



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **200540013**
Release Date: 10/7/05

Date: 07/14/05

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

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State=
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Dear :

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 previous letter dated July 22, 2002.

FACTS

You, M are a State non-profit corporation, formed on Date. Your Articles of Incorporation state that your specific purpose is “[t]o provide down payment assistance to low and moderate income home buyers and exclusively within the meaning of section 501(c)(3) of the Internal Revenue Code, as amended, including the operation of activities to further the exempt purposes of the Corporation.”

Your Form 1023 Application provides that you will engage in the following activities:

1. Provide gifts of up to 5% of the contract sales price to low and moderate income home buyers for homes included in your program. You further state that you will offer your program on a nationwide basis. In addition, you expect this to constitute 47.5% of your activity and 75% of your expenditures.

2. Collect a service fee from home sellers and builders in the amount of \$1000 for their homes to be included in your program. You expect this activity to constitute 47.5% of your overall activities and 97% of your revenues. You state that this will provide you with an on-going source of income with which to provide future gifts to low and moderate-income homebuyers.
3. Solicit charitable contributions from people working in the real estate industry such as mortgage companies, real estate agents and builder to help you identify potential home buyers and home sellers. In addition, you will conduct personal visits, advertising, home shows and fax broadcasting to market your program. You state that you expect this activity to constitute 5% of your overall activity and 3% of your revenue.

On your Form 1023, you represented that you will provide down payment gifts to individuals and families for the purpose of purchasing a home. To qualify, applicants must fall into either the low or moderate income categories as defined by the Federal Housing Administration (FHA). Applicants must qualify for a mortgage, complete an education requirement, demonstrate need for down payment assistance, and purchase a home in your program.

You state that your program is open to all participants who qualify for any loan program that accepts gifts from charities. By letter dated July 9, 2002, you estimate that 10% of the people who will use your program will be very low income category, 40% will be low income and 50% will be moderate income. In your letter of February 11, 2003, these estimates were slightly modified to 10% low income category, 50% low income, and 40% moderate income. You state that these figures were just targets and that you could not say with certainty whether many very low income buyers would be able to participate in your program.

You do not intend to distinguish between very low-income, low-income, or moderate-income persons before allowing participation in your program nor will you limit your services based on income or assets. You state that all persons who fall into such income categories will receive the same potential assistance. You state that the benefits of your program will be available to all classes of people. In addition, you will not “specifically target the benefits of M towards any one disadvantaged group.” [Your] program is available to anyone who is able to qualify for a mortgage from any lender in any State in the United States. Your website states that “although the program was created to help low and moderate income buyers, there are no income restrictions for others to use the program. The only restriction is that the home purchase price be less than [300.7z], and that the property be owner-occupied. “

You state that your down payment assistance program transfers funds at settlement using a pre-existing pool of funds to provide a buyer with the required down payment amount towards the purchase of a seller’s home. In your letter of February 11, 2003 and reiterated in your letter of August 11, 2003, you describe a typical down payment assistance transaction as including the following steps:

1. A buyer works with a realtor to find a home that is within their price range.
2. Once a home is found, the buyer applies for a mortgage.

3. Realtor may inform the seller or buyer about your program.
4. If the buyer is interested, the realtor may inquire whether the seller is willing to participate in the program.
5. If both parties agree to participate, the buyer must request from the lender a loan that will allow gifts from charitable organizations.
6. The buyer completes the Gift Funds request form and the Gift Letter form. The gift request form asks the buyer for limited information such as annual income, mortgage lender, loan type, and property to be purchased. The gift letter provides that the buyer understands that the gift funds provided are not made available from any person or entity with an interest in the sale of the property including the seller, real estate agent or broker, builder, loan officer, or any entity associated with them. In addition, the letter states that the buyer is under no obligation to repay the down payment assistance received for the purchase of the home.
7. The seller completes the Seller Participation form. This form indicates that you are assisting the seller in the sale of their home by providing down payment assistance. The seller agrees to pay a service fee to you in the amount of \$1000 plus 5% of the contract sales price within 2 business days from the transfer of the home. The seller acknowledges that the contribution will not be used to provide assistance to the buyer of the home and that gifts come from a pre-existing pool. Seller also acknowledges that they are under no obligation to pay the service fee if closing does not occur and any funds not used will be returned to seller.
8. A representative of M reviews the documents for completeness and accuracy.
9. The closing office or agent completes the Closing Office form, which requires the closing agent to ensure that all forms are signed. In addition, the closing agent is responsible for collecting and distributing the contribution to you from the seller's proceeds within 2 business days of the closing and the closing agent must return any funds not utilized by the buyer.
10. All forms must be received by you, 48 hours prior to the closing to ensure that there is time to review and address any incomplete or inaccurate forms.
11. Upon approval by you, you will wire transfer the funds into the closing or escrow account of the buyer.
12. The closing office records the gift on the HUD-1 statement.
13. The seller makes a gift to M of 5% of the contract sales price of the home plus a service fee of \$1000 for using the program.

