



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Number: **201634025**
Release Date: 8/19/2016

UIL: 501.03-00
501.03-22

Date:
May 26, 2016
Employer ID number:

Contact person/ID number:

Contact telephone number:

Form you must file:

Tax years:

Dear _____ :

This letter is our final determination that you don't qualify for tax-exempt status under Section 501(c)(3) of the Internal Revenue Code (the Code). Recently, we sent you a proposed adverse determination in response to your application. The proposed adverse determination explained the facts, law, and basis for our conclusion, and it gave you 30 days to file a protest. Because we didn't receive a protest within the required 30 days, the proposed determination is now final.

Because you don't qualify as a tax-exempt organization under Section 501(c)(3) of the Code, donors can't deduct contributions to you under Section 170 of the Code. You must file federal income tax returns for the tax years listed at the top of this letter using the required form (also listed at the top of this letter) within 30 days of this letter unless you request an extension of time to file.

We'll make this final adverse determination letter and the proposed adverse determination letter available for public inspection (as required under Section 6110 of the Code) after deleting certain identifying information. Please read the enclosed Notice 437, *Notice of Intention to Disclose*, and review the two attached letters that show our proposed deletions. If you disagree with our proposed deletions, follow the instructions in the Notice 437 on how to notify us. If you agree with our deletions, you don't need to take any further action.

We'll also notify the appropriate state officials of our determination by sending them a copy of this final letter and the proposed determination letter (under Section 6104(c) of the Code). You should contact your state officials if you have questions about how this determination will affect your state responsibilities and requirements.

If you have questions about this letter, you can contact the person listed at the top of this letter. If you have questions about your federal income tax status and responsibilities, call our customer service number at 1-800-829-1040 (TTY 1-800-829-4933 for deaf or hard of hearing) or customer service for businesses at 1-800-829-4933.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosures:

Notice 437

Redacted Letter 4036, *Proposed Adverse Determination Under IRC Section 501(c)(3)*

Redacted Letter 4038, *Final Adverse Determination Under IRC Section 501(c)(3) - No Protest*



Department of the Treasury
Internal Revenue Service
P.O. Box 2508
Cincinnati, OH 45201

Date: March 29, 2016

Employer ID number:

Contact person/ID number:

Contact telephone number:

Contact fax number:

Legend:

B = State
C = Organization Name
D = Date
E = Foundation Name
F = Scholarship Program
G = Organization Name

v = Number
w dollars = Amount
x dollars = Amount
y dollars = Amount
z dollars = Amount

UIL:

501.03-00
501.03.22

Dear :

We considered your application for recognition of exemption from federal income tax under Section 501(a) of the Internal Revenue Code (the Code). Based on the information provided, we determined that you don't qualify for exemption under Section 501(c)(3) of the Code. This letter explains the basis for our conclusion. Please keep it for your records.

Issues

Do you qualify for exemption under Section 501(c)(3) of the Code? No, for the reasons stated below.

Facts

You were incorporated on D in the state of B. Your Articles of Incorporation indicate your purpose is to establish, maintain and award scholarships to B students in order to pursue post-secondary study including, but not limited to, trade and technical, undergraduate, graduate and professional education. Your Form 1023 indicates you were formed to fund scholarships for the young women who compete and earn scholarship assistance in F, the official state entity for C, which is exempt under Section 501(c)(4). C's primary activity is operating a beauty pageant. F operates the pageant for Miss B.

You are affiliated with G and E which are both affiliated with C and F; in addition, E is the state organization that offers a scholarship package to the winner of the Miss B pageant and is also exempt under Section 501(c)(4). You were established because a separate scholarship fund was seen as a simpler and a more productive way to raise scholarship money for contestants in the pageant since your sole purpose is to solicit and fund academic scholarships for participants in these pageants. You wrote that tax exempt status will open the door widely for the solicitation of funds

Prior to competing in the pageant for Miss B, each contestant must sign a contract common to all pageants affiliated with C.

The contract states:

- Contestants must agree to raise a minimum amount of funds for a specific charity and for C's scholarship fund as well as participate in the series of events and appearances leading up to the final selection of Miss B.
- Contestants will be bound by the rules and regulations governing C and the procedures for the awarding and supervision of all scholarships.
- If she is selected as the winner of the competition, she will serve as Miss B during the Year of Service and until her successor is selected or appointed.
- As winner she will dedicate her entire time, efforts and energy during the Year of Service to the fulfillment of these duties and obligations, and that she will engage in no other business or other activities that will in any way interfere with the duties and obligations of her Year of Service.
- The winner's participation in the competition shall include all public appearances required by G including, but not limited to, television and radio broadcasts, personal appearances, interviews, still photo sessions, and video and audio taping or filming of all or any part of the events associated with the competition.
- For the runner up she agrees to remain available to assume all of the rights, obligations and commitments of the Year of Service.
- The competition is critically important and the single most widely recognized element of the program.

