**TO:** Senator Grassley
**FROM:** Tax Staff
**RE:** Review of ACORN Tax-exempt Status
**DATE:** September 22, 2009

## ACORN and IRS Responses

ACORN, through its attorney, provided three responses to your letter of October 25, 2006. ACORN's response was essentially that it was not a tax-exempt entity.

After receiving ACORN's first response dated November 3, 2006, you wrote to the Internal Revenue Service on November 8, 2006. IRS responded on December 19, 2006. Most of the response and supporting materials provided by the IRS are protected under section 6103. IRS confirmed that ACORN is a taxable entity and that the ten organizations listed in your letter were tax-exempt. IRS indicated that it would continue to look for additional affiliated organizations. We have not communicated with IRS about ACORN since receiving that response.

## Staff Work

Shortly after receiving ACORN's third response, we determined that ACORN did not intend to comply with your requests for information. We had consulted with the Chairman's staff about issuing a subpoena for the requested information. Because the U.S. Attorney's office was conducting an investigation of ACORN on the issue of voter registration fraud, a decision was made not to pursue the subpoena at that time.

Since then, we have researched over 100 organizations identified by various sources as affiliated with ACORN. We began with a list published by the Employment Policies Institute in its report *"Rotten ACORN: America's Bad Seed"*. We then searched Guidestar.org and all online state corporate records databases, except Maine, New Jersey and Oklahoma because these states either did not have online records or charged fees. We also searched for entities on Guidestar.org using addresses affiliated with ACORN. Finally, we conducted general internet searches for organizations not found on Guidestar or in state corporate records databases.

Our research indicates that ACORN's response that it is not tax-exempt is disingenuous and misleading. Millions of charitable dollars from individuals, foundations and federal, state, and local governments flow to ACORN and its related taxable entities from ACORN-affiliated charitable organizations. A memo prepared for ACORN executives, which was provided to us anonymously, confirms the existence of numerous charitable organizations. The memo dated June 19, 2008, details issues regarding governance and commingling of funds, among other things. This memo was prepared by the same attorney who represented ACORN in responding to your letter.

## Tax Status of ACORN and affiliates

Our review of Forms 990 available on Guidestar.org confirmed that 42 tax-exempt organizations have some affiliation with ACORN. Through our review of these Forms 990 as well as our state records and general internet search, we identified 52 other organizations with ties to ACORN.[1]

Many of these 94 organizations are located at one address: 1024 Elysian Fields Avenue, New Orleans, LA 70117. The signage on the building identifies ACORN – Local 100 SEIU as the occupant. See attached picture downloaded from the internet. The number of organizations listed at this address would make this building the equivalent of Ugland House for tax-exempt organizations. This address is used on Forms 990 for 31 of the 42 tax-exempt entities. For the other 52 organizations, this address is the mailing address for 32 and the domicile address for 36.

Another nine tax-exempt organizations are housed in one of two buildings in Brooklyn, NY or at another New Orleans address, 2609 Canal Street. Four of the five addresses that were featured in the investigative videos released in September 2009, were not found in our research.

The 52 taxable entities include Citizens Consulting, Inc. ("CCI"), Elysian Fields Corporation, Inc, Elysian Fields Partnership, and People's Equipment Resource Center. The primary shareholders and partners of these organizations are the Rathke brothers, the original founders of ACORN. We understand that CCI provides consulting services to many, if not all, of the ACORN family of organizations. We also understand that the Elysian Fields entities actually own the ACORN buildings in Louisiana, so all the organizations situated there may be paying rent or other compensation to those for-profit entities. The People's Equipment Resource Center is apparently an equipment and/or administrative services entity whose primary client may be ACORN entities.

Interestingly, we were not able to locate information on the Association of Community Organizations for Reform Now (ACORN) which is apparently the taxable parent organization. ACORN is presumably the taxable entity engaging in the political and lobbying activity.

