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TAX EXEMPT AND GOVERNMENT ENTITIES DIVISION

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

Date: May 14, 2004

UIL: 501.00-00

Contact Person:

Identification Number:

Telephone Number:

Employer Identification Number:

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we conclude that you do not qualify for exemption under that section. Moreover, you do not meet the requirements necessary for recognition of exemption under section 501(c)(4). The basis for our conclusion is set forth below.

You were incorporated in the state of on Your Articles of Incorporation state the following:

." You further represent, in your Form 1023, Application for Recognition of Exemption (Application), that you were

You indicated in your letter of April 9, 2003, that was principally responsible for the formation of your organization "in order to expand and improve the services available to such needy persons." served for a number of years, on a voluntary basis, as the President and a director of , another credit counseling organization. He selected and recruited the initial members of your board of directors. You further indicated in your August 9th letter that has taken a salaried position with another credit counseling agency, as Executive Director at a salary of $ per year but will continue to contribute his experience

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to you on a voluntary basis. . has been intimately involved in submitting the additional information we requested to support your Application.

Your current board of directors consists of President/Director and Vice President/Secretary/Director. They were selected by and have served since your incorporation. is a business executive with a background in personnel management and has a background in billing for the medical industry. Your letter of October 2, 2002, indicates that "The compensation for the executive director, anticipated at $ per year, will be set by the Board of Directors. The compensation for other staff will be set by the executive director within ranges approved by the Board of Directors." You projected that your CEO's salary will likely be in the range of $ $. per year. In your Application, you projected salaries for a maximum of high school graduate credit counselors and clerical employees at $. and $. for the years . and You stated in response to our letter dated October 3, 2003, that anticipates paying its budget counselors a starting salary of approximately $ per annum and paying its administrative aides somewhat less."

You stated in your letter of October 2, 2002, " budget plan services will be limited to those who might otherwise have to declare bankruptcy. These are generally those who have substantial debt, are incurring late fees and penalties, and do not have access to home equity or other sources of financing." That you will not restrict your services to low-income individuals and families is reflected in your letter of October 2, 2002, however, where you state: ' does not anticipate initially considering any income guidelines or criteria when evaluating applicant [sic] for its credit counseling services, since estimates that more than two-thirds of its clients will qualify as low income according to the Lower Living Standard Income Level developed by the Secretary of Labor under Title I of the Workforce Investment Act of 1998 (Public Law 105-220). expects that substantially all of the remainder will be middle income individuals and families."

In response to our questions as to how you plan to service clients enrolled in your budget plan program, you submitted a proposed, unexecuted contract, to be effective as of ' with Inc., a for-profit company located in . The agreement provides the following: "Whereas, , provides fulfillment, back-office, and customer relations services for budget plan clients of debt counseling companies and desires to provide such services for Agency's budget plan clients; Whereas, Agency, a debt counseling company, desires to retain to perform fulfillment, back-office, and customer relations services for its budget plan clients." The agreement provides that obligations to you would include: "(i) preparing a proposal to creditors reflecting the budget plan approval by the client; (i) communicating the proposal to the creditors; (iii) negotiating with the creditors on necessary or appropriate changes in the proposal; (iv) obtaining the client's approval to any changes in the budget plan negotiated with the creditors; (v) receiving, depositing, and disbursing client budget plan payments; (vi) negotiating with clients any claims from clients for refunds and disbursing refunds; (vi) receiving and remitting to Agency all direct fair share contributions from creditors, and (vii) responding promptly to client inquiries regarding disbursements and balances." The agreement also states that with regard to fair share shall diligently solicit fair share from all creditors. . shall deposit creditors fair share contributions in Agency's fair

share accounts no later than the business day following the business day of receipt."

Under the agreement, you would pay the following: "(i) a one-time fee of ($ (sic) per new budget plan client (ii) a fee of per budget plan client per month for each client for whose account Americorp received or made a budget plan payment during the course of the month (iii) reimbursements of all disbursement by for postage, check printing, agency letterhead and envelopes, and related items including costs associated with all methods of receiving and transmitting client payments." The agreement also provides the following: "Agency shall maintain, and aford, full access to, one [or] more accounts for the deposit of budget plan payments from clients, the disbursement of funds, if any, to clients, and the disbursement of payments to creditors. Any interference with access to such account(s) shall represent a substantial breach of this Agreement entitling to terminate this Agreement and/or recover liquidated damages (and not a penalty) of %) of the amount of the check or withdrawal." Thus, it appears that you intend for to perform all services related to your debt management program, other than intake and "counseling services." In a letter dated August 19, 2003, you stated that you prefer because offers the advantage of a quarterly analysis of client profiles, 24-hour client customer service access, and a significant lower client hold time for personal technical assistance. Attached is a copy of the service contract proposed by in You stated that the only other outside vendors you contacted were and

You have represented that the vast majority of your revenue (at least 90%) will be derived from clients enrolled in your budget plan program. As part of your program, youwill inform clients of the availability of the program, which would allow clients to enter into a debt management plan (DMP) with creditors. In the client contract you submitted, in the first paragraph, on behalf of the client you state that you provide "debt management and counseling services in negotiating a repayment plan with my creditors." This statement implies that your services are supplied only in the context of debt management plans. The client contract provides warnings that negotiation of a DMP can take up to 120 days; if the client fails to make required payments during this period, his credit standing can be impaired. There is a disclaimer of responsibility for any negative consequences on the client's credit record for entering into a DMP. The contract also states that the client may be referred to other entities for debt consolidation loans. Your April 9th letter indicates, however, that you do not anticipate that any clients will be referred for a debt consolidation loan through or through you.

With regard to what clients will pay to participate in the program, your Application states that "each client will be requested, when it (sic) signs up for the budget plan service, to make voluntary commitment to pay periodic fees to to help defray the costs of the service. will be suggesting a payment of $ per creditor per month, with a minimum suggested payment of $ and a maximum suggested payment of $ per client." You further stated the following: "In addition, all clients, whether or not they participate in the budget plan program, will be requested to help defray costs through a one-time, initial payment of 3% of their outstanding indebtedness. As with the monthly budget plan, such a payment will be strictly voluntary, and no one will be denied any service to failing to make any payment. expects, however, that % of clients will make some level of payment." In

an undated letter to the Service you stated that "about % of those who enroll in a debt management plan will make the full suggested initial and monthly payments."

Proposed financial information provided in your Application, shows that for and you will receive "voluntary payments from clients (initial) and monthly" amounting to $, $ and $, in each respective year. While you may consider these payments as "voluntary" in nature, we view them as fees received in exchange for the sale of program-related services. Although you represented to the Service that you will not withhold assistance to clients if they do not wish to make such a contribution, you have provided no documentation that supports this claim. As to the length of time a debtor would be enrolled in a DMP, you stated in a letter in response to our letter of October 3, 2003, that "Consumer enrolled on debt management plans will require on average five years enrollment to pay off their debts." You have presented no data indicating the number of clients you expect to enroll during or However, the amount of revenue you expect to receive strongly suggests that you anticipate significant numbers of clients to enroll in DMPs. Moreover, given the large number of clients you expect to serve, it would appear difficult for your staff to provide much more than DMP intake type services.

