



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE
TE/GE: EO Examination
625 Fulton Street, Room 503
Brooklyn, NY 11201

Release Number: 200649033

Release Date: 12/08/2006

UIL: 501.03-01

Date: May 8, 2006

Taxpayer Identification Number:

Person to Contact:

Identification Number:

Contact Telephone Number:

LAST DATE FOR FILING A PLEADING
WITH THE TAX COURT, THE CLAIMS
COURT, OR THE UNITED STATES
DISTRICT COURT FOR THE DISTRICT
COLUMBIA:

Dear :

This is a Final Adverse Determination Letter as to O's exempt status under section 501(c)(3) of the Internal Revenue Code.

Recognition of your exemption from Federal Income Tax as an organization described in Internal Revenue Code section 501(c)(3) is retroactively revoked effective January 1, 2002 for the following reasons:

You have not demonstrated that you are operated exclusively for exempt purposes within the meaning of Internal Revenue Code section 501(c)(3). You are not a charitable organization within the meaning of Treasury Regulations section 1.501(c)(3)-1(d). You operate substantially for non-exempt purposes. You are not an organization which operates exclusively for one or more of the exempt purposes which would qualify it as an exempt organization.

Contributions to your organization are no longer deductible under section 170 of the Internal Revenue Code.

You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending December 31, 2002, and for all years thereafter.

Processing of income tax returns and assessment of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination in court, you must file a pleading seeking a declaratory judgment in the United States Tax Court, the United States Court of Federal Claims, or the United States District Court for the District of Columbia before the 91st day after the date this final determination was mailed to you. Please contact the clerk of the appropriate court for rules regarding filing pleadings for declaratory judgments and refer to the enclosed Publication 892. You may write to these courts at the following addresses:

United States Tax Court
400 Second Street, NW
Washington, D. C. 20217

United States Court of Federal Claims
717 Madison Place, NW
Washington, D. C. 20005

United States District Court for the District of Columbia
333 Constitution Avenue, NW
Washington, D. C. 20001

You also have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers.

You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling or writing to:
Internal Revenue Service
Taxpayer Advocate Services

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

We will notify the appropriate State Officials of this action, as required by section 6104(c) of the Internal Revenue Code.

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

Sincerely yours,

Marsha A. Ramirez
Director, EO Examinations

Enclosure:
Form 886-A
Publication 892

cc: CPA



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
TE/GE EO: Examination
1100 Commerce Street MC:4900 DAL
Dallas, TX 75242

March 8, 2006

Taxpayer Identification Number:

Form:

990

Tax Year(s) Ended:

December 31, 2002

Person to Contact/ID Number:

Contact Numbers:

Telephone:

Fax:

Certified Mail - Return Receipt Requested

Dear _____,

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, take no further action. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, *The Examination Process*, and Publication 892, *Exempt Organizations Appeal Procedures for Unagreed Issues*, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

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

Letter 3618 (04-2002)
Catalog Number 34809F

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter. We will also notify the appropriate state officials of the revocation in accordance with section 6104(c) of the Code.

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

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

Thank you for your cooperation.

Sincerely,

Marsha A. Ramirez
Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

Form 886-A

ISSUES PRESENTED:

1. Whether O is operated exclusively for exempt purpose as described within Internal Revenue Code section 501(c)(3):

a. Whether O is engaged primarily in activities that accomplish an exempt purpose?

b. Whether more than an insubstantial part of O's activities are in furtherance of a non-exempt purpose?

FACTS

BACKGROUND

An audit of O was commenced on June 2, 2005 for the year ended December 31, 2002.

O was incorporated under the laws of the State under Section 402 of the Not-for-Profit Corporation Law . In a determination letter O was determined to be exempt from Federal income tax as an organization described in IRC section 501(c)(3). It was further determined to be classified as a public charity as described under IRC section 509(a)(2).