## Review of ACORN Tax-Exempt Entities

We reviewed the Forms 990 available on Guidestar.org in October 2008, for all 42 tax-exempt organizations for the following:

- exempt purpose and activities furthering that purpose
- primary sources of revenue and primary expenditures
- governance, management and compensation
- transactions and relationships with affiliated organizations

[1] We reviewed an additional 15 organizations for which we were not able to confirm relationships with ACORN.

The attached spreadsheets contain entity specific information on the 42 tax-exempt organizations and the following is a summary of our observations on the four categories listed above.

*Primary Exempt Purpose & Program Service Accomplishments for Tax-Exempt Organizations*
Of the 42 tax-exempt organizations, two are 501(c)(4) social welfare organizations, two are 501(c)(5) labor unions and the remaining 38 are 501(c)(3) charitable organizations. Information about the Primary Exempt Purpose and Program Service Accomplishments are summarized from Forms 990, Part III.

The primary exempt purpose for 20 of the 38 charities appears to be the provision of housing for low and moderate income individuals. While three of the 20 did not state a primary exempt purpose, their purpose was assumed from the name of the organization. It would seem that these 20 organizations are involved in either constructing and acquiring buildings or holding the land on which buildings reside. However, almost all of these organizations repeated their primary exempt purpose for their statement of program service accomplishments. None of these organizations reported any data on the criteria for residence in these properties, the number of individuals or families served, or any other information relevant to understanding how an organization may have accomplished its primary exempt purpose.

The primary exempt purpose of the remaining 18 charities is as follows:

- 11 can be described as research and community organizing, including training and leadership development for community members.
- 5 of the 38 charities can be described as promoting or operating community television or radio stations.
- “fighting pollution in low income and minority neighborhoods in New Orleans through research, training and information dissemination.” (American Environmental Justice Program)
- voter registration and education. (Project Vote)

As with the housing related organizations, most of the 18 other charities also repeated their primary exempt purpose for their statement of program service accomplishments. None of them reported any other information relevant to understanding how an organization may have accomplished its primary exempt purpose.

*Primary Sources of Revenues and Primary Expenditures*
Over half of the 42 tax-exempt organizations have insignificant or zero revenue or expenses. However, there are four ***charitable*** organizations that received over $1 million in direct public support which primarily would consist of charitable contributions and grants. These four also received significant government contributions and program service revenue in the form of contracting fees. These

four also funnel over 50% of their revenues to ACORN affiliates, including the taxable entities ACORN and Citizens Consulting Inc. These four are Project Vote/Voting for America, American Institute for Social Justice (formerly ACORN Institute for Social Justice), ACORN Housing Corporation, and ACORN Institute.

Per its 2006 Form 990, Project Vote received $8,688,580 in direct public support, and $250,759 in contractual fees. It then paid $4,649,037 to ACORN for contractual and campaign services and $779,016 to Citizens Consulting, Inc. Thus, $5,428,023, or over 60% of its revenues, was paid to two taxable, affiliated entities.

Per its 2006 Form 990, the American Institute for Social Justice (AISJ) received over $8,800,000 of revenue, including $8,255,938 of direct public support. Out of a total of $6,659,145 in grants AISJ made, $4,952,288 went to ACORN and $1,696,178 went to “Various Other Affil Organizations” so almost 100% of grants went to ACORN organizations. In addition, AISJ contracted with ACORN for “personnel, contractual” of $566,136.

Per its 2006 Form 990, ACORN Housing Corporation received $4,258,565 in direct public support and $1,700,317 in government contributions. Out of a total of $1,224,850 of grants made, $1,100,152 went to affiliated ACORN organizations, including $846,817 to AISJ. In addition, it paid CCI $309,350 for Admin Services and $58,003 to People’s Equipment Resource Center.

Per its 2006 Form 990, ACORN Institute received $1,276,895 in direct public support and $2,275,182 of government contributions. Out of a total of $1,476,024 of grants made, $1,471,144 went to ACORN affiliated entities. In addition it paid ACORN $501,099, ACORN Services $117,261 and CCI $61,443 for contractual services.

The next two biggest organizations in terms of revenues are the New York Agency for Community Affairs and the New York ACORN Housing Corporation. Both of these organizations also contract with ACORN.

