



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Release Number: **200818023**

Release Date: 5/2/08

Date: February 6, 2008

UIL Code: 501.03-00

501.36-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

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.

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,

Robert Choi
Director, Exempt Organizations
Rulings & Agreements

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



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: DEC 17, 2007

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

UIL:

501.33-00
501.36-00

Legend:

B= Applicant
C= State
D= Similar-type organization
E= President
F= Vice-president
G= Address
H= Similar-type organization
I= Similar-type organization

P= State Agency
Q= Local court
R= State employee
S= State employee
T= Date
w=Dollar amount
x= Dollar amount
y= Dollar amount
z= Dollar amount

Dear

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

Issue:

Considering the facts, as described herein, does an organization primarily involved in the sale of annuity plans qualify for exemption from federal income tax as an organization described in section 501(c)(3) of the Internal Revenue Code of 1986?

Facts:

B was formed as a nonprofit corporation in the state of C on . The Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, Form 1023, was filed in . The narrative description of activities provided in the application, Form 1023, explained that (B):

...plans to coordinate and conduct, through its staff, evangelistic campaigns in a number of countries wherein the people are receptive to the Gospel of Jesus Christ. In addition, the organization may co-sponsor evangelistic campaigns with other organizations that have a track record of proven evangelistic results, such as D (a religious organization)...B may also underwrite the costs of operating orphanages that teach children the Gospel. The organization may also distribute Bibles, build churches and install fresh water wells, particularly in third world communities where such opportunities are unavailable.

The Third Article of B's Articles of Incorporation describes its purposes as follows:

"The corporation shall exist to promote the sponsorship and support of a world-wide missionary effort, including without limitation the development and support of youth groups and camps, crusades, orphanages, nursing homes, humanitarian services, radio and television ministry, prison ministry, bible translation and distribution programs, alternate food supply research and development, health care programs, religious educational training and the management and administration of donor accounts to fund any or all of the foregoing purposes."

Article V of B's bylaws state that "...the business and affairs of the corporation shall be managed by its board of directors." The initial board of directors as shown on page two of the application Form 1023 are E and F. E and F are husband and wife that reside at the same address as shown on page one of the Form 1023 at G address. The application explains that "E, president of B, will be initiating and supervising the activities of the organization, from his home office. F will be performing administrative functions."

The application further explains that "E, President and Director, completed several courses at H." In E went to work for a nonprofit organization, teaching charitable planned giving courses all across the United States. At the time the application was filed E was "...the executive vice president of development for a nonprofit organization, I." "F, Vice President and Secretary, will be serving principally in an administrative role for the organization."

In the narrative attachment to Part VIII, item 4e of the Form 1023 it states that E...

is familiar with the nature and limitations of donor advised accounts. While B has no plans to activate a donor advised account campaign, it remains open to the desires of donors who may wish to use such a device in connection with the promotion of the mission of B. Donors would likely be permitted to provide advice regarding distributions affecting the citizens of a particular country and with a particular benefit (such as Bibles for , fresh water wells for or churches in) or for a particular organization that may be co-sponsoring projects with B, such as D.

B also maintained a website to promote their programs. The website explained that "...B assists financial professionals, estate planning attorneys, and CPAs with tax saving solutions." In addition, the website states that

B has enjoyed the privilege of providing plans, which are quite simple, to families all across the United States as they create their financial legacy... The various

strategies of B continue to help clients nationwide in their estate planning. We offer the client the ability to exchange a variety of assets, including: annuities, real estate, securities, bonds and cash for a B Tax Deductible Installment Plan with a guaranteed payout for a guaranteed period of time.

B's primary focus is the "Asset Exchange Programs" rather than the charitable programs described in its Articles and application. B's website promotes the three programs. These asset exchange programs allow individuals to exchange Real Estate, Securities and Annuities for the "B Tax Deductible Installment Plan" product. The website also affirmed that when a person exchanges an asset for a B Tax Deductible Installment Plan, they receive the following:

- A generous income tax deduction
- A tax-favored income
- Elimination of a portion of any capital gains
- A guaranteed income that grows every year, and
- An estate tax reduction

The website also explains that B supports multiple charitable organizations throughout the world.

C state law requires all new charitable organizations to file quarterly financial reports with the secretary of state during its first fiscal year of operation. Since B was formed in _____ of _____ the Service requested copies of the four quarterly financial reports filed with the secretary of state during the organizations first year of operation. These reports show the total amount of revenues earned and expenses incurred each quarter.

