C. AGENCY: A CRITICAL FACTOR IN EXEMPT ORGANIZATIONS AND UBIT ISSUES

by
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1. Introduction

The question whether an entity or individual is deemed to be an agent of another for tax purposes, is at the heart of many tax controversies. The existence of an agency relationship is sometimes favorable to the revenue, sometimes unfavorable. For these reasons, it is important that IRS EO staff have a uniform understanding of agency law and apply it consistently.

Several important exempt organization issues center on agency, such as whether a fundraiser is an agent of the organization so that payments to the fundraiser are deductible; whether a publisher is an agent of an exempt organization so that its advertising activities constitute unrelated "business" of the exempt organization; and whether a licensee of an exempt organization's intellectual property is an agent for purposes of determining whether payments are royalties.

In making the decision on agency, IRS EO staff must apply what amounts to a federal common law of agency, since state law concepts may vary considerably. This article will first explain basic common law principles, and then discuss cases and rulings that apply these principles to common situations in determining UBIT, contributions/public support, and tax exemption.

The article is lengthy and broad in scope. The following outline of the article may help the reader find subject matter of particular interest:

(4) Special-Purpose Conduit Funds: Does the EO Hold Them as Agent or Trustee for the Members?

C. Charitable Contribution and Public Support Issues
(1) Is the Recipient of Contributions Acting as the Agent of the EO?
(2) Are Workers Agents of EOs When They Deflect Earned Funds to the EOs?
(3) Religious Order Members: When Are They Agents of the Order in Receiving Compensation?
(4) Are Church Leaders Handling Funds as Agents of Their Churches?
(5) Other EO Staff Receiving Funds as Agents of EOs
(6) Persons Conducting Their Own Businesses but Claiming to Be Agents of EOs
(7) Is the EO the Agent of Another Person for Charitable Deduction or Support Purposes?

D. Exemption Issues
(1) Effect on 501(c)(3) Exemption Where the Organization Serves as Agent
(2) How Acting as Agent Will Affect Other 501(c) Exemptions
(3) Agency in Political Intervention Issues
(4) Whether Individuals Performing Illegal Act Are Agents of Exempt Organizations

4. Conclusion

2. Important Concepts of Agency Law

Where agency issues arise in federal tax cases, the courts typically look to federal case law and treatises on common law, particularly the Restatement (Second) of Agency (1958) (hereafter "Restatement"), rather than State law. The following discussion focuses on the Restatement.

A. The Relationship and the Parties

"Agency" is defined as the fiduciary relation which results from the manifestation of consent by one person (the principal) to another (the agent) that the agent shall act on the principal's behalf and subject to the principal's control, and consent by the agent so to act. Restatement § 1.

Issues of agency arise where the purported agent deals with third parties, such as whether the agent's acts are binding on or attributable to the principal, for purposes of contract or tort liability. In the EO area, resolving the question of agency determines whether income (such as donations or unrelated business income) received by the purported agent, or the acts of the purported agent, should be attributed to the purported principal. This is so because receipt of funds by an agent constitutes receipt by the principal for federal tax purposes. Maryland Casualty Co. v. United States, 251 U.S. 342, 347 (1920). Similarly, income received as agent on behalf of another person is not

income to the agent. Brittingham v. Commissioner, 57 T.C. 91 (1971), acq., 1971-2 C.B. 2. Where an agent incurs expenses on behalf of the principal, reimbursement from the principal is not income to the agent, except to the extent reimbursement exceeds expenses. See, e.g., Rev. Rul. 67-30, 1967-1 C.B. 9. Expense allowances in some cases are limited under I.R.C. 62, 132, 162, and 274.

The principal and agent may be individuals or entities. Restatement § 1 comment a. Consideration is not necessary to form the relation--thus, an agent may be a volunteer. Restatement § 16.

A person acting as an agent in a transaction ordinarily acts for only one principal. Situations occur, however, where a person employed by two others to conduct a transaction between them is the agent of both; in such case the agent must deal with each fairly. A person may act as agent of one for part of a transaction and agent of the other for the remainder, as where an insurance broker represents the insured in securing a policy and represents the insurer in receiving premiums. Also, a person may be generally employed by one principal and nevertheless be employed by another to conduct a transaction with the general employer. The ultimate question is to whom the agent owes a duty of loyalty in the transaction. See Restatement § 14 L and comments.

B. Ways to Create Agent Authority

An agent obtains authority to bind the principal through agreement with the principal (actual authority), or through actions of the principal (apparent authority or ratification).

Since the actual principal/agent relationship is consensual, a written agreement between the parties is of primary importance. The principal's manifestation of consent to the agent's authority may be made by words or other conduct, including acquiescence. Restatement § 7 comment c. The consensual relationship is terminated when either party manifests to the other dissent to its continuance. Restatement § 119.

It must be emphasized here that while the contract terms setting forth the parties' rights and obligations are of major importance, the designation of the parties in the agreement as having (or not having) a principal/agency relationship is not binding on the Service or other third parties; instead, all the facts and circumstances must be considered. See Board of Trade v. Hammond Elevator Co., 198 U.S. 424 (1905); State Police Ass'n of Massachusetts v. Commissioner, 125 F.3d 1, 18 (1st Cir. 1997). Thus, the Service may ignore the designation in the agreement if the substance indicates otherwise. The taxpayer, however, while free to organize his affairs as he chooses, must accept the tax consequences of his choice, whether contemplated or not, in order to minimize burden and uncertainty. Higgins v. Smith, 308 U.S. 473, 477 (1940); Commissioner v. Nat'l

Alfalfa Dehydrating & Milling Co., 417 U.S. 134, 149 (1974); Church of Scientology of California v. Commissioner, 83 T.C. 381, 473 (1984).

Apparent authority results from a manifestation by a person that another is his agent, the manifestation being made to a third person and not, as when actual authority is created, to the agent. Restatement § 8 comment a. Facts and circumstances indicating apparent authority may include the following: statements by the principal supporting an agency relationship; use of stationery with the principal's letterhead; advertisements, telephone listings, or business cards indicating agency; posted signs on business areas or vehicles indicating agency; apparently unrestricted use of principal's facilities; and a prior course of dealings between the parties in which the agent's authority has remained unchallenged. See Am.Jur.2d Agency § 365.

Action taken without actual or apparent authority is authorized if "ratified" by the principal. Ratification is the affirmance by a person of a prior act which did not bind him but which was done or professedly done on his account, whereby the act, as to some or all persons, is given effect as if originally authorized by him. Restatement § 82. "Affirmance" is either (a) a manifestation of an election by one on whose account an unauthorized act has been done to treat the act as authorized, or (b) conduct by him justifiable only if there were such an election. Restatement § 83. Acquiescence by the principal in conduct of an agent indicates affirmance (in other words, silence gives consent). Restatement § 43.

C. Two Types of Agents: Servants and Independent Contractors

A factor distinguishing an agency relationship from other legal relationships is that a principal has the right to control the conduct of the agent with respect to matters entrusted to him. Restatement § 14. A principal has greater control over a servant than over an independent contractor, but an independent contractor may still be considered an agent. See State Police Ass'n of Massachusetts v. Commissioner, 125 F.3d 1, 18 (1st Cir. 1997); Common Cause v. Commissioner, 112 T.C. 332 (1999). The servant/independent contractor distinction is made for purposes of tort liability to third parties and special duties of masters to servants. It is also relevant for employment tax purposes--see, e.g., Rev. Rul. 87-41, 1987-1 C.B. 296.

Restatement § 2(1) defines a master/servant relationship (commonly known as employer/employee relationship) as follows:

> A master is a principal who employs an agent [the servant] to perform service in his affairs and who controls or has the right to control the physical conduct of the other in the performance of the service.

