It has been brought to our attention over the past few months that there are some rumors going around concerning tax-exempt nonprofit organizations that use scrip fundraising. Specifically those that share a portion of the rebates with their families for tuition, band camps, and the like, being contacted by the IRS and told they cannot do that. We know that you want to run your program properly, and **we want to reassure you that crediting your members' scrip rebates toward their tuition or other fees has been reviewed and approved by the IRS, *if you have structured your program correctly.***

We believe many of the rumors are caused by a 2013 court case which resulted in an organization losing its tax-exempt status because it did not follow all of the rules regarding its fundraising methods. To our knowledge, we are unaware of any case where a scrip program was the reason an organization lost its tax-exempt status. To ensure you have set up your scrip program properly to give tuition credit, or help fund other fees associated with your organization, there are a few things you need to know. We have done extensive research and work in this area, and have secured a Private Letter Ruling from the IRS on the topic. We've included an easy to understand version of the findings, and feel free to share it with others as well.

As always, we are here for you. You, someone else in your organization, or your own local tax professional may have more questions after reviewing the document, so we encourage you to reach out to us via email, at taxquestions@glscrip.com, or call us at 1-800-727-4715 option 3, and we'll get your questions answered quickly.

Thank you for your commitment to your scrip program!

Dan Springer
President

If Properly Structured, You Can Share the Proceeds From Scrip Fundraising

May 15, 2014

Introduction

It has been brought to our attention that there is a lot of misinformation about tax-exempt non-profit organizations being contacted by the IRS about their fundraising activities; especially when they share a portion of the proceeds with their participating families. So we thought we'd summarize all we've learned about the subject for scrip fundraising to help clear the air, and help set the record straight. We are confident that all organizations want to run their fundraising programs in compliance. We are providing this short paper to explain what we have learned in this area, and what you need to consider to properly share proceeds from a scrip program directly with families.

Please note: We're not CPAs or Tax Attorneys (check out the full disclaimer at the end). We've worked with some of the best in the business however, and from that we are confident in our thoughts expressed here. We always suggest that you consult with your own tax professionals to add to your understanding, and discuss your specific program details. Please feel free to share this paper with them as well so that they can provide you the best advice possible.

So what's the Big Deal?

First and foremost, fundraising is an important activity for most non-profit organizations. It is typically vital to the ongoing operation and financial health of a school, marching band, hockey team, and countless other similar organizations. So you want to make sure you are following all the rules and regulations.

Second, if you provide something called *inurement* or *private benefit*, the rules say that your 501(c)(3) status may be revoked. That's a VERY big deal, and you don't want to go there. Great news – it's not difficult to follow the rules to prevent that from happening.

Some Background and Some New Words

Let's start with an example; if a scrip program at St. Mary's School shares half the money generated in scrip fundraising with participating families (what we call a 50/50 program), and the Jones family buys $10,000 worth of scrip, while the Smith family buys $5,000, the Jones family will benefit twice as much as the Smith family. Then there's the Davis family that didn't participate, and will receive no direct benefit like the Smith and Jones families.

The first concern around sharing some of the money this way is whether or not that practice might cause a problem with inurement or private benefit with the IRS. This means that no part of the earnings of a section 501(c)(3) organization may inure to the benefit of private persons that are "insiders" who have an opportunity to control or influence the activities of the organization. It also means that the organization must be operated for public purposes rather than to serve the interests of any private individuals, regardless of whether they are insiders.

The second concern was around the idea of the Jones family or the Smith family having to pay tax on their share of the funds. Is this income to the family? Does St. Mary's need to issue a **Form 1099** to them? 1099s are tax forms issued to report non-wage income to individuals that generally isn't subject to income tax withholding.

In **2009**, we decided to enlist the help of one of the nation's largest accounting firms to address these questions. They assisted us in requesting a **Private Letter Ruling** (PLR) from the IRS on the topic of scrip fundraising. A PLR is defined on the IRS web site as "…*a written statement issued to a taxpayer that interprets and applies tax laws to the taxpayer's represented set of facts*." Several months later the IRS issued PLR 200945022 (a copy is attached) which answers key questions regarding scrip fundraising. More about this below.

Why is PLR 200945022 Helpful?

PLR 200945022 clearly established that the proceeds from a scrip program such as the Great Lakes Scrip Center program are **rebates**, which has a very special meaning for tax purposes. Rebates are a reduction of purchase price rather than income. If a portion of a rebate through scrip fundraising is shared with a participating family for a purchase they made, it's not income to them, and therefore no 1099 is needed. It's exactly the same as a family that purchases a car and receives a rebate from the dealer or manufacturer; it is not taxable income because the rebate is a reduction of purchase price. PLR 200945022 and some other rulings demonstrate that 1099's are not necessary in scrip programs that share rebates, and in the example above, St. Mary's would not have to issue a 1099 to the Jones family or the Smith family. Although a private letter ruling is binding only on the IRS with respect to the taxpayer that received the ruling, it is instructive of the position the IRS has taken on these issues.

