



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Release Number: **201127014**
Release Date: 7/8/2011
Date: April 13, 2011

501.03-00
501.32-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

Tax Years:

Dear

This is our final determination that you do not qualify for exemption from Federal income tax as an organization described in Internal Revenue Code section 501(c)(3). Recently, we sent you a letter in response to your application that proposed an adverse determination. The letter explained the facts, law and rationale, and gave you 30 days to file a protest. Since we did not receive a protest within the requisite 30 days, the proposed adverse determination is now final.

Because you do not qualify for exemption as an organization described in Code section 501(c)(3), donors may not deduct contributions to you under Code section 170. You must file Federal income tax returns on the form and for the years listed above within 30 days of this letter, unless you request an extension of time to file. File the returns in accordance with their instructions, and do not send them to this office. Failure to file the returns timely may result in a penalty.

We will make this letter and our proposed adverse determination letter available for public inspection under Code section 6110, after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in Notice 437. If you agree with our deletions, you do not need to take any further action.

In accordance with Code section 6104(c), we will notify the appropriate State officials of our determination by sending them a copy of this final letter and the proposed adverse letter. You should contact your State officials if you have any questions about how this determination may affect your State responsibilities and requirements.

If you have any questions about this letter, please contact the person whose name and telephone number are shown in the heading of this letter. If you have any questions about your Federal income tax status and responsibilities, please contact IRS Customer Service at 1-800-829-1040 or the IRS Customer Service number for businesses, 1-800-829-4933. The IRS Customer Service number for people with hearing impairments is 1-800-829-4059.

Sincerely,

Lois G. Lerner
Director, Exempt Organizations

Enclosure
Notice 437
Redacted Proposed Adverse Determination Letter
Redacted Final Adverse Determination Letter



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Date: March 9, 2011

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

Legend:

State =
Date =
Community =
Language1 =
Language2 =
Company =
President =

Dear

We have considered your application for recognition of exemption from Federal income tax under Internal Revenue Code section 501(a). Based on the information provided, we have concluded that you do not qualify for exemption under Code section 501(c)(3). The basis for our conclusion is set forth below.

Facts

You are a State nonprofit, non-stock corporation incorporated on Date. Your amended Articles of Incorporation provide that you are "organized exclusively for one or more of the purposes as specified in Section 501(c)(3) of the Internal Revenue Code . . ." and to allocate your assets to exempt purposes upon dissolution. Your specific purpose is to "[p]rovide advice to prospective homebuyers regarding mortgage financial provide financial education provide counseling to homeowners who have mortgage defaulted mortgage and/or foreclosure [sic]." You cater largely to the Community, and have counselors who are native speakers of Language1 and Language2.

The information you submitted indicates that your primary activities are "to provide financial education programs and . . . housing counseling (home buyer education, foreclosure, post-purchase education, homeownership, counseling [sic])." Your application states that you offer general financial and credit counseling services. You originally represented that you would provide reverse mortgage counseling and refinancing counseling, but you later stated that you

have "insufficient financial support and inadequate resources" to maintain those programs. You represent that you do not offer debt management plans.

Your budget counseling and financial literacy services consist of helping customers to understand their credit history and set financial priorities. You state that you help customers identify and correct erroneous information on their reports, and assist them in understanding and exercising their rights under the Fair Credit Reporting Act. You did not provide significant additional detail regarding your credit repair activities.

You also provide housing counseling services such as homebuyer education and pre-purchase counseling. You state that homebuyer education informs customers of the advantages and disadvantages of homeownership, helps customers develop a budget plan and obtain a loan, assists customers in choosing homes, and discusses negotiations, inspection, and closing. You state that your pre-purchase counseling service consists of providing customers with basic knowledge about mortgages and the requirements of homeownership; and post-purchase counseling to address issues that arise after a home purchase, such as making mortgage payments, escrow, taxes, insurance, maintaining the home, and predatory lending. You state that your counselors determine how much customers can afford to spend on a home, assist customers in dealing with real estate agents, help customers choose home inspectors, appraisers, attorneys, escrow officers, title insurance officers, and property insurance agents, and instruct customers on the closing process. It is not clear how or whether your "homebuyer education" service is different from your pre-purchase and post-purchase counseling services.

Your information also indicates that you provide foreclosure prevention counseling. You state that you explore alternatives to housing foreclosure for customers who are behind on their payments or are in danger of falling behind. You determine whether a customer's situation is curable or incurable, and explain their options to them, including forbearance, modification, refinance, bankruptcy, deed in lieu, pre-sale, short sale and straight sale. You prepare a loss mitigation package to send to the mortgage servicer, help the customer access any financial resources that can be used to make housing payments, and help them develop a long-term budget. You then monitor the customer's success in complying with the workout plan.

