

LEGAL ISSUES IN ADVANCED FUNDRAISING

May 25, 2016
Regional Foundation Center
Free Library of Philadelphia

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AGENDA

A. Quick Reminders

1. State fundraising registrations
2. Federal substantiation letters to donors

B. Corporate Sponsorships

C. Illiquid Assets

D. Planned Giving

E. Large Gifts

A. Quick Reminders

Registering to Fundraise – PA

- **Required** before paying any fundraiser
OR
more than \$25,000 annually
- Annual filing
- Contracts
- Bonds
- Disclosure language



Registering to Fundraise – NJ

- **Required** before paying any fundraiser
OR
more than \$10,000 annually
- 30 days to file after crossing \$10,000
- As of 2006, \$30 for voluntary registration
- Annual renewal – due 6 months after fiscal year end



Fundraising – NY

- State the purpose or state that information is available from organization
- Nonprofit Revitalization Act of 2013 – lots of new policy requirements



Substantiation



- **Receipts: Your donors need them to deduct – IRS very strict recently**
- Don't tell your donors what to deduct
- What did you give in return?
- Include disclosure language
- Look to IRS Publication 1771

B. Corporate Sponsorships

Unrelated Business Income Tax “UBIT”

501(c) means your income is exempt from federal income taxes

501(c)(3) adds deductible contributions for donors

The **regular corporate tax rate** applies, though, for traditional business activities

Unrelated Business Income Tax

“UBIT”

Any trade or business

Not related to the organization’s exempt purpose

Unrelated Business Income Tax “UBIT”

Is the Corporate Sponsorship:

1. A **Donation** to the organization

OR

2. A **Payment** to the organization made in exchange for the organization conducting a trade or business activity that is not related to the organization's exempt purpose?

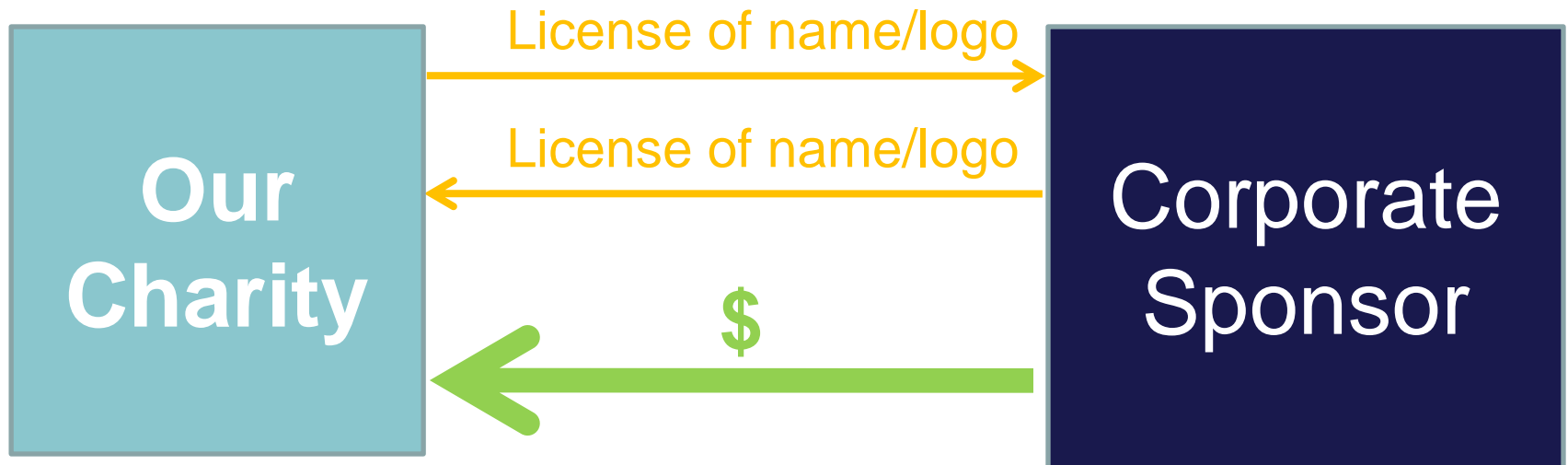
Unrelated Business Income Tax

“UBIT”

When might UBIT apply?

