

Internal Revenue Service
TEGE Appeals Division
300 N. Los Angeles Street
Los Angeles, CA 90012

CERTIFIED

Department of the Treasury

Release Number: **201029036**
Release Date: 7/23/10
Date: 4/26/10
UIL Code: 501.03-00
501.36-00

Taxpayer Identification Number:

Person to Contact:

Eric M. Wong
Employee ID Number:
Tel:
Fax:

Refer Reply to:

AP:LA:EMW

In Re:

Tax Years:
years

Dear

This is a final adverse determination as to your exempt status under section 501(a) as an organization described under section 501(c)(3) of the Internal Revenue Code. Our adverse determination was made for the following reason(s):

You did not establish that you were operated exclusively for educational, charitable or other exempt purposes as required by section 501(c)(3) of the Internal Revenue Code. You did not engage primarily in activities which accomplish one or more of the exempt purposes specified in section 501(c)(3). Treas. Reg. § 1.501(c)(3)-1(c)(1).

Contributions to your organization are not deductible under Code § 170. You are required to file federal Form 1120 for the years shown above.

By executing Form 906-c, Closing Agreement on Final Determination Covering Specific Matters, you have waived your right to contest this determination under the declaratory judgment provisions of section 7428 of the Internal Revenue Code.

You 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.

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals procedures, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, or 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 final adverse determination of your exempt status, as required by Code section 6104(c).

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

Sincerely,



Karen A. Skinder
Appeals Team Manager

cc:



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY

Internal Revenue Service
55 N. Robinson, MC: 4900-OKC
Oklahoma City, Oklahoma 73102

ORG
ADDRESS

Taxpayer Identification Number:

Form:

Tax Year(s) Ended:

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.

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,

Renee B. Wells
Acting Director, EO Examinations

Enclosures:
Publication 892
Publication 3498
Report of Examination

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LEGEND

ORG = Organization name Organization = organization XX = Date
Address = address City = city State = state DIR-1, DIR-2, DIR-3 &
DIR-4 = 1ST, 2ND, 3RD & 4TH DIRECTORS VO-1, CO-2, CO-3, CO-4 & CO-5 = 1ST,
2^{NS}, 3RD, 4TH & 5TH COMPANIES

ISSUES:

Whether ORGs (ORG) dba Organization is operated exclusively for exempt purposes described within Internal Revenue Code section 501(c)(3).

Whether ORG had the substantial nonexempt purpose of providing debt management program services to the general public.

Whether ORG was operated for the purpose of serving private rather than public interests.

FACTS:

Background and History:

ORGs (ORG) dba as Organization, was initially created by DIR-1 and DIR-2, a husband and wife, and also members of the board of directors. DIR-1 was the initial board chairman. One board member quit the board to pursue private interests leaving the DIRECTORS's and one other board member on a three-member board. Initially DIR-2 was designated as the President and DIR-1 as Vice President, Secretary and Treasurer. It was also resolved that DIR-1 and DIR-2 would serve as the day-to-day co-operations directors of the organization. DIR-1 and DIR-2 were also authorized to sign checks.

Certificate and Articles of Incorporation were filed with the Secretary of State of State as a Domestic Non-profit Corporation May 28, 19XX. ORG's stated purpose is "*organized exclusively for one or more of the purposes as specified in Section 501(c)(3) of the Internal Revenue Code, including for such purposes, the making of distributions to organizations that qualify as exempt organizations under section 501(c)(3) of the Internal Revenue Code, or corresponding section of any future federal tax code.*" The Articles of Incorporation also states ORG's purpose is

"
financial actions, including but not limited to: the payment of debt; debt management; budgeting; living with credit and debt free living. Negotiate payments between creditors and consumers, obtain the negotiated payments from consumers and pay the creditors. The education of the general public about responsible financial actions through print, radio, television, seminars, lectures, video, and individual counseling. To circulate financial products and seminars, developed or purchased, to aid consumers in the

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payment of debt; debt management; budgeting; living with credit and debt free living. To aid whenever possible in the enhancement of a persons credit through negotiations with creditors."

On March 12, 19XX, the Internal Revenue Service (IRS) issued Letter 1045 to ORG stating that it was exempt from federal income tax as an organization described under section 501(c)(3) of the Internal Revenue Code (IRC) or "the Code"). ORG also received an advanced ruling that it was publicly supported within the meaning of IRC section 509(a)(2) of the Code. On January 11, 20XX, the IRS issued Letter 1078 confirming exempt status under IRC section 501(c)(3) with a definitive ruling that ORG was a publicly supported organization described under IRC 509(a)(2).

