Analysis of Joint Venture/Partnership with For-profit Entity

The IRS has indicated that inquiries such as the following are relevant in determining whether a joint venture/partnership in which an exempt entity is a general partner with a for-profit partner furthers exempt purposes of the exempt organization and whether private benefit to the for-profit partner and/or manager is more than incidental.

1. Is the exempt entity’s participation due to a need for capital, expertise, or assets? __ Yes __ No __ N/A

2. Do governing partnership documents require the partnership to operate for charitable purposes by community benefit standards [i.e., to engage in activities that promote the exempt entity’s exempt purpose(s)]? __ Yes __ No __ N/A

3. Do governing partnership documents:
   a. Explicitly require board members to give the exempt purpose(s) of the exempt entity priority over any other fiduciary duty, such as maximizing profits or otherwise operating for the financial benefit of the for-profit partners or members? __ Yes __ No __ N/A
   b. Have a dispute resolution provision that would cause the joint venture to satisfy charitable purposes without regard to profitability when a disagreement arises between the board and the members over the joint venture’s policies or actions? __ Yes __ No __ N/A
   c. Give the exempt organization the unilateral right, if a CEO manages the day-to-day affairs of the joint venture, to remove the CEO if he or she is not acting to further (or is acting contrary to) the exempt organization’s charitable purposes? __ Yes __ No __ N/A

4. Is there evidence that partnership activities are undertaken primarily to promote an exempt purpose rather than to produce profits? __ Yes __ No __ N/A

5. Does the exempt entity appoint a majority of the governing board of the partnership or have effective control over the affairs of the partnership? __ Yes __ No __ N/A

6. Are the members of the governing board that are appointed by the exempt entity:
   a. Experienced in activities conducted by the partnership? __ Yes __ No __ N/A
   b. Persons who do not normally engage in business transactions with the exempt entity? __ Yes __ No __ N/A
   c. Representative of the community? __ Yes __ No __ N/A

7. Must a majority of all board members approve:
   a. Changes in the partnership’s governing documents? __ Yes __ No __ N/A
   b. The partnership’s annual capital and operating budgets? __ Yes __ No __ N/A
   c. Distributions of cash or property? __ Yes __ No __ N/A
   d. Capital contribution calls? __ Yes __ No __ N/A
   e. Partnership incurrence or assumption of significant indebtedness? __ Yes __ No __ N/A
f. Acquisition of additional business operations or major operational assets?  ____  ____  ____

g. Unusually large contracts?  ____  ____  ____

h. Material changes in the types of services, if any, provided by the partnership?  ____  ____  ____

i. Material changes in fees or prices for the partnership’s services, if any?  ____  ____  ____

j. Selection of key executives of the partnership?  ____  ____  ____

k. Renewal or termination of management agreements?  ____  ____  ____

l. An outside audit of the partnership?  ____  ____  ____

8. If there is a management firm:

   a. Is it unrelated to the for-profit partner?  ____  ____  ____

   b. Is its fee reasonable based on fees charged by other management firms for similar services (rather than an improper revenue-sharing agreement)?  ____  ____  ____

   c. Are the terms of the management agreement customary and reasonable, especially those concerning the length of the contract, renewals, and termination rights?  ____  ____  ____

   d. Does it have any duties that may conflict with the partnership’s ability to carry out its exempt purpose(s)?  ____  ____  ____

   e. Do its powers restrict the authority of the exempt entity’s board to initiate or react to decisions that are appropriate to carrying out the entity’s exempt purpose(s)?  ____  ____  ____

   f. Does it have a binding and enforceable obligation to further the charitable purposes of the exempt organization?  ____  ____  ____

   g. Do the governing partnership documents give the exempt organization the unilateral right to terminate the management agreement if the management company is not acting to further (or is acting contrary to) the exempt organization’s charitable purposes?  ____  ____  ____

9. Are the partnership’s accounting and law firms:

   a. Selected and engaged by the board?  ____  ____  ____

   b. Different from the firms providing services to the for-profit partner?  ____  ____  ____

10. Must the allocation of partnership profits or losses be proportionate to capital contributions?  ____  ____  ____

11. Does the exempt entity have meaningful control over the quality of services, if any, performed by the partnership?  ____  ____  ____

12. Have all sales or leases of land or other property to the joint venture by the exempt organization been at or above fair market value (FMV)?  ____  ____  ____

13. Are all loans to the joint venture by the exempt organization being made at or above the prevailing interest (AFR) rate for similar loans?  ____  ____  ____

14. Are all loans to the joint venture by the exempt organization secured?  ____  ____  ____

15. Is the exempt organization adequately compensated for services it renders to the joint venture?  ____  ____  ____
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<tr>
<th>Question</th>
<th>Yes</th>
<th>No</th>
<th>N/A</th>
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<td>16. Does the exempt organization receive an economic benefit from the partnership commensurate with its investment in it?</td>
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<td>17. If a general partner, does the exempt organization exert control over the normal day-to-day operations of the partnership?</td>
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<td>18. Are the provisions in the joint venture agreement with respect to charitable activities legal, binding and enforceable under the laws of the state where the joint venture was formed?</td>
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<td>19. Does the joint venture agreement contain a non-compete provision that causes the exempt organization to yield significant market advantages and competitive benefits to the for-profit partner or member?</td>
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<td>20. Were any of the exempt entity’s board members, officers or key employees offered financial incentives of any kind to approve the exempt entity’s participation in the partnership?</td>
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<td>21. Do any of the exempt entity’s officers, directors or key employees have any ownership, either directly or under the attribution rules of IRC Sec. 318, in the for-profit partner or any of its affiliates?</td>
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<td>22. Are any of the exempt entity’s representatives on the partnership’s board dependent on the partnership’s activities for their livelihood?</td>
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<td>23. Does the exempt entity have specific responsibilities to the partnership that could interfere with its requirement to operate exclusively for exempt purposes?</td>
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Notes:

“Yes” answers to questions 1–18 and “No” answers to questions 19–23 indicate that the partnership furthers the exempt entity’s exempt purposes and allows the exempt partner to act exclusively in furtherance of its exempt purpose(s), with private benefit to the for-profit partner being incidental.

The ultimate determination of whether the partnership jeopardizes the exemption of the exempt partner is based upon all the facts and circumstances. Consequently, all of the answers to questions 1–18 need not necessarily be “Yes,” nor do all of the answers to questions 19–23 necessarily need be “No.” No single question is determinative.