



# **Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies**

July 12, 2012

12:00 p.m. – 2:00 p.m. EDT

Venable LLP

575 7<sup>th</sup> Street, NW

Washington, DC 20004

## **Moderator:**

Jeffrey S. Tenenbaum

## **Panelists:**

George E. Constantine, III

Janice M. Ryan

VENABLE<sup>®</sup><sub>LLP</sub>

# Presentation



## Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies

Thursday, July 12, 2012  
12:30 p.m. - 2:00 p.m. EDT  
Venable LLP  
Nonprofit Organizations Practice  
Washington, DC

Moderator:  
Jeffrey S. Tenenbaum, Esq.

Panelists:  
George E. Constantine, III, Esq.  
Janice M. Ryan, Esq.



### Upcoming Venable Nonprofit Legal Events

August 2, 2012 - [How Nonprofits Can Raise Money and Awareness through Promotional Campaigns without Raising Legal Risk](#)

September 13, 2012 – Details Coming Soon



## Today's Discussion

- Common affiliation structures
- Key legal pitfalls
  - Attribution of liability to affiliated entities
  - Intellectual property ownership and use
  - Antitrust considerations
  - Governance-related challenges
- Special tax considerations
  - Group tax exemption
  - 501(c)(3) affiliates of non-501(c)(3) entities (e.g., association foundations)
- Managing affiliate relationships
  - Affiliation agreements, and other successful strategies



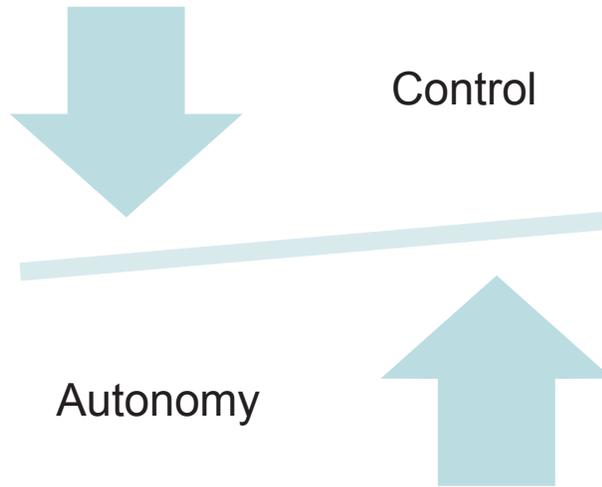
## Common Affiliation Structures

### Reasons to Affiliate



## Common Affiliation Structures

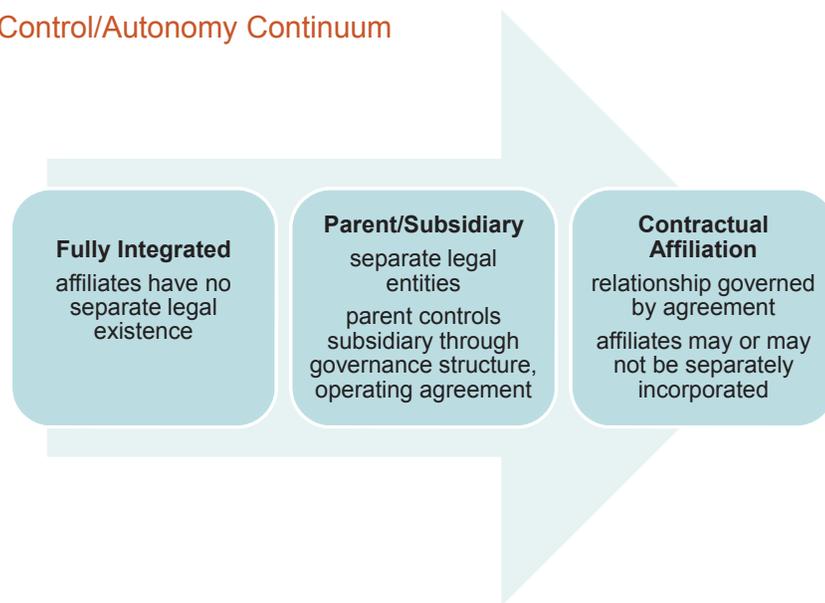
Control v. Autonomy is Key Factor in Choice of Structure



