

study or research. The term includes the value of contributed services and accommodations (see paragraph (d) of this section) and the amount of tuition, matriculation, and other fees which are furnished or remitted to an individual to aid him in the pursuit of study or research. The term also includes any amount received in the nature of a family allowance as a part of a fellowship grant. However, the term does not include any amount provided by an individual to aid a relative, friend, or other individual in the pursuit of study or research where the grantor is motivated by family or philanthropic considerations.

(d) *Contributed services and accommodations.* The term “contributed services and accommodations” means such services and accommodations as room, board, laundry service, and similar services or accommodations which are received by an individual as a part of a scholarship grant or fellowship grant.

(e) *Candidate for a degree.* The term “candidate for a degree” means an individual, whether an undergraduate or a graduate, who is pursuing studies or conducting research to meet the requirements for an academic or professional degree conferred by colleges or universities. It is not essential that such study or research be pursued or conducted at an educational institution which confers such degrees if the purpose thereof is to meet the requirements for a degree of a college or university which does confer such degrees. A student who receives a scholarship for study at a secondary school or other educational institution is considered to be a “candidate for a degree.”

[T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, as amended by T.D. 8032, 50 FR 27232, July 2, 1985]

§ 1.117-4 Items not considered as scholarships or fellowship grants.

The following payments or allowances shall not be considered to be amounts received as a scholarship or a fellowship grant for the purpose of section 117:

(a) *Educational and training allowances to veterans.* Educational and training allowances to a veteran pursuant to section 400 of the Servicemen's Readjustment Act of 1944 (58 Stat. 287)

or pursuant to 38 U.S.C. 1631 (formerly section 231 of the Veterans' Readjustment Assistance Act of 1952).

(b) *Allowances to members of the Armed Forces of the United States.* Tuition and subsistence allowances to members of the Armed Forces of the United States who are students at an educational institution operated by the United States or approved by the United States for their education and training, such as the United States Naval Academy and the United States Military Academy.

(c) *Amounts paid as compensation for services or primarily for the benefit of the grantor.* (1) Except as provided in paragraph (a) of §§ 1.117-2 and 1.117-5, any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research, if such amount represents either compensation for past, present, or future employment services or represents payment for services which are subject to the direction or supervision of the grantor.

(2) Any amount paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research primarily for the benefit of the grantor.

However, amounts paid or allowed to, or on behalf of, an individual to enable him to pursue studies or research are considered to be amounts received as a scholarship or fellowship grant for the purpose of section 117 if the primary purpose of the studies or research is to further the education and training of the recipient in his individual capacity and the amount provided by the grantor for such purpose does not represent compensation or payment for the services described in subparagraph (1) of this paragraph. Neither the fact that the recipient is required to furnish reports of his progress to the grantor, nor the fact that the results of his studies or research may be of some incidental benefits to the grantor shall, of itself, be considered to destroy the essential character of such amount as a scholarship or fellowship grant.

[T.D. 6500, 25 FR 11402, Nov. 26, 1960; 25 FR 14021, Dec. 21, 1960, as amended by T.D. 8032, 50 FR 27232, July 2, 1985]

§ 1.117-5 Federal grants requiring future service as a Federal employee.

(a) *In general.* Under section 117(c), amounts received by an individual

under a Federal program as a scholarship or grant for qualified tuition and expenses at an institution of higher education are excluded from the gross income of the recipient even though the recipient is required to perform future service as a Federal employee. See paragraph (c) of this section for the definitions of the terms “qualified tuition and expenses” and “institution of higher education.”

(b) *Exception for uniformed services scholarship programs.* The requirements of this section do not apply to amounts received before 1985 by a member of a uniformed service who entered training before 1981 under the Armed Forces Health Professions Scholarship Program, National Public Health Service Corps Scholarship Training Program, or other substantially similar Federal programs requiring the recipient to work for a uniformed Federal service after completion of studies. These awards are governed by section 4 of Pub. L. 93-483 as amended by Pub. L. 95-171, Pub. L. 95-600 and Pub. L. 96-167. See section 101(3) of title 37, United States Code for the definition of the term “uniformed service.”

(c) *Definitions—(1) Qualified tuition and related expenses.* For purposes of section 117(c) and this section, qualified tuition and related expenses are those amounts which under the terms of the Federal program are required to be used and in fact are used for payment of:

(i) Tuition and fees that are required for the recipient’s enrollment or attendance at an institution of higher education; and

(ii) Those amounts used for payment of fees, books, supplies and equipment required for courses of instruction at such an institution.

Incidental expenses are not considered related expenses and thus are not excludable from gross income under section 117(c). Incidental expenses include room and board at an institution of higher education, expenses for travel (including expenses for meals and lodging incurred during travel and allowances for travel of the recipient’s family), research, clerical help, equipment and other expenses which are not required for enrollment at the institu-

tion or in a course of instruction at such institution.

