

JUL 24 1987

Dear Sir or Madam:

We have considered your application for recognition of exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code.

Information submitted with your application shows that Articles of Organization were approved [REDACTED]. Those Articles were amended to meet the organizational test of Internal Revenue Code section 501(c)(3) [REDACTED]. You provided a statement that your organization has no By-laws

Your purpose as stated in your amended Articles of Organization is, "Said Association is organized exclusively for charitable, religious, educational, and scientific purposes, including, for such purposes, the making of distributions to organizations under section 501(c)(3) of the Internal Revenue Code, or corresponding section of any future federal tax code."

Your activities are the operation of a local beauty pageant and the awarding of scholarships based upon how contestants place in the annual pageant. The winner of your pageant attends the [REDACTED] Pageant. Your organization has a franchise agreement with the [REDACTED] Pageant.

You indicate that financial support for your organization is from local contributions, program advertisement sales, and ticket and program sales.

Section 501(c)(3) of the Code provides exemption for:

"Corporations...organized and operated exclusively for religious, charitable,...or educational purposes,...no part of the net earnings of which inures to the benefit of any private shareholder or individual..."

Section 1.501(c)(3)-1 of the regulations provides, in part, as follows:

"(a)(1) 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."

Code	Initiator	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer	Reviewer
		[REDACTED]					
Surname		[REDACTED]					
Date		7/24/87					



"(a)(2) The term "exempt purpose or purposes," as used in this section, means any purpose or purposes specified in section 501(c)(3), as defined and elaborated in paragraph (d) of this section."

"(c)(1) Primary activities. An organization will be regarded as "operated exclusively" for one or more exempt purposes only if it engages primarily in activities which 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."

"(d)(1)(ii) 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."

Section 74 of the Internal Revenue Code states:

"(a) General rule. - Except as provided in subsection (b) and in section 117 (relating to scholarships and fellowship grants), gross income includes amounts received as prizes and awards.

(b) Exception. - Gross income does not include amounts received as prizes and awards made primarily in recognition of religious, charitable, scientific, educational, artistic, literary, or civic achievement, but only if-

- (1) the recipient was selected without any action on his part to enter the contest or proceeding; and
- (2) the recipient is not required to render substantial future services as a condition to receiving the prize or award."

Section 1.117-4 of the Income Tax Regulations states in part as follows: Items not considered as scholarships or fellowship grants...

(c) Amount paid as compensation for services or primarily for the benefit of the grantor (1) Except as provided in paragraph (a) of section 1.117-2 and section 1.117-3, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either

[REDACTED]

compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

In the case of Miss Georgia Scholarship Fund, Inc. v. Commissioner of Internal Revenue Service, 12 T.C.M. (C) 217 (1973), it was held that a scholarship grant is compensatory in nature - payment for the contestant's agreement to perform the requirements of a contestant contract. The primary purpose of the scholarship was compensatory, therefore, the organization did not qualify for exemption under section 501(c)(3) of the Code.

Your activities are not exclusively for purposes specified in section 501(c)(3). Your activity of operating the pageant is not exclusively educational, as the educational part of the pageant is a minor activity - the education of the contestants. Since the number of contestants that are educated is rather small there is also a question whether the educational content of the pageant is for public benefit or private benefit. In regards to the scholarship activity this activity is similar to the activity in the Miss Georgia Scholarship Fund, Inc. case previously cited. We conclude that you are awarding scholarships compensatory in nature, and not in recognition of religious, charitable, scientific, educational, artistic, literary or civic achievement.

Your organization believes there is no contractual agreement and you have stated in your Articles of Organization that, "Recognizing the need to differentiate the Association from other similar pageants that provide educational or other benefits in trade for services performed, said Association expressly agrees to be formed for the purposes shown in the Fourth Article hereof without any requirement of contractual services from those receiving such educational or other benefits as expressed in the Fourth Article." However your organization has a franchise agreement with the [REDACTED] Pageant and that agreement indicates certain contractual agreements by the local pageant on behalf of the local pageant winners:

- (1) The Local Pageant is granted the sole and exclusive right to conduct a Local Pageant within the territory listed for the selection of a candidate to compete in the State Finals of the [REDACTED] Pageant.
- (2) Local Pageant agrees with respect to the Local Finalist to cause her to execute an Application and Rules/Regulation Form with [REDACTED] Pageant.
- (3) A Contestant may not compete in another contest in the same year after having been selected a winner in any Local Pageant.
- (4) To cause all contestants to execute an Application and Rules/Regulation Form; said Contestant's Application shall contain a

provision that the applicant will abide by the rules and regulations established by the Local Pageant, [REDACTED] Pageant and the [REDACTED] Pageant.

It is apparent that your winners have certain contractual agreements in regards to further competition at the State and National level and that those competitions can result in further contractual agreements.

Consequently your organization is not operated exclusively for Internal Revenue Code section 501(c)(3) purposes and you do not qualify for exemption under Code section 501(c)(3).

It appears your organization could qualify for exemption under Code section 501(c)(6) as promoting the common good and general welfare of the community since the pageant promotes your local community.

If you do not agree with these conclusions, you may, within 30 days from the date of this letter, file in duplicate a brief of the facts, law, and argument that clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. The enclosed Publication 892 gives instructions for filing a protest.

If you do not file a protest with this office within 30 days of the date of this report or letter, this proposed determination will become final.

If you do not protest this proposed determination in a timely manner, it will be considered by the Internal Revenue Service as a failure to exhaust available administrative remedies. Section 7428(b)(2) of the Internal Revenue Code provides in part that, "A declaratory judgment or decree under this section shall not be issued in any proceeding unless the Tax Court, the Court of Claims, or the district court of the United States for the District of Columbia determines that the organization involved has exhausted administrative remedies available to it within the Internal Revenue Service."

If this determination letter becomes a final determination, we will notify the appropriate State Officials, as required by section 6104(c) of the Code, that based on the information we have, we are unable to recognize you as an organization of the type described in Code section 501(c)(3).

If you agree with these conclusions or do not wish to file a written protest, please sign and return Form 6018 in the enclosed self-addressed envelope as soon as possible.

[REDACTED]

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

Sincerely,

[REDACTED]
District Director

Enclosures:
Form 6018
Publication 892