On February 8, 20XX, the IRS notified ORG of a pending examination of its books and records to be conducted beginning March 18, 20XX. Specifically, Form 990 for the tax year ended December 31, 20XX was selected for examination. The examination was subsequently expanded to include the tax year ended December 31, 20XX, and ORG was notified in writing of the audit expansion on May 7, 20XX.

ORG's current mailing address is Address, City State. The physical office location is Address, City State. In the beginning of ORG's existence, the organization's principal office was located at Address, City State. The organization was relocated to City sometime during 20XX and resumed operations at Address, City State, until sometime in 20XX when the organization was moved to the current Address address.

Governance:

ORG was initially created per Certificate and Articles of Incorporation filed with the State Secretary of State Office on May 28, 19XX. Article Four indicates five initial corporate directors, however only four are listed. The four listed are DIR-2 and DIR-1, DIR-3 and DIR-4.

At the first meeting of the board of directors on September 14, 19XX, three board members were present, DIR-1 and DIR-2, and DIR-3. According to minutes, DIR-1 was unanimously voted the Chairperson and DIR-2 was elected Secretary. Further, it was resolved that DIR-2 D. and DIR-1 were assigned signing authority for all checks, drafts and other instruments obligating the corporation to pay money.

In addition to their board member positions, DIR-1 and DIR-2 are also self-elected officers of ORG. During the initial meeting it was noted during election of officers, a unanimous vote to elect DIR-2 as President and DIR-1 as Vice President/Treasurer/Secretary. It was also resolved that DIR-1 and DIR-2 would act as the day-to-day Co-Operations Directors. Officer compensation was discussed and established as follows:

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President	\$	DIR-2
Vice President		DIR-1
Secretary		DIR-1
Treasurer		DIR-1

It was resolved the salaries will be waived until the corporation is on a more financially sound footing. These salary amounts were never realized in any year of this examination or prior years.

Subsequent annual board meetings usually took place in the first quarter of each year. It is noted in all meetings, board minutes indicate DIR-1 and DIR-2 were present as directors as well as board members. Aside from DIR-1 and DIR-2, other board members would come and go, usually never leaving a board of more than three members present during meetings. DIR-1, the father of DIR-1, and now deceased, attended some of the meetings as a board member. During the examination the DIRECTORS's stated they have always found it difficult to attract new board members because of liability concerns of potential board members.

Bylaws, Article 3, Section 1, Directors, states the corporation shall have Three (3) or more directors.

Bylaws, Article 3, Section 11, Quorum for Meetings, states a quorum shall consist of a majority of the members of the Board of Directors, as long as, the majority is three or more of the members of the Board of Directors. Also, no business shall be considered if the required quorum is not present and the only motion the Chair shall entertain is a motion to adjourn.

For the following annual board meetings, for which a quorum was present, a majority of the attendees were shown to be family members.

09-14-19XX	Initial meeting - two out of three attending board members are family members
06-10-19XX	Three out of four attending board members are family members
04-08-1998	Two out of three attending board members are family members
03-09-1999	Three out of four attending board members are family members
04-13-20XX	Two out of three attending board members are family members
03-05-20XX	Two out of three attending board members are family members
02-05-20XX	Two out of three attending board members are family members
02-03-20XX	Two out of three attending board members are family members
01-03-20XX	Two out of three attending board members are family members
01-10-20XX	Two out of three attending board members are family members
02-06-20XX	Two out of three attending board members are family members
01-08-20XX	Two out of three attending board members are family members

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With two, sometimes three of the attending members being members of the DIRECTORS family, the board is effectively a family controlled board.

