

**Internal Revenue Service**

**Department of the Treasury**

TEGE Appeals Programs  
300 N. Los Angeles Street  
Los Angeles, CA 90012

Release Number: 201043052  
Release Date: 10/29/10  
Date: August 2, 2010

**Taxpayer Identification Number:**

**Person to Contact:**

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

**Refer Reply to:**

AP:LA:EMW

**In Re:**

**Tax Years ending:**

**UIL Index:**

501.03-00  
501.36-00

**CERTIFIED MAIL**

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 for all years beginning on or after January 1, 2005. You are required to file federal Form 1120 for the year(s) shown above.

If you decide to contest this determination under the declaratory judgment provisions of Code section 7428, a petition to the United States Tax Court, the United States Court of Claims, or the district court of the United States for the District of Columbia must be filed before the 91<sup>st</sup> (ninety-first) day after the date this determination was mailed to you. Contact the clerk of the appropriate court for rules for filing petitions for declaratory judgment. To secure a petition form from the United States Tax Court, write to the United States Tax Court, 400 Second Street, N.W., Washington, D.C. 20217.


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  
TE/GE: EO Examinations  
1100 Commerce Street, MS 4900-DAL  
Dallas, TX 75242-1027

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,

Sunita B. Lough  
Director, EO Examinations

Enclosures:  
Publication 892  
Publication 3498  
Report of Examination

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer  <b>ORG</b>		Year/Period Ended December , 20XX thru December 20XX

**LEGEND**

ORG = Organization name      ORG-1 = ORG-1      XX = Date      Address = address  
City = City      State = state      website = website      President = president  
Secretary = secretary      DIR-1, DIR-2 & DIR-3 = 1<sup>ST</sup>, 2<sup>ND</sup> & 3<sup>RD</sup> DIRECTORS  
HS-1, HS-2, HS-3 & HS-4 = 1<sup>T</sup>, 2<sup>ND</sup>, 3<sup>RD</sup> & 4<sup>TH</sup> HIGH SCHOOL      CO-1, CO-2, CO-3,  
CO-4, CO-5 & CO-6 = 1<sup>ST</sup>, 2<sup>ND</sup>, 3<sup>RD</sup>, 4<sup>TH</sup>, 5<sup>TH</sup> & 6<sup>TH</sup> COMPANIES

**ISSUES**

Should ORG's Federal tax exempt status under IRC section 501(c)(3) be revoked for failure to operate exclusively for exempt purposes described under such section?

**FACTS**

**Background of ORG**

ORG (hereinafter is referred to as ORG) was formed on January , 20XX in City, State by President. ORG was formerly known as ORG-1 In its Form 1023 Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, ORG states, *"This organization was formed for the purpose of providing credit counseling, negotiation, and debt management services to the public at no cost."*

In February 20XX, ORG applied for Federal tax exempt status and was subsequently recognized as an organization exempt from Federal income tax under IRC section 501(c)(3) and 509(a)(2). ORG serves residence of City County and surrounding areas.

**Board of Directors**

ORG's Board of Directors include:

- President, President and Counselor.
- Secretary, Secretary. Secretary is a registered nurse with CO-1.
- DIR-1, a PhD in clinical psychology.
- DIR-2, a nurse.

Of the Directors above, only President is trained in the financial and credit counseling fields. President is certified by the )

. In addition to holding the office of the president, President also runs the day-to-day activities of ORG. The other Directors do not get involved in ORG's activities. The Directors meet twice a year.

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ORG		December 31, 20XX thru December 31, 20XX

During the tax years under audit, ORG had two employees, President and a receptionist. President performed debt management and counseling activities while the receptionist performed office duties and processing debt management clients' applications. Currently, ORG has four employees:

- One certified counselor (President).
- One non-certified/in-training counselor.
- Two receptionists.

