

QUESTION 5-a

a. The Church uses the "modified cash" method of accounting. Please define this method of accounting and describe all adjustments necessary to change from the cash method to the modified cash method of accounting.

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Modified cash basis means that the annual summaries of cash receipts and disbursements, as recorded in the Church's routine monthly audits, are modified or adjusted as follows:

- acquisitions of fixed assets are capitalized as balance sheet items (not written off to Revenue); any surplus/deficit on disposals is adjusted through the Income and Expenditure account;

- annual depreciation is reflected as a expenditure (a charge against income) on the annual income and expenditure statements. In addition, the depreciation charge is also reflected in a balance sheet account for accumulated depreciation.

- assets not placed in service at year-end are identified and excluded from depreciable assets;

- bookstore inventories are adjusted to reflect the end of year physical inventory at lower of cost or market and the cost of goods sold account on the Income and Expense summary is adjusted accordingly;

- parishioners' unused advance donations are adjusted by excluding them from cash Revenue and including them as liabilities or deferred receipts, whichever is appropriate;

- any amounts due on contracts, loans, or time payment purchases are adjusted to show the end of year liability in the balance sheet;

- where applicable, inter-corporate loans from or to another Scientology organization are adjusted to ensure they are reflected in the appropriate balance sheets.

Most non-US Churches prepare annual balance sheets on the full accrual basis; thus it is US Church organizations to whom the modified cash method of accounting mainly applies.

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QUESTION 5-b

b. The submissions contain numerous references to HCO Policy Letters and other portions of the Scriptures relating to the Church's financial activities. To facilitate our understanding of the Church's accounting and financial systems, please provide a current and complete set of the Organization Executive Course volumes, excluding the HCO Technical Bulletin volumes.

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Based on the Service's assurances that the sole purpose for requesting these volumes is for reference purposes to better understand the Church's internal workings and finances, we are including one full set of the Organizational Executive Course ("OEC") with this submission. Nevertheless, these materials must be viewed in their context.

The full materials of Scientology are contained in over forty million spoken and written words by Mr. Hubbard. This includes over 3,000 taped lectures (which when fully transcribed will fill 100 encyclopedia sized books), 13 volumes of technical writings on the procedures and philosophy of auditing (red volumes), and dozens of individual books on a variety of Scientology subjects. The OEC volumes are but a small portion of the philosophy and technology of the Scientology religion. The currently published Scientology materials and reproduced taped lectures on cassette - excluding the confidential advanced course materials - are shown in the attached photograph. The OEC consists of the 12 green volumes in the center of the photograph. Please also refer to pages 705 through 781 of the book What is Scientology?. Those 76 pages of text give a complete listing of Dianetics and Scientology books, technical and administrative issues, articles, films, recorded lectures, cassettes, and special publications all in the chronological order in which they were created.

Each OEC volume corresponds to a division on the organizing board; each volume is meant to be a training or "hatting" manual for the head of that numbered division. For example, Division 4, the Technical Division, is responsible for teaching auditor training courses and for the ministry of auditing services. Volume 4 of the OEC contains the materials relevant to operating Division 4 and performing its functions, including how courses are supervised and how auditing is scheduled. (Volume 4 does not cover what is taught in the courses or what actions are performed in an auditing session; that is the subject of the Technical (Red) volumes.) The other volumes correspond to the

relevant divisions as follows:

Volume 1:	Division 1 -- Hubbard Communications Office (HCO)
Volume 2:	Division 2 -- Dissemination
Volume 3:	Division 3 -- Treasury
Volume 4:	Division 4 -- Technical
Volume 5:	Division 5 -- Qualifications
Volume 6:	Division 6 -- Public Divisions
Volume 7:	Division 7 -- Executive Division

Volume zero does not represent any division on a Scientology org board. Rather, this volume is the Basic Staff Hat, which contains general information on church organizational principles that all staff members should know regardless of their specific posts.

The OEC volumes do not represent one copy of each different issue. Some data is relevant to more than one division head, in which case the relevant issue will be contained in the volume applicable to each division. Furthermore, each volume is categorized by org board department within each division. So that department heads may study their responsibilities from these books, the materials for their department are individually categorized. Individual sections and units within each department are individually categorized. Additionally, within these categorizations, the materials appear in chronological order to provide the church staff member with the history and evolution of the relevant function within Scientology. In this way, instead of simply gaining rote understanding of what actions are to be performed or of what the structure is, the staff member instead learns why it is that way.

Management Series volumes 1, 2 and 3 similarly do not correspond to any division but instead contain material relevant to higher level management of such organizations, such as by the Exec Council. Their sequence has no relevance and in fact each volume contains self contained series of issues on different subjects. For instance, volume 1 contains the Data Series, which covers the subject of logic and how to evaluate. This is followed by the Organizing Series which is relevant material for an Organizing Officer and covers such topics as hatting and the theory of organization.

As explained in our meeting of 26 October 1992, we were reluctant to furnish the Service with the OEC volumes. Our consistent experience has been that the IRS and its attorneys have used small parts of policies, or single policies, out of context as a method of attacking Scientology. In fact, during the last round of negotiations, a full set of OEC Volumes,

Technical Volumes, books and the then existing taped lectures were provided to the Service. As we expected and predicted, the Service used these materials to quote the EXACT SAME OUT OF CONTEXT PASSAGES as the Service had advanced in the CSC case.

For example, in one policy letter in Management Volume 2, which contains the Finance Series, Mr. Hubbard instructs an FBO that, among other things, a governing policy of finance is to "make money". Taken in its entirety, however, this policy letter is simply common sense managerial direction for any organization that wants to survive and expand. Indeed, the principal function of the finance officer of any organization, profit or not for profit, taxable or exempt, is to "make money" to assure that the organization remains financially viable. This policy appears only in the Finance Series, which would not be the case if it were applicable to other Church functions. Yet, the Service has routinely cited these few simple lines as "proof" that the overriding purpose of all of Scientology is "commercial." In truth, barely one percent of Scientology Scripture has anything at all to do with finance.

Further, nowhere in that policy letter does Mr. Hubbard cite money as a motivation. In fact the only policy that does contain information on motivation is HCOPL 11 November 1969 which states:

" MONEY MOTIVATION

The weakest motivation is money. People and businesses that are motivated only by money are wobbly people.

The scale of motivation from the highest to the lowest is:

**Duty -- highest
Personal Conviction
Personal Gain
Money -- lowest**

Money is important in the world. But it is the grease on the machinery, not the motors. In a society which has lost its patriotism and pride, money will be found as a primary motivation. True, one is in trouble without money and it is a crime in the eyes of the society to be without money. But one also needs dirt to stand on and yet dirt cannot be said to be the primary motivation for living."

Yet somehow the IRS and other detractors never quote the above policy, which is the definitive Church policy on the subject of motivation and purposes as related to money. Instead we are vilified with out-of-context quotes that are further interpreted falsely by the Service passing their interpretations off on courts. The result is so-called facts stated by a court allegedly communicating our beliefs; but which are totally false and abhorrent to us.

In another policy, Mr. Hubbard advises church staff in handling tax people to "never volunteer anything." The Service has used this statement to argue that the Church is "theologically hostile" to taxes. Yet that same paragraph states that one must not give tax people false data and must always be able to back up data one gives. The rest of that policy stresses recording and reporting the exact truth of all transactions. While it is true that Mr. Hubbard makes an unflattering reference to the government's "bloodsucking appetite," that is hardly a novel view.

Entire policies can also be taken out of context. For example, Scientology refund policies have been criticized as being commercial. Yet, taken in the full philosophical context of our religion, this is an extremely ethical practice. Refunds are also a very important cross-check, because a refund request from a parishioner alerts the Church that the religious technologies of Dianetics and Scientology have not been applied properly.

Despite our concerns, we are producing these materials so that there can be no question that we are fully cooperating with your requests and are making full disclosure. It is impossible, however, simply to study these materials and then understand them in context. To begin with, they were written not for the IRS, but for Scientologists who have a basic understanding of the philosophy and practice of Dianetics and Scientology. Our attorneys and accountants have prepared a detailed audio-visual presentation that thoroughly explains our finance system, which we believe is a more productive way for the Service to more fully understand our system.

One of Mr. Hubbard's observations, which forms the basis of the secular application of Scientology principles in the field of education, is that no reader should continue past any word or concept he or she does not understand. Please come back to us for any explanation or clarification you may need. The Service would not (nor would a court permit it to) make a tax

determination based on its own interpretation of Catholic, Jewish or Mormon doctrine; because it is new and comparatively unknown, there is even less reason for the Service to do so with Scientology.

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