

## **HOME ASSOCIATIONS, A GUIDE TO ORGANIZATION AND OPERATION**

### **I. INTRODUCTION.**

While Home Associations have existed in the Department of Pennsylvania for decades, they are not recognized or addressed by the national organization. The American Legion recognizes only Departments and Posts. Departments have authority to create intermediate bodies between the Posts and the Department to act as a liaison between such organizations and for the purpose of promoting the programs of the American Legion. County, District and Sectional units fall within this authority. Prior to the July 2004 Convention of The American Legion, Department of Pennsylvania, no formal authorization for the formation of Home Associations existed within the Department of Pennsylvania. ARTICLE XI – HOME ASSOCIATIONS, in Section 1 for the first time authorized Posts to form or continue Home Associations provided they are organized and operated in accordance with the requirements of the standardized By-Laws.

Two (2) principal reasons exist for the creation of a Home Association. They are insulation of the Posts and its assets from liability and the opportunity to have social or associate members who can contribute to a Post's financial success.

If properly established and operated a Home Association can insulate the Post and the Post's assets from liability, primarily liability associated with liquor related operations. In order to accomplish this, the Post and Home Association must be separate and distinct entities so that the Home Association, Liquor Licensee, is not considered to be an agent or representative of the Post subject to its control.

The Post may also have protection against contractual liability of the Home Association except in cases where it directly contracts with a third party, or on behalf of the Home Association, or where municipal services such as water are concerned. Liens for municipal services may be entered against the real estate regardless of the contracting entity.

Under ARTICLE IV, Section 2 of the National Constitution of The American Legion, there can be no form or class of membership except an active membership. Social memberships are precluded. Subject to requirements of the Internal Revenue Service, Home Associations may have social members. Such members can increase the individuals participating in American Legion programs, further contributing to their success and enhance the financial well-being of the Post/Home Association through their payment of dues and participation in other fund raising activities of the Post/Home Association.

The provisions in ARTICLE XI of the standardized Post By-Laws setting forth the authorization to form or continue a Home Association and establishing some requirements for the structure thereof, are designed to afford Posts protection for what is for most of our Posts their primary asset, i.e. the real estate, and to enable them to enhance their financial basis by attracting social members.

## **II. ORGANIZATION.**

### **A. General Requirements.**

Section 2 of ARTICLE XI of the standardized Post By-Laws requires all Home Associations to be formed as a separate Non-Stock Domestic Non-Profit Corporation. If not previously so incorporated, the Home Association

must be organized pursuant to the Pennsylvania Non-Profit Corporation Law of 1988 as the same may be amended or substituted for.

The national organization does not permit use of the designation “American Legion” or the symbol of the American Legion without the prior written consent of it. The number of the Post may be utilized in the name of the Home Association. For example, the Home Association could be named “Legion Post \_\_\_\_\_ Home Association”. The symbol of the American Legion however may not be used in conjunction with Home Association materials without the prior written consent of the national organization.

Under Section 3 of ARTICLE XI of the standardized Post By-Laws, Home Associations may have different classes of members. However, only those members, who are Legionnaires in good standing of the Post, may have voting rights or hold a position as Director, Executive Committeeman or other officer in the Home Association. Non-Post members may attend meetings, participate in discussions and generally participate in Home Association functions.

Whether a Home Association elects to have members other than Post members must be considered in light of federal and state income tax requirements. (If the Home Association does not wish to have income tax exempt status, these need not concern it.) Each Post receiving a Charter from the American Legion does by virtue thereof, have federal income tax exempt status. When a Charter is issued, the Federal Employer’s Identification

Number for the Post is transmitted to the national organization and is then filed with the Internal Revenue Service. By virtue thereof, the Post enjoys federal income tax exempt status. However, no such automatic federal income tax exempt status exists for Home Associations. The fact that a Home Association is organized as a non-profit corporation does not in and of itself confer federal income tax exempt status on it. To obtain federal income tax exempt status, a Home Association must apply for the same.