You submitted copies of the materials you plan to use in your educational programs in English, Language1 and Language2. You represent that the copies provided in English are translations of all the materials you submitted in Language1 and Language2. You included manuals with titles such as "Financial Education Program Design" and "Home Purchase Process Counseling." Although you provided materials entitled "Education Materials for Participants," these were in Language1 or Language2 and there were no equivalent English versions submitted.

The educational materials you submitted are training manuals used for training housing counselors, as opposed to educating homeowners. The materials appear to be portions of training manuals produced by NeighborWorks and distributed to individuals seeking certification as financial and housing counselors, and seeking to set up financial and housing counseling businesses. All of these documents have a NeighborWorks copyright on each page.

You provided a copy of your web site. The web site contains basic information pertaining to home ownership and financial literacy but no educational materials. You provided English

translations of this material. It directs potential customers to contact you for counseling services. You indicated that your web site is not yet available on the Internet.

You state that you intend to fund your programs through grants and service fees. Specifically, you plan to receive grant funding from NeighborWorks. You also indicated that you applied for funding from several banks. You did not specify whether the funding from these banks would be in the form of grants, loans, or both. In the future, you plan to apply for funding from the U.S. Department of Housing and Urban Development ("HUD").

You submitted a fee schedule for your services, which shows that you plan to charge a fee to certain customers for your services, including "Credit Analysis," "Housing Education," and "Foreclosure Preventions [sic]." You provided several contradictory criteria by which you decide whether a customer is entitled to a fee waiver. You stated that you "provide[] customers with counseling without charging fees, when customer presents a hardship and reasonable reason that prove client's financial difficulties." You later said that your services are "[f]ree of charge for person who can not afford (the below poverty) [sic]: W-2 or paystub that can prove the below poverty is required 'Poverty' is considered as customers' households earning below state median income." You also stated, "Conditions for approval of free of charge: DTI above 45%, hardships due to illness, unexpected financial crisis." In addition, your fee schedule states that you will provide "financial counseling" free of charge to all customers, regardless of their income or other factors.

You stated that you intend to offer homeownership education to 80 individuals per month, of which approximately 20 would qualify for a fee waiver. You also stated that you will assist 40 individuals per month through your foreclosure prevention counseling services, with 10 of them qualifying for a fee waiver.

On your Statement of Revenues and Expenses, you classified all your income as contributions. You planned to receive \$ _____ in contributions in your first year of operation, \$ _____ in your second year and \$ _____ in your third year. However, when asked how much money you expected to collect in fees from your customers, you estimated that such fees would total \$ _____ per month (\$ _____ per month for homeownership education and \$ _____ for foreclosure prevention). You also predicted that in your first five years of operation you would collect between 80 and 100 percent of your revenue from funding sources such as NeighborWorks, HUD, and financial institutions, while between 0 and 20 percent of your revenues would be derived from fees charged to customers. However, your predicted revenue of \$ _____ in monthly fees from customers by itself would add up to significantly more than your projected total revenues indicated on your Statement of Revenues and Expenses for your first three years of operation. Moreover, if these fees account for only 20 percent of your projected revenue, you expect approximately an additional \$ _____ in annual revenue from NeighborWorks, HUD, and financial institutions that is not reflected on your Statement of Revenues and Expenses. You have not explained this discrepancy.

You are governed by a Board of Directors, which is currently comprised of President and four other individuals. You have stated that none of these individuals are compensated by your organization. You listed the time devoted by each individual as "10," but it is unclear whether this refers to hours per week, hours per month, or another measurement. You did not specify

whether your board members are community leaders or government officials acting in their capacities as such.

President is also the President of Company, an organization that provides credit counseling services and debt management plans. Company operates out of the same address as your headquarters, and leases office space to your organization. The lease is signed by President as President of your organization, and by President as President of Company. All of the employees whose resumes you have submitted are former employees of Company. The acronyms by which the two organizations are referred to are identical. As the names of the two organizations are similar, there is conflicting information in your application as to which organization conducts which activity. You stated that customers seeking credit counseling services will be directed to Company, while customers seeking housing counseling services will be directed to your organization.

You provided resumes for your three employees. They each have approximately 18 months' experience in financial counseling. You represented that they all gained this experience during their time as financial counselors for Company. Your counselors have undergone training with NeighborWorks, an organization that provides instruction and certification for housing counselors. Your counselors have certification in areas such as Homeownership Counseling and Foreclosure Basics.

