



TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

NO PROTEST RECEIVED
DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
Request to Manager, EO Determinations - Cincinnati

DATE: 6-3-02

SURNAME [REDACTED]

Date: APR 11 2002

[REDACTED]

Contact Person:

[REDACTED]

Identification Number:

[REDACTED]

Contact Number:

[REDACTED]

INTERNAL REVENUE SERVICE
CINCINNATI, OHIO

OCT 01 2002

RECEIVED
TEGE DIVISION

Employer Identification Number: [REDACTED]

Dear Applicant:

We have considered your application for recognition of exemption from federal income tax under section 501(a) of the Internal Revenue Code as an organization described in section 501(c)(3). Based on the information submitted, we have concluded that you do not qualify for exemption under that section. The basis for our conclusion is set forth below.

You were originally incorporated under the laws of [REDACTED] on [REDACTED]. You subsequently amended your articles of incorporation to provide that "This corporation is organized and operated exclusively for charitable purposes within the meaning of section 501(c)(3) of the Internal Revenue Code. The specific purpose of this corporation is to provide educational scholarships for persons under 18 years of age who graduate from high school and enroll in an institution of higher education."

You initially stated that you would engage in the following activities:

- (1) Raising funds from businesses and individuals to pay for your operations and to establish and grow the scholarship fund. The scholarship fund will be used to award scholarships for higher education. You intend to identify organizations that seek to offer their members scholarships for higher education and work with them to raise money to be designated for scholarship awards for their members. You will work with personnel from these organizations to identify potential contributors. All contributions will be held in trust by you until distributed pursuant to the scholarship award criteria established by each organization or by you. You are in the process of identifying organizations that desire to have scholarship awards programs as a part of their benefits that it provides to its youth members. You indicate that you will also raise funds for scholarships for youth in general that meet your criteria.
- (2) You will also undertake to raise money for scholarship awards which you may award to deserving youth.

- [REDACTED]
- (3) Scholarship awards in all cases are contingent upon the recipient graduating from high school and enrolling in an accredited college or technical education program, and approval of their application for the award which includes a description of their positive characteristics as a young person.

You state that it is your intent to raise funds that may be used to provide scholarship awards to deserving youth who exhibit the characteristics of pride, self discipline, self sacrifice, determination, respect for others, and leadership. It is expected that such youth will be identified through a program of direct application by youth and nomination for an award by an adult.

The scholarship benefit is a gift that may only be used to pay for the cost of attending an accredited college or post-high school technical education program. The availability of scholarship awards will be publicized by membership-based organizations that offer their members scholarship awards, mailings to schools, boys and girls clubs, and other organizations that support youth programs. Awards may range from \$50 to \$1,000 or more depending on the level of donations and earnings of the fund. Recipients will be determined by the organization that raised the scholarship fund in accordance with your criteria. The award will be paid to the accredited educational institution for the direct benefit of the recipient for payment of tuition, books, or other educational expenses.

All persons under the age of 19 are eligible for scholarship awards. There are no restrictions or limitations in the selection procedures based on race, religion, national origin or employment status of the prospective recipient or relative of the prospective recipient. Scholarship awards may be awarded on a contingent basis to any person who is under 19 and still in high school. The awards will be recorded in your records. All scholarship award recipients will be given an identification number by you and will be required to provide other personal identification.

You state that your role is to work with organizations that seek to add your Scholarship Awards Program ("Program") to their activities. You will work directly with such organizations to raise funds, which are deposited with you in the name of the organization, to fund that organization's scholarship awards, with that organization issuing press releases, creating marketing materials, sending out flyers, and holding events to promote that organization and its participation in your Program. You are currently working with [REDACTED] [REDACTED] which has adopted your Awards Program and is seeking to provide scholarship awards to youth who participate in junior golf.

You enclosed [REDACTED]'s current media package, which included program materials, event announcements, press releases, news articles and other materials referencing [REDACTED]'s participation in your Program. This material establishes that [REDACTED] is a membership organization that provides scholarships to its dues-paying members. Membership must be renewed annually. It also reveals that [REDACTED] is not a junior golf tour or a facilities-based program and does not compete with junior golf associations, tournament sponsors, or other golf course facilities. Rather, the [REDACTED] directly supports and complements these vital organizations through a

[REDACTED]

You state that your investment strategy (relating to the funds received for scholarship awards) is very simple and conservative. Funds are invested in a Transamerica Life Insurance Company annuity so that the principal amount of the scholarships is always protected. Your officers and directors will monitor these annuity contracts. Separate annuity contracts will be established for each organization adopting your Program.

The annuity established for [REDACTED], the only organization with whom you are currently working, indicates that you are the policy owner for the benefit of [REDACTED] with [REDACTED], your founder and director, named as annuitant and, with you named as contingent beneficiary.

Our records do not show [REDACTED] to be an organization that has been recognized as exempt from federal income tax under section 501(c)(3) of the Code.

Section 501(c)(3) of the Code provides for the exemption from federal income tax of organizations organized and operated exclusively for charitable 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(d)(1)(ii) of the Income Tax Regulations provides that an organization must serve a public rather than a private interest. It must not be operated for the benefit of private interests such as designated individuals.

Section 1.501(a)-1(c) of the regulations defines "private shareholder or individual" as persons having a personal and private interest in the activities of the organization.

It is well established in the law of charities that scholarships and student loans are a charitable endeavor if they are granted on the basis of need, as in Rev. Rul. 66-103, 1966-1 C.B. 134, or merit, as in Rev. Rul. 69-257, 1969-1 C.B. 151, and are not subordinate of private purposes.