Activities:

Debt Management Program:

TP provides as one option to a client's financial difficulties a debt management plan (also referred to as Debt Consolidation). The agreement enables ORG to provide debt management services where by the client agrees to make payments to ORG which are then disbursed to the client's creditors. The agreement states the purpose of the debt consolidation program is to educate the client on financial matters, get the client out of debt and save the client money. ORG services include negotiating lower payments, lower interest rates, reduction in late fees, reduction in over-the-limit fees and indicates creditor benefits will vary depending on the creditor and their particular debt management plan. ORG will assist in preparing a household budget, negotiate with creditors and handle payments. The client or ORG may cancel the agreement at anytime with 48 hour written notice. ORG will notify creditors once a DMP is completed. A monthly fee is charged to process money orders, cashier checks and electronic payments (\$ in 20XX, \$ in 20XX) through CO-1. A one-time set-up fee of \$ is charged and is included with first payment and is to cover the cost of labor involved in data entry and paperwork involved in establishing a client into the DMP. Client is to agree to making a "voluntary" monthly contribution of \$ to cover "the expenses of the DMP" for unsecured debt, and an additional \$ for "educational material" to cover the cost of monthly mail outs to clients. Both of these "contributions" is to be included with the client's monthly payment. All contributions, fees, charges or expenses of ORG are deducted first from the client's monthly payment to ORG before client's creditors are paid. ORG's DMP agreement also stipulates the client will incur an additional \$ "contribution" if any unsecured debt is included in the plan. All contributions in the event of discontinuing the DMP are non-refundable. Client is to agree not to hold ORG or any of it's employees, directors, or officers responsible for any claim, suit, or action which may arise as a result of the DMP agreement for negligence. In addition to the already mentioned fees and charges, an additional \$ fee may be automatically deducted by ORG for any funds not paid by client's bank for any reason and also an increase in the monthly payment amount by \$ (\$ in 20XX). The agreement summary page includes the client's identifying information, amount of debt owed, negotiated monthly payment amount, estimated time to complete the plan and monthly payment due date. Nowhere in the agreement is there mention of any fees, or other charges being eligible for waiver or reduction in hardship situations.

Per information provided by ORG, in 20XX, a total of 338 caller leads were worked by phone. Of these, 91 clients signed DMP agreements. Of this total 28 signed up using money orders for payment and 63 utilized the electronic fund transfer option. The only information provided for 20XX was 21 cleints signed DMP agreements.

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Organization indicated it conducts most all of it's business with clients over the telephone or by email. There are no in-office visits or counseling sessions. ORG indicated it, on average, spends about 20 minutes per initial call with additional time expended if follow-up consultation is required. This average time is for all calls whether or not the client signs a DMP agreement. During the initial call bills are discussed and creditor information is obtained and a budget is worked with the client over the phone or the client can email or call back with information.

TP did not provide information about how the fees are determined, simply that they are "spelled out in the contract." TP indicates fees are voluntary, however the wording in the DMP agreement indicate these fees are required. Organization indicated 95% of clients pay the fee. This does not indicate the clients would pay if they knew they didn't have to. Apparently the organization does not volunteer this waiver information unless asked.

According to the organization, fees waivers depend on the budget information, directors and certified counselor are authorized to waive fees and are considered upon request by the client. For those fees waive, all are fully waived, there are no partial waivers. If a client does not want to pay the fee, TP claims counselor is instructed to waive the fee without manager consultation, again however, waivers of fees are not volunteered information provided to the client and is provided only if the client raises the question. TP claims it does not turn away clients because they do not want to pay their fees. About 5 percent of clients on DMPs did not pay any fees due to hardship situations.

TP claims it will work with both unsecured and secured debt and actually encourages this so the client can work toward being totally debt free.

TP stated monthly payment amount and payment term is determined by the creditor.

Qualification for a DMP depends on the budget and whether or not DMP payments are affordable after determining disposable income. If a client has less disposable income than the determined monthly DMP payment the counselor works with the client to rework budget (revising spending where possible). ORG indicated there is no minimum monthly payment required, no minimum total debt a client must have, and no maximum amount of income a client must have to qualify for a DMP. If a client does not qualify for a DMP the counselor helps to rework their budget initially and then refer them to different social services in their area, have the client go to their local church or have them look in the phone book or go online to obtain services in their area. TP states they do not refer clients to specific organizations by name.

When a client is put on a DMP a contract is faxed or emailed to the client to read over and complete. It is then faxed or mailed back permissions for the TP withdrawal funds from their

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bank account or they can send in a money order. Client forms are reviewed for accuracy prior to implementing. Payments are only accepted by bank draft or money order/cashier check.

If a client does not enroll into a DMP, the TP may send educational information to the client.

Fees charged during 20XX and 20XX for setting clients up on debt management programs include an up-front one-time \$ fee, a required monthly \$ "voluntary contribution" to cover expenses of the DMP, and an additional \$ monthly "voluntary contribution" for educational materials. The \$ fee is for unsecured credit card debt only. If client wishes to also add secured debt or other type of debt an additional \$ monthly contribution is required. There is also a \$/month fee for processing of money orders, cashier checks or electronic payments. There is also a \$ fee for any funds not paid by the client's bank. Similar fees were also charged in 20XX.

