



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Number: **200637039**
Release Date: 9/15/2006
Date: June 19, 2006

UIL: 501.00-00

Contact Person:

Identification Number:

Contact Number:

Employer Identification Number:

Form Required To Be Filed:

1120

Tax Years:

All

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.

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.

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
Rulings & Agreements

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



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

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

Date: May 4, 2006

UIL: 501.00-00

Contact Person:

Identification Number:

Contact Number:

FAX Number:

Employer Identification Number:

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.

You submitted as your Articles of Organization a document entitled "Declaration of Trust" and purporting to create a Charitable Trust. This document was not signed by any trustees or certified by a notary public. You also submitted a document entitled "Charter" purporting to create a non-profit corporation under the laws of the State in which you are located. This document was also not signed and has never been filed with the State authorities. The individuals identified in both documents as your initial trustees were also identified as the owners and governing body of a related for-profit business (FP.) Information filed with the Secretary of State indicates that FP continues in operation as an active business.

You represented in your Form 1023 that you are a successor to FP and that FP's owners served as your initial board of directors. You provided conflicting information regarding the percentage of ownership interests among your initial board members and those appointed later. Further, you did not provide a copy of any sales agreements, appraisals, or other information explaining the terms of your assumption of FP's business or any evidence that FP is no longer operating. In addition, you and FP share the same location and have the same phone number. Although you indicated that you pay \$500 per month rent for that location, you did not submit a copy of a rental agreement. It appears that you continue to be controlled by and operated as an integral part of FP's ongoing business.

In your Form 1023, you represented that your "organizational goal" would emphasize "minority community, educational, real estate investment, youth activities, civic leadership, and mall business development." You also represented that you will be operating a "school," operating a "childcare center," and that you are an "instrumentality" of a state or political subdivision. You did not submit documentation describing any of these activities.

You submitted information indicating that FP's primary business is the sale of financial and mortgage services to the general public. FP sells Debt Management Plans (DMPs) and credit repair services. You state that, like FP, your primary activity will be the sale of financial services, including mortgage products, credit repair, and DMPs to the general public.

You did not provide detailed information as to how your DMP or credit repair programs would be conducted, as requested in our letters dated December 16, 2004 and February 21, 2006. As regards your DMP services, however, you stated that the amount of fee to be charged to a client would be based on the amount of debt owed to a creditor. You further indicated that these services are not limited to "a particular class of people such as minority, low-income, elderly, etc." Moreover, you indicated that you do not expect to receive any payments ("fair share") from the creditors. You also provided representations that you would offer credit repair services to the general public. You provided a copy of a letter, which you apparently sent to a creditor, requesting that "incorrect information" be removed from a credit report. As to fee structure, you stated the following: "The fees structure would (sic) determined for their services." You provided no other information as to how much would be charged for credit repair services. Although you haven't described these programs in full, the Federal Trade Commission (FTC), (see attached FTC Facts sheet) describes these programs as very risky.

You submitted a copy of your website. It is clear on its face that you share this website with FP. (Your name and FP's are shown as one on the main page of the website.) The website describes FP's purposes as follows: "The purpose of FP is to provide our clients a (sic) financial & brokerage services for building strong and effective assets." The website also indicates that the following services are provided: "Buying, Trust Deeds, Mortgage Notes, Annuities, Balloon Payments, Structured Settlements, Wrap Around, Etc." Marketing promotions on the website include: "Frustrated with mounting debt that you can't seem to get out of? Tired of being turned down for the money you need? Haunted by bad credit reports you can't seem to shake? America's [FP] wants to help!" There is mention of a "Membership Benefits" plan on the website though it is not clear what this program entails.

You provided several copies of documents to be used in the mortgage part of your business operations. In a letter to a "Mortgage Note Holder," you stated the following: "WE PAY TOP DOLLAR FOR YOUR MORTGAGE, TRUST DEED, OR CONTRACT!!" You indicated that you could give clients "a quote within 24 hours." Other documents included a "Mortgage Purchase Worksheet", and a copy of a "Fee Agreement" contract.