In its Articles of Incorporation, O stated its purposes to be:

- (a) To provide consumer credit and budget counseling and advocacy (but under no circumstances will this include the practice of law), to families and individuals, especially low income families and individuals who are in need of assistance;
- (b) To educate the public to the uses and abuses of consumer credit;
- (c) To establish a resource center and clearinghouse to compile, collect and disseminate statistical and other data about unconscionable and abusive consumer credit practices
- (d) To engage and support research about consumer credit practices and abuses, including how they impact adversely on the low income working class;
- (e) Other assistance and guidance and the conduct of any and all activities as shall from time to time be found appropriate in connection with the foregoing and as are lawful for not-for-profit corporations;

Nothing herein shall authorize the Corporation, directly or indirectly, to engage in or include among its purposes any of the activities mentioned in Sections 404 (b) through (t) of the Not-for-Profit Corporation Law.

The members of the Board of Directors as of December 31, 2002 were D1, D2, D3, D4, D5, D6, D7, D8, and D9.

P is a recognized authority on consumer credit and holds a degree in Business. He has many years of experience in the field of business administration and is a member of numerous civic organizations and has been singled out for his contributions to economic and community development.

Salaries for the year ended December 31, 2002 were as follows:

D2 (Chairperson) -	\$
P (President) -Salary	\$
VP (Vice President)- Salary	\$
T (Vice Chairperson/Treasurer)	
S (Secretary)	
D6 (Director)	
D7 (Director)	
D8 (Director)	
D9 (Director)	

The Board Members of O consisted of the management of O as well as other Directors.

O claimed in their response to Information Document Request number 1 (item 2c) that the organization is dedicated to assisting individuals in budget planning and debt management and claimed to provide one-on-one counseling and advice on such topics as budgeting, money management, debt consolidation, credit bureau reporting activities, consumer rights and responsibilities, establishing credit, home ownership and bankruptcy. O claimed that the counselor assists the client in analyzing their financial situation and identifying all options available to help remedy the current problems that exist. O claimed in their response to the above mentioned Information Document Request, which is in a narrative form, that its goal is not only to remedy the immediate problem, but also to "rehabilitate" the debtor, through education so that a financially healthy consumer is returned to the credit market.

The organization claimed its basic mission and purpose is education of the individual and is to assist individuals and families that are experiencing financial difficulties. This mission is accomplished by arranging debt repayment plans with creditors.

ACTIVITY DESCRIPTION

DEBT MANAGEMENT PLANS (DMP'S)

The primary activity engaged in by O during the year under examination was solicitation of clients to enroll in Debt Management Plans (hereinafter DMPs).

Information Document Request number 1, item 2c requested a narrative of the organization's activities. The organization responded in the narrative and addressed the DMP as one of its activities. The narrative furnished stated that an overextended consumer may qualify for a DMP, which is designed to assist the consumer in paying off their debts. The narrative went on to state that the client through this plan makes one affordable monthly payment, based on their income, expenses and indebtedness. The payment is then distributed by O to each of the client's creditors in accordance with the plan established during the counseling session.

The narrative stated that the plan lasts for approximately 48 months and provides for complete debt repayment, in addition to giving the client the necessary skills to manage their own finances at the conclusion of the plan.

According to the organization, the DMP is set up for a client only when necessary. Potential clients were individuals with unsecured debt. O claimed in the narrative, that the organization negotiates on behalf of the client and acts as a budget advisor to the client and a liaison with the creditor. O claimed to have access with client's creditors to reduce interest rates charged on balances and reduce the monthly payment.

Information Document Request number 7, item 14, requested information as to how O determines if a potential client qualifies for a DMP. The organization claimed that a budget is prepared to determine if the client has enough surplus to qualify for a DMP. The organization was unable to substantiate this claim and did not provide copies of any budgets or client files.

Information Document Request number 18, item 2, requested whether or not a list of income and expenses is obtained from the client and how this information is used during the initial contact with the potential client. The organization claimed in the response to item 2 that that "yes" the information is used to determine if the client can afford the DMP, however it did not provide copies of any lists of income and expenses.

