

Compliance Issues for the Use of Foundation Funds

UNDERWOOD

Presented by:
Janet Bubert
4.18.2024

Use of Foundation Funds

To maintain exempt status as a 501(c)(3), a Foundation must:

- Engage primarily in activities that **accomplish** one or more of its **exempt purposes**;
- Ensure the organization's net earnings **do not inure to the benefit of private individuals**; and
- Serve a valid purpose that **confers a public benefit**.

I.R.C. Reg. § 1.501(c)(3)-1(c) (a failure to satisfy any one of the requirements is fatal to continued entitlement to exempt status).



Accomplish Exempt Purpose

Use of funds must accomplish exempt purpose

Statement of exempt purpose in governing documents defines the scope of allowable exempt activities of the organization.

```
graph TD; A[Statement of exempt purpose in governing documents defines the scope of allowable exempt activities of the organization.] --> B[Be familiar with the scope of your organization's exempt purpose.]; B --> C[If necessary, consider amendment to change scope of activities.];
```

Be familiar with the scope of your organization's exempt purpose.

If necessary, consider amendment to change scope of activities.



Use of Restricted Funds



Use of Restricted Funds

- Restricted funds should not be used for general operations of the organization.
- Ensure organization and donor have the same understanding regarding acceptable use of funds.
 - Grants
 - MOU with School District
 - Scholarship criteria

Use of Restricted Funds

- Designated funds are held by the organization as a separate “trust” for the donor’s specific purpose.
- Directors are liable for misdirected funds.
- Changes to use of restricted funds may require court approval.



Avoid Improper Private Benefit

Use of Foundation Funds

- If an organization engages in either private inurement or private benefit, then the organization is furthering a non-exempt purpose.

Use of Foundation Funds

- “Private benefit” – generally, means **nonincidental** benefits conferred on **anyone other than the intended recipients** of the organization’s exempt purpose that serve private interests.
- An incidental private benefit may occur without risk to the organization’s exempt status.

Use of Foundation Funds

Whether a private benefit is “incidental” is evaluated through both a qualitative and quantitative lens:

- a **qualitative private benefit** is a mere byproduct of the public benefit;
- a **quantitative private benefit** is insubstantial compared to the public benefit provided by the exempt organization.

Use of Foundation Funds

- *Oliveri v Commissioner* (2019)
- U.S. Tax Court reviewed gifts to specific individuals, including a \$500 gift card to a retired police officer; organization's stated purpose was to "provide religious and spiritual counsel to people of need, including inmates and hospital patients."

Use of Foundation Funds

Oliveri v Commissioner (2019)

- Tax Court ruled the **gift was not in furtherance of the organization's exempt purpose** and conferred a private benefit because the gift was made to individual for whom **no substantial charitable need was established.**
- Amounts paid to a charity for the benefit of a specified individual are generally not deductible as charitable contributions, regardless of the circumstances of the recipient or the intent of the donor.

Use of Foundation Funds

Rameses School of San Antonio v. Commissioner (2007)

- Exempt organization was formed to operate a charter school in the San Antonio area. Organization funds were used to make mortgage and lease payments for the **benefit of specific individuals**, and the Court revoked the organization's exempt status.
- Use of organization's funds for **personal use by individuals** problematic because it provides for an "obvious opportunity for abuse of the claimed tax-exempt status."

Use of Foundation Funds

Capital Gymnastics Booster Club v. Commissioner (2013)

- Exempt status revoked for not operating exclusively for tax-exempt purposes.
- Club provided “points” to parents/members who raised funds for the organization; points (valued at \$10) used to offset fees paid to organization for competition costs (entry fees, travel, etc.)
- Use of points was private inurement to individuals without any showing of need or part or financial distress.

