

200511024

DEPARTMENT OF THE TREASURY
Internal Revenue Service



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

October 27, 2004

Exempt Organization

Taxpayer Identification Number:

Form:
990

Tax Year(s) Ended:

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

CERTIFIED MAIL – RETURN RECEIPT REQUESTED

Dear

We have enclosed a copy of our report of examination explaining why we believe an adjustment of your organization's exempt status is necessary.

If you do not agree with our position you may appeal your case. The enclosed Publication 3498, *The Examination Process*, explains how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

If you request a conference, we will forward your written statement of protest to the Appeals Office and they will contact you. For your convenience, an envelope is enclosed.

If you and Appeals do not agree on some or all of the issues after your Appeals conference, or if you do not request an Appeals conference, you may file suit in United States Tax Court, the United States Court of Federal Claims, or United States District Court, after satisfying procedural and jurisdictional requirements as described in Publication 3498.

You may also request that we refer this matter for technical advice as explained in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*. If a determination letter is issued to you based on technical advice, no further administrative appeal is available to you within the IRS on the issue that was the subject of the technical advice.

If you accept our findings, please sign and return the enclosed Form 6018, *Consent to Proposed Adverse Action*. We will then send you a final letter modifying or revoking exempt status. If we do not hear from you within 30 days from the date of this letter, we will process your case on the basis of the recommendations shown in the report of examination and this letter will become final. In that event, you will be required to file Federal income tax returns for the tax period(s) shown above. File these returns with the Ogden Service Center within 60 days from the date of this letter, unless a request for an extension of time is granted. File returns for later tax years with the appropriate service center indicated in the instructions for those returns.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

Taxpayer Advocate

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

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Thank you for your cooperation.

Sincerely,

R.C. Johnson
Director EO Examinations

Enclosures:
Publication 892
Publication 3498
Form 6018
Report of Examination
Envelope

the actual receipts of the organization were under the Form 990 filing requirements.
(currently)

- For the period under examination the president of X was the sole individual responsible for the record-keeping of X. P was also the sole individual responsible for the bank accounts of X.

Notes of the above interview were shared with R and P via a letter dated November 28, 2003. That letter also included a request for any clarification or corrections. To date, no modifications of any of R's statements have been received.

During the initial examination R provided the bank statements of X for the 1999 and 2000 calendar years, as well as minimal receipts and other supporting documents for the organization for 1999 and 2000.

After the initial examination, records verifying the source and destination of all funds flowing through X accounts for the examination periods, as well as supporting records of the activities of the organization for the [REDACTED] years were requested.

No additional records have been provided for [REDACTED] tax year transactions. To date, the organization has failed to provide any records for the [REDACTED] year. Records for the [REDACTED] tax year were requested in the initial examination letter, an information document request left with the taxpayer on [REDACTED], and again in a follow-up request on [REDACTED]. To date, none of the requested [REDACTED] records have been provided.

As a result of the taxpayers' failure to timely provide records in a related matter, the Internal Revenue Service issued bank summonses for the accounts of X. In response to those summonses, records for 2 accounts were provided by Bank.

Records provided were for [REDACTED] Account # 1, titled X
[REDACTED] Account #2, titled X.

A review of the two bank accounts of the X showed the following transactions within the accounts of X for which no supporting documents have been provided. The summary information lists the transaction dates, deposit or withdrawal, the type of funds or withdrawal method, check numbers and the amounts as applicable. Transactions involving bank interest payments and documented expenditures of the organization have been excluded.

Bank Checking Account #2, X,		calendar year deposits.	
Deposit Date	Amount	Deposit	Item
02/09/1998		Cash	
02/18/1998		Cash	
02/23/1998		Cash	
03/02/1998		Cash	
03/03/1998		Cash	
03/09/1998		Cash	
03/16/1998		Cash	
03/17/1998		Cash	
03/23/1998		Cash	
03/23/1998		Cash	
03/24/1998		Cash	
03/30/1998		Cash	
03/31/1998		Cash	
04/06/1998		Cash	
04/08/1998		Cash	
04/13/1998		Cash	
04/14/1998		Cash	
04/20/1998		Cash	
04/22/1998		Cash	
04/27/1998		Cash	
04/29/1998		Cash	
04/30/1998		Cash	
05/04/1998		Cash	
05/06/1998		Cash	
05/08/1998		Cash	
05/11/1998			Money order
			Cashiers Check
05/18/1998		Cash	
07/21/1998		Check	
08/05/1998		Check	
08/10/1998		Check	

The total deposits into this account for [redacted] totaled \$ [redacted] including 26 separate cash deposits of \$ [redacted]. Additionally, the specific payee on all of the checks and money orders was the X.

The total of all deposits into this account for [redacted] period were [redacted] meaning that 99.72 percent of deposits into the account for the period were appear to be non-exempt income. Additionally, none of the income for the period has been documented as exempt source income.

Bank Checking Account # 2, X			calendar year Withdrawals.		
Check Date	Number	Amount	Payee	Notation	
11/12/97	102	[REDACTED]	P	Reimb supplies	
11/17/97	110		Dept. of Commerce & Consumer Affairs	Annual Reg	
02/25/98	Debit				
02/27/98	5		Bank		
03/03/98	106		Dept. of Commerce & Consumer Affairs	Annual Fee	
03/13/98	T3		Bank		
03/19/98	107		Bank		
03/30/98	Debit				
04/03/98	108		Bank		
04/17/98			Bank		
04/29/98	Debit				
05/01/98	101		Bank	re	
05/08/98	103		Bank	re	
05/22/98	104		Bank	re	
07/21/98	105		Cash	Refunds	
07/24/98	106		Cash	Refunds	
07/28/98	107		Cash	Refunds	
07/29/98	108		Cash	Refunds	
07/31/98	109		Cash	Refunds	
08/03/98	110		Cash		
08/05/98	111		Cash	Refunds	
08/07/98	112	Bank	Reimb		
08/10/98	113	Cash	Refunds		
08/18/98	114	Cash	Refunds		
08/21/98	116	Inc	Reimb		

These transactions included [REDACTED] in 9 cash withdrawals by P and [REDACTED] in payments to P and his company. Although records have been requested, none of these transactions have been documented.

Bank Preferred Checking, Account #1, X Client Trust Account, [REDACTED] calendar year withdrawals.

Check Date	Number	Amount	Payee	Notation
05/07/98	1		Bank	
05/14/98			Bank	
05/12/98	3		Limited Partnership	from
05/22/98	101		Bank	re: [redacted]
05/29/98	102		Bank	re: [redacted]
06/22/98	104		Bank	
06/15/98	103		Escrow	
07/09/98	105		Bank	
07/17/98	106		Escrow	Deposit
07/20/98	107		Bank	
08/03/98	108		Limited Partnership	Re: Cr Line
08/05/98	109		X	For refunds
08/10/98	110		X	Refunds
08/14/98	111		Bank	re: [redacted]
08/21/98	112		Cash	re: [redacted]
08/31/98	113		Inc	services
09/08/98	114		Inc	services
09/10/98	115		Bank	re: refund
09/21/98	116		Inc	
09/29/98	117		Inc	
10/07/98	118		Inc	Re: [redacted]

No supporting documents were provided for any of the above expenditures, including paid to F, a for profit entity owned by P.

For the tax year ended December 31 [redacted] the income and expenditures from both accounts was minimal.

For account number # 2, the organization had total [redacted] income of [redacted] as one deposit from V. For the same period, account withdrawals from this account totaled [redacted] including [redacted] paid to local [redacted] and [redacted] paid to the S for annual registration fees.

For account number # 1, the organization had total [redacted] income of [redacted], including a one time deposit of [redacted] from a C for [redacted] and [redacted] from a V. For the same period, account withdrawals from this account totaled [redacted] including [redacted] paid to cash.

deposits.		, Account #1, X		calendar year	
<u>Deposit Date</u>	<u>Amount</u>		<u>Deposit Item</u>	<u>Payor</u>	
05/19/00			Check		
			Cashiers Check		
06/01/00			Currency	Possible wire transfer	
08/11/00			Check	Limited Partnership	
			Check	Limited Partners	

As summarized above, during the calendar year _____ in deposits were made into this account, including _____ reported as cash on the bank statement. Again, all checks and cashiers checks were specifically written to the X.

withdrawals.		, Account #1, X :		calendar year	
<u>Check Date</u>	<u>Check Number</u>	<u>Amount</u>	<u>Payee</u>		
05/19/00	126		(remarks indicate wire transfer)		
06/02/00	127		(remarks indicate wire transfer)		
08/11/00	128		Cash - (Remarks indicate Wire)		

Law:

IRC 501(c)(4) provides for the exemption of (A) Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes.

(B) Subparagraph (A) shall not apply to an entity unless no part of the net earnings of such entity inures to the benefit of any private shareholder or individual.

Section 1.501(c)(4)-1(a)(2) of the Income Tax Regulations provides that an organization is operated exclusively for the promotion of social welfare if it is primarily engaged in promoting in some way the common good and general welfare of the people of the

community. An organization embraced within this section is one that is operated primarily for the purpose of bringing about civic betterments and social improvements.