Inquiry made as to the number of clients assisted during 20XX. Organization responded by saying all clients were put on debt management plans. Of all leads received about 50% were put on DMPs and the remainder were sent educational materials. Statistical information provided shows 91 total clients signed up for DMPs in 20XX.

During the examination, TP stated they had decided to shut down the business as they are receiving fewer and fewer clients, stating the for-profit debt settlement companies are taking more clients away from them, coupled with the fact many of their current clients are "graduating" from their debt management plans. From this information it appears the DMP activity is a very important activity for this organization and crucial to the funding and existence of this organization.

Counseling sessions:

ORG's exempt purpose as stated during the initial interview is to reach people with financial problems and provide education and educational materials in a Christian format. During 20XX-20XX, activities primarily consisted of taking calls from individuals with debt/credit related problems. The counselor listens to the caller, evaluates the client's situation and makes a determination of possible workable solutions which include debt management programs, education, working with creditors, referral to other organizations, and credit repair.

During 20XX-20XX, the organization published a limited amount of educational materials but did possess and have access to significant amounts of third party pamphlets, booklets, brochures and forms to carry out the education of their clients in conjunction with the telephone counseling session. Some of the sources of educational materials include the Federal Trade Commission (FTC), various credit card companies and other sources.

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Agent's observation of office activity to include listening in to call-ins revealed sporadic calls. Some days there are few if any calls, and other days there are more. Callers seem to be mainly interested in getting on a debt management plan, partly due to the DMP promotion on their website. Depending on the caller's situation dictates what action is taken. If the caller is determined to require a personal in-office counseling session requiring time to sort through bills and perform budgeting analysis and discussion of lifestyle changes, then the caller is referred to other organization's affiliated with CO-2 TP does not do in-office counseling, only by phone.

Most callers hear about the organization online, thru the website. If the caller calls in for a debt management plan, the information is received over the phone or mailed in. The DMP agreement is then provided either by mail or online for the individual to sign. A budget is worked up over the phone with the client as the counselor inquires about creditors owed, types of expenditures made, nature of employment, family size, living arrangements and other factors which are considered to basically determine whether or not the client can afford to realistically work within a debt management plan.

Educational:

As previously mentioned, during 20XX-20XX, the organization published a limited amount of educational materials but did possess and have access to significant amounts of third party pamphlets, booklets, brochures and forms to carry out the education of their clients in conjunction with the telephone counseling session. Verbal educational information by telephone during the call-in, or mailed information was provided to about one-half of the DMP sign-ups, in connection with the telephonic counseling session was the extent of education information provided by the organization.

The examination revealed most of the educational information provided to clients by mail was information provided at no charge or minimal cost to the organization from various third parties to include governmental organizations and credit card companies.

The TP did not do much in the way of educational outreach i.e. seminars, etc. TP indicated it's very difficult getting local schools to buy into this organization's desire to provide seminars because of the "Christian" component inherent in the TP's activity and the issues of conflict between church and state. TP has previously set up workshops and seminars "in-house" and advertised, but very low turnout or no turnout caused the workshops to be discontinued. ORG also stated they prepared for 3 workshops which no one attended. It was claimed they spent 3-4 hours preparing for these workshops. Organization indicated intention present to provide outreach but the fact remains no significant outreach education was conducted. Therefore educational outreach activities was shown to effectively be discontinued.

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TP indicated many of their clients just want a "quick fix" to their problems and are not interested in change of behavior or lifestyle. They simply want their problems to "go away." In these situations the client is asked for the necessary information to place the client on a debt management plan and receives an up-front fee in addition to the monthly payments paid to the TP by the client which is sent to client creditors. However, the TP does make repeated attempts to provide the needed education through mailings of educational materials whether they ask for it or not.

