

PROTECTING YOUR POSSIBILITIES PODCAST WITH LUKE FEDLAM

Episode 27: Impacting Your Community: Understanding Foundations and Nonprofits | Feb. 10, 2020

The following is a transcription of the audio podcast recording. It is largely accurate but in some cases it is incomplete or inaccurate due to inaudible passages or transcription errors.

Luke: I'm sports attorney Luke Fedlam, and welcome to the Protecting Your Possibilities podcast. Each conversation we focus on sharing information and having conversations around how athletes can best educate and protect themselves or their life outside of their sports.

Thank you so much for tuning in to the protecting your possibilities podcast. I'm your host, Luke Fedlam. I'm excited for another conversation today, because today's topic actually comes from you. So we've had listeners who have reached out and have actually asked questions about nonprofits and foundations. And so today's conversation is going to focus on how do you protect your possibilities when it comes to setting up or participating in a foundation or a nonprofit. And so again, thank you so much for sending your thoughts, your comments, please do continue to share the podcast rated write a review all that good stuff, it just helpful for us as we put out information that we hope is meaningful to you.

So let's get into it. Nonprofits foundations, it's a topic that comes up a lot with professional athletes around the idea of wanting to have their own foundation or their own nonprofit that they can put their name on that they can use to help leave a positive impact on their community. And one of the first things that always comes up when I'm talking to an athlete about a foundation is why I asked that question intentionally. Why? Why do you want a foundation and it's not to discourage them, but rather to understand so that we can have a conversation that makes sense for their situation.

So not all athletes need foundations. But a lot of times, athletes aren't always aware of other options as well to have a positive impact on their community. So when you think about one of the common answers that I get when I ask the question, why is because they want to be able to have events or raise funds for a particular cause or issue that affects their community where they currently play, or maybe where they're originally from. And that's what they've seen other athletes do is have their foundation and host events, whether that's a deep sea fishing, or celebrity golf, or a bowling event, or some other type of gala event where they raise funds. And so a lot of times athletes feel like that's what I need to do in order to give back to my community. I also asked the question why so that we can get to the actual purpose and what it is that they want to affect or impact within their community or society at large?

So this question of why is a powerful question that I think if you're someone who's listening to the podcast, and you're considering potentially starting a foundation, launching a charitable effort, I think you have to take the time to ask yourself the why. So with that, one of the things that comes up when I hear athletes, or others talk about wanting to lend their name to raising money for particular cause, and they want to host events to be able to do that they want to be able to get the social capital, if you will, for being known as someone who gives back to the

community who raises funds for the community for different causes, you can achieve that through other means, besides starting your own foundation.

So one of the things that I talk to athletes about quite often is the idea that if you want to raise funds, let's just say for a cause, like cancer, maybe cancer has affected your family, and you want to raise money for cancer research. Instead of launching your own foundation and having all of the administrative and liability requirements that come with that you could potentially partner with, let's say the American Cancer Society, or a local Cancer Research Hospital, you can find ways to engage with organizations that already are doing that work that you want to support, they may be already have their own nonprofit 501c3 status established. So you could partner with them lend your name to a particular event, or cause promote it, you get that benefit of that social capital, they get the benefit of you and your celebrity status and lending your name to their efforts potentially to raise more money than maybe they could have just on their own. And yet when the event is over, when that particular event that you're doing comes to an end, you're able to walk away knowing that you made a positive impact on your community that you raised money for a great cause. But then you go on about your life as opposed to now having to deal with the financial reporting that's required, the charitable contribution letters that are required to go out, making sure that all the vendor contracts are closed out, everybody's gotten paid for what they've done. And you don't have to worry about all that follow on work that comes with actually having a nonprofit organization, a nonprofit corporation that you're responsible for. So thinking about that as a way of partnering with other organizations is a great way to still achieve your charitable desires without necessarily taking on the potential risk or the administrative headache of having an actual operating nonprofit.