The President of the organization claimed initial calls for DMP and NON-DMP consumers are given follow up calls within a few weeks for further discussion, however the organization could not provide any documentation to substantiate this claim.

Information Document Request number 18, item 1, requested data on what percentage of clients interviewed during 2002 actually signed up and enrolled on a DMP for the year ended December 31, 2002. The organization claimed in their response to item 1 that percent of the clients counseled in 2002 actually signed up for the DMP, however documentation was not provided which could substantiate this percentage.

Information Document Request number 7, item 1, requested data on the total number of clients that enrolled in the DMP for the year ended December 31, 2002. The organization claimed in their response to item 1 that clients enrolled in the DMP for the year ended December 31, 2002, however again documentation was not provided which could verify this figure.

Information Document Request number 7, item 15, requested information as to if a potential client does not qualify for a DMP, what other counseling is provided. Item 15 also requested information as to if the organization refers clients to other entities for assistance and requested the names, addresses, and telephone numbers of the entities and names of principals in the event referrals are made. The organization claimed that if a potential client does not qualify for a DMP, the counselor may provide suggestions to adjust expenses in the client's budget, suggest additional income or refer the client to other entities or discuss bankruptcy as a last resort. A list of other agencies and organizations to which referrals were claimed to be made was furnished with the addresses and telephone numbers, however documentation was not provided with the Counselor's "suggestions" as client files for both DMP and non-DMP clients were requested on numerous occasions and not provided.

SOURCES OF REVENUE

O's primary source of revenue was derived from Fair Share revenue from client's creditors and fees generated through the enrollment of clients in their DMPs. O also derived revenue from its Bankruptcy and Mortgage programs.

The revenue received for the period January 1, 2002-December 31, 2002 was as follows:

	2002	Percentage of Total Revenue
Client fees		
Creditor "fair share" payments		
Contributions		
In -Kind Contributions		
Interest		
Miscellaneous Revenue		

Total	\$	

The revenue received for the years ended December 31, 2000 and 2001 were as follows:

	2000	Percentage of Total Revenue	2001	Percentage of Total Revenue
Client fees	\$			
Creditor "fair share" payments				
Interest				
Contributions				
In-Kind Contributions				
Grants				
Miscellaneous Revenue				
Total	\$			

O's primary sources of revenue were derived from Fair Share revenue and client fees which made up 98.39 percent of the total revenue derived for the year ended December 31, 2002. O received a relatively small amount of interest (percent), contributions (percent) and in kind contributions (percent) for the year ended December 31, 2002.

FEES

O claimed in Information Document Request number 24, item 5, that fees were waived when necessary in the event that the client's budget did not allow for additional fees. The organization however was unable to provide any documentation to support the waiving of fees or provide the percentage of fees related to the DMP which were partially or totally waived. Information Document Request number 24, requested data as to the number of clients who a) did not initially pay any portion of the requested fee for enrollment and b) did not pay any portion of the requested fee for monthly services. The organization was unable to provide this data in their response.

The following is a list of fees charged by O for various categories of services that were provided to clients:

- Credit Counseling
- Monthly DMP Payment Average Fee
- Negotiation Fee
- Credit Report Interpretation
- First Time Homebuyers Counseling Fee
- Bankruptcy Fee- Individual
- Bankruptcy Fee Joint
- Bankruptcy Fee-Joint Living Separate
- Bankruptcy Individual Self Employed

Bankruptcy Joint One Self Employed
Bankruptcy Both Self Employed

COUNSELOR CERTIFICATION AND EVALUATION

In response to IDR number 15, item 3, the organization claimed that the Counselors are required to be certified and the certification is performed by the . In response to IDR number 15, item 3, the organization claimed that the Counselors were given a Study Guide and as each Counselor studied a particular section they took a test on line. However the organization did not provide a copy of the Study Guide or a copy of the test results when requested.

