non-exempt commercial purpose, rather than for a tax-exempt purpose. “Among the major factors courts have considered in assessing commerciality are competition with for profit commercial entities; extent and degree of below cost services provided; pricing policies; and reasonableness of financial reserves. Additional factors include, *inter alia*, whether the organization uses commercial promotional methods (e.g. advertising) and the extent to which the organization receives charitable donations.”

Rev. Rul. 67-138, 1967-1 C.B. 129, holds that helping low income persons obtain adequate and affordable housing is “charitable” because it relieves the poor and distressed or underprivileged. The organization carried on several activities directed to assisting low-income families obtain improved housing, including (1) coordinating and supervising joint construction projects, (2) purchasing building sites for resale at cost, and (3) lending aid in obtaining home construction loans.

Rev. Rul. 70-585, 1970-2 C.B. 115, discusses four examples of organizations providing housing and whether each qualified as charitable within the meaning of section 501(c)(3) of the Code. Situation 1 describes an organization formed to construct new homes and renovate existing homes for sale to low-income families who could not obtain financing through conventional channels. The organization also provides financial aid to eligible families who do not have the necessary down payment. When possible, the organization recovered the cost of the homes through very small periodic payments, but its operating funds were obtained from federal loans and contributions from the general public. The revenue ruling holds that by providing homes for low-income families who otherwise could not afford them, the organization relieved the poor and distressed.

Situation 2 describes an organization formed to ameliorate the housing needs of minority groups by building housing units for sale to persons of low and moderate income on an open-occupancy basis. The housing is made available to members of minority groups who are unable to obtain adequate housing because of local discrimination. The housing units are located to help reduce racial and ethnic imbalances in the community. As the activities were designed to eliminate prejudice and discrimination and to lessen neighborhood tensions, the revenue ruling holds that the organization was engaged in charitable activities within the

meaning of section 501(c)(3) of the Code.

Situation 3 describes an organization formed to formulate plans for the renewal and rehabilitation of a particular area in a city as a residential community. The median income level in the area was lower than in other sections of the city and the housing in the area was generally old and badly deteriorated. The organization developed an overall plan for the rehabilitation of the area; it sponsored a renewal project; and involved residents in the area renewal plan. The organization also purchased apartment buildings that it rehabilitated and rented at cost to low and moderate income families with a preference given to residents of the area. The revenue ruling holds that the organization is described in section 501(c)(3) of the Code because its purposes and activities combated community deterioration.

Situation 4 describes an organization formed to alleviate a shortage of housing for moderate-income families in a particular community. The organization planned to build housing to be rented at cost to moderate-income families. The Service held that the organization failed to qualify for exemption under section 501(c)(3) of the Code because the organization's program did not provide relief to the poor or further any other charitable purpose within the meaning of section 501(c)(3) and the regulations.

Rev. Rul. 72-147, 1972-1 C.B. 147, holds that an organization that provided housing to low income families did not qualify for exemption under section 501(c)(3) of the Code because it gave preference to employees of a business operated by the individual who also controlled the organization. Although providing housing for low income families furthers charitable purposes, doing so in a manner that gives preference to employees of the founder's business primarily serves the private interest of the founder rather than a public interest.

Rev. Rul. 85-1, 1985-1 C.B. 177, sets out a two-part test for determining whether an organization's activities lessen the burdens of government. The ruling holds that an activity is a burden of government only if there is objective manifestation by a governmental unit that it considers such activities to be its burden. The ruling also holds that little weight should be given to statements of government officials that merely praise or express approval of an organization and its activities. Rather, the government must formally recognize the organization and its functions to be considered a governmental burden. The ruling sets out relevant factors in determining whether the government unit has made the necessary objective manifestation include:

- a. A statute specifically creates the organization and clearly defines the organization's structure and purposes.
- b. The activity is an integral part of a larger governmental program, or is acted jointly with a governmental unit.
- c. The governmental unit controls the activities of the organization, such as appointing all the board members.
- d. The organization pays governmental expenses.
- e. Regular government funding of the organization's activities through grants or general obligation bonds backed with the full faith and credit of the governmental unit (as opposed to general revenue bond financing).
- f. The governmental unit is not prohibited from performing the particular activity.