When asked about the difference between you and Company, you stated that Company "aims at educating debtors and advancing their social welfare, along with improving consumer's financial obligations that might be greatly influenced by the usage of credit cards, loans and other debts," and your mission is "to assist people [to] develop their proper spending plan, and increase housing affordability and management by eliminating barriers and discrimination caused by lack of language proficiency, cultural deviation and financial literacy."

You also said that Company "is a credit counseling agency providing credit counseling and Debt Management Plan. In contrast, [you are] a housing counseling agency specializing the [sic] housing counseling services including consumer financial counseling, housing counseling and foreclosure prevention counseling." You stated that you will direct a client to one organization or the other based on the client's needs. You stated that "[d]irection to visit each agency will be shown top [sic] of the office door by a sign, indicating [you] for Housing matters and Company for Credit/Debt matters when a client is in the building." We asked you to provide photographs showing any signage, but the photographs you provided do not indicate the presence of such a sign.

When asked whether you and Company were related in any manner, you stated that:

Employees from [Company] joined [you] to help [Community] develop financial/housing literacy. They are all certified by 'Center for financial certifications' as personal finance counselors having knowledge of personal finance and housing matters as well as having many experiences on budget/financial counseling through dealing with [Community]. These counselors also participated in a wide variety of professional workshops and completing well-rounded courses and exams to make qualification about financial/housing

consulting [sic].

You also stated that:

[Company]'s activities providing financial education to [Community] leads to establish [you] in that [Community] needs a reputational housing counseling organization since [Community] suffer[s] from lack of financial, literacy, solution of housing matters caused by language barriers [sic]. [Your services] are more specified and more focusing on housing counseling including pre/post purchasing housing counseling and foreclosure prevention counseling.

When asked whether you will allow other entities to promote their products or services to your customers, you responded that:

[You] will permit entities to advertise their program indirectly which means they may provide audience with useful education materials in the program or directly which mean [sic] they may provide audience with free coupon which can purchase their products in a discount price or stationary products, souvenirs on which they put their company logo if they officially support our program through donation. We do not allow individual profession to advertise them [sic]. However, if individual profession who is willing to support our program, board member will decide whether s/he can participate in program as a lecturer based on his/her expertise.

You were asked whether any of your board members, officers, directors, or employees are or have been an officer, director or employee of a credit counseling organization, a credit repair organization or an organization issuing credit cards. In response, you stated only that "[President] is the only Board member who works [for a] credit counseling or[g]anization." You provided an identical response when asked whether any of your board members, officers, directors, or employees have or had any ownership interests in for-profit businesses that perform credit counseling, credit repair, or other services that may be used by your organization; and when asked whether any of your organization's Board members, officers, directors or employees have expertise or experience in the area of consumer credit counseling or credit repair.

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

Section 501(q) of the Code presents special requirements for organizations which provide credit counseling services as a substantial purpose. It defines credit counseling services as providing educational information to the general public regarding budgeting, personal finance, financial literacy, saving and spending practices, and the sound use of consumer credit and assisting individuals and families with financial problems through counseling:

(1) An organization with respect to which the provision of credit counseling services is a substantial purpose shall not be exempt from tax under subsection (a) unless such organization is described in paragraph (3) or (4) of subsection (c) and such organization is organized and operated in accordance with the following requirements:

(A) The organization--

- (i) provides credit counseling services tailored to the specific needs and circumstances of consumers,
- (ii) makes no loans to debtors (other than loans with no fees or interest) and does not negotiate the making of loans on behalf of debtors,
- (iii) provides services for the purpose of improving a consumer's credit record, credit history, or credit rating only to the extent that such services are incidental to providing credit counseling services, and
- (iv) does not charge any separately stated fee for services for the purpose of improving any consumer's credit record, credit history, or credit rating.

(B) The organization does not refuse to provide credit counseling services to a consumer due to the inability of the consumer to pay, the ineligibility of the consumer for debt management plan enrollment, or the unwillingness of the consumer to enroll in a debt management plan.

(C) The organization establishes and implements a fee policy which--

- (i) requires that any fees charged to a consumer for services are reasonable,
- (ii) allows for the waiver of fees if the consumer is unable to pay, and
- (iii) except to the extent allowed by State law, prohibits charging any fee based in whole or in part on a percentage of the consumer's debt, the consumer's payments to be made pursuant to a debt management plan, or the projected or actual savings to the consumer resulting from enrolling in a debt management plan.

(D) At all times the organization has a board of directors or other governing body--

- (i) which is controlled by persons who represent the broad interests of the public, such as public officials acting in their capacities as such, persons having special knowledge or expertise in credit or financial education, and community leaders,
- (ii) not more than 20 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of

reasonable directors' fees or the repayment of consumer debt to creditors other than the credit counseling organization or its affiliates), and

(iii) not more than 49 percent of the voting power of which is vested in persons who are employed by the organization or who will benefit financially, directly or indirectly, from the organization's activities (other than through the receipt of reasonable directors' fees)

....