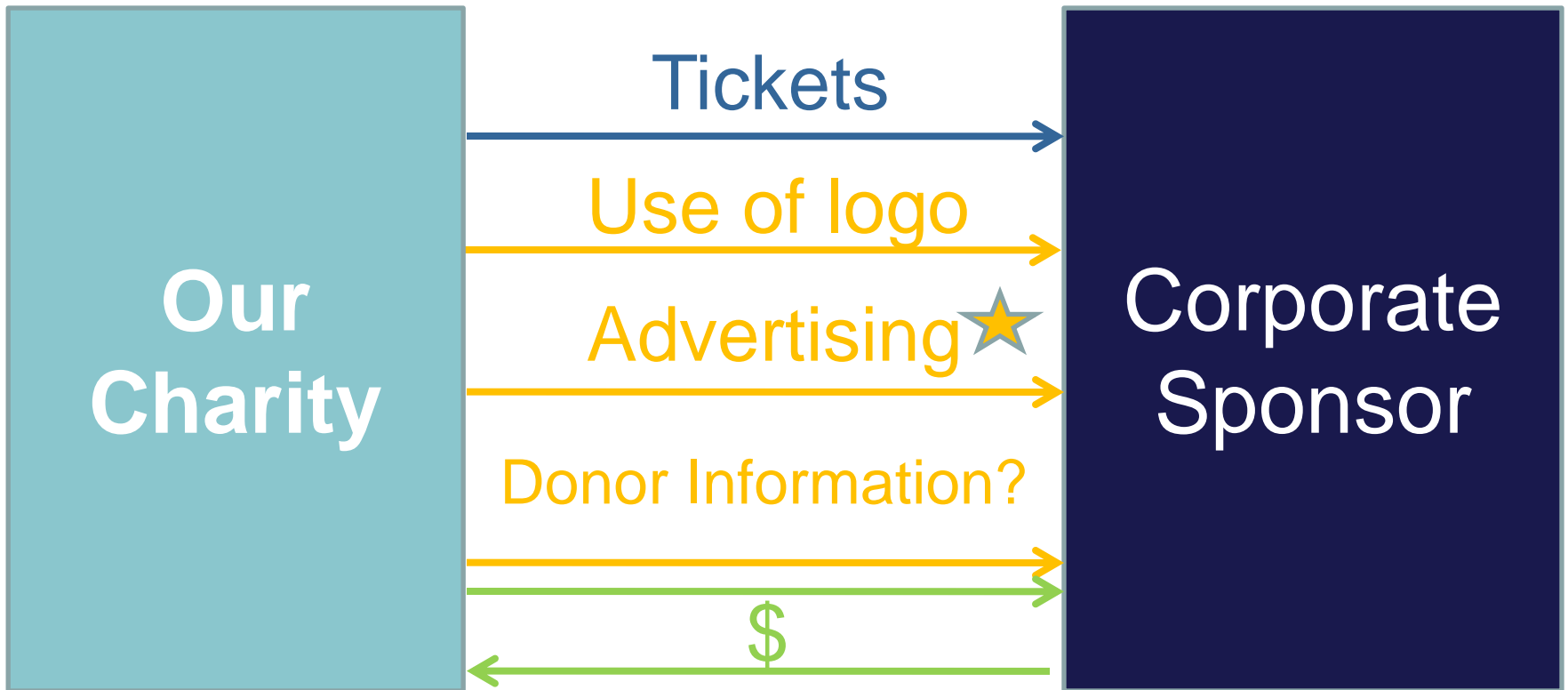
- Any commercial activity
- Debt-financed income (such as income from a property subject to a mortgage)
- Gift shops – each item is considered individually
- Thanking donors – distinguishing acknowledgments from advertising
- Providing certain services when leasing your office space
- Providing certain services when renting out your donor lists
- Engaging in activities with for-profit entities: Joint ventures, commercial co-ventures, etc.

Corporate Sponsorships



- Defined term for tax purposes
- De minimis exception – mostly a donation

As Proposed by Sponsor?

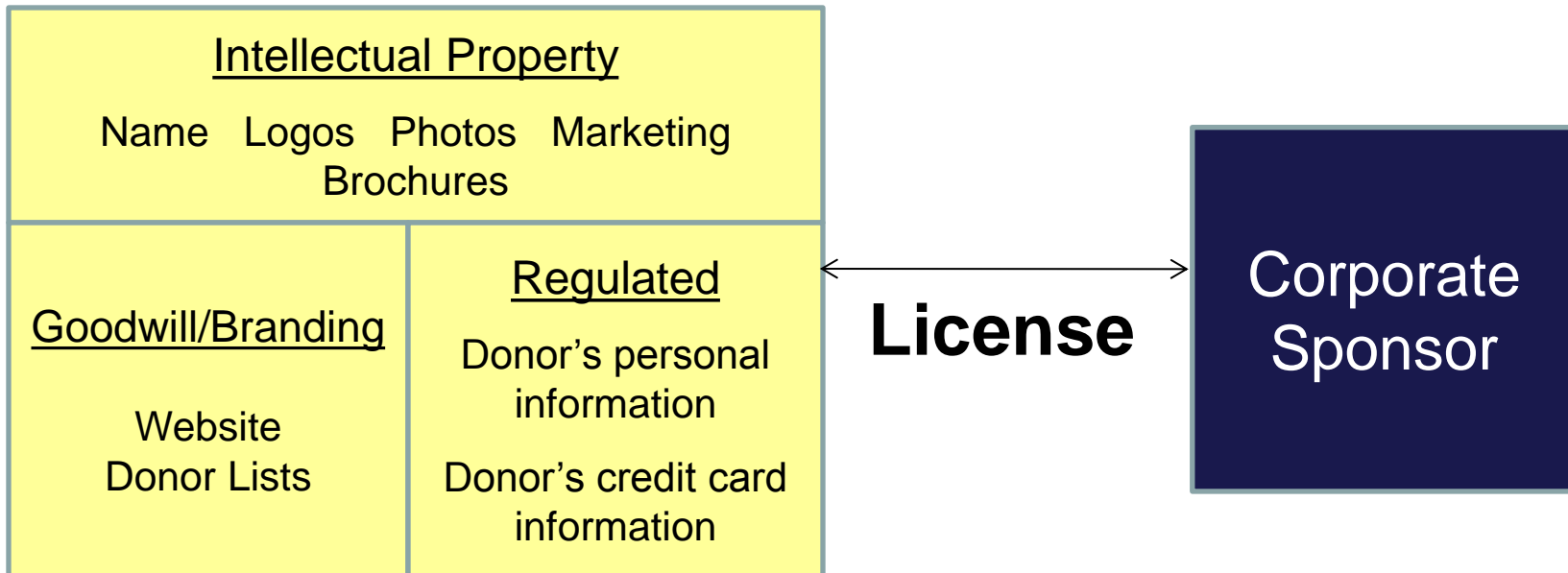


Corporate Sponsorships

Consider **every benefit** you provide the sponsor

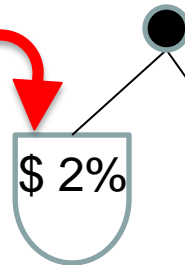
- Tickets
- Advertising (*specific language*)
- Use of your space
- Exclusive provider rights
- Use of your logo or name

Corporate Sponsorships



Corporate Sponsorships

Benefit going
back to
Sponsor



- Total the \$ value of the Sponsor's contribution
- Is there any “**quid pro quo**” – something the Sponsor receives in exchange?
- Is the quid pro quo < 2% of the contribution?