In material describing your DMP program to potential clients, you make the following representation: "Our Certified Account Specialists offer you personal, one-on-one counseling and are ready to answer any questions you have regarding our services. Having your very own Account Specialist to represent you is a tremendous asset-he/she will shield you from your creditors and deal directly with each of them until your debts are paid off." You further stated, as regards the Account Specialist: "He/she will review your financial situation and answer all of your questions and concerns. This experienced Account Specialist will represent and guide you every step of the way-from beginning to end of the Program. You can call anytime, day or night. Our friendly counseling and customer service is second to none." You also provided material in which you made the following statements: "

" You have also represented that you will intercede on behalf of clients, with creditors to try to persuade them to accept partial payments in satisfaction of debt. It is common in this industry for creditors to publish in advance the adjustments they will allow debtors enrolled in DMPs. Generally, these terms are not subject to negotiation.

Financial information submitted with your Application indicates that your secondary source of revenue will come from the "fair share" program. As was previously discussed, any fair share program you participate in would be administered by an outside source, such as With regard to fair share revenue, you stated in your Application "All payments from creditors will be strictly voluntary, and will work as readily to reorganize debts for clients with creditors that do not make any such payments. understands that approximately half of all creditors can be expected to make a so-called "fair share" payment to of %- % of each monthly remittance made." Proposed financial information in your Application, shows that for and you will receive "fair shares" from creditors amounting to $ $ and $ in each respective year. As in the case of fees paid by clients enrolled in your DMPs, we view fees paid to you through "fair share" to be in the nature of payments for

program-related services. Though you claim you will even work with creditors who do not pay a "fair share", you have provided no documentation that supports this claim and you clearly have more of an incentive to work with creditors who pay a "fair share."

With regard to your counseling activities, you represented in your Application that once you develop a full clientele you will increase your time, effort, and resources dedicated to counseling activities from % up to %. You stated that you will employ full-time budget counselors. These counselors will be paid a starting salary of $ You further stated in response to our letter dated October 3, 2003, that with regard to qualifications: will seek individuals with financial services experience." You also stated that: ". counselors will become certified as credit counselors by the National Institute For Financial Counseling Education, a private, independent credentialing body, within ninety days of being hired." As to how your counselors are to be evaluated, you stated: "The financial counselors will be evaluated based upon the extent to which they are providing client satisfaction. Factors considered will include courteousness, flexibility, knowledge, and productivity measured by the numbers and quality of client interactions satisfactorily concluded. Evaluations will be made by monitoring telephone calls and meetings and by conducting anonymous client satisfaction surveys." You stated that counselors will not be eligible for any bonuses. However, counselors will receive in-step and position promotions based in part upon their evaluations.

With respect to actual counseling sessions, your Applicationstates the following: "For most clients, the first, and often only contact with will consist of one or more counseling [sessions] in person or over the telephone. Individuals and families referred to will receive personalized advice, from trained financial consultants, on budgeting and the appropriate use of consumer credit. They will also receive copies of the public information materials." You also stated that counselors will be expected to complete a preliminary client profile for each consumer. Consumers will be directed to your website for additional information. If the client has no internet access, brochures will be mailed without charge. If the consumer wishes to consider the possibility of enrolling in a DMP, your counselors will send a debt management plan and budget worksheets with instructions for completion.

With regard to the amount of time spent with a client, you stated the following: "It is anticipated that counselors will spend an average of **twenty minutes** (emphasis added) in total counseling each consumer who does not enroll in a debt management plan and **thirty minutes** (emphasis added) with each consumer who does." You further stated the following: "The participants in the workshops and in the one-on-one budget counseling sessions will be self-selected. They are likely to be people having numerous creditors and experiencing serious debt problems. No criteria will be utilized other than a willingness to attend the workshops and counseling sessions and, in the case of the counseling sessions, a willingness and ability to complete a financial questionnaire." You have not provided information indicating the number of people you expect to attend these counseling sessions; and, have not provided information indicating the amount of time spent by a counselor, with an individual client, in credit education versus the time spent in soliciting, enrolling, and referring a client to your debt management program. Although you give clients copies of public information materials, you do not explain when, where, or how, these materials are to be used by your counselors in formal counseling sessions with clients.

With regard to the materials used for training your employees, they concentrate and focus on preparing counselors on how best to persuade a potential client to consider enrolling in a DMP. Your Application includes employee training materials that contain some educational material, including a 26-page document captioned: "The materials below will be used to formulate the above outline into a full training manual." There is an outline of a two-week training program, in which a prospective employee spends 2 days of the first week and the entire second week observing and being coached by experienced credit counselors. The outline contains the following statement "Counselors are given marketing materials that are used to promote the...debt management program. This gives the counselor an idea of how we promote the service to consumer."

You stated in your Application, that you will also attempt to educate the general public on credit matters through preparing videos, pamphlets, and other educational materials and conducting workshops. Your Application indicates that you do not "currently anticipate charging any fees for its public information or workshop services, although voluntary donations for the workshops (not exceeding $ per session) may be solicited." You stated that, apart from free distribution of brochures, you will charge fair market value for any additional materials. You have not provided substantial details on how you would use videos, pamphlets and other educational materials to educate the general public on credit issues. Moreover, you have not provided information detailing how your workshops would be conducted including when, where, subjects to discussed, and the number of people you expect to attend.

Your proposed budgets for and , show anticipated revenues from creditors and debtors. In you anticipate receiving $ in income. Of this amount you will expend $ in office expenses, and $ in processing cost. In you anticipate $ income. Of this amount you will expend $ in office expenses, and $ in processing cost. In you anticipate $ in income. Of this amount you will expend $ in office expense, and $ in processing cost. Your budgets do not show how you anticipate spending the excess revenues in each year. Notwithstanding the lack of specificity, you have submitted information leading us to conclude that you will be spending substantial funds on advertising and lead purchases and development. You indicate that you will place advertisements in the telephone yellow pages and other local media. You will also seek referrals from internet financial sites, publicize your services through financial and budgetary workshops, and eventually develop your own website. Your budgets do not show any expenditures for educational activities or programs.

You indicated on your Application that you are described in section 509(a)(2) of the Code. In the event we determined that you were otherwise exempt under section 501(c)(3), this would be an appropriate foundation classification because you have shown that your primary sources of revenue will be, primarily if not exclusively, from fees charged to debtors and creditors who participate in your debt management program. You have not shown that you intend to raise any revenue from public contributions.

Section 501(c)(3) of the Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the

net earnings of which inures to the benefit of any private shareholder or individual.

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations provides that, 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(b)(1)(i) of the regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization:

(a) Limit the purposes of such organization to one or more exempt purposes; and
(b) Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities that in themselves are not in furtherance of one or more exempt purposes.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that 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(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(a)-1(c) defines the words "private shareholder or individual" in section 501 to refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations provides that an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. Thus, to meet the requirements of this subsection, 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(d)(2) of the regulations provides that the term "charitable" is used in section 501(c)(3) of the Code in its generally accepted legal sense and includes relief of the poor and distressed or of the under privileged as well as the advancement of education.

Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term "educational" refers to:

(a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
(b) The instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e)(1) of the regulations provides that 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 purposes of carrying on an unrelated trade or business.

In Rev. Rul. 69-441, 1969-2 C.B. 115, the Service found that a nonprofit organization formed to help reduce personal bankruptcy by informing the public on personal money management and aiding low-income individuals and families with financial problems was exempt under section 501(c)(3) of the Code. Its Board of Directors was comprised of representatives from religious organizations, civic groups, labor unions, business groups, and educational institutions.

The organization provided information to the public on budgeting, buying practices, and the sound use of consumer credit through the use of films, speakers, and publications. It aided low-income individuals and families who have financial problems by providing them with individual counseling, and if necessary, by establishing budget plans. Under the budget plan, the debtor voluntarily made fixed payments to the organization, which held the funds in a trust account and disbursed the funds on a partial payment basis to the creditors. The organization did not charge fees for counseling services or proration services. The debtor received full credit against his debts for all amounts paid. The organization did not make loans to debtors or negotiate loans on their behalf. Finally, the organization relied upon voluntary contributions, primarily from the creditors participating in the organization's budget plans, for its support.

The Service found that, by aiding low-income individuals and families who have financial problems and by providing, without charge, counseling and a means for the orderly discharge of indebtedness, the organization was relieving the poor and distressed. Moreover, by providing the public with information on budgeting, buying practices, and the sound use of consumer credit, the organization was instructing the public on subjects useful to the individual and beneficial to the community. Thus, the organization was exempt from federal income tax under section 501(c)(3) of the Code.

Rev. Rul. 71-529, 1971-2 C.B. 234, held that a nonprofit organization providing assistance in the management of participating colleges' and universities' endowment or investment funds for a charge substantially below cost qualified for exemption under section 501(c)(3) of the Code. Most of the operating expenses of the organization, including the costs of the services of the investment counselors and the custodian banks, were paid for by grants from independent charitable organizations. The member organizations paid only a nominal fee for the services performed. These fees represented less than 15 percent of the total costs of the operation. By performing these services for a charge substantially below its cost, the organization was performing a charitable activity for purposes of section 501(c)(3) of the Code.

Rev. Rul. 72-369, 1972-2 C.B. 245, held that an organization formed to provide managerial and consulting services at cost to unrelated exempt organizations did not qualify for exemption under section 501(c)(3) of the Code. 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 were provided at cost and solely for exempt organizations was not sufficient to characterize the activity as charitable for purposes of section 501(c)(3) of the Code. "Furnishing the services at cost lacks the donative element necessary to establish this activity as charitable."

Rev. Rul. 76-244, 1976-1 C.B. 155 ,,held that home delivery of meals to the elderly free or with charges on a sliding scale, depending on recipients' ability to pay, is a charitable purpose.

Rev. Rul. 78-99, 1978-1 C.B. 152, held that the provision of individual and group counseling for widows based on their ability to pay is an educational activity.

Rev. Proc. 84-36, 1984-1 C.B. 541, provides in part, that exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere statement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned, and the nature of the contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, a record of actual operations may be required before a ruling or determination letter will be issued.

An organization must establish through the administrative record that it operates as a section 501(c)(3) organization. Denial of exemption may be based solely upon failure to provide information describing in adequate detail how the operational test will be met. American Science Foundation v. Commissioner, T.C. Memo. 1986-556; La Verdad v. Commissioner, 82 T.C. 215, 219 (1984); Pius XII Academy v. Commissioner, T.C. Memo. 1982-97. Exempt status can be recognized in advance of operations if proposed operations can be described in enough detail to permit a conclusion that the organization will clearly meet the requirements of section 501(c)(3). American Science Foundation v. Commissioner, T.C. Memo. 1986-556.

In Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purposes, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes.

In The Founding Church of Scientology v. U.S, 188 Ct. Cl. 490, 506 (1969), the Court of Claims found as a damaging fact that one of the reasons Scientology was organized as a religion was to evade regulation, as one state was investigating Scientology for operating a medical school without a license.

In Consumer Credit Counseling Service of Alabama, Inc. v. United States 78-2 U.S.T.C. 9660 (D.D.C. 1978), the court held an organization that provided free information on budgeting, buying practices, and the sound use of consumer credit qualified for exemption from income tax because its activities were charitable and educational.

The Consumer Credit Counseling Service, which has been recognized as exempt under section 501(c)(3) in a group ruling, is an umbrella organization made up of numerous credit counseling service agencies. In this case, these agencies provided information to the general public through the use of speakers, films, and publications on the subjects of budgeting, buying practices, and the sound use of consumer credit. They also provided counseling on budgeting and the appropriate use of consumer credit to debt-distressed individuals and families. They did not limit these services to low-income individuals and families, but they provided such services free of charge. As an adjunct to the counseling function, they offered a payment plan. Approximately 12 percent of a professional counselor's time was applied to the payment activity as opposed to an educational activity. Moreover, the agencies only charged a nominal fee of up to $10 per month for this service.. This fee was waived in instances when payment of the fee would work a financial hardship.

The agencies received the bulk of their support from government and private foundation grants, contributions, and assistance from labor agencies and the United Way. An incidental amount of their revenue was from counseling fees. In 1974, the Service ruled that each of the agencies constituted organizations described in section 501(c)(3). However, two years later, the Service notified the agencies that it had made a mistake and was reclassifying them under section 501(c)(4). The reasons given by the Service for revocation of section 501(c)(3) were that: (1) the agencies were not organized and operated exclusively for charitable or educational purposes; (2) the debt management service is not limited to low-income individuals or families; and (3) fees are charged for the services rendered.

The court did not agree with the Service and directed verdicts for the plaintiff. Providing information regarding the sound use of consumer credit is charitable because it advances and promotes education and social welfare. These programs were also educational because they instructed the public on subjects useful to the individual and beneficial to the community. The counseling assistance programs were likewise charitable and educational in nature. Because the community education and counseling assistance programs were the agencies' primary activities, the agencies were organized and operated for charitable and educational purposes. The limited debt management and creditor intercession activities were an integral part of the agencies' counseling function, and thus were charitable and educational undertakings. Even if this were not the case, these activities were incidental to the agencies' principal functions.

Finally, the court found that the law did not require that an organization must perform its exempt functions solely for the benefit of low-income individuals to qualify under section 501(c)(3). Nonetheless, the agencies did not charge a fee for the programs that constituted their principal activities. A fee may be charged for a service that was an incidental part of an agency's function, but even when a fee was so charged, it was nominal. Moreover, even this nominal fee was waived when payment would work a financial hardship. Thus, the court ordered that "each of the plaintiff consumer credit counseling agencies was an organization described in section 501(c)(3) as a charitable and educational organization." See also, Credit Counseling Centers of Oklahoma, Inc. v. United States, 79-2 U.S.T.C. 9468 (D.D.C. 1979), in which the facts were virtually identical and the law was identical to those in the case styled Consumer Credit Counseling Centers of Alabama, Inc. v. United States discussed immediately

above. Thus, the court ordered that the consumer credit counseling agencies were described in section 501(c)(3) as charitable and educational organizations.