(4) Credit counseling services; debt management plan services.--For purposes of this subsection--

(A) Credit counseling services.--The term "credit counseling services" means--

(i) the providing of educational information to the general public on budgeting, personal finance, financial literacy, saving and spending practices, and the sound use of consumer credit,

(ii) the assisting of individuals and families with financial problems by providing them with counseling, or

(iii) a combination of the activities described in clauses (i) and (ii).

Section 1.501(c)(3)-1(a)(1) of the Income Tax Regulations (regulations) provides that, in order to be exempt as an organization described in section 501(c)(3), an organization must be both organized and operated exclusively for one or more of the purposes specified in such section. If an organization fails to meet either the organizational test or the operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

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 underprivileged 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.

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

The organization provided information to the public on budgeting, buying practices, and the sound use of consumer credit through the use of films, speakers, and publications. It aided low-income individuals and families who have financial problems by providing them with individual counseling, and if necessary, by establishing budget plans. Under the budget plan, the debtor voluntarily made fixed payments to the organization, which held the funds in a trust account and disbursed the funds on a partial payment basis to the creditors. The organization did not charge fees for counseling services or proration services. The 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.

Section 4.03 of Rev. Proc. 2011-9, 2011-2 I.R.B. 283, provides that exempt status may be recognized in advance of the organization's operations if its proposed operations are described in sufficient detail to permit a conclusion that it will clearly meet the particular requirements for exemption pursuant to the section of the Code under which exemption is claimed. Section 4.03(2) states that the organization must fully describe all of the activities in which it expects to engage, including the standards, criteria, procedures or other means adopted or planned for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures.

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 est of Hawaii v. Commissioner, 71 T.C. 1067 (1979), a nonprofit organization paid a for-profit corporation for the licenses to conduct "est" programs. The est programs involved training, seminars, and lectures in the areas of intrapersonal awareness and communication. The court held that an organization's denial of exemption was proper because the organization had a substantial commercial purpose that served private rather than public interests. Although the nonprofit claimed that it had no connection, direct or indirect with the for-profit, the court found that the for-profit exerted considerable control over the nonprofit's activities. The nonprofit's only function was to present to the public for a fee, ideas that were owned by the for-profit with materials and trainers supplied by the for-profit. Regardless of whether the payments made by the nonprofit to the for-profit were excessive, the for-profit benefited substantially from the

operation of the nonprofit. The nonprofit was the instrument to subsidize the for-profit corporations and not vice versa and had not life independent of the for-profits.

In Consumer Credit Counseling Service of Alabama, Inc. v. United States, 78-2 U.S. Tax Cas. 9660 (D.D.C. 1978), the court held that 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 had 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. The professional counselors used only 12 percent of their time for debt management programs. They did not limit these services to low-income individuals and families, but they provided their services free of charge. 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, these agencies did not charge a fee for the programs that constituted their principal activities. A nominal fee was charged for the debt management services but was waived when payment 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 fees. Thus, the court concluded 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. Tax Cas. 9468 (D.D.C. 1979), in which the facts were virtually identical and the law was identical to those in Consumer Credit Counseling Centers of Alabama, Inc. v. United States, discussed immediately above.

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.

In addition, 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 did not limit its clientele to organizations that were section 501(c)(3) exempt organizations.

In P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), an organization operated bingo at a bar (a for-profit enterprise) for purposes of raising money for scholarships. The board of directors included the bar's owners and accountant, and two other persons. The court

reasoned that, because the bar owners controlled the organization and appointed its directors, the organization's fundraising activities could be used to the advantage of the bar owners, and thus, provide them with a maximum private benefit.

The organization claimed that it was independent because there was a separate accounting and that no payments were going to the bar. The court maintained that the organization's and the bar's activities were so interrelated as to be "functionally inseparable." A separate accounting did not change that fact. Thus, the organization did not operate exclusively for exempt purposes, but rather benefited private interests - the bar owners. Exemption was properly denied.

In Easter House v. United States, 12 Cl. Ct. 476 (1987), aff'd, 846 F. 2d 78 (Fed. Cir. 1988) cert. denied, 488 U.S. 907, 109 S. Ct. 257, 102 L. Ed. 2d 246 (1988), the court found an organization that operated an adoption agency was not described in section 501(c)(3) of the Code because a substantial purpose of the agency was a nonexempt commercial purpose. The court concluded that its primary activity was placing children for adoption in a manner indistinguishable from that of a commercial adoption agency. The court found that the health-related services provided to unwed mothers and their children were merely incidental to the organization's operation of an adoption service, which, in and of itself, did not serve an exempt purpose. The organization's sole source of support was the fees it charged adoptive parents, rather than contributions from the public. The court also found that the organization competed with for-profit adoption agencies, engaged in substantial advertising, and accumulated substantial profits. Accordingly, the court found that the "business purpose, and not the advancement of educational and charitable activities purpose, of plaintiff's adoption service is its primary goal" and held that the organization was not operated exclusively for purposes described in section 501(c)(3).