Loans From Officers:

During the examination, organization disclosed DIR-1 and DIR-2 had loaned money to ORG for startup costs initially when the organization was established during the mid 90's. Additional loans were also made to cover a shortage of capital during operations in 20XX. The following information regarding the loan activity was provided:

	<u>20XX</u>	<u>20XX</u>	<u>20XX</u>	<u>Totals</u>
Loan Balance on January 1		-	-	
<u>Loan Repayment Activity</u>				
DIR-1				
DIR-2				
CO-3 (DIRECTORS)				
Other personal charges made by DIRECTORSs toward loan deduction				
CO-4 and Misc Charges				
Payee unknown				
Mispostings/corrections to Loan Acct				
Security Service Card				
Total Loan Reduction				
<u>Additional Loan Activity</u>				
Additional Loans Made to ORG by DIR-1 and/or DIR-2				
Total Additions to Loan				
Loan Balance on December 31				

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The organization balance sheet for the year ended 20XX showed a balance of \$ owed to the DIRECTORSs by ORG. During the examination the agent attempted to establish amounts loaned, loan dates, existence of loan documentation containing loan terms, etc. The organization provided a spreadsheet showing as of 12/31/20XX a balance owed to the DIRECTORSs of \$. During 20XX an additional \$ was loaned to ORG from the DIRECTORSs as well as an additional \$ later that year. In 20XX, 20XX, and 20XX, various amounts were paid to the DIRECTORSs to pay back the loan. Additional loans from the DIRECTORSs were being made to ORG, again absent any loan documentation being drawn up for the loans. During 20XX it was shown many significant payments being made to the DIRECTORSs, in an apparent attempt to pay back the DIRECTORSs as they had indicated during the examination they were going to shut down the organization. Not only did the loan get paid back but the DIRECTORSs continued to receive additional payments after the loan was paid. As there is no loan documentation, there is no substantiation that the payments received by the DIRECTORSs are in fact amounts deemed to be repayment for a loan they claimed to have made to ORG.

Contrary to statements by the directors, there is no board resolution in board minutes for any loan activity. Form 990, signed by DIR-1, reports a \$ beginning of year balance on a loan from an officer, director, trustee or key employee. (page 4, line 63) in 20XX and \$ beginning of year balance for 20XX. However, on Schedule A, Part III, question 2b, the organization answers “no” to the question of whether a loan was made with a trustee, director, officer, key employee or member of their family. Additionally, no interest expense was reported on page 2, line 41.

Neither ORG or either of the DIRECTORS’s have provided any other documentation evidencing a loan: no promissory note or other evidence of indebtedness, no record of the rate and amount of interest, no evidence of any security or collateral, and no fixed maturity date. While there were some records of alleged repayments by ORG to the DIRECTORS’s, the repayments and the records were sporadic, haphazard, and informal. Information provided regarding reasons why the loans were necessary do not provide substantiation of the loans.

During the examination, the directors provided documentation of a personal home equity loan they took out against their personal property to create a funding source to loan funds to the exempt organization they control. The source of the funds loaned by the DIRECTORS’s is not relevant to the issue of substantiation of a loan from the directors to the organization they control and are two separate transactions. Again, no documentation of the loan from the officers to ORG was provided.

This issue is addressed under the Intermediate Sanctions rules of Internal Revenue Code section 4958 for inurement and excess private benefit in a related case.

Related Entity – CO-5

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CO-5 (CO-5), a for-profit entity previously controlled by DIR-1 and DIR-2, currently the directors of ORG. CO-5 was dissolved in 19XX, shortly after ORG was incorporated.

TP stated in the examination that CO-5, Inc. was in the business of credit report restoration but was dissolved in 19XX due to the Credit Repair Organizations Act of 19XX which prohibits selling of any "credit repair" services for an up front fee. The act required that the clients would have 6 months to pay the fee after the services were completed. The State Attorney General had the Sheriff serve papers to cease and desist the service of credit repair with up front fees and this is when CO-5 was dissolved.

From all information gathered during the examination, CO-5 was dissolved for providing credit repair services for an upfront fee and was shutdown as a result of this activity. ORG was then started up to provide credit counseling and debt management plans within a Christian atmosphere. Credit repair for was not pursued by ORG.

LAW:

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.

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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

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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

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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.

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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.

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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 providing the 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 organization operated 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.

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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

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501(c)(3) of the Code because a substantial purpose of the 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.

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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’d* 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.

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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.

Government Position:

First, you lack the public support and public control that are characteristic of a charitable organization seeking to serve the public. You are not supported by contributions from the general public, government or private foundation grants, or assistance from the United Way, with only an incidental part of your revenue from counseling fees, as were the credit counseling agencies in Consumer Counseling Service of Alabama, and Credit Counseling Centers of Oklahoma, *supra*. In fact, you do not even have a fundraising program to solicit such contributions. According to your 20XX and 20XX Forms 990, you receive all your revenue from fees from setting up client’s DMPs, fair share from creditors and credit repair fees. You are similar to the organization described in B.S.W. Group, *supra*, in which the court cited lack of solicitation and sole support from fees as factors disfavoring exemption.