© 2012 Venable LLP

## Common Affiliation Structures

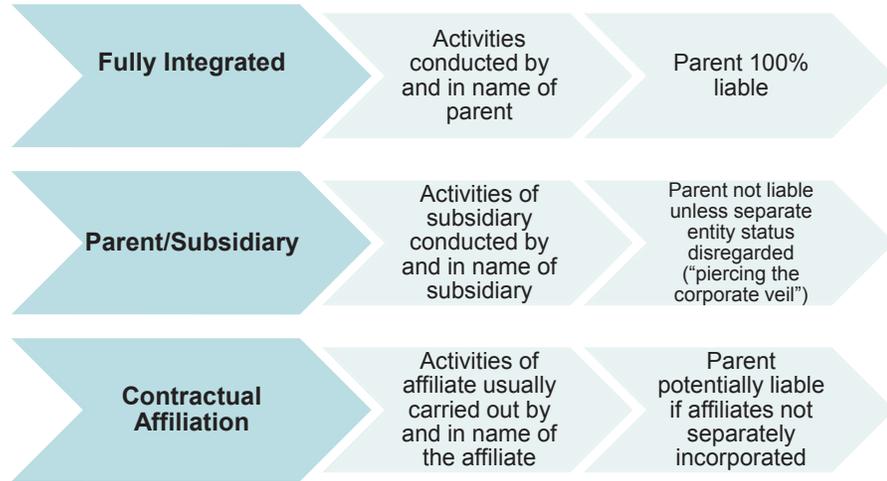
Control/Autonomy Continuum



© 2012 Venable LLP

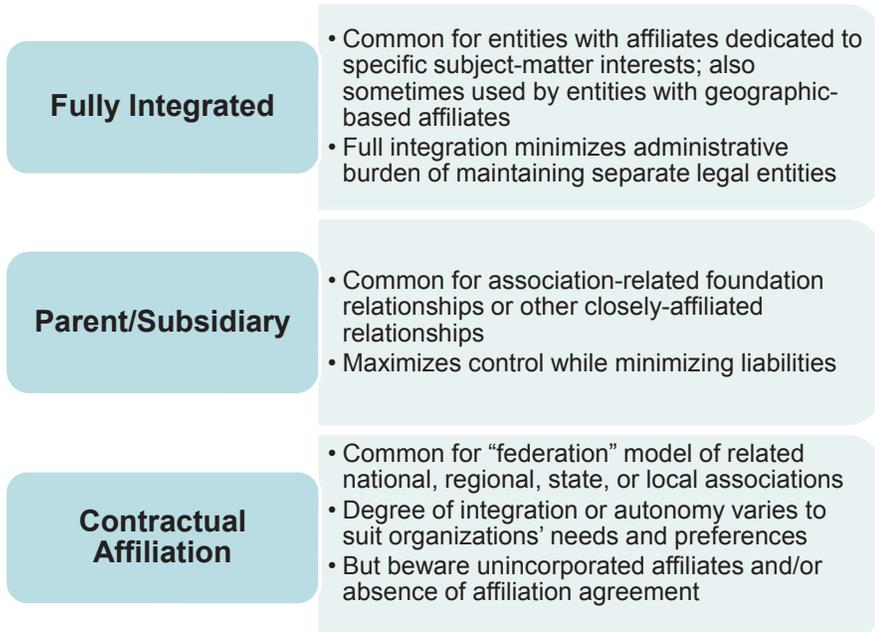
# Common Affiliation Structures

## Risk Profile of Common Affiliation Structures



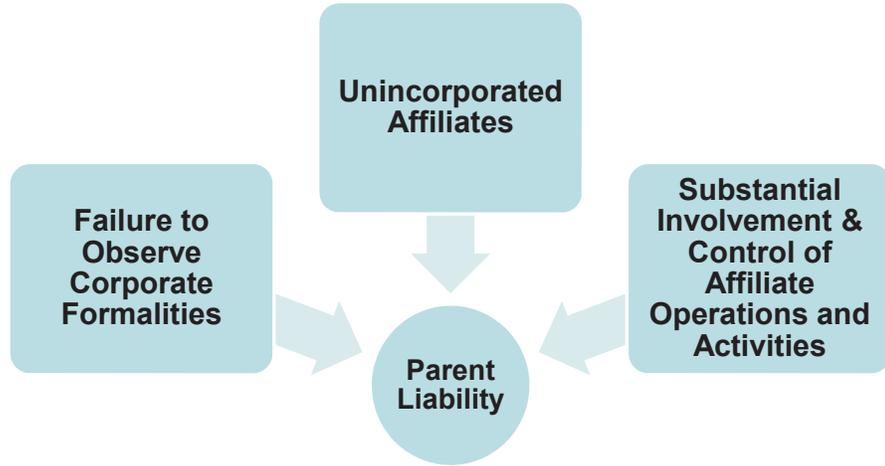
# Common Affiliation Structures

## Other Characteristics



## Key Legal Pitfalls

Attribution of Liability to Parent (Tort, Contract, etc.)



© 2012 Venable LLP

## Key Legal Pitfalls

Intellectual Property Ownership and Use

### Names & Logos

- Common practice for affiliate name to include parent's name
- Disputes over use of name likely in the event of disaffiliation
- Specify trademark license terms in affiliation agreement and/or bylaws or policies
- Consider trademark registration (U.S. and foreign, if operating internationally)

### Publications & Data

- Address ownership and licensing of membership lists, data, and works created by or through affiliates in affiliation agreement or on a project-by-project basis as necessary
- Consider 501(c)(3) tax implications before assigning rights to a non-501(c)(3)

© 2012 Venable LLP

## Key Legal Pitfalls

### Antitrust Considerations

Price Restrictions

Territorial  
Restrictions

Common  
Membership  
Requirements

Facilitating or  
Participating in  
Anticompetitive  
Activities of Affiliate



## Key Legal Pitfalls

### Governance-related Challenges

- Fiduciary duties
  - Overlapping directors on parent and affiliate boards
  - Affiliate representatives on parent board
- Common governance structure requirements
  - What works for parent might not be best for affiliate
- Common membership requirements
  - Qualifications
  - Termination
- Managing Affiliate Status
  - Threshold for granting charter
  - Dispute resolution
  - Inactive or probation status
  - Disaffiliation
- Financial management
  - Dues collection arrangements
  - Internal controls at affiliate level



## Special Tax Considerations

### Federal Group Tax Exemption

#### Application Process

Increasingly Lengthy & Expensive Process

Changes May Be Forthcoming

#### Benefits & Limitations

Substantial Benefit for Subordinates

“General Supervision or Control” Element & Liability Risk

UBIT  
Federal Employment Taxes  
State & Local Taxes

#### Compliance

Annual Filings & Automatic Revocation

Monitoring Subordinate Activities

Training

© 2012 Venable LLP

## Special Tax Considerations

### 501(c)(3) Affiliates of Non-(c)(3) Entities

- Private benefit and private inurement
- Transferring funds and other resources from (c)(3) to non-(c)(3)
  - Grants to non-(c)(3)s
  - Providing fair market value consideration
- Attribution of political and lobbying activities to (c)(3)
  - Shared websites

© 2012 Venable LLP

# Managing Affiliate Relationships

Key Elements for Agreements, Articles & Bylaws, Affiliate Charters, Policies



© 2012 Venable LLP



# Managing Affiliate Relationships

Key Elements for Agreements, Articles & Bylaws, Affiliate Charters, Policies

- |                      |  |
|----------------------|--|
| Governance           | <ul style="list-style-type: none"> <li>• Parent entity control mechanisms</li> <li>• Requirements for governance structure, nominations &amp; elections, etc.</li> <li>• Common membership requirements</li> </ul>   |
| Finances & Resources | <ul style="list-style-type: none"> <li>• Cost allocation for shared staff, facilities, and other resources</li> <li>• Allocation of revenues, fundraising requirements</li> <li>• Dues collection arrangements</li> <li>• Internal controls requirements</li> <li>• Annual reports for group exemption purposes</li> </ul> |

© 2012 Venable LLP



## Managing Affiliate Relationships

### Key Elements for Agreements, Articles & Bylaws, Affiliate Charters, Policies

#### Purposes & Activities

- Common (or at least not inconsistent) mission and purposes
- Expectations and parameters for affiliate activities; geographic territory (but note franchise issue)
- Support and other services, if any, to be provided by parent to affiliate

#### Tax Exemption

- Expectation for affiliates to maintain tax-exempt status (group exemption or otherwise)
- Reasonable cost allocation for shared staff and facilities to avoid adverse tax consequences (UBIT, private benefit, private inurement)



## Managing Affiliate Relationships

### Key Elements for Agreements, Articles & Bylaws, Affiliate Charters, Policies

#### Intellectual Property

- Ownership and license terms applicable to use of names, logos, and other trade or service marks
- Ownership and license terms applicable to use of membership lists and other copyrighted or proprietary data or materials

#### Liability & Insurance

- Confidentiality
- Limitations on authority to speak or act on behalf of affiliated entity
- Indemnification
- Insurance expectations



## Managing Affiliate Relationships

Key Elements for Agreements, Articles & Bylaws, Affiliate Charters, Policies

### Dispute Resolution & Disaffiliation

- Establish clear procedures and authorities governing dispute resolution, including and up to probation or disaffiliation
- Consider leverage of respective parties
- At minimum, address parent's right to terminate license of name, logo, and other trade or service marks



## Managing Affiliate Relationships

Other Successful Strategies

- Invest in dedicated affiliate or chapter relations staff
- Provide affiliate leaders with resources and training on fundamentals of nonprofit governance and tax-exempt status requirements
- Include affiliate leaders in decision-making where appropriate
- Insurance



## Questions and Discussion

Venable LLP  
575 7<sup>th</sup> Street, NW  
Washington, DC 20004  
202.344.4000

Jeffrey S. Tenenbaum, Esq.  
[jstenenbaum@Venable.com](mailto:jstenenbaum@Venable.com)  
t 202.344.8138

George E. Constantine, III, Esq.  
[geconstantine@Venable.com](mailto:geconstantine@Venable.com)  
t 202.344.4790

Janice M. Ryan, Esq.  
[jmryan@Venable.com](mailto:jmryan@Venable.com)  
t 202.344.4093

To view Venable's index of articles, PowerPoint presentations, recordings, and upcoming seminars on nonprofit legal topics, see [www.Venable.com/nonprofits/publications](http://www.Venable.com/nonprofits/publications), [www.Venable.com/nonprofits/recordings](http://www.Venable.com/nonprofits/recordings), [www.Venable.com/nonprofits/events](http://www.Venable.com/nonprofits/events).