In Living Faith, Inc. v. Commissioner, 950 F.2d 365 (7th Cir. 1991), the Court of Appeals for the Seventh Circuit upheld a Tax Court decision that an organization operating restaurants and health food stores in a manner consistent with the doctrines of the Seventh Day Adventist Church was not described in section 501(c)(3) of the Code because the organization was operated for a substantial nonexempt commercial purpose. The court found that the organization's activities were "presumptively commercial" because the organization was in competition with other restaurants, engaged in marketing, and generally operated in a manner similar to commercial businesses.

In KJ's Fund Raisers, Inc. v. Commissioner, 74 T.C.M. 669 (1997), the court held that a nonprofit organization, which sold lottery tickets on the premises of a for-profit business had a substantial non-exempt purpose to enhance the profits of the for-profit business. The owners of the for-profit business to purportedly raise funds for distribution to charitable causes formed the nonprofit organization. The nonprofit's lottery tickets were sold during the regular business hours by the owners and employees of the for-profit business. The owners of the for-profit initially controlled the board and later indicated that it would vest control in unrelated parties. The nonprofit opined that the organization "would fold without the original founders of the organization as officers." In finding that the nonprofit had a substantial nonexempt purpose, which was promoting the for-profit, the court reasoned that the identity of the for-profit owners and the officer of the nonprofit, placed the owners of the for-profit in a position to control the nonprofit. Additionally, the court found that the publicity received by the for-profit was a

significant benefit.

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 this organization conducted its activities, the court found that it 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."

New Dynamics Foundation v. United States, 70 Fed. Cl. 782 (2006), was an action for declaratory judgment that the petitioner brought to challenge the denial of his application for exempt status. The Court in finding that the actual purposes displayed in the administrative record supported the Service's denial stated, "It is well-accepted that, in initial qualification cases such as this, gaps in the administrative record are resolved against the applicant." The Court noted that if the petitioner had evidence that contradicted these findings, it should have submitted it as part of the administrative process.

In Solution Plus, Inc. v. Commissioner, T.C. Memo. 2008-21, the Tax Court held that a credit counseling organization was not exempt under section 501(c)(3) because it was not organized and operated exclusively for educational or charitable purposes and impermissibly served private interests. The organization was formed by an individual with experience selling debt management plans. The founder and his spouse were the only member's of the organization's board of directors. The organization did not have any meaningful educational program or materials for providing to people who contacted the organization, and its financial education seminars for students constituted an insignificant part of the organization's overall activities.

The Court held that the organization's purposes were not educational because its "activities are primarily structured to market, determine eligibility for, and enroll individuals in DMPs." Its purposes are not to inform consumers "about understanding the cause of, and devising personal solutions to, consumers' financial problems," or "to consider the particular knowledge of individual callers about managing their personal finances." The Tax Court also held that the organization's purposes were not charitable because "its potential customers are not members of a [charitable] class that are benefited in a 'non-select manner * * * because they will be turned away unless they meet the criteria of the participating creditors."

The Tax Court further held the organization would operate for the private interests of its founder because the founder and spouse were the only directors, the founder was the only officer and employee, and his compensation was based in part on the organization's DMP sales activity levels. The organization was "a family-controlled business that he personally would run for financial gain, using his past professional experience marketing DMPs and managing a DMP call center." The Court further held that the organization's principal activity of providing DMP services, which were only provided if approved by a caller's creditors, furthered the benefit of private interests.

Finally, the Tax Court held that the facts in Credit Counseling Services of Alabama v. United States, 78-2 USTC para. 9660 (D.D.C. 1978) "stand in stark contrast" because "the sale of DMPs is the primary reason for [Solution Plus's] existence, and its charitable and educational purposes are, at best, minimal."