By contrast, an independent contractor is a person who contracts with another to do something for him but who is not controlled by the other nor subject to the other's right to control with respect to his physical conduct in the performance of the undertaking. He may or may not be an agent. Restatement § 2(3). One who contracts to act on behalf of another and subject to the other's control except with respect to his physical conduct is an agent and also an independent contractor. Restatement § 14 N. Most persons known as "agents" (brokers, factors, attorneys, collection agencies, selling agencies) are independent contractor agents. Non-agents include builders and others who have contracted to accomplish physical results, without supervision by the person who has employed them to produce the results. Restatement 14 N comments a and b.

D. Distinctions Between Agents and Trustees

An agent owes his principal the duty to act primarily for the principal's benefit in matters connected with his agency, and thus is a kind of fiduciary. Restatement § 13 comment a. The element of control over the agent's conduct (discussed above) distinguishes agents from trustees, boards of directors, or other fiduciaries. Restatement § 14 comment c. Courts, however, sometimes use the terms "agent" and "trustee" loosely and interchangeably.

Aufiero v. Commissioner, 43 B.T.A. 753 (1941), discussed the distinction between a trust and agency relationship. The taxpayer made payments to an old friend residing in the taxpayer's place of childhood to build a school. The issue was whether the relationship created was a charitable trust, to which contributions were deductible, or an agency. The court reasoned that an agent (on behalf of and subject to the control of the principal) does not have title to the principal's property, and that the relationship can be terminated by either at any time. A trustee acts according to the terms of the trust, can be compelled by the beneficiary to so perform, takes title to property for the benefit of the beneficiaries, and the relationship ordinarily cannot be terminated at the will of the settlor, trustee, or beneficiary. The type of relationship is determined by the parties' intent, although the designation used is not controlling. The court considered the friend as the taxpayer's agent, since the taxpayer retained entire control of the school project and the friend merely carried out the taxpayer's instructions. Therefore, the taxpayer's payments were not deductible as contributions to a charitable trust.

Appleby v. Commissioner, 48 T.C. 330 (1967), held that a gift to a trust for the benefit of a college constituted "the classic example of a gift for the use of the charity that is named beneficiary" rather than a gift "to" the agent of the college for I.R.C. 170 purposes.

3. Applying Basic Principles to Tax Cases

As is evident from the following discussion of authorities, agency principles are applied in somewhat different manners depending on the particular facts and circumstances. It is often not easy to determine how these general principles should be applied to a given exempt organization issue. This does not mean that agency determinations are devoid of principle, or that one can simply "make up" an agency relationship to fit one's tax or non-tax purposes. For example, it would be nigh impossible to hold that a person was an agent of an EO if the EO had neither actual nor constructive control of the person. Similarly, if reliable contemporaneous written or other evidence existed stating that the parties reject an agency relationship, and the parties did not operate in a principal–agent manner, then it could hardly be argued that a principal-agency relationship existed.

In the following pages, we will analyze cases and rulings that discuss how agency principles are determined in common exempt organization situations, and how that determination affects the tax result.

A. Is the Entity Treated as Separate or as an Agent?

A frequent tax issue in the EO area is whether a corporation is to be treated as a separate entity, or whether it may be disregarded or treated as an agent of another entity or individual. For example, should a small "think tank" corporation be treated as an entity separate from the individuals who founded and run it?

Taxpayers sometimes want to assert the separate existence of a corporate entity and sometimes want to disregard it, depending on the facts. Courts have applied the Moline Properties and National Carbide tests discussed below, regardless whether the taxpayer or the government benefits from disregarding the entity.

Moline Properties, Inc. v. Commissioner, 319 U.S. 436 (1943) held that, for income tax purposes, a taxpayer cannot ignore the form of the corporation that he creates for a valid business purpose or that subsequently carries on business, unless the corporation is a sham or acts as a mere agent.

Because of the potential for tax avoidance by means of hindsight, the Supreme Court set forth narrow circumstances in which a taxable corporation may be regarded as an agent of its owner for tax purposes. Fundamentally, the organization's agency must be unambiguous. National Carbide Corp. v. Commissioner, 336 U.S. 422, 437 (1949), established two requirements for determining that an agency relationship exists:

(1) If the corporation is a true agent, its relations with its principal must not be dependent upon the fact that it is owned by the principal, if such is the case.

The court expressly repudiated the reasoning in an earlier case, Southern Pacific Co. v. Lowe, 247 U.S. 330 (1918), that a wholly-owned subsidiary is the agent of its parent corporation by virtue of the parent's control as sole stockholder.

(2) The corporation's business purpose must be the carrying on of the normal duties of an agent. The opinion set forth four relevant considerations in determining whether a true agency exists: whether the corporation (1) operates in the name and for the account of the principal, (2) binds the principal by its actions, (3) transmits money received to the principal, and (4) receives income that is attributable to the services of employees of the principal and to assets belonging to the principal.

Commissioner v. Bollinger, 485 U.S. 340 (1988), held that a corporation acted as its shareholder's agent for a particular asset because the agency agreement was written contemporaneously, the corporation acted solely as an agent, and the corporation held itself out as agent in all dealings with third parties.

These questions arise in the EO area as well as others. However, because the Moline Properties/Nat'l Carbide line of cases requires fairly compelling evidence to show that a corporation with proper formalities is a sham or agent of the taxpayer, it is only in egregious situations that a court will hold that the IRS may disregard the taxpayer's corporate form. For example, in Church of Scientology of California v. Commissioner, 83 T.C. 381, 399 (1984), the court held that a Panamanian corporation was a mere sham because the board members were all employees of taxpayer; and the board conducted only one board function in several years, kept no minutes or separate financial records, had no officers or employees, and allowed taxpayer to handle all its finances.

Disabled Veterans Service Found. v. Commissioner, TCM 1970-46, rejected the contention of the 501(c)(4) EO that a separately incorporated thrift shop was the agent or integral part of a 501(c)(4) organization. The court reached this conclusion even though the thrift shop operated under a trust agreement in which the 501(c)(4) organization controlled the thrift shop's board, proposed its annual budget (subject to the thrift shop's ultimate control), and received an annual accounting. The court held that the EO had insufficient control over the thrift shop, and never completed necessary paper work to merge the thrift store into itself. The thrift shop was held to be a feeder organization under I.R.C. 502 for the tax years at issue (prior to the enactment of I.R.C. 502(b)(3)). See also TAM 200102051 (Sept. 5, 2000) (501(c)(6) organization did not incur UBTI where its separately-organized members, acting voluntarily and not subject to the control of the 501(c)(6) organization, published advertising for a national business organization in exchange for its payments to the 501(c)(6) organization).

In G.C.M. 39326 (Aug. 31, 1984), it was held that a for-profit management company was not the mere agent of its exempt hospital shareholders. As a result, the for-profit's activities could not be attributed to the parent exempt hospitals. The G.C.M. reasoned:

> For federal income tax purposes, a parent corporation and its subsidiary are separate taxable entities so long as the purposes for which the subsidiary is incorporated are the equivalent of business activities of the subsidiary . . . . However, where the parent corporation so controls the affairs of the subsidiary that it is merely an instrumentality of the parent, the corporate entity of the subsidiary may be disregarded. . . . Thus the activities of a separately incorporated subsidiary cannot ordinarily be attributed to its parent organization unless the facts provide clear and convincing evidence that the subsidiary is in reality an arm, agent or integral part of the parent.

