

## PUTTING TAX-DEDUCTIBLE GIFTS TO WORK

Except in the rare event that an alumni and volunteer corporation has received tax-exempt status under Internal Revenue Code Section 501(c)(3) (Charitable, Religious, and/or Educational Organizations), donations by alumni to the alumni and volunteer corporation are not tax deductible. To qualify for tax deduction, donated funds must be used for charitable, religious, and/or educational purposes and must be made to an organization recognized by the IRS as a qualified charitable, religious, and/or educational organization.

Alumni and volunteer corporations may raise funds for renovations and building projects or to build reserves and fund scholarships, but fund-raising efforts may be hindered by the lack of tax deduction for gifts. However, alumni and volunteer corporations can raise money for projects and scholarships through tax-deductible gifts to a named fund in the Sigma Phi Epsilon Educational Foundation. Of course, there are restrictions and limitations on access and use of these funds. The Sigma Phi Epsilon Educational Foundation offers three types of funds to which gifts can be made on a tax-deductible basis and can be restricted for use by a specific chapter and alumni and volunteer corporation. The legal and practical restrictions on those funds are:

### ❑ *Library Funds*

Gifts to a named Sigma Phi Epsilon Educational Foundation Library Fund are available to the corresponding alumni and volunteer corporation for renovating and providing a library or other dedicated educational areas in chapter houses. Contributed funds become the property of the Sigma Phi Epsilon Educational Foundation but can only be used for the benefit of the chapter and alumni and volunteer corporation associated with the named fund. Because the IRS has a strict definition of dedicated educational areas and because the Sigma Phi Epsilon Educational Foundation's tax-exempt status is at risk for proper use of the funds, funds are disbursed to alumni and volunteer corporations only on previously approved plans for educational capital projects. Library funds are deposited as cash equivalents to provide flexibility to the corpus of the named chapter fund.

### ❑ *Chapter Funds*

Gifts to a named Sigma Phi Epsilon Educational Foundation chapter fund are endowment gifts, invested to produce an annual return that is available to the alumni and volunteer corporation for scholarships and other educational purposes. The Sigma Phi Epsilon Educational Foundation will loan some or all of the money in a named chapter fund to the corresponding alumni and volunteer corporation as part of its investment program. Interest from such loans is earnings available for scholarships and other educational programs. By definition, the principal or corpus of a chapter endowment fund remains intact and earnings are available for educational purposes.

### ❑ *Added Dimension Funds*

Gifts to a named Sigma Phi Epsilon Educational Foundation Added Dimension Fund are invested under a pre-defined working agreement that provides for disbursement of funds to corresponding alumni and volunteer corporations for scheduled ongoing scholarships and educational programs, such as Balanced Man Scholarships and other annual scholarships. Added Dimension Funds are invested to provide an annual return; however, unlike chapter endowment funds, use of principal or corpus is allowed as defined in the working agreement.

Some chapters and alumni and volunteer corporations have formed their own educational foundations to raise funds through tax-deductible donations. Only a few of these attempts have been successful in providing a significant base of funds for scholarships and projects. Because of the expense of establishing and maintaining an educational foundation at the local level, the Sigma Phi Epsilon Educational Foundation has tried to develop its program of funds to provide a conduit for tax-deductible giving in a way that gives alumni and volunteer corporations flexibility in access and use of funds.

## **EDUCATIONAL & CHARITABLE PURPOSES**

Often, chapters and alumni and volunteer corporations have income deemed by the IRS to be unrelated to the exempt purpose of the organization. Any investment income such as interest on bank accounts and Chapter Investment Fund earnings automatically meets the definition of unrelated business income. For any year in which gross unrelated business receipts exceed \$1,000, the organization is required to file Form 990T with the Internal Revenue Service. If the activity's direct expenses are less than revenues and net unrelated business income results, income taxes may be due, subject to a specific exemption of \$1,000. Chapters and alumni and volunteer corporations can avoid this tax by following IRS revenue procedures associated with the Internal Revenue Service Code Section 512, commonly called the "set-aside rules."

IRC Section 512 provides that certain tax-exempt organizations (including organizations exempt under IRC Sections 501(c)(2) and 501 (c)(7), may permanently "set aside" net unrelated income for charitable, religious, or educational purposes and be exempt from income tax on the amount set aside. While there is no limit on the amount that may be set aside, there are significant restrictions on the use of funds set aside, and there are specific requirements for maintaining and accounting for funds set aside.

The permanency of funds set aside is a significant requirement. Once set aside, funds must be used for a charitable, religious, or educational purpose and can be used for no other purpose. Likewise, amounts set aside cannot be reduced by subsequent net unrelated taxable losses. In loss years, nothing is set aside. A separate accounting must be kept for funds set aside each year, showing how funds were expended for an appropriate purpose.

Typically, only educational purpose expenditures are available to chapter and alumni and volunteer corporations. Examples of such expenditures would be scholarships and leadership grants. The IRS has challenged organizations which allowed set aside funds to build indefinitely without making appropriate expenditures, citing lack of charitable intent in applying the set aside rules.

IRC Section 512 should be investigated by chapters and alumni and volunteer corporations as a means to avoid unrelated business income tax. Organizations should consult their accountant or tax advisor before applying the code in preparing Form 990, to ensure that all procedures related to the code are followed.