Analysis

To satisfy the 501(c)(3) operational test, an organization must establish that it is both organized and operated exclusively for one or more exempt purposes. Section 1.501(c)(3)-1(a)(1) of the regulations. 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) of the Code. Section 1.501(c)(3)-1(c)(1) of the regulations. A single nonexempt purpose will destroy exemption regardless of the presence of any truly exempt purposes. Better Business Bureau, 326 U.S. 279. Under the operational test, the purpose towards which an organization's activities are directed, and not the nature of the activities themselves, is ultimately dispositive of the organization's right to be classified as a section 501(c)(3) organization. B.S.W. Group, 70 T.C. 352, 356-57 (1978). Your activities are not directed exclusively toward one or more exempt purposes. While you engage in one-on-one discussions with homeowners and public presentations that may, in part, further educational or charitable purposes, your activities primarily further the substantial nonexempt purpose of selling financial services to homeowners and lenders for a fee. Thus, you have failed to establish that you are operated exclusively for one or more exempt purposes.

You are Not Operated Exclusively for Educational Purposes

Your activities demonstrate that you do not operate exclusively for educational purposes within the meaning of section 501(c)(3) of the Code. The vast majority of the materials you submitted in response to our request for copies of your educational materials are not intended to facilitate homeowner and financial education. Rather, they are training materials produced by NeighborWorks for the purpose of instructing counselors on how to establish and manage such programs. While you provided some materials purported to be educational literature for your customers, the material was in Language1 and Language2, without an English equivalent to allow us to fully review the materials. Your website content alone is not sufficient to demonstrate that you are engaged in educational activities.

You have not established that you have an educational program that will provide substantive counseling in housing and financial matters. The materials you submitted in English that aim to educate homeowners are minimal. Therefore, you have failed to establish that the services you plan to offer constitute educational activity under section 1.501(c)(3)-1(d)(3) of the regulations. You did not submit a curriculum, textbook, lesson plan or other materials that would suggest that you plan to provide education. Your application and subsequent submissions fail to adequately describe your intended educational activities as required by Rev. Proc. 2010-9. Although you were specifically asked for such details and were given the opportunity to present them in your application, you failed to submit a full explanation of how you would assist distressed homeowners. In addition, some of the answers that you gave conflicted with each other.

You were asked directly to describe the expertise of your board members and employees with credit counseling and credit repair, and whether any board members or employees have or had any ownership interests in for-profit businesses that perform credit counseling, credit repair, or other services that may be used by your organization. You were also asked to disclose whether any of your board members or employees are or have been officers, directors or employees of a credit counseling or credit repair organization. In response to these questions, you stated only that “President is the only Board Member who Works Credit Counseling Organization.” [sic] This statement is not an adequate response to the questions we asked you, as it does not fully describe or explain President’s affiliation with other organizations or expertise in credit counseling. It makes no mention of the experience or expertise of your organization’s other board members or employees. Therefore, we are entitled to draw inferences from the missing information. See New Dynamics Foundation, 70 Fed. Cl. 782. In addition, your response contradicts other parts of your application that claim that your employees are certified in credit counseling, have experience in that area, and were formerly employed by Company, your president’s credit counseling company. It is thus unclear whether your employees are equipped to provide any meaningful educational services.

You are Not Operated for Exclusively for Charitable Purposes

Providing services exclusively for the benefit of the poor, a recognized charitable class, furthers charitable purposes. Treas. Reg. sec. 1.501(c)(3)-1(d)(2). For instance, counseling the poor about economics and personal finance can achieve an exempt purpose. See Rev. Rul. 69-441, supra.

You have failed to establish that your operations will be charitable through relief of the poor and distressed. You do not restrict your activities to the benefit of the poor. Although you represented that you provide your services to the needy at no cost, you do not appear to have a consistent definition of who qualifies for a waiver of your fees. Moreover, the housing and financial consulting you offer are sold to anyone who is willing to purchase your services.

You Have a Substantial Nonexempt Purpose

Section 1.501(c)(3)-1(c)(1) of the regulations provides that an organization does not qualify for exemption if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. A nonexempt purpose may be evidenced by activities that are conducted in a commercial manner or for a commercial purpose. Indeed, in discerning whether an organization has a substantial nonexempt commercial purpose, courts focus on a number of factors related to the nature of the activities and how an organization conducts its business, including pricing policies, funding sources, and the organization’s competitiveness with and similarity to other commercial ventures. See, e.g., B.S.W. Group, 70 T.C. 352 (1978); Easter House, 12 Cl. Ct. 476 (1987); Airlie Foundation, 283 F. Supp. 2d 58 (D.D.C. 2003); Living Faith, 950 F.2d 365 (7th Cir. 1991).