**Debt Management Program (Debt Consolidation Program)**

According to President, debt management program (DMP) services accounted for percent of ORG's total activities. ORG enrolled 240 DMP clients during the tax years ended December 31, 20XX.

The DMP service begins with an individual calling ORG. If the individual needs to talk to the Counselor, the receptionist will transfer the call to the Counselor.

If the individual did not know what ORG does, the receptionist would describe what ORG does using a telephone scrip. The following is the content of the telephone scrip:

- *We lower your interest rate*
- *We lower your finance charges*
- *We lower your monthly payments*
- *You only make a single monthly payment*
- *We stop over limit fees, if there are any*
- *We stop collection calls, if there are any*
- *We also offer free seminars on budgeting and how to establish/re-establish your credit.*

According to the receptionist, she never had to go to the last bullet point of the telephone script advising the individual of the free seminars. If the individual wants to make an appointment, the receptionist would make an appointment to have the individual come to the office. The receptionist would provide the individual with a budget form and instruct the individual to fill it out and bring it to the appointment. She further informs the individual on what to bring to the appointment, credit cards statements, etc. Once the individual got to ORG's office, the session will begin.

**Step 1 – Gathering Income and Expense Information**

If the individual did not fill out the budget form or only partially filled out the form, the Counselor will ask for the missing information to complete the form. The Counselor asks for information such as:

- Income and expenses



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- Balance of debt
- Debt information
- Any underlying reasons, etc.

### **Step 2 – What Are the Options**

Once the Counselor gathered all income and expense information, he will recommend one of the following options:

1. Debt Management Program – If the individual has sufficient income to repay debts, the Counselor will offer DMP. The Counselor will go over the benefits of the DMPs, such as lower interest rate, lower finance charges, lower monthly payment, stop over limit and late fees, stop collection calls, and shorter pay off time. If the Counselor believes the individual is over-spending on an item (paying too much for phone bills) or paying for unnecessary expenses (cell phone for a 12 year-old kid), the Counselor will recommend cutting down or getting rid of these expenses accordingly. The Counselor also provides the client with a 8-page brochure. The contents of the brochure are as follow:
  - Important Information (4 pages) – discusses the benefits of DMP and covers questions and answers about DMPs.
  - Tips About Spending (1 page) – contains 10 tips on spending.
  - Mission Statement (1 page) – describes ORG's mission, which is also available on ORG's web site. The mission statement almost exclusively discusses DMP. At the end of the page, a phrase \_\_\_\_\_ was disclosed.
  - Budgeting, Credit Re-establishment / Establishment, and Credit Report Information (1 page) – informs the clients about how bill consolidation can improve their situation in renting an apartment or qualifying for employment. ORG also informs the clients of classes on budgeting and improving credit FICO scores.
  - Budget Form (1 page) – fill-in-the-blank income and expense items.
2. Bankruptcy – if the individual did not have sufficient income to repay debts, the Counselor will inform the individual there is nothing ORG can do for them. If there is no other alternatives, the Counselor will advise the individual to consider filing bankruptcy and refer him or her to a bankruptcy attorney. The Counselor also recommends to the individual to cut down spending. The Counselor further provides the individual with the same brochure provided to DMP clients. With this, the session ends. The counselor does not refer the individual to other organizations for assistance.

### **Step 3 – Processing DMP Clients**

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Once the client signs up for the DMP, the Counselor will enter the client's information into the database. The data base will assign a client number. The application package will go to the Receptionist for processing. The Receptionist will send the proposal to the client's creditors. If the client's accounts are not in collection status or if the creditor is one of the law firms, the proposal will be sent electronically via email to CO-2. CO-2 will forward the proposal to the client's creditors. If the client's accounts are in collections or if the creditor is a law firm, the proposal will be faxed to the creditor. If the creditors accepted the proposal, they will respond accordingly.