Tax-exempt status is controlled by Section 501 of the Internal Revenue Code. Today, depending on their organization and purposes, veterans' organizations may be recognized as tax exempt under the following Sections of the Internal Revenue Code: 501 (c) (2), 501 (c) (4), 501 (c) (7), 501 (c) (8), 501 (c) (10), 501 (c) (23) and 501(c) (19). Of these, (c) (19) and (c) (7) are most likely to be considered. Before enactment of I.R.C. 501 (c) (19), War veterans' organizations were grouped together with all other veterans' organizations and recognized as exempt under I.R.C. 501 (c) (4) as social organizations. Their subsidiaries, i.e. Home Associations, which were formed to maintain and operate their social facilities, were often recognized as exempt social clubs under I.R.C. 501 (c) (7). Section 501 (c) (19) applies only to veterans' organizations and their related auxiliaries. The national organization and therefore Posts are federally tax-exempt under Section 501 (c) (19).

B. §501 (c) (19) Requirements.

In an organization exempt under §501 (c) (19), at least seventy-five (75%) percent of the members of the organization must be past or present members of the Armed Forces of the United States (Veterans). Substantially all other members must be:

- a. Cadets; or
- b. Spouses, widows or widowers, ancestors or lineal descendants of veterans or Cadets.

Cadets include students in college or University ROTC programs or at armed services academies.

“Substantially all” means ninety (90%) percent. Of the twenty-five (25%) percent of the members that do not have to be veterans, ninety (90%) percent have to be Cadets or spouses, widows or widowers, ancestors or lineal descendants of veterans or Cadets. Members of the Auxiliary and Sons could therefore make up to twenty-five (25%) of the Home Association Membership under §501 (c) (19). Only 2.5% of the organization’s total membership may consist of individuals who are not veterans, Cadets or spouses, widows or widowers, ancestors or lineal descendants of veterans or Cadets. An entity organized as a 501 (c) (19) tax exempt organization may permit “social members” or “friends” membership privileges without jeopardizing its exempt status only if it limits the number of such members to no more than 2.5% of its total membership. If the entity fails to meet the membership requirements contained in I.R.C. 501 (c) (19), it will no longer qualify for exemption. The

entity may include non-veterans' sons, daughters, and other related individuals as part of its membership, so long as they, along with any other non-veteran class of membership, make up no more than 2.5% of the entity's membership.

In addition, the organization must be operated for one or more of the following purposes:

- (a) Promoting the social welfare of the community;
- (b) Assisting needy and disabled veterans, widows or orphans of deceased veterans;
- (c) Providing entertainment, care and assistance to hospitalized veterans or members of the Armed Forces of the United States;
- (d) Perpetuating the memory of veterans and comforting their survivors;
- (e) Conducting programs for religious, charitable, scientific, literary or educational purposes;
- (f) Sponsoring or participating in patriotic activities;
- (g) Providing insurance benefits to members or members' dependents; and
- (h) Providing social and recreational activities for members.

Also, significant for Section 501 (c) (19) organizations is that they may allow acceptance of charitable gifts and bequests. Contributions may be deductible to the donor pursuant to 26 U.S.C. 170 (c) (3) of the Internal Revenue Code of 1954, as amended, thereby encouraging donations. Section 170 (c) (3) reads as follows:

“Section 170. Charitable, etc., Contributions and Gifts.

(a) Allowance of Deduction.

- (1) General Rule. - There shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year .

...

(c) Charitable Contribution Defined. For purposes of this section the term "Charitable Contribution" means a contribution or gift to or for the use of –

- (3) A Post or organization of war veterans or an auxiliary unit or society of, or trust or foundation for, any such Post or organization –

(A) Organized in the United States or any of its possessions, and

(B) No part of the net earnings of which inures to the benefit of any private shareholder or individual.”

Note the organization must be one ninety percent (90%) of the members of which are "War Veterans" not merely "veterans". War Veterans are those serving during a period of war, the periods are:

- A. April 21, 1898, through July 4, 1902;
- B. April 6, 1917, through November 11, 1918;
- C. December 7, 1941, through December 31, 1946;
- D. June 27, 1950, through January 31, 1955;
- E. February 28, 1961, through May 7, 1975, in the case of a veteran who served in the Republic of Vietnam during that period;

F. August 5, 1964, through May 7, 1975; and

G. August 2, 1990, and ending on the date prescribed by Presidential Proclamation or by law.

C. §501 (c) (7) Requirements.

The other section many Home Associations seek to qualify for federal income tax exempt status under is I.R.C. §501 (c) (7). I.R.C. §501 (c) (7) exempts from tax social clubs that are organized and operated primarily for pleasure, recreation and similar non-profitable purposes. In keeping with this purpose, non-member income from all sources is limited and may be taxed as unrelated business income. To satisfy the organizational requirements for exemption, a club's Charter, By-Laws or other governing instrument must not include purposes that are not directed toward pleasure and recreation.

