Will Reimbursing Board Members Risk Tax–Exempt Status?

Is it O.K. to pay your board members for their meeting expenses? Or will doing so jeopardize your organization's tax–exempt status?

Q: Our nonprofit 501(c)(3) organization is a membership association. We have seven board members, most of whom are elected from our membership.

Our policy for covering board expenses states, "Expenses for members of the board of directors and staff that will be paid or reimbursed are: air fare, mileage (not to exceed the cost of a coach, round-trip airline ticket), lodging, and meals for approved trips."

One of those approved trips is coming up soon. Board members will be attending our organization's annual convention and will hold their annual board meeting there.

The board treasurer has announced that our organization will pay for board members to attend a sightseeing trip offered by the convention hosts. The cost is $25 per board member.

My question is this: Since sightseeing trips are not listed in our policy on board expenses, is it O.K. for the organization to pay for them? Or are we jeopardizing our 501(c)(3) tax–exempt status by using membership dues and donated funds to pay for board members' entertainment?

A: As you know, your organization must meet certain conditions to qualify for tax–exempt status under Internal Revenue Code 501(c)(3). One requirement is known as the private inurement standard. It states that your organization's earnings cannot benefit anyone with a personal interest in your organization's activities. Your board members qualify as people with such an interest.

Thus, paying board members' expenses which aren't directly connected to the organization's purposes may be considered private inurement. Such payments may indeed place your organization's tax exemption at risk.

Whether an expense qualifies for reimbursement under organization policy is irrelevant with respect to whether private inurement exists. If it were your organization's policy to make loans to board members at 0% interest, for example, you would still jeopardize your 501(c)(3) status by exercising such a policy.

Your organization's exemption is theoretically at risk if the slightest bit of private inurement exists. However, the additional $25 for each board member is

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barely a blip on the radar screen. It is O.K. for an organization to bear the incidental cost of refreshments for special events, and the inexpensive sightseeing trip you mention is somewhat comparable to such "refreshments." Moreover, most cases in which 501(c)(3) status has been challenged have involved more substantial private inurement situations.

Of greater concern is the fact that you reimburse board members for air fare and lodging in conjunction with board meetings. Even though such reimbursement is within organization policy, this practice may cause problems. The answers to the following questions are important:

1. Is yours a national organization, making it necessary for board members to travel long distances to attend meetings?
2. Do you hold your board meetings at resort locations?

Reimbursing expenses for trips to resorts or unnecessarily distant locations is not a good idea. Even if you hold legitimate meetings, the IRS may decide that you chose locations partly to provide board members with sightseeing, recreational, or entertainment opportunities. The IRS may judge reimbursement for such expenses to be private inurement. If you don't want to risk your tax–exempt status, then, you would be wise to keep your board meetings close to home if at all possible. ■

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