The next two largest organizations in terms of revenue are KNON Radio, a Texas radio station with an address in Louisiana, and ACORN International.

In general, the flow of money among the ACORN family of organizations is a big shell came. Dollars raised for charitable activity appear to be used for impermissible lobbying and political activity. This is similar to the use of charities by Jack Abramoff. Similar to those organizations, charities are being used to raise monies which are then funneled to other charities or other organizations for purposes other than what a donor may have intended.

*Governance, Management, and Compensation*

We compiled and compared the list of officers and directors for all 52 non-exempt organizations with the list of officers and directors from the 42 tax-exempt organizations. Information on the non-exempt organizations is from state incorporation records and information on the tax-exempt organizations is from Forms 990, which also includes compensation information.

There were 24 individuals who were listed as officers or directors of one of the 42 tax-exempt organizations that were also listed as the director of at least one of the non-exempt entities. Interestingly, it appears that, in all of the 42 organizations, only four individuals received compensation as an officer, director or trustee. Mike Shea was an officer of four tax-exempt entities and one non-exempt entity but received compensation from one tax-exempt entity. Carolyn Carr was an officer of one tax-exempt entity and one non-exempt entity and received compensation from the non-exempt entity. Keith Kelleher received compensation from the one and only tax-exempt entity of which he was a director. Ismene Speliotis was an officer of four tax-exempt entities and received compensation from only one of those entities.

The following individuals received no compensation from any of the tax-exempt entities:

- Dorothy Amadi, who was officer for 12 tax-exempt entities;
- Donna Pharr, who was an officer for 27 tax-exempt entities and one non-exempt entity;
- Maude Hurd, who was an officer of 2 tax-exempt entities, 6 non-exempt entities, and the National President of ACORN to whom you wrote in 2006;
- Arlene Kimata, who was an officer of 3 tax-exempt entities and 2 non-exempt entities;
- Donna Massey, who was an officer of 2 tax-exempt entities and 1 non-exempt entity;
- Dale Rathke, who was an officer of 1 tax-exempt entity and 11 non-exempt entities;
- Wade Rathke, who was an officer of 3 tax-exempt entities and 24 non-exempt entities.

The very low levels of officer compensation reported on the 42 Forms 990 suggest that compensation may be disguised in the form of contractual payments for services and that individuals may be receiving significant compensation from the non-exempt entities. For example, we found on ACORN International's Form 990 that Wade Rathke received $94,487 of compensation from the Chief Organizing Fund.

Note that, while the largest four charities by revenue – Project Vote, AISJ, ACORN Housing and ACORN Institute – apparently did not compensate any of its officers or directors, they did make significant payments to tax-exempt and non-exempt ACORN organizations through grants and payments for contractual services.

*Transactions and Relationships with Affiliated Organizations*
We reviewed three specific questions on Form 990 and Schedule A for the 42 tax-exempt organizations.

Eleven of the 42 organizations answered “yes” to Form 990, question 80b. The question asks whether the organization is related (other than by association with a statewide or nationwide organization) through common membership, governing bodies, trustees, officers, directors, etc., to any other exempt or nonexempt organization.

Three of the 42 organizations provided information about taxable subsidiaries and disregarded entities in Form 990, Part IX.

Five of the 42 organizations answered “yes” to Form 990, Schedule A, Part III, question 2. This question asks whether the organization, either directly or indirectly, engaged in certain transactions with substantial contributors, trustees, directors, officers, creators, key employees, or members of their families, or with any taxable organization with which any such person is affiliated as an officer, director, trustee, majority owner, or principal beneficiary.

Note that the majority of organizations that share the address in New Orleans or have a common bookkeeper or treasurer would not be considered related since these would not be criteria that would require a response to any of these three questions. Most of these organizations would likely not meet the definition of related for 990 reporting purposes. Note that payments to the taxable entities for contractual services were reported on Schedule A, under payments to the five highest independent contractors. If those taxable entities – such as the CCI, People’s Equipment Resource Center, Chief Organizing Fund, or the Elysian Fields entities – were not the top five payees, we may not even have had that information.