A club is not exempt under I.R.C. 501 (c) (7) if it provides commercial services, such as the sale of packaged liquor or carryout food, as such activities are not traditionally engaged in by social clubs.

501 (c) (7) veterans' organizations may establish several types of memberships, such as veterans, auxiliary and friends. The club may specify voting and non-voting members and may choose to limit member benefits, such as the use of the club facilities, based on membership categories.

Eligibility requirements, formal admittance procedures and a dues structure are internal matters to be decided in accordance with the club's Charter and By-Laws. Section 501 (c) (7) does not require that a specific percentage of



members be veterans. However, the membership must have shared goals and interests.

As a general rule, an I.R.C. 501 (c) (7) club may receive up to thirty-five (35%) percent of its gross receipts from sources outside its membership. This includes investment income. Within the thirty-five (35%) percent limitation, no more than fifteen (15%) percent of the gross receipts may be derived from the use of the club's facilities or services by the general public. Gross receipts are receipts from the normal and usual activities of the club. However, the income received by an I.R.C. 501 (c) (7) club from non-members may be subject to unrelated business income tax.

D. Pennsylvania Requirements.

A Pennsylvania Non-Profit Corporation which secures federal income tax exempt status is automatically afforded exempt status for purposes of the Pennsylvania Department of Revenue and is exempt from payment of the Corporate Net Income Tax and Capital Stock Tax.

E. Pennsylvania Liquor Control Board Requirements.

In considering whether or not to admit social members to the Association, it is also important to consider whether or not the Home Association has or will obtain a liquor license. Most liquor licenses issued to Home Associations are club or catering club licenses. Nothing in the Liquor Code or the Board's Regulations addresses whether a club licensee may establish different classes of membership or how many members can belong to any category of membership. Thus, the types of membership and what ratio one (1) class of

membership bears to another class are matters not specifically regulated by the Board. However, club licensees must adhere to the provisions of their Constitution and By-Laws. Therefore, to the extent a club's Constitution and/or By-Laws establish a social class of members or specify a number for categories of members, they must be observed. OPN 2005-317-OPN 05-317-  
Re: Social Members.

Given the above, whether or not a Home Association will have social members, their categorization and number are primarily driven by the Internal Revenue Code requirements for tax-exempt status. Home Associations should therefore be organized and structured with these regulations in mind.

### **III. NON-OWNERSHIP OF REAL ESTATE.**

Under Section 6 of ARTICLE XI of the standardized Post By-Laws, the affiliated Home Association of the Post may not acquire or own real estate or fixtures attached thereto. In prior years, many Home Associations took title to the real estate obtained for the use of the Post. Such an arrangement is now prohibited. For most Posts in the Department the most valuable asset it has is its real estate. In order to protect that real estate, the provisions prohibiting Home Associations from owning real estate were adopted. Since those Posts having a Home Association generally have a liquor license, concern existed for liability arising from liquor related activities. When an entity obtains a liquor license from the Commonwealth of Pennsylvania, it is liable for injuries to anyone harmed as a result of its service of alcoholic beverages to a visibly intoxicated person. The licensee is also liable for harm resulting from the service of alcohol to minors. Should a licensee violate these restrictions and harm comes to another, it may

find itself being sued and subject to a substantial judgment. If the realty and other significant assets used by the Home Association are owned by the Post separate and apart from the Home Association, the Post and its assets may be shielded from such liability.

Most people seeking to obtain and operate a liquor license generally form two (2) separate and distinct business entities. One entity is used as the holding company and the major assets are placed in that entity with the liquor license, consumables, and only those items necessary to operate the liquor license being held in the other. In this way, parties seeking to operate a liquor business shield their assets from potential liquor related liability by having those assets separately owned. That same approach is the approach being recommended for Posts and Home Associations. Since Home Associations can no longer own real estate, real estate must be transferred to the Posts. However, the liquor license and all liquor related activities should be conducted by the Home Association. In that way, should liquor related liability occur, any liability would be that of the Home Association rather than the Post. Since the assets of the Home Association would be little more than the liquor license, consumables, and cash necessary to operate its business, the bulk of the assets would be protected. Having the real estate and liquor license owned by the same entity exposes the real estate to potential liability. While under Section 6 of ARTICLE XI of the standardized Post By-Laws, Home Associations are not required to transfer any assets other than their real estate to the Posts with which they are affiliated, the same concepts and principles apply to all assets. It is therefore recommended that Home Associations transfer any other valuable assets they may have, such as cash and/or investments to their Posts and thereby shield the same from any potential liquor liability.