# **Speaker Biographies**



## Jeffrey S. Tenenbaum

Partner

Washington, DC Office

T 202.344.8138 F 202.344.8300

[jstenenbaum@Venable.com](mailto:jstenenbaum@Venable.com)

### AREAS OF PRACTICE

Tax and Wealth Planning  
 Antitrust  
 Political Law  
 Business Transactions Tax  
 Tax Controversies  
 Tax Policy  
 Tax-Exempt Organizations  
 Wealth Planning  
 Regulatory

### INDUSTRIES

Nonprofit Organizations and Associations  
 Credit Counseling and Debt Services  
 Financial Services  
 Consumer Financial Protection Bureau Task Force

### GOVERNMENT EXPERIENCE

Legislative Assistant, United States House of Representatives

### BAR ADMISSIONS

District of Columbia

Jeffrey Tenenbaum chairs Venable's Nonprofit Organizations Practice Group. He is one of the nation's leading nonprofit attorneys, and also is an accomplished author, lecturer and commentator on nonprofit legal matters. Based in the firm's Washington, D.C. office, Mr. Tenenbaum counsels his clients on the broad array of legal issues affecting trade and professional associations, charities, foundations, think tanks, credit and housing counseling agencies, advocacy groups, and other nonprofit organizations, and regularly represents clients before Congress, federal and state regulatory agencies, and in connection with governmental investigations, enforcement actions, litigation, and in dealing with the media.

Mr. Tenenbaum was the 2006 recipient of the American Bar Association's Outstanding Nonprofit Lawyer of the Year Award, and was the inaugural (2004) recipient of the *Washington Business Journal's* Top Washington Lawyers Award. He was one of only seven "Leading Lawyers" in the Not-for-Profit category in the 2012 *Legal 500* rankings, and was the 2004 recipient of The Center for Association Leadership's Chairman's Award, and the 1997 recipient of the Greater Washington Society of Association Executives' Chairman's Award. Mr. Tenenbaum was a 2008-09 Fellow of the Bar Association of the District of Columbia and is AV Peer-Review Rated by *Martindale-Hubbell*. He started his career in the nonprofit community by serving as Legal Section manager at the American Society of Association Executives, following several years working on Capitol Hill.

### REPRESENTATIVE CLIENTS

AARP  
 American Academy of Physician Assistants  
 American Association for the Advancement of Science  
 American Association of Museums  
 American College of Radiology  
 American Institute of Architects  
 Air Conditioning Contractors of America  
 American Society for Microbiology  
 American Society for Training and Development  
 American Society of Anesthesiologists  
 American Society of Association Executives  
 American Society of Civil Engineers  
 American Society of Clinical Oncology  
 American Staffing Association  
 Associated General Contractors of America  
 Association for Healthcare Philanthropy  
 Association of Corporate Counsel  
 Association of Private Sector Colleges and Universities  
 Automotive Aftermarket Industry Association  
 Brookings Institution

## EDUCATION

J.D., Catholic University of America, Columbus School of Law, 1996

B.A., Political Science, University of Pennsylvania, 1990

## MEMBERSHIPS

American Society of Association Executives

California Society of Association Executives

New York Society of Association Executives

The College Board  
Council on Foundations  
Cruise Lines International Association  
Foundation for the Malcolm Baldrige National Quality Award  
Goodwill Industries International  
Homeownership Preservation Foundation  
The Humane Society of the United States  
Independent Insurance Agents and Brokers of America  
LeadingAge  
Lions Club International  
Money Management International  
National Association of Chain Drug Stores  
National Athletic Trainers' Association  
National Coalition for Cancer Survivorship  
National Defense Industrial Association  
National Fallen Firefighters Foundation  
National Hot Rod Association  
National Propane Gas Association  
National Quality Forum  
National Retail Federation  
National Student Clearinghouse  
National Telecommunications Cooperative Association  
The Nature Conservancy  
NeighborWorks America  
New York Blood Center  
Peterson Institute for International Economics  
Professional Liability Underwriting Society  
Project Management Institute  
Public Health Accreditation Board  
Public Relations Society of America  
Recording Industry Association of America  
Romance Writers of America  
Texas Association of School Boards  
Trust for Architectural Easements  
Volunteers of America

## HONORS

Recognized as "Leading Lawyer" in the 2012 edition of *Legal 500*, Not-For-Profit

Listed in *The Best Lawyers in America 2012* for Non-Profit/Charities Law, Washington, DC (Woodward/White, Inc.)

Washington DC's Legal Elite, *SmartCEO Magazine*, 2011

Fellow, Bar Association of the District of Columbia, 2008-09

Recipient, American Bar Association Outstanding Nonprofit Lawyer of the Year Award, 2006

Recipient, *Washington Business Journal* Top Washington Lawyers Award, 2004

Recipient, The Center for Association Leadership Chairman's Award, 2004

Recipient, Greater Washington Society of Association Executives Chairman's Award, 1997

Legal Section Manager / Government Affairs Issues Analyst, American Society of Association Executives, 1993-95

AV® Peer-Review Rated by *Martindale-Hubbell*

Listed in *Who's Who in American Law* and *Who's Who in America*, 2005-present editions

## ACTIVITIES

Mr. Tenenbaum is an active participant in the nonprofit community who currently serves on the Editorial Advisory Board of the American Society of Association Executives' *Association Law & Policy* legal journal, the Advisory Panel of Wiley/Jossey-Bass' *Nonprofit Business Advisor* newsletter, and the ASAE Public Policy Committee.

He previously served as Chairman of the *AL&P* Editorial Advisory Board and has served on the ASAE Legal Section Council, the ASAE Association Management Company Accreditation Commission, the GWSAE Foundation Board of Trustees, the GWSAE Government and Public Affairs Advisory Council, the Federal City Club Foundation Board of Directors, and the Editorial Advisory Board of Aspen's *Nonprofit Tax & Financial Strategies* newsletter.

## PUBLICATIONS

Mr. Tenenbaum is the author of the book, *Association Tax Compliance Guide*, published by the American Society of Association Executives, and is a contributor to numerous ASAE books, including *Professional Practices in Association Management*, *Association Law Compendium*, *The Power of Partnership*, *Essentials of the Profession Learning System*, *Generating and Managing Nondues Revenue in Associations*, and several Information Background Kits. He also is a contributor to *Exposed: A Legal Field Guide for Nonprofit Executives*, published by the Nonprofit Risk Management Center. In addition, he is a frequent author for ASAE and many of the other principal nonprofit industry organizations and publications, having written more than 400 articles on nonprofit legal topics.

## SPEAKING ENGAGEMENTS

Mr. Tenenbaum is a frequent lecturer for ASAE and many of the major nonprofit industry organizations, conducting over 40 speaking presentations each year, including many with top Internal Revenue Service, Federal Trade Commission, U.S. Department of Justice, Federal Communications Commission, and other federal and government officials. He served on the faculty of the ASAE Virtual Law School, and is a regular commentator on nonprofit legal issues for *The New York Times*, *The Washington Post*, *Los Angeles Times*, *The Washington Times*, *The Baltimore Sun*, *Washington Business Journal*, *Legal Times*, *Association Trends*, *CEO Update*, *Forbes Magazine*, *The Chronicle of Philanthropy*, *The NonProfit Times* and other periodicals. He also has been interviewed on nonprofit legal issues on Voice of America Business Radio and Nonprofit Spark Radio.



## George E. Constantine

Partner

Washington, DC Office

T 202.344.4790 F 202.344.8300

[geconstantine@Venable.com](mailto:geconstantine@Venable.com)

### AREAS OF PRACTICE

Antitrust  
 Antitrust Investigations  
 Political Law  
 Tax-Exempt Organizations  
 Tax Controversies  
 Tax and Wealth Planning  
 Regulatory

### INDUSTRIES

Nonprofit Organizations and Associations  
 Credit Counseling and Debt Services

### BAR ADMISSIONS

Maryland  
 District of Columbia

### EDUCATION

J.D., University of Maryland School of Law, 1998

Recipient, Order of the Coif law school honors society

Recipient, Judge R. Dorsey Watkins Award for excellence in torts

B.A., Loyola College In Maryland,

George Constantine concentrates his practice exclusively on providing legal counseling to and advocacy for nonprofit organizations, including trade associations, professional societies, advocacy groups, charities, and other entities. He has extensive experience with many of the major legal issues affecting nonprofit organizations, including contracts, tax, antitrust, governance, and political activity matters.

