

BALLARD SPAHR LLP

TO: Board of Directors, The Haven

FROM: Kendis Key Muscheid, Esq.

RE: Questions for The Haven Board to Consider Prior to Making Contributions or Donations to The Haven Butterfly Foundation and Possible Requests for Amendments to the Foundation's Documents.

DATE: July 22, 2022

Introduction:

You requested we review the formation and proposed governing documents of The Haven Butterfly Foundation, a newly formed Arizona nonprofit corporation, intending to apply for tax-exempt status as a public charity under Section 501(c)(3) of the Internal Revenue Code (the "Foundation").¹ Our review was conducted for the benefit of The Haven, an addiction recovery facility just for women, a tax-exempt Section 501(c)(3) public charity ("The Haven").

Our review of the Foundation Articles of Incorporation ("Foundation Articles") and current *draft* Bylaws was undertaken with the understanding that the Foundation was formed, in substantial part, to safeguard The Haven's assets, both its immediate and long-term reserve assets, as well as possible future growth assets and possibly an endowment or other gift assets. With that understanding, it is our recommendation The Haven reconsider placing any assets with the Foundation under the Foundation's current structure, or, *alternatively*, significantly restrict all assets placed with the Foundation in order to ensure such assets must be either used for the benefit of The Haven or made available to The Haven upon request.

Set forth below are a series of questions for The Haven's Board of Directors to address as to its goals for protection of assets and control over those assets. Following discussion of the questions and goals are suggested alternative structures and possible amendments to the Foundation's structure or governing documents that will ensure the Foundation closely aligns with The Haven and provide The Haven additional assurance for the protection of its assets. Also included are comments on some potential accounting and other effects of certain suggested amendments/structures.

Brief Summary of Current Facts:

Foundation's Board of Directors. The Foundation's initial Board of Directors in its Articles of Incorporation ("Foundation Articles") are: Colette Barajas, Jean Gadea, and Patricia McCabe. Two of these individuals are currently on The Haven's Board of Directors: Colette Barajas (Director) and Patricia McCabe (Director and Treasurer). Meaning, at this time, a majority of the Foundation Board is comprised of Haven Directors, resulting in The Haven having "control" of the Foundation Board.

¹ We understand the Foundation is still in the process of drafting its IRS Form 1023, Application for Recognition of Exemption, as of the date of this memorandum. We have seen only draft Bylaws for the Foundation, nothing in final form. If any of our recommendations are implemented, the Articles of Incorporation, Bylaws and the Form 1023 would all be amended to reflect the recommendations.

Foundation Articles/Bylaws. Neither the Foundation Articles nor its *draft* Bylaws provide The Haven any rights or ability to appoint Foundation directors or to approve any amendments or changes to the Foundation Articles or Bylaws, or take any other actions with respect to the Foundation.

Foundation Purpose. As stated in the Foundation Articles, the Foundation Purpose is very broad:

The Non-Profit Corporation is organized **to support women and families in the pursuit of living free of substance misuse, and provide education and public advocacy in the area of women's health**, in accordance with §501(c)(3) of the Code, **with the intent to benefit mankind in the United States and abroad**, by conducting all activities incidental or necessary to accomplishing the foregoing purposes and otherwise permitted by said section of the Code and **by making charitable contributions [to organizations] that qualify as tax exempt organizations under said section of the Code**. Specifically, the Non-Profit Corporation **will provide financial support to The Haven, provided that it remains a recognized charitable organization under § 170(b)(1)(A) of the Code**.

(Foundation Bylaws, Art. IV, emphasis added.)

QUESTIONS:

1. **Foundation Purpose: What does The Haven's Board desire from the Foundation?**

ANSWER A: Support Only The Haven and Protect Its Assets.

- i. The Foundation Purpose is currently broadly stated and allows the Foundation to support women and families, provide education and advocacy, benefit mankind in the US and abroad, make contributions to qualifying tax-exempt organization, and to provide some support to The Haven.
- ii. Currently, there is no specific limitation in the Foundation Purpose for funds raised to go to support The Haven or its more limited mission.
- iii. In order to specifically limit the Foundation to supporting The Haven only (or substantially) several alternatives are available, set forth in 2, below.

ANSWER B: Support and Grant-making for Women and Families in the US and Abroad, Provide Education and Advocacy; Provide Some Support for The Haven.

- i. Leave the Foundation Purpose as stated.
- ii. Foundation will be permitted to make grants across the US and abroad, raise funds for many entities.
- iii. Currently, there is no specific amount of support designated for The Haven as to time or amount.
- iv. To secure The Haven's assets placed with or donated to the Foundation, and have the Foundation provide some support to The Haven, the Haven should follow the steps in 3, below.