Rev. Rul. 85-2, 1985-2 C.B. 178 holds that an organization is lessening the burdens of government if it engages in activities that a governmental unit considers to be its burden and such activities actually lessen such governmental burden. An organization must demonstrate through all the relevant facts and circumstances that a government unit considers the organization to be acting on its behalf, thereby freeing up the government assets that would otherwise have been devoted to the particular activity.

RATIONALE AND CONCLUSION

Based on the information you provided in your application and supporting documentation, we conclude that you are not operated for exempt purposes under section 501(c)(3) of the Code. An organization cannot be recognized as exempt under section 501(c)(3) unless it shows that it is both organized and operated exclusively for charitable, education, or other exempt purposes. Among other things, the application and supporting documentation must demonstrate conclusively that the organization meets the operational test of section 1.501(c)(3)-1(c) of the regulations. Your information indicates that your primary purpose is to operate a down payment assistance program that does not exclusively serve a purpose described in section 501(c)(3).

Charitable purposes include relief of the poor and distressed. See section 1.501(c)(3)-1(d)(2) of the regulations. However, you do not conduct your down payment assistance program in a manner that establishes that your primary purpose is to address the needs of low-income grantees by enabling low-income individuals and families to obtain decent, safe housing. See Rev. Rul. 70-585, Situation 1.

Your down payment assistance program does not serve exclusively low-income persons. Instead, your program is open to anyone without any income limitations. You have not demonstrated that your down payment assistance program exclusively serves any other exempt purpose such as combating community deterioration and lessening racial tensions. You indicated that you do not specifically target the benefits of your program towards any one disadvantaged group. For example, you have not shown that your program is designed to attract a mixed-income group of homeowners to a specifically defined geographical area that has a history of racial problems. See Rev. Rul. 70-585, Situations 2 and 3

Your information indicates that you do not limit your assistance to certain geographic areas or target those areas experiencing deterioration or racial tensions. See Rev. Rul. 70-585, Situation 4. Your program is available to anyone who is able to qualify for a mortgage from any lender in any State in the United States. Arranging the purchase of homes in a broadly defined metropolitan area does not combat community deterioration within the meaning of section 501(c)(3) of the Code.

Furthermore, you do not engage in any activity to ensure that the house will be habitable or that the buyer will be able to afford to maintain the house over time. Instead, you rely solely on the mortgage lender, insurance agency, home inspector or other third party to conduct such review. While you indicate that you require completion of an education program, you do not provide oversight or conduct any educational program or other activity to ensure that buyers are purchasing properties that are safe, decent, sanitary, and affordable.

Only an insubstantial portion of the activity of an exempt organization may further a nonexempt purpose. As the Supreme Court held in Better Business Bureau of Washington D.C., Inc. v. United States, *supra*, the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. You conduct your operations in a manner that is consistent with a commercial firm seeking to maximize sales of services, rather than in a manner that would be consistent with a charitable or educational organization seeking to serve a charitable class or the public at large. The manner in which you operate your down payment assistance program indicates that you facilitate the sales of homes in a manner that is indistinguishable from an ordinary trade or business. You operate as a business that provides services to home sellers for which you charge a market rate fee. For example, your sample transaction explains how the seller and agent will benefit from your program as sellers are able to sell their homes at the full list price. This type of approach, as well as your representation that the gift amount was determined to maximize the number of potential homeowners, helps to demonstrate that your primary purpose consists of maximizing the fees you derive from facilitating sales of real property. In this respect you are similar to an organization which was denied exemption because it operated a conference center for a commercial purpose. See Airlie Foundation, Inc. v. U.S., 283 F. Supp. 2d 58 (D.D.C., 2003). Likewise, operating a trade or business of facilitating home sales is not an inherently charitable activity. Thus, a substantial part of your activities further a nonexempt purpose.

