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8 September 2010

Ms. Barb Hook  
Black Oak Lake Preservation Foundation, Inc.  
P.O. Box 803  
Land O' Lakes, WI 54540

Re: Black Oak Lake Preservation Foundation, Inc.

Dear Ms. Hook:

In your August 15, 2010 e-mail correspondence to me on behalf of the Board of Directors of Black Oak Lake Preservation Foundation, Inc (the "Foundation") you asked several questions regarding the Foundation's tax-exempt status under § 501(c)(c) of the Internal Revenue Code (the "Code"). These questions are reproduced in bold, followed by my answers.

**What are the new Foundation's responsibilities for documentation should we have an IRS audit? For example; what documentation do we need to keep? Minutes of annual meetings? Donation records? What else?**

The Foundation should keep copies of the minutes of all board of directors meetings. If the Foundation converts to a membership organization (discussed below) it should also keep a record of all membership meetings.

The Foundation should also keep a copy of its original IRS determination letter evidencing its recognition by the IRS as a § 501(c)(3) public charity. The Foundation should also maintain a copy of its original Form 1023 application. In addition, the Foundation should keep copies of its annual IRS Form 900 filings and supporting workpapers.

The Foundation should keep records of the name, address, and amount received from each of its donors. In addition, the Foundation should maintain records of its expenditures and any supporting documentation that could be used to show that such expenditures were in furtherance of the Foundation's exempt purpose of preserving, maintaining and improving Black Oak Lake and the surrounding watershed.

**The Association has members and collects dues. The Foundation has no members. Should we absorb the Association into the Foundation will the Foundation be able to have members and charge dues? Will all members be eligible to act as Directors and Officers of the governing Board?**

There are two kinds of § 501(c)(3) organization; membership organization and non-membership organizations. The difference between a member and non-member organization mainly involves the method in which the board of directors of the organization is selected.

### ***Membership Organizations***

A membership organization generally charges annual dues. Those individuals who pay the annual dues are eligible to be members of the organization. Membership normally provides the individual with the right to attend membership meetings, receive a newsletter, etc.

Importantly, membership also normally provides the individual with the right to vote on the election of individual to the organization's board of directors, as well as to stand for election. Normally, each member is provided with one vote, regardless of the amount of such individual's monetary contributions to the organization in a given year. The term of each director of a membership organization is normally set by the organization's by-laws (i.e., a one or two year term). At the end of such term the individual may choose to stand for reelection (unless term limits are imposed by the bylaws).

### ***Non-membership Organizations***

A non-membership organization does not charge annual dues in return for membership. Further, it does not have "members" which have voting rights. However, a non-membership organization may still request annual donations in order to be listed as a "friend" of the organization and, for example, mail a newsletter to its "friends."

A non-membership organization's initial board of directors is normally composed of the founders of the organization. Often, the directors of a non-membership organization have no set limit to their term as a director. Vacancies on the board are normally filled by candidates selected by the remaining members of the board. A vote of the individual donors to the organization is not held. Thus, a non-membership organization's board of directors is "self-perpetuating," while the composition of a membership organization's board of directors is dependent on the vote of the members.

**Will the merger of the two entities necessitate re-filing for 501(c)(3) status/determination for the Foundation? What legal documentation is necessary to effect the merger? For instance, what resolutions for each entity, merger agreement and/or government filings are required?**

The simplest way to accomplish the proposed reorganization is for the Association to vote to dissolve itself and pay over its net assets to the Foundation. The Association would then cease to exist as a legal entity. The Foundation would receive a donation of the Association's remaining assets and continue as a § 501(c)(3) organization.

In order to dissolve the Association, the Association's board of directors must first pass a resolution authorizing the dissolution. The Board should then call a special meeting of the members in accordance with Article IX, Section 3 of the Association's Bylaws to vote on the proposed dissolution of the Association and contribution of its net assets to the Foundation.

Assuming the members approve of the Association's dissolution (Wisconsin law requires approval by the lesser of a majority of the total votes eligible to be cast or 2/3rds of the votes actually cast), the Association would then file Articles of Dissolution with the Wisconsin Department of Financial Institutions and cease as a legal entity. Any remaining assets of the Association would then be contributed to the Foundation.