When does a subsidiary act as the "arm, agent, or integral part" of its parent? The Service will rarely question the separate status where the subsidiary actively conducts business (or activities proper for its exempt status), observes basic corporate formalities (being separately organized; keeping separate books and records; maintaining separate bank accounts; maintaining clear distinctions in the activities of overlapping directors, officers, and employees), and does not observe the formalities of an agent. The kind of "agency" control referenced above was analyzed by Judge Learned Hand as follows:

> There are numerous cases in which a parent corporation has been held liable because of control over its subsidiary . . . . Control through the ownership of shares does not fuse the corporations, even when the directors are common to each. One corporation may, however, become an actor in a given transaction, or in part of a business, or in a whole business, and, when it has, will be legally responsible. To become so it must take immediate direction of the transaction through its officers . . . . At times this is put as though the subsidiary then became an agent of the parent. That may no doubt be true, but only in quite other situations; that is, when both intend that relation to arise, for agency is consensual. This seldom is true, and liability normally must depend upon the parent's direct intervention in the transaction, ignoring the subsidiary's paraphernalia of incorporation, directors and officers. **The test is therefore rather in the form than in the substance of the control; in whether it is exercised immediately, or by means of a board of directors and officers, left to their own initiative and responsibility in respect of each transaction as it arises. Some such line must obviously be drawn, if shareholding alone does not fuse the corporations in every case.** [Emphasis added.]

Kingston Dry Dock Co. v. Lake Champlain Transp. Co., 31 F.2d 265, 267 (2d Cir. 1929).[1]

B. UBIT Issues

(1) Advertising: Provided by Agent of EO or Independent Service Provider?

Determining whether an activity is conducted by an agent of an EO can be critical in determining UBIT. Any activity of a corporation conducted for profit is a trade or business for UBIT purposes. See, e.g., Professional Ins. Agents of Michigan v. Commissioner, 78 T.C. 246, 262 (1982), affirmed, 726 F.2d 1097 (6th Cir. 1984). However, if a contractor conducts all or nearly all of the activity and is not an agent of the EO, then the contractor's activity is not attributable to the EO in determining whether the EO "regularly carries on" the activity.

NCAA v. Commissioner, 92 T.C. 456 (1989), rev'd on other grounds, 914 F.2d 1417 (10th Cir. 1990), held that income received by the NCAA (a 501(c)(3) organization) for publishing commercial advertisements in its game programs for the basketball tournament was unrelated business taxable income not excludible as a royalty. NCAA made a written agreement for a Publisher to produce and sell the programs, and to sell advertising to be placed in the programs. Publisher agreed to pay NCAA for publishing and advertising rights the greater of $50,000 or 51% of net revenues. Publisher agreed to indemnify NCAA from claims arising from contracts between Publisher and third parties, or claims arising from the preparation or sale of the programs or advertising.

The Tax Court held that Publisher's activities should be attributed to NCAA as NCAA's agent, since the contract called for Publisher to perform services (1) on behalf of, and (2) under the control of, NCAA. Therefore, NCAA's advertising business was regularly carried on by it. The court noted that the contract designated Publisher as NCAA's "agent" (although contract designation is not controlling); that the contract expressly called for Publisher to "provide services" to NCAA "in an efficient and workmanlike manner"; and that the contract contemplated that Publisher would "represent" NCAA in soliciting advertising. The court also noted that NCAA could control Publisher's activities, particularly by reserving the right to approve all advertising (the court accorded little weight to the fact that NCAA devoted little time to actual oversight). The court found an agency relationship existed despite the compensation structure (which shifted the risk of loss to Publisher) and the indemnification clause in favor of NCAA. Regarding the royalty issue, the court noted that licensors may reserve

[1] Some courts have held the common-law arm/agent/integral part test (sometimes called the "alter ego" test) to be separate from the Moline Properties/National Carbide test and not applicable for federal tax purposes. See United States v. Creel, 711 F.2d 575 (5th Cir. 1983); Wolfe v. United States, 798 F.2d 1241 (9th Cir. 1986) (IRS justified in applying Moline Properties test to tax corporation and common law "alter ego" test to collect taxes).

quality control rights (see Rev. Rul. 81-178, 1981-2 C.B. 135), but that the contract at issue was not a mere license to Publisher to use a valuable right of NCAA; it rather set forth an agency relationship, imposing a duty on Publisher to perform services on NCAA's behalf and under its control. This reasoning is in accord with the general agency principles explained in Part 2 above.

On appeal, the Tenth Circuit did not discuss the agency issue, but held that the advertising business was not regularly carried on. It found that the display of advertising lasted only a few weeks and held that the activity of soliciting and selling advertising is mere "preparatory time" - - not part of the business of advertising. The Service disagrees with this conclusion, since Reg. 1.513-1(b) defines as a fragmented business the activity of soliciting, selling, and publishing advertising.

G.C.M. 39860 (Oct. 7, 1991) involved advertisements in a university's football programs. The University paid a publisher (T) to produce the program. T sold and received the income from the program for a price approved by the University, and also sold and received the income from the advertisements except for several pages reserved for the University. The University received payment from an advertising agency (S) to sell the ads in the reserved space, and provided written guidelines to S prohibiting political advertisements and advertisements for objectionable products. The Service held that S acted as an agent of the university, but T did not. Although T solicited sales in the name of the University, the University did not maintain sufficient control over T for it to be considered the University's agent--T established the advertising rates and bore the burden of profit or loss. Unlike T, S paid the University for the advertisements, received guidance on acceptable advertisements, and was identified as the University's agent in the contract.

State Police Ass'n of Massachusetts v. Commissioner, TCM 1996-407, aff'd, 125 F.3d 1 (1st Cir. 1997), held that income from advertising in the annual publication of a 501(c)(5) labor organization of state troopers was UBTI. The organization contracted with Publisher to conduct advertising on the organization's behalf. The organization argued that the contract designated Publisher as an independent contractor and not as the organization's agent; that the organization had no control over Publisher's personnel or business activities; that Publisher agreed to indemnify the organization from liability resulting from Publisher's activities; and that the contract guaranteed a minimum payment to the organization, shifting the risk of loss to Publisher.

The court noted that the manner in which the parties to an agreement designate their relationship is not controlling. The court concluded that the agreement set forth an agency relationship in substance between Publisher (and its subcontractors) and the organization. Publisher acted on the organization's behalf because Publisher had the authority to use the organization's name in soliciting advertising, and collected payments made payable to Association. Publisher was subject to Association's control because the

organization reserved the right (1) to enter Publisher's offices at any time without prior notice to verify compliance with agreement and (2) to approve advertisements, and Publisher reported weekly to Association on payments received. Thus, Publisher's activities were attributable to Association in determining whether Association's advertising activities were regularly carried on.

The appellate court noted that the facts, taken as a whole, solidly supported the finding that Publisher acted as Association's agent, noting that the Association retained tight control over the method and manner of solicitation, the sales pitch, the identity of solicitors, the financial aspects of the arrangement, the use of the Association's name, the advertising formats, and the contents of the yearbook.

See also Arkansas State Police Ass'n v. Commissioner, TCM 2001-38 (discussed below); TAM 200102051 (Sept. 5, 2000) (discussed above).

(2) Royalties: Does the Licensee Act as the Agent of the EO Licensor?

Some cases present the question whether income received by an EO is excludible from UBTI as a royalty under I.R.C. 512(b)(2). Under the traditional Service analysis, royalties are payments for the use of a valuable right, but not payments for personal services. The EO may retain the right to approve the quality and style of licensed products and services, but the provision of personal services in connection with endorsements results in UBTI. Rev. Rul. 81-178, 1981-2 C.B. 135.

In the cases discussed below (as in NCAA discussed above) the EO characterized the agreement between the EO and another person as a license giving rise to royalties. The Service argued that the EO's level of service in connection with the agreement precluded royalty treatment, and sought to treat the purported licensee as the EO's agent in substance (or alternatively, as the EO's partner in a partnership).