Copies of advertisements used to hire Counselors were requested in Information Document Request number 15, item 1. However this documentation was not provided as the organization claimed they did not have copies and Counselors had not been hired since 2002.

O claimed in response to Information Document Request number 15, item 5 that newly hired Counselors should have a degree. However, those Counselors that do not have degrees were promoted after learning the business of the company such as customer service and sitting in on counseling sessions and then passing the Certification test. O did not provide copies of any of the Counselor applications used when potential candidates applied for a position.

Counselors are evaluated once a year through performance appraisals and self appraisals. The organization provided copies of Counselor Evaluations prepared in 2002 and 2003 for five different Counselors in response to Information Document Request number 15, item 6. Areas on the performance appraisal included "Major Responsibilities", "Professional Strengths", "Results and Accomplishments", "Areas for Improvement" and an "Action Plan". A review of the Counselor Evaluations provided by the organization indicated that one of the "Major Responsibilities" of one of the Counselors was: "to encourage clients to join the DMP". The "Results and Accomplishments" section on the Counselor evaluations included the following for four different counselors: "signed up a ratio of percent of clients seen in 2001", "signed up a ratio of percent of clients seen", "signed up a ratio of more than percent of clients seen" and "more than percent of my clients sign up to the DMP". "Areas for Improvement" on three of the Counselors Evaluations included "improve DMP sign up ratio".

Copies of Counselor Evaluations prepared for the years of 2002 and 2003 have been attached to this Form 886-A and are marked as "Exhibit A".

Information Document Request number 7, items 2, 3 and 4 respectively requested data on a) the average length of time spent on an initial call with a potential DMP client b) with respect to a potential client who the organization enrolls in a DMP, the average length of time spent on a call and c) with respect to a potential client who does not enroll in a DMP, the average length of time spent on the call. The organization in response to Information Document Request, number 3 items 2, 3 and 4 respectively indicated that a) the average length of time spent on a call for a client that does not enroll in a DMP is 4 minutes b) the average length of time spent on a call with an average DMP is 20 minutes and c) the average length of time spent on a call of a client that enrolls in the DMP is 30 minutes. The organization did not track or compile any data and did not generate any reports for the telephone site as stated in response to Information Document Request number 26, items 1, 2 and 3. Call transcripts were not provided.

The organization in Information Document Request number 26 stated that statistical data pertaining to the telephone site was not compiled, maintained or tracked and as a result no documentation was provided. The President of the organization in an interview with the agent claimed that on the initial telephone call the prospective client's financial situation is analyzed and all options are explored. Item 3 of Information Document Request number 20 requested data on how much time is spent on each phase of training (DMP Processing vs. Counseling and Education) for the counselors. The organization in response to item 3 stated that 75% of the counselors time is spent on counseling and education and that 25 percent of the Counselors time is spent on the DMP which ranks 3rd on their priority list, however substantiation to verify this claim was not provided..

Information Document Request number 28, item 16, requested information on whether the organization performs education and counseling to clients on the telephone or is all counseling done in person. The organization responded that telephone counseling is offered to their clients. The organization claimed in its literature that the Counselors perform both face to face counseling and counseling over the telephone.

Information Document Request number 28, item 2, requested information concerning counselors maintaining adequate records on each client to demonstrate that the organization followed an educational methodology and also requested copies and records for the file. The organization responded to item number 2 and claimed that counselors maintained adequate records, however all files were forwarded to an agency (A) who is now handling all the organization's past client accounts.

Information Document Request number 20, item 2, requested copies of client files for DMP enrollees as well as non-DMP enrollees and the organization claimed that all copies of client files were forwarded to A.

Information Document Request number 30, item 3, requested again copies of client files

maintained for DMP enrollees as well as non-DMP enrollees, however these were not provided to the agent. Again the President claimed initial calls for DMP and NON-DMP consumers are given follow up calls within a few weeks for further discussion, however the organization could not provide any documentation to substantiate this claim.

