



# DEPARTMENT OF THE TREASURY

Internal Revenue Service  
TE/GE EO Examinations  
1100 Commerce Street, MC 4920 DAL  
Dallas, TX 75242

**TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION**

501.03-00

November 17, 2010

Release Number: **201119034**

Release Date: 5/13/2011

**LEGEND**

ORG = Organization name    XX = Date    Address = address

Person to Contact:  
Identification Number:  
Contact Telephone Number:  
In Reply Refer to: TE/GE Review Staff  
EIN:

ORG

ADDRESS

**CERTIFIED MAIL - RETURN RECEIPT REQUESTED**

Dear

This is a Final Adverse Determination Letter as to your exempt status under section 501(c)(3) of the Internal Revenue Code. Your exemption from Federal income tax under section 501(c)(3) of the code is hereby revoked effective January 1, 20XX.

Our adverse determination was made for the following reasons:

Organizations exempt from Federal income tax under section 501(c)(3) of the Code are required to operate exclusively for charitable, educational, or other exempt purposes. Organizations are not operated exclusively for exempt purposes if the net earnings of the organization inure in whole or in part to the benefit of private shareholders or individuals of the organization. See Treas. Reg. § 1.501(c)(3)-1(c)(2). We have determined that your net earnings inured to the benefit of your Board Director, who is also the spouse of the President/Founder of ORG. Several unsubstantiated payments were made to your Board Director. These multiple payments were not substantiated as reimbursements of expenses incurred, were substantial in comparison to your total expenditures, and were repeated over two years. You have not implemented safeguards to prevent a recurrence of funds inuring to your Director or President/Founder. As such, you have not operated exclusively for exempt purposes but have operated for the benefit of private individuals and shareholders in contravention of the requirements of Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii).

Contributions to your organization are no longer deductible under section 170 of the Internal Revenue Code. You are required to file Federal income tax returns on Form 1120. These returns should be filed with the appropriate Service Center for the year ending December 31, 20XX and for all years thereafter.

Processing of income tax returns and assessment of any taxes due will not be delayed should a petition for declaratory judgment be filed under section 7428 of the Internal Revenue Code.

If you decide to contest this determination in court, you must initiate a suit for declaratory judgment in the United States Tax Court, the United States Claim Court or the District Court of the United States for the District of Columbia before the 91<sup>st</sup> day after the date this determination was mailed to you. Contact the clerk of the appropriate court for the rules for initiating suits for declaratory judgment.

You also have the right to contact the office of the Taxpayer Advocate. However, you should first contact the person whose name and telephone number are shown above since this person can access your tax information and can help you get answers. You can call 1-877-777-4778 and ask for Taxpayer Advocate assistance. Or you can contact the Taxpayer Advocate from the site where the tax deficiency was determined by calling: (949) 389-4804, or writing to:

Taxpayer Advocate assistance cannot be used as a substitute for established IRS procedures, formal appeals processes, etc. The Taxpayer Advocate is not able to reverse legal or technically correct tax determinations, nor extend the time fixed by law that you have to file a petition in the United States Tax Court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling.

We will notify the appropriate State Officials of this action, as required by section 6104(c) of the Internal Revenue Code.

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

Sincerely yours,

Nanette M. Downing  
Director, EO Examinations



DEPARTMENT OF THE TREASURY

INTERNAL REVENUE SERVICE  
300 N. Los Angeles St., MS 7300  
Los Angeles, CA 90012

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

**Date: 12/18/2009**

**Employer Identification**

**Form Number**  
**Tax Years Ended**  
**Person to Contact/ID Number**  
**Contact Number**  
Tel:  
Fax:

LEGEND

ORG = Organization name  
XX = Date    Address = address

ORG  
ADDRESS

**CERTIFIED MAIL – RETURN RECEIPT REQUESTED**

Dear

We have enclosed a copy of our report of examination explaining why we believe revocation of your exempt status under section 501(c)(3) of the Internal Revenue Code (Code) is necessary.

If you accept our findings, please sign and return the enclosed Form 6018, Consent to Proposed Action - Section 7428. If you have already given us a signed Form 6018, you need not repeat this process. We will issue a final revocation letter.

If you do not agree with our proposed revocation, you must submit to us a written request for Appeals Office consideration within 30 days from the date of this letter to protest our decision. Your protest should include a statement of the facts, the applicable law, and arguments in support of your position.

An Appeals officer will review your case. The Appeals office is independent of the Director, EO Examinations. The Appeals Office resolves most disputes informally and promptly. The enclosed Publication 3498, The Examination Process, and Publication 892, Exempt Organizations Appeal Procedures for Unagreed Issues, explain how to appeal an Internal Revenue Service (IRS) decision. Publication 3498 also includes information on your rights as a taxpayer and the IRS collection process.

You may also request that we refer this matter for technical advice as explained in Publication 892. If we issue a determination letter to you based on technical advice, no further administrative appeal is available to you within the IRS regarding the issue that was the subject of the technical advice.