Arkansas State Police Ass'n v. Commissioner, TCM 2001-38, involved an EO that entered into a "Royalties and Licensing Agreement" with a publisher to publish EO's official magazine containing articles and advertising. Publisher solicited the ads in EO's name. EO approved the sales pitches, ads, and editorial content. Publisher bore all production costs, paid EO an annual fee, and received 73% of the proceeds. The EO received 27%. The court rejected EO's royalty argument, reasoning that EO substantially participated in and maintained control over significant aspects of the publication. The court distinguished the mailing list and affinity credit card cases (discussed below) as involving minimal activity on the EO's part. See also Fraternal Order of Police v. Commissioner, 87 T.C. 747 (1986), aff'd, 833 F.2d 717 (7th Cir. 1987).

The Service had less success in recent years in recharacterizing agreements involving mailing lists and affinity credit cards. Sierra Club, Inc. v. Commissioner, 103

T.C. 307 (1994), rev'd, 86 F.3d 1526 (9th Cir. 1996), on remand, TCM 1999-86, involved an affinity credit card program, in which a credit card bearing an EO's name and logo was marketed to EO members. The agreement called for a marketing firm (ABS) to market the credit cards (issued by Chase Lincoln bank) to EO members, and for EO to cooperate with ABS in the marketing. EO received a "royalty" percentage of the total sales volume charged on the cards. EO was similarly compensated for its members' use of an 800 number on the card for travel services. The agreement specifically stated that it did not constitute a partnership or agent/principal relationship between the parties.

The court held that the agreement was essentially a license of the right to use the EO's name, logo, and mailing list in return for royalties exempt from UBTI under I.R.C. 512(b)(2). The Tax Court rejected the Service's argument that the agreement in substance involved a joint venture between EO and the bank, or the EO's provision of services to the bank with ABS acting as EO's agent. On the agency issue, the court emphasized EO's lack of control over ABS: although EO had the right to approve all marketing materials, it had no right to direct the details of ABS's performance. The court also noted that EO lacked a stake in the net profits or losses/expenses of the program; ABS approached EO to propose the agreement, rather than vice-versa; ABS could retain data on credit card customers; EO dealt at arm's length with ABS in accepting advertising from ABS in EO publications; and ABS's use of EO's nonprofit mailing rates was described as a "mistake" by EO. The appellate court remanded the case for further factual development; on remand, the court rejected the argument that EO's quality control rights amounted to control over ABS's operations, and found EO's exercise of such rights consistent with a royalty arrangement.

Common Cause v. Commissioner, 112 T.C. 332 (1999), and Planned Parenthood Federation of America v. Commissioner, TCM 1999-206, both held that brokers who managed the EOs' list rentals were not agents of the EOs, so that list rental payments to the EOs constituted nontaxable royalties. In the mailing list industry, list owners allow "mailers" to use their list for a fee. "List brokers" help mailers find mailing lists to use, coordinate the deal on the mailer's behalf (a "list manager" acts on the list owner's behalf), transfer the payment (less their commission) from mailer to list owner, and analyze the results of the mailing to determine whether it was successful for the mailer. The Service argued, in part, that the list brokers involved were agents of EO in conducting its list rental business, and that any payments they received from mailers for their services should be attributed to EO. The court found that (1) the list brokers (and the list manager where it acted in the capacity as a list broker) acted solely on behalf of mailers and not the list owner, and (2) the list brokers were not subject to EO's control and were thus not agents of the EO list owners.

In the mailing list and affinity credit card cases litigated, most of which were lost by the Service, both taxpayers and the Service advanced all-or-nothing approaches, rather than attempting to bifurcate the payments into part-royalty, part-compensation for services. In a Dec. 16, 1999 memorandum signed by Jay Rotz as Director, EO Division (2000 TNT 46-19), it was noted that the cases decided in favor of the taxpayer generally involved outside contractors (rather than EO employees or members) performing most services associated with exploitation of the use of intangible property. The memo instructed EO Area Managers to resolve royalty cases in a manner consistent with the existing court cases, and to consider requesting technical advice in cases in which the organization provides extensive services, or the facts indicate a good case for allocating the payment between services and the intangible.

(3) Insurance Refunds: Are They Received by the EO as a Principal or as an Agent of the Members?

EOs often are involved in arranging for group insurance to be provided to members. The Service typically regards fees received by the EO for conducting such activity to be UBTI. See, e.g., United States v. Am. Bar Endowment, 477 U.S. 105 (1986). The insurance company often refunds some of the premiums paid by the group to the EO, depending on the claims experience of the group. The question arises whether the refund is includable in the EO's UBTI for the performance of insurance-related services. The answer depends on the circumstances.

In Am. Bar Endowment, supra, the EO required all members to assign to it all such refunds ("dividends") as a condition of participating in the insurance program. The EO claimed that it received the refunds as the agent of the members, so that the refunds constituted charitable contributions by the members. However, the court held that the refunds were in the nature of additional member payments for insurance, and thus UBTI.

By contrast, G.C.M. 38955 (June 29, 1982) involved an EO that offered the refunds to its well-educated, literate members through announcement in a newsletter. Members who did not claim the refund were presumed to have designated the EO as their agent for receipt of the funds. The members were not required to participate in the program. The Service held that the EO acted as the agent of the insured members with respect to the refunds, and therefore the refunds were in fact contributions by the members and not UBTI of the EO.

PLR 8725056 (March 25, 1987) involved a situation and analysis similar to G.C.M. 38955. The EO received refunds from the insurance company. Part of the refunds were used to pay administrative expenses of the EO in managing the insurance program and were conceded to be UBTI. The rest of the refunds could be obtained by member insureds, or retained by the EO. The EO set reasonable deadlines for members to claim refunds, and provided notice by letter and in the EO's journal regarding the right to refunds. This portion of the refunds retained by the EO were accordingly held to be charitable contributions and not UBTI.

See also Rev. Rul. 74-321 and Michigan Retailers Ass'n, discussed below, for situations where the refunds were used for the benefit of the members rather than for contributions.

(4) Special-Purpose Conduit Funds: Does the EO Hold Them as Agent or Trustee for the Members?

Some situations present the issue whether an organization that provides services to its members receives certain payments as agent or trustee of the member-payors rather than as ordinary member dues or fees.

A significant case in this regard is Seven-Up Co. v. Commissioner, 14 T.C. 965 (1950), acq., 1950-2 C.B. 4, acq. in result only, 1974-2 C.B. 4. The case involved a 7-Up manufacturer that sold extract to bottlers. To fund a national advertising campaign negotiated and controlled by the bottlers themselves, nearly all of the bottlers agreed in writing to pay the manufacturer an additional amount per gallon of extract. The manufacturer accordingly billed the participating bottlers. The manufacturer maintained separate accounts for the advertising on its books but commingled the funds with its other funds in its general bank account. The manufacturer did not promptly spend all advertising funds received, but all funds were to be eventually spent on advertising until exhausted. At all times the manufacturer's cash and government securities on hand exceeded the balance of the advertising account. The Service argued that the funds were compensation paid by the bottlers for services and thus includible in the manufacturer's taxable income, and that the manufacturer's advertising expenditures were deductible business expenses.

The court held that the amounts paid by the bottlers constituted a trust fund for advertising, administered by the manufacturer as the bottlers' agent. The court reasoned that such was the parties intent, and not that the manufacturer receive the funds under a claim of right without restriction as to disposition. The court referenced North Am. Consol. Oil v. Burnet, 286 U.S. 417 (1932) for the "claim of right" doctrine, which holds that if a taxpayer receives earnings under a claim of right and without restriction as to disposition, then the taxpayer has income in the year received, even though it may still be claimed that the taxpayer is not entitled to retain the money, and even though the taxpayer may still be adjudged liable to refund it. In the instant case, the Tax Court held that the taxpayer had no claim of right to the funds because it held them as an agent or trustee for the benefit of the payors.