Corporate Sponsorships

**Benefit going
back to
Sponsor**

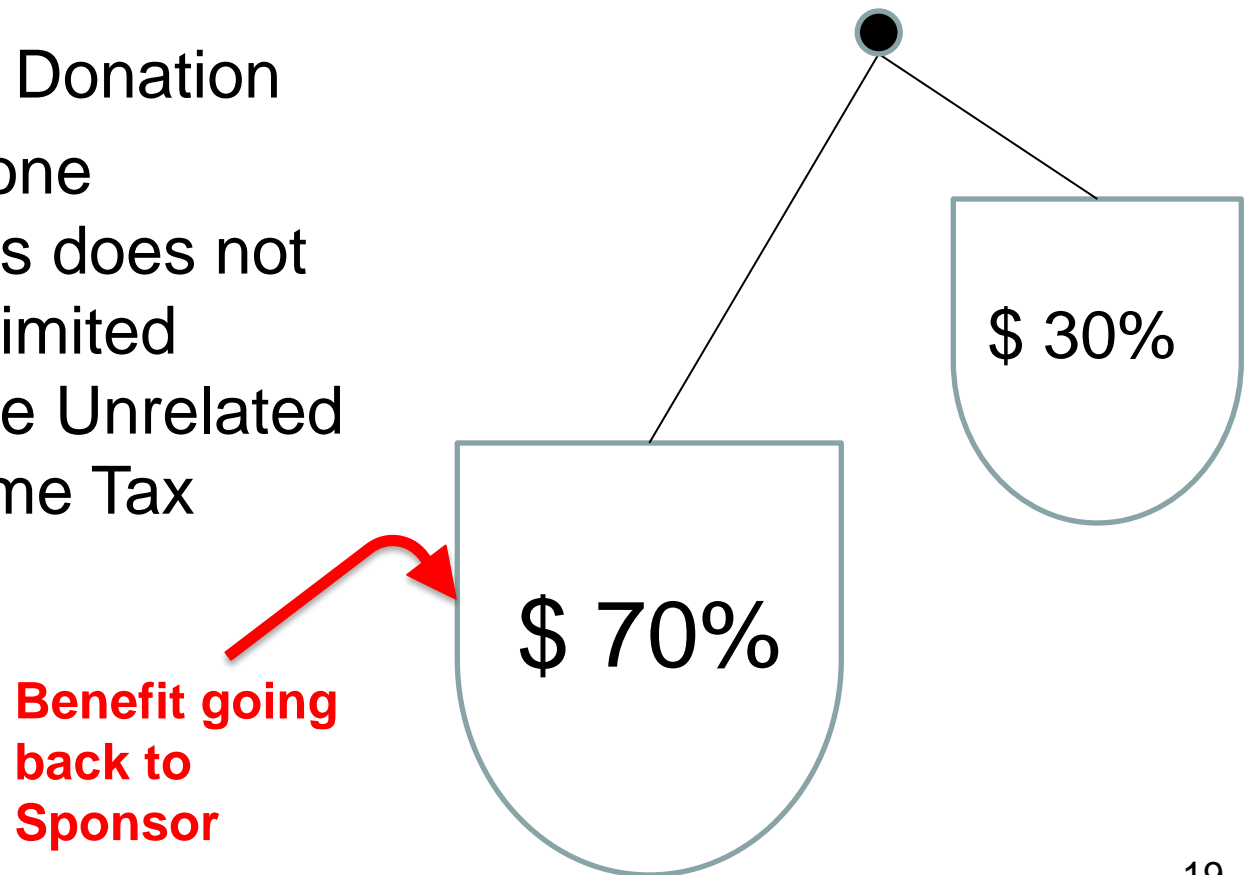


- Looks more like a Donation



Corporate Sponsorships

- Not so much a Donation
- Structured as one transaction, this does not qualify for the limited exception to the Unrelated Business Income Tax (UBIT)



Triggering UBIT

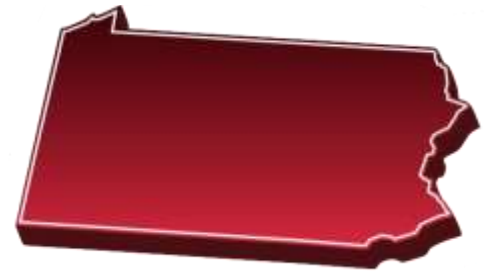
- Advertising v. Acknowledgment
- Website links – pass through intermediate site preferred
- Exclusive right to provide products at an event v. Exclusive category sponsorship
- Actively providing services to Sponsor
- Donation \$ based on event or product success
- UBIT is OK – Just make an educated business decision

Business Decision

- Is paying the tax worth it? Do you still bring in money?
- Should you ask your “donor” for more money to balance the tax consequences?
- 10% charitable deduction
- Consider a nonprofit restructure

Registering to Fundraise – PA

- Professional fundraising counsel
- Professional solicitor
- Commercial coventurer