If the creditors wanted the terms of the proposal changed, such as higher monthly payment amounts, etc., they will inform ORG of the changes. Either the Counselor or the Receptionist will contact the client to inform the client of the changes and ask whether or not the client wants to proceed with the DMP. If the client agreed to the changes, the Receptionist will send the modified proposal to the creditors for approval.

Once the client is admitted into the program, the Administrator will send a welcome package that includes the following 3 letters:

1. Credit Counseling Bureau of City County Inc Guidelines.
2. A letter informing the client that a proposal has been sent to their creditors.
3. A letter advising the client of the responsibilities once admitted into the DMP.

The Counselor makes no further contact with the clients. If the client contacts the Counselor for questions, the Counselor addresses them accordingly. A review of 10 client files obtained during the examination discloses no evidence of the Counselor following up with the clients after they signed on to the DMP program.

**Step 4 – Receiving Payment from Client and Disbursing Payments to creditors**

The client selects a date where he or she wants the fund to be withdrawn from his or her bank account for the purpose of repaying debts and paying the monthly DMP management fee to ORG. ORG contracts with CO-3 to withdraw the fund from the client's account. CO-3 holds the client's fund for five days after it withdraws the funds and then forwards the funds to ORG's bank account. Once ORG receives the funds, it will forward the funds to CO-2 the next day. CO-2 will disburse the funds to the client's creditors accordingly. Once a month, ORG sends an invoice to the client informing the client of the amount ORG has paid to the client's creditors.

ORG charges DMP clients an initial set up fee of \$ and a monthly management fee of \$. The monthly management fee is included in the scheduled monthly payment and is automatically withdrawn from the client's bank account.



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**Counseling Activities**

According to President, the counseling activities account for     percent of ORG's total activities. The counseling activities include people calling ORG with questions about their credit card problems, credit report, etc. If the caller qualified for DMP, the Counselor will sign the caller up. If not, the Counselor will advise them on considering bankruptcy and refer them to a bankruptcy attorney.

During the field audit on April 30, 20XX, the Agent listened to a live face-to-face counseling session between the Counselor and a client. The client came in with the budget form filled out and credit card statements ready. The client is currently working. She has been current with her credit card payments. However, her concern was that once Medicare stops paying for her benefits and she has to pay the costs on her own, she will not be able to keep up with the credit card payments. Once she's behind, the interest rate will go up, and she won't be able to pay off the credit card debt balances. The counselor went over the budget form to clarify the client's responses. The following is a partial conversation between the client and the Counselor.

*Counselor: You pay \$ for cable.*

*Client: Yes. I got the maximum. I also have phone bill included in it.*

*Counselor: you put down \$ for food.*

*Client: I went to CO-4.*

*Counselor: How much do you spent?*

*Client: Few hundred. I buy dried stuff at CO-4. They last for months.*

*Counselor: How often do you buy groceries?*

*Client: Weekly.*

*Counselor: You spend \$ a month on clothes.*

*Client: Yes. I spend at least \$ on clothes. I buy nice things. I put them on credit cards.*

*Counselor: You spent \$ on entertainment.*

*Client: I belong to the     . We play cards and go out for dinner.*

*Client: I am on     . I will not be soon. I have to pay \$/month for my prescriptions.*

*I have to make a decision, to pay for     or get behind.*

*Counselor: Let me see how much you owe altogether.*

The Counselor went over the balance of each credit card and came up with approximately \$ in credit card debt.

The Counselor offered DMP to the client and informed her that she will pay \$ per month under the program and it will take her 30 months to pay off the balance.

*Client: So it is not much lower than what I am paying now.*

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*Counselor: Yes. But the advantages are:*

*You cut only one check.*

*We send out an invoice to you to notify you how much we pay the credit card companies.*

*The credit card companies will send statements to you to show the payment balance.*

*Client: What's about the interest rate?*

*Counselor: The interest rate will be lower, except for the CO-5. It will be about 15%.*

*They only lower it by % . Right now, your interest rate is % .*

*Client: How much does it cost me to do this?*

*Counselor: We charge a \$ set up fee and a \$ monthly fee.*

The client agreed to sign up for the DMP. The Counselor instructed the client to pick a date where she wants the funds withdrawn from her bank account. The client signed the debt consolidation agreement and direct payments authorization agreement; selected a withdrawal date and paid the \$ setup fee.