Rev. Rul. 58-209, 1958-1 C.B. 19, involved a nonprofit membership corporation of dealers of related products or services, organized primarily to advertise such products or services. The Service held the member payments to be income to the corporation, distinguishing Seven-Up on the ground that the corporation had other stated purposes and activities, such as compiling and distributing information on effective business methods

and holding conferences for members to exchange business ideas. The Service said that Seven-Up would be followed only where the organization is a conduit for the expenditure of a fund established for a specific purpose.

In Rev. Rul. 74-319, 1974-2 C.B. 15, the Service held on facts similar to Seven-Up that while the manufacturer does not receive income, the fund itself is an association for tax purposes that must report the funds as income and file returns. The revised AOD on Seven-Up (Dec. 3, 1973) reasoned as follows:

> The mere fact that an entity receives funds with an obligation to expend such funds for a specific pre-arranged ultimate purpose beneficial to its contributors is not determinative of whether such entity may treat such funds as nontaxable; if, as in this case, the entity has the power to exercise day-to-day business judgments and to control the details respecting the manner in which the funds shall be expended in achieving the overall purpose, then the entity is not acting as an agent but has the attributes of an independent contractor with respect to such funds and would be taxable on the annual excess of its receipts over expenditures.

In Rev. Rul. 74-321, 1974-2 C.B. 16, a farm loan association conducted a group credit life insurance purchasing program on behalf of borrowers, received and forwarded borrowers' premiums, and received lump-sum dividends on behalf of the group (not allocated to particular members). The Service held that the credit life insurance premiums, and the group dividends used to lower the annual premiums of the group, were not income to the association. The Service reasoned, under the Seven-Up doctrine, that the association acted as agent in dealing with the premiums and dividends under the intent of the parties, had only ministerial powers over the funds, and could not divert them to its own purposes.

Michigan Retailers Ass'n v. United States, 676 F.Supp. 151 (W.D.Mich. 1988), involved a tax-exempt business league that conducted a group insurance purchasing program for its members. The organization argued, and the court held, that the premiums and experience credits received by the organization were not income to the organization, but were effectively held in trust despite the absence of an express trust agreement (the organization in later years had formally created a trust to conduct the activity).

The courts have been more liberal than the Service in finding a conduit , agency or constructive trust, regardless of the breadth of its purposes, and in not considering the fund as an association with taxable income. See Florists' Transworld Delivery Ass'n v. Commissioner, 67 T.C. 333 (1976); Schochet v. Commissioner, TCM 1982-416; Field Service Advice CC:FS-I-58333-96 (Aug. 7, 1996). As noted in Schochet, the courts have sometimes used terms such as "trustee," "agent," or "conduit" in such cases for purposes of analogy, rather than in the technical legal sense, in finding that the funds are not

income to the intermediary holder of them. The Service seeks to limit application of this doctrine, however, given its serious abuse potential.

C. Charitable Contribution and Public Support Issues

The nature, sources, and timing of an organization's support (aside from UBIT considerations) can be affected by matters of agency. Situations that involve the issue whether a person receives contributions or income as an agent of the EO are discussed in parts 1-6 below. The issue whether an EO receives funds as an agent of another person is discussed in part 7. Most of the precedents in this area are under I.R.C. 170 rather than subchapter F, but the same principles generally apply.

(1) Is the Recipient of Contributions Acting as the Agent of the EO?

A contribution made to an EO's agent is considered received by the EO. Thus, in Rev. Rul. 55-192, 1955-1 C.B. 294, the portion of membership dues of a social club earmarked for distribution to qualified charities was a deductible charitable contribution when paid to the club treasurer, where the treasurer was designated by the charities as their agent. If the treasurer had not been designated by a charity to act as its agent, he would be considered the agent of the contributor, and contributions would be deductible only in the tax year actually transferred to the charity. See also Rev. Rul. 57-487, 1957-2 C.B. 157. Reg. 1.170A-1(b) contains special rules for the timing of contributions of stock, which depend on whether the intermediary receiving the gift is the agent of the charitable donee.

Similarly, Rev. Rul. 85-184, 1985-2 C.B. 8, held that utility customers, who paid additional amounts on their utility bills to a utility company acting as agent for a charity that assisted individuals with emergency energy needs, were entitled to a charitable deduction for the additional amounts in the year paid. The charity established the program and made an agreement with the utility designating it as the charity's agent for collecting contributions. The utility bill solicited contributions. Amounts collected were segregated from other utility funds and transferred to the charity on a weekly basis. The utility did not exercise dominion or control over the charitable funds and did not draw upon them to cover expenses incurred in connection with the program. The Service reasoned that the utility acted as the charity's collection agent and exercised no control over donations.

PLR 8707074 (Nov. 19, 1986), involved a 501(c)(4) veterans organization that hired an independent contractor (M) to operate a thrift shop. The contract designated M as the organization's agent. Under the contract, M was authorized to solicit and pick up donations at the donor's residence on the organization's behalf, and deliver the goods to M's place of business. Upon delivery, the goods were deemed sold by the organization to M for a fixed "per-pick-up" price (determined by the State Attorney General to be

acceptable), and M's status as agent with respect to the delivered goods terminated. The Service held that the contributions were deductible by the donors under I.R.C. 170(c)(3), and that the donated goods exception to unrelated business under I.R.C. 513(a)(3) applied.

Used car charitable donation programs have proliferated lately. These programs typically involve a contract between a charity and a dealer for the dealer to receive the donated car, sell the car, and distribute some amount to the charity. The Service has been concerned with some of these programs, for several reasons. One is overvaluation of the charitable deduction by donors, with the encouragement and assistance of the charity and dealer involved. Another is inurement or private benefit to the dealer, if the contract is unreasonable or was not made at arm's length. Another issue in some cases is whether the relationship between the charity and dealer is that of principal and agent. Some charities may fail to exercise any real supervision over the dealer's activity and may lack even the right to exercise significant control under the contract. In such case, the dealer would not be the charity's agent, because the arrangement did not give the charity the over-all control over the purported agent that is required by Restatement § 1. If the dealer is not the charity's agent, then the donor may be denied a charitable deduction, and the income received by the charity may be gross income from unrelated business received from a single source (the dealer) rather than contributions or other public support. The Service is studying this issue. For further discussion, see the May 27, 1999 memorandum from Marcus Owens, Director, EO Division (1999 TNT 117-45), and "Fund-Raising Issues," 2000 CPE 267.

(2) Are Workers Agents of EOs When They Deflect Earned Funds to the EOs?

A fundamental federal income tax principle is that a person who earns income is taxed on it, even if he makes an advance assignment of the income to another. In the words of Justice Holmes in Lucas v. Earl, 281 U.S. 111, 115 (1930), the fruits are not "attributed to a different tree from that on which they grew." Accordingly, Reg. 1.61-2(c) provides that:

> Where. . . pursuant to an agreement or understanding, services are rendered to a person for the benefit of an organization described in section 170(c) and an amount for such services is paid to such organization by the person to whom the services are rendered, the amount so paid constitutes income to the person performing the services.

In Rev. Rul. 57-135, 1957-1 C.B. 307, members of a church provided volunteer services to an exempt hospital at the direction of the church. The hospital donated funds to the church based primarily on the pay employees normally receive for such work. The volunteers were treated as agents of the church, received no taxable income, and the funds were hospital contributions to the church.

On the other hand, in Rev. Rul. 58-495, 1958-2 C.B. 27, an industry labor management committee agreed to donate a portion of the wages of member-employees to certain charitable organizations. The employees provided no direct services to the charities. Citing Reg. 1.61-2(c), supra, the Service held that all of the donated wages were taxable to the employees, since the employees were not the agents of the charities.