In B.S.W. Group, Inc. v. Commissioner, 70 T.C. 352 (1978), the court found that a corporation formed to provide consulting services was not exempt under section 501(c)(3) because its activities constituted the conduct of a trade or business that is ordinarily carried on by commercial ventures organized for profit. Its primary purpose was not charitable, educational, nor scientific, but rather commercial.

The court found that the corporation had completely failed to demonstrate that its services were not in competition with commercial businesses. The court found that the organization's financing did not resemble that of the typical 501(c)(3) organization. It had not solicited, nor had it received, voluntary contributions from the public. Its only source of income was from fees from services, and those fees were set high enough to recoup all projected costs, and to produce a profit. Moreover, it did not appear that the corporation ever planned to charge a fee less than "cost." And finally, the corporation had failed to limit its clientele to organizations that were section 501(c)(3) exempt organizations.

The Court in est of Hawaii v. Commissioner, 71 T.C. 1067 (March 28, 1979) found that an organization formed to educate people in Hawaii in the theory and practice of "est" was a part of a "franchise system which is operated for private benefit," and therefore may not be recognized as exempt under section 501(c)(3) of the Code. The applicant for exempt status was not formally controlled by the same individuals controlling the for-profit organization owning the license to the est body of knowledge, publications, methods, etc. However, the for-profit exerted "considerable control" over the applicant's activities by setting pricing, the number and frequency of different kinds of seminars and training, and providingthe trainers and management personnel who are responsible to it in addition to setting price for the training. The court found that the fact that the applicant's rights were dependent upon its tax-exempt status showed the likelihood that the for-profit corporations were trading on that status. The question for the court was not whether the payments made to the for-profit were excessive, but whether it benefited substantially from the operation of the applicant. The court determined that there was a substantial private benefit because the applicant "was simply the instrument to subsidize the for-profit corporations and not vice versa and had no life independent of those corporations.

In P.L.L. Scholarship v. Commissioner, 82 T.C. (1984), an organizationoperated bingo at a bar for the avowed purpose of raising money for scholarships. The board included the bar owners, the bar's accountant, also a director of the bar, as well as two players. The board was self-perpetuating. The court reasoned that, because the bar owners controlled the organization and appointed the organization's directors, the activities of the organization could be used to the advantage of the bar owners. The organization claimed that it was independent because there was separate accounting and no payments were going to the bar. The court was not persuaded.

> A realistic look at the operations of these two entities, however, shows that the activities of the taxpayer and the Pastime Lounge were so interrelated as to be functionally inseparable. Separate accountings of receipts and disbursements do not change that fact.

The court went on to conclude that, because the record did not show that the organization was operated for exempt purposes, but rather indicates that it benefited private interests, exemption was properly denied.

In St. Louis Science Fiction Limited v. Commissioner, T.C. Memo 1985-162, April 2, 1985, the Court reviewed the annual convention of a science fiction organization. It held that while the conventions may have provided some educational benefit to some of the individuals involved, that social and recreational purposes, and private benefit predominated. The Court distinguished Goldsboro Art League, Inc. v. Commissioner, 75 T.C. 337 (1980) in which the organization provided public art education by using juries to insure artistic quality and integrity.

> Petitioner relies heavily upon Goldsboro Art League, Inc. v. Commissioner, 75 T.C. 337 (1980), in support of its contention that it is tax-exempt. In Goldsboro Art League, the taxpayer was an organization that operated two art galleries that exhibited and sold artworks. We held that the taxpayer was tax-exempt under section 501(c)(3) because it was organized and operated exclusively for an exempt purpose--art education. We noted that in order to insure artistic quality and integrity, the artworks displayed were selected by jury procedures. We also noted that the taxpayer was the only such museum or gallery within its county, or any contiguous county. We held that it served public, rather than private interests and that its sales activities were incidental to advancing its exempt purpose. By contrast, petitioner in this case did not apply any controls to insure the quality of the books and artworks sold at its convention. Also, the tone of petitioner's convention is substantially, if not predominantly, social and recreational, rather than educational. In addition, petitioner's huckster's room and art auction provided substantial benefit to private interests that is not incidental to its exempt purpose. Consequently, we think the case Goldsboro Art League is clearly distinguishable on its facts from the instant case.

In Church By Mail, Inc. v. Commissioner, T.C. Memo 1984-349, *aff'd* 765 F. 2d 1387 (9th Cir. 1985) the tax court found that a church was operated with a substantial purpose of providing a market for an advertising and mailing company owned by the same people who controlled the church. The church argued that the contracts between the two were reasonable, but the Court of Appeals pointed out that "the critical inquiry is not whether particular contractual payments to a related for-profit organization are reasonable or excessive, but instead whether the entire enterprise is carried on in such a manner that the for-profit organization benefits substantially from the operation of the Church."

In Easter House v. United States, 846 F. 2d 78 (Fed. Cir. 1988), aff'g 12 Cl. Ct. 476 (1987), 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 ofthe adoption activity was a non-exempt commercial purpose. It found that the adoption services did not further the exempt purposes of providing educational and charitable services to the unwed mothers and children. Rather, the services for unwed mothers and children were merely provided "incident" to the organization's adoption service business. Moreover, the court found that "adoption services do not in of themselves constitute an exempt purpose."

The court agreed with the IRS' determination that the agency operated in a manner not "distinguishable from a commercial adoption agency." First, the agency's operation made substantial profits, and there was a substantial accumulation of capital surplus in comparison to direct expenditures by the agency for charitable and educational purposes. Second, the agency's operation was funded completely by substantial fixed fees charged adoptive parents. It relied entirely on those fees and sought no funds from federal, state or local sources, nor engaged in fund raising programs, nor did it solicit contributions. In fact, the agency had no plans, nor intention to seek contributions, government grants or engage in fund raising relative to its operations. Third, the fixed fees the agency charged adoptive parents were not subject to downward adjustment to meet potential adoptive parents' income or ability to pay. Fourth, the agency's membership was organized into classes of memberships, single life member, member and ordinary member. And fifth, the agency functions by means of a paid staff of 15 to 20 persons, with no volunteer help.

In International Postgraduate Medical Foundation v. Commissioner, T.C. Memo 1989-36, the court found an organization that ran tours aimed at doctors and their families was operated to benefit the private interests of an individual who controlled the organization and a for-profit travel agency (H&C Tours) that handled all of its tour arrangements.

The organization used the H&C Tours exclusively for all travel arrangements. There was no evidence that the organization solicited competitive bids from any travel agency for travel arrangements for its tours other than H&C Tours. The organization physically located its office within the offices of H&C Tours, which provided it secretarial, clerical, and administrative personnel for a fee equal to H&C Tours' costs. The organization spent 90 percent of its revenue on travel brochures prepared to solicit customers for tours arranged by the travel agency. The brochures emphasized the sightseeing and recreational component of the tours, but did not describe the medical curriculum for the seminars and symposia that was the basis for exemption. Educational activities occurred on less than one-half of the days on a typical tour.