If closing is successful, the closing agent will disburse seller's "gift" to you and document the transaction on the HUD-1 form. You will retain a certified copy of the HUD-1 statement as a

permanent record. Upon receipt of the HUD-1 statement, you will send the buyer a "home upkeep book" for their reference. You state that in the event that closing does not take place, the closing office must return any and all funds to you. You will then return the seller's matching gift contribution to the seller within 5 business days.

In your letter of August 11, 2003, you represent that the seller's contribution is placed into a pre-existing fund to enable further gifts to other prospective home buyers. The \$1000 service fee is paid to ensure on-going viability, develop marketing materials, cover administrative costs and to expand the organization. You state that there are no circumstances under which the seller is not required to pay the service fee. And, your pro-forma "Downpayment Gift Letter" requires the potential home buyers to acknowledge that the "gift" funds to be given to them are "not made available from any person or entity with an interest in the sale of the property, including the seller."

In your letter of February 11, 2003 and confirmed in your letter of August 11, 2003, however, you state that in order for a seller to participate in your program, the seller's gift must match the amount of down payment assistance provided to the buyer. You state that in the event the seller's gift does not match the amount provided to the buyer, the transaction may be cancelled. The down payment assistance amount and the seller's gift must be agreed upon prior to the closing; otherwise, the transaction cannot be conducted using your program. You state that in the "unlikely event that the seller's contribution is greater than the actual down payment assistance provided," the seller has the option of receiving a refund of the contribution amount not used or can gift the additional monies to you. You further state, in your letter of August 11, 2003 and in your "Sellers Participating Agreement," that if closing does not take place, the seller is not obligated to pay the service fee and that the seller's contribution is refundable.

In your letter of February 11, 2003, you state that other than the benefits of sellers being able to sell their homes to a larger pool of applicants, buyers purchasing homes without a down payment, the only savings to a buyer is not worrying about having enough funds for a down payment. You state that no other savings or income is earned by the buyer, seller, mortgage lender, title company, closing agent or you. However, your website provides a sample transaction wherein you state that your program "makes everyone a winner." The sample transaction is provided below:

	Without the Program	With the Program
List (Asking) Price	150z	150z
Selling Price	139.5z	150z
Service Fee		8.5z
Net Selling Price		141z
Commissions (6%)	8.37z	9z
Net before Closing Costs	131.13z	132.5z

You also represent that your "seller participation" form requires sellers affirm that they have not increased the market value of their houses due to their participation in your down payment assistance program. But, you also represent that your program will enable sellers to

reduce the amount of the negotiated discount on their homes.

You state that under this example, the "Service Fee" represents the service fee to you of \$1000 plus the "gift" or down payment assistance provided by the seller. The seller realizes an additional 1.37% of net income. The real estate agent realizes an additional 0.63% in commission. In turn, the buyer has a higher base cost for the home but does not have to personally put down the required down payment amount.

In your letter dated August 20, 2002, 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.

The financial data that you included on your Form 1023 shows that you anticipate receiving approximately \$10,900,000 in gross receipts from services during your first three years of operation. You anticipated making "gifts" of approximately \$8,700,000 during that same period of time. You also expect to pay approximately \$345,500 in compensation to two of your three officers and other salaries of \$567,000 during your first three years of operation. In addition, you represented that you expect to incur expenses of approximately \$280,000 in advertising and marketing. When asked how your officers' compensation is determined, you responded that they are determined by a vote by the board of directors. In the same letter, however, you indicated you have not held formal board meetings since your bylaws were approved.