If the Foundation continues as a non-membership organization, it would not need to take any steps other than to accept the contribution of the Association's remaining assets (which I assume are just cash). However, if the Foundation wishes to convert to a membership organization, its Articles of Incorporation and Bylaws will need to be amended and restated to account for such a conversion.

If the Foundation converts to a membership organization, it would not be required to reapply to reapply for § 501(c)(3) status. However, it would be required to file its amended and restated Articles of Incorporation and Bylaws with the IRS. It is possible the Foundation would receive a request for additional information from the IRS on account of the conversion. If the Foundation continues to operate as a non-membership organization, no IRS filings by the Foundation would be required.

**Will the merger complicate our compliance with 501(c)(3) going forward either in our operations or our tax filings? Would any of the activities we currently sponsor like picnics, dinners, boat parties, etc., be curtailed by merging with the Foundation and following the rules that govern the Foundation? Must we advertise these activities to non-members?**

The dissolution of the Association followed by the contribution of its assets to the Foundation will cause any tax filing complications for the Foundation on a going-forward basis. Its tax reporting obligations will remain the same.

However, as I have stated to you on several occasions, the Foundation's primary purpose (i.e., the uses to which it puts its funds) must be the conservation, maintenance and

betterment of the lake and the surrounding watershed for the benefit of the general public. Assuming the picnics, dinners, boat parties, etc. are simple affairs (i.e., burger cookouts with a lunch or dinner worth approximately \$5-\$10), there is no problem providing these types of occasional *de minimis* or token benefits to the members or donors as a means of staying in touch with the organization's donor base. As in most issues involving tax-exempt organizations, the issue is one of degree.

**Should we lose 501(c)(3) status can we correct the issues and re-apply? Would all gifts under the tax-free status, prior to the loss of status, retain their tax deduction as filed?**

It would be highly unusual for an organization such as the Foundation to lose its tax-exempt status. However, if it did lose such status it could reapply. Assuming the Foundation lost its tax-exempt status, charitable donations made to it prior to the loss of tax-exempt status would still qualify as charitable deductions to the respective donors.

There are two main ways in which the Foundation could lose its § 501(c)(3) status. First, failure to file the required IRS Form 990 reports for three straight years can lead to the loss of exempt status. I understand the Foundation has always timely filed its Form 990, so this should not be a problem.

Second, the Foundation could lose its exempt status after an IRS audit which determined that the Foundation was no longer operating in conformance with its original exempt purpose. The most foreseeable instance in which this could occur is if the Foundation began using its charitable donations primarily for the improvement of the property of private land owners with only a tangential benefit to the lake and the general public as a whole.

**What are the liabilities and responsibilities for a 501(c)(3) organization which raises money, recruits members, addresses environmental issues, donates money, charges dues, writes grants, and receives grant monies and host social functions? Are these activities allowable under 501(c)(3) status? Is there a publication/primer which outlines responsibilities of a 501(c)(3) organization?**

This is obviously a very broad question. In short, the responsibility of the Foundation is to act in a manner that is consistent with its tax-exempt purpose; to-wit: the conservation, maintenance, and improvement of Black Oak Lake and the surrounding watershed. Fundraising, member recruitment, public education and working on environmental issues are all part of the Foundation's charitable mission. Writing grant proposals and receiving grant monies are common activities of a § 501(c)(3) organization.

The main obligation of the Foundation's board of directors is to ensure that the charitable donations it collects, as well as grant money received, are utilized for the benefit

of the lake and watershed as a whole, as opposed to being expended for the primary benefit of the lake shore property owners.

I have included with this letter some IRS publications regarding § 501(c)(3) status, as well as a Wisconsin DNR publication regarding lake associations.

**Could the Foundation buy and sell land?**

The Foundation has the ability buy and sell land. It also has the ability to accept donations of land.

**Will any member of the Foundation be able to bring an issue to the Foundation Board with the expectation that the Board will address that issue? For instance, can a 501(c)(3) organization act to protect the private, but lake-related, interests of its members or is it limited to act only to protect the lakefront environment for the benefit of the general public?**

The Foundation is recognized as a § 501(c)(3) public charity. In order to maintain its public charity status, the Foundation must be operated for the benefit of the general public as a whole, and not for the private benefit of the lakefront property owners, or any individual lakefront property owner. It is allowable, and expected by the IRS, that the charitable activities of the Foundation will indirectly benefit the owners of private property in the area. However, the primary purpose, and the primary benefit, of the Foundation's activities must accrue to the public as a whole. For example, the repair of a public boat landing would generally benefit the public as a whole although used occasionally by a lakefront property owner. By contrast, repairing a private boat landing would primarily benefit the property owner, and not the general public.