The court found that a substantial purpose of the organization's operations was to increase the income of H&C Tours. The president of H&C Tours controlled the organization and exercised that control for the benefit of H&C Tours. Moreover, the administrative record supported the finding that the organization was formed to obtain customers for H&C Tours.

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 an organization conducted its activities, courts have found that an organization 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."

The court maintained that, if private individuals or for-profit entities have either formal or effective control of a non-profit organization, it was presumed that the organization furthered the

profit-seeking motivations of those private individuals or entities. This was the case, even when the organization was a partnership between a non-profit and a for-profit entity. (citing Redlands Surgical Services v. Commissioner, 113 T.C. 47 (1999)).

The Credit Repair Organizations Act ("CROA"), 15 U.S.C. section 1679 et seq., effective April 1, 1997, imposes restrictions on credit repair organizations, including forbidding the making of untrue or misleading statements and forbidding advance payment, before services are fully performed. 15 U.S.C. section 1679b. Section 501(c)(3) organizations are by definition excluded from regulation under the CROA. The CROA defines a credit repair organization as:

(A) any person who uses any instrumentality of interstate commerce or the mails to sell, provide, or perform (or represent that such person can or will sell, provide, or perform) any service, in return for the payment of money or other valuable consideration, for the express or implied purpose of—

(i) improving any consumer's credit record, credit history, or credit rating, or
(ii) providing advice or assistance to any consumer with regard to any activity or service described in clause (i).

15 U.S.C. section 1679a(3). The courts have interpreted this definition broadly to apply to credit counseling agencies. The Federal Trade Commission's policy is that if an entity communicates with consumers in any way about the consumers' credit situation, it is providing a service covered by the CROA. In Re National Credit Management Group, LLC, 21 F. Supp. 2d 424, 458 (N.D.N.J. 1998).

In FTC v. Gill, 265 F.3d 944 (9th Cir. 2001), aff'g 183 F. Supp. 2d 1171 (2001), the appellate court inferred that a credit repair organization that first promised a "free consultation," but charged fees in advance of the full performance of services was being subsequently operated as a charity primarily for purposes of evading regulation under the CROA.

In Credit Counseling Centers v. S. Portland, 814 A.2d 458 (S. C. Me. 2002), the Supreme Court of Maine denied state tax exemption to a credit counseling agency that provided significant benefits to creditors. Credit card companies commonly make payments to credit counseling agencies of a portion of the funds they receive from clients of the agencies. These payments are known as "fair share" payments and are a source of substantial funding for credit counseling agencies. In this case, the credit counseling agency received 60 percent of its income from "fair share" payments from credit card companies, at the rate of 8.5% to 9% of debt payments.

Businesses are prohibited from cold-calling consumers who have put their phone numbers on the National Do-Not-Call Registry, which is maintained by the Federal Trade Commission ("FTC"). Nonprofit organizations are not subject to this rule. This registry was created by rules promulgated by the FTC and the Federal Communications Commission. See 16 C.F.R. section 310.4(b)(1)(iii)(B); 47 C.F.R. section 64.1200(c)(2).

Section 501(c)(4) of the Code describes, in relevant part, civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare.

Section 1.501(c)(4) of the regulations provides that an organization may be exempt as an organization described in section 501(c)(4) if it is not organized or operated for profit and is operated exclusively for the promotion of social welfare.

Section 1.501(c)(4)-1(a)(2) of the regulations provides, in relevant part, 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 an general welfare of the people of the community. An organization embraced within this section is one, which is operated primarily for the purpose of bringing about civic betterments and social improvements. An organization is not operated primarily for the promotion of social welfare if its primary activity is carrying on a business with the general public in a manner similar to organizations, which are operated for profit.

In Rev. Rul. 65-299, 1965-2 C.B. 165, the Service recognized a credit counseling service (agency) open to the general public as exempt under section 501(c)(4) of the Code. The agency was incorporated as a nonprofit corporation to assist families and individuals with financial problems and to help reduce the incidence of personal bankruptcy. The Service maintained that the objective and activities of the agency contribute to the betterment of the community as a whole. The agency did not limit its services to those in need of such assistance as proper recipients of charity.

The agency employed specialists to interview applicants who are in financial difficulty, analyze the specific problems involved, and counsel on the payment of their debts. It arranged a monthly distribution to creditors on the debtor's ability to pay. Moreover, it communicated with creditors and, with the creditors' consent, set up plans that applicants agree to follow. It made its facilities available for debtors to make their monthly pro rata distributions to creditors. It made no loans to the applicants or negotiated on their behalf. It charged nominal fees for monthly prorating services, but charged no fees for the counseling services. The organization relied upon voluntary contributions from local businesses, lending agencies, and labor unions to cover its cost of operations.

Based on our analysis of the information provided in your Application and supporting documentation, we have concluded that while you are organized for charitable purposes you are not properly operated under section 501(c)(3) of the Code. You fail the operational test for a number of reasons. You have failed to establish that you are or will be operated for either a charitable or educational purpose. In fact, your file demonstrates that you operate for the substantial non-exempt purpose of operating a business. Another non-exempt purpose appears to be your operation to avoid regulation under the CROA. In addition, you have not shown that your income does not inure to any private individual. In addition, you have not shown that your operations will be exclusively charitable and educational rather than for the substantial private benefit of the company that processes your DMPs (or similar back-end service provider), its shareholders or managers or others with whom you conduct business. Finally, you also substantially benefit the credit card companies to whom your clients owe money because you function as a collection agent for those companies.

An organization seeking exemption must establish that it operates as a section 501(c)(3) organization. Denial of exemption may be based solely upon failure to provide information describing in adequate detail how the operational test will be met. Revenue Procedure 84-36, 1984-1 C.B. 541; American Science Foundation v. Commissioner, T.C. Memo. 1986-556; La Verdad v. Commissioner, 82 T.C. 215, 219 (1984); Pius XII Academy v. Commissioner, T.C. Memo. 1982-97.

Rev. Proc. 84-36, requires an applicant to submit sufficient information during the application process for the Service to conclude that the organization is in compliance with the organizational and operational requirements of section 501(c)(3) before it must issue a ruling. You failed to fully describe your activities as relates to the number of clients you expected to enroll in DMPs during and . the provision of proof that your counselors/account specialists are in fact certified and experienced as represented in some of your materials provided to clients; substantial evidence that you will meet with clients on a regular, systematic basis to provide substantive counseling in credit matters; substantial evidence detailing how your workshops would be conducted including when, where, subjects to be discussed, and number of people you expect to attend.

Moreover, you failed to provide information as to the location of your facilities, including a lease agreement; failed to provide detailed income guidelines for potential clients; failed to provide tapes or scripts to be used by your counselors/account specialists; failed to provide a copy of a typical DMP plan; failed to provide an executed contract with or some other selected service provider; failed to provide a detailed "breakdown" of your processing costs, including the name of the company, and your basis for paying the amounts you would pay in processing costs; failed to provide a copy of all agreements with companies other than that you would purchase services from or perform services for, failed to provide a copy of the comparability study used to determine client fees, including the monthly DMP and one-time % fees; and failed to provide a detailed description of employment and educational history of each of your employees, including administrators.

