



FULFILLING OUR PROMISES
TO THE MEN AND WOMEN WHO SERVED

NONPROFIT ADVISOR

For DAV Departments and Chapters

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JOHN BARLEYCORN AND DAV: HIDDEN RISKS

The late comedian W.C. Fields, who made no secret of his fondness for adult beverages, once confided to a friend that he'd received a dire medical warning: stop drinking or you'll go deaf. The concerned friend protested, "Well you are going to stop, aren't you Bill?" Replied Fields: "No son, I don't think I will. You see, the stuff I've been drinking is better than the stuff I've been hearing."

In previous issues of this newsletter, we've highlighted the liability that can arise for DAV bar/lounges under state liquor liability laws, i.e., the so-called "dram shop acts." In general, dram shop acts allow someone who has been injured by an intoxicated individual to sue the establishment that served alcoholic beverages to the intoxicated individual.

But the risk doesn't end there, not by a long shot. DAV bar/lounge operations run several other risks as well. This newsletter explains some of the principal ones.

UNRELATED BUSINESS INCOME TAX (UBIT)

DAV subordinate units are so-called "social welfare organizations" under the Internal Revenue Code. If a social welfare organization runs a business (and a bar is a business) that is not designed to promote the good of the community, it must pay tax on the earnings from the business. The tax is levied at the highest available corporate rate. This tax is imposed for two reasons: (1) to keep nonprofits doing what they're supposed to do, which is NOT running businesses; and (2) to prevent unfair competition between tax-exempt organizations and regular businesses.

Now, some astute readers may object that bar/lounge operations in veterans chapters and posts are part of the tradition of our sector of the fraternal world. They may further argue that the bars DO promote an important exempt purpose, namely, the encouragement of camaraderie among members. And, after all, such fostering of bonds among disabled veterans *is* one of DAV's chartered purposes!

Nice try. The IRS has addressed the issue and opined that the typical chapter meeting, which involves discussions of fraternal issues and developments in the world of veterans' rights does indeed "promote social welfare" and is an exempt activity. And it may even be the case that the meeting would end with a beer or two (bottles, not cases). But when a full-scale bar is launched, even if limited to members, that may well cross the line. A handful of DAV bar/lounges have been targeted by IRS over the years. When it happens, it's not pretty.

[By the way, 501(c)(19) organizations can run bars without paying UBIT. That is because one of the chartered purposes of 19's is to have "social activities" for veterans. DAV has consistently chosen the service function over the social function, and will continue to do so. Oh, and if a 501(c)(19) opens its bar to the public – and many of them do – they are on the hook for UBIT as well!]



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LOSS OF EXEMPTION

The “primary activity” of a 501(c)(4) must be directed to social welfare. For DAV chapters, that means service to veterans. Published rulings make clear that, independent of any UBIT considerations, a department or chapter whose primary activity is running a bar is not eligible for continuation of its 501(c)(4) tax exemption.¹ The same is true if the primary activity is gaming, or even if it is a thrift operation.

It is perfectly acceptable if most of the chapter’s MONEY comes, for example, from legal bingo or from a thrift store. It simply cannot be the focus of the chapter’s efforts, i.e., where it devotes the bulk of its human and financial resources. Obviously, this is a little vague and the IRS is vested with a great deal of discretion in determining just what the “primary activity” of a given 501(c)(4) actually is. Our suggestion is to follow the DAV guidelines as carefully as possible and, in the event of questions, contact the Inspector General for a definitive interpretation.

CONCLUSION

DAV chapters will be well served by making sure that most of their energy is devoted to direct service to veterans. When ancillary fundraising sources are considered – like thrift stores or bingo – get good counsel to ensure that the income from those sources is exempt from UBIT. The chapters should not allow pursuit of those sources of funding to detract in the least from the DAV mission of service to veterans. And, remember well, income from bars and lounges is ALWAYS subject to UBIT.

Back to Fields. His friend went on to say “Bill, if you don’t stop drinking you’ll mess up your constitution.” Replied the comedian, “I wrecked the constitution years ago—now I’m working on the bylaws.”

Pay close attention to DAV’s constitution and bylaws.

¹ IRS Revenue Ruling 66-150 holds that a 501(c)(4) organization whose primary activity is operation of a bar and a gaming room cannot retain its exemption.

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