TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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

Release Date: 10/20/2006
Release Number: **200642012**
Date: July 27, 2006

Contact Person:

Identification Number:

UIL: 501.00.00

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 24, 2006

Contact Person:

Identification Number:

Contact Number:

FAX Number:

UIL: 501.00-00

Employer Identification Number:

Dear :

We have considered your application for recognition of exemption from Federal income tax under section 501(a) of the Internal Revenue Code as any organization described in section 501(c)(3). Based on the information provided, 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 on . According to your Articles of Incorporation, you are, "organized exclusively for charitable, religious, scientific, literary, or educational purposes within the meaning of section 501(c)(3) of the Internal Revenue Code of 1986 (the "Code"), including, for such purposes, the making of distributions to organizations that qualify as exempt organizations under section 501(c)(3) of the Code, or corresponding section of any future federal tax code. In particular the Corporation shall advance education and promote social welfare by providing information regarding the sound use of consumer credit. In addition, the Corporation shall instruct the public on subjects useful to individuals and beneficial to the community."

Our evaluation of your Form 1023 Application, and other supporting documentation, indicates that your primary activity in furtherance of your purposes is the sale of a "debt consolidation" program. In your application, you stated that "representatives of the organization will counsel debtors on problems with debt and how to relieve it." In your "Sales Script", which you use to sell and promote your program, you made clear that you market a debt consolidation program, when you stated the following: "As you know we are not a loan company. We are a debt management company. We help consumers become Debt Free. The best program to become debt free is our Debt Consolidation program." You also made the following statement: "As you pay your bills through this program, we are able to gain certain benefits for you from

your creditors to help you save money. We can reduce the interest rates the banks are charging you anywhere from 7% to 13%. Some go as low as 0%, depending on the creditor. They also allow us to lower the amount of money you are spending monthly to make things a little more comfortable for you, and we'll simplify your bill-paying process so you only have one monthly payment."

You administer the program through a joint arrangement with another organization engaged in the debt management business. You call this program a "Debt Management Plan" (DMP). You stated, in your application, that clients with five or fewer creditors pay $39 per month, clients with six or more creditors pay $50 per month, and all clients pay a $75 processing fee. You represented that clients learn of the availability of your services through word-of-mouth. You also stated that your services are not limited to a particular group or class. You do, however, require that potential DMP clients "have $7500 in unsecured debt" to participate in the program.

The joint venture arrangement requires that potential clients send enrollment forms to you; that clients discuss goals, expectations, and financial history with you; that you draw up the agreement and send it to the client; and that after you review the agreement, you fax it to your business partner. Essentially, your role appears to be limited to procuring potential clients and delivering those qualified clients to your partner, who handles all processing services related to your DMP. You do not directly negotiate with creditors on behalf of your clients to achieve reductions in monthly payment amounts, or reduction or elimination of interest rates and penalties. You do not directly arrange to forward payment on the debtors' behalf at mutually accepted times. You do not negotiate with creditors on behalf of the debtors by submitting repayment proposals, but rather contract for these services with your partner who acts as the DMP processor for a fee. You represented that your "counselors" spend thirty minutes in their initial inquiry with a client, subsequent calls last from 5 to 10 minutes, and after enrollment in a DMP, from 5 to 30 minutes per month. You also stated that employees make from 5 to 10 calls per hour, and they answer from 20 to 30 calls per day. You appear to be operated solely as an intake office to secure qualified DMP clients for your joint venture partner.

Under the agreement, your partner is responsible for all processing services related to the DMP, including "the initial setup of debt management clients, normal management of client's funds received and creditors paid, negotiations with creditors, and customer service for clients." In return for your operation of the front-end call center on behalf of your processor, you receive a share of the fees generated from the DMP. A $13 fee is transferred to your partners operating account, and all remaining funds are shared between you (95 percent) and your partner (5 percent). In addition, any fair share contribution the processor receives from the creditors in relation to clients you refer to them is shared with you.

It is not clear whether these fees are in lieu of or in addition to the fees you initially charge your clients. You indicated that there is no charge for educational material to the debtor. It is not clear, however, whether you provide any material to callers who do not sign up for your DMP.

All of the materials you submitted, in support of your application, were provided to you by your DMP processing partner, or other organizations affiliated with your partner. You provided no evidence that you created any of these materials. The materials included a sales script, a income worksheet, a client debt management agreement, a sheet titled "Ten Steps To Financial

Success", a client information form, a creditor information sheet, a monthly budget worksheet, etc. You provided no indication of how these materials would be used in a systematic educational program with a structured educational methodology to "counsel" your clients. Additionally, you provided no evidence that you have or will conduct any seminars, workshops, or other educational forums on money management, consumer buying or budgeting directed to the general public.