You also provided a copy of an "Independent Contractor Agreement", which you plan to use in the mortgage part of your business operations. You have not fully or clearly explained how "independent contractors" would be used in the context of your operations. However, in the agreement it is clearly stated that any contractual arrangement would be between the "independent contractor" and you and FP. In the "Commission Agreement" portion of the document, the following is stated: "Whereas, FP is an entity primarily engaged in the business of securing real estate financing for third parties in its capacity as a mortgage broker." With regard to the "independent contractor," it was stated that he/she is in the business of soliciting applications from the general public for the specific purpose of securing real estate financing for its clients, whether it be for the acquisition of the refinancing of real estate." In a questionnaire

to be completed by potential “independent contractors,” you asked the following question: “Have you ever been involved with credit repair services?”

You represented that each member of your staff would receive \$25,000 in annual compensation. You indicated that your officers/directors would receive compensation ranging from \$25,000 to \$50,000. You did not provide a description of their specific duties and responsibilities. However, in one of your letters to a potential client, you identified one of FP’s owners as your “Marketing Manager.” You indicated that under your State’s law employees are not required to be licensed, bonded or insured.

Although we requested information regarding substantive educational materials that you use in training your employees to “counsel” your clients, you failed to provide any details. In addition, you failed to provide any information regarding seminars or workshops you will offer the general public. Nor have you submitted any substantive educational materials used in any of your programs.

You provided budgets, which included a copy of your Form 990 for _____ and a proposed budget for _____. In your Form 990, you listed _____ in total expenses. Of this amount, _____ was for salaries, other compensation and employee benefits. There were no entries for expenses attributable to charitable and/or educational programs or materials.

Your proposed budget for _____, shows _____ in expected expenses. Of this amount, you expect to pay _____ in employee salaries, compensation, and employee benefits. Again, there are no entries for expenses attributable to charitable and/or educational programs or materials.

Section 501(c)(3) of the Internal Revenue Code exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other exempt purposes provided that no part of the net earnings inure to the benefit of any private shareholder or individual.

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

Section 1.501(c)(3)-1(b)(1)(i) of the regulations provides that an organization is organized exclusively for one or more exempt purposes only if its articles of organization:

- (a) Limit the purposes of such organization to one or more exempt purposes; and
- (b) Do not expressly empower the organization to engage, otherwise than as an insubstantial part of its activities, in activities that in themselves are not in furtherance of one or more exempt purposes.

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

Section 1.501(c)(3)-1(c)(2) of the regulations provides that an organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. Section 1.501(a)-1(c) defines the words “private shareholder or individual” in section 501 to refer to persons having a personal and private interest in the activities of the organization.

Section 1.501(c)(3)-1(d)(1)(ii) of the regulations assigns the burden of proof to an applicant organization to show that it serves a public rather than a private interest and specifically 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 the relief of the poor and distressed or of the under privileged as well as the advancement of education.

Section 1.501(c)(3)-1(d)(3) of the regulations provides that the term “educational” refers to:

- (a) The instruction or training of the individual for the purpose of improving or developing his capabilities; or
- (b) The instruction of the public on subjects useful to the individual and beneficial to the community.

Section 1.501(c)(3)-1(e)(1) of the regulations provides that an organization may meet the requirements of section 501(c)(3) although it operates a trade or business as a substantial part of its activities, if the operation of such trade or business is in furtherance of the organization’s exempt purpose or purposes and if the organization is not organized or operated for the primary purposes of carrying on an unrelated trade or business.

In Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purpose, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. The Court found that the trade association had an “underlying commercial motive” that distinguished its educational program from that carried out by a university.

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered an organization that provided analyses of securities and industries and of the economic climate in general. It sold subscriptions to various periodicals and services providing advice for purchases of individual securities. The court noted that education is a broad concept, and assumed *arguendo* that the organization had an educational purpose. However, the totality of the organization’s activities, which included the sale of many publications as well as the sale of advice for a fee to individuals, were indicative of a business. Therefore, the court 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.

In Consumer Credit Counseling Service of Alabama, Inc. v. United States, 78-2 U.S.T.C. 9660 (D.D.C. 1978), the court held 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 of Alabama is an umbrella organization made up of numerous credit counseling service agencies. These agencies provided information to the general public through the use of speakers, films, and publications on the subjects of budgeting, buying practices, and the sound use of consumer credit. They also provided counseling on budgeting and the appropriate use of consumer credit to debt-distressed individuals and families. They did not limit these services to low-income individuals and families, but they did provide such services free of charge. As an adjunct to the counseling function, they offered a debt management plan. Approximately 12 percent of a professional counselor's time was applied to the debt management plan as opposed to education. The agencies charged a nominal fee of up to \$10 per month for the debt management plan. This fee was waived in instances when payment of the fee would work a financial hardship.

The agencies received the bulk of their support from government and private foundation grants, contributions, and assistance from labor agencies and the United Way. An incidental amount of their revenue was from service fees.

The court found the organizations exempt under section 501(c)(3) because providing information to the public regarding the sound use of consumer credit is charitable in that it advances and promotes education and social welfare. These programs were also educational because they instructed the public on subjects useful to the individual and beneficial to the community. The counseling assistance programs were likewise charitable and educational in nature. Because the community education and counseling assistance programs were the agencies' primary activities, the agencies were organized and operated for charitable and educational purposes. The court also concluded that the limited debt management services were an integral part of the agencies' counseling function, and thus charitable, but stated further that even if this were not the case, these activities were incidental to the agencies' principal functions.

Finally, the court found that the law did not require that an organization must perform its exempt functions solely for the benefit of low-income individuals to qualify under section 501(c)(3) or to provide its services solely without charge. Nonetheless, these agencies did not charge a fee for the programs that constituted their principal activities. They charged nominal fees for services that were incidental. Moreover, even this nominal fee was waived when payment would work a financial hardship.

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 Rev. Rul. 61-170, 1961-1 C.B. 112, an association composed of professional private duty nurses and practical nurses that supported and operated a nurses' registry primarily to afford greater opportunities for its members was not entitled to exemption under section 501(c)(3) of the Code. Although the public received some benefit from the organization's activities, the primary benefit of these activities was to the organization's members.

In Rev. Rul. 80-287, 1980-2 C.B. 185, a lawyer referral service that aids persons who do not have an attorney by helping them to select one was not entitled to exemption under section 501(c)(3) of the Code. Although the service provides some public benefit, its principal purpose is to introduce individuals to the use of the legal profession in the hope that they will enter into lawyer-client relationships on a paying basis as a result of their experience.

Rev. Proc. 90-27, 1990-1 C.B. 514, provides in part that exempt status will be recognized in advance of operations if proposed operations can be described in sufficient detail to permit a conclusion that the organization will clearly meet the particular requirements of the section under which exemption is claimed. A mere statement of purposes or a statement that proposed activities will be in furtherance of such purposes will not satisfy this requirement. The organization must fully describe the activities in which it expects to engage, including the standards, criteria, procedures, or other means adopted or planned, and the nature of the contemplated expenditures. Where the organization cannot demonstrate to the satisfaction of the Service that its proposed activities will be exempt, a record of actual operations may be required before a ruling or determination letter will be issued.

An organization must establish through the administrative record that it operates as a section 501(c)(3) organization. Denial of exemption may be based solely upon failure to provide information describing in adequate detail how the operational test will be met. American Science Foundation v. Commissioner, T.C. Memo. 1986-556; La Verdad v. Commissioner, 82 T.C. 215, 219 (1984); Pius XII Academy v. Commissioner, T.C. Memo. 1982-97. Exempt status can be recognized in advance of operations if proposed operations can be described in enough detail to permit a conclusion that the organization will clearly meet the requirements of section 501(c)(3). American Science Foundation v. Commissioner, T.C. Memo. 1986-556. The organization has the burden of providing sufficient substantive information regarding its activities and operations to establish entitlement to tax-exempt status. Information that is vague or nonspecific is not sufficient to meet the requirements under section 501(c)(3). Tully v. Commissioner, T.C. Memo, 1999-216.