Mr. Constantine has represented Internal Revenue Code § 501(c)(3), 501(c)(4) and 501(c)(6) clients on a number of critical tax-exemption matters, including representing clients that are undergoing Internal Revenue Service examinations challenging their exempt status; he has assisted associations and other nonprofit organizations going through mergers, consolidations, joint ventures, and dissolutions; and he has provided ongoing counseling on numerous transactional and governance matters that are unique to nonprofit organizations.

Mr. Constantine serves on the Legal Section Council of the American Society of Association Executives. In addition, Mr. Constantine is the former Staff Counsel of the American Society of Association Executives (ASAE), the 25,000-member national society for trade and professional association executives. As ASAE's sole staff attorney, he gained in-depth experience with the many legal issues facing associations. He also represented ASAE's interests before Congress and federal agencies. Mr. Constantine co-chairs Venable's Regulatory Practice Group.

### HONORS

Recognized in the 2012 edition of *Legal 500*, Not-For-Profit

### PUBLICATIONS

Mr. Constantine is the author of numerous articles regarding legal issues affecting associations and other nonprofit organizations published by ASAE, the Greater Washington Society of Association Executives, the American Chamber of Commerce Executives, the New York Society of Association Executives, and the Texas Society of Association Executives.

- July 12, 2012, Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies
- June 12, 2012, Nonprofit Contracts: Best Practices, Negotiation Strategies, Practical Tips and Common Pitfalls
- May 2012, Groups Sponsoring Electioneering Communications Must Disclose All Donors Pending Appeal of District Court Order
- May 2012, FCC Orders TV Stations to Post Their Political Files Online
- May 17, 2012, Nonprofit Contracts: Best Practices, Negotiation Strategies, Practical

## Tips, and Common Pitfalls

- May 2012, Representing Foreign Entities
- May 2012, Tax-Exempt Organizations the Focus of Upcoming Congressional Hearings
- April 26, 2012, Changes in Store for Group Tax Exemptions?
- January 10, 2012, Top Ten Things Every New Nonprofit General Counsel Should Know
- December 19, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- November 18, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- November 4, 2011, Top Ten Things a New Nonprofit General Counsel Should Investigate
- September 27, 2011, Protecting and Licensing Nonprofit Trademarks: Key Trademark and Tax Law Issues
- August 3, 2011, Could Your Nonprofit's Chapters Be Considered "Franchises" under State Law?
- Summer 2011, Grassroots Lobbying: A Legal Primer
- July 20, 2011, Related Foundations of Associations: Top Five Legal and Tax Pitfalls to Avoid
- February 2011, Recent IRS Determination Highlights Importance of Separation Among Affiliates
- December 16, 2010, So You Want To Be On The Internet<sup>®</sup>
- November 3, 2010, Cyberspace Risk: What You Don't Know Could Hurt You
- July 22, 2010, Lobbying for Your Agency: Avoiding the Tax and Legal Pitfalls
- May-June 2010, The IRS Tax-Exempt Examination Process
- April 27, 2010, IRS Provides Guidance to Nonprofits Assisting Homeowners
- April 9, 2010, Legal Traps of Internet Activities for Nonprofits
- March 30, 2010, D.C. Circuit Paves Way for Unlimited Contributions for Independent Expenditures
- March 2010, D.C. Circuit Paves Way for Unlimited Contributions for Independent Expenditures, Political Law Alert
- February 18, 2010, *Citizens United*: How the Supreme Court's Decision Will Impact Associations and Their Members
- January 2010, Supreme Court Strikes Down Laws Banning Corporate Expenditures, Political Law Alert
- October 6, 2009, Legal Traps of Internet Activities for Nonprofits
- July 16, 2009, Steering Clear of the Most Common Legal Hazards in Hotel, Convention Center, and Meeting Contracts
- March 3, 2009, Steering Clear of the Most Common Legal Hazards in Hotel, Convention Center, and Meeting Contracts
- September 22, 2008, The New IRS Form 990: What Does It Mean for Your Organization?
- May 19, 2008, The New IRS Form 990: What Does It Mean for Your Nonprofit Organization?
- March 4, 2008, The New IRS Form 990: What Does It Mean for Your Nonprofit Organization?
- February 15, 2008, Political Activity, Lobbying Law and Gift Rules Guide
- January 10, 2008, The Honest Leadership and Open Lobbying Act: New Lobbying and Ethics Rules
- June 13, 2007, Contracts - 10 Steps to a Better Contract
- November 2006, Pension Protection Act of 2006: Provisions of Interest to Exempt Organizations

- October 1, 2006, New Tax Law Establishes Additional Standards and Requirements for Credit Counseling Agencies
- September 7, 2006, Legal and Tax Issues for Nonprofit Associations
- January 2005, IRS Issues 'Virtual' Trade Show Guidance
- January 4, 2005, Characteristics of a Tax-Exempt Credit Counseling Agency
- October 27, 2004, New IRS Ruling Could Have Taxing Impact on 501(c)(3) Associations with Certification Programs
- August 10, 2004, Association Codes of Ethics: Identifying Legal Issues and Minimizing Risk
- April 16, 2004, Antitrust Concerns with Association Information Exchanges
- March 25, 2004, Untangling the Web - Internet Legal Issues for Associations
- November 4, 2003, Avoiding Association Tax Pitfalls in Cyberspace
- May 6, 2003, Summary of Provisions in S. 476 — The Charity Aid, Recovery, and Empowerment Act of 2003
- December 16, 2002, Good Governance — Ensuring That Your Association's Governing Documents Pass Legal Muster
- September 1, 2002, Association Activities Targeted in Recent Antitrust Enforcement Actions
- May 1, 2002, Corporate Sponsorship: The Final Regulations
- April 1, 2002, Associations and Campaign Finance Reform
- January 1, 2002, Recent Antitrust Decision on Salary Surveys Highlights Risks to Associations
- November 1, 2001, Legal and Tax Considerations for Capital Campaigns
- January - February 2001, New Campaign Finance Disclosure Law Hits the Wrong Target, *Journal of Taxation of Exempt Organizations*

## SPEAKING ENGAGEMENTS

Mr. Constantine is a frequent lecturer on association and tax-exemption organization legal topics, including corporate and tax issues.

- July 12, 2012, Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies
- June 13, 2012, "Starting and Sustaining a Nonprofit Organization" for the Washington, DC Economic Partnership
- June 12, 2012, Legal Quick Hit: "Nonprofit Contracts: Best Practices, Negotiation Strategies, Practical Tips, and Common Pitfalls"
- May 17, 2012, Nonprofit Contracts: Best Practices, Negotiation Strategies, Practical Tips, and Common Pitfalls
- May 2, 2012, "Risk and Reward – Keeping Your Tax-Exempt Status" for the Nonprofit Risk Management Center
- January 18, 2012, "Generating New Revenue Streams—Legal and Tax Issues for Nonprofit Organizations" at NYSAE Finance & Management Institute Luncheon
- January 10, 2012, Legal Quick Hit: "Top Ten Things Every New Nonprofit General Counsel Should Know"
- December 19, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- October 21, 2011, "IRS Group Exemption Procedures" for ABA
- September 27, 2011, Webcast: "Protecting and Licensing Nonprofit Trademarks: Key Trademark and Tax Law Issues" for the Association of Corporate Counsel's Nonprofit Organizations Committee
- July 20, 2011, "Related Foundations of Associations: The Top Five Legal and Tax Pitfalls to Avoid" for the Association Foundation Group
- June 22, 2011, "Play on Natural Turf: Authentic and Transparent Grassroots Lobbying" for the American Society of Association Executives