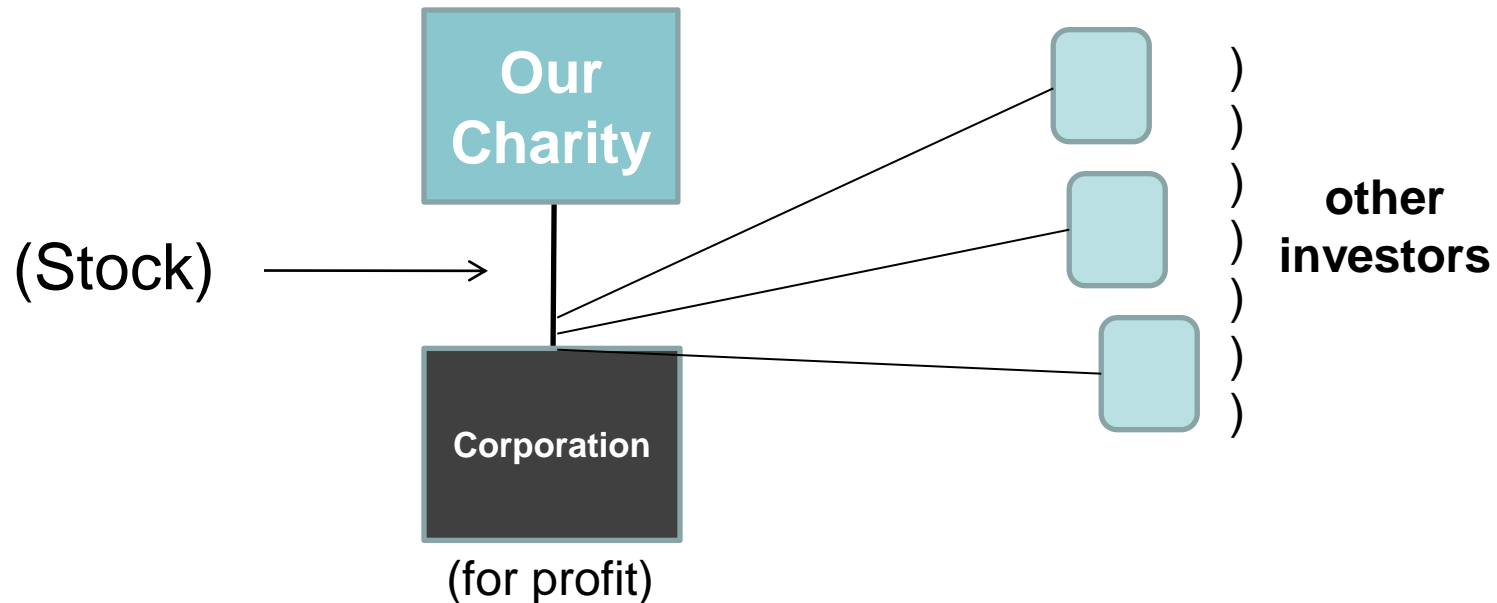


C. Illiquid Assets

Illiquid Assets

- Stock in publicly traded companies
- Stock in closely held companies
- Interests in partnerships
- Real estate
- Collectibles, including art
- Intellectual property

Shareholder in a For profit Corporation



- Our Charity holds stock of a separate taxable entity
- Dividends paid to our Charity are passive and not subject to UBIT

Holding Stock

- Provides liability protection because activities of the for profit company are not attributed to Our Charity
- “Blocks” UBIT for activities conducted in the subsidiary

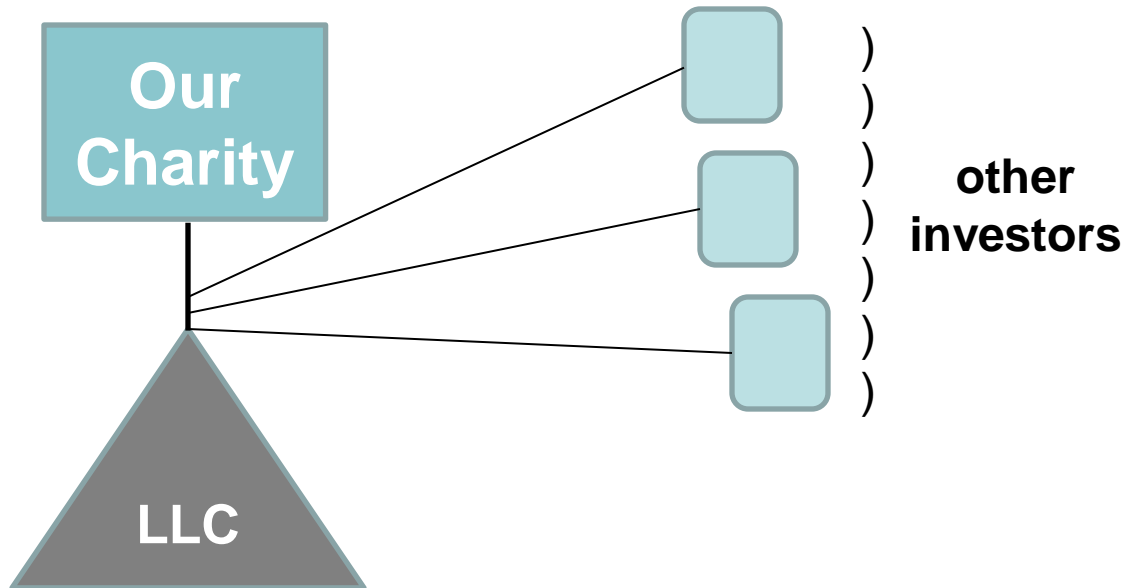
Holding Stock

- What is the exit strategy?
- Is it publicly traded?
- Is it subject to any restrictions?
- Valuation for the donor's purposes should be as of the date the asset is transferred to the charity. When does the charity have control over the asset?