Factors to be considered in assessing whether an organization is operating in a commercial manner include competition with for-profit commercial entities, extent and degree of below cost services provided, pricing policies, and the extent to which the organization receives charitable donations. Airlie Foundation, 283 F. Supp. 2d at 63. You have not indicated the

extent to which your services are offered below cost, and your pricing policies are inconsistent. Your revenue sources further demonstrate that you operate for a substantial nonexempt commercial purpose. The exempt organization described in Consumer Credit Counseling Service of Alabama, 78-2 U.S.T.C. 9660 (D.D.C. 1978) received support from grants and contributions. While you indicated that you will solicit government grants, you have not received any government grants and there is no evidence that you have received contributions or gifts from disinterested members of the public. See B.S.W. Group, 70 T.C. 352 (citing lack of solicitation of contributions and sole support from fees as factors disfavoring exemption).

You also plan to receive advertising revenue. The manner in which you will promote your advertisers conflicts with your stated goal of assisting financially distressed homeowners, and suggests that you are operated commercially. For example, you indicated that you would permit entities that donate to your organization to provide your customers with coupons that can be used toward discounts on such sponsors' services. This provides a return benefit to the contributors, making their contributions fees for service rather than disinterested donations. You also stated that such sponsors "may provide audience with useful education materials in the program." Although you were asked to provide all your educational materials to us, you provided no materials from such sponsors, nor did you describe your sponsorship arrangements in any detail. However, based on the information you provided, it appears that your customers serve as an audience for the advertisements of your sponsors.

Additional evidence of your commerciality is found in your relationship with Company. An organization is not operated exclusively for exempt purposes unless it serves a public rather than a private interest. See section 1.501(c)(3)-1(d)(1)(ii) of the regulations. A substantial part of your activities consists of the private purpose of generating customers and revenue for Company. Company is a for-profit financial services business owned by President. Your officers and directors are employees and/or owners of Company. Company is headquartered at your address, leases space to you pursuant to a lease signed by President as both your President and as President of Company. This suggests that you intend for a portion of Company's expenses to be paid by grant funding, donations and other opportunities that would only be available to you as a tax-exempt organization. Given the commonality of ownership and the functional similarity of the two organizations, the potential exists for the organizations to share resources in the areas of advertising, facility-related expenses, supplies, managerial/legal services, and other areas. Moreover, you have not represented to us that the accounting records for the two organizations will be kept separately.

Although you claim that Company is an independent entity, your activities and those of Company are functionally inseparable. Your name sounds and looks similar to Company's. Additionally, despite repeated opportunities to do so, you have not demonstrated that your customers will perceive any distinction between you and Company. See P.L.L. Scholarship Fund, 82 T.C. 196 (citing insufficient separation between organization seeking exemption and for-profit entity as a factor weighing against recognition of exemption); Easter House, 846 F. 2d 78 (Fed. Cir. 1988), aff'g 12 Cl. Ct. 476 (1987) (lack of difference between organization seeking exemption and for-profit entities weighed against recognition of exemption). You have clearly stated that you will refer your clients to Company for credit counseling services. You have made no indication that you will change this practice. Thus, Company is likely to gain additional clients and additional revenue from your clients. See est of Hawaii, 71 T.C. 1067 (nonprofit's

activities served the commercial purposes of the for-profit organization that formed it, even where individuals unrelated to the for-profit organizations formally controlled the nonprofit); KJ's Fund Raisers, Inc., 74 T.C.M. 669 (same).

Your financial data also suggests that you are not devoting substantially all your resources to exempt activities. Some of these unaccounted-for funds may be serving private, rather than public, interests. The Statement of Revenues and Expenses you provided conflicted with other financial information you submitted to us. You projected that you would receive between \$ and \$ per year in your first three years of operation in total revenue. In another part of your application you stated that you would receive approximately \$ per month in fees from your customers in exchange for the services you provide. This would add up to approximately \$ per year, more revenue than you expected to receive in any one year, according to your Statement of Revenue and Expenses. Elsewhere in your application, you stated that you expected fees received from customers to account for between 0 and 20 percent of your total revenue in your first five years of operation. If such fees (roughly \$ per year) accounted for 20 percent of your total revenue, based on this estimate, you would expect to receive approximately \$ per year in grants. This money is not accounted for in your Statement of Revenues and Expenses. You provided no explanation for this discrepancy, and it is unclear whether this unaccounted-for revenue will be used exclusively for exempt purposes. Since you have thus not established that your income will be used exclusively for exempt purposes, we are entitled to draw the inference that you are not operated exclusively for such purposes. New Dynamics Foundation, 70 Fed. Cl. 782; see also section 1.501(c)(3)-1(c)(1) of the regulations.

Based on the foregoing, like the organization in Solution Plus, T.C. Memo. 2008-21, we conclude that your primary purpose is to benefit private interests through the promotion and delivery of financial and other services to individuals for a fee. The activities you identify as educational and charitable are merely incidental to your business of providing consulting services for a fee and referrals to Company. Thus, more than an insubstantial part of your activities are in furtherance of a nonexempt purpose, in contravention of section 1.501(c)(3)-1(c)(1) of the regulations. Therefore, you are not operated for an exempt purpose.