2. If the Goal is for the Foundation to Support Only The Haven and Protect Its Assets (see 1.A., above), Then the Following are Possible Recommendations For Requested Changes To the Foundation’s Structure/Documents.²

RECOMMENDATION A: Foundation Purpose Narrowed. The Foundation Articles should be amended to a more narrow purpose aligned with The Haven’s purpose and geographic area, including specifically stating the Foundation intends to support The Haven. (Limiting the purposes to supporting The Haven and fundraising to support The Haven will aid in restricting all funds from donors to that purpose, while allowing for very general purposes to allow funds to be raised for those general purposes.) Stating that the Foundation intends to support The Haven does not mean the Foundation will be a “supporting organization” for tax classification purposes.³

RECOMMENDATION B: The Haven Granted Certain Rights. Currently, the Foundation Articles and Bylaws provide no rights of control or even input by The Haven Board into the Foundation’s operations or governance. Recommendations are for The Haven to be granted certain rights. The Foundation Articles and Bylaws can be amended to provide a level of control by The Haven so that the Foundation Board cannot “go rogue” in the future and either raise funds for another organization or divert assets donated for The Haven to another entity. The recommended provisions include:

- i. The Haven being the sole member of the Foundation with the right to appoint the entire Board of the Foundation; OR
- ii. The Haven is the sole member of the Foundation with the right to appoint a majority of the Foundation Board and the remainder of the Foundation Board will be elected by those remaining members of the Foundation Board.⁴
- iii. One of the above should be coupled with provisions providing that the sole member must give its affirmative approval of items such as: amendments to Foundation governing documents, transfer/granting away substantially all of the Foundation’s assets, dissolution or merger of the Foundation, and similar items.
- iv. Plus, for purposes of protection from The Haven’s creditors, it is recommended the foregoing rights are limited such that The Haven appoint no more than a small percentage (e.g., 20-25%) of overlapping Board members to the Foundation, and that the Foundation always be treated as a separate legal entity, observing all corporate formalities, and any employees spending time on both entities’ activities need to separately track and account for their time to each entity. Corporate formalities mean: all things between the Foundation and The Haven are separate: separate Board meetings, separate books & records, grant requests/distributions to and from

² The Foundation is not a separate legal entity because it is incorporated. Consequently, The Haven will need to request the Foundation’s Board agree to file amended and restated Articles of Incorporation and make amendments to its draft Bylaws in order to adopt some or all of the recommendations herein.

³ Internal Revenue Code section 509(a)(3) and related Treasury Regulations.

⁴ Another option is for The Haven to be the sole member of the Foundation with the right to appoint a minority of the Foundation Board, but then The Haven has given up control of the Foundation Board.

are tracked, Services Agreements are in place for shared personnel, expenses are appropriately allocated for shared items, etc.

- v. If The Haven controls appointments to the Foundation Board it is likely that The Haven and the Foundation will have consolidated financial statements, but separate IRS Forms 990 will be filed by each entity. According to The Haven's CPA, control is measured at a point in time, and The Haven's ability to appoint the Board or a majority of the Board will require consolidation. That said, however, the balance is risk of loss of assets/control v. consolidation.

RECOMMENDATION C: Additional Insurance. The Haven should periodically speak with its insurance broker to ensure it had adequate coverage for its operations as often coverage lags behind coverages that come into the market, e.g., cyber security, malpractice, etc.

RECOMMENDATION D: Real Property. Real property assets might be moved into a single member limited liability company for additional protection from creditors. It is sometimes wise to separate real property assets from the operating entity, but not put them into the Foundation because it is for different purposes. This type of segregation may offer additional protection for The Haven's real property/facility assets. (Details are beyond the scope of this memo.)

3. If the Goal is to Allow the Foundation to have a Broad Purpose to Support and Make Grants for Women and Families in the US and Abroad, Provide Education and Advocacy; and to Provide Some Support for The Haven, then the Following are Recommendations.

RECOMMENDATION A: Contractual Relationship with the Foundation. The Haven should consider a contractual relationship with the Foundation for investment of The Haven's Reserve Funds. Under a contractual relationship, the Foundation will hold and invest (as appropriate) The Haven's Reserve Funds placed with it by The Haven.

- i. Such funds remain the property of The Haven and can be called by The Haven at any time.
- ii. These Reserve Funds remain on The Haven's balance sheet/financials.

RECOMMENDATION B: Restricted Funds/Endowment Funds with Foundation. The Haven may donate funds to the Foundation for the benefit of The Haven and place restrictions on such funds.

- i. Only a donor may restrict funds, so The Haven should consider that if the Foundation is raising funds for others, any funds The Haven donates be restricted in use and a gift agreement be executes.
- ii. This can also be done by The Haven's donors to create funds that cannot be used for any purpose by The Haven, so long as The Haven is a 501(c)(3) public charity.
- iii. The Gift Agreement(s) should be carefully drawn so The Haven's creditors cannot reach the funds.
- iv. Without some control or input into the Foundation's Board of Directors, having restricted funds at the Foundation is helpful, but does not ensure a flow of funds.