The other piece, as I mentioned about the why question comes back to what is it that you want to achieve? What is it that you want to solve for what issue in society are you trying to address. And it's important for that for a couple of reasons to think of those of that reason, because on the one hand, the IRS when you're going to file for tax exempt status to achieve being a 501c3 you're going to need to be able to list out what your charitable purpose is. And so when you think about what it is that you're trying to achieve, that ultimately is going to be your charitable purpose, which then leads to what your mission is, etc. So that's going to be important to figure out the other reason why it's important is, because if your charitable purpose is something that's already being done, oftentimes, you're in a better position to take on less risk, less administrative headaches and burdens, and ultimately, less stress by partnering with an organization that's already doing work along the lines of that charitable purpose that you've identified. So being able to articulate what that is, and what that charitable purpose is that you're working towards, could help you identify opportunities to partner instead of necessarily doing it all yourself. So when you think about the why that's going to help guide you in terms of maybe what the best path for you is, when starting off, and thinking about your charitable endeavors that you want to be involved in.

And oftentimes with athletes who are brand new, professional athletes, they're in their rookie or sophomore year of playing professionally, right. So there's only a couple, two or three years of playing experience, sometimes it takes some time for you to figure out what it is that you want to do to impact your community. And so early in your career, partnering with organizations can be a great way to test the waters and get your feet wet in this charitable space before jumping all in. And getting into a full blown nonprofit organization, by partnering with others, can help you test that out a little bit. So that's one of the things that I like to share with players early on. Now, there are some exceptions to the rule, there are some players who come in and say no, there are specific causes that I know without a doubt that have impacted my life that I want to address right away. And I believe that I can create a platform or create a curriculum or create something

that doesn't really exist in my community, or communities, right, either the community where I'm currently playing professionally or my community back home. And that creates this desire in me to start something because it doesn't otherwise exist.

So it could be something like when I was in fourth grade, I had some teachers who really helped me with reading comprehension. And that changed the trajectory of my academic life. Because I started to understand what I was reading better. It helped me in sports, it helped me in academics that helped me socially, whatever it might be. And so I want to create a program for reading comprehension for fourth graders. And I want to do that back at the high schools around my hometown, or where I'm from, and I want to do it with fourth grade classes in schools where I currently play professionally. And that's an example of something didn't exist, I know that I want to create that I have that desire. And so I'm going to launch something so that I can raise funds to be able to support the development of this platform or this program. Again, that's totally fine. But oftentimes, those are more rare.

What you often hear are athletes who say I want to give back, I'm not exactly sure how to give back. I'm not exactly sure what changes I want to make, but I know I want to give back to my community. And in those instances, that's where we talked about like before opportunities to partner with other organizations.

So we talked about this charitable purpose and the charitable purpose is something that has to be obviously shared on an application for tax exempt status. With the IRS, and it helps to guide the mission of a foundation or a nonprofit organization. But there are other corporate formalities that have to come into play as well, that a lot of times people don't think about. And this comes up a lot of times, just like in conversations that I'll have with entrepreneurs, about working in your business versus working on your business, those same hurdles come with nonprofit organizations as well.

So working in your business is actually executing that charitable purpose. It's donating food to families who are food insecure, it's providing reading services to young people who need to hear it, it's that work that you do for a charitable purpose. But working on your business are things like marketing, fundraising, like how do I get people to donate to this cause this organization that I've created, it's thinking about the like strategic marketing, partnerships, engagement, what type of accounting is being done by our accounting firms so that we can make sure that charitable contribution letters are sent out regularly? How are we maintaining our database? What states do I need to register for charitable solicitation, and there's a lot of other work that comes with the foundation that that's the working on your business aspect.

And so recognizing that that work has to be done is critically important for the success of any foundation that's getting launched. When you think about that process, the process is to think about, okay, what's that charitable purpose. And if I want to start my own foundation, my own nonprofit organization, it's filing the articles with, with a particular state for establishing a nonprofit organization, a nonprofit corporation, it's drafting and making sure that we have bylaws in place, it's recognizing that we're going to need that recruit directors.

So you're going to have a board of directors and thinking about who are those initial directors that you want to bring on, who are going to help guide your nonprofit organization, because again, you're not starting a for profit company, you're starting a nonprofit organization that ultimately is seeking out tax exempt status. And so it's not like the nonprofit is really your company, it really kind of belongs to the people, right? It belongs to society, it's established to ensure that certain ills within a society or certain challenges in the community are addressed.