*Client: I don't want to give up all of my credit cards. Can I keep one?*

*Counselor: Yes. You can keep the one with the lowest interest rate.*

*Counselor: You need to find a way to cut down your entertainment and clothes. You can save lots of money.*

*Client: Yes. I already began cutting back. My prescription is killing me. The Advair is the most expensive one, \$/month. They will be switching to a generic drug. That will save me some.*

*Counselor: Use credit cards wisely. Some people buy things they don't need. I will give you two business cards. Give one to your friend. I will give you some paper to bring home. If you have nothing to do, read them. The credit card companies make money on interest. Call me if you have questions.*

The Counselor cut up the credit cards and ended the session.

### Education Activities

According to President, ORG conducts educational seminars both in-house and outside.

#### In-House Seminars

According to President, the in-house seminars accounted for percent of the total activities during 20XX. In 20XX, ORG conducted seminars once a month.

Approximately 10-12 people attended each seminar and 8 on average. In a written response received by the Revenue Agent (Agent) on July , 20XX, President

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disclosed that ORG also conducted educational seminars in April, June, September and December 20XX.

The seminars were conducted by President. President sent letters to City residences and business establishments to notify them of the seminars. President got the addresses from the Yellow Page. President, however, did not produce the list of the individuals whom he contacted to offer the seminars. ORG also states on its web site that it offers free seminars. President also informs the callers of the classes when they called in for counseling. The subjects for the seminars included:

- Credit report
- Establish and re-establish credit
- Budgeting
- Financial management

The materials used for these seminars are taken from the Financial Guide book and other books that President used in the face-to-face counseling sessions.

ORG also provided no documentation such as sign-up and attendance sheets for the seminars. According to President, when people attended the seminars, he did not ask them to sign-in or take their name and contact information. Each seminar lasted from 1 to 1 ½ hours. President did not think that he had to prove to anyone that he conducted these seminars.

Out-Side Seminars

President also conducted seminars and presentations to schools and other organizations. In 20XX, President conducted 5 presentations to the following high schools and organizations:

- HS-1 – on the use of credit cards
- HS-2 – on the use of credit card
- HS-3 – re-establishing credit
- HS-4 – organized by the City to get people off welfare and get back to work. Part of the program is establishing credit for employment purposes
- Mental institution for people who can function with medication
- Half-way houses

President did not take the name of the participants. He also did not take the contact information of the individuals who requested him to conduct the presentations. According to President, he did not think that he had to prove to anyone that he conducted these classes. Each presentation lasted from 1 to 1 ½ hours. The Agent requested the name of the individuals whom President contacted to offer the seminars

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for the purpose of confirming whether these seminars took place. To the date of this report, such information has not been provided.

**Hiring Practices, Employee's Training and Evaluation**

Other than President, ORG has not hired another counselor. During 20XX, President trained the only Receptionist to take on the duties of a counselor. This Receptionist is no longer with ORG. Presently, President is training his son, DIR-3, to become a counselor. DIR-3 has not yet been certified. President trained the Receptionist in general areas such as:

- Customer services
- Processing DMP clients
- Reading credit reports
- Basics of bankruptcy (chapter 7, 11, or 13, etc.)