Non-publicly Traded Stock

- **Increased due diligence**
- Understand exit/liquidation strategy
- Understand restrictions that accompany the asset
- Discuss valuation
- Consider requesting cash for liquidity to cover any immediate costs
- Initial Public Offerings (“IPO”s) and secondary offerings

Partnerships and LLCs



- Our Charity holds an interest in a partnership
- Partnership is a pass-through entity for tax purposes

Partnerships and LLCs

- Lots of due diligence
- Look for active UBIT and debt-financed UBIT
- Management role not generally appropriate for Our Charity
- Increased filing obligations?
- Review current liabilities and potential future costs, such as capital calls
- Restrictions on transfer, both legal and practical
- Consider a “put” option as an exit strategy
- Valuation

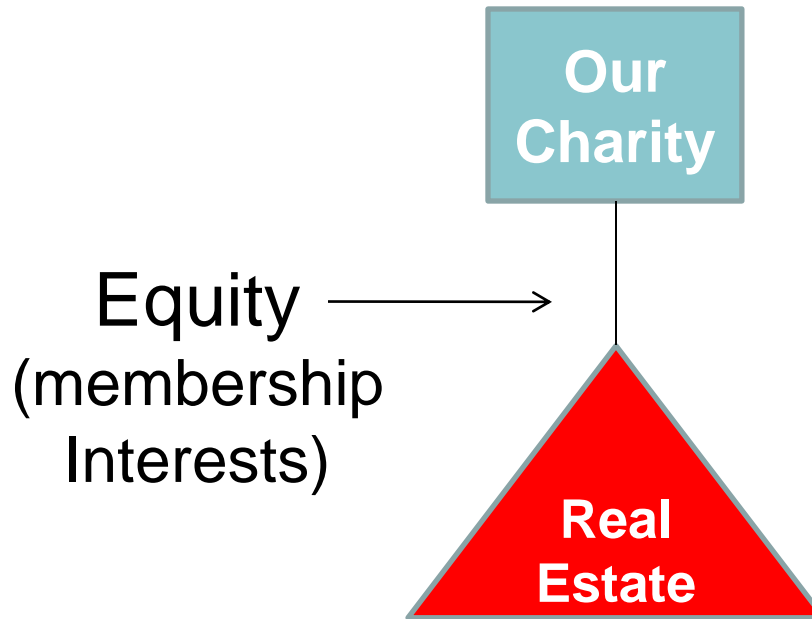
Interests in Entities

- Check for liabilities
- Exit strategy/transferability
- Review of asset by an appropriate subject matter expert
- Donation contract
- Assignment of income as a tax trap for the unwary

Real Estate

- Due diligence
- Zoning and environmental review
- Physical Inspection
- Transfer taxes

Single Member Limited Liability Company



- Subsidiary is disregarded for income tax purposes
- Regarded for state law purposes
- Member managed or Manager managed

Single Member Limited Liability Company

- Benefits and Opportunities
 - Easy to set up
 - Uses exempt status of Parent
 - Contributions can be made directly to LLC
 - Provides additional liability protection for LLC assets and/or activities
 - Flexible management

D. Planned Giving

Charitable Planning Techniques

- Outright Gifts of Cash and Property
 - including life insurance
- Charitable Bequests
 - including qualified retirement plans – built in gain never taxed; bequest other assets to heirs; great tax result
- Split Interest Gifts
 - Charitable Remainder Trusts
 - Charitable Lead Trusts

Planned Giving Vehicles

- Private Foundation
- Supporting Organization
- Lead Trusts
- Remainder Trusts
- Charitable Gift Annuity (“CGA”)
- Donor advised fund (“DAF”)