If we do not hear from you within 30 days from the date of this letter, we will process your case based on the recommendations shown in the report of examination. If you do not protest this proposed determination within 30 days from the date of this letter, the IRS will consider it to be a failure to exhaust your available administrative remedies. Section 7428(b)(2) of the Code provides, in part: "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Claims Court, or the District Court of the United States for the District of Columbia determines that the organization involved has exhausted its administrative remedies within the Internal Revenue Service." We will then issue a final revocation letter.

You have the right to contact the office of the Taxpayer Advocate. Taxpayer Advocate assistance is not a substitute for established IRS procedures, such as the formal appeals process. The Taxpayer Advocate cannot reverse a legally correct tax determination, or extend the time fixed by law that you have to file a petition in a United States court. The Taxpayer Advocate can, however, see that a tax matter that may not have been resolved through normal channels gets prompt and proper handling. You may call toll-free 1-877-777-4778 and ask for Taxpayer Advocate Assistance. If you prefer, you may contact your local Taxpayer Advocate at:

If you have any questions, please call the contact person at the telephone number shown in the heading of this letter. If you write, please provide a telephone number and the most convenient time to call if we need to contact you.

Thank you for your cooperation.

Sincerely,

Nanette M. Downing  
Acting Director, EO Examinations

Enclosures:  
Publication 892  
Publication 3498  
Report of Examination

Form <b>886A</b>	Department of the Treasury - Internal Revenue Service <b>Explanation of Items</b>	Schedule No. or Exhibit
Name of Taxpayer  ORG (EIN)		Year/Period Ended December 31, 20XX through December 31, 20XX

**LEGEND**

ORG - Organization name      XX - Date      Address - address      City - city  
State - state      Founder - founder      BM-1 = 1<sup>st</sup> BM      EMP-1 = 1<sup>st</sup> EMP  
CO-1 THROUGH CO-17 = 1<sup>ST</sup> THROUGH 17<sup>TH</sup> COMPANIES      RA-1 THROUGH RA-31 - 1<sup>ST</sup>  
THROUGH 31<sup>ST</sup> RA

**ISSUES**

1. Whether ORG (ORG) was operated exclusively for one or more exempt purposes set forth under Internal Revenue Code (IRC) section 501(c)(3).
2. Whether ORG was operated for the private benefit of Founder, founder of ORG, and CO-1, a for-profit company co-owned and operated by Founder and BM-1, Board Director and spouse of Founder,
3. Whether the disbursements to BM-1, constituted inurement.

**FACTS**

**Background of ORG**

ORG was founded by Founder in July 19XX in City, State. ORG's office subsequently relocated to City, State. ORG was located at Address, City, State. According to Founder, ORG was formed for the purpose of helping people getting out of debt.

On Form 1023 Application for Recognition of Exemption Under Section 501(c)(3) of the IRC, ORG planned to conduct the following activities:

1. Free Individual Counseling. 45 minutes – 1 hour.
  - a. Helping clients restructure debt with repayment plan. 45 – 90 days.
2. Credit restoration and debt management.
  - a. Personal self help and instruction. 2 hours.
3. Follow up with customer individual progress periodically.
  - a. Reviewing all customer accounts and structuring debt management procedures for each account. 30 – 60 days.
4. Reviewing derogatory credit. 45 – 60 days. From clients credit report.
  - a. Showing them how to rebuild their credit file. 45 – 60 days.
5. Counseling and educating clients on debt management. 2 hours.
  - a. Debt elimination and debt management.

**ORG's Board of Directors**

During the years under examination, the Board of Directors included:

1. Founder, President and Counselor. (Certified through the Fair Credit Reporting Act in 20XX.)
2. BM-1, spouse of Founder.

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3. EMP-1, a financial advisor whom ORG used to refer clients to. EMP-1 is no longer with ORG.

During the years in question, Founder was the only counselor. Her primary duties and responsibilities included:

- Clients in-taking
- Clients screening
- Referring clients to service providers
- Working with lenders on behalf of clients, and
- Organizing and conducting workshops.

#### Related Entity

**CO-1 d.b.a. CO-2** – a for-profit biweekly mortgage payment owned by and Founder. CO-1 put mortgagees on bi-weekly mortgage payment programs whereby they can pay off their mortgage earlier. In a written response received by the Service on July 12, 20XX, Founder stated that ORG did not refer clients to CO-1 since it did mortgage acceleration, ORG's clients could not do this program. and Founder owns 51% and 49% of CO-1 respectively.

#### ORG's Programs

ORG engaged in little activity in 20XX and was inactive in 20XX due to Founder's illness. Since Founder was the only counselor, ORG had to temporarily suspend activity. ORG resumed operations in 20XX and is currently active. According to Founder, ORG conducts two primary programs:

1. Credit Card Relief Program
2. Foreclosure Assistance Program

#### Credit Card Relief Program

In this program, ORG refers individuals with credit card debts to debt settlement company for enrollment in debt elimination programs. The company that ORG refers clients to is CO-3s. The process begins with the caller contacting ORG and involves the following steps.