LACK OF EDUCATIONAL ACTIVITIES AND DOCUMENTATION

The organization stated as part of a listing of events entitled "Education 2002", that during the audit year 2002 it provided educational workshops and seminars to colleges, community groups, employee assistance programs, Churches, parent teacher associations and many more organizations throughout the . The topics discussed included the principles of money management, budgeting, debt consolidation, what is credit, why is credit important, credit reporting issues, first time home buying, bankruptcy and other related topics. The President of O, conducted the majority of the workshops and seminars.

O claimed in response to Information Document Number 3, item 1, that each of the seminars are about the consumers financial future with questions being addressed as to what is happening now and how to handle it with a focus on how does the consumer handle their financial situation in the future.

The organization provided a listing of the different events in 2002, 2003, 2004 and 2005 in response to Information Document Number 3, item 1, which reflected the date of the event, the host of the event, the general location of the event and the time of the event. The organization also provided a more detailed listing of different events in response to Information Document Request number 3, item 1, only for the year 2002. This listing provided details including the agency/organization hosting the event, the general location, dates and times of the event as well as a brief description of the host and a brief description of the topic discussed. The number of participants and the amount of fees charged (if any) were also provided.

There was no detailed documentation provided in response to Information Document Request number 3, item 3, which requested copies of all syllabus, agenda, handouts, videos, and audio tapes. The organization did not provide any copies of syllabus, agendas, handouts, rosters of attendees, sign in sheets, other registration forms, video tapes, audio tapes or any other information substantiating the specific events and participants.

The organization's President claimed in a letter dated June 6, 2005 to the agent, which was attached to the Education 2002 listing, that the television and radio shows reached millions of consumers and that the face to face seminars ranged in attendance from ten people to 300 people per seminar. The number of attendees, viewers and listeners could not be substantiated. The President of O claimed to be on both the television and radio shows, however again was unable to produce any video or audio tapes requested to substantiate these shows as requested in Information Document Request number 3.

O again was unable to provide any documentation on registration or other proof of who attended the workshops, seminars and other outreach programs including the audience for the television and radio shows.

ADVERTISING

Information Document Request number 1, item 2e requested copies of all marketing and advertising materials. The organization only provided copies of advertisements it placed on bus shelters. These advertisements showed the name of the President of the organization and the name of the Vice President of Operations with the phrase "We Can Help-Call" and it listed the name of the organization, telephone number and web site on the advertisement. These advertisements did not list the services it provided or mention any workshops or outreach programs.

The organization provided pamphlets, brochures and other printed literature in response to Information Document Request number 1, item 2b. The pamphlets, brochures and other printed literature received and reviewed contained information on the various services provided by the organization and the areas the organization could provide assistance with: Advice on how to clean up your Credit Report, Budget your Money, Payment Plans, Stop Foreclosure, Refinance your Home, No Credit Check, One Monthly Payment, Student Loan Counselors, Bankruptcy, Attorney on Staff, Face to Face or Telephone Counseling. The pamphlets, brochures and other literature provided did not mention any workshops or outreach programs.

Information Document Request number 28, item 3, requested information on the content of any mass media and direct mail advertising and if the advertising described seminars, classes and counseling or is the DMP prominently featured in the advertising. The organization stated that when it advertised the advertisements contained information on the services the organization offered: No Credit Check, One Monthly Payment, Advice on how to Clean up the Credit Report, Student Loan Counselors, Mortgage Counselors, Bankruptcy, Attorney on Staff and Face to Face or Telephone Counseling. As stated above the only copies of advertisements provided was the bus shelter advertising, which made no mention of the services offered.

WEB SITE

O utilized its website to provide information to the general public regarding the services the organization offered. Information Document Request number 12, item 1, requested the date the organization's web site made its on-line debut. The organization responded to item 1 by stating that the O's web site made its online debut in 2001.