One more note - In **2013** the US Tax Court revoked the 501(c)(3) status of an organization called Capital Gymnastics Booster Club in Virginia. One of the forms of fundraising that the organization did was scrip fundraising. This has caused some unfortunate and unnecessary concern among our customers. The Tax Court's decision was not related specifically to their scrip fundraising activities, but rather to the fact that the organization existed solely for the purpose of fundraising, and its overall fundraising methods did not comply with the tax rules. <u>While scrip was mentioned in the case, it was not the cause of their losing tax-exempt status</u>.

But What About the Consequences to Our Organization?

PLR 200945022 answered questions regarding the tax treatment to the participating families in a scrip fundraising program. Although the Capital Gymnastics Booster Club case resulted in the organization's exempt status being revoked due to inurement and private benefit, there are major differences between the circumstances in that case and those involving a Great Lakes Scrip Center fundraising program. Most importantly, the funds being shared with families in that case belonged to the organization, not to the families. In a Great Lakes Scrip Center fundraising program, the funds belong to the family, and they are free to choose whether to keep the rebate, donate it to the charity, or have it applied for tuition or other benefits, without it causing inurement or private benefit because the shared amounts do not belong to the organization.

Does This PLR Apply to Other Types of Fundraising?

No, this PLR is extremely narrow. It applies only to a scrip fundraising program involving rebates which may be used at the discretion of the participating family. You HAVE to structure your program with agreements with the participating families consistent with the structure of the PLR if you want to share a portion of the rebate with them and fit within the rules.

This makes scrip fundraising unique as a fundraising program. Most other types of fundraisers involve selling a product to your family members, or friends, that generate earnings from those activities that are NOT rebates. PLR 200945022 does not address that type of activity. Those fundraisers work fine for raising money for the general fund, but if you share a portion of the money raised with the people selling them, you expose your organization, and the participating families, to possible tax issues that do not apply to a properly structured scrip fundraising program.

So, What Do I Need to Do?

First, call or email us if you have questions, or just want to talk through this some more. Remember – we're not CPAs or Tax Attorneys, and although we can discuss these issues with you, we are not your tax advisors. Send emails to taxquestions@glscrip.com, and ask any questions you have. We'll answer them if we can, or try to point you in the right direction if we can't. If you'd like to talk on the phone, mention in your email what the best days/times to reach you are, and what number to use. You can also call our Customer Service team at 800-727-4715 option 3, and they will direct you to the right extension. Feel free to pass on the contact information to anyone in your organization that may be interested in this topic, and to your local tax professionals if they have any questions. We'd be delighted to speak to them as well. We would like to be a resource to help you get comfortable that your program satisfies all of the rules.

Second, *and this is the important one*, <u>if you share a portion or all of the rebates, you must have agreements with your families, and they must include the option for the families to receive their portion of the rebate back in cash, if you are sharing some of the rebate</u>. This cash option establishes that portion of the rebate that belongs to the family, not the organization, and is necessary to make sure the program fits within the rules that protect your organization's exempt status. You can and should include in the agreement any other aspects of your program that they should be aware of and agree to, such as your policy on returned payments, what you do with accrued rebates if they leave the school, etc. We have a sample agreement you can start with on our web site.

We know, from lots of conversations with other programs, that the idea of giving families cash back may rub you the wrong way. You are running the program to help them with tuition, or trip expenses, or other things associated with your group, not to put money in their pocket. It has been our experience, and we hear all the time, that you can expect none or very few of the participants to choose the cash back option. Why would they? They owe your group for some expenses and the scrip program helps them with those. You should also think about this; if your program splits the rebates with families, even when you write them a check, your group still collected as much money on their sales as anyone else's!

Internal Revenue Service

Number: **200945022**
Release Date: 11/6/2009

Index Number: 170.00-00

Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable
Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:ITA:B02
PLR-118535-09
Date:
July 29, 2009

In re:

LEGEND:

Taxpayer =

Dear :

This responds to your letter dated April 3, 2009, in which you request rulings related to §§ 61 and 170 of the Internal Revenue Code.

RULINGS REQUESTED

The following rulings are requested:

(1) The portion of the purchase price Taxpayer pays a charity for scrip that Taxpayer can either receive back in cash or allow the charity to retain ("rebate") does not constitute gross income under § 61;

(2) The amount of the rebate that Taxpayer elects not to receive in cash and allows a charity to retain is a charitable contribution deductible under § 170.