Split-Interest Gifts

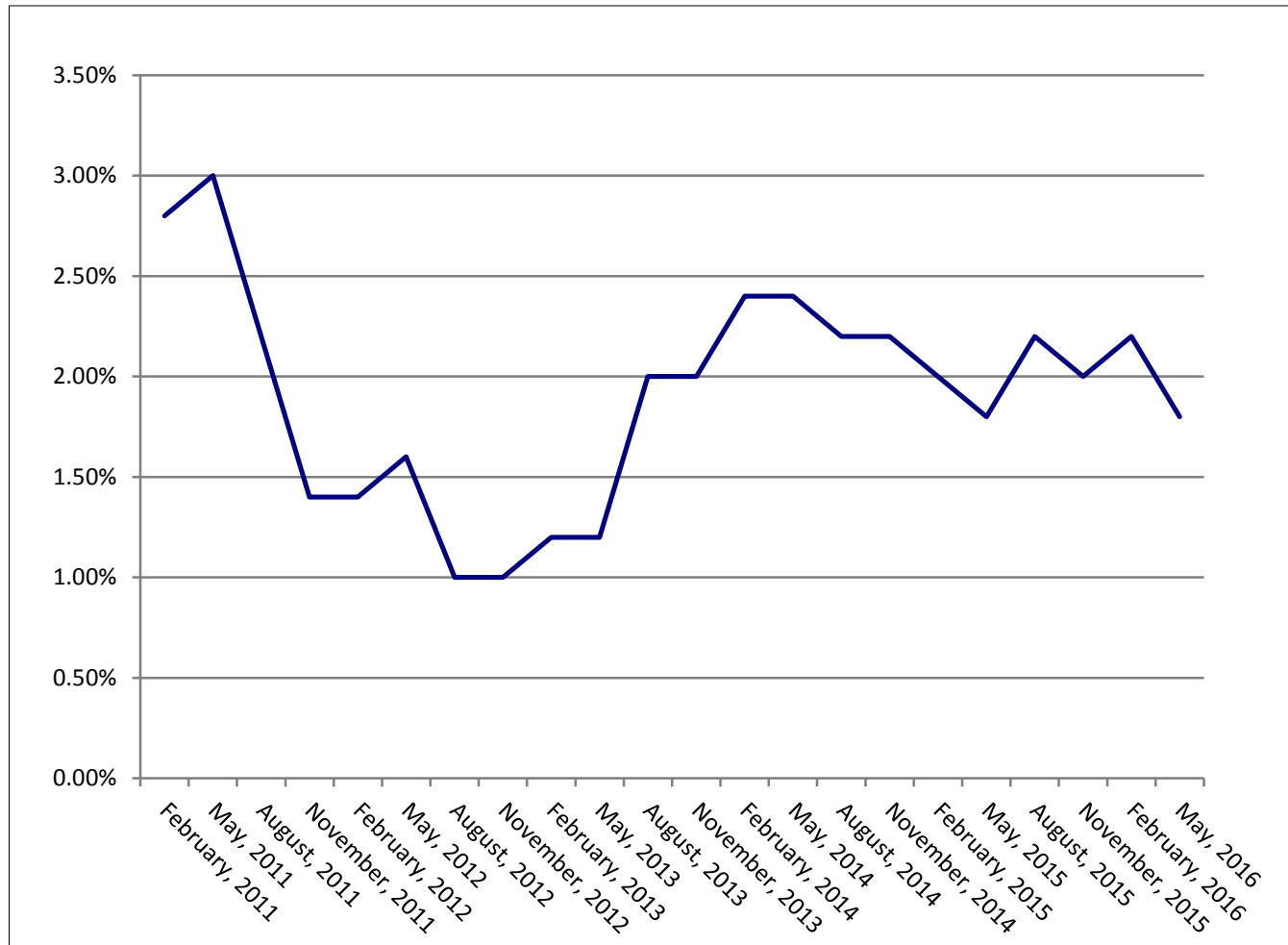
- Lead Trusts

- (charity gets the “lead” first interest)

- Remainder Trusts

- (charity gets the “remainder” last interest)

AFR – 7520 Rate



Remainder Options

- Charitable Gift Annuity (“CGA”)
 - (Charity’s assets available in full to satisfy)
- Remainder Trusts
 - (Separate entity for liability purposes but held by Trustee(s))
- Donor advised funds
 - (Do you host it? Or are you just preferred?)
- Endowment or other fund

E. Large Gifts

Restricted Charitable Funds

- Institutional Fund
- Temporarily Restricted
- Permanently Restricted
- Endowment
- Quasi-Endowment
- Trust

Fund Restrictions

- Removal through Agreement with the Donor
- Removal through Orphans' Court review
- Attorney General supervision

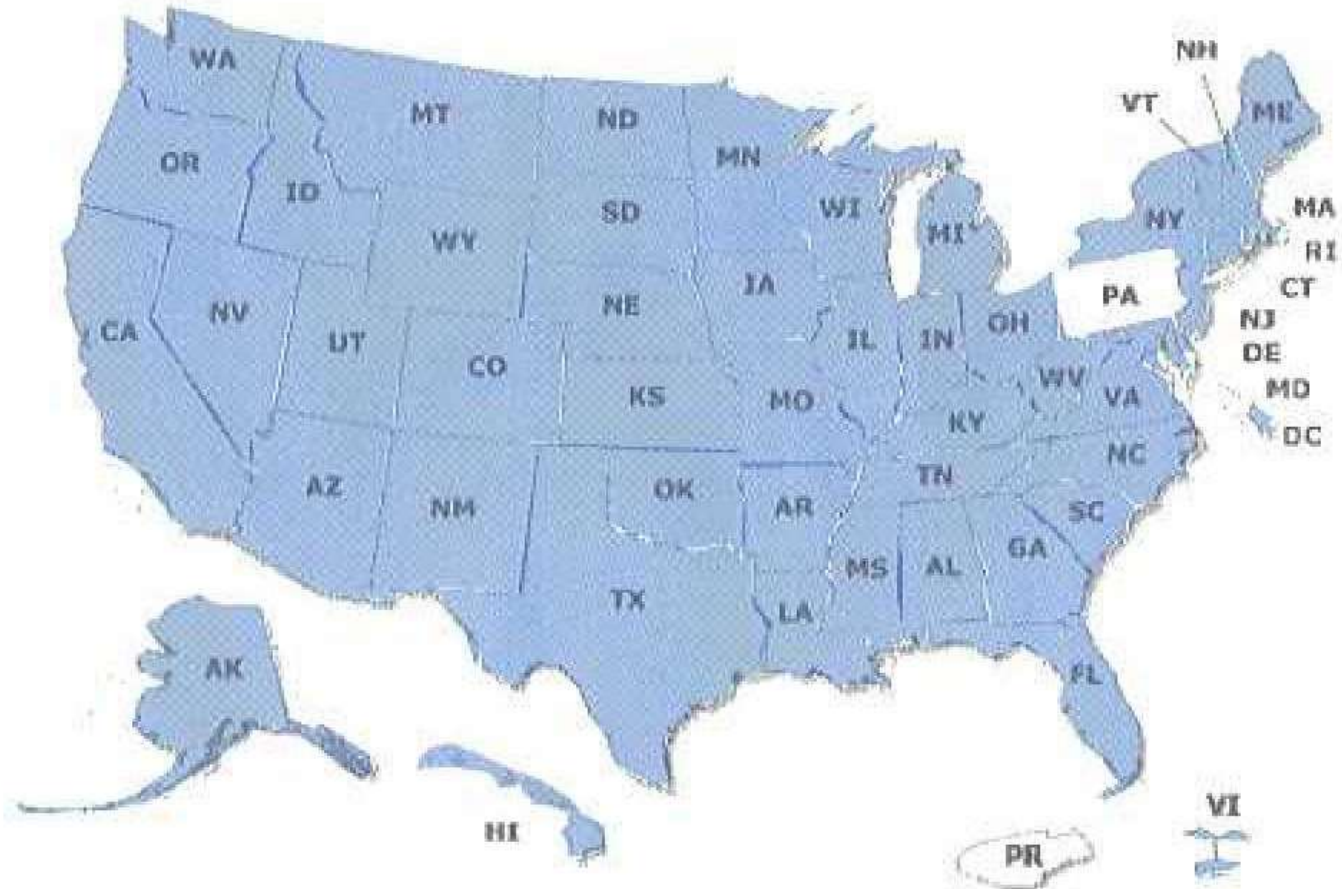
Lessons Learned - Some Tax Considerations

- A high level of donor control could prevent tax deductions for that donor
- A high level of donor control could create a separate trust, subject to the more restrictive private foundation rules
- Beware of reversionary interests
- Do the restrictions constitute earmarking?

