

## ***Nellie Callahan Scholarship Fund v. Commissioner, 73 T. C. 643 (1979)***

A scholarship fund can qualify as a supporting organization under section 509(a)(3) even if it does not make direct payments to the supported organization, as long as it benefits the charitable class supported by that organization.

### **Summary**

The Nellie Callahan Scholarship Fund sought a declaratory judgment to be classified as a supporting organization rather than a private foundation. The fund, established under the will of Nellie Callahan, provided scholarships to graduates of Winterset Community High School. The court ruled that the fund qualified as a supporting organization under section 509(a)(3) because it was operated in connection with the Winterset Community School District, satisfying both the responsiveness and integral part tests. The decision hinged on the fund's payments benefiting the school's charitable class and the school's attentiveness to the fund's operations.

### **Facts**

Nellie Callahan's will established the Nellie Callahan Scholarship Fund as a testamentary trust in 1967. The fund was managed by trustees and provided scholarships to graduates of Winterset Community High School based on academic qualifications and financial need. The school's officials selected the recipients, but the trustees controlled the fund's investments and operations. In 1976, three school officials were appointed as additional trustees, though the fund did not formally notify the IRS of any intent to terminate its private foundation status.

### **Procedural History**

The fund applied for recognition of exemption in 1976, and the IRS classified it as a private foundation. After exhausting administrative remedies, the fund petitioned the Tax Court for a declaratory judgment that it was a supporting organization under section 509(a)(3). The case was submitted based on pleadings, oral arguments, and stipulated administrative records.

### **Issue(s)**

1. Whether the Nellie Callahan Scholarship Fund meets the requirements of section 509(a)(3) to be classified as a supporting organization rather than a private foundation.

### **Holding**

1. Yes, because the fund was operated in connection with the Winterset Community School District, satisfying both the responsiveness test and the integral part test under section 1. 509(a)-4, Income Tax Regs.

## **Court's Reasoning**

The court applied the requirements of section 509(a)(3) and the relevant Treasury regulations to determine if the fund qualified as a supporting organization. It focused on the relationship between the fund and the Winterset Community School District, analyzing whether the fund met the responsiveness and integral part tests. The court found that the fund satisfied the responsiveness test because it was a charitable trust under Iowa law, and the school district was effectively the named beneficiary since the fund's scholarships benefited the school's graduates. The integral part test was met because the fund's payments constituted a significant part of the school's support for its guidance counseling function. The court emphasized that the fund's activities were integral to the school's operations, ensuring the school's attentiveness to the fund. The court noted that prior cases and revenue rulings supported the conclusion that indirect support through scholarships to students could satisfy the operational test.

## **Practical Implications**

This decision clarifies that scholarship funds can qualify as supporting organizations without making direct payments to the supported organization if they benefit the supported organization's charitable class. Legal practitioners should consider the indirect benefits of scholarship programs when advising clients on potential supporting organization status. The ruling also highlights the importance of demonstrating a close relationship and attentiveness between the supporting and supported organizations. This case may influence how other scholarship funds structure their operations to avoid private foundation status and its associated regulations. Subsequent cases and IRS guidance should continue to refine the application of the responsiveness and integral part tests in similar contexts.