In the four quarterly reports for _____ the total amount of revenues that B received were classified as contributions. The total amount of contributions reported in _____ was w dollars. The itemized list of contributions that was attached to each report shows that these revenues were primarily from the sale of annuity plans.

The expenses reported on these reports are classified into the following four categories; program services or other charitable purposes, fundraising; administrative and other expenses. Administrative and the other expenses for _____ included utilities expense, automobile expenses and lease, rent, phone, entertainment, meals, health care, office expenses, furniture and wages. The total amount for automobile lease expenses in _____ was x dollars. B leased two automobiles for E and F who were the only authorized users. The officers stated that E and F had sold their separate personal use automobiles. However, the cars were used "almost exclusively for business purposes". Business purposes included transportation to the business office, seminars, presentations and meetings with financial planners. Utility expenses in the first six months were for the original office in E's and F's home. B's officers stated that in June of _____ a business office was established in addition to the home office. B's total expenses from operations in _____ were reported to be y dollars.

The total amount of funds for charitable programs and services were reported to be z dollars. However, additional information submitted by B clarified that certain amounts were incorrectly reported as contributions to charities when they should have been operating expenses. Therefore, the total amount of funds for charitable purposes is less than the z dollars reported.

The z dollars amounts reported for charitable programs in the four quarterly financial reports for the tax year is less than one half of one percent of the total revenues (or contributions to B) reported. In addition, the funds for charitable programs are approximately three percent of the total expenses reported to operate B in

In May of , P, a state agency, issued a media release stating that the agency's Commissioner filed a petition in Q court seeking an order placing B in receivership. The Petition alleges that B is an unauthorized insurance entity marketing a term annuity product to state consumers as well as consumers across the country. This media release included a warning to consumers to never purchase insurance products from unlicensed insurance companies, nor should they deal with insurance agents or producers who are not licensed. In addition, it was reported that 5 other states have all issued cease and desist orders to prohibit B from conducting business in their states.

In June of the Q court placed B into receivership. The Consent Order reported that "R, in the capacity as Rehabilitator of B, has custody of all assets and operations of B and will wind-down the company's operations" and that "...S has been appointed as Special Receivership Counsel." The court determined that "...authority and control by former management and employees of B has been suspended, and are strictly prohibited from communicating with contract holders." The Commissioner, Special Deputy Receiver and Special Counsel "...will conduct the wind-down of B's business."

Special Receivership Counsel, S notified the Internal Revenue Service that "on August Commissioner R filed a Verified Petition to convert the B receivership from a rehabilitation proceeding to a liquidation proceeding....The Receiver has also requested a finding of insolvency of B from the receivership court."

Tax Law:

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable purposes.

Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term 'charitable' is used in section 501(c)(3) of the Code in its generally accepted legal sense, and includes the lessening of the burdens of government.

An organization described in section 501(c)(3) of the Code, must, among other requirements, be organized and operated exclusively for certain purposes.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations states: "In order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt."

Section 1.501(c)(3)-1(c)(1) of the regulations states: "An organization will be regarded as 'operated exclusively' for one or more exempt purposes only if it engages primarily in activities

which accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations state that: "An organization is not organized and operated exclusively for one or more of the purposes specified...unless it serves a public rather than a private interest. Thus, to meet the requirements...it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled directly or indirectly, by such private interests."

Section 1.501(c)(3)-1(e)(1) of the regulations states: "An organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization's exempt purpose or purposes and if the organization is not organized or operated for the primary purpose of carrying on an unrelated trade or business, as defined in section 513. In determining the existence or nonexistence of such primary purpose, all the circumstances must be considered, including the size and extent of the trade or business and the size and extent of the activities which are in furtherance of one or more exempt purposes."

In Rev. Rul. 64-182, 1964-1 C.B. 186, an organization derived its income principally from the rental of space in a large commercial office building. The organization's charitable purposes are carried out by making contributions and grants to other charitable organizations. In this revenue ruling, the IRS concluded that this organization met the primary purpose test of section 1.501(c)(3)-1(e)(1) of the regulations because it carried on a charitable program that was commensurate in scope with its financial resources.