#### Step 1 – Initial Contact

In this step, Founder will go through a yellow Questionnaire Card asking the caller the type of service they need. The Questionnaire Card lists the following services:

- Mortgage Saving Analysis
- Semi-monthly / Bi-weekly Program
- Debt Management / Credit Report
- Financial / Retirement Analysis
- Real Estate Purchase / Sell
- Networking and Strategies



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The caller's response will be indicated on the Questionnaire Card. The caller can also pick up the card ahead of time and bring it to the appointment. Due to the lack of funding, Founder requested that the caller send her a pre-paid envelope so she can mail the Questionnaire Card to them.

### Step 2 – Client In-Take

This is the face-to-face or over the phone process. The caller fills out *The Debt Negotiator Confidential Questionnaire* answering questions about their income, expense, debts, etc. Founder will also ask for other information not listed on the questionnaire to get a complete financial picture.

### Step 3 – Presenting the Options

Once Founder gathers all the necessary information, she presents the client with several options. Depending on the situation of the client, not all clients will go through the same process or options. In general, this step involves the following options:

1. Budgeting – This involves creating a budget for the client to follow. Per Founder, most of the time clients have sufficient income to live comfortably but they just don't know it. The budget will give them a picture of where their money is going.
2. Referral to Service Providers:
  - i. Debt relief – This involves Founder referring the client to **CO-3 (CO-3)** for enrollment debt settlement program. The client will sign up with CO-3 to pay off their debts in 30 months or less. CO-3 is located at Address, City, State. CO-3 serves clients nationwide. The clients will sign the debt settlement agreement directly with CO-3. If the clients need assistance with filling out the DMP agreement, they can bring it to ORG for assistance. Otherwise, ORG's involvement ends here unless the clients need other referral services.
  - ii. There were other services providers. However, according to Founder, ORG did not refer clients to these service providers.

### Referring Clients to CO-3 (CO-3)

ORG refers clients to CO-3 for enrollment in debt settlement programs. Per Founder ORG referred 1 client to CO-3 in 20XX and 3 clients in 20XX. Founder further disclosed that ORG did not receive referral fees from CO-3. During the examination, Founder provided the Service with 10 client files who contacted ORG in 20XX. 3 of the 10 clients were referred to CO-3 for enrollment in debt settlement program. These were:

1. RA-1
2. RA-2
3. RA-3

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The Service contacted CO-3 to confirm the information ORG provided. CO-3 responded stating that it received no clients from ORG. CO-3, however, disclosed that it received 5 clients referred by Founder. CO-3 also provided the names of the 5. 3 of the 5 clients were ORG's clients:

1. RA-1
2. RA-4
3. RA-3
4. RA-5
5. RA-6

CO-3 further disclosed that the referral fees were paid directly to Founder and CO-1. The referral fees were paid on the above 5 clients.

The referral fees paid directly to Founder during the tax years 20XX and 20XX totaled \$ and \$ respectively. Founder disclosed that The referral fees were deposited into Founder's bank account. No referral fees were paid to ORG in 20XX.

The referral fees made directly to CO-1 during the tax years 20XX and 20XX totaled \$ and \$ respectively. The referral fees were deposited into CO-1's bank account. No referral fees were made to CO-1 in 20XX. According to a document titled "Salesperson Master" provided by CO-3, CO-1 is located at Address, City, State. The phone number for CO-1 is Phone #. CO-1's address and phone are the same as ORG's.

Founder responded to CO-3's statement stating that the referral fees were paid to CO-1 not Founder. Founder further stated that the 5 clients were CO-1's clients not ORG's and that CO-1 is one of ORG's referral service providers.

### **Foreclosure Assistance Program**

in this program, ORG will work with the lenders on behalf of homeowners who are behind in their mortgage payments and facing foreclosure. ORG represents the homeowners in working with the lenders to modify the terms of the loan so that the homeowners can continue to stay in their house and the lender getting their money back. ORG will:

- Assist the clients in contacting their lender.
- Assist the clients in preparing a budget for submission to the lender.
- Prepare documents to be submitted to the lender.
- Review and analyze all documents the clients receives from their lender.

ORG charges fees for this service. During the tax years 20XX to 20XX, the fees were determined based on the following factors:

- The client's financial situation.
- The number of loans involved.



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- The amount of document preparation.
- The number of hours that will be spent interacting with the client.

Beginning in 20XX, ORG charges a universal fee of \$\$ for all new clients. In the past, ORG used to refer clients to loan modification firms located in City, State and City, State for loan modification services. Depending on the firm and client situation, the fees range from \$\$ to \$\$.

The gross receipts from the loan modification activity totaled \$ and \$ of total receipts for the tax year 20XX and 20XX respectively.

#### **The Debt Elimination and Foreclosure Assistance Workshop**

In the past, ORG offered workshops on the subject of debt elimination. The workshop was conducted every 3<sup>rd</sup> Thursday of each month. The speakers were owners of local businesses who offer financial products and services. The workshop was conducted at the CO-4.