FACTS

Taxpayer is an individual who purchases scrip from an organization described in § 170(c) ("charity"). The charity purchases the scrip at a discount but sells the scrip at face value to individuals such as Taxpayer. Thus, for scrip with a face value of $ that the charity purchases at a % discount, Taxpayer pays the charity $, and the charity's cost for the scrip is $.

As part of Taxpayer's purchase of scrip, the charity gives Taxpayer the option of receiving in cash a portion of the difference between the face value of the scrip and the charity's cost for the scrip ($X[1]). That is, at the time of purchase, the charity provides Taxpayer two options: (1) Taxpayer may elect to receive $X in cash, or (2) Taxpayer may elect to allow the charity to retain $X.

Taxpayer's proposed transaction:

Taxpayer plans to purchase scrip at face value from the charity. At the time of Taxpayer's purchase, Taxpayer will elect not to receive $X in cash in favor of allowing the charity to retain $X.

LAW AND ANALYSIS

Section 61 provides that gross income means all income from whatever source derived. A rebate received by a buyer from the party to whom the buyer directly or indirectly paid the purchase price for an item is an adjustment in purchase price, not an accession to wealth, and is not includible in the buyer's gross income. See Rev. Rul. 76-96, 1976-1 C.B. 23, as modified by Rev. Rul. 2005-28, 2005-1 C.B. 997.

A deduction for contributions and gifts to or for the use of organizations described in § 170(c) will be allowed to the extent payment of the charitable contribution is made within the taxable year. Sec. 170(a). A charitable contribution must be made voluntarily and with donative intent. U.S. v. American Bar Endowment, 477 U.S. 105 (1986).

Deductions for charitable contributions are limited to a percentage of the taxpayer's contribution base for the taxable year. See § 170(b). No deduction is allowed under § 170(a) unless the donor properly substantiates the contribution as required under §§ 170(f)(8) (relating to contributions of $250 or more) and (f)(17) (relating to all contributions of a cash, check, or other monetary gift, regardless of amount), as applicable.

Ruling request (1)—Rebate from charity:

Taxpayer first asks us to rule that, if a charity gives Taxpayer the option to receive a cash rebate of $X of the purchase price Taxpayer pays the charity for scrip, Taxpayer will not be in receipt of gross income under § 61.

A rebate received from the party to whom the buyer directly or indirectly paid the purchase price for an item is an adjustment to the purchase price paid for the item. It is

[1] Where the face value of the scrip is $ and the charity's cost for the scrip is $, $X is an amount less than $ (i.e., the difference between the face value and cost of the scrip, with such difference reduced by the charity's additional cost to provide Taxpayer with the option of receiving an amount in cash).

not an accession to wealth and is not includible in the buyer's gross income. See Rev. Rul. 76-96, 1976-1 C.B. 23, as modified by Rev. Rul. 2005-28, 2005-1 C.B. 997.

In this case, Taxpayer purchases scrip from the charity and has the option to receive a cash rebate of $X. In lieu of receiving cash, Taxpayer may allow the charity to retain the $X rebate. In either case, this rebate constitutes an adjustment to the purchase price of the scrip and, consequently, is not includible in Taxpayer's gross income.

Ruling request (2)—Contribution of rebate:

Taxpayer also asks us to rule that, if Taxpayer elects to allow the charity to retain the $X Taxpayer could have received in cash, $X will be a charitable contribution under § 170.

Taxpayer in this case may elect to receive a rebate in cash or to allow the charity to retain the rebate. This program, therefore, is distinguishable from the program in American Bar Endowment. The opportunity for Taxpayer to elect whether rebates will be retained by the charity or received in cash by Taxpayer renders the payments in this situation voluntary.

Accordingly, if Taxpayer chooses the option of allowing the charity to retain the $X and complies with all other requirements under § 170, then Taxpayer is treated as making a charitable contribution in the amount of $X in the taxable year Taxpayer otherwise would have received the $X in cash.

CONCLUSIONS

(1) The portion of the purchase price Taxpayer pays a charity for scrip that Taxpayer can either receive back in cash or allow the charity to retain does not constitute gross income under § 61.

(2) The amount of the rebate that Taxpayer can receive in cash but instead allows the charity to retain constitutes a charitable contribution at the time Taxpayer could have received the amount in cash, to the extent provided in § 170.

The charitable contributions that are the subject of this ruling request will be deductible only if all other requirements under § 170 (including substantiation requirements under §§ 170(f)(8) and (f)(17)) are met, subject to the percentage limitations of § 170(b).

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in

this letter. In addition, no opinion is expressed or implied on whether any aspect of the transaction or item discussed or referenced in this letter may impact the charity's tax exempt status under section 501(c)(3) or results in unrelated business income tax under section 511.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

John P. Moriarty
Chief, Branch 1
Office of Chief Counsel
(Income Tax & Accounting)

cc: