

August 2018

## Private Foundations Bulletin

### Self-Dealing – A Refresher

The term “self-dealing” has been in the news more and more in recent months in connection with some high profile state attorney general investigations into various private foundations and other tax-exempt organizations. So, we hope this e-bulletin will serve as a reminder that: “self-dealing” is any direct or indirect transaction between a private foundation and a disqualified person.

Generally speaking, a disqualified person is one who is in a position — such as a trustee — to exercise substantial influence over the affairs of a tax-exempt organization. It is an area where a trustee can unknowingly violate rules and regulations pertaining to the oversight of a private foundation. It is irrelevant whether the transaction provides any benefit to the foundation.

#### Illustrations of Self-Dealing

The term “self-dealing” refers to any direct or indirect action(s) corresponding to those listed below:

- Sale or exchange, or leasing, of property between a private foundation and a disqualified person, except when a disqualified person gives property to a foundation as a gift or leases property to a foundation at no charge.
- Lending of money or other extension of credit between a private foundation and a disqualified person. However, a loan to a foundation, which is interest-free and the proceeds of which are used exclusively for the foundation’s exempt purposes, is not a violation of the self-dealing regulations.
- Furnishing of goods, services, or facilities between a private foundation and a disqualified person, except when goods, services or facilities are provided to a foundation by a disqualified person at no charge and the goods, services or facilities are used exclusively for the foundation’s exempt purpose.
- Payment of compensation (or payment or reimbursement of expenses) by a private foundation to a disqualified person, except when such compensation or reimbursement is for personal services, which are reasonable and necessary to the carrying out of the foundation’s tax-exempt purposes and the compensation or reimbursement is not excessive.
- Transfer to, or use by or for the benefit of, a disqualified person of the income or assets of the private foundation. However, if a disqualified person receives only an incidental or slight benefit from the use of the foundation’s income or assets, such act by itself may not be considered an act of self-dealing.
- Agreement by a private foundation to make any payment of money or other property to a government official.

#### Self-Dealing Penalties

A federal tax is imposed on both the disqualified person, such as a trustee, who engages in an act of self-dealing and on any foundation manager who knowingly participates in the act. (There is no self-dealing tax imposed on the foundation itself.)

The initial tax on the disqualified person is equal to 10% of the “amount involved” in each act for each year in which the act occurred. The “amount involved” is defined as the greater of the amount of money and the fair market value of the other property given or the amount of money and fair market value of other property received.

A disqualified person must pay this tax even if the disqualified person had no knowledge of having participated in the act of self-dealing.

Upon imposition of this initial tax, any foundation manager who knowingly participated in the act is taxed 5% of the amount involved unless the participation of the foundation manager was not willful and was with reasonable cause.

If the act of self-dealing is not corrected within the required time period, then a tax of 200% of the amount involved is imposed upon the disqualified person and a tax of 50% of the amount involved is imposed upon the foundation manager.

The maximum initial tax imposed on the foundation manager is \$20,000 and the maximum additional tax is \$20,000 for any one act. There is no maximum on the liability of the self-dealer including one who is a foundation manager. If more than one person is liable for the initial and additional taxes imposed for any act of self-dealing, all parties will be jointly and severally liable for those taxes.

## Conclusion

Knowing and following the self-dealing rules are in the best interests of all associated with the private foundation. The reputation of the foundation and its governance is such an important component of public perception and is the catalyst of the foundation’s mission.

## Contact Us

We welcome the opportunity to speak with you concerning any questions you may have about this bulletin or any other accounting, auditing, tax or other business and financial matters of interest to your private foundation. Please contact us.

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