You state that your program does not discriminate against any applicant who is able to obtain a mortgage. You do not review credit histories of the applicants. Instead, you state that credit histories are reviewed by the individual mortgage lenders and that you rely on the expertise and professional licensing of the mortgage lender to ensure that the potential home buyer will be able to satisfy the loan. You will also rely on the mortgage lender, the insurance agency, the home inspector and the appraiser to ensure that the property is safe, decent, sanitary, and affordable. You state that "as with any investment, buying a home has inherent risks. The buyer, through working with the lender and throughout the entire home buying process will learn what the risks are and must be prepared to deal with them on their own accord. [M] makes no guarantee and cannot legitimately guarantee that adverse effects will not occur to the home buyer."

In your letter of August 11, 2003, you state that buyers and the general public will have access to an M representative who is available to answer questions. You will also provide buyers with access to web-based home buyer education materials and pamphlets. You will be providing on-going homeowner education by providing a list of resources on your website. You

will refer prospective participants to mortgage insurance groups and provide the name of a “commercially available book” to guide home buyers to ensure that their home is safe, decent, and sanitary. However, neither you nor your staff conducts the actual education program or any other program to help ensure that a buyer is purchasing a safe, decent and affordable house. You state that you cannot guarantee that adverse effects will not occur to the buyer, but hope that by providing such references, you will minimize the chance for adverse effects.

In your description of your down payment assistance program, you state that you plan to promote your program through a direct marketing campaign via your website to real estate agents, mortgage lenders and home sellers and builders. You plan to solicit these parties to help identify potential homebuyers in need of down payment assistance and to fund your “pre-existing pool” of down payment assistance monies. You state that you plan on soliciting donations and charitable gifts from any and all donors ensuring that there is no conflict of interest between parties and that no donor will benefit. However, your financial statements indicate that you anticipate receiving 97% of your financial support from service fees and 3% from contributions from sellers and other parties involved in the down payment assistance program such as mortgage lenders and realtors. Finally, you state that you set 5% as the “gift” amount to “maximize the number of new homeowners who will be able to participate in your program.”

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.”

In Church of Eternal Life and Liberty, Inc. v. Commissioner, 86 T.C. 916, 926 (1986), the court stated that while the payment of reasonable salaries does not constitute prohibited inurement, the payment of excessive salaries does.

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.

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 5% 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. 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 you. 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 you and indirectly to the homebuyer to facilitate the sale of their homes. In fact, your representation that seller's payment will enable the seller to reduce the amount of the negotiated discount demonstrates the circular character of the payments. Upon the closing of the sale, the sellers "contribution" to you is returned to seller as part of the proceeds the seller receives from the sale of the home.

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.

Moreover, you have not established that your net earnings will not inure to the benefit of private shareholders or individuals. You state that you will pay two of your three officers \$345,500 in compensation during your first three years of operations. However, you have not explained in sufficient detail what services these officers will perform in return for the

compensation and how those services further exempt purposes within the meaning of section 501(c)(3). You have not established that these compensation levels are reasonable. In addition, you have not established that the "compensation" will be anything other than a distribution of your net earnings to these individuals.

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 your 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 protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a 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 officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section 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 administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service,

TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with section 6104(c) of the Code.

In the event this ruling becomes final, it will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, *Notice of Intention to Disclose*. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions, you should follow the instructions in Notice 437.

If you decide to protest this ruling, your protest statement should be sent to the address shown below:

Internal Revenue Service
TE/GE Exempt Organizations
SE:T:EO:RA:T:2

1111 Constitution Ave, N.W., Rm. PE-3P3
Washington, D.C. 20224

If it is convenient, you may also fax your reply using the fax number shown in the heading of this letter. If you fax your reply, please contact the person whose name and number are shown in the heading of this letter to confirm that your fax was received.

If you do not intend to protest this ruling, and if you agree with our proposed deletions as shown in the letter attached to Notice 437, you do not need to take any further action.

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(s)
Notice 437

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