In Rev. Rul. 72-369, 1972-2 C.B. 245, an organization was formed to provide managerial and consulting services for section 501(c)(3) organizations to improve the administration of their charitable programs. The organization enters into agreements with unrelated section 501(c)(3) organizations to furnish managerial and consulting services on a cost basis. This revenue ruling stated that:

An organization is not exempt merely because its operations are not conducted for the purpose of producing a profit. To satisfy the 'operational test,' the organization's resources must be devoted to purposes that qualify as exclusively charitable within the meaning of section 501(c)(3) of the Code and the applicable regulations. Providing managerial and consulting services on a regular basis for a fee is a trade or business ordinarily carried on for profit. The fact that the services in this case are provided at cost and solely for exempt organizations is not sufficient to characterize this activity as charitable within the meaning of section 501(c)(3) of the Code. Furnishing the services at cost lacks the donative intent element necessary to establish this activity as charitable.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the Tax Court held that an organization did not qualify for exemption under section 501(c)(3) of the Code because it was primarily engaged in an activity that was characteristic of a trade or business and ordinarily

carried on by for-profit commercial businesses. The Tax Court stated: "We must agree with the Commissioner that petitioner's activity constitutes the conduct of a consulting business of the sort which is ordinarily carried on by commercial ventures organized for profit."

In Airlie Foundation v. Internal Revenue Service, 283 F.Supp. 2d 58 (D.D.C. 2003), the District Court found that that the organization was formed principally to organize, host, conduct and sponsor educational and other charitable functions on its facilities. The organization's patrons were not limited to tax-exempt entities, but included patrons of a private and corporate nature. The organization paid significant advertising and promotional expenses and derived substantial income from weddings and special events held at its conference center. The court determined that the organization's activities competed with a number of commercial, as well as non-commercial entities, which strongly evidenced a commercial nature and purpose. The court concluded that although the organization carried out a number of charitable and educational activities, these were incidental to its primary activity of operating a for-profit conference center. The court stated: "While plaintiff's organizational purpose is exempt and the foundation operates, in important respects, in an exempt fashion, there is a distinctive 'commercial hue' to the way Airlie carries out its business"

Application of Tax Law:

The fact that your activities consist primarily of performing services for individuals who wish to exchange assets for annuity plans as an estate planning tool, you are performing commercial services for these individuals. Because less than one half of one percent of the funds received go to charity, this does not render your activities as charitable, Rev. Rul. 72-369, *supra*.

In addition, since your activities primarily constitute the operation of a commercial activity, you are organized and operated for the primary purpose of carrying on an unrelated trade or business. As a result, under section 1.501(c)(3)-1(e)(1) of the regulations, you do not meet the requirements of section 501(c)(3) of the Code. Unlike the organization described in Rev. Rul. 64-182, *supra*, you do not carry on a charitable program that is commensurate in scope with your financial resources.

The Service's position that the sale of annuity plans has a "distinctive commercial hue" is supported by the fact that several states consider these annuity contracts as commercial products subject to their securities and insurance laws.

The _____ by the state agency reported that you have been ordered to cease and desist the sale of your annuity plans in five other states. It also went on to say that "over 230 insurance contracts were sold by (B), only _____ consumers were personally solicited in (B's home state)." (B) maintained a website soliciting business nationwide." These cease and desist orders are based on your violation of certain state laws concerning the sale and marketing of annuities.

We view the sale of these securities constitute common commercial activities, rather than activities that further a charitable purpose. See B.S.W. Inc. v. Commissioner, *supra*; and Airlie

Foundation v. Internal Revenue Service, supra.

Applicant's Position:

In response to the Service's position, S notified the IRS that "Commissioner (R) is unaware of any facts that would rebut or supplement the questions raised....Commissioner (R) would like to receive your (the Service's) formal determination as to whether (B) would have received designation as a § 501(c)(3) tax-exempt organization."

Conclusion:

Based on the information submitted and the programs promoted on your website it appears that you are primarily involved in the sale of annuity plans associated with their asset exchange programs. The sale of annuity plans would constitute a trade or business and without a charitable program commensurate in scope with the business of selling these plans, you do not qualify for exemption under IRC § 501(c)(3). We also determined you do not qualify under any other subsection under IRC § 501(a).

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. If your statement does not provide a basis to reconsider our determination, we will forward your case to our Appeals Office. You can find more information about the role of the Appeals Office in Publication 892, *Exempt Organization Appeal Procedures for Unagreed Issues*.

An attorney, certified public accountant, or an individual enrolled to practice before the Internal Revenue Service may represent you during the appeal process. If you want representation during the appeal process, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. You can find more information about representation in 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 appeal 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 the applicable address:

Mail to:
Internal Revenue Service
EO Determinations Quality Assurance

Deliver to:
Internal Revenue Service
EO Determinations Quality Assurance

You may 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