Rev. Rul 58-235, 1958-1 C.B. 26, involved the appearance by an EO's executive director as a contestant on a quiz show. The show's producer invited him because he was well known. He agreed to appear because the EO's board approved his diverting time for the show. Part of his duties as executive director was fundraising. He requested the producer to pay any prize he might win directly to the EO, and his prize winnings were so paid. The Service held that the executive director received the income, reasoning that appearing on quiz shows was not part of the executive director's duties, and the director was thus not the agent of the EO for this purpose.

Thus, assignment-of-income cases turn on whether the person earning the income is truly acting in the capacity of an agent. If so, then the principal, not the agent, receives the income. If not, then the transaction is treated as income to the person who earned it (and ordinarily as a contribution from that person to the assignee).

(3) Religious Order Members: When Are They Agents of the Order in Receiving Compensation?

The controversies in the assignment-of-income area have largely involved members of religious organizations performing services as employees of other organizations. In Rev. Rul. 68-123, 1968-1 C.B. 35, a member of a 501(c)(3) religious society was held to be acting as the society's agent in serving as a nurse at a hospital. A purpose of the society was to provide personnel to hospitals, the society assigned her to serve there, and the nurse remained under the society's general direction and control, although the details of her daily activities were supervised by the hospital. The nurse had no right to direct the disposition of the society's funds, and the society requested that the hospital directly pay the nurse's compensation to it. Although the hospital made the payroll checks to the nurse, the nurse immediately endorsed them over to the society. The underlying G.C.M. (33574, July 28, 1967) indicated that the hospital was affiliated with the society.

The scope of Rev. Rul. 68-123 was limited in subsequent rulings and cases. Rev. Rul. 76-323, 1976-2 C.B. 18, held that amounts received by members of an exempt religious order for work performed outside the religious community and paid over, in full or part, to the order at its direction, were includible in the members' incomes, but the members were entitled to I.R.C. 170 deductions for amounts donated to the order. In considering whether the members acted as agents, the Service reasoned that ordinarily, a member performs services as an agent only if the order is engaged in the performance of such services as principal. Ordinarily an order is not engaged in the performance of

services as principal where the legal relationship of employer and employee exists between the member and a third party regarding such services.

Rev. Rul. 77-290, 1977-2 C.B. 26, reached a similar conclusion as Rev. Rul. 76-323, despite the fact that the member of the religious order had taken a vow of poverty. The Service applied the same assignment-of-income and agency principles. A distinction was drawn between a member being directed to perform services for another agency of the supervising church or an associated institution (the member is considered an agent for the order), and a member being directed to undertake outside employment (the member is not an agent). Accord, Kelley v. Commissioner, 62 T.C. 131 (1974). Rev. Rul. 80-332, 1980-2 C.B. 34, applied the ruling of Rev. Rul. 77-290 to members of 501(d) organizations.

Rev. Rul. 77-436, 1977-2 C.B. 25, involved a member of a religious order who was also a trust beneficiary. Under a vow of poverty, the member turned over all payments from the trust to the order. The trust instrument prohibited assignment of the beneficial interest in the trust. The Service ruled that the member received income and charitable contribution deductions.

Rev. Rul. 83-127, 1983-2 C.B. 25, involved a member of a religious order instructed to secure employment as a teacher in a 501(c)(3) secular private school. The member contracted with the school in an individual capacity, and remitted the paychecks to the religious order. The Service ruled that the member did not receive the school pay as agent of the order and had to take it into income.

Rev. Rul. 84-13, 1984-1 C.B. 21, involved a member of a religious order who conducted a private practice as a psychologist with permission of the order and, under a vow of poverty, paid all earnings to the order. The Service held that the member did not serve as an agent of the order because the order did not control the member's work other than to review the member's annual budget, the services were not the type provided by the order, and the clients looked directly to the member rather than the order for the performance of the services.

Schuster v. Commissioner, 84 T.C. 764 (1985), aff'd, 800 F.2d 672 (7th Cir. 1986), held that a nurse was not an agent of a religious order where she served as an employee of the federal government, which assigned her to work at a clinic. The work satisfied her obligation to the government to work in a health manpower shortage area for receiving federal funds for her education. The nurse handled all aspects of her relationship with the federal government and clinic, except that the religious order sent letters stating that the order wished to contract with them for the nurse's services and for her wages to be paid directly to the order. The federal government issued the checks to the nurse; the clinic advised the order that the nurse could endorse them over to the order.

The court cited two relevant factors: lack of evidence of agreement between the order and the government/clinic such that the latter would look to the order for performance of the nurse's services; and lack of direction and control by the order over the nurse in the nurse's duties with the clinic and government (the order could grant or deny her request to serve in the federal government, and reject an offered position, but otherwise lacked control over the appointing process). The court distinguished the situation from one where a nurse works in facilities of the order. Accord, Fogarty v. United States, 6 Cl.Ct. 612 (1984), aff'd, 780 F.2d 1005 (Fed. Cir. 1986) (religion professor at State university); Kircher v. Commissioner, 14 Cl.Ct. 738 (1988), aff'd, 872 F.2d 1014 (Fed. Cir. 1989) and McEneany v. Commissioner, TCM 1986-413 (chaplains at State hospitals). In reaching their conclusions, the courts of appeals relied on a flexible six-factor test set forth in Fogarty: (1) degree of control exercised by order over member; (2) ownership rights between member and order; (3) purposes or mission of order; (4) type of work performed by member vis-à-vis purposes or mission of order; (5) dealings between member and third-party employer; and (6) dealings between order and third-party employer.

(4) Are Church Leaders Handling Funds as Agents of their Churches?

The Service has had problems with persons seeking to avoid tax on their earnings by forming a "church." Typically, the church acts as little more than the bank account of the individual, who assigns his outside employment to the church and pays his personal expenses with the use of the church funds. The Service and courts have routinely denied exemption to these organizations on the grounds of inurement and private benefit. Moreover, the individual is deemed to act individually and not as church agent in his outside employment. See, e.g., McGahen v. Commissioner, 76 T.C. 468 (1981), aff'd, 720 F.2d 664 (3d Cir. 1983); Duck v. Commissioner, TCM 1984-212; Mone v. Commissioner, 774 F.2d 570 (2d Cir. 1985); Pollard v. Commissioner, 786 F.2d 1063 (11th Cir. 1986).

On the issue whether a church leader handles funds received from the church on behalf of the church rather than for personal use, see United States v. Moon, 718 F.2d 1210 (2d Cir. 1983) (conviction for failure to pay personal income taxes upheld where the evidence established that the defendant held assets personally and not for the benefit of the church); Church of Scientology of California v. Commissioner, 83 T.C. 381 (1984) (church's net earnings inured to founders where they had unfettered control over funds purportedly belonging to a separate church corporation and trust).

(5) Other EO Staff Receiving Funds as Agents of EOs

In many situations, physicians and lawyers work for EOs with an agreement that all funds received from patients or clients for services rendered must be turned over to the EOs. In appropriate situations, the professional is treated as the agent of the EO and is not taxed on receipt of such funds.

Examples of persons affiliated with EOs considered to receive payment as agents of the EO include: Rev. Rul. 58-220, 1958-1 C.B. 26 (employee physicians of hospital occasionally receiving direct payment from patient and immediately endorsing over to hospital); Rev. Rul. 65-282, 1965-2 C.B. 21 (employee attorneys for legal aid society receiving government fees for court appointments and immediately endorsing over to society under terms of employment contract); Rev. Rul. 69-274, 1969-1 C.B. 36 (faculty physicians made available by university to local hospital to teach hospital workers and provide medical care to indigent patients and required by university to remit all Medicare or other fees to university); Rev. Rul. 74-581, 1974-2 C.B. 25 (law school faculty and students representing indigent defendants as part of curriculum's clinical program and required by law school to remit all court-paid fees for services to law school); and Rev. Rul. 76-479, 1976-2 C.B. 20 (medical staff of a nonprofit hospital who form medical research foundation and treat patients with limited incomes on behalf of foundation to collect research information, where the foundation establishes the treatment program and fee schedule and collects the funds for its own use).