According to Founder, 4 people attended the workshop in 20XX and 2 people attended the workshop in 20XX. ORG stopped conducting the workshop in April 20XX.

The materials used for the workshop included:

1. Questionnaire Card (Refer to page 2 of this report for a description of the Questionnaire Card), and
2. ORG Program –

program is a 8-page brochure. The

contents of the brochure are as follow:

- 2 pages (including pictures) describing ORG, the services its offers and the network of its referrals
- 1 page containing proclamation from the City of City
- 4 pages of ads from local business that supports ORG.
- 1 acknowledgement page.

In 20XX, ORG revised the brochure. The contents of the new version are as follow:

- 3 pages (including pictures) describing ORG, the services its offers and the network of its referrals
- 2 pages of ads from local business that supports ORG
- 1 page describes the Credit Card Relief Program
- 1 page describes the Foreclosure Assistance Program
- 1 page solicits donations.

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The Credit Card Relief Program, as described in used in the debt elimination workshop, promises the workshop participants:

- Immediate reduction of monthly payments
- One low monthly payment
- Stop harassing phone calls
- No bankruptcy or any form of bankruptcy
- No debt consolidation
- Settle debt for pennies on the dollar
- Elimination of debt

The Foreclosure Assistance Program shows the homeowners who are behind in their mortgage payments the 7 alternatives to foreclosure.

**Announcements of the Debt Elimination and Foreclosure Workshop**

ORG was allowed to announce the workshop in CO-5 newspaper. The following is a content of the ad that was placed on December 12, 20XX,

ORG— offers a debt elimination workshop every third Thursday of each month from 6 to 8 p.m. at CO-4, Address This month speaker is RA-7 on home buying tips and qualifying. Phone #.

The following was the announcement placed in CO-5 on April 24, 20XX,

Nonprofit group is hosting a free seminar on building wealth in real estate from 12:30 to 2:30 p.m. Saturday at the CO-4, Address Information: Phone #.

The following was the announcement in CO-5 on December 13, 20XX,

**A FREE FORECLOSURE WORKSHOP** will be from 6:30 to 8p.m. Dec. 20 in the east room of the CO-4, Address Reserve a seat before Tuesday. People can also get free consultations. Phone #.

The following announcement was made in the CO-6 newsletter, a newsletter published by the CO-7.

Free Non Profit Counseling Assistance Learn your options and get help with foreclosure prevention and debt relief. Call Phone # to save your home/get out of debt.

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### Counseling Activity

Founder disclosed that during the tax year 20XX, ORG assisted 577 clients with creating and maintaining a budget. Of the 577 clients, 566 were counseled over the phone (most of which just wanted quick answers to their budget needs or wanted a referral). ORG maintains a call log containing the phone memos recording the contacts with these callers. The phone memos contain the following information:

- Name
- Date called
- Contact number, and
- A brief message (for some)

Some phone memos contain only date and month. Some of the phone memos were dated back in 20XX and 20XX. Some dates were crossed out and were replaced with a different date.

ORG provided the Service with the phone memos. The phone memos were faxed over to the Service via several separate transmittals. Some phone memos were transmitted as many as three times creating duplications. With the duplications, the call log received by the Service contains 510 phone memos. Without the duplications, the call log contains 290 phone memos.

### Information Provided By Third Parties

The Service contacted 65 individuals on the call log to confirm the information ORG provided. Since the phone memos only contain a name and a phone number, the Agent called these individuals asking for their address. Of the 65 numbers, 59 numbers were either disconnected or no longer in service. The Service was able to contact the remaining 6 individuals. The results of the contacts are as follows:

- 1 individual disclosed that he contacted ORG to repair his credit but decided not to accept the services offered by ORG because it was too much money. The individual also paid \$ as a service provider fee to ORG.
- 1 individual disclosed that he contacted ORG for credit debt counseling but decided not to go through with the application process.
- 4 individuals disclosed that they had no contact with ORG and were not aware of ORG.

In response to the individuals who stated that they were not aware of ORG, Founder stated that most of these people don't even remember talking with ORG because of the years in question from 20XX-20XX.

In response to Founder, the Service contacted 3 of the 4 individuals again. The results of the second contact are as follows:

- 1 individual maintained that he had no contact with ORG and was not aware of ORG.

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- 1 individual maintained that she had no contact with ORG but remembers knowing Founder about 10 years ago when Founder was doing bi-monthly programs. The individual does not recall hearing ORG and has not seen Founder in about 10 years.
- 1 individual maintained that he had no contact with ORG. The individual, however, dealt with CO-1 and Founder in a real estate transaction. The individual did not know that Founder was from ORG Enterprise. See Exhibit 1.

In addition to contacting the individuals on the call log, the Service also contacted 3 of the 10 individuals who ORG maintained client files for.