Because you failed to provide the requested information, you have not fully described the activities in which you expect to "engage, including the standards, criteria, procedures, or other means adopted or planned." See Rev. Proc. 84-36, supra. Thus, in accordance with the revenue procedure and the previously mentioned Tax Court cases, you have failed to provide sufficient information to adequately detail how you will satisfy the operational test. The Service may decline to issue a favorable ruling under these circumstances.

While you have not submitted sufficient information to support a favorable ruling, you have submitted sufficient information to conclude that the activities you plan to engage in will fail to meet the requirements of the organizational test for the reasons explained below.

You state in your Application that your primary purposes include "(a) providing information to the general public on sound money management; (b) counseling individuals and families who have serious financial difficulties; and (c) preparing budget plans for those needy individuals and families who can benefit from them." Providing individual counseling to clients on credit matters

may be educational or, if provided in a charitable manner, may be charitable within the meaning of section 501(c)(3). See, e.g., Rev. Rul. 78-99, 1978-1 C.B. 152 (individual and group counseling for widows based upon their ability to pay is an educational activity). You have not submitted sufficient documentation, however, that the counseling you do is either charitable or educational in the sense recognized by the law.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as operating exclusively for exempt purposes only if it engages primarily in activities that accomplish one or more of the exempt purposes specified in section 501(c)(3) of the Code. Providing services exclusively for the benefit of the poor, a recognized charitable class, furthers charitable purposes. For instance, counseling the poor about economics and personal finance can achieve an exempt purpose. See Rev. Rul. 69-441, supra.

You do not restrict your activities to the benefit of the poor. Though you represented that two-thirds of your clients will come from low-income backgrounds, you have not provided any substantial evidence (demographic studies, etc.) that you will serve, primarily, a specific, identifiable charitable class. You even stated that beyond the two-thirds that will come from low-income backgrounds, "substantially all of the remaining will be middle income individuals and families." Moreover, in your letter of October 2, 2002, you stated that your budget plans "will be limited to those who might have to declare bankruptcy." If your standard is that you will only provide services to individuals that may declare bankruptcy, you have not established a standard that will insure the Service that your activities are limited to low-income individuals. An organization that is exempt because it provides services to the needy must have procedures in place that will ascertain whether each potential client is needy. You have demonstrated that you do not have these procedures. You have no standards because the DMP you offer is sold to anyone who has unsecured debt and is willing to purchase your services. No court or Service ruling has indicated that the sale of DMP's is a charitable activity. Since the sale of DMP's to the general public appears to be a substantial purpose of yours, we cannot conclude that you are operating for charitable purposes.

Further, based on the information you submitted, you have not established that you operate for educational purposes within the meaning of section 501(c)(3). Training an individual to develop his capabilities or instructing the public on subjects useful to the individual and beneficial to the community are both educational purposes, recognized as exempt. See section 1.501(c)(3)-1(d)(3) of the regulations. Financial counseling could be carried out as an educational activity. Consumer Credit Counseling Service of Alabama, Inc. v. United States, Rev. Rul. 69-441, supra. While education is a broad concept, the Service and the Courts require that some rigor must be evident. In St. Louis Science Fiction Limited, supra. the Court made it clear, by contrasting the applicant with Goldsboro, that an organization must have an educational program not a predominantly non-educational program with some random educational features.

The information you submitted provides no basis to conclude that you offer either education to the public on subjects useful to the individual and beneficial to the community or training to the individual. It is essentially devoid of any support that you provide education. The information you provided in support of your Application demonstrates that counseling

activities and educating the public on credit issues are an insubstantial part of the activities you conduct. In your Application, you stated that once you develop a full clientele you will increase your time, effort, and resources dedicated to counseling activities from % up to %. You stated that you would employ full-time budget counselors. It seems unlikely,in view of the large number of clients likely to be serviced by you, how you realistically expect your small staff to provide any meaningful, substantive credit education to these clients. You have represented that "It is anticipated that counselors will spend an average of twenty minutes in total counseling each consumer who does not enroll in a debt management plan and thirty minutes with each consumer who does." This limited amount of time with a client is barely enough to get financial information, introduce the program, and determine if a DMP can be sold There is clearly no time for any meaningful, substantive counseling and education oncredit matters.

Moreover, you are using your counselors ina deceptive manner in representing that your counselors/account specialist are "experienced" when in fact they are merely trained for intake processing of DMPs. You have even stated that: "For most clients, the first and often only contact with will consist of one or more in-person counseling sessions or over the telephone." This is a clear admission that you spend limited amounts of time with individuals or families in "counseling sessions." We further note that in your letter of April 9, 2003, you stated that you would not require that your counselors be licensed, bonded or insured. The lack of credentials and low salary you propose to pay your counselors does not support your assertion that they are highly trained and credentialed in seeking to perform their "counseling" duties. You have not provided information indicating the number of people you expect to attend any structured counseling sessions; and have not indicated the amount of time to be spent in "pure" counseling versus time spent in soliciting, convincing, enrolling, and referring clients to the debt management program. You have submitted no schedule of classes or seminars. Any information you have submitted about your potential educational activities is vague, self-serving and provided with no substantiation.

You even stated that credit counselingis not a mandatory condition for participation in your DMP, when you said the following: "The participants in the workshops and in the one-on-one budget counseling sessions will be self-selected. They are likely to be people having numerous creditors and experiencing serious debt problems. No criteria will be utilized other than a willingness to attend the workshops and counseling sessions and, in the case of counseling sessions, a willingness and ability to complete a financial questionnaire." Moreover, as evidenced in your proposed budgets, you have made no specific expenditures related to educational activities or programs that would indicate more than an insubstantial commitment to this particular activity. These so-called counseling sessions are primarily dedicated to carrying-out your role as intake-administrator and referral facilitator to clients before they enroll in a DMP. Thus, it would appear that your counselors' primary duty and responsibility consists of marketing DMPs to as many clients as possible, rather than the provision of one-on-one counseling sessions or the provision of education to the general public on credit issues.

Moreover, the public information materials to be given to your clients do not indicate when, where, or how they are to be used by your counselors in any structured, formal counseling sessions. The training material to be used to train your employees seemingly places its primary emphasis on preparing counselors to effectively persuade clients to enroll in a DMP. For

example, you make the following statement in your training material: "Counselors are given marketing materials that are used to promote the...debt management program. This gives the counselor an idea of how we promote the service to consumers." Furthermore, you have not provided substantial details on how you would use videos, pamphlets and other educational materials to educate the general public on credit issues. You also have provided no information detailing how your workshops would be conducted including when, where, subjects to be discussed, and the number of people expected to attend. We note that your financial and budgeting workshops are easily used to recruit potential DMP clients, thus, serving as a marketing tool for the promotion of your business. We also note that in your Application, you state that you will offer free educational seminars, videotapes, etc. However, you also state that, apart from free distribution of brochures, you will charge fair market value for any additional materials. You are unlike the organizations described in Consumer Credit Counseling Services of Alabama, Inc. v. United States, supra, Credit Counseling Centers of Oklahoma, Inc. v. United States, supra, and Rev. Rul. 69-441, supra. Those organizations provided information to the general public through the use of speakers, films, and publications on the subject of budgeting, buying practices, and the sound use of consumer credit. Unlike your activities, in those cases and the Rev. Ruls., the community education and counseling assistance programs were the agencies' primary activities.