- May 12, 2011, "Starting and Sustaining the Growth of a Nonprofit Organization" for the Washington, DC Economic Partnership Program
- November 12, 2010, Protecting Your Association from Cyber Attacks and Financial Fraud
- November 3, 2010, "Cyberspace Risk: What You Don't Know Could Hurt You," Nonprofit Risk Management Center
- September 13, 2010, "Board Leadership: Legal Issues" at Greater DC Cares Nonprofit Board Leadership Program
- July 22, 2010, "Lobbying for Your Agency: Avoiding the Tax and Legal Pitfalls" at the Association of Independent Consumer Credit Counseling Agencies Summer 2010 Conference
- June 8, 2010, Legal Quick Hit: "Lessons in Tax Compliance: The Broad Impact of the IRS' Interim Report on the Colleges and Universities Compliance Project" for the Association of Corporate Counsel's Nonprofit Organizations Committee
- April 9, 2010, "Legal Traps of Internet Activities for Nonprofits" a Lorman Teleconference
- March 16, 2010, The Form 990: Dealing with the Fall Out (Audioconference)
- February 18, 2010, *Citizens United*: How the Supreme Court's Decision Will Impact Associations and Their Members
- February 18, 2010, "Legal Issues 2010: Keeping Your Association Out of Trouble" for the American Association of Medical Society Executives
- October 13, 2009, "Risk Management for Events and Meetings" course at the George Washington University's School of Business
- October 13, 2009, Presentation on meeting contracts to George Washington University students
- October 6, 2009, Legal Traps of Internet Activities for Nonprofits
- July 16, 2009, Steering Clear of the Most Common Legal Hazards in Hotel, Convention Center, and Meeting Contracts
- July 16, 2009, Steering Clear of the Most Common Legal Hazards in Hotel, Convention Center and Meeting Contracts: A Roadmap for Nonprofits
- March 3, 2009, Steering Clear of the Most Common Legal Hazards in Hotel, Convention Center and Meeting Contracts
- February 24, 2009, Legal Issues for Nonprofit Associations
- October 1, 2008, The New IRS Form 990: What Does it Mean for Your Organization?
- September 22, 2008, The New IRS Form 990: What Does It Mean for Your Nonprofit Organization?
- May 19, 2008, New IRS Form 990 Audio conference
- January 10, 2008, The Honest Leadership and Open Lobbying Act: New Lobbying and Ethics Rules
- November 5, 2007, American Public Health Association Annual Meeting
- September 28, 2007, Annual Association Law Symposium
- June 13, 2007, Contracts - 10 Steps to a Better Contract
- September 7, 2006, Legal and Tax Issues for Nonprofit Associations
- February 10, 2004, American Society of Association Executives Winter Conference
- November 4, 2003, Avoiding Association Tax Pitfalls in Cyberspace
- October 3, 2003, American Society of Association Executives 2003 DC Legal Symposium
- August 25, 2003, American Society of Association Executives' Annual Meeting
- April 17, 2003, Board Fiduciary Duties
- March 13, 2003, Protecting Your Chamber's Intellectual Property
- March 7, 2003, The Ins and Outs of Nonprofit Liability
- February 7, 2003, Legal and Tax Aspects of Raising Non-Dues Revenue
- December 10, 2002, ASAE 2002 Winter Conference



## Janice M. Ryan

Associate

Washington, DC Office

T 202.344.4093 F 202.344.8300

[jryan@Venable.com](mailto:jryan@Venable.com)

### AREAS OF PRACTICE

Political Law  
Tax-Exempt Organizations  
Legislative and Government Affairs

### INDUSTRIES

Nonprofit Organizations and Associations

### GOVERNMENT EXPERIENCE

Legislative Assistant, United States Senate, Office of Senator Patrick Leahy (D-VT)

### BAR ADMISSIONS

District of Columbia  
Maryland

### COURT ADMISSIONS

U.S. Tax Court

### EDUCATION

J.D., *summa cum laude*, Catholic University of America, Columbus School of Law, 2008

Associate Editor, *The Catholic University Law Review*

Janice Ryan is an associate in the firm's Regulatory Affairs Practice Group, where she focuses her practice on counseling trade and professional associations, public charities, private foundations, and other nonprofits on a wide variety of legal topics, including tax exemption, corporate governance, antitrust, transactional, and political activities matters. Ms. Ryan also advises for-profit and nonprofit clients on all aspects of state and federal political law, including campaign finance, lobbying disclosure, gift and ethics rules, pay-to-play laws, and tax implications of political activities. Ms. Ryan develops comprehensive political compliance programs tailored to clients' needs, and assists clients to implement those programs on an ongoing basis.

Previously, Ms. Ryan served as a Legislative Assistant to U.S. Senator Patrick Leahy (D-VT), where she handled health care, education, human services, and food and nutrition policy matters.

### PUBLICATIONS

- July 12, 2012, Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies
- May 2012, Groups Sponsoring Electioneering Communications Must Disclose All Donors Pending Appeal of District Court Order
- May 2012, FCC Orders TV Stations to Post Their Political Files Online
- May 2012, Representing Foreign Entities
- May 9, 2012, The Top Ten Things You Need to Know about the New District of Columbia Nonprofit Corporation Act
- May 8, 2012, Election Year Issues for 501(c)(3) Organizations
- March 14, 2012, Four Ways Corporations Can Participate in Federal Elections, *Inside Counsel*
- March 2012, Forming a Corporate Political Action Committee
- January 2012, Forming an Association Political Action Committee
- December 19, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- December 13, 2011, The Nuts and Bolts of Lobbying for 501(c)(3) and 501(c)(6) Exempt Organizations
- November 18, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- February 2011, Understanding Force Majeure Clauses
- January 2010, Supreme Court Strikes Down Laws Banning Corporate Expenditures, Political Law Alert

Recipient, The John L. Garvey  
Faculty Award

A.B., Dartmouth College, 2000

## MEMBERSHIPS

American Bar Association

Maryland State Bar Association

## SPEAKING ENGAGEMENTS

- July 12, 2012, Nonprofit Chapters and Affiliates: Key Legal Issues, Pitfalls and Successful Strategies
- May 8, 2012, Legal Quick Hit: "Election Year Issues for 501(c)(3) Organizations" for the Association of Corporate Counsel's Nonprofit Organizations Committee
- May 3, 2012, "Hot Topics - The District of Columbia Nonprofit Corporation Act of 2010" at AFG's 10th Annual National Conference on Association Foundations & Fundraising
- February 16, 2012, "Everything You Need to Know to Comply With The New D.C. Nonprofit Corporation Act" at West, Lane & Schlager Realty Advisors Applied Knowledge Lunch Series
- December 19, 2011, The New D.C. Nonprofit Corporation Act Takes Effect on Jan. 1, 2012: Everything You Need to Know to Comply
- December 13, 2011, "The Nuts and Bolts of Lobbying for 501(c)(3) and 501(c)(6) Exempt Organizations" for CooperationWorks!

VENABLE<sup>®</sup><sub>LLP</sub>

# **Additional Information**

## Articles

April 26, 2012

### Changes in Store for Group Tax Exemptions?

#### AUTHORS

George E. Constantine

#### RELATED INDUSTRIES

Nonprofit Organizations  
and Associations

#### ARCHIVES

2012 2008 2004  
2011 2007 2003  
2010 2006 2002  
2009 2005

Related Topic Area(s): Tax and Employee Benefits

There has been much news related to group exemptions for tax-exempt organizations in recent months, from an influential advisory committee suggesting last summer that group returns be jettisoned to an announcement from the Internal Revenue Service ("IRS") early this year that it plans to send out questionnaires to group exemption holders to see how they are complying with applicable law while maintaining their group exemptions.