IRC section 6001 states: "Every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the secretary it is necessary, he may require any person, by notice served upon such person or regulations, to make such returns, render such statements, or keep such records, as the Secretary deems sufficient to show whether or not such person is liable for tax under this title."

IRC section 6033(a)(1) states: "IN GENERAL.—Except as provided in paragraph (2), every organization exempt from taxation under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts, and disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe, and shall keep such records, render under oath such statements, make such other returns, and comply with such rules and regulations as the Secretary may from time to time prescribe; except that, in the discretion of the Secretary, any organization described in section 401(a) may be relieved from stating in its return any information which is reported in returns filed by the employer which established such organization.

Regulation 1.6001-1 requires an exempt organization to keep permanent books and records sufficient to show specific items of gross income, receipts, and disbursements and to substantiate the information required by section 6033.

Reg. Section 1.6001-1(a) provides for the keeping of records by an organization. It states: "*In general.* Except as provided in paragraph (b) of this section, any person subject to tax under subtitle A of the Code (including a qualified State individual income tax which is treated pursuant to section 6361(a) as if it were imposed by chapter 1 of subtitle A), or any person required to file a return of information with respect to income, shall keep such permanent books of account or records, including inventories, as are sufficient to establish the amount of gross income, deductions, credits, or other matters required to be shown by such person in any return of such tax or information."

Reg. Section 1.6033 -2(i)(2) provides that an organization exempted from filing an annual return under IRC section 6033 is not relieved of other record keeping requirements.

In *Church of Gospel Ministry, Inc. v. United States*, Civil Action No. 85-1527, U. S. District Court for the District of Columbia, 640 F. Supp. 96; 1986 U.S. Dist. LEXIS 24782; 86-2 U.S. Tax Cas. (CCH) P9497; 58 A.F.T.R.2d (RIA) 5232, May 30, 1986, Decided, the revocation of a church was upheld where the organizations' failure to maintain adequate records prevented it from meeting its burden of showing that it was operated exclusively for charitable purposes, and that its assets did not inure to the benefit of its officers.

Government Position:

It is the position of the government that X has engaged in a substantial non-exempt purpose, the funneling of money not intended for exempt purposes through the accounts of the X, and is therefore not primarily engaged in promoting in some way the common good and general welfare of the people of the community as provided in IRC section 501(c)(4) and the regulations there under.

Statements made by the organizations attorney, R, that deposits and withdrawals flowing through the X accounts were simple errors, are not supported by the facts in this case. This is illustrated by the bank statements secured by the Internal Revenue Service via summons. The statements for the X account number 2 at Bank, for example, show 29 separate deposits, and accompanying withdrawals. Of these deposits, 26 were for cash, totaling [REDACTED]. Of the remaining deposits, all checks and money orders were specifically made payable to the X. Obviously, the intent in this case was to use the accounts of the X as a transfer point for funds which never had any exempt purpose.

In comparison, per the X attorney, R, the exempt receipts of the organization were minimal. Per R's own statements, they were under the [REDACTED] 990EZ filing threshold. Additionally, the limited records reviewed during the examination showed exempt expenditures of less than [REDACTED] annually, and these expenditures remain suspect since no exempt purpose has been shown for many of the items paid to P and his companies.

Additionally, it is the position of the government that X has failed to meet the record-keeping requirements outlined in IRC sections 6001 and 6033 and Reg. Section 1.6001-1.

As part of an examination of the exempt activities of X, the Service requested that the organization provide the books of accounts and other records required under IRC Section 6033 and Reg. Section 1.6001-1 for the tax years ended

in order to verify the gross income, deductions and exempt activities of the organization.

In response to these requests, X has made available source documents of minimal expenditures made by the exempt organization during the examination period. However, no documentation has been provided to document the purposes of the large sums of money transferred through the accounts of the

Taxpayers Position:

To date, the only position provided by the taxpayer has been the statements made by the attorney during the initial examination. The statements indicated that the large transactions documented in this report were, in fact, not the funds of the EO. The attorney further states that the deposit of these funds into the accounts of the EO were simple erroneous transactions. Additional taxpayers response is being solicited with this report.

Conclusions:

X has been used for a substantial non-exempt purpose. Its sole remaining officer, P has used accounts in the name of the organization to collect and transfer funds used for non-exempt purposes. These transactions were engaged in purposely, and occurred repeatedly over a period of years.

These transactions occurred even as the exempt activities of the exempt organization were reduced and eventually stopped.

The exempt status of the X should be revoked effective the year the substantial non-exempt activities began, the tax year ended

X has also failed to provide required documentation supporting exempt activities for the tax years. The exempt status of the X should be revoked effective the first day of the first year of such failure, the tax year ended