

IRS Fact Sheet

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IRS Takes Steps to Ensure Credit Counseling Organizations Comply With Requirements for Tax-Exempt Status

FS-2003-17, October 2003

For decades, many organizations have provided valuable credit counseling and education that assist consumers in putting their personal finances in order. The Internal Revenue Service continues to view organizations that counsel and educate consumers as qualifying for tax exemption under Section 501(c)(3) of the Internal Revenue Code.

However, federal and state officials have become increasingly aware that as the market for consumer credit has undergone changes in the past 30 years, so have some of the entities that offer services to debtors. Many of these services do not provide meaningful education or counseling.

For example, some organizations put their clients on fixed payment plans to pay down their debt. But an organization that offers only this service, without significant education and counseling, would not qualify for tax-exempt status.

IRS officials are concerned that some credit counseling organizations that might have qualified for tax-exempt status in the past may no longer qualify due to changes in the services they provide. This problem is magnified because the organizations, by reason of their tax exemption, are exempted from many state and federal consumer protections.

For example, the Credit Repair Organization Act of 1997 sought to further regulate the practice of for-profit organizations involved in "credit repair," a series of activities aimed at improving a customer's credit history. But the Act exempted Section 501(c)(3) organizations from the provisions of this law. A similar pattern of exceptions for tax-exempt organizations is replicated in many state consumer laws.

The IRS is concerned that the combination of tax-exempt status and exemption from consumer protections may leave certain taxpayers vulnerable. To address this concern, the Exempt Organizations (EO) office of the IRS has taken the following steps:

- Credit counseling organizations submitting applications for exemption will only receive that status after a full review, which includes answering additional questions and a close analysis of the marketing materials the organizations distribute. The aim is to ensure that the organizations' activities qualify for tax exemption.

- In January, 2003, EO published a 50-page Continuing Professional Education article that reviewed the law in this area and provided tools for reviewing applications by new organizations. This article is posted on our Web site at www.irs.gov/charities and is available to the public.
- EO officials held sessions to train both those reviewing new applications for exempt organization status and those examining existing qualified organizations. Developed in conjunction with state charity officials and the Federal Trade Commission, these training sessions focused on changes in the credit counseling industry and their implications for the EO office.
- EO has initiated a project to address concerns in this area and to recommend strategies. A number of examinations of consumer credit services organizations have commenced. The results of these examinations will be monitored to assess the extent to which tax-exempt credit counseling organizations are operating in a manner that conforms with the laws and regulations governing Section 501(c)(3) status.
- EO officials are conducting outreach with the consumer credit industry and attorneys practicing in this area and speaking to them on the tax rules relating to non-profit consumer credit organizations.