Information Document Request number 12, item 2, requested a printout of each of the organization's web site pages as they appeared during the year ended December, 31, 2002. A copy of the pages from the web site were furnished by the organization in response to this Information Document Request, however the date was not reflected on the printouts. Agent obtained a copy of the pages of the O web site from another web site (www.archive.org). These pages were dated November 30, 2002 and are attached (Exhibit B) to this Form 886-A. The O's web site contained various subject areas including "Financial Counseling and Debt Management", "Debt Management", "Home Ownership", "Credit Reports", "Bankruptcy", "Educational Services", "Membership", "Member Services" and a section for an on line "Mortgage Application". The "Educational Services" section of the web site contained only one sentence which stated the following: "O provides presentations and workshops for major corporations, community groups, Churches and schools". The "Educational Services" section of the web site did not provide a list or any details of upcoming presentations and workshops to be presented. The time and location of the workshops and presentations as well as a list and description of the topics were not provided on the web site. The web site contained minimal educational material and promoted O's Debt Management Program (DMP), Mortgage Program and Bankruptcy Program. The majority of the website was devoted to the Debt Management Program (DMP).

A response to Information Document Request number 25 (item 1) indicated that the O web site was for informational purposes only and it was not tracked. Item number 3 of Information Document Request number 25 claimed that reports were not generated for the web site.

MORTGAGE PROGRAM

O claimed in response to Information Document Request number 1, item 2c, (in the form of a narrative), that one of the activities conducted was assisting families in obtaining mortgages and/or the refinancing of their existing mortgage. O claimed in response to the Information Document Request mentioned above that the organization through their Mortgage Department assisted and educated consumers and that many of the individuals and families who were previously not eligible were able to be considered for mortgages as a result of O counseling program. The organization recommended mortgage financing and/or refinancing as a measure of budgeting. The organization claimed to have participated in outreach programs with various community development groups and major banks to educate the public about home ownership, however were unable to provide detailed documentation and substantiation of these outreach programs.

Details on this program were requested in Information Document Request number 30, item 9, however the organization failed to provide any additional details of the mortgage program or its activities.

BANKRUPTCY PROGRAM

O claimed in response to Information Document Request number 1, item 2c, that the organization was assisting their clients with the Bankruptcy Process and attempting to make the process as simple as possible. The purpose was to provide consumers with the necessary tools to file Chapter 7 bankruptcy petitions with the courts without the need for any legal representation.

O claimed in response to Information Document Request number 30, item 8, that providing bankruptcy services was a rehabilitative process for clients that had no other solution.

Details on this program were requested in Information Document Request number 30, item 8, however the organization failed to provide any additional details of the bankruptcy program or its activities.

O derived revenue from their clients as a result of the Mortgage Program (\$ for the year ended December 31, 2002 or percent of total revenue) and the Bankruptcy Program (\$ for the year ended December 31, 2002 or percent) it conducted.

LAW

Section 501(a) of the Internal Revenue Code provides that an organization described in section 501(c)(3) is exempt from income tax. Section 501(c)(3) of the Internal Revenue 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 inure to the benefit of any private shareholder or individual. The term charitable includes relief of the poor and distressed. Income Tax Regs. Section 1.501(c)(3)-1(d)(2).

The term educational includes (a) instruction or training of the individual for the purpose of improving or developing his capabilities and (b) instruction of the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3). In other words, the two components of education are public education and individual training.

Section 1.501 (c)(3)-1 (a)(1) of the 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(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. The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. Better Business Bureau of Washington, D.C. v. U.S. 326 U.S. 279 (1945).

Educational purposes include instruction or training of the individual for the purpose of improving or developing his capabilities and instruction of the public on useful and beneficial subjects. Treas. Reg. § 1.501(c)(3)-1(d)(3). 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 purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. The Court found that the trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered the status of an organization that provided analyses of securities and industries and of the economic climate in general. The organization sold subscriptions to various periodicals and services providing advice for purchases of individual securities. Although the court noted that education is a broad concept, and assumed for the sake of argument that the organization had an educational purpose, it held that the organization had a significant nonexempt commercial purpose that was not incidental to the educational purpose and was not entitled to be regarded as exempt.