Rev. Rul. 67-367, 1967-2 C.B. 188, provides that a nonprofit organization whose sole activity is the operation of a "scholarship" plan for making payments to pre-selected, specifically named individuals does not qualify for exemption under section 501(c)(3) of the Code. Under these agreements, whereby the organization pays "scholarships" to pre-selected, specifically named individuals designated by subscribers, the organization is serving private interests rather than public charitable and educational interests contemplated under section 501(c)(3) of the Code. Therefore, it does not qualify for exemption from federal income tax under that section. Compare Rev. Rul. 56-403, C.B. 1956-2, 307, which holds that awarding scholarships by a foundation solely to undergraduate members of a designated fraternity will not preclude the foundation from exemption under section 501(c)(3) of the Code.

An organization whose only activity was awarding scholarships to contestants in a beauty pageant did not qualify for exemption under section 501(c)(3) of the Code. Miss Georgia Scholarship Fund, Inc. v. Commissioner, 72 T.C. 267 (1979). All contestants, as a condition of receiving a scholarship, were required to sign a contract that obligated them to abide by pageant rules if selected to participate in the Miss America Pageant. The court concluded that

[REDACTED]

the scholarships did not qualify as scholarship grants under section 117 because they were awarded in consideration of contractual obligations, and the organization did not qualify for exemption under section 501(c)(3) because this was its only activity.

An organization is not operated exclusively for charitable purposes, and thus will not qualify for exemption under section 501(c)(3), if it has a single non-charitable purpose that is substantial in nature. This is true regardless of the number or importance of the organization's charitable purposes. Better Business Bureau v. United States, 326 U.S. 278 (1945); Stevens Bros. Foundation, Inc. v. Commissioner, 324 F.2d 633 (8th Cir. 1963), aff'd, 39 T.C. 93 (1962), cert. denied, 376 U.S. 969 (1964). Operating for the benefit of private parties who are not members of a charitable class constitutes such a substantial nonexempt purpose. Old Dominion Box Co., Inc. v. United States, 477 F.2d 340 (4th Cir. 1973), cert. denied, 413 U.S. 910 (1973).

In order to qualify for exemption under section 501(c)(3) of the Code, you must establish that you are organized and operated exclusively for religious, charitable, or educational purposes and that no part of your net earnings inure to the benefit of a private individual or shareholder.

You have no written agreements or other written guidelines describing your interactions with your donors. There are no flyers, ads, brochures or other media presented to describe your representations to potential donors or the general public. Your sole role is to collect, invest and disburse funds on behalf of [REDACTED] when properly notified. You have failed to establish that your primary activity is an activity described in section 501(c)(3) of the Code.

By allowing your contributors to pre-select the ultimate scholarship recipients, and, by establishing accounts on behalf of the pre-selected recipients, you are conducting your activities in a manner that is indistinguishable from those of the scholarship plan discussed in Rev. Rul. 67-367, supra. [REDACTED] has a membership roster of pre-selected and pre-named members on whose behalf [REDACTED] contributes funds to you for dispersal, providing the potential recipient has entered, and won, another unrelated organization's youth golf event. This membership obligation is analogous to the contractual obligations discussed in Miss Georgia Scholarship Fund, supra. Like the organizations discussed in the court case and in the ruling, respectively, your distribution of funds on behalf of [REDACTED] does not qualify as a scholarship grant under section 117, and you are serving the private interests of [REDACTED] members more than incidentally. Therefore, you do not qualify for exemption under section 501(c)(3) of the Code.

Furthermore, by investing your funds in an annuity in which your founder, president and director, [REDACTED] is annuitant, and [REDACTED], a non-exempt entity, is primary beneficiary, your funds are being used to further private purposes. Such use of your funds is a substantial nonexempt purpose within the meaning of Better Business Bureau, supra. In addition, because your funds inure to the benefit of a private shareholder or individual, [REDACTED], exemption under section 501(c)(3) is precluded.

Accordingly, you do not qualify for exemption as an organization described in section 501(c)(3) of the Code and you must file federal income tax returns.

[REDACTED]

You have the right to protest this ruling if you believe it is incorrect. To protest, you should submit a statement of your views to this office, with a full explanation of your reasoning. This statement, signed by one of your officers, must be submitted within 30 days from the date of this letter. You also have a right to a conference in this office after your statement is submitted. You must request the conference, if you want one, when you file your protest statement. If you are to be represented by someone who is not one of your officers, that person will need to file a proper power of attorney and otherwise qualify under our Conference and Practicing Requirements.

If you do not protest this ruling 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 Code provides, in part, that a declaratory judgement or decree under this section 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 administrative remedies available to it within the Internal Revenue Service.

If we do not hear from you within 30 days, this ruling will become final and a copy will be forwarded to the Ohio Tax Exempt and Government Entities (TE/GE) office. Thereafter, any questions about your federal income tax status should be directed to that office, either by calling 877-829-5500 (a toll free number) or sending correspondence to: Internal Revenue Service, TE/GE Customer Service, P.O. Box 2508, Cincinnati, OH 45201. The appropriate State Officials will be notified of this action in accordance with Code section 6104(c).

When sending additional letters to us with respect to this case, you will expedite their receipt by using the following address:

Internal Revenue Service
[REDACTED]
1111 Constitution Ave, N.W.
Washington, D.C. 20224

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

Sincerely,

(signed) [REDACTED]

[REDACTED]
Manager, Exempt Organizations
Technical Group 3