(2) *Institution of higher education.* To qualify as an institution of higher education under this section, the institution must be a public or other non-profit institution in any state which—

(i) Admits as regular students only individuals who have a certificate of graduation from a high school or the recognized equivalent of such a certificate;

(ii) Is legally authorized within the state to provide a program of education beyond high school; and

(iii) Provides an education program for which it awards a bachelor’s or higher degree or which is acceptable for full credit towards such a degree, or which trains and prepares students for gainful employment in a recognized health profession. For purposes of this section, recognized health professions are those health professions which are supervised or monitored by appropriate state or Federal agencies or governing professional associations and which require members to be currently licensed or certified in order to practice.

(3) *Service as a Federal employee—(i) In general.* Except as otherwise provided in paragraph (c)(3)(ii) of this section, service as a Federal employee refers to employment of the recipient by the Federal government to work directly for the Federal government. Thus, Federal grants or scholarships which do not require the recipient to work directly for the Federal government are not governed by the rules of this section.

(ii) *Service in a health manpower shortage area.* For purposes of this section an obligation under a grant for the recipient to serve in a health related field in a health manpower shortage area as designated by the Secretary of Health and Human Services according to the criteria of the Public Health Services Act (42 U.S.C. 254(e)) and the regulations promulgated thereunder (42 CFR 5.1-5.4) will be considered an obligation to serve as a Federal employee.

(d) *Records required for exclusion from gross income.* To exclude amounts received under Federal programs requiring future services as a Federal employee, the recipient must maintain records that establish that the

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amounts received under such programs were used for qualified tuition and related expenses as defined in paragraph (c)(1) of this section. Qualifying uses may be established by providing to the Service, upon request, copies of relevant bills, receipts, cancelled checks or other convenient documentation or records which clearly reflect the use of the money received under the grant. The recipient must also submit, upon request, documentation establishing receipt of the grant and setting out the terms and requirements of the particular grant.

(e) *Applicability of rules of §§ 117(a) and 117(b).* Except where a different rule has been expressly provided in this section, amounts received under Federal grants requiring future service as a Federal employee, and which meet the requirements for exclusion from gross income under this section, are subject to the rules, limitations and definitions specified in §§ 117 (a) and (b) of the Code and §§ 1.117-1 through 1.117-4.

(f) *Effective date.* Except as provided in paragraph (b) of this section, this section will apply to amounts received after December 31, 1980 under Federal programs which meet the requirements of this section.

[T.D. 8032, 50 FR 27232, July 2, 1985]

§ 1.118-1 Contributions to the capital of a corporation.

In the case of a corporation, section 118 provides an exclusion from gross income with respect to any contribution of money or property to the capital of the taxpayer. Thus, if a corporation requires additional funds for conducting its business and obtains such funds through voluntary pro rata payments by its shareholders, the amounts so received being credited to its surplus account or to a special account, such amounts do not constitute income, although there is no increase in the outstanding shares of stock of the corporation. In such a case the payments are in the nature of assessments upon, and represent an additional price paid for, the shares of stock held by the individual shareholders, and will be treated as an addition to and as a part of the operating capital of the company. Section 118 also applies to contributions to capital made by persons other than

shareholders. For example, the exclusion applies to the value of land or other property contributed to a corporation by a governmental unit or by a civic group for the purpose of inducing the corporation to locate its business in a particular community, or for the purpose of enabling the corporation to expand its operating facilities. However, the exclusion does not apply to any money or property transferred to the corporation in consideration for goods or services rendered, or to subsidies paid for the purpose of inducing the taxpayer to limit production. See section 362 for the basis of property acquired by a corporation through a contribution to its capital by its stockholders or by nonstockholders.

§ 1.118-2 Contribution in aid of construction.

(a) *Special rule for water and sewerage disposal utilities—(1) In general.* For purposes of section 118, the term *contribution to the capital of the taxpayer* includes any amount of money or other property received from any person (whether or not a shareholder) by a regulated public utility that provides water or sewerage disposal services if—

(i) The amount is a contribution in aid of construction under paragraph (b) of this section;

(ii) In the case of a contribution of property other than water or sewerage disposal facilities, the amount satisfies the expenditure rule under paragraph (c) of this section; and

(iii) The amount (or any property acquired or constructed with the amount) is not included in the taxpayer's rate base for ratemaking purposes.

(2) *Definitions—(i) Regulated public utility* has the meaning given such term by section 7701(a)(33), except that such term does not include any utility which is not required to provide water or sewerage disposal services to members of the general public in its service area.

(ii) *Water or sewerage disposal facility* is defined as tangible property described in section 1231(b) that is used predominately (80% or more) in the trade or business of furnishing water or sewerage disposal services.