You also provided no materials to be specifically used in the training of your "counselors" or employees. You provided no manuals, employee guides, or other materials commonly used in any such training. Moreover, you provided no evidence that any of these individuals have been certified to perform credit counseling by an accredited credit counselor training agency.

As part of your response to our letter dated July 5, 2005, you attached "Appendix B", in which you indicated that for fiscal years and "all revenue is generated from debt consolidation activities." You provided no evidence that you have an active fundraising program in operation. You also did not show, in your proposed budgets, that you have or will allocate any revenue for donations to educational or charitable programs. You did, however, indicate that you paid $182 per month for shared use of office space with a relative during . You did not provide a copy of any written agreement between you and the relative.

We also note that, in your letter dated August 9, 2005, you failed to answer the question of whether you have ever been a party any lawsuits. You also failed to indicate whether you have been the recipient of any start-up loans/capital from any sources.

Your Board of Directors is controlled by five individuals, two of whom are related by blood. You stated that the majority of members of your Board of Directors also serve as employees of your organization. You did not provide a copy of any employment agreements. These individuals have employment experiences in general business and the customer service industry.

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 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)(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.

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, was 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. Tax Cas. 9660 (D.D.C. 1978), the court held an organization that provided free information on budgeting, buying practices, and the sound use of consumer credit qualified for exemption from income tax because its activities were charitable and educational.

The Consumer Credit Counseling Service, which 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 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 debtor received full credit against his debts for all amounts paid. The organization did not make loans to debtors or negotiate loans on their behalf. Finally, the organization relied upon voluntary contributions, primarily from the creditors participating in the organization's budget plans, for its support.

The Service found that, by aiding low-income individuals and families who have financial problems and by providing, without charge, counseling and a means for the orderly discharge of indebtedness, the organization was relieving the poor and distressed. Moreover, by providing the public with information on budgeting, buying practices, and the sound use of consumer credit, the organization was instructing the public on subjects useful to the individual and beneficial to the community. Thus, the organization was exempt from federal income tax under section 501(c)(3) of the Code.

For an organization claiming the benefits of section 501(c)(3), "exemption is a privilege, a matter of grace rather than right." Christian Echoes National Ministry, Inc. v. United States, 470 F.2d 849, 857 (10th Cir. 1972), cert. denied, 414 U.S. 864 (1973). The applicant for tax exempt status under section 501(c)(3) has the burden of showing it "comes squarely within the terms of the law conferring the benefit sought." Nelson v. Commissioner, 30 T.C. 1151, 1154 (1958).

The Tax Court has stated that an application for tax-exempt status "calls for open and candid disclosure of all facts bearing upon [an Applicant's] organization, operations, and finances to assure [that there is not] abuse of the revenue laws. If such disclosure is not made, the logical inference is that the facts, if disclosed, would show that the [Applicant] fails to meet the requirements of section 501(c)(3)." Bubbling Well Church of Universal Love, Inc. v. Commissioner, 74 T.C. 531 (1980). See also, Founding Church of Scientology v. United States, 188 Ct. Cl. 490, 498, 412 F.2d 1197, 1201 (1969), cert. denied, 397 U.S. 1009 (1970). Furthermore, the courts have repeatedly upheld the Service's determination that an organization has failed to establish exemption when the organization fails to provide requested information. "[Applicant] has, for the most part, provided only generalizations in response to repeated requests by [the Service] for more detail on prospective activities....Such generalizations do not satisfy us that [applicant] qualifies for the exemption." Peoples Prize v. Commissioner, T.C. Memo 2004-12 (2004).

Section 5.02 of Rev. Proc. 90-27, 1990-1 C.B. 514, provides 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 restatement 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 for carrying out the activities, the anticipated sources of receipts, and the nature of contemplated expenditures. An organization that cannot demonstrate to the satisfaction of the Service the proposed activities will be exempt may be required to provide a record of actual operations for the Service to issue a ruling or determination letter.

Our analysis of the information you submitted shows that while you are organized for charitable purposes you do not satisfy the operational requirements to be recognized as exempt under section 501(c)(3) of the Code. There is no 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. In fact, the administrative record demonstrates that you operate for the substantial non-exempt purpose of selling DMP services to the general public. In addition, you have not shown that you operate for exclusively charitable and educational purposes rather than for purely private purposes.