- 2 of the 3 letters were returned undeliverable. The clients moved and the Post Office was not able to forward the letters.
- 1 of the 3 clients the Service contacted disclosed that he never used ORG for any services. On a subsequent follow up call, the individual maintained that he had no contact with ORG and did not use ORG for any services.

#### ORG's Web Site

ORG maintains a web site. On the web site, ORG offers the following services:

- Budget counseling
- Obtaining/understanding your credit report
- Biweekly loan payments
- Debt settlement/mediation
- Mortgage/loan analysis
- Financial budget analysis
- Low cost family healthcare
- 8 Steps To Debt Elimination and other debt management material
- Loan counseling/consolidation (services only available locally)
- Real estate counseling-new homebuyer plans (services only available locally)
- Financial counseling (services only available locally)

The web site further describes that,

- ORG helps eliminate credit card (unsecured debt) in 30 months or less as well as residential, commercial and auto loans (secured debt) 8-10+ years sooner – without refinancing, consolidating, bankruptcy or increasing your monthly payments. This past year, ORG assisted/helped 42 families get out of debt without having to declare bankruptcy; which most of them had been instructed to do. We saved a lot of homeowners millions of dollars they would have paid to their lending institutions (without refinancing or changing their monthly payment) just by putting their 15/30 year mortgages, mobile homes, auto loans and other secured debt on a split payment or biweekly payment plan with their existing lenders.
- Its debt elimination strategies utilizes network of professional referral services based on the individuals specific needs.

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- We have trained debt specialist that will work directly with you during your 30-month completion of your program. You will not have to talk with your creditors. That is what the trained debt specialist job is.
- The individuals select a 12, 20 month or 30 month program.
- The trained debt mediators use the power of leverage in packaging up hundreds of other accounts pooled with yours to get the lowest settlement possible.
- You complete our debt settlement program in 30 months or less whether you have \$ or \$ of credit card and other unsecured debt.
- It costs approximately 60 cents on the dollar for the total amount of unsecured debt enrolled in the debt settlement program, including all retainer, monthly maintenance, program and settlement fees.
- The individuals will make monthly payments will be about 2% of the total enrolled debt amount for the next 30 months to a trust account rather than their creditor.
- Once a settlement offer is accepted by the creditor, a lump-sum settlement payment will be made to the creditor.

Qualifications for the debt elimination program

- Individuals who have a minimum of \$ of credit card/unsecured debt and is struggling financially.
- Individuals who have been more than 30 days late to your creditors; in collections or considering bankruptcy, never been late but have a high or low debt-to income ratio
- Individuals who have suffered a financial hardship due to medical problems, loss of job or a dramatic decrease in take-home pay.

**Financial Information**

ORG was not required to file Form 990 Return of Organization Exempt from Federal Income Tax for the years in questions. ORG's gross receipts were under \$. A review of ORG's bank statements discloses the following:

Deposits Made in 20XX			
Deposit Date	Payor	Amount	Memo
3/21/XX	RA-8		Deposit checking
12/7/XX	CO-8		
9/29/XX	RA-9		Credit report
11/1/XX	RA-13		Your credit booklet and CD
11/1/XX	RA-13		Your credit booklet and CD
2/10/XX	RA-10		CD
2/10/XX	RA-10		Credit report
2/9/XX	RA-101		
2/1/XX	RA-12		property profile
12/19/XX	RA-12		Credit report

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1/23/XX RA-14  
12/12/XX RA-15

Deposits Made in 20XX			
Deposit Date	Payor	Amount	Memo
1/1/XX	RA-16		
1/16/XX	RA-17		Property profile (2)
1/20/XX	RA-12		recorded grant deed
1/23/XX	RA-18		
1/23/XX	RA-19		
3/14/XX	RA-20		Balance due 4/30/XX partial payment
4/4/XX	RA-20		Final Payment
4/11/XX	RA-20		
4/21/XX	RA-13		Loan
5/15/XX	RA-21		#
6/2/XX	RA-21		#
6/5/XX	RA-22		Donation for ORG
7/26/XX			
10/27/XX	RA-21		Ref #
11/25/XX	RA-21		Ref #
12/22/XX	RA-23		#

The payments from RA-20, RA-21 and RA-23 totaled \$ respectively. ORG represented these individuals in dealing with their lenders to modify the terms of their mortgage.

Deposits Made in 20XX			
Deposit Date	Payor	Amount	Memo
1/19/XX			
1/25/XX	RA-23		#
2/6/XX	RA-24		
3/7/XX	RA-25		For credit correction
9/6/XX	RA-26		ORG PRT
10/20/XX	RA-26		
11/1/XX	RA-26		
11/15/XX	RA-26		HC
12/1/XX	RA-26		HC
12/26/XX	RA-27		Donation



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\_\_\_\_\_ Replacement check  
\_\_\_\_\_

The payments from RA-26 totaled \$. ORG represented RA-26 in dealing with his lender to modify the terms of his mortgage. The payments from RA-23 and RA-26 totaled \$.

DISBURSEMENTS				
Date	Check No.	Payee	Amount	Memo
2/11/XX		Secretary of State		ORG corp filing
3/7/XX		RA-28		Beauty
6/29/XX		CO-9	_____	#XX
			_____	
4/5/XX		BM-1		Deposit
4/24/XX		BM-1		Deposit B of A
5/16/XX		BM-1		Deposit
11/8/XX		BM-1		Deposit
12/28/XX		BM-1		B of A Deposit
1/26/XX		RA-29		\$ tip
4/5/XX		CO-10 – loan		April payment
2/6/XX		RA-30		RA-30
4/4/XX		RA-30		RA-30
6/10/XX		Founder		Counter withdrawal
2/11/XX		CO-15		
4/16/XX		CO-15		Pmt of postage
3/14/XX		CO-9		March donation
7/6/XX		CO-11		ORG corp renewal
7/6/XX		CO-13 #62		purchase
3/23/XX		CO-14		Office water system
3/7/XX		Secretary of State		
6/10/XX		Vital Records		BM-1
6/12/XX		Vital Records	_____	birth cert
			_____	
11/2/XX		CO-12		
2/1/XX		BM-1		
9/8/XX		BM-1		
11/2/XX		BM-1		

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12/1/XX	BM-1	Deposit B of A
12/7/XX	BM-1	
12/30/XX	BM-1	
8/16/XX	City of City	ORG business license renewal
12/23/XX	CO-16	
12/19/XX	RA-29	\$ tip
3/14/XX	CO-1	
11/15/XX	Founder	
12/7/XX	CO-15	
12/4/XX	CO-17	

Founder discloses that ORG relies on in-kind donations from local business such as Staples, Office Depot and a bookstore for office supplies such as papers, ink, etc.

The payments to BM-1 totaled \$ and \$ for the tax years 20XX and 20XX respectively. Of the 11 payments to BM-1, 8 contain no description of the purposes of the payments or the expenses being reimbursed. The remaining 3 contain "Deposit B of A" or "B of A Deposit" on the memo line.

Founder disclosed that the payments to BM-1 were reimbursements for operating expenses BM-1 paid on behalf of ORG. The Service requested substantiations such as receipts and canceled checks for the payments made to BM-1. Founder disclosed that there were no invoices, receipts, or paid bills that existed. Founder further stated that BM-1 paid these operating expenses either by phone or by electronic debit and he keeps no records of the payments that he made on behalf of ORG.

### LAW

IRC section 501(c)(3) exempts from federal income tax corporations organized and operated exclusively for charitable, educational, and other purposes, provided that no part of the net earnings inure to the benefit of any private shareholder or individual. Treasury Regulations (Treas. Reg.) 1.501(c)(3)-1(a)(1) 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.

Treas. Reg. 1.501(c)(3)-1(b)(1)(i) 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

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(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.

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

Treas. Reg. 1.501(c)(3)-1(c)(2) 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.

Treas. Reg. 1.501(c)(3)-1(d)(1)(ii) requires an organization to demonstrate 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.

Treas. Reg. 1.501(c)(3)-1(d)(2) 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.

Treas. Reg. 1.501(c)(3)-1(d)(3) 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.

Treas. Reg. 1.501(c)(3)-1(c)(1) provides that an organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities that accomplish one or more of such exempt purposes specified in section 501(c)(3). An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. Better Business Bureau of Washington, D.C. v. U.S., 326 U.S. 279 (1945).

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Treas. Reg. 1.501(c)(3)-1(d)(1)(ii) states that an organization is not organized or operated exclusively for one or more of the purposes specified in subdivision (i) of this subparagraph unless it serves a public rather than a private interest. Thus, to meet the requirement of this subdivision, it is necessary for an organization to establish that it is not organized or operated for the benefit of private interests such as designated individuals, the creator or his family, shareholders of the organization, or persons controlled, directly or indirectly, by such private interests.

Educational purposes include instruction or training of the individual for the purpose of improving or developing his capabilities and instruction of the public on useful and beneficial subjects. Treas. Reg. § 1.501(c)(3)-1(d)(3). In Better Business Bureau of Washington D.C., Inc. v. United States, 326 U.S. 279 (1945), the Supreme Court held that the presence of a single non-exempt purposes, if substantial in nature, will destroy the exemption regardless of the number or importance of truly exempt purposes. The Court found that the trade association had an "underlying commercial motive" that distinguished its educational program from that carried out by a university.

Rev. Rul. 69-441, 1969-2 C.B. 115, granted 501(c)(3) status to an organization with two functions: it educated the public on personal money management, using films, speakers, and publications, and provided individual counseling to "low-income individuals and families." As part of its counseling, it established budget plans, *i.e.* debt management plans, for some of its clients. The debt management services were provided without charge. The organization was supported by contributions primarily from creditors. By virtue of aiding low income people, without charge, as well as providing education to the public, the organization qualified for section 501(c)(3) status.

In the case of Consumer Credit Counseling Service of Alabama, Inc. v. U.S., 44 A.F.T.R.2d 78-5052 (D.D.C. 1978), the District Court for the District of Columbia held that a credit counseling organization qualified as charitable and educational under section 501(c)(3). It fulfilled charitable purposes by educating the public on subjects useful to the individual and beneficial to the community. Treas. Reg. section 1.501(c)(3)-1(d)(3)(i)(b). For this, it charged no fee. The court found that the counseling programs were also educational and charitable; the debt management and creditor intercession activities were "an integral part" of the agencies' counseling function and thus were charitable and educational. Even if this were not the case, the court viewed the debt management and creditor intercession activities as incidental to the agencies' principal functions, as only approximately 12 percent of the counselors' time was applied to debt management programs and the charge for the service was "nominal." The court also considered the facts that the agency was publicly supported and that it had a board dominated by members of the general public as factors indicating a charitable operation. See also, Credit Counseling Centers of Oklahoma, Inc. v. United States, 79-2 U.S.T.C. 9468 (D.D.C. 1979), in which the facts and legal analysis were

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

The court in est of Hawaii v. Commissioner, 71 T.C. 1067(1979) found that an organization formed to educate people in Hawaii in the theory and practice of "est" was a part of a "franchise system which is operated for private benefit," and therefore may not be recognized as exempt under section 501(c)(3) of the Code. The applicant for exempt status was not formally controlled by the same individuals controlling the for-profit organization owning the license to the est body of knowledge, publications, methods, etc. However, the for-profit exerted "considerable control" over the applicant's activities by setting pricing, the number and frequency of different kinds of seminars and training, and providing the trainers and management personnel who are responsible to it in addition to setting price for the training. The court found that the fact that the applicant's rights were dependent upon its tax-exempt status showed the likelihood that the for-profit corporations were trading on that status. The question for the court was not whether the payments made to the for-profit were excessive, but whether it benefited substantially from the operation of the applicant. The court determined that there was a substantial private benefit because the applicant "was simply the instrument to subsidize the for-profit corporations and not *vice versa* and had no life independent of those corporations."

In American Institute for Economic Research v. United States, 302 F. 2d 934 (Ct. Cl. 1962), the Court considered the status of an organization that provided analyses of securities and industries and of the economic climate in general. The organization sold subscriptions to various periodicals and services providing advice for purchases of individual securities. Although the court noted that education is a broad concept, and assumed for the sake of argument that the organization had an educational purpose, it held that the organization had a significant non-exempt commercial purpose that was not incidental to the educational purpose and was not entitled to be regarded as exempt.

In The Founding Church of Scientology v. United States, 412 F.2d 1197 (Ct. Cl. 1969), the court ruled that the absence of a suitable explanation for other payments made to and for the founder and his family disqualified the organization for tax-exempt status.

### **GOVERNMENT'S POSITIONS**

Issue 1: Whether ORG. was operated exclusive for one or more exempt purposes set forth under IRC section 501(c)(3).

#### Government's Position



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An organization exempt from Federal income tax under IRC section 501(c)(3) must demonstrate that it is operated exclusively for one or more exempt purposes set forth under such section.

A review of the services you provided in and are currently providing disclosed that you neither operated for charitable nor educational purposes. You operated like a referral service company whereby you screen individuals contacted you and then refer them to other for-profit businesses for services.

One of your primary programs, the Credit Card Relief Program, in essence, is a debt settlement program whereby the debtors settle their unsecured debts at 60 cents on the dollar for the total amount of unsecured debt enrolled in the debt settlement program, including all retainer, monthly maintenance, program and settlement fees.

The Credit Card Relief program is offered to any debtors who have \$ or more of credit cards or unsecured debt. In the Credit Card Relief program, you acted as a middleman between the debtors looking for debt settlement service providers and CO-3, a debt settlement service provider. You disclosed that your roles were to perform in-take and screen debtors for enrollment in debt settlement programs. If the debtors qualified for debt settlement program, you referred them to CO-3. In return, CO-3 paid you referral fees. Once the debtors are referred to CO-3, your involvement ends, unless the debtors need assistance with completing the debt settlement forms or need other referral services.

The Foreclosure Assistance Program, the other primary activity that you conduct, is similar to loan modification services offered by for-profit businesses. The Foreclosure Assistance Program generated 93% of total gross receipts for each of the tax years 20XX and 20XX respectively. In the Foreclosure Assistance Program:

- You represent the homeowners who are behind in their mortgage payments in negotiating the terms of their mortgage with financial institution.
- You assist the homeowners in contacting their lenders.
- You prepare documents required by the lender.
- You review and analyze all documents the homeowners received from their lenders

You perform these services for the purpose of attaining approval for the clients' loan modification application. In return, you charge your clients fees for your services. Your fee structures are set in a manner similar to those of for-profit loan modification service providers. Prior to 20XX, your fee structure was based on the numbers of loan involved, the amount of document preparation, document review and the hours spent interacting with the client. Your fees could be as high as \$. For example, you charged RA-20 \$ RA-21 \$ and RA-26 \$ for loan modification services.



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In 20XX, you adopted an universal fee policy of \$\$ per property. The fee of \$\$ is the same amount of fees charged by for-profit loan modification firms such as the ones in City and City that you once referred homeowners to.

You disclosed that ORG was inactive in 20XX. However, a review of your bank records disclosed that you were offering loan modification services and received payment for these services. The loan modification services were offered to RA-31, RA-21, and RA-23.

Therefore, it is concluded that you primarily offer fees for services that neither further a charitable or educational purpose set forth under IRC 501(c)(3). The existence of a substantial nonexempt purpose, regardless of the number or importance of exempt purposes, will cause failure of the operational test. See also Better Business Bureau of Washington, D.C. v. U.S.

You disclosed that in 20XX, you counseled 577 individuals in setting up and maintaining a budget. Of the 577 individuals, 566 of them were counseled over the phone. The phone memos you faxed to our office do not support your claim. The same phone memos were faxed to our office several times. Without the duplication, there were 290 calls not 566 as you claimed. Some phone memos were dated in 20XX and 20XX. The date on some phone memos were crossed out and replaced with dates in 20XX.

Our contacts with these individuals to confirm the information disclosed otherwise. These individuals disclosed that they either:

- Were not aware of ORG.
- Did not receive any counseling from ORG.
- Did not contact ORG for services

In one instance, the individual disclosed that he dealt with Founder, BM-1 and CO-1 in a real estate transaction. At no time did the individual disclose that was he aware of ORG.

You stated that these individuals disclosed to the IRS that they were not aware of ORG so that they did not have to deal with the IRS. The Service reconfirmed with these individuals and received the same responses that they either were not aware of ORG or did not have any dealing with ORG. Therefore, the Service has reason to believe that these individuals were truthful in giving with their responses to the Service.

In summary, ORG was not operated to further one or more exempt purposes described under IRC section 501(c)(3). The Credit Card Relief Program is a referral service whereby ORG intakes, screens and refers debtors to for-profit debt settlement business

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for fees. The Foreclosure Assistance Program is a fee-for-service whereby ORG assists the homeowners getting the terms of their loan(s) modified. In return, ORG charges fees similar to those of for-profit loan modification service providers.

Issue 2: Whether ORG was operated for the private benefits of Founder, founder of ORG, and CO-1, a for-profit company co-owned and operated by Founder and BM-1.

Government's Position

Treas. Reg. 1.501(c)(3)-1(d)(1)(ii) requires an organization to demonstrate 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.

You disclosed that in the years under examination, ORG referred clients to CO-3 for enrollment in debt settlement programs. You further disclosed that ORG did not receive referral fees from CO-3. You then provided the names of these clients. CO-3, however, disclosed that it paid referral fees for the clients. The referral fees were paid directly to Founder and CO-1. Founder and CO-1 then deposited the referral fees into their bank accounts. In response to CO-3's response, you stated that the referral fees were paid to CO-1 not Founder. You also disclosed that CO-1 referred clients to CO-3 not ORG. You further disclosed that CO-1 is one of ORG's referral service providers. In a written response to the Information Document Request (IDR) 02 titled "Form 4564 IRS Information Document Request" completed on July 12, 20XX, you stated that "ORG did not refer clients to CO-1 Inc since it did mortgage acceleration, ORG clients could not do this program." (Item 15 of your response).

The evidence indicates that you operated ORG for your private benefits. You first used ORG to obtain clients. Once the clients qualified for debt settlement program, you referred the clients to CO-1, a for-profit company owned by you and your spouse, even though ORG's clients could not do the mortgage acceleration. CO-1 then referred clients to CO-3 and received the referral fee payments from CO-3.

Issue 3:

Whether the disbursements to BM-1, Board Director and spouse of Founder, constitute inurement.

Government's Position

IRC section 501(c)(3) expressly prohibits the inurement of net earnings to the benefit of private shareholders or individuals. Treas. Reg. 1.501(c)(3)-1(c)(2) clarifies 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.

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During the tax years 20XX and 20XX, ORG made several payments to BM-1, director and spouse of Founder. The payments totaled \$ and \$ or % and % of total disbursements for the tax years 20XX and 20XX respectively. Founder disclosed that the payments to BM-1 were reimbursements for operating expenses that BM-1 paid on behalf of ORG. However, ORG failed to provide substantiations for the payments made to BM-1. The unsubstantiated disbursements to BM-1 constituted inurement. See also The Founding Church of Scientology v. United States, 412 F.2d 1197 (Ct. Cl. 1969)

**TAXPAYER'S POSITIONS**

ORG's positions on issues 1, 2 and 3 are not known at this time.

**CONCLUSION:**

ORG was not operated to further one or more exempt purposes set forth under IRC section 501(c)(3). ORG's net earnings inured to the private individuals and shareholders. Therefore, ORG's tax exempt status under IRC section 501(c)(3) should be revoked effective January 1, 20XX. ORG is required to file Form 1120 US Corporation Income Tax Return for the tax year 20XX and all years after.