Section 501(q) of the Code

An organization that provides educational information on financial topics or financial counseling to homeowners who are at risk of foreclosure is providing "credit counseling services" within the meaning of section 501(q)(4)(A) of the Code. An organization that engages in such activities as a substantial purpose must, in addition to complying with the requirements of section 501(c)(3), comply with the provisions of section 501(q). You do not meet the requirements of section 501(c)(3) and you do not meet the requirements of section 501(q).

An exempt credit counseling organization must establish and implement a fee policy which requires that any fees charged to a consumer for services are reasonable and allows for the waiver of fees if the consumer is unable to pay. Section 501(q)(1)(C). You failed to establish that you have a consistent fee policy that complies with these requirements.

Credit counseling organizations must be governed by a board controlled by persons

representing the broad interests of the public rather than by persons who benefit from the organization's activities. Section 501(q)(1)(D) of the Code There is no indication that any of your directors represent the broad interests of the public. Although you have indicated that one of your board members (President), has experience in credit counseling, there is no indication that your other board members do. This is in violation of section 501(q)(1)(D)(i).

Moreover, based on your fee schedule, you charge a separate fee for credit analysis services aimed at improving a consumer's credit, in violation of section 501(q)(1)(A)(iv). Encouraging distressed homeowners to purchase products and services sold by your advertisers could prevent them from emerging from debt, and thus would be contrary to their particular needs, thus violating section 501(q)(1)(A)(i) of the Code, which requires that credit counseling organizations "provide[] credit counseling services tailored to the specific needs and circumstances of consumers." Therefore, even if your educational program did constitute credit counseling services, you would not be eligible for exempt status because you would not be organized and operated in accordance with the requirements of section 501(q).

Therefore, had you established that you otherwise met the requirements of section 501(c)(3) of the Code, your failure to satisfy the requirements of section 501(q) would prevent you from being exempt from taxation under section 501(a).

Conclusion

Based on the facts and information provided, you are not operated exclusively for exempt purposes as required by sections 1.501(c)(3)-1(a)(1) and 1.501(c)(3)-1(c)(1) of the regulations. You are operated for a substantial nonexempt purpose in contravention of section 1.501(c)(3)-1(c)(1) of the regulations. Any public purposes for which you may operate are only incidental to this primary nonexempt purpose. You do not serve a public rather than a private interest as required by section 1.501(c)(3)-1(d)(1)(ii) of the regulations. Therefore, you are not described in section 501(c)(3). In addition, you do not meet the requirements of section 501(q).

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns. Contributions to you are not deductible under section 170.

You have the right to file a protest if you believe this determination is incorrect. To protest, you must submit a statement of your views and fully explain your reasoning. You must submit the statement, signed by one of your officers, within 30 days from the date of this letter. We will consider your statement and decide if the information affects our determination.

Your protest statement should be accompanied by the following declaration:

Under penalties of perjury, I declare that I have examined this protest statement, including accompanying documents, and, to the best of my knowledge and belief, the statement contains all the relevant facts, and such facts are true, correct, and complete.

You also have a right to request a conference to discuss your protest. This request should be made when you file your protest statement. An attorney, certified public accountant, or an

individual enrolled to practice before the Internal Revenue Service may represent you. If you want representation during the conference procedures, you must file a proper power of attorney, Form 2848, *Power of Attorney and Declaration of Representative*, if you have not already done so. For more information about representation, see Publication 947, *Practice before the IRS and Power of Attorney*. All forms and publications mentioned in this letter can be found at www.irs.gov, Forms and Publications.

If you do not file a protest within 30 days, you will not be able to file a suit for declaratory judgment in court because the Internal Revenue Service (IRS) will consider the failure to protest as a failure to exhaust available administrative remedies. Code section 7428(b)(2) provides, in part, that a declaratory judgment or decree shall not be issued in any proceeding unless the Tax Court, the United States Court of Federal Claims, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted all of the administrative remedies available to it within the IRS.

If you do not intend to protest this determination, you do not need to take any further action. If we do not hear from you within 30 days, we will issue a final adverse determination letter. That letter will provide information about filing tax returns and other matters.

Please send your protest statement, Form 2848 and any supporting documents to this address:

Internal Revenue Service
SE:T:EO:RA:T:1

1111 Constitution Ave, N.W.
Washington, DC 20224

You may also fax your statement using the fax number shown in the heading of this letter. If you fax your statement, please call the person identified in the heading of this letter to confirm that he or she received your fax.

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

Sincerely,

Lois G. Lerner
Director, Exempt Organizations