There is no bright line answer to whether a particular undertaking primarily benefits the general public (and therefore is an acceptable use of Foundation assets), or primarily benefits one or more private property owners (and therefore is an inappropriate use of Foundation assets). The Foundation's Board will need to make such determinations on a case by case basis based upon each project's particular facts and circumstances.

**Currently both the Association and the Foundation carries commercial liability insurance. Will this be adequate for the new Foundation Board?**

I assume neither the Association nor Foundation has paid employees (i.e., all activities are volunteer in nature, or third party independent contractors are retained). If so, there is no need for the Foundation to carry Worker's Compensation insurance.

Although unlikely, it is foreseeable that a lawsuit could be brought against the Foundation for an accidental injury occurring at the lake. In the litigious society in which we

live, it is not unusual for numerous parties to become involved in litigation in the event of an injury or death. Although there are several substantial legal defenses to liability available to a non-profit, volunteer, § 501(c)(3) organization, often the costs of defending against litigation, even if the claim is dismissed, can be substantial. Liability insurance will often cover such costs of litigation in addition to providing coverage for any liability.

For example, the Foundation could be sued for the acts taken by its members (if it converted to a membership organization), directors or volunteers who are acting on its behalf. In addition, the Foundation's board of directors could be sued by its members (if converted to a membership organization) for mismanagement. Generally, Wisconsin law provides that a member of a non-profit organization's board of directors can only be sued for actions taken as a director if such action involves a criminal act, willful misconduct, or a transaction in which the director obtained an improper financial benefit.

It is also important to remember that a person can always be sued in his or her individual capacity (separate and apart from the organization) for his or her own acts. However, Wisconsin law affords special protections to volunteers providing services to non-profit organizations. Generally speaking, such volunteers cannot be sued for their own acts unless such acts involved criminal behavior or willful misconduct.

Further, Wisconsin's recreational immunity statute provides important liability protections. Generally, a property owner is not liable for any injury to a person engaged in a recreational activity (such as swimming, diving, boating, etc.) on the property owner's property, if the property owner did not charge a fee for the use of his or her property.

The Foundation's insurance agent should be able to supply more information on the types of coverage currently provided under the Foundation's insurance policy.

**Will a newly formed 501(c)(3) organization be able to launch a campaign to initiate a Lake District? Be a part of a Lake District? Would the new organization retain 501(c)(3) status as a member of a Lake District? Would we even need a separate organization?**

A lake district is a specialized unit of local government designed to manage a lake or group of lakes. A lake district is established by a local county or town board and is a wholly separate legal entity from any private § 501(c)(3) organization. Unlike a § 501(c)(3) organization, membership in a lake district is not voluntary. All property owners within the boundaries of the lake district are subject to its regulatory powers.

Section 501(c)(3) organizations may have opinions on local lake issues, but such organizations have no regulatory power to force or prevent any particular activity involving a lake. By contrast, lake districts are empowered by the State with certain regulatory powers

such as the power to tax and levy special assessments. In addition, lake districts may be delegated additional powers such as establishing boating ordinances.

Because a lake district is a unit of local government, a § 501(c)(3) organization may not be “part of” a lake district, or a “member” of the lake district. However, the owners of the property contained within the lake district will be subject to its regulatory powers. Such property owners would have the right to run for election to the lake district’s board of directors. Individuals whom are active in a § 501(c)(3) organization could also seek election to the board of directors of the lake district.

If the Foundation believes that the establishment of a lake district would be beneficial to the lake and the surrounding watershed, the Foundation could utilize some of its resources to investigate the feasibility of petitioning the county board for the establishment of a lake district. Alternatively, a separate organization could be established.

I hope this letter has been of assistance to the Board of Directors. Please feel free to contact me with any further questions.

Sincerely,

A handwritten signature in black ink, appearing to read 'S. Grimm', written over a horizontal line.

Steven E. Grimm

SEG:mcr  
25501.101661  
Foundation lt