By signing the contract, contestants understand and acknowledge:

- Scholarships granted are subject to the terms and conditions of the Scholarship Rules and Regulations provided by F.
- They agree to be bound by those rules and regulations.
- All scholarships that may be awarded will be non-forfeitable in the event that there is a breach of the contract or fail to perform any duties as Contestants.
- Scholarships may be forfeited if there are any misrepresentations as to their eligibility to compete.

The contract also indicates that the winner authorizes G and anyone duly licensed or authorized by G to:

- (1) Televising, photographing, broadcasting and/or making radio, television, video and audio tapes or motion picture recordings of her individually or in a group;
- (2) Use or re-use such photographs, recordings, video tapes, audio tapes and/or motion picture films in all media throughout the world in perpetuity; and

- (3) Use her name, likeness and/or physical depiction for any purpose in perpetuity, in an unedited or edited manner or fashion as G, in its sole discretion, shall determine. This authorization shall also include the use of all such photographs, recordings, videotapes, audiotapes and/or motion picture films made during her Year of Service.

The contract calls the winner an independent contractor with respect to C and that she is not and will not become an employee of C during her Year of Service.

Your Schedule H states the following:

- There is no application process for scholarships payable to contestants in F who will alert you of eligible recipients, including the level of scholarship earned. Upon proof of tuition due, your treasurer will make payment as directed.
- Scholarships payable to participants are payable without consideration of academic performance. If they are earned and a participant is enrolled in school and has educational related expenses due, it will be paid up to the amount of the scholarship earned. Scholarships payable to other individuals will be based on the letter of application demonstrating an educational plan, need and achievements to date and verification by you.
- You are unlikely to have very large sums of money to award, perhaps no more than w dollars per year anytime within the near future. Up to as much as x dollars of this sum (over 80%) will be set aside for participants in the beauty pageant. The goal is to award as many other scholarships as possible. The current maximum for other scholarships is z dollars per person. If exemption is granted, the chances are very good that more funds will be received and the number of all scholarships can be increased.

For the current year, E intends to award about v scholarships consisting of a scholarship package of y dollars, which is allocated among the winner of the pageant and the first through fourth runners-up. Also as a part of that package there are other smaller scholarships available to contestants such as most talented non-finalist and a community service scholarship. Your goal is to enrich the lives and potential grant of scholarships to as many participants as possible.

You also wrote that when sufficient money has been accumulated, you may fund scholarships of at least z dollars each for both men and women. These will be awarded based on demonstrated need and academic achievement. Moreover you will give special consideration to older students returning to school and those entering into trade and technical programs.

Finally, you stated that there is a relationship between you and E, but each is a separate entity with an independent board of directors and officers so as to avoid any conflict of interest.

Law

Section 501(c)(3) of the Code provides for exemption from federal income tax of organizations organized and operated exclusively for educational or 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(a)(1) of the Income Tax Regulations states that in order to qualify under section 501(c)(3) of the Code, 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 or operational test, it is not exempt.

Section 1.501(c)(3)-1(c)(1) of the Income Tax Regulations states that 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 such exempt purposes specified in section 501(c)(3) of the Code. An organization will not be so regarded if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.

Section 1.501(c)(3)-1(d)(1)(ii) of the Income Tax Regulations states that an organization is not operated exclusively for one or more exempt purposes unless it serves a public rather than a private interest. It must not be operated for the benefit of designated individuals or the persons who created it.

In *Bingler v. Johnson*, 394 U.S. 741 (1969), the court considered whether educational stipends paid by Westinghouse Electric Corp., to its employees were "scholarships" excludable from gross income. The court held the stipends were compensation, not scholarships excludable from income, because they required employees to submit progress reports while on educational leave of absence and return to Westinghouse's employ for a substantial period of time after completing the leave. The Court explained that under I.R.C. 117 scholarship grants must be "relatively disinterested, 'no strings' educational grants, with no requirements of any substantial quid pro quo from the recipients."

In *Miss Georgia Scholarship Fund, Inc. v. Commissioner*, 72 TC 267 (1979), the Tax Court held that a separate fund created by the Miss Georgia Pageant solely to award scholarships to the pageant's contestants, did not qualify under Section 501(c)(3) of the Code because the scholarships were awarded in consideration of contractual obligations. The contract required contestants to participate in the Miss Georgia Pageant and appear in public as directed by pageant officials. A winning contestant who failed to honor the contract forfeited all rights to her "scholarship." The Tax Court concluded that the "scholarships" were compensation for signing the pageant contract and for performing services under it. Therefore, these awards were not Section 117 scholarships and the fund was not operated exclusively for Section 501(c)(3) purposes.

Application of Law

You are not as described in section 501(c)(3) of the Code because you are not exclusively organized and operated for charitable or educational purposes.

You have not established you meet the operational test as per Section 1.501(c)(3)-1(a)(1) of the Regulations because you are operating for substantial non-exempt private purposes in contravention to Section 1.501(c)(3)-1(c)(1) of the regulations. The information you provided shows you are operating for substantial private purposes as indicated by the following:

- You are operating for the private purpose of benefiting E, which is exempt under Section 501(c)(4) and has been providing scholarships to contestants in the beauty pageant. For example, you were established because you believe a separate scholarship fund was seen as a simpler and a more productive way to raise scholarship money for contestants in the pageant.
- You are operating for the private purpose of benefiting the contestants in the pageant because many contestants receive a scholarship for signing the contract to participate in the pageant. For instance, you stated it is your goal to maximize the number of scholarships awarded to as many participants as possible.