The training is provided for the purpose of handling callers' questions. As for President's on-going training, he takes CPE classes once every 3-4 years. In addition, he also reads books to educate himself on credit counseling matters. Some of the books include:

- *The ABC's of Getting Out of Debt*
- *Planning and Protecting Your Financial Planning*
- *Making Cents – Money, Debt, and Credit*
- *American Credit and Financial Guide*
- *Foreclosure Preventing Counseling – Reserving the American Dream*

**Advertising Practices**

ORG primarily advertises its debt consolidation program in the Yellow Pages and Penny Saver. The following is ORG's advertising in the PennySaver and Yellow Pages:

**DEBT CONSOLIDATION  
CREDIT CARD BILLS**  
LOWER single monthly payment.  
LOWER interest rates. SAVE  
\$'s on finance charges.  
STOP Collection Calls!  
#

**Credit Counseling Bureau of City County**  
**DEBT CONSOLIDATION**  
Lower Monthly Payments  
Lower Interest Rates

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Save Thousands of \$\$\$  
 In Finance Charges  
 Stop Harassing Phone Calls  
 Member B.B.B.  
 #

ORG also advertises in the Spanish Yellow Pages. The following is the translation of a Spanish ad:

**Credit Counseling Bureau Inc.**  
 DEBT CONSOLIDATION  
 Lower Monthly Payments  
 Lower Interest Rates  
 Save Thousands of \$\$\$  
 In Finance Charges  
 Stop Those Annoying Calls  
 #  
website  
 CO-6  
 Address, City, State  
 City, State

ORG maintains a web site. According to President, the web site has not been an effective advertising channel. The clients cannot sign up for DMP online. The web site brings in about 2 DMP clients per month. The following are ORG's web pages.

(ADVERTISEMENT DELETED)

**Financial Information**

ORG's Form 990 shows the following financial information.

	<u>-Dec-XX</u>	<u>-Dec-XX</u>
<b><u>Income</u></b>		
Program service revenue		
Interest income		
<b>Total Income</b>		
<b><u>Expenses</u></b>		
Officer compensation		



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- Salaries & other compensations
- Employee benefits
- Payroll taxes
- Accounting fees
- Legal fees
- Supplies
- Telephone
- Postage and shipping
- Occupancy
- Equipment rental and maintenance
- Travel
- Service charges
- Miscellaneous expenses
- Credit report
- Advertising
- Insurance
- Other professional fees
- Internet & website expenses
- Customer refund
- Excess program payments
- Contributions
- Other taxes
- Printing and publication
- Depreciation
- Total Expenses**
- Excess (deficit) for the year

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The program service revenue was made up of DMP initial set up fees and monthly management fees from DMP clients and DMP related revenue.

**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 Code exempts from federal income tax corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals, no part of the net earnings of which inures to the benefit of any private shareholder or individual,

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no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation (except as otherwise provided in subsection (h)), and which does not participate in, or intervene in (including the publishing or distributing of statements), any political campaign on behalf of (or in opposition to) any candidate for public office.

Section 1.501(c)(3)-1(a)(1) of the Treasury 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.

Treasury Regulations section 1.501(c)(3)-1(c)(1) 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.

Treasury Regulations section 1.501(c)(3)-1(d)(1)(i) states, in general, an organization may be exempt as an organization described in section 501(c)(3) if it is organized and operated exclusively for one or more of the following purposes:

- (a) Religious,
- (b) Charitable,
- (c) Scientific,
- (d) Testing for public safety,
- (e) Literary,
- (f) Educational, or
- (g) Prevention of cruelty to children or animals.

Treasury Regulations section 1.501(c)(3)-1(d)(2) defines "charitable". The term "charitable" is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes which may fall within the broad outlines of "charity" as developed by judicial decisions. Such term includes: relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and

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juvenile delinquency. The fact that an organization which is organized and operated for the relief of indigent persons may receive voluntary contributions from the persons intended to be relieved will not necessarily prevent such organization from being exempt as an organization organized and operated exclusively for charitable purposes. The fact that an organization, in carrying out its primary purpose, advocates social or civic changes or presents opinion on controversial issues with the intention of molding public opinion or creating public sentiment to an acceptance of its views does not preclude such organization from qualifying under section 501(c)(3) so long as it is not an "action" organization of any one of the types described in paragraph (c)(3) of this section.