Though you indicated you provide educational pamphlets, brochures, and other educational media, and also store a considerable amount of educational material at your facility premises, you submitted no evidence that you provide any significant educational programs or activities.

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 during the examination demonstrates that counseling activities and educating the public on credit issues are an insubstantial part of the activities you conduct.

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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 95%) will be derived from fees charged to clients enrolled in your debt management program. Though you may view some of the fees you charge as “voluntary contributions,” we have determined that they are in fact fees received in exchange for the sale of a program related service.

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 95%) will pay some amount of your requested “contribution” is evidence that your clients do not perceive these payments as voluntary. Additionally, your DMP agreement provided to clients does not stipulate any waiverability or reduction of the \$ monthly “voluntary contribution” to cover your DMP expenses and the \$ monthly “voluntary contribution” to cover educational materials.

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 only 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 programs to solicit such contributions. According to financial information submitted and information reported on your Form 990 primarily all revenues are derived from client fees/service charges/first payments and fair share payments related to your debt management program. 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. A large proportion of your revenue is expended to pay DMP related costs. In having a paid staff with no volunteer help, and having little or no direct expenditures for charitable purposes, you are similar to the organization described in Easter

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House v. United States, *supra*, where the court determined that the organization was not exempt because its conduct of adoption services was in furtherance of a non-exempt commercial purpose.

You reported significant advertising expenditures. Like many commercial businesses, you advertised in local media and other publications. You also had your own website developed to promote and sell your services in ways that are typical for any for-profit business. Though you initially indicated in interviews you did not advertise for other businesses, we note your display of many hyperlinks to other for-profit business's websites containing information about those businesses and advertisements of their products and services, thereby providing a private benefit to those businesses. Though you stated the links are reciprocal links aimed to increase your search engine standing, the fact remains links to for-profit entities existed on your website whereby a visitor to your website is afforded the opportunity to provide a benefit to those companies. Though your website has been changed, the prior version is noted.

It appears your organization was established in the same time frame in which the for-profit entity U.S.A. Credit, Inc., formerly controlled by your current directors, was dissolved (19XX). You indicated in interviews that the local sheriff's office served notice to U.S.A. Credit that it was to cease and desist the charging of clients an up-front fee for credit repair services (forbidden under the Credit Repair Organization Act of 19XX). 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. During the years under examination you received fees charged to clients for credit repair services. You have not substantiated the fees were not charged in advance of the service provision. Your apparent attempt to avoid regulation under the CROA also indicates that you continue to operate for a substantial non-exempt purpose. 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 is one of your purposes, you are not entitled to exemption.

In addition to operating for substantial non-exempt purposes, 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 document a loan to you by it's creators. Further you have failed to show that you do not substantially benefit the private interests of the creators through the loan payments made to them. Absent a loan document, there is no substantiation of loan terms to

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include regular payment amounts, interest rate, collateral, etc. Typically banks would require collateral and interest. Absent any documentation, there is no way to establish accurate loan information. Also, after the loan to the creators was paid back during 20XX, the creators then made additional draws resulting in \$ now being owed to your organization, as of your 12/31/20XX balance sheet. This represents funds which inure to the benefit of the creators DIR-1 and DIR-2.

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 two or three individuals of which two members are the creators which are husband and wife. This would indicate a closely-held family controlled board. A board with so few people 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. 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.

Based on our examination of your organization operations and records, and interviews conducted, 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 its creators DIR-1 and DIR-2, through the marketing and sale of DMPs 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.

CONCLUSION:

ORGs (ORG) dba Organization is not operated exclusively for exempt purposes described within Internal Revenue Code section 501(c)(3).

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ORG engaged in a substantial nonexempt purpose of providing debt management program services to the general public.

ORG was operated for the purpose of serving private rather than public interests.

Accordingly, you no longer qualify for exemption as an organization described in section 501(c)(3) of the Code effective January 1, 20XX, and you must file federal income tax returns.

Contributions to you are no longer deductible under section 170 of the Code.

Taxpayer Position:

Taxpayer position is unknown as of the mailing of this report.