



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

Number: **200510044**

Release Date: 3/11/2005

Date: December 16, 2004

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

UIL: 501.03-00

Legend:

You =

Dear _____ :

The market for consumer credit counseling services has undergone changes in the past 30 years. In 2002, the IRS began a comprehensive study of organizations offering credit counseling and debt-management services. On July 30, 2004, the IRS Office of Chief Counsel released IRS Chief Counsel Advice (CCA 200431023 2004 IRS CCA Lexis 22 (July 13, 2004)), presenting a comprehensive legal analysis as to whether credit counseling organizations can qualify as charitable or educational organizations described in section 501(c)(3) of the Internal Revenue Code. We have enclosed a copy of the CCA for your information.

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

You were incorporated under the General Not For Profit Corporation Law. Your Articles of Incorporation and Bylaws provide that you were formed to "provide credit counseling services to individuals and families, as well as other related credit or debt counseling services." Your Board of Directors and officers include a husband and wife, the father of the aforementioned husband, and another individual.

You maintain that fifty percent of your time and resources will be devoted to "credit counseling for debt payment." This includes "educating and assisting clients in their communication and negotiations with creditors in order to obtain discounts, adjusted payment or penalty terms, and other debt adjustments." You will be responsible for administering and processing debt management plans (DMPs) and negotiating with credit card

companies/creditors, and will use credit counseling management software to accomplish these tasks. "A DMP will offer the ability to lower existing monthly debt payments by combining or consolidating all debt payments into one monthly payment." You represent that the other 50 percent of your time and resources will be devoted to "financial-credit management education," which consists of "counseling and advising clients on the use and management of credit, budget, and following through with debt payments...[This] information will be provided to clients via Internet website, mailings, and personal conferences." You maintain that your website is under construction.

You state that you are just beginning operations and do not have any clients. However, you have submitted several documents governing your debt management program, including a document on repayment terms, a client agreement, a client information sheet, an acknowledgement letter to the consumer, a sample monthly payment sheet, and a sample creditors list. Clients who take advantage of the DMP will be asked to pay a monthly contribution of \$10 per creditor/per month up to a maximum of \$40 per month. There are no initial start up fees to enter the program. When asked what happens when a client misses a payment on the DMP, you stated that the client's payments would not be made to their creditors that month and that creditors may choose to raise their interest rates back up to the original level for a probationary period until the client can demonstrate the ability to pay the negotiated terms on time.

Your sources of support will include fees that you call voluntary donations from clients (45 percent of expected donations), donations from creditors-lenders (aka fair share payments) (45 percent of support), and general donations from other parties (10 percent of expected donations). Your fundraising program includes an initial goal of collecting \$10,000 from creditors and general donors. You also expect to raise funds through "regular fundraising in the form of voluntary monthly donations from clients and their creditors receiving counseling services." So far, you have not raised any revenue.

Based on the information provided, we cannot conclude that you are operated for a charitable purpose under section 501(c)(3) of the Code. Although you are only in the start-up phase of your debt management operations, have not raised any revenue, and do not have any clients yet, you have outlined detailed plans for conducting a full-capacity debt management program that furthers a substantial non-exempt commercial purpose. You state that at least 50 percent of your time and resources will be devoted to administering and processing DMPs, and negotiating with credit card companies. You also submitted a number of documents that outline and govern your debt management program.

Your financial structure does not resemble that of a typical charity because it is based entirely upon revenue earned by selling services to the public. Ninety percent of your support is expected to come from monthly fees from clients and creditors. Aside from receiving money from creditors-lenders and from your DMP clients, you have not established a fundraising program to raise revenue. You only expect to receive 10 percent of your funding from general donations from other parties. Thus, an insignificant amount of your funding is expected to come from contributions or gifts from disinterested members of the general public.

In addition to operating for substantial non-exempt purposes, once the debt management program is operating, you will provide substantial private benefit to the credit card companies by operating as their collection agency. The "fair share" paid by the credit card companies would undoubtedly result in significant savings over the possible costs of not recovering any of the unpaid debt owed them. These companies clearly realize substantial financial benefits through their business relationship with you.

Furthermore, your directors and officers consist of the husband and wife, and the father of the aforementioned husband, rather than being representative of a broad cross-section of the community. They control your operations, and therefore, we cannot conclude that your assets will not inure to their benefit. Thus, the husband, wife, and father have a substantial interest in ensuring your success, and as a result, their financial success. Your board, as presently constituted, has inherent conflicts of interest.

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 of the Code.

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practices Requirements.

If you do not protest this ruling in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Code provides, in part, that a declaratory judgment or decree under this section 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 administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
1111 Constitution Ave, N.W.
Washington, D.C. 20224

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
Rulings & Agreements

Attachments
IRS Chief Counsel Advice
Notice 437