When one considers that approximately 500,000 organizations have tax-exempt status by virtue of inclusion on a group exemption letter, it becomes clear just how broad an impact any tinkering with the rules or heightened enforcement may have on associations and other nonprofits. In light of the recent focus, now is a good time for associations that hold group exemptions or wish to obtain a group exemption to take a close look at the existing requirements.

#### Background

The IRS's group exemption process allows a "central" tax-exempt organization to have more than one "subordinate" organization to be considered an exempt organization without the need for each subordinate to file for and obtain recognition of exempt status from the IRS. In the association community, a group exemption is frequently used by a national organization to permit its chapters to have the benefits of exempt status without need for the completion and filing of multiple application forms. Historically, the IRS began allowing such group exemptions as far back as 1940, although no formal procedures were established for obtaining group exemption until 1968.

At present, the rules of the road for obtaining and maintaining group exemption recognition are set forth in a 1980 Revenue Procedure (Rev. Proc. 80-27, 1980-1 C.B. 677). According to the requirements of this Revenue Procedure, at the outset, it is necessary for a central organization to first have its own exempt status recognized by the IRS. Note that associations which are exempt under Internal Revenue Code § 501(c)(6) are permitted to "self-certify" as exempt without obtaining specific recognition. Those self-certifiers would not, however, qualify to serve as central organizations.

Other threshold matters for consideration by organizations that would seek to obtain a group ruling are: no subordinates that are organized and operated in a foreign country may be included in a group exemption letter and no IRC § 501(c)(3) private foundation may be included as a subordinate. Finally, subordinates that are included in a group exemption letter should not apply separately for recognition of exempt status.

In general, the structure envisioned by the group exemption process is one in which the central organization is putting itself in the place of the IRS when it comes to a determination of whether its subordinates are operating consistent with tax-exempt status. In this role, the central organization will essentially take on the legal duty of ensuring that its chapters/subordinates are operating consistent with the exempt status being sought. Thus, oversight should be exerted by the central organization over the subordinates to ensure ongoing compliance.

In order to obtain group exemption recognition, the central organization must establish that the subordinates that it wishes to include in the letter are: (1) affiliated with it; (2) subject to its general supervision or control; (3) all exempt under the same section of the IRC; (4) not private foundations (in the case of § 501(c)(3) group exemptions); (5) all on the same accounting period as the central organization if they are to be included in a group return; and (6) organizations that have been formed within the 15-month period prior to the date of the submission of the group exemption application (in the case of § 501(c)(3) organizations).

As part of the group exemption application process, each subordinate is required to authorize the

central organization to include it in the application for the letter. The authorization must be signed by a duly authorized officer of the subordinate and retained by the central organization while the group exemption letter is in effect.

According to the Revenue Procedure, the application should set forth information that verifies the relationship between the central organization and its subordinates, a sample copy of a subordinate's governing instruments, a detailed description of the purposes and activities of the subordinates (including sources of receipts and nature of expenditures); a list of the subordinates to be included in the list; and certain signed affirmations. It should be noted that in practice the IRS recently has sought more detail than what one might expect is necessary based on the wording of the Revenue Procedure. For instance, the IRS will usually request not just a "sample" copy of a subordinate's governing instruments, but rather copies of all subordinate governing instruments.

To maintain the group exemption, the central organization must submit an annual report to the IRS (at least 90 days before the close of its fiscal year) confirming that the subordinates are still active and included in the group exemption, adding or deleting any affiliates as appropriate, and detailing any significant changes in the purposes, character, or method of operation of the subordinates.

Finally, separate and apart from the annual reporting required by the group exemption rules, both the central organization and its covered affiliates must comply with the IRS's annual Form 990 filing requirements. In this regard, the central organization may (but is not required to) file a group Form 990 for its covered subordinates on a consolidated basis. Because the central organization must file its own Form 990, this process results in two federal returns—one for the parent and one for all affiliates under the group exemption that elect to be included in the group return.

### **Recent Developments**

It is possible that the above-described regime will be in for some changes in the near future. Practitioners have noted anecdotal instances of increased hesitancy on the part of IRS to approve group exemption applications; further, the ACT Report included a number of suggestions for changes, and one of the IRS's own officials stated publicly in reaction to that report that the group exemption option may no longer make sense.

The ACT Report specifically recommended that the group return option may no longer be consistent with the IRS's stated goals of enhancing transparency, accountability, and responsibility in the exempt organization arena. Specifically, group returns are not able to reflect, for example, an individual subordinate organization's compensation levels.

While the ACT Report recommended removal of the group return option, it came out in support overall of retaining the group exemption option—citing the tremendous burden of requiring a separate application for recognition of exempt status for the hundreds of thousands of subordinates and pointing out the unique and virtually insurmountable transition issues that would arise. The ACT Report does recommend some changes to the process, though. Specifically, it suggests that the IRS update its 32-year-old Revenue Procedure so that it: (1) better defines what is meant by "supervision or control"; (2) excludes certain types of supporting organizations; and (3) allows for retroactive recognition for any subordinate that was formed within 27 months of its application (rather than the current 15-month lookback period). In addition, the ACT Report recommends that the IRS find a way to include on its master list of § 501(c)(3) organizations that are eligible to receive tax-deductible contributions those subordinates that have been identified in a group exemption.

While officials at the IRS have not made any further remarks calling into question the continued existence of the group exemption option, there was an announcement in the IRS 2012 work plan indicating that the IRS is preparing a questionnaire for completion by group exemption holders. The IRS has in the past used the compliance questionnaire as a means of determining whether a more comprehensive enforcement regime should be conducted. The IRS ties this focus not just to the recently released ACT Report, but also to the automatic revocations that have only recently begun to come to light as a result of the 2006-enacted IRC § 6033(j). That section of the IRC mandates that organizations which fail to file annual Forms 990 for three consecutive years will have their tax-exempt status automatically revoked. The initial wave of automatic revocations shows that a large number of group exemption subordinates were among those that were revoked.

### **Conclusion**

In light of the current focus on group exemptions, those associations with group exemptions in place should take a close look at their current procedures to ensure they will stand up to scrutiny. Those procedures should include some form of annual reporting from the subordinates/chapters to ensure that

activities are consistent with exemption. The annual reporting might include a brief description of program achievements from the previous year, information regarding receipts and expenditures, and information about directors and officers. In addition, the national organization should take affirmative steps to ensure that Form 990, corporate reporting, and other administrative compliance steps are being taken by each chapter.

---

*For more information, please contact George Constantine at [geconstantine@Venable.com](mailto:geconstantine@Venable.com).*

*The author is an attorney in the law firm of Venable LLP. This article is not intended to provide legal advice or opinion and should not be relied on as such. Legal advice can only be provided in response to specific fact situations.*

<sup>1</sup> Advisory Committee on Tax Exempt and Government Entities. "Exempt Organizations: Group Exemptions—Creating a Higher Degree of Transparency, Accountability, and Responsibility," June 15, 2011. Available at: [http://www.irs.gov/pub/irs-tege/tege\\_act\\_rpt10.pdf](http://www.irs.gov/pub/irs-tege/tege_act_rpt10.pdf). This report includes an in-depth and informative look at both the history of the group exemption process and the current implementation by the IRS. (This report will hereinafter be referred to as the "ACT Report.")

<sup>2</sup> Note that the subordinates could all be exempt under a different set of the IRC than the central organization. For instance, a § 501(c)(3) central organization may obtain group exemption recognition under § 501(c)(6) for its chapters.

<sup>3</sup> If the application is for a § 501(c)(3) group exemption and the chapters/subordinates have been in existence for longer than 15 months, a group exemption letter still may be issued, but only if all subordinates are willing to be recognized as exempt from the date of the application.