Lessons Learned - Some Specific Drafting Considerations

- Make sure to include the details of any required accounting or progress reports
- Consider spending restrictions
- Consider investment restrictions
- Consider restrictions on pledging funds or internal borrowing
- Standing to enforce?
- Are donor's heirs or third parties involved?

Enactment Status Map



UPMIFA

■ = Enacted □ = Introduced this Year

Fund Management

- Prudent Investor Rule in PA
- UPMIFA in most states
- PA spending election 2% - 7%
- Investing for total return

Fundraising – NY

- Solicitations for endowments must add reference to new spending rules



Internal Charitable Funds

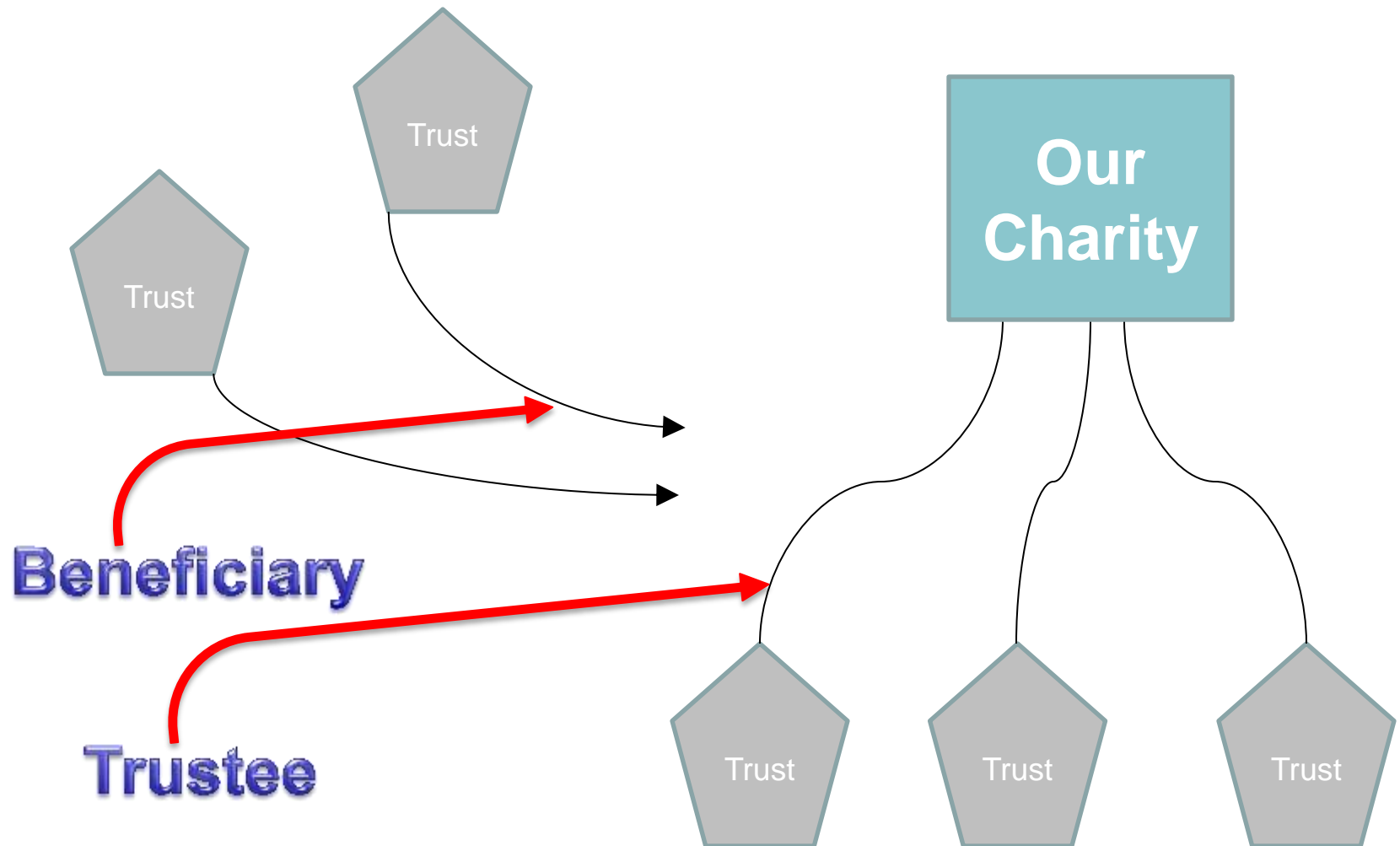