Use of Foundation Funds

Compare:

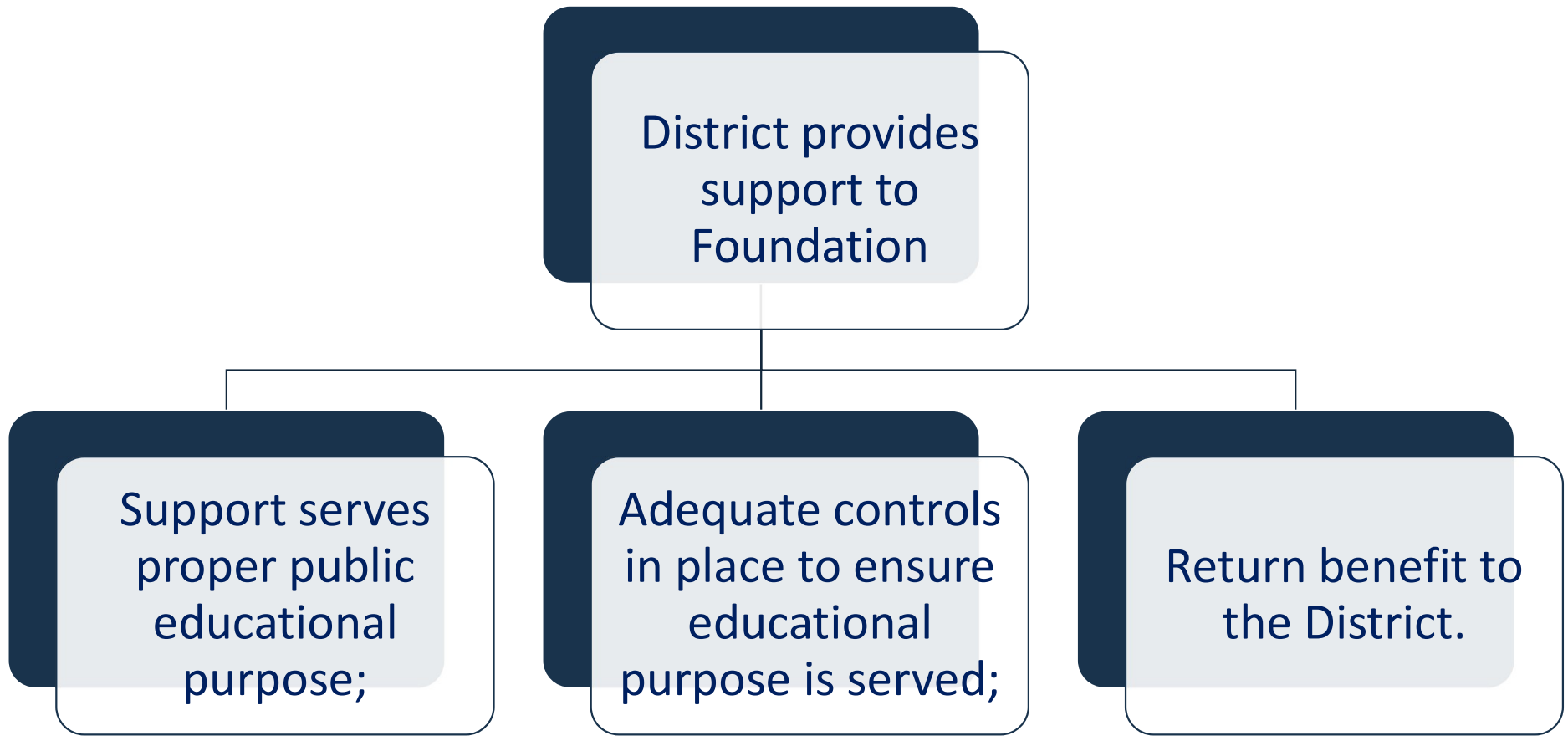
- Fifth grade teacher awarded grant from Foundation to implement innovative program for teaching science. The program attracts media attention, and the teacher is recruited to a higher paying position at another school.
- All fifth-grade teachers within the school district are given a \$100 gift card from the Foundation with a note of appreciation for their hard work.



Valid Purpose Confers Public Benefit

Use of Funds if Foundation Receives District Support

- Tex. Const. Art. III Section 51, 52(a); Art. XI, Section 3; Art. XVI, Section 6(a) **prohibit granting public money for a private benefit** ("gift of public funds"). Tex. Att'y Gen. Op. JC-138 (1999).
- Support to a private organization not unconstitutional if certain conditions met to ensure the support serves a public purpose.
- Texas Attorney General Opinion DM-256 (1993) (school district may provide office space and other benefits to education foundation if conditions met).



Session Evaluation

Access the evaluation
using the QR Code
on page 21 of the
Conference Program.



Questions?
Janet.Bubert@uwlax.com

UNDERWOOD

Presented by:
Janet Bubert