

A corporation was organized primarily for the purpose of extending loans to needy students of a college to enable them to complete their educational programs. Certain loans are granted on an unsecured basis, while others require a type of security. Both types of loans are made at the same nominal rate of interest which is substantially lower than commercial interest rates, thereby representing a substantial saving to the students. Held, the organization may qualify for exemption from Federal income tax as an organization described in section 501(c)(3) of the Code as one which is organized and operated exclusively for charitable and educational purposes.

Revenue Ruling 61-87, C.B. 1961-1, 191, amplified.

Advice has been requested whether an organization, which is organized and operated for the purpose of making loans to students for educational purposes under the circumstances described herein, may qualify for exemption from Federal income tax under section 501(a) of the Internal Revenue Code of 1954 as a charitable and educational organization of the type described in section 501(c)(3) of the Code.

The organization was incorporated as a nonprofit corporation, under state law, exclusively for charitable and educational purposes. Its primary activity is making loans for educational purposes to needy students of a college. Its charter provides that no part of its net earnings shall inure to the benefit of any private shareholder or individual. In the event of dissolution, its assets are to be distributed for charitable and educational purposes.

Loans are available only to full-time students of the college who are in good standing and need financial assistance. The loans are made at a comparatively low rate of interest and are made on an unsecured basis except as follows:

1. If a student to which a loan is made is a minor, a responsible adult must cosign the note; and
2. A student obtaining a loan of \$500 or more must carry a life insurance policy in an amount sufficient to cover the face amount of the loan and assign the policy to the organization for as long as the principal remains outstanding.

Where life insurance policies are required, the student or his parents pay the premiums and determine which type of insurance to buy, i.e., term or straight life.

Loans from commercial lending agencies in the area are available to students, but only on a secured basis and at commercial or conventional rates of interest, which vary depending

upon the size of the loan. Such a loan would result in a considerably greater expense to the student when compared to his cost of a similar loan from the organization.

The organization's income is derived from contributions and interest on loans. Expenditures are for loans and operating expenses of the loan fund.

Section 501(c) of the Code describes certain organizations which are exempt from income tax under section 501(a) of the Code and reads, in part, as follows:

(3) Corporations, and any community chest, fund, or foundation, 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, no substantial part of the activities of which is carrying on propaganda, or otherwise attempting, to influence legislation, \* \* \*

Revenue Ruling 61-87, C.B. 1961-1, 191, holds that an organization whose primary purpose and activity is to extend unsecured loans to needy students, at a comparatively low rate of interest to enable them to finance their education, is exempt from Federal income tax under section 501(a) of the Code as a charitable and educational organization within the contemplation of section 501(c) (3) of the Code.

This published ruling points out that students usually are not employed and are not considered good credit risks by commercial lending agencies, and that students without substantial collateral find it extremely difficult to obtain loans through regular commercial channels to help finance their education. The ruling further points out that the organization's purpose of aiding students to attain an education is a charitable purpose, and the mere fact that interest is charged on loans is not sufficient, of itself, to deny exemption.

The organization in the instant case is, in effect, organized and operated in essentially the same manner and for the same purposes as the organization held exempt in Revenue Ruling 61-87, and serves an equally charitable purpose in making loans available to students at substantially less than commercial rates. The fact that under certain circumstances security is required before a loan may be granted is not sufficient to destroy the charitable aspect of the organization's purposes and activities.

Accordingly, it is held that the corporation may qualify for exemption from Federal income tax under section 501(a) of the Code as an organization described in section 501(c) (3), since it has been shown that it is organized and operated exclusively for charitable and educational purposes.

An organization may not consider itself exempt from tax

merely because it falls within the scope of Revenue Ruling. In order to establish its status, an organization claiming exemption under section 501(c)(3) of the Code should file its application on Form 1023, Exemption Application, with the District Director of Internal Revenue for the internal revenue district in which is located the principal office of the organization. See section 1.501(a)-1 of the Income Tax Regulations.

Revenue Ruling 61-87, C.B. 1961-1, 191, is hereby amplified.