**<u>IRS Penalties and Excise Taxes</u>**
*Penalties for Criminal Activities*
Aside from an excise tax on excess benefit transactions, which include embezzlement, no penalties or excise taxes apply to tax-exempt organizations participating in or furthering criminal activity.

Tax-exempt organizations could be subject to revocation of tax-exempt status. Reg. 1.501(c)(3)-1(c)(1) states that an organization will not be regarded as operated "exclusively" for IRC 501(c)(3) purposes if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. The presence of a single non-charitable purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly charitable purposes. Better

Business Bureau v. United States, 326 U.S. 279 (1945). Therefore, if an organization engages in illegal acts that are a substantial part of its activities, it does not qualify for exemption under IRC 501(c)(3). In ACORN's case, however, IRS would likely have a high hurdle to clear in order to revoke the tax-exempt status of any of the ACORN tax-exempt entities.

First, it is not clear whether the activities under scrutiny - voter fraud, false tax preparation, child prostitution or human trafficking - were conducted by the tax-exempt entities. Of the five known offices at which the investigators videotaped employees and volunteers, we were only able to verify one of the addresses as being related to a tax-exempt entity. The other four may either be under an organization we have not yet identified or may be an office of one of the 42 organizations.

Second, it is unclear that the level of activity would meet the substantial part test for any one entity. In order to revoke the exemption of any one tax-exempt organization, IRS may need to prove that such activity is the primary activity of that organization.

*Penalties for Electioneering*
Under section 4955, an amount paid or incurred by a section 501(c)(3) organization to participate in, or intervene in, a political campaign for public office is considered a "political expenditure."[2] Section 4955(a) imposes an initial tax on each political expenditure by a section 501(c)(3) organization equal to 10 percent of the amount of the expenditure. In addition, an initial tax equal to 2½ percent of the organization's political expenditures is imposed on any organization manager who agrees to the making of any expenditure, knowing it to be a political expenditure. If the expenditure is not promptly corrected, section 4955(b) imposes an additional tax equal to 100 percent of the political expenditure upon the organization, and an additional tax equal to 50% of the expenditure upon any manager who refuses to agree to the correction.

It is unclear whether IRS could assess section 4955 taxes on any of the ACORN charitable organizations. The charitable organizations are likely to argue that they were primarily engaged in voter registration and voter education, which are both generally permissible activities as long as such activities are generally non-partisan. Charities are not allowed to endorse candidates or campaign for them. In this case, it appears that the charitable entities were contracting out voter registration and voter education activities to taxable entities such as ACORN and Citizens Consulting, Inc. It is not clear whether such contractual payments would be deemed political expenditures.

*Form 990 Penalties*
Penalties exist for not filing a Form 990 or for filing an incomplete return. IRS rarely imposes incomplete return penalties and most likely does not impose

[2] I.R.C. § 4955(d)(1).

penalties for the failure to explain how charitable expenditures further an organization's exempt purpose. In addition, IRS frequently abates failure to file and incomplete return penalties.

**Proposals for Reform**

Impose a new excise tax on managers when pervasive criminal activity is conducted by employees or volunteers of an organization that are acting in their capacity as an employee or volunteer.

Allow IRS to suspend tax-exempt status of an organization when there is significant evidence of criminal activity conducted by employees or volunteers of an organization that are acting in their capacity as an employee or volunteer.

Clarify that incomplete return penalties would apply for failing to report how activities further charitable purpose.

Impose expenditure responsibility requirements similar to those imposed on private foundations to ensure that grants made by public charities are dedicated to charitable purposes.

Clarify that IRS 4955 political expenditures tax would apply to grants that are ultimately used for political purposes.

Require public disclosure of non-individual donors. This is similar to a recommendation that the majority staff, then minority staff, made in its report regarding Abramoff tax-exempt organizations.

Require consolidated Form 990 reporting, in addition to individual entity reporting, so that information about all affiliates is available in one location.

Ensure that volunteer preparers are subject to certain return preparer standards.