Based on the information and documentation you provided, we find that you do not meet the organizational requirements necessary to show that you are organized exclusively for charitable and educational purposes. You failed to submit a conformed copy of your organizing document. Neither the "Charitable Trust" document nor the "Charter" document were properly executed and/or filed with the proper State Officials. These documents are insufficient to create a legal entity. Accordingly, we can only conclude that you are indistinguishable from FP and rather than replace it as a successor organization you are one and the same entity. The information on the State website indicates that FP continues in operation as an active business.

Further, in the event one or the other of the organizing documents you submitted were sufficient to create a legal entity, your stated “organizational goal” involving real estate investment and small business development does not state a purpose that is within section 501(c)(3) of the Code. These are commercial business purposes and both too broad and too vague to be considered “charitable.” See, section 1.501(c)(3)-1(b)(1)(i) of the regulations.

Moreover, you do not satisfy the operational requirements to be recognized as exempt under section 501(c)(3) of the Code. You are primarily operated for the substantial non-exempt purpose of selling financial services, including DMPs and credit repair to the general public. You failed to submit sufficient evidence that your primary purpose is to provide financial education to individuals or to the general public, in that you do not have a tailored educational program with a structured educational methodology in place.

Because the sale of financial services, including DMPs and credit repair will be your primary activity, you must show that the sale of these services is incidental and integral to a substantial and substantive educational program. Section 1.501(c)(3)-1(d)(3). Financial counseling can be considered educational. See Rev. Rul. 69-441 and CCCS of Alabama, supra. However, a single substantial non-exempt purpose is sufficient to preclude exemption, regardless of the number of exempt purposes. Better Business Bureau of Washington, supra. A inconsequential educational program will not overcome an substantial commercial purpose. American Institute for Economic Research.

You failed to provide any documentation that your DMP, credit repair and/or other financial services are an incidental adjunct to a substantial and substantive program of public education and individual counseling. In fact, you have provided no materials that indicate you will have a substantive on-going educational program directed to the individuals and families you serve in your DMP and credit repair programs. You also provided no documentation that you have or plan to conduct “credit counseling” seminars and/or workshops for the general community. The only “educational” materials you provided are the “promotional” information on your website and mortgage purchase documents you and FP use to market your mortgage services over the Internet. You did not explain when, where or how these materials would be used to “educate” individuals or families enrolled in your DMP or other financial services programs.

Providing commercial services to a charitable class for free would further “charitable” purposes within the meaning of section 501(c)(3). However, you have not provided substantial evidence that you will restrict your DMP, credit repair, and other financial services to low-income customers. If you do have “low-income limits” for participation in your DMP and other programs, you have provided no evidence of the specific guidelines that participants will be required to meet. You have provided no advertising materials stating that your services will be restricted to low-income individuals and/or families. In fact, information you provided indicates that your services will be available to the general public without regard to individual or family income.

Because you are operated as an integral part of FP, we further conclude that you are operated to further private financial interests of that business corporation and its owners. You share a common website, office space, and you conduct your DMP and credit repair activities in the same premises. It is not possible to distinguish your clients from those of FP. You are similar to the nurses’ registry described in Rev. Rul.61-170 in that one of your purposes is to enhance the business of a non-exempt entity. (Also see P.L.L. Scholarship Fund v. Commissioner, 82 T.C. 196 (1984), in which the court found that the organization and the for-

profit enterprise were so interrelated as to be functionally inseparable. Thus, the organization did not operate exclusively for exempt purpose, but rather benefited the private interests of the for-profit owners).

In addition, it is an inescapable conclusion that the income you generate inures directly to the benefit of FP and its owners. The owners of FP have sole authority and control over all of your decisions. Since you are an integral part of FP, it is impossible for you to negotiate on an arms-length basis.

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.

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
TE/GE (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
Rulings & Agreements

Attachment:
FTC Facts for Consumers, December 2005