The Service has issued two rulings holding credit counseling organizations to be tax exempt. Rev. Rul. 65-299, 1965-2 C.B. 165, granted exemption to a 501(c)(4) organization whose purpose was to assist families and individuals with financial problems and to help reduce the incidence of personal bankruptcy. Its primary activity appears to have been meeting with people in financial difficulties to "analyze the specific problems involved and counsel on the payment of their debts." The organization also advised applicants on proration and payment of debts, negotiated with creditors and set up debt repayment plans. It did not restrict its services to the needy. It made no charge for the counseling services, indicating they were separate from the debt repayment arrangements. It made "a nominal charge" for monthly prorating services to cover postage and supplies. For financial support, it relied upon voluntary contributions from local businesses, lending agencies, and labor unions.

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 a typical 501(c)(3) organization. It had not solicited, nor had it received, voluntary contributions from the general public. Its only source of income was from fees for 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.

Rev. Rul. 69-441, 1969-2 C.B. 115, granted 501(c)(3) status to an organization with two functions: it educated the public on personal money management, using films, speakers, and publications, and provided individual counseling to "low-income individuals and families." As part of its counseling, it established budget plans, *i.e.*, debt management plans, for some of its clients. The debt management services were provided without charge. The organization was supported by contributions primarily from creditors. By virtue of aiding low income people, without charge, as well as providing education to the public, the organization qualified for section 501(c)(3) status.

In the case of Consumer Credit Counseling Service of Alabama, Inc. v. U.S., 44 A.F.T.R. 2nd 78-5052 (D.D.C. 1978), the District Court for the District of Columbia held that a credit counseling organization qualified as charitable and educational under section 501(c)(3). It fulfilled charitable purposes by educating the public on subjects useful to the individual and beneficial to the community. Treas. Reg. § 1.501(c)(3)-1(d)(3)(i)(b). For this, it charged no fee. The court found that the counseling programs were also educational and charitable; the debt management and creditor intercession activities were "an integral part" of the agencies' counseling function and thus were charitable and educational. Even if this were not the case, the court viewed the debt management and creditor intercession activities as incidental to the agencies' principal functions, as only approximately 12 percent of the counselors' time was applied to debt management programs and the charge for the service was "nominal." The court also considered the facts that the agency was publicly supported and that it had a board dominated by members of the general public as factors indicating a charitable operation.

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 and legal analysis were virtually identical to those in Consumer Credit Counseling Centers of Alabama, Inc. v. United States, discussed immediately above.

The organizations included in the above decision waived the monthly fees when the payments would cause a financial hardship. The professional counselors employed by

the organizations spent about 88 percent of their time in activities such as information dissemination and counseling assistance rather than those connected with the debt management programs. The primary sources of revenue for these organizations were provided by government and private foundation grants, contributions, and assistance from labor agencies and the United Way.

Outside the context of credit counseling, individual counseling has, in a number of instances, been held to be a tax-exempt charitable activity. Rev. Rul. 78-99, 1978-1 C.B. 152 (free individual and group counseling of widows); Rev. Rul. 76-205, 1976-1 C.B. 154 (free counseling and English instruction for immigrants); Rev. Rul. 73-569, 1973-2 C.B. 179 (free counseling to pregnant women); Rev. Rul. 70-590, 1970-2 C.B. 116 (clinic to help users of mind-altering drugs); Rev. Rul. 70-640, 1970-2 C.B. 117 (free marriage counseling); Rev. Rul. 68-71, 1968-1 C.B. 249 (career planning education through free vocational counseling and publications sold at a nominal charge). Overwhelmingly, the counseling activities described in these rulings were provided free, and the organizations were supported by contributions from the public.

The Credit Repair Organizations Act (CROA), 15 U.S.C. § 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. § 1679b. Significantly, section 501(c)(3) organizations are 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. § 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).