<sup>4</sup> "IRS Considers Changes in Disclosure Rules for Many Groups," *Chronicle of Philanthropy*, June 15, 2011, citing a statement by IRS's Holly Paz. Available at: <http://philanthropy.com/article/IRS-Considers-Changes-in/127922/>.

<sup>5</sup> ASAE has taken an active role in connection with the group exemption issue, filing comments to the IRS in response to the ACT Report. In its comments, ASAE favors retention of the group return option. Further, ASAE expresses strong support for the retention of the group exemption option generally. ASAE's comments are available at: <http://www.asaecenter.org/files/Group%20Exemption%20Letter%207-11.pdf>

<sup>6</sup> See [http://www.irs.gov/pub/irs-tege/fy2012\\_eo\\_work\\_plan\\_2011\\_annrpt.pdf](http://www.irs.gov/pub/irs-tege/fy2012_eo_work_plan_2011_annrpt.pdf).

## AUTHORS

Setareh Deljo-Roland  
George E. Constantine  
Jeffrey S. Tenenbaum

## RELATED INDUSTRIES

Nonprofit Organizations  
and Associations

## ARCHIVES

2012 2008 2004  
2011 2007 2003  
2010 2006 2002  
2009 2005

## Articles

August 3, 2011

### Could Your Nonprofit's Chapters Be Considered "Franchises" under State Law?

Related Topic Area(s): Antitrust and Trade Regulation

A recent U.S. Court of Appeals for the Seventh Circuit decision held that the national Girl Scouts organization violated a Wisconsin franchise law when it attempted to take away territory from a local chapter as a part of the national organization's broader plan to reorganize local council boundaries. In this case, *Girl Scouts of Manitou Council, Inc. v. Girl Scouts of the United States of America, Inc.*, the Manitou council sought to enjoin the national organization from transferring all of its territory in Wisconsin, arguing that the local Manitou chapter (called a "council") was a "dealer" under Wisconsin law and that such action would be violating the Wisconsin Fair Dealership Law without good cause. While the transfer of all of the Manitou council's territory would not have served to dissolve the Manitou council as an entity, it would have prevented it from representing itself as a Girl Scouts organization and from otherwise using Girl Scouts trademarks, which the Court characterized as a "constructive termination."

#### Background

The Girl Scouts of the United States of America, Inc. is a nonprofit organization that was founded in 1912 and incorporated in 1950 by an Act of Congress. In 2004, a time when there were over 300 local Girl Scout councils across the country, the national organization determined it would cut back drastically the number of local councils and expand the surviving councils' boundaries. Each council is party to a charter agreement. According to the Court's decision, the agreement with the Manitou council did not permit the national organization to change its territory at the time the national organization attempted to take away the council's territory, though the council had agreed to be subject to a rule that allowed the national organization to have the final say over "all matters concerning jurisdictional lines."

The Court noted that the Manitou council and the national Girl Scouts organization relied heavily on the sale of cookies and other merchandise for fundraising.

#### Wisconsin Law

The Wisconsin Fair Dealership Law forbids a franchisor from terminating, canceling, failing to renew, or substantially changing "the competitive circumstances of a dealership agreement without good cause." A "dealer" is defined as a "grantee of a dealership" and the applicable "dealership" definition is an agreement that grants "the right to sell or distribute goods or services, or use a trade name, trademark, service mark, logotype, advertising, or other commercial symbol, in which there is a community of interest in the business of offering, selling or distributing goods or services."

#### The Court's Decision

In response to the Manitou council's lawsuit, the national organization raised several arguments which were each dismissed by the Court, the first of which was that the national organization's first amendment right of free expression would be violated if it wasn't allowed to reorganize. The Court then disagreed with the national organization's argument that the Wisconsin law does not apply to nonprofit entities due to an absence of commercial activities; the Court said that nonprofits often engage in commercial activities and that the Girl Scouts definitely do, stating that, "[f]rom a commercial standpoint, the Girl Scouts are not readily distinguishable from a Dunkin' Donuts." The Court also rejected other arguments from the national organization attempting to show it was exempt from the state law. Ultimately, the Court held that although the national organization's board of directors had the authority in its chartering agreement with the Manitou council to make final decisions "in all matters concerning jurisdictional lines," when attempting "to use that authority to terminate the franchise altogether," the national organization violated the Wisconsin Fair Dealership Law which, as mentioned

above, requires "good cause" to terminate a "dealership."

### **The Impact of this Decision**

While the facts involved in this case are somewhat unique – given how significant and recognizable the Girl Scouts' cookie sales and other activities are – the decision of the Court was a broad one that could be construed as applying to more traditional nonprofits that may have less visible commercial activities. The contractual relationship between the Girl Scouts and its councils (which the Court viewed as akin to that of "franchisor to franchisee") appears to be very similar to relationships that associations and other nonprofit organizations have with their state and local chapters and other affiliates. As a result, this decision may pave the way for state dealership and franchise laws to be imposed on nonprofit organizations' relationships with their chapters and affiliates. Approximately 20 states have dealership or franchise laws that could now come into play for nonprofit organizations across the country.<sup>1</sup>

Consequently, nonprofit organizations with chapters should review their organizational structure, charter agreements, and related documentation, as well as state dealership and franchise laws, to determine whether changes to these documents may be necessary or prudent.

\* \* \* \* \*

<sup>1</sup>Matthew Moloshok, "Constraints Against Termination of Dealers and Franchisees," *The Antitrust Source*, (2005), 5; and ABA Section of Antitrust Law, *Franchise and Dealership Termination Handbook* (2004), App. A.

\* \* \* \* \*

For more information, please contact the authors at [sdeljo-zargarani@venable.com](mailto:sdeljo-zargarani@venable.com), [geconstantine@venable.com](mailto:geconstantine@venable.com), [jstenenbaum@venable.com](mailto:jstenenbaum@venable.com), or at 202-344-4000.

*This article is not intended to provide legal advice or opinion and should not be relied on as such. Legal advice can only be provided in response to a specific fact situation.*

## AUTHORS

George E. Constantine

## RELATED PRACTICES

Tax Policy

Tax-Exempt Organizations

## RELATED INDUSTRIES

Nonprofit Organizations  
and Associations

## ARCHIVES

2012 2008 2004

2011 2007 2003

2010 2006 2002

2009 2005

## Articles

February 2011

### Recent IRS Determination Highlights Importance of Separation Among Affiliates

Related Topic Area(s): Miscellaneous, Tax and Employee Benefits

*This article was originally published in the February 2011 edition of Association Law and Policy.*

A recent action by the Internal Revenue Service highlights the importance of maintaining separateness between an association and its affiliates, particularly with regard to how the entities are portrayed to the public through the Internet.

#### Background

It has long been understood that related entities could be at risk of a court or the IRS disregarding the separateness between the two entities, even though each entity may have separate corporate and tax statuses, thus creating exposure to potential legal and tax liability to both entities. In such instances, the legal and tax liabilities of a foundation (for example) could become the legal and tax liabilities of its related association, a result which could place the association at greater financial and legal risk. In determining whether to disregard the separateness of two entities, whether with regard to potential corporate or tax liability, courts apply state-based common law (often called "piercing the corporate veil").<sup>1</sup>

A parent corporation and its subsidiaries generally will be considered separate entities for federal income tax purposes as long as the subsidiary is incorporated for purposes which are the equivalent of business activities or the subsidiary subsequently carries on business activities. Thus, if an entity is organized with a bona fide intention that it will have some "real and substantial business function, its existence may not generally be disregarded for tax purposes." However, if one entity so controls the affairs of a subsidiary that it "is merely an instrumentality of the parent, the corporate entity of the subsidiary may be disregarded."<sup>2</sup>

The general presumption has always been that corporate separateness should be honored, except in extreme circumstances. A determination about whether two organizations' corporate separateness should be disregarded is fact-specific; courts over the years have looked to the following key factors to determine whether two entities are truly separate for tax or liability purposes:

1. Inadequate capitalization of the subsidiary given its business goals and operations;
2. Financial support of the subsidiary's operations by the parent;
3. A joint accounting and payroll system;
4. The subsidiary's lack of substantial business contacts with any except the parent;
5. Commingling of assets;
6. Reference to the subsidiary in financial statements as a division of the parent or to the fact that the subsidiary's obligations are those of the parent;
7. The property of the corporations is used by each entity as if jointly owned;
8. Failure to follow corporate organizational requirements:
  - A. No meetings of directors;
  - B. Failure to elect officers;
  - C. Failure to file annual reports or other required governmental reports;
  - D. Failure of the directors or management to approve and control corporate activities;
  - E. Failure to maintain minutes of meetings; and
  - F. Inadequate allocation of costs and expenses.

As a practical matter, the IRS and courts are very hesitant to attribute the activities of an affiliate to a parent organization or vice versa.<sup>3</sup> In general, the IRS has taken the position that the activities of a

separately incorporated subsidiary cannot ordinarily be attributed to its parent organization unless the facts provide “clear and convincing evidence that the subsidiary is in reality an arm, agent or integral part of the parent.”<sup>4</sup>

In short, the current state of the law demonstrates that certain common-sense steps can and should be taken to preserve the separateness between an association and its related foundation or taxable subsidiary, and after doing so the risks of having the separateness disregarded can be managed adequately. For instance, while it is generally understood that a majority or all of the directors of the affiliate may be named or appointed by the parent, many organizations will seek to avoid substantial (i.e., majority) overlap of individuals serving on both entities’ boards of directors.<sup>5</sup> Also, associations should establish written agreements among affiliates to properly allocate expenses for any shared equipment and services, as well as to address use of trademarks and other intellectual property. Further, it is important that associations properly manage the manner in which communications and activities are attributed, so that it can be clearly understood which entity is responsible for the communication or activity.

### **Recent Technical Advice Memorandum**

A recent IRS Technical Advice Memorandum (“TAM”),<sup>6</sup> highlights the importance of remaining vigilant about maintaining separateness among affiliates. The TAM involved a website shared by an organization exempt from federal taxation under Section 501(c)(3) of the Internal Revenue Code (“IRC”) and its subsidiary affiliate exempt under IRC Section 501(c)(4). Pursuant to federal tax law, a 501(c)(3) organization is strictly prohibited from engaging in political campaign activities; such activities are, however, permissible for 501(c)(4) organizations. At issue in the TAM was whether, due to the affiliates’ shared website, the IRS would attribute the political campaign communications of the 501(c)(4) organization to the 501(c)(3) organization, thereby potentially jeopardizing the parent 501(c)(3) organization’s tax-exempt status.

In order to avoid certain technical problems and duplicative costs associated with maintaining separate websites, a decision was made to house the 501(c)(4) organization’s website within the 501(c)(3) organization’s website. The affiliated organizations underwent an expense allocation process to ensure that the 501(c)(4) organization paid for its share of expenses associated with the site. In addition, each web page that was being used by the 501(c)(4) affiliate had a heading that included the 501(c)(4) organization’s name. However, there were a number of aspects of the website arrangement that the IRS cited as blurring the line between the two affiliates. Notably:

- Every web page in the 501(c)(3) organization’s website, including those pages reserved for use by the 501(c)(4) organization, contained a banner with the 501(c)(3) organization’s logo and electronic links along the top, left side, and bottom;
- Every web page in the 501(c)(3) organization’s website, including those pages reserved for use by the 501(c)(4) organization, included a disclaimer notice and a copyright notice for the 501(c)(3) organization;
- The only visual distinction between the 501(c)(3) organization’s pages and the 501(c)(4) affiliate’s pages was the inclusion of the 501(c)(4)’s logo and address on the top banner, below the name and logo of the 501(c)(3) parent.

Based on the IRS’s description of the shared website, it appears that the 501(c)(3) organization used a template for all pages, which enabled a consistent layout and graphic design across the site with differing content appearing inside the 501(c)(3) “frame.” Given the fact that the 501(c)(4) pages looked “virtually indistinguishable” from the 501(c)(3) pages, the IRS concluded that it would treat the statements and communications on those pages as the communications and statements of the 501(c)(3) organization, with potentially significant adverse tax consequences to the 501(c)(3). In effect, the IRS states in the TAM that appending the 501(c)(4) affiliate’s name and logo to the 501(c)(3) frame is not sufficient to separate the 501(c)(4) organization’s content from the rest of the 501(c)(3) site.

### **Lessons Learned**

The key point to take away from this TAM is not that the IRS has reworked its position with regard to the separateness of affiliated entities. All of the common sense steps that associations take to manage risks in this regard should continue to be taken. Nonetheless, this decision highlights the importance of remaining vigilant about maintaining separateness among affiliates, particularly when it comes to websites. Very often an association will share its base URL with its affiliates and provide links within its website to its affiliates. When doing so, an association should take care to ensure that

those affiliate pages are not substantially similar to the association pages in design and appearance. The casual visitor to the site should be able to easily recognize that the page being viewed is for an organization separate from the association. These lessons can and should be applied across all activities and projects of an association and its affiliate—whether online or not. Clear branding of each entity's programs and activities is a vital component of effectively maintaining affiliated entities' separate legal status.

####

**George E. Constantine, III** is a partner in the nonprofit organizations practice at Venable LLP. He can be reached at 202-344-4790 or [geconstantine@venable.com](mailto:geconstantine@venable.com)

This article also appeared in the Annual Legal Review section of the March 17, 2011 issue of Association TRENDS. To read the entire section, visit the [Association TRENDS website](#).

<sup>1</sup> See, e.g., *Moline Properties, Inc. v. Comm'r*, 319 U.S. 436, 439 (1943) (holding that, for income tax purposes, a taxpayer cannot ignore the form of the corporation that he creates for a valid business purpose or that subsequently carries on business, unless the corporation is a sham or acts as a mere agent).

<sup>2</sup> IRS Priv. Ltr. Rul. 2002-25-046 (Mar. 28, 2002), citing *Moline Properties*, 319 U.S. at 438; *Britt v. United States*, 431 F. 2d 227, 234 (5th Cir. 1970); and *Krivo Indus. Supply Co. v. National Distillers and Chem. Corp.*, 483 F.2d 1098, 1106 (5th Cir. 1973).

<sup>3</sup> See Rev. Rul. 58-293, 1958-1 C.B. 146 (holding that a bar association recognized as exempt under Section 501(c)(6) of the Internal Revenue Code ("IRC") may form a separate and related IRC Section 501(c)(3) fund); see also, IRS Priv. Ltr. Rul. 2001-32-040 (Aug. 13, 2001) (holding that the formation and operation by an IRC Section 501(c)(3) organization of a wholly-owned for-profit subsidiary will not give rise to concerns about the separateness of the two entities).

<sup>4</sup> IRS Priv. Ltr. Rul. 2001-32-040 (Aug. 13, 2001).

<sup>5</sup> Note, however, that even where a subsidiary's board is solely comprised of directors from the parent organization, separateness may still be honored. See, e.g., I.R.S. Gen. Couns. Mem. 39,776 (Feb. 6, 1989). Furthermore, IRC Section 509(a)(3) specifically contemplates that an IRC Section 501(c)(3) supporting organization to an IRC Section 501(c)(6) parent organization will have at least a majority of its directors appointed by the parent organization.

<sup>6</sup> IRS Tech. Adv. Mem. 2009-08-050 (Feb. 20, 2009).