Treasury Regulations section 1.501(c)(3)-1(d)(3) defines the term "educational". (i) In general, the term "educational", as used in section 501(c)(3), relates 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.

An organization may be educational even though it advocates a particular position or viewpoint so long as it presents a sufficiently full and fair exposition of the pertinent facts as to permit an individual or the public to form an independent opinion or conclusion. On the other hand, an organization is not educational if its principal function is the mere presentation of unsupported opinion.

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. 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 non-exempt commercial purpose that was not incidental to the educational purpose and was not entitled to be regarded as exempt.

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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.

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.2d 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



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identical to those in Consumer Credit Counseling Centers of Alabama, Inc. v. United States, discussed immediately above.

In Solution Plus, Inc. v. Commissioner, T.C. Memo. 20XX-21, the United States Tax Court held that an organization whose principal activity was to market and process consumer debt management plans was not entitled to exemption under section 501(c)(3) because the organization was not organized or operated exclusively for exempt purposes and failed to establish that it did not operate for a substantial non-exempt purpose.

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.

Treasury Regulations section 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, 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.

### **TAXPAYER'S POSITION**

On March 20XX, the Service issued a preliminary report of examination proposing revocation of ORG's Federal tax exempt status under IRC section 501(c)(3) effective January 1, 20XX. In the preliminary report, the Service also solicited ORG's positions on the proposed actions. To the date of this report, ORG has not responded to the Service's proposed actions.

### **GOVERNMENT'S POSITION**

The Government determines that ORG was not operated exclusively for one or more exempt purposes specified under IRC section 501(c)(3). An organization will be regarded as operated exclusively for one or more exempt purposes only if it engages



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primarily in activities that accomplish one or more of such exempt purposes specified under IRC section 501(c)(3).

**Whether ORG was operated for an educational purpose**

The term "education" as specified in IRC section 501(c)(3) includes (a) instruction or training of an individual for the purpose of improving his capabilities and (b) instruction of the public on subjects useful to the individual and beneficial to the community.

When an individual contacts ORG and is not aware of what ORG does, the receptionist would immediately follow a telephone script to inform the individual of all the benefits that ORG can provide if the individual enrolls in the DMP; benefits such as lower interest rate, lower finance charges, lower monthly payments, one single monthly payment, stopping of over limit fees, and stopping of collection calls. The telephone script did not provide for determining the individual's broader financial situation or proposing any alternatives to the DMP. Of the entire telephone script, one bullet point was devoted to informing the individual of free seminars. Even then, according to the receptionist, this point is rarely mentioned to the individual.

There is also no evidence indicating that the ORG's Counselor attempts to devise a personal and specific solution to each client. During the counseling session, ORG's Counselor obtains enough information from the individual to determine whether he or she is qualified for DMPs. If the individual is qualified for DMPs, the Counselor will offer DMPs. If the individual did not have sufficient income to repay debts, the Counselor informs the individual that there is nothing the Counselor can do for them and ends the session. This is evidenced during the live counseling session that the Counselor conducted on April 20XX (refer to Fact section for details). While the client has been current with her credit card payments and has sufficient income to make credit card payments, the client was concerned with her future once Medicare ceases paying for her prescription drugs. The Counselor, however, offered only one solution to the client after gathering necessary income and expense information. The option the Counselor offered was a debt management plan. When the client showed signs of resistance to the DMPs, the Counselor immediately listed the advantages of enrollment in the DMPs, advantages such as cutting only one check, having ORG manage the account, and lower interest rate, to entice the client to sign up for the DMP. The Counselor did not attempt to find out what the client needed or present the client with other options such as following a strict budget that would include cutting down or getting rid of unnecessary expenses or contacting other agencies that offer prescription drug assistance, or both. Although the Counselor noted that the client has been overspending on entertainment and clothes, the Counselor only advised the client of cutting down on these two items at the end of

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the counseling session after the client signed up for the DMPs and paid the initial set up fee.