You are not described in Section 1.501(c)(3)-1(d)(1)(ii) of the Regulations. You are serving the private interests of the contestants by providing many of them at least a nominal scholarship as compensation for signing the contract to participate in the pageant. Furthermore, you are taking over the same scholarship

program currently conducted by E using the same criteria, rules and contract. Your activities do not differ significantly from E's. Therefore, you are operating for private interests of E.

Your scholarship program has characteristics like that described in Bingler v. Johnson, 394 U.S. 741 (1969) because it serves as compensation to the contestants since they are required to sign an extensive contract. Even though you state your scholarships are non-forfeitable, the fact is all participants must sign the contract to compete in the pageant which indicates a quid pro quo relationship. Like the organization in the court case, there are strings attached which disqualifies your program from exemption.

Your scholarship program is also similar to that found in Miss Georgia Scholarship Fund, Inc. v. Commissioner because your "scholarships" to contestants in the pageant serve as compensation. For example, you were created to solely award scholarships to contestants in F's beauty pageant. As an eligibility requirement to compete in the pageant, all contestants must agree to the terms of the contract before participating in the beauty pageant. There is no application for the scholarship program and scholarships are payable without consideration of academic performance. The winner is also referred to as an independent contractor and must fulfill numerous obligations directed by the contract. Therefore, these awards are not section 117 scholarships and you are not operating exclusively for section 501(c)(3) purposes.

Conclusion

Based on the above facts and analysis you do not qualify for exemption under Section 501(c)(3) of the Code because you are not operated exclusively for an exempt purposes as required by Sections 1.501(c)(3)-1(a)(1) and 1.501(c)(3)-1(c)(1) of the Income Tax Regulations. You are operating for the benefit of E as well as for the participants in your beauty pageant. Although the scholarships are non-forfeitable, they are considered compensation because participants must agree to the terms in the contract before competing in the pageant. Accordingly we conclude you do not qualify for exemption under Section 501(c)(3).

If you don't agree

You have a right to file a protest if you don't agree with our proposed adverse determination. To do so, you must send a statement to us within 30 days of the date of this letter. The statement must include:

- Your name, address, employer identification number (EIN), and a daytime phone number
- A copy of this letter highlighting the findings you disagree with
- An explanation of why you disagree, including any supporting documents
- The law or authority, if any, you are relying on
- The signature of an officer, director, trustee, or other official who is authorized to sign for the organization, or your authorized representative
- One of the following declarations:

For an officer, director, trustee, or other official who is authorized to sign for the organization:

Under penalties of perjury, I declare that I examined this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

For authorized representatives:

Under penalties of perjury, I declare that I prepared this protest statement, including accompanying documents, and to the best of my knowledge and belief, the statement contains all relevant facts and such facts are true, correct, and complete.

Your representative (attorney, certified public accountant, or other individual enrolled to practice before the IRS) must file a Form 2848, *Power of Attorney and Declaration of Representative*, with us if he or she hasn't already done so. You can find more information about representation in Publication 947, *Practice Before the IRS and Power of Attorney*.

We'll review your protest statement and decide if you provided a basis for us to reconsider our determination. If so, we'll continue to process your case considering the information you provided. If you haven't provided a basis for reconsideration, we'll forward your case to the Office of Appeals and notify you. You can find more information about the role of the Appeals Office in Publication 892, *How to Appeal an IRS Decision on Tax-Exempt Status*.

If you don't file a protest within 30 days, you can't seek a declaratory judgment in court at a later date because the law requires that you use the IRS administrative process first (Section 7428(b)(2) of the Code).

Where to send your protest

Please send your protest statement, Form 2848, if needed, and any supporting documents to the applicable address:

U.S. mail:

Internal Revenue Service
EO Determinations Quality Assurance
Room 7-008
P.O. Box 2508
Cincinnati, OH 45201

Street address for delivery service:

Internal Revenue Service
EO Determinations Quality Assurance
550 Main Street, Room 7-008
Cincinnati, OH 45202

You can also fax your statement and supporting documents to the fax number listed at the top of this letter. If you fax your statement, please contact the person listed at the top of this letter to confirm that he or she received it.

If you agree

If you agree with our proposed adverse determination, you don't need to do anything. If we don't hear from you within 30 days, we'll issue a final adverse determination letter. That letter will provide information on your income tax filing requirements.

You can find all forms and publications mentioned in this letter on our website at www.irs.gov/formspubs. If you have questions, you can contact the person listed at the top of this letter.

We sent a copy of this letter to your representative as indicated in your power of attorney.

Sincerely,

Jeffrey I. Cooper
Director, Exempt Organizations
Rulings and Agreements

Enclosure:
Publication 892

cc: POA Name