Second, the counselors in Consumer Credit Counseling Service of Alabama spent their time providing information to the general public through speakers, films, and publications on the subjects of budgeting, buying practices, and the sound use of consumer credit. You have submitted no evidence that you provide any similar information to the general public.

Also, in contrast to the organization in Consumer Credit Counseling Service of Alabama, you have not demonstrated the individual training content of your "counseling" sessions with your clients. In that case, counselors spent additional time in individual counseling concerning budgeting and the appropriate use of consumer credit to "debt-distressed" individuals and families. The professional counselors used only 12 percent of their time for debt management programs. You have stated that your budget planning activities should increase from 5 percent up to a maximum of 20 percent, more than the 12 percent spent in CCCS Alabama. The information you provide your counselors seems entirely aimed at selling and servicing DMPs.

You operate in a manner that it is strikingly different from the charitable credit counseling organization described in Rev. Rul. 69-441. That ruling states:

> The organization did not charge fees for counseling services or proration services. The debtor received full credit against his debts for all amounts paid.

The organization in the revenue ruling assisted the debtor by using all of the debtor's funds to pay off creditors. You, on the other hand, put your clients in a worse financial picture than they started with by your retention of the first month's payment and your significant monthly charges.

An analysis of the information provided shows that you are operated primarily for the nonexempt purpose of operating a for-profit business. That your primary activity is to promote and to further your private business interests is reflected in the fact that the vast majority of your

revenue (at least %) will be derived from fees charged to clients enrolled in your debt management program (DMP). Though you may view these fees as "voluntary contributions," we have determined that they are in fact fees received in exchange for the sale of a program-related service. Your proposed financial information shows that for , you will receive "voluntary payments from clients (initial) and monthly" amounting to $ $ in each respective year. You project your total income as $ You have provided no indication of how you will spend the substantial income you will be earning. You indicated that proposed salaries for your employees high school graduate credit counselors and clerical employees) is expected to be $ in the year . Since you informed the Service that your employees would be receiving salaries of approximately $ each, we are at a loss to determine why the total compensation figures you providing are so high. This is particularly troubling in light of the fact that your employees' have a marked lack of experience, training and credentials related to the services you provide.

You have not provided any evidence that the fees to be charged to clients enrolled in your DMPs are any less than would be paid by individuals serviced by a for-profit credit counseling company. In Airlie Foundation v. Commissioner, supra, one of the factors considered in assessing commerciality was the extent and degree of below cost services provided. You provided no evidence that your clients ever receive free services, or can pay according to their ability. The fact that the vast majority of your clients (you estimate %) will pay some amount of your requested "contribution" is evidence that your clients do not perceive these payments as voluntary. Although you have provided no data on the number of clients you expect to serve in the years , the amount of revenue you expect to generate in those years strongly suggests that you anticipate enrolling large numbers of individuals in DMPs. We also note that the significant expected spike in DMP income from suggests that you will make an intense effort to enroll more clients, an effortmore consistent with a for-profit credit counseling company. In an apparent effort to advance your sale of DMPs, you have even made the "misleading" claim to potential clients that you will intercede on their behalf with creditors to try to persuade them to accept partial payment in satisfaction of debts. In fact, these creditors have previously published the fact that these arrangements are available, there is no negotiation needed. That you are operating a business is further evidenced by your request for a % one-time first payment of a client's outstanding indebtedness. This fee is above and beyond the DMP monthly payment made by clients. It would appear that this payment bears no relation to the costs of servicing the client's individual account(s), and is a purely profit making tool. Moreover, the higher the amount of debt owed by the client, the greater your fee. For example:

Balance	Fee
$	$
$	$
$	$
$	$
$	$

An individual with a $ balance can be paying numerous creditors, each requiring a contact letter from your back-end provider. On the other hand, an individual owing $ could have

only one creditor. The above chart demonstrates that there is no relationship between your charges and the amount of work it may take to establish the DMP.

Thus, it would appear that you have a traditional business "mentality" that emphasizes that you are operated to make money, not to give-away free or reduced priced services. That you may or may not immediately make a profit would not be conclusive proof that you are not operating a business venture.

Unlike the agencies in Consumer Credit Counseling Services of Alabama, you receive token or no support from contributions from the general public, government or private foundation grants, or assistance from the United Way. In fact, you have virtually no fundraising program to solicit such contributions. According to your proposed budgets for and you plan to receive all your revenue from fees from setting up and processing clients' DMPs and fair share payments from creditors. For-profit business enterprises are supported by fees paid by those who receive services. While charitable institutions often do provide services to individuals, the cost is generally subsidized by contributors who do not receive anything in return. In B.S.W. Group, Inc. v. Commissioner, *supra*, the court cited lack of solicitation and sole support from fees as negative factors for exemption. See also, Easter House v. United States, *supra*.

You have not shown that revenue from operation of your DMP, is used for any purpose other than to cover operating expenses. Like any ordinary commercial business, your expenditures are almost exclusively to pay salaries, office expenses, and processing costs to your proposed for-profit service provider In fact, a large proportion of your revenue will be expended to pay DMP processing costs. You have not provided any information to indicate that you plan to dedicate any specific revenue to activities involving educational and/or charitable programs. In having a paid staff with no volunteer help, and having no direct expenditures for charitable and educational purposes, you are similar to the organization described in Easter House v. United States, supra, where the court determined that the organization was not exempt because its conduct of adoption services activity was in furtherance of a non-exempt commercial purpose.

Although your budgets do not show specific expenditures for advertising in your proposed budgets, like many commercial businesses, you indicate you will place advertisements in the telephone yellow pages and other local media. You will also seek referrals from internet financial sites, publicize your services through financial and budgetary workshops, and eventually develop your own website. Therefore, you will promote and attempt to sell your services in ways that are typical for any for-profit business. We note your use of sales "pitch" language such "C " This language is clearly "puffery" of the sort used by many for-profit debt consolidation organizations and others.