Rev. Ruls. 66-377, 1966-2 C.B. 21, and 69-275, 1969-1 C.B. 36, are instructive situations where EO medical staff are not considered to act as agents. Rev. Rul. 66-377 held that where a university medical school permitted faculty to operate in private practice but part or all of the earnings from the practice were required to be turned over to the university, the amounts required to be turned over were income to the faculty, but the faculty received a business expense deduction under I.R.C. 162. Rev. Rul. 69-275 involved a charitable hospital whose staff physicians treated patients admitted without a physician's recommendation. Some physicians voluntarily agreed to assign all patient fees to the hospital. The Service held that the physicians had to include such fees in income, but could claim a charitable contribution for the assignment. The Service distinguished Rev. Rul. 66-377 as involving a required assignment.

(6) Persons Conducting Their Own Businesses but Claiming to Be Agents of EOs

Business organizations may periodically set aside a day as "charity day" and contribute their net income from that day's business to a charity. In such situations, where a person is conducting its ordinary trade or business on a short-term basis for the benefit of an EO, the Service has developed special rules for applying the assignment-of-

income doctrine. The business will not be considered the charity's agent if the business is considered the "promoter" of the event.

Rev. Rul. 72-542, 1972-2 C.B. 37, held a race track corporation's charity day proceeds turned over to a charity to be income to the track, where the track was deemed the promoter and not the charity's agent under the facts presented (no lease of the track to the charity; the track provided the liability insurance for the event; the track conducted the advertising and promotion). The track received a charitable deduction for the distribution to the charity.

Rev. Rul. 77-121, 1977-1 C.B. 17, distinguished Rev. Rul. 72-542. It held the charity rather than the racetrack to be the promoter of charity day. Under the agreement between the charity and the track, the charity assumed all responsibility for promoting the event and agreed to absorb any losses arising from the event. Although the track received reimbursement of expenses, they were deemed incurred as the charity's agent and thus not includible in the track's gross income.

Rev. Rul. 77-124, 1977-1 C.B. 39, involved facts like Rev. Rul. 72-542, except that the track was required to conduct the charity days as a condition of obtaining its license to operate the track. The Service held the distributions to charity to be business expenses under I.R.C. 162 rather than charitable contributions.

G.C.M.s 35630 (Jan. 22, 1974) and 36375 (Aug. 12, 1975) elaborate on the "promoter" concept. The promoter is considered as the true principal. A written agreement designating the business as the charity's agent is not dispositive. All facts are taken into account. Other critical facts include whether the track could conduct the event on its own behalf rather than the charity's behalf; who provides and controls the employees and management; and who handles the proceeds (if the track employees, are the funds segregated?)

Rev. Rul. 58-276, 1958-1 C.B. 23, held that a TV station did not receive income where it conducted a "telethon" to solicit contributions for a charity and transferred all contributions (unreduced by any expenses incurred) to the charity. G.C.M.s 35630 and 36375 distinguished Rev. Rul. 58-276 from Rev. Rul. 72-542: the TV station was not receiving the contributions as payment for its services, but was merely using its facilities to solicit donations from viewers.

(7) Is the EO the Agent of Another Person for Charitable Deduction or Support Purposes?

Some cases involve the question whether the EO that receives the donation or income is itself acting as an agent for the payor or for another EO.

The Service's longstanding position is that an EO receives a charitable contribution where it has full control and discretion as to the use of donated funds, but not where the donor earmarks the contribution for use by an individual or nonexempt organization (or makes the contribution pursuant to a commitment or understanding that the funds will be so used). Rev. Rul. 62-113, 1962-2 C.B. 10. In the latter situation, the charity acts like an agent of the donor.

Rev. Rul. 63-252, 1963-2 C.B. 101, involving the deductibility of contributions to domestic charitable organizations that transfer funds to foreign organizations, can also be understood largely in agency terms. Contributions are not deductible where the domestic organization acts as an agent or conduit for the foreign charity, rather than exercising independent control over the funds. Contributions to foreign charities are not deductible for income tax purposes. The contribution must be to an American charity to be deductible. See "Foreign Activities of Domestic Charities and Foreign Charities," 1992 CPE 220, 225-232, for a fuller discussion of this area.

Donor-"directed" or "advised" funds involve similar considerations. G.C.M. 39875 (June 24, 1992) withdrew for reconsideration G.C.M. 39748 (Jan. 27, 1988). G.C.M. 39748 had reasoned that earmarked contributions would not be support to a donor-directed fund if the fund received them only as agent of donors for delivery to ultimate recipients, and would not be deductible by donors until delivered to ultimate recipients. The rulings held that there was no evidence that the funds at issue received the contributions only as agents of the contributors (citing Aufiero, discussed above). Such funds have been discussed in a number of CPE texts, most recently "Control and Power," 2001 CPE 107, 119-122. If the fund acts as an agent of the contributors, then the contributions may not constitute support to the fund for I.R.C. 509 purposes, and the fund may not be operated exclusively for exempt purposes. See Fund for Anonymous Gifts v. IRS, 79 AFTR 2nd 2520 (D.D.C. 1997), vacated on other grounds, 194 F. 3d 173 (D.C. Cir. 1999).

In some cases, the donor wants the intermediary EO to be treated as an agent or conduit. For instance, Rev. Rul. 55-1, 1955-1 C.B. 26, held that a donation to a non-170(b)(1)(A) fundraiser charity, acting as the donor's transfer agent for direct and unconditional delivery to a 170(b)(1)(A) public charity, was made to the public charity for deductibility purposes. Rev. Rul. 55-269, 1955-1 C.B. 26, held that donations to a 501(c)(4) organization for the purpose of distributing its literature to 501(c)(3) organizations were not deductible, where the 501(c)(4) organization was held to be acting in furtherance of its own purposes rather than as the donor's agent. Accord, Kluss v. Commissioner, 46 T.C. 572 (1966). Appleby v. Commissioner, 48 T.C. 330 (1967), held that a gift to a charitable trust whose sole beneficiary was a college was not a gift "to" the college (as the trust was not an agent of the college) but only "for the use of" the college, for purposes of the higher 170(b)(1)(A) charitable deduction.

Rev. Rul. 75-387, 1975-2 C.B. 216, held that a blood bank that supplied blood for use by hospital patients for a fee qualified as a public charity under I.R.C. 509(a)(2). Participating hospitals agreed that all blood furnished to them remained the property of the blood bank until used, subject to the blood bank's direction and control; that the hospitals were responsible for collecting charges from patients for use of the blood and reimbursing the blood bank; and that the hospitals were liable for any amounts uncollected from patients ("guarantee payments"). I.R.C. 509(a)(2)(A) generally treats gross receipts from related business as good support to the extent of the greater of $5000 or 1% of the organization's support received from any person. The main issue was whether the "person" subject to the $5000/1% limitation was the hospital (in which case the blood bank would not qualify under I.R.C. 509(a)(2)) or the hospital patient. The Service reasoned that under the facts presented, the hospitals acted as the agents of the blood bank, and therefore the amounts received by the blood bank were received from the patients, except for the guarantee payments. The Service noted that the hospitals' guarantee of amounts they failed to collect did not preclude their status as agents of the blood bank, citing Restatement § 14 J, comment b(2). See also United States v. General Electric Co., 272 U.S. 476 (1926), which held that retail sellers of GE lamps acted as sales agents of GE rather than as buyers from GE, even though the retail sellers guaranteed payment to GE for all merchandise sold.