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. 16 C.F.R. § 310.4(b)(1)(iii)(B); 47 C.F.R. § 64.1200(c)(2). Section 501(c)(3) organizations are not subject to this rule against cold-calling.

Because 501(c)(3) organizations are exempt from regulation under the CROA and the cold-calling restrictions, organizations that are involved in credit repair have added incentives to be recognized as section 501(c)(3) organizations even if they do not intend to operate primarily for exempt purposes.

GOVERNMENT'S POSITION

The primary activity of O was not "educational" or "charitable" as defined under the Internal Revenue Code, its regulations or legal precedence. The primary activity was the enrollment of debtors in DMP's. The operations of O were not consistent with organizations described in section 501(c)(3) of the Internal Revenue Code and its exemption should be revoked.

O was not engaged primarily in activities that accomplish an exempt purpose. The organization operated to serve a substantial non-exempt purpose.

The purpose of O's activities differs substantially from those of the organizations in Rev. Rul. 65-299, Rev. Rul. 69-441, and Consumer Credit Counseling Service of Alabama, Inc. v. U.S. In this case, O engaged in minimal activities which further an exempt purpose. The majority of income, 98.39 percent, for the year ended December 31, 2002 was derived from Fair Share Revenue and from fees relating to the Debt Management Program (DMP), the Bankruptcy Program and the Mortgage Program. O received a very minimal amount of grants and contributions compared to the total amount of revenue derived.

During the year under examination (year ended December 31, 2002), the organization provided limited records to substantiate the seminars, classes, outreach and other educational activities it was involved with. The records provided by the organization only included a listing of the activity, the host, the dates and times and the general location of the activity. The documentation of the outreach activities including classes, seminars, workshops and other education activities was very minimal during the audit year and prior to the audit year.

O claimed it engaged in meaningful outreach during the tax year ended December 31, 2002, however the organization could not provide specific documentation to substantiate these activities. Records maintained were very limited with respect to seminar outlines/syllabus, rosters of attendees, sign in sheets of participants attending the event and other related documentation to substantiate the event.

There is very little evidence to substantiate that the primary activity of the organization

was education and outreach, when the primary activities were placing individuals on DMP's. There was no documentation provided to substantiate the claim that followup, counseling or education is performed by O with their clients once they are placed on a DMP.

The requirements of Section 501(c)(3), especially education, were not met during the audit year as minimal documentation was furnished to substantiate the events the organization was involved with. Detailed documentation was not available as previously stated. There was no substantiation provided as far as the counseling and education of these individuals when they contacted O and client files were not provided.

In addition, O has a substantial non-exempt purpose of selling a product, the DMP. O was not furthering any charitable or educational purpose by offering a DMP, a Bankruptcy Program or a Mortgage Program.

Finally, as previously stated O received a very small percentage of the total revenue derived from contributions from the general public (.35 percent contributions and .44 percent in kind contributions) during the year examined. Substantially all revenues were generated from the administration of the Debt Management Programs (DMP's) and other programs, including the Bankruptcy Program and the Mortgage Program, with the majority of this revenue derived from Fair Share payments made by credit card companies and client fees.

CONCLUSION

In summary, O was not operated exclusively for educational or for any other exempt purposes within the meaning of section 501(c)(3) of the Internal Revenue Code since its primary activity was the sale of Debt Management Plans (DMP's). O did not engage primarily in activities which accomplish an exempt purpose. More than an insubstantial part of the activities of O were in furtherance of a non-exempt purpose.

The amount of time devoted to education and outreach activities was minimal compared to O's primary activity of setting up DMP's. There was no detailed documentation provided on the educational workshops and seminars. O only was able to provide a list of all seminars, lectures or programs held off site during the audit year. Therefore, O was unable to substantiate the educational outreach activities it claimed were conducted at this time.

Accordingly, it is determined that O is not an organization described in section 501(c)(3), and is not exempt from Federal income tax under section 501 of the Internal Revenue Code. The organization should be revoked effective January 1, 2002.