Another indication of your substantial nonexempt purpose is your lack of public support. You are not supported by contributions from the general public, government or private foundation grants. Almost all of your revenue comes from the sellers you serve through N and R, two related organizations. That your primary activity is to promote and to further your private business interests is reflected in the financing structure of your down payment assistance program. In this respect you are similar to the organization described in Easter House, *supra*, which derived most of its support from fees it charged for its adoption services. In this case, the court stated that the substantial fees were not incidental to the organization's exempt purpose because they were designed to make a profit. Facilitating home sales, like running an adoption service, is not an inherently charitable activity, and receiving support primarily from fees charged to home sellers is indicative of your commercial purpose.

Even if your program is directed to exclusively low-income individuals, your reliance entirely on home sellers or other real-estate related businesses that stand to benefit from the transactions to finance your down payment assistance activities demonstrates that you are operated for the purpose of benefiting private parties.

Your grant making procedures indicate that gift funds are only provided if a seller has paid a processing fee or has made a contribution to N. In fact while you call the funds you will receive from the sellers "contributions", these transactions are not contributions because they will not "proceed from detached and disinterested generosity." Commissioner v. Duberstein, 363 U.S. 278, 285 (1960). Your characterization of these transactions as contributions ignores the business realities surrounding the payments. The sellers will make the payments to N and indirectly to the homebuyer through a "contribution" to you to facilitate the sale of their homes. Upon the closing of the sale, the sellers' "contribution" is returned to seller as part of the proceeds the seller receives from the sale of the home. This demonstrates the circular character of the payments.

These "contributions" are more appropriately characterized as fees received in exchange for the sale of a service. Your information indicates that your staff is able to take into account whether there is a home seller willing to make a payment to cover the down payment assistance an applicant has requested. That you receive a payment from the home seller corresponding to the amount of the down payment assistance in virtually every transaction indicates that the benefit to the home seller is not a mere accident but rather an intended outcome of your operations. In this respect, you are like Easter House, *supra*, which provided health care to indigent pregnant women, but only when a family willing to adopt a woman's child sponsored the care financially. Similar to American Campaign Academy, *supra*, you are structured and operated to directly benefit the home sellers who pay for your services. Therefore, a substantial part of your activities serve a private rather than a public interest.

You state that your program makes home ownership available to persons in accordance with HUD initiatives. Rev. Rul. 85-1, *supra*, holds that an activity is a burden of government only if there is objective manifestation by a governmental unit that it considers such activities to be its burden and the government must formally recognize the organization and its functions to be considered a governmental burden. However, you have not provided any facts, documentation or otherwise that indicates that providing down payment assistance is a burden of the government or that the government formally recognizes such activity as an integral part of a larger governmental program.

Even if an organization's activities lessen the burdens of government, it must otherwise satisfy the requirements under section 501(c)(3) of the Code. Thus, an organization must demonstrate that its activities serve a public rather than a private interest within the meaning of section 1.501(c)(3)-1(d)(1) of the regulations.

Finally, you assert that other organizations similarly situated have been recognized as exempt under section 501(c)(3). While you may have provided some facts relating to those other organizations, you have not provided all the facts relating to the applications for recognition of exempt status submitted by those organizations. In any event, you must establish based on the facts you submitted that you are organized and operated exclusively for exempt purposes described in section 501(c)(3). See Interneighborhood Housing Corporation v. Commissioner, T.C. Memo 1982-661.

Based on the facts and information submitted, you are not operated exclusively for exempt purposes. You have not established that you activities exclusively serve a charitable class or any other purpose defined in section 501(c)(3). Your proposed operations further a substantial nonexempt business purpose and will further the private interests of home sellers and other private parties. In addition, you have not established that your net earnings will not inure to the benefit of private shareholders or individuals. Therefore, you are not described in section 501(c)(3) of the Code.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

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

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit

the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
TE/GE (SE :T :EO :RA :T :)
1111 Constitution Ave, N.W.
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations
Rulings & Agreements

Enclosure

An Examination of Downpayment Gift Programs Administered by Non-Profit Organizations
HUD Contract No: C-OPC-22550/M0001 (March 1, 2005)