Based on the information you submitted, you have not established that you operate for educational purposes within the meaning of section 501(c)(3). Training an individual to develop his capabilities or instructing the public on subjects useful to the individual and beneficial to the community are both educational purposes recognized as exempt. See section 1.501(c)(3)-1(d)(3) of the regulations. Financial counseling could be carried out as an educational activity. Consumer Credit Counseling Service of Alabama, Inc. v. United States, and Rev. Rul. 69-441, supra. While education is a broad concept, the Service and the Courts require an organization to have a substantial educational program not a non-educational program with some random educational features.

The information you have submitted provides no basis for us to conclude that you offer either education to the public on subjects useful to the individual and beneficial to the community or training to the individual. You failed to substantiate that you follow an educational methodology in operating your DMP. You failed to provide any evidence that your DMP is an incidental adjunct to a substantial and substantive program of public education and individual counseling. Your discussion with clients does not appear to include any educational material or counseling component. In fact, the limited materials you submitted were not created by you, instead they were supplied to you by your DMP partner. You did not explain how these materials would be used in the context of a systematic educational program with a structured educational methodology. You have not demonstrated that you conduct seminars, workshops, interactive on-line classes, or other educational forums on money management, consumer buying, budgeting, and financial management. You have provided no evidence that you provide individual counseling or additional educational activities after you sell a DMP. In fact, your contract with your processor seems to preclude ongoing educational activities upon completing the sale. Your Statement of Revenue and Expenses reflects no expenditures related to educational activities. Your primary focus is the “sale” of your DMP rather than the provision of substantial education to your clients. The activities you have described are completely different

from those found to be providing community education and individual training by the court in Consumer Credit Counseling Service of Alabama, Inc. v. United States, supra.

You are also unlike the organization described in Rev. Rul. 69-441, supra. That organization aided low-income individuals and families by providing them with individual counseling, and if necessary, by establishing budget plans. You represent that you will not limit your services to a particular class of people, such as minorities, low-income, or the elderly.

In addition, the information your submitted is insufficient to establish that you are not operated for a substantial non-exempt commercial purpose. This is reflected in the fact that your revenue will come exclusively from fees charged to clients and creditors for enrollment in DMPs. You limit your responsibility for managing your DMPs to that of merely selling the products, while you have contracted out all other processing and customer service responsibilities to another company for a percentage of the fees generated. Furthermore, the efforts of your "counselors," as reflected in the language in your "sales script" are primarily focused on aggressively promoting and selling DMPs.

Your financial structure does not resemble that of a typical charity. You have provided no evidence that any part of your funding will come from donations from foundations, private corporations and individual contributions. Moreover, you have failed to provide evidence that you received such donations or that you have a substantive plan to solicit these types of donations. Your funding comes entirely from fees from the sale of DMPs (both client fees and creditor fees). 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. (See, Better Business Bureau of Washington D.C., Inc. v. United States, supra.) You appear to have a substantial non-exempt commercial purpose.

Lastly, rather than being representative of a broad cross-section of the community, your board of directors is controlled by five directors, two of whom are related to each other. The majority of the directors also serve as employees, and as such, it would be impossible for them to conduct arms-length negotiations as it relates to their individual compensation, and other financial matters that will affect the organization's financial interests as well as their own. This presents an obvious and inherent conflict of interest where each individual is concerned. Moreover, you have not shown that the rent payments made to a "relative" during 2004, were negotiated and made on an arms-length basis. Thus, you have failed to establish that you serve a public rather than a private interest and that your income will not inure to the benefit of private individuals. (See section 1.501(c)(3)-1(d)(1)(ii) of the regulations.)

Because much of the information you provided is nonspecific and vague, it does not meet the burden of showing that your activities and operations are such that you are entitled to recognition of exemption under section 501(c)(3). See Christian Echoes National Ministry, Inc., Nelson and Rev. Proc. 90-27, *supra.* You have failed to describe your operations in sufficient detail to show that you are furthering an exclusively educational purpose. You failed to provide any documentation to establish that you engage in a substantial educational program and failed to clearly and fully explain how your operating a telephone call center to procure DMP clients for your "joint venture" processor furthers charitable purposes. You have not provided sufficient information and documentation to clearly establish that you will be operated for public rather than private purposes. You failed to answer the question of whether you have ever been a party to any lawsuits. You failed to indicate whether you have been the recipient of any start-up

loans/capital from any sources. Lastly, you failed to provide adequate documentation of the financial transactions, including compensation between you and members of your board of directors to permit us to conclude that you are not operated for the private benefit of private individuals and that your income will not inure to private individuals.

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:

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