The facts in your case also show that your activities serve to promote the private business interests of , rather than to promote the public interest. Your proposed agreement with / allows it to perform all services related to your debt management program other than intake and counseling services. Under the agreement, would have the authority to prepare, present, and negotiate with creditors on behalf of all clients, once

they are enrolled in a DMP. The agreement also authorizes to solicit and distribute "fair shares" from creditors to you.. Thus, as in est of Hawaii, 71 T.C. 1067 (1979), certain aspects of your business operation are controlled to a certain extent by a for-profit company. The essence of the agreement with allows it to dictate charges and methods of operation, and assures long-term financial support for . For example, if the agreement with . should be terminated, any DMPs generated by you would remain the property of

Moreover, the agreement gives " full access to one or more accounts for the deposit of budget plan payments from clients, the disbursement of refunds, if any, to clients, and the disbursement of payments to creditors. Any interference with access to such account(s) shall represent a substantial breach of this Agreement entitling to terminate this Agreement and/or recover liquidated damages (and not a penalty) of percent %) of the amount of the check or withdrawal." Furthermore, you apparently would be agreeing to a contract where the cost is ambiguous. It is not clear in the contract whether you would be responsible to pay a one-time fee of $ or $ per budget plan client. It is also not clear why you would pay an additional $ per client per month beyond the one-time $ or $ fee. The contract provides that in addition to the monthly $ per client, you have to pay all of the considerable processing costs. You have not submitted a signed copy of this contract but you have submitted this proposed contract to the Service as an example of the contract you will enter. You have not supplied any information to support your agreeing to a contract that is ambiguous as to the amount of money you need to pay, In addition you have not provided any information to indicate why you would accept a contract that on its face appears to require duplicative payments. The way this contract is set up, charitable assets are being transferred from you to the back-end provider through duplicative billing. The conclusion that this will result in substantial private benefit to your back-end service provider is inescapable. We previously noted that the first month client fee o % of the debt balance does not appear to bear a relationship to the cost associated with setting up a DMP. The contract you submitted supports that conclusion. You are required to pay or $ dollars for start-up. You have not explained why, in many cases, you will be receiving much more from your clients.

As was previously mentioned, the largest share of your operating expenses is budegeted to pay for services rendered to you by a back-end service provider, such as Therefore, it appears that the potential financial benefit to be bestowed on far exceeds any potential public benefit. Furthermore, you would also benefit in your business operation in that your proposed financial information for shows that you will receive "fair share" payments from creditors amounting to $ $ and $ in each respective year. You are like International Postgraduate Medical Foundation, *supra,* where an alleged exempt organization was found to have been established to provide business to a travel agency owned by the same individual. Other cases on point are P.L.L. Scholarship and KJ's Fundraisers, *supra*, in which charitable fundraising was conducted on the premises of for-profit businesses in such a way as to benefit the businesses by attracting customers. Even though the organizations provided some scholarships, the court found that they had a substantial nonexempt purpose of promoting for-profit businesses. Based on the information you submitted, we conclude that a substantial purpose of your creation is to provide business to or other back-end providers.

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Your apparent attempt to avoid regulation under the CROA also indicates that you are operated for a substantial non-exempt purpose. See 15 U.S.C. section 1679 et seq This statute imposes restrictions on credit repair organizations, including forbidding advance payment before services are fully performed. 15 U.S.C. section 1679b. Section 501(c)(3) organizations are by definition excluded from regulation under the CROA. As stated above, the courts have interpreted the CROA so as to apply to the activities of credit counseling organizations.

The information you have provided can only be interpreted as evidence that you charge an advance fee, a practice forbidden to for-profit organizations under the CROA. Your Debt Management Agreement provides a fee structure of $ per month per creditor plus a first payment or "contribution" for operational costs. Neither your debt management agreement nor your client contract refers to an option for waiver of fees. You have not provided any data on the number of clients that have not paid the initial "contribution." Only tax-exempt charitable organizations are permitted under the CROA to charge any of these advance fees. From the information you have submitted, it is clear that you are operating as the intake arm of a for-profit service provider to avoid regulation under the CROA. Any successful sale is serviced entirely by an organization that is not controlled by you. Your role in this plan is to assure that the real service provider will not be subject to either the CRQA or the Do Not Call List.

In FTC v. Gill, 265 F.3d 944 (9th Cir. 2001), aff'g 183 F. Supp. 2d 1171 (2001), the appellate court inferred that a credit repair organization that first promised a "free consultation," but charged fees in advance of the full performance of services was being subsequently operated as a charity primarily for purposes of evading regulation under the CROA. Your lack of documentation of educational or other charitable purposes and your operation for the substantial non-exempt purpose of operating a business, suggests that your attempt to be recognized as a tax-exempt charitable organization is for the purpose of evading regulation under the CROA.

An organization cannot prove that it is entitled to exemption where one of its purposes is the avoidance of regulation. See The Foundation Church of Scientology v. U.S., 188 Ct. Cl. 490, 506 (1969). Since that it is one of your purposes, you are not entitled to exemption.

In addition to operating for substantial non-exempt purposes, you also benefit the private interests of a select few. Under section 1.501(c)(3)-1(d)(1)(ii) of the regulations, an organization is not organized or operated exclusively for one or more exempt purposes unless it serves a public benefit rather than a private interest. An organization must 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. You failed to submit sufficient information to show that you do not substantially benefit the private interests of its shareholders or managers or others.

You also provide substantial private benefit to credit card companies in a manner similar to the organization in Credit Counseling Centers v. S. Portland Fair share is commonly defined as

"that amount the organization receives from the creditors for each payment remitted to them." In the absence of any charitable or meaningful educational activities you are operating as a collection agency for these companies. The "fair share" paid by the credit card companies would undoubtedly result in significant savings over the possible costs of not recovering any of the unpaid debt owed them. Thus, these companies clearly realize substantial financial benefits through their business relationship with you.

You have not shown that you have a governing board that would be considered as representative of a broad cross-section of the community. Your current board apparently consists of only individuals. A board with so few people from limited backgrounds could be viewed as more likely to be concerned with their narrow private interests than with benefiting the general public. Your governing board is unlike the Board of Directors described in Rev. Rul. 69-441, supra, that was comprised of representatives from religious organizations, civic groups, labor unions, business groups, and educational institutions. Moreover, your Bylaws, Article 3, Section 14, have a restriction regarding interested directors. Under the restriction, "not more than percent %) of the persons serving on the board may be interested persons." Assuming you continued to function with your current two-person Board of Directors, and have a paid individual receiving compensation for a role outside of being a director, you would be in violation of the restriction on interested directors.

Finally, your Executive Director, has no apparent prior work experience or educational background in nonprofit "credit counseling." You stated that is a business executive with a background in personnel management. Likewise, your other director, has no apparent prior work experience or educational background that would be expected of someone involved in providing "counseling" to individuals and families in debt. You have stated that has a background in billing in the medical industry.

Based on our analysis of your actual and proposed activities and, in light of the applicable law, we have determined that you are not operated for exempt purposes. Rather, you are, primarily, operated for the non-exempt purpose of furthering your business interests, and those of through the marketing and sale ofDMPs to the general public. Any activities involving "authentic" credit counseling provided to a genuine charitable class, along with the provision of credit education to the general public, would be purely incidental to your predominant non-exempt purpose of operating and carrying-on an ordinary for-profit "credit counseling" business.

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.

We note that, in view of the holding in Rev. Rul. 65-299, supra, along with the Code and regulations, we do not believe that you qualify for exempt status under section 501(c)(4). Unlike the organization in Rev. Rul. 65-299, your activities do not contribute to the betterment of the community as a whole, rather your activities serve to further the nonexempt purpose of operating a for-profit credit counseling business.

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 judgement 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 Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
TE/GE (SE:T:EO:RA:T:4)

1111 Constitution Ave, N.W.
Washington, D.C. 20224

200440045

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

Sincerely,

Debra J. Kawecki, Esq.
Manager, Exempt Organizations
Technical Group 4

cc: