

Internal Revenue Service
TE/GE Division
Director, Exempt Organizations

Department of the Treasury
1100 Commerce Street
Dallas, Texas 75242

Person to Contact: [REDACTED]

Contact Telephone Number: [REDACTED]

In Reply, Refer to: [REDACTED]

Date: MAR 16 2000

[REDACTED]
[REDACTED]
[REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from Federal income tax under Section 501(c)(3) of the Internal Revenue Code of 1986.

The information submitted discloses that you were incorporated on [REDACTED] at [REDACTED]. As stated in your organizing document, "The purposes for this corporation shall be:

- (1) For charitable and educational purposes and to provide college scholarships to high school seniors of active [REDACTED].
- (2) To make distributions to organizations that qualify as exempt organizations under Section 501(c)(3) of the Internal Revenue Code or the corresponding provision of any future United States Internal Revenue Laws.
- (3) To do any and all things and exercise any and all powers, rights and privileges for which a corporation may now and hereafter be organized under the [REDACTED] or any act amendatory thereof, supplemental thereto, or substituted therefor..."

We received your Form 1023 Application For Recognition of Exemption on [REDACTED]. The application indicated that your organization's activity would be "to provide scholarships for graduating seniors of [REDACTED]". In the Schedule H, attached to the Form 1023 application it was stated that "Qualifications to be considered are: High school grade point average of C or higher; Have a parent who is or [REDACTED]."

Your response to a request for additional information was received on [REDACTED]. It included the following: "Active parent would include [REDACTED]."

[REDACTED] officer or a committee member of a county [REDACTED] or [REDACTED]."

Examples of questions the Scholarship Committee would ask an applicant during an interview were:

- A. How have your parents [REDACTED]?
- B. Have you been active [REDACTED]? If yes in what way.
- C. What is your favorite subject in high school?
- D. What extracurricular activities have you been involved in?
- E. What course of study do you plan to pursue in college?
- F. Do you have a role model?"

Section 501(c)(3) of the Code provides for exemption from Federal income tax of corporations organized and operated exclusively for religious, charitable, literary, scientific, and educational purposes; no part of the net earnings of which inures to any private shareholder or individual.

Section 1.501(c)(3)-1 of the Income Tax Regulations relates to the definition of the organization and operation of organizations described in Section 501(c)(3). It is quoted, 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."

"(a)(2) The term "exempt purpose or purposes", as used in this section, means any purpose or purposes specified in Section 501(c)(3)...."

"(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."

"(c)(2) Distribution of earnings. 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...."

"(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."

"(d)(2) Charitable defined. The term 'charitable' is used in section 501(c)(3) in its generally accepted legal sense and is, therefore, not to be construed as limited by the separate enumeration in section 501(c)(3) of other tax-exempt purposes, which may fall within the broad outlines of 'charity' as developed by judicial decisions. Such term includes: Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency."

"(d)(3)(i) In General. The term "educational" as used in Section 501(c)(3), relates 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."

Revenue Ruling 66-103, 1966-1 CB 134, (Jan. 01, 1966) held, in part: "An organization which makes unconditional grants to individuals (writers, composers, painters, sculptors, scholars, etc.), who are in need of funds to initiate, develop, or complete creative or scholarly works, or to conduct necessary research for such projects, may qualify for exemption under section 501(c)(3) of the Code, where the purpose of such grants is to assist the recipient to carry on his creative efforts. The fact that the recipient may receive money or other benefits from other sources in addition to the grant or award, as a result of his work does not preclude the grantor organization from qualifying as a charitable organization within the meaning of section 501(c)(3) of the Code."

[REDACTED]

An excerpt from Revenue Ruling 69-257, 1969-1 CB 151, (Jan. 01, 1969) reads as follows:

"Advice has been requested whether a nonprofit organization that awards scholarships to individuals on the basis of scholastic ability rather than financial need qualifies for exemption from Federal income tax under section 501(c)(3) of the Internal Revenue Code of 1954.

The organization was formed and is operated to award scholarships to students for educational studies in institutions of higher learning. The recipients are selected from a broad class of applicants on the basis of scholastic standing only. The organization is supported by grants and contributions.

Section 501(c)(3) of the Code provides for the exemption from Federal income tax of organizations organized and operated exclusively for charitable purposes. Section 1.501(c)(3)-1(d)(2) of the Income Tax Regulations provides that the term "charitable", as used in its generally accepted legal sense, includes the advancement of education.

A trust for educational purposes is charitable although the persons to be educated are not limited to the poor. Therefore, the fact that recipients of the scholarships are selected on the basis of scholastic ability without regard to financial need does not preclude exemption under section 501(c)(3). Where a trust is created for the education of poor children it is charitable not merely as a trust to promote education but also as a trust for the relief of poverty. See Scott on Trusts, Third Edition, paragraph 370 (1967)."

Scholarships have been determined to be an educational activity under 501(c)(3) when the qualifications to receive them are based on either financial need or scholastic merit, as demonstrated in the above excerpts from Revenue Ruling 66-103 and Revenue Ruling 69-257.

In this case, neither financial need nor scholastic merit are primary factors in determining a student's eligibility for a scholarship. In order to receive your scholarship, the primary consideration is [REDACTED]. If the parent cannot demonstrate such activity, then the child cannot receive the scholarship. Also, during the interview by the selection panel, the scholarship candidates are asked about [REDACTED]. Basic requirements that are unrelated to scholastic merit or financial need disqualify a scholarship from exemption under 501(c)(3). Further, the requirement that scholarship candidates have a high school grade point average of C or higher does not present a strong case that scholastic merit is a factor in selection.

Finally, the requirement that at least one of the parents of a scholarship candidate demonstrate activity in [REDACTED] constitutes a private benefit to that party organization, because it results in [REDACTED].

Accordingly, we have concluded that you are not qualified for recognition of exemption from Federal Income Tax under Section 501(c)(3) of the Code, because you are not organized and operated exclusively for charitable, religious, educational or other exempt purposes within the meaning of Section 501(c)(3).

You are required to file Federal income tax return Form 1120.

Contributions made to you are not deductible by the donors as charitable contributions as defined in Section 170(c) of the Code.

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.

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 which clearly sets forth your position. If you desire an oral discussion of the issue, please indicate this in your protest. A conference will be arranged in the Regional Office after we have had an opportunity to consider the brief and it appears that the conclusions reached are still unfavorable to you. Any submission must be signed by one of your principal officers. If the matter is to be handled by a representative, the Conference and Practice Requirements regarding the filing of a power of attorney and evidence of enrollment to practice must be met. We have enclosed Publication 892, Exempt Organization Appeal Procedures for Adverse Determinations, which explains in detail your rights and procedures.

[REDACTED]

If you do not protest this 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".

Please keep this determination letter with your permanent records. If we do not hear from you within 30 days from the date of this letter, this determination will become final. In accordance with Code Section 6104(c), we will notify the appropriate State officials of this action.

Sincerely yours,

Steven T. Miller

Steven T. Miller
Director, Exempt Organizations

Enclosures:
Publication 892
Form 6018
Return Envelope