ORG provides a 8-page brochure to all DMP clients as well as those ORG's Counselor determined were not qualified for DMPs due to insufficient income to repay debts. Of the 8 pages, 4 pages were devoted to answering DMP questions; a one-page mission statement which primarily discusses the benefits of DMPs; one page was devoted to informing how bill consolidation can improve the clients chance of being able to rent an apartment or qualify for employment; one-page containing 10 tips on spending; and a fill-in-the-blank budget form. This indicates that ORG does not tailor its services to meet the specific needs of each individual. Furthermore, a review of the client files did not disclose any evidence of ORG's Counselor contacting the clients after they signed on to the DMP program to follow up on their situation or to find out if they need further counseling.

ORG does not appear to have options other than selling DMPs to clients. ORG received no public and governmental supports. It relies solely on DMP revenue for survival. ORG generated \$ and \$ of revenue for the tax years 20XX and 20XX respectively; 100 percent of which was DMP initial set up, monthly management fees and DMP related revenue.

ORG's web site also primarily promotes DMP, based on size and space devoted. ORG's web site contains 5 tabs, "Home", "FAQs", "Services", "Applications" and "Contact Us". While budgeting classes were mentioned, substantially all of the web pages were devoted to discussing and answering DMP questions.

ORG claimed that in 20XX it offered free seminars on the subject of budgeting to the general public. However, despite repeated verbal and written requests, ORG has not provided evidence that such seminars had occurred.

In summary, ORG's primary purpose was to offer DMPs to the general public for fees. The educational purpose, if any, was insubstantial and secondary. Offering DMPs to the general public for fees did not further an educational purpose as defined by IRC section 501(c)(3). See also, Better Business Bureau of Washington D.C., Inc. v. United States, American Institute for Economic Research v. United States, American Institute for Economic Research v. United States, and Solution Plus, Inc. v. Commissioner.

**Whether ORG was operated for a charitable purpose**

The term charitable as specified in IRC section 501(c)(3) includes relief of the poor and distressed or of the underprivileged. ORG, however, does not restrict its DMP services

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to the poor, distressed, or underprivileged. ORG offers its DMP service to anyone who responds to it advertising.

ORG utilizes the widely distributed directories such as \_\_\_\_\_ in \_\_\_\_\_ and \_\_\_\_\_ and \_\_\_\_\_ to market its DMPs to the general public. The contents of the ads primarily entice debtors to sign up for DMPs by promising them a lower single monthly payment, lower interest rates, saving of thousands of dollar on finance charges, and the elimination of harassing phone calls. Once an individual responds to the ad, ORG makes no determination whether the individual is a member of a charitable class. The only determination ORG makes is whether the individual has sufficient income to repay the debt. If the individual has sufficient income to repay the debts, DMPs service is offered. If the individual does not have sufficient income to repay the debts, ORG's Counselor informs the individual there is nothing ORG can do for them. The Counselor does not refer the individual to other organizations for assistance such as financial or employment.

In summary, ORG offers DMP services to anyone who is qualified for DMPs without making a determination whether the individual is a member of a charitable class. Primarily providing DMP services for a fee does not further charitable purposes. As such, ORG was not operated exclusively to further a charitable purpose under IRC section 501(c)(3). See also Better Business Bureau of Washington D.C., Inc. v. United States, American Institute for Economic Research v. United States, American Institute for Economic Research v. United States, and Solution Plus, Inc. v. Commissioner.

### **CONCLUSION**

Since ORG was not operated exclusively for one or more exempt purposes under IRC section 501(c)(3), its Federal tax exempt status under such section should be revoked effective January 1, 20XX. ORG is liable for filing Form 1120 U.S. Corporation Income Tax Return for the tax year ended December \_\_\_\_\_ 20XX and all years after.