Our Charity

Charitable
Gift
Annuity

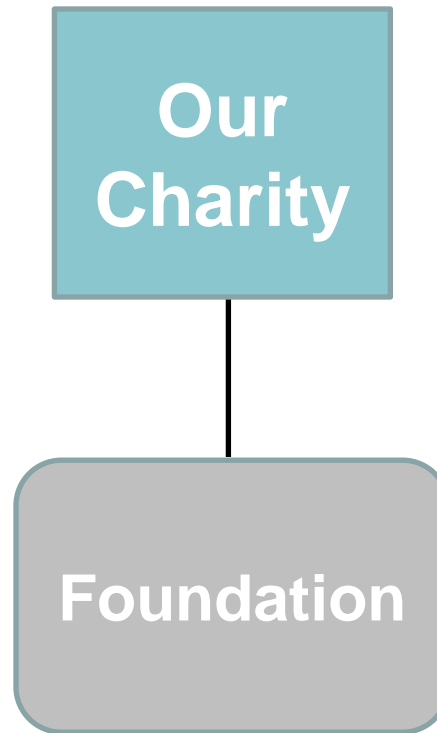
Donor
Advised
Fund

Restricted
Fund

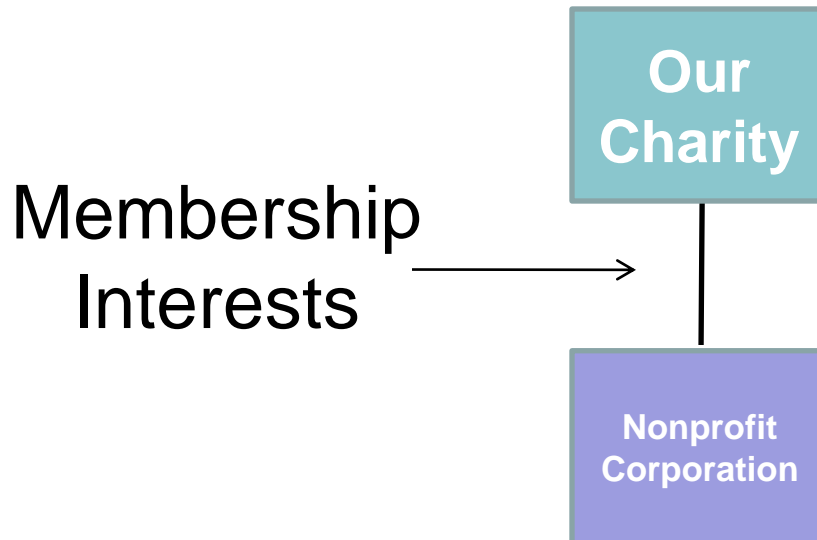
Trusts – 2 Different Roles



Common Example: Creating a Foundation

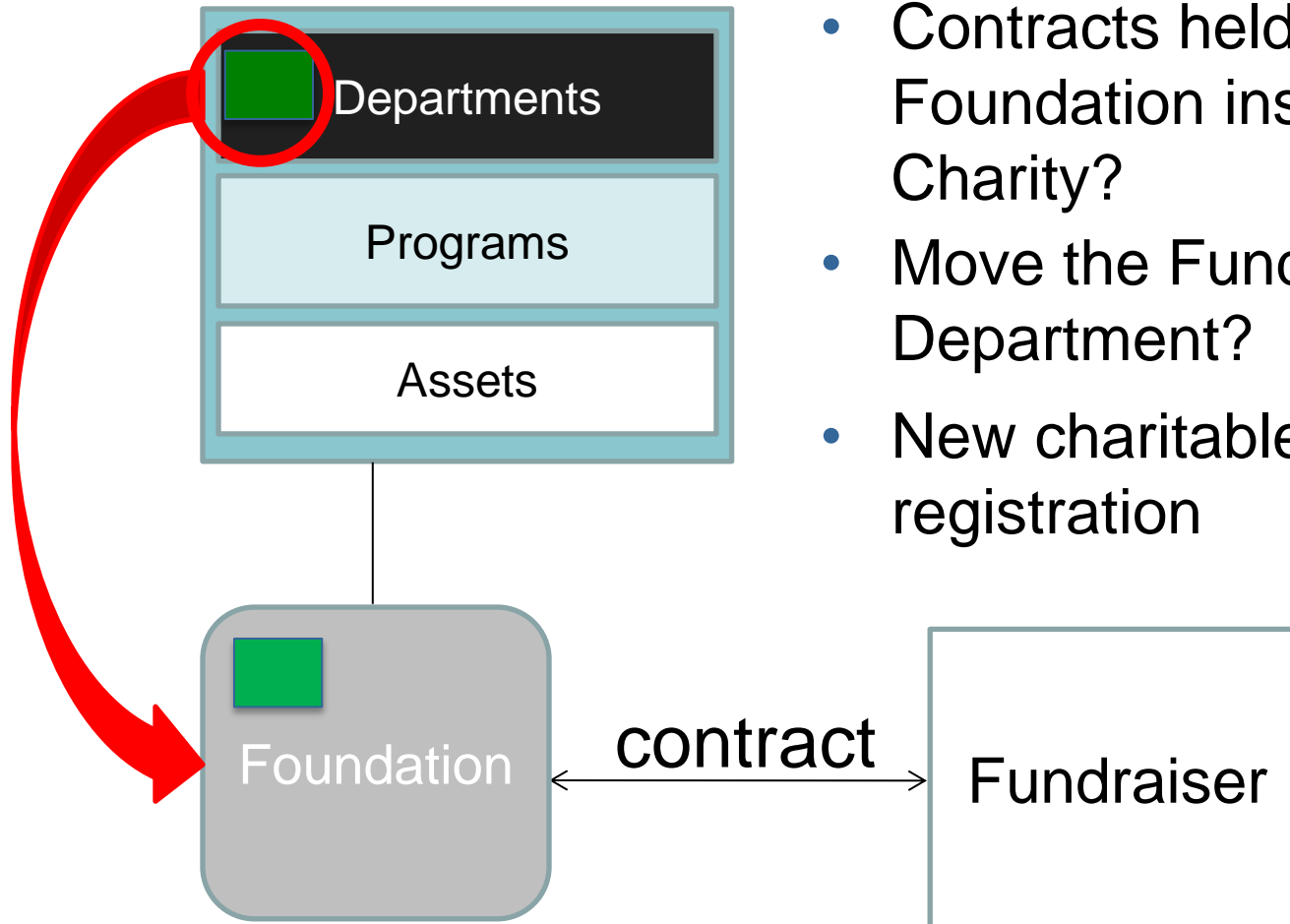


Corporate Subsidiary Nonprofit Option



- Separate corporate entity
- Independent tax-exempt status (e.g., supporting organization)
- Parent is the controlling member

What Moves to the Foundation?



- Contracts held by Foundation instead of Our Charity?
- Move the Fundraising Department?
- New charitable solicitation registration

QUESTIONS?

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