So the directors that you're going to bring on are going to help you in terms of guiding the work of the foundation. So you've got the articles of incorporation to get it set up, you've got the bylaws, you have to file for that tax ID number, then you're going start looking at the policies that you're going to put in place the conflict of interest policy, a whistleblower policy, all of those different policies that are going to guide the day to day operation of your organization.

And then comes the big application around tax exempt status. And this is how you ultimately get to achieving tax exempt status, and that is with filing with the IRS, and you're either going to file a 1023, IRS Form 1023, or IRS Form 1023 Easy. And so that second, that latter form that I mentioned, the 1023 Easy, it's just that it's easier, it's a much, much shorter form. And the IRS came up with this maybe about five years ago or so. And it's for nonprofit organizations that are smaller, because most nonprofit organizations start off small. And so these are for organizations that can attest to the idea that they will raise less than \$50,000 in each of the first three years. So year one, I'm attesting that I'm going to raise less than \$50,000. Year two, same thing, year three, same thing. If you believe that you're going to raise more than \$50,000. Or maybe you even have commitments from sponsors that you work with or other organizations that they're going to contribute a significant amount that will put you over the threshold of raising \$50,000, then you need to do the full 1023 form with the IRS. That's the distinction between the two forms.

And a lot of people have heard about how the IRS has made it easier for nonprofit organizations to get their tax exempt status. And that is true, but there are certain hurdles that you have to attest to that you have to agree to or acknowledge and that is that you're expecting less than \$50,000 of contributions in each of the first three years. So that's then the filing that you make to the IRS over time depending on which form you filed and how busy the IRS is determines kind of how long it will take for you to get back that tax exemption letter that says that when people make contributions to your foundation, that those are considered tax deductible for their benefit.

So that's the ongoing kind of corporate piece that is oftentimes overlooked when it comes to establishing a foundation. But it's so critical, because the other piece of that ongoing management comes from financial management, and making sure that your funds are managed in a way that's appropriate for the foundation. And one of the key features to that is making sure that there's no personal benefit, or sometimes you might hear the phrase private inurement, which means that this foundation is set up for its charitable purpose and for the benefits of society, not for the benefits of individuals.

And that's where we get into questions, sometimes from athletes around this idea of I want to hire a family member to run my foundation. And that's a way in which I can pay them for their services, they can get paid, they can help me out by providing the ongoing day to day overseeing and administration of my foundation. But the big challenge here is, again, making sure that the finances align, and having that conversation with an attorney with an accountant to make sure that you're not going sideways with any of the IRS regulations as it relates to private or personal benefit.

And here's just an example. If let's say your foundation were to raise \$80,000, and your foundation the cause is for let's just say cancer research, and you decide that you want to hire a cousin to run your foundation, and then that cousin gets paid \$75,000. Now what you can see is you've raised \$80,000, you've paid out \$75,000 to your cousin, you may have other expenses based on raising that money that you did. Money's not going to the charitable purpose. So you've acknowledged in your filing with the IRS that you're going to be raising money and contributing to a particular charitable purpose. And yet, your finances and accounting does not

reflect that. So that is not a good thing. And that's something where you can ultimately end up going sideways of the IRS. And this is something again that is not necessarily a hard and fast rule in terms of what the dollar amount is, what that ratio or equation is. But it's something that you want to make sure that you have conversation with a professional service advisor based on your specific set of circumstances, for your potential organization. So that you can make sure that you're managing the ongoing financial requirements appropriately for your foundation.

The other thing that I'll bring up because it happens a lot with athletes, is the idea of people will come to you saying that they want to raise money for you that they'll go out and they'll raise money for your foundation. And they'll just take a percentage of what they raise. Sometimes your marketing agent may say that they'll do that for you as well. Other folks, other independent individual companies will come to you and say they will raise funds for you. So that you don't have to focus on that we're experienced and have experience in raising funds for athletes in particular. And we'll take a certain percentage. Now I've seen those percentages go from anywhere of 20%, up to 25-30%, and even 33%, taking a third of what they raise one of the biggest points here to highlight because this may or may not be a good fit for you. But one of the things when I look over those contracts, number one, you always want to make sure that you get that in a contract in a written form. And that you review and have someone who's looked at those review those kind of agreements. Because one of the things that I think is always important is to understand how expenses work in all of that.

So let's just use a numeric example to hopefully make this clear a little bit. So if you were to have a fundraiser who says hey, someone, an agent, let's say you're someone who comes and says I want to I want to raise funds for your organization, and I'm going to charge you for ease of numbers, we'll say 20%. And what I'm going to do is I'm going to throw some events for you. I've got this Rolodex of heavy hitters who are going to come in and they're going to write checks, and they're going to pay for auction items and all this kind of stuff we're going to raise funds, and I'm going to take 20% of whatever we raise.

Well, let's just say they throw an event for you, and you raise \$20,000 at that event. And of that, if they're going to be getting paid based on gross versus net is going to have a very big difference to you. So let's just say that it's based on gross that they're getting 20% gross, and I've seen this time and time again, and these are great. Well, if they throw an event, and they raise \$20,000, and they get 20% of gross, that means they get \$4,000. So you pay them \$4,000 \$16,000 comes back to the organization, but they're throwing an event. And we all know that events have costs. So now, if we look at it in terms of the cost of throwing the event itself, let's just say that it costs \$6,000. So if it cost \$6,000, to throw that event, and you're paying this agent, this marketing person 20%, so they've taken 20%, they've taken their \$4,000, away from that \$20,000. So now, that leaves you with \$16,000 for your organization. And now the actual cost of throwing the event costs you \$6,000. So now you can see that you raised \$20,000, but only \$10,000 is actually going to the organization.

All right. Now that's on gross, but if you pay them based on net, as a fundraiser as someone who's raising you funds, and you will use that same example, those same numbers, so now you've raised \$20,000, that there are \$6,000 of expenses. So that brings your net number down to \$14,000. And so of that \$14,000, if they're getting paid 20%, now you're paying them cutting them a check for \$2,800, as opposed to \$4,000. Right. So \$1,200 more now is going to the organization. And so you can play that out with any numbers, given your situation on fundraising. And those numbers can obviously get really big. If you raised \$100,000, and 20%, on gross versus on net, and all that kind of stuff. You can play that out yourself. But you can see that's just one of those aspects of those kind of contracts with people who want to raise money

for you and get paid off of that. That's one aspect that you've got to understand within those agreements.

Number two, you also want to understand what access do they have for your donors, because what you don't want is for them to continue to increase their Rolodex of donors based on them controlling your attendance list of people who attended your event. And then they go on to the next athlete and say, hey, I've got this even bigger Rolodex, and the next one, I've got even bigger, right? So you can see how people can make a lot of money off of you and get so much benefit by doing this for you. Is there a place for someone to potentially make money off of raising funds for you? Maybe. I mean, that's really a question you have to answer for yourself based on your organization. But one of the things you really want to be mindful of is, what is it that you're getting for what you're paying? And is it worth it to your organization. And you always want to make sure that you have a professional review that agreement as well, because you don't want to get in a place where somebody's really just taking advantage of your desire to make a positive impact on your community through charitable giving, and charitable work.

So a lot to unpack here, great depth on various topics here. But we can go even deeper. And so if you have additional questions or you want to follow up on a particular point, please feel free to reach out, you can find me @LukeFedlam on all social platforms, you can reach out to me via email, pretty easy to find. You can leave a leave a comment or review wherever you listen to podcasts.

But again, there's some there's some really important information here. Because people always want to take advantage of other people in situations. A nonprofit is just another platform where people might want to take advantage of you. And so understanding all that you're getting into understanding all that is going to be required of you is critically important before you launch a nonprofit organization or some form of charitable foundation for your community and for society at large.

So again, thanks for your time. Thanks for tuning in today. Again, feel free to reach out with any questions. And please do feel free to share this podcast. Let me know if there are other topics that you want us to unpack happy to do that love having the conversation with you. And again, thank you for listening. Have a great day.

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