



Beware! Self-Dealing and the Corporate Foundation

Corporate, Securities, and Governance



CHEAT SHEET

- **Asset sharing.** For shared office space and equipment, the foundation and the corporation should have separate agreements with the third-party owner or vendor. If the corporation is the owner, then the space or equipment must be donated to the foundation.
- **Dual employees.** Payment for professional and managerial personnel services from the corporation that are necessary for the accomplishment of a foundation's charitable purposes are an exception to self-dealing. This includes accounting and legal services but not janitorial or secretarial services.
- **Galas.** The corporation, not the corporate foundation, should make the donation to a charity gala if it provides benefits such as free admissions, discounts, or other benefits that are not available for free to the general public.
- **Intangible benefits.** Benefits that are incidental, like an enhanced reputation, or tenuous — a

manger of a private foundation who is also an officer at a public charity — are not considered self-dealing.

Many corporations have focused charitable activities within a corporate foundation to better manage their charitable giving. With such a close connection between a corporate foundation and its related corporation's business, there is potential for inadvertent self-dealing, whether it's distributing foundation-sponsored tickets to members of the corporation or charging the foundation for its share of office space. Generally, acts of self-dealing between a private foundation and its substantial contributors (such as the related corporation) are subject to severe excise taxes, with few exceptions. As a result, careful planning must be undertaken regarding any proposed transaction between the related business and the foundation.

There is no work-around where the related business owns the space; use of the space must be donated to the foundation or the foundation should lease an office elsewhere.

Sharing of assets

Corporate foundations and their founding companies often share office space, equipment, supplies, and similar items. Under the private foundation rules, when a disqualified person, such as the founding business, furnishes goods or services without charge to a private foundation, self-dealing is not a concern. However, when the foundation reimburses the corporation for the use of office space, supplies, and equipment, it is considered self-dealing.

Methods for addressing shared office space, equipment, and supplies will depend on the ownership of these amenities. If a third party owns the office space, then separate leasing arrangements with and direct payments to a landlord will be workable. There is no work-around where the related business owns the space; use of the space must be donated to the foundation or the foundation should lease an office elsewhere.

With equipment and supplies, the same rationale applies. Leases from the corporation to the private foundation (other than a no-cost lease) or reimbursement arrangements present self-dealing concerns. With respect to these matters the parties effectively have two choices: (1) either the corporation can donate the use of the equipment and supplies to the private foundation, or (2) the private foundation can directly engage with third-party vendors to buy or lease equipment and supplies.

Sharing of employees

Generally, the payment of compensation or reimbursement by a private foundation to a related corporation is an act of self-dealing. There is a narrow exception to this rule for compensation of or reimbursement for personal services that are professional and managerial in nature and necessary to accomplish a foundation's charitable purposes. This exception to self-dealing applies to investment, banking, accounting, and legal services. It has also been extended to other professional services, including real estate management services, tax coordination services, and anthropological and archeological services. The exception does not apply to janitorial, repair, and maintenance services,

or to secretarial services. Payment to the related corporation for these types of services would result in self-dealing.

While some foundations take the position that the services of their executive directors and other staff fall within the professional and managerial exception, there is a risk with this position. Because the exception is to be narrowly construed, there would be a risk to a company that it would be engaging in self-dealing if its related foundation reimburses it for services of the company's employees that the IRS does not consider to be professional and managerial. Many companies instead simply donate the services of their employees to the corporate foundation. It is also possible for the foundation to establish a separate payroll and benefits system through which it compensates its workers directly.

Gala tickets

With corporate foundations, being a sponsor of a charity's gala can create difficulties under the self-dealing rules. For example, at a fundraising event, sponsoring the event may include purchasing an event table with tickets to the charity event. Tickets to a fundraising event have economic value, which generally is the fair market value of the goods and services provided. Donors generally must reduce the amount of any charitable contribution deduction taken in connection with a gift that yields benefits with economic value by the amount of that value.

The receipt of these donor benefits is more complicated in the private foundation setting. The self-dealing rules applicable to private foundations generally provide that it is an act of self-dealing for disqualified persons to receive tangible economic benefits that flow from foundation grants. Thus, the private foundation rules generally bar disqualified persons from using tickets that are made available as a result of foundation grants, unless they are attending for a necessary business purpose.

For example, when it is necessary for foundation officers or directors to attend an event to monitor the manner in which the foundation's funds have been spent, use of the tickets by the foundation directors and officers does not constitute self-dealing. Spouses, other relatives, and friends of these disqualified persons are not covered by the exception to the self-dealing rules, and should not be using foundation-sponsored tickets.

If a donation to a charity provides benefits such as free admissions, discounts, or benefits not otherwise available for free to the general public, then the business should make the donation, not the corporate foundation. If, however, the foundation declines all benefits to be received with respect to the grant or donation, or distributes the tickets only to foundation employees who can meet the business purpose exception, then the corporate foundation can make the donation without fear of running afoul of the self-dealing rules. Some private foundations make a practice of donating tickets back to the charity that issues them, but it is simplest to refuse to accept the tickets in the first place.

Note, too, that the IRS does not allow bifurcation of the cost of attending the event. For the purpose of the self-dealing rules, the IRS takes the position that it is not possible to separate the price of a ticket into its charitable and noncharitable components. In other words, a private foundation cannot avoid the self-dealing problem by having the related corporation pay for the cost of the dinner or other tangible benefits and having the foundation pay the charitable portion of the ticket. The reasoning behind this IRS position appears to be that the foundation is relieving a related person from a financial obligation that it would otherwise incur. The IRS has found that such "bifurcation" would constitute an act of self-dealing, because the corporate foundation's payment of the charitable contribution portion of the fundraising event cost would result in a direct economic benefit to the corporation, since the corporation would be relieved of its obligation to pay that portion.

Incidental and tenuous benefits

As a result of the relationship between a corporate foundation and its related business, there will be certain goodwill and intangible benefits received by the for-profit corporation by virtue of having a corporate foundation. The self-dealing rules allow for these types of benefits, provided they are merely “incidental and tenuous.” An enhanced reputation of a person or business is not considered self-dealing under this exception. A private foundation that makes a grant to a public charity whose officer, director, or trustee also manages or founded the private foundation is not deemed self-dealing. This exception also allows a private foundation to condition a grant on certain naming rights associated with its founding business or individual, such as having the foundation’s name prominently displayed on a building.

The IRS has issued a number of private letter rulings demonstrating the incidental and tenuous exception. For example, a grant by a private foundation to a university to establish an educational program that teaches manufacturing engineering was not an act of self-dealing even though a corporation intended to hire its graduates and encourage employees to enroll in the program. This finding was based on the corporation not receiving preferential treatment in recruiting graduates of the program.

Similarly, a private foundation’s loan program that provided financing for construction projects in disadvantaged areas was not self-dealing even though some construction contractors and subcontractors had financial relationships with a bank that was connected to the foundation. The IRS ruled that even the work done by foundation interns was incidental and tenuous where the related private foundation established a program to provide on-the-job training and education for the benefit of at-risk, underserved, and underexposed youth. The company hosted program participants at its facilities and the participants worked in a sponsoring department of the company. The company agreed that it would not hire the participants for an unspecified number of years following completion of the program. This ruling is generally regarded as generous by the IRS. Foundations should be careful in relying too heavily on its findings.

With careful planning, corporations and the related corporate foundations can safely avoid self-dealing transactions. Consulting with experienced counsel before a proposed transaction between the related business and the foundation can help avoid problems before they begin

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[Considerations and Factors for Foundations in Accepting Gifts, Grants and Other Donations \(Oct. 2015\).](#)

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