D. Exemption Issues

(1) Effect on 501(c)(3) Exemption Where the Organization Serves as Agent

Some cases involve whether an organization may act as an agent on behalf of other 501(c)(3) organizations (or other persons) and qualify for exemption. The answer will depend on the circumstances. For instance, Rev. Rul. 64-275, 1964-2 C.B. 142, held exempt under I.R.C. 501(c)(3) a sailboat racing school, one of the activities of which was acting as agent of the 501(c)(3) U.S. Olympic Association in selecting boats/teams for international competition. The organization’s primary purpose and activities were to conduct athletic education and training programs.

Rev. Rul. 75-283, 1975-2 C.B. 201, held exempt under I.R.C. 501(c)(3) an association of public housing tenant organizations that acted as the State-recognized agent for public housing tenant organizations before the State public housing agency to negotiate solutions to State-wide problems. The organization also conducted substantial educational programs for public housing tenants. The ruling held that the purposes and activities were primarily educational.

Problems arise where the agent activity is commercial in nature. The Service's longstanding position is that an association formed by or in support of unrelated 501(c)(3) organizations to conduct commercial activities on a cooperative basis is not exempt. See Reg. 1.502-1(b). For example, Rev. Rul. 54-305, 1954-2 C.B. 127, held

that a purchasing agency for unrelated exempt members was a nonexempt feeder organization. Similarly, Rev. Rul. 67-327, 1967-2 C.B. 187, denied 501(c)(3) status to an organization whose sole activity was arranging group tours as a travel agent for university students and faculty.

By contrast, Rev. Rul. 67-392, 1967-2 C.B. 191, granted 501(c)(3) status to an organization that helped young musical artists by conducting workshops, sponsoring concerts, and securing paid engagements by the artists. The Service distinguished the booking activity from that of for-profit agents because the organization did not charge a fee and only booked for those who lacked sufficient professional standing to support themselves through engagements.

In some situations, an EO distributes funds to individuals or nonexempt organizations in their alleged capacity as the EO's agent. If the reality is otherwise, the EO may be said to serve private interests rather than exclusively exempt purposes. For example, G.C.M. 36618 (March 10, 1976) involved an organization that reimbursed a person who paid a ransom to secure the release of individuals kidnapped while studying wildlife. The Service reasoned that the ransoming of prisoners has in certain contexts been recognized as a charitable activity. However, the person who paid the ransom did not act as the organization's agent in doing so, as the organization at that time had not even adopted its program of financial assistance. Therefore, the organization's reimbursement did not free any hostages, but only enriched the person who paid the ransom, resulting in private benefit.

(2) How Acting as Agent Will Affect Other 501(c) Exemptions

Rev. Rul. 86-98, 1986-2 C.B. 74, held not exempt under I.R.C. 501(c)(4) an "individual practice association" of physicians. The association primarily served as an agent for its members in dealing with HMOs (bargaining and collecting payment). The Service reasoned that the organization’s primary activities benefited the member physicians and did not qualify as social welfare activities under I.R.C. 501(c)(4). In addition, the Service held that the activities were particular services and thus did not qualify for exemption under I.R.C. 501(c)(6).

A primary purpose of labor organizations is to collectively bargain with employers through collective bargaining agents. Serving as the members’ agents for this purpose is therefore an exempt activity under I.R.C. 501(c)(5). See Rev. Rul. 59-6, 1959-1 C.B. 121. Similarly, acting as farmers’ agents to better their economic and other conditions is an exempt purpose under I.R.C. 501(c)(5). This includes negotiating with food processors over the price to be paid to members for their crops. Rev. Rul. 76-399, 1976-2 C.B. 152. However, in Rev. Rul. 66-105, 1966-1 C.B. 145, the Service denied 501(c)(5) status where the organization not only was the farmers’ agent for negotiating prices, but also acted as their agent to market their livestock, including furnishing the necessary

labor, advertising, bookkeeping and physical facilities. The ruling held that these additional activities were not described in I.R.C. 501(c)(5). Accord, G.C.M. 36192 (March 14, 1975).

Organizations that serve as agents of their members to perform various non-exempt activities are typically denied exemption under I.R.C. 501(c)(6), on the basis that they are providing particular services. For example, in Rev. Rul. 86-98, 1986-2 C.B. 74, an individual practice association serving as a bargaining and collection agent for physicians was denied I.R.C. 501(c)(6) exempt status. G.C.M. 39723 (Aug. 31, 1987) held that an association of insurance agents was not described in I.R.C. 501(c)(6) where it performed various insurance-related services for a fee, as a middleman between its member agents and governmental unit insureds. The Service reasoned that it engaged in business typical of a for-profit insurance agent or broker, and performed particular services for members.

Rev. Rul. 73-307, 1973-2 C.B. 186, held that a 501(c)(17) supplemental unemployment benefit plan may permit an employee to authorize the trustee to deduct and pay union dues from his benefit payments. Such action is not the diversion of income to a purpose other than providing supplemental unemployment benefits, because the trustee acts as the employee's agent in making the payment.

(3) Agency in Political Intervention Issues.

The question whether the political activities of an individual or organization are attributable to a 501(c)(3) organization is discussed at length in "Election Year Issues" in this year's CPE text. See also "Affiliations Among Political, Lobbying and Educational Organizations," 2000 CPE 255.

(4) Whether Individuals Performing Illegal Act Are Agents of Exempt Organizations

For discussion of whether the illegal activities of individuals are attributable to an EO, see "Activities That Are Illegal or Contrary to Public Policy," 1985 CPE 109, 110-11; "Illegality and Public Policy Considerations," 1994 CPE 155, 167-69.

4. Conclusion

Questions of agency arise in many different situations involving EOs--the above discussion is not comprehensive. In determining whether an agency relationship exists between an exempt organization and another person, a number of facts and circumstances may be relevant, depending on the situation. Verifying the written agreement and the actual course of dealing between the parties is of critical importance. Factors that the

Service and the courts have considered important in determining that a principal/agent relationship exists vary somewhat, depending on the situation, but generally include the following (drawn from the authorities discussed above):

- the agent is designated as such in a written agreement
- the agent conducts business in the name of the principal or otherwise makes his agency known to third parties
- the agent's acts are legally binding on the principal
- the agent transfers funds received to the principal, or uses them as directed by the principal, rather than using them for his own purposes
- the income received by the agent is attributable to services and assets of the principal
- the agent's sole business activity is acting as an agent
- the agent does not take title to property in his own name (except as a nominee)
- all or part of the agent's activity is subject to the principal's right to approve or control (e.g., right to inspect agent's offices or books, right to approve agent's publications, right to approve agent's manner of conducting activity, right to approve business clients, right to approve agent's budgets)
- the principal actually exercises control or supervision over part or all of the agent's activity
- the principal rather than the agent bears the risk of loss in the transaction
- the principal indemnifies and insures the agent in his agency activities
- the agent is required to financially account to the principal
- the agent uses the principal's nonprofit mailing rates or sales tax exemptions
- the agent is otherwise subject to the principal's control under the facts and circumstances
- where the agent performs services for others for a fee, the person receiving the services contracts with the principal and looks to the principal rather the agent for

performance, and the agent's services are activities ordinarily engaged in by the principal and fulfill its purposes

- in "charity day" situations, the principal conducts the advertising, bears the risk of loss, leases the agent's facilities, provides the liability insurance, provides the employees and management, and handles the proceeds, and the agent is not required to conduct the event as a condition to obtaining its license to conduct non-charity business