While it is recommended that all Posts/Home Associations serving alcohol have Dram shop coverage insurance (i.e. liquor liability insurance), many Posts/Home Associations find they cannot afford it. It is significant to note that liquor liability insurance is **NOT** included in the standard fire and casualty policy. This type of protection must be acquired by rider or separate policy. If your Post/Home Association has only a fire and casualty policy with standard liability coverage and has not purchased a separate liquor liability rider or policy, it will not have this coverage available to it. If it cannot afford to obtain this type coverage, the structure being recommended whereby the Home Association operates the liquor license and the Post owns the real estate is necessary in order to achieve the maximum protection available from liquor related claims.

All insurance should cover **BOTH** the Post and the Home Association.

#### **IV. LIQUOR LICENSE.**

The Pennsylvania Liquor Control Board is authorized to issue new licenses to incorporated units of national veterans' organizations even when the number of licenses in a County exceeds the statutorily limited number of licenses prescribed by the Liquor Code. Licenses issued under this provision 47 Purdon's Statute §4-461.1 (a) are limited to the incorporated unit of a national veterans' organization. The term "Incorporated unit of a national veterans' organization" means any incorporated Post, branch, camp, detachment, lodge or other subordinate unit of a national veterans organization having 100 or more paid up members and organized for a period of at least one (1) year prior to filing the application for a license.<sup>1</sup> The term does not include auxiliaries, "sons of" or other similar organizations. In the 1998 case of Pennsylvania Liquor Control Board v.

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<sup>1</sup> 47 P.S. 4-461.1 b. (1) eliminates the one-year requirement.

Richard E. Craft American Legion Home Corporation, 718 A.2d 276, the Pennsylvania Supreme Court held the Home Association of that particular Post to in fact be a subordinate unit of the Post. At the time the case arose, the Liquor Code provided for the issuance of licenses to a “subordinate unit” of a national veterans’ organization. The P.L.C.B. ruled that the Home Association was not a “subordinate unit” within the meaning of the Pennsylvania Liquor Code. The matter was appealed to the Common Pleas Court, which reversed the Board and found that, in fact, the Home Association was a subordinate unit of a national veterans’ organization and therefore directed that the P.L.C.B. issue a license. The P.L.C.B. in turn appealed the case to the Pennsylvania Commonwealth Court, which then reversed the Common Pleas Court siding with the Liquor Control Board. The matter was then appealed to the Pennsylvania State Supreme Court, which reversed the Commonwealth Court and reinstated the findings of the Common Pleas Court. Justices Newman and Nigro both dissented from the decision contending that the Home Association did not constitute a subordinate unit and that it would not constitute such a unit under what was then an already passed amendment to the Liquor Code.

That amendment exists currently as 47 Purdon’s Statute §4-461.1. The amendment to the Code, which took effect in August of 1998, and further amendments, constitute the current law on the issuance of licenses. Subsection (a) of 47 Purdon’s Statute §4-461.1 authorizes the P.L.C.B. to issue new licenses to incorporated units of national veterans’ organizations. It also clearly authorizes the transfer of a license from such an organization to an “affiliated organization” which is defined to mean “...Home Associations, Home Corporations, auxiliaries, “sons of” or similar organizations which

are directly affiliated with an incorporated unit of a national veterans organization.” An affiliated organization must also meet the definition of a “club” set forth in Section 102 of the Liquor Code except that the time provisions therein for existence prior to applying for a transfer of a license are made inapplicable. In reviewing both the P.L.C.B. v. Craft American Legion Home case and the current statute, it may be that the P.L.C.B. will again argue that Home Associations are not incorporated units of a national veterans’ organization. However, the Craft case appears to continue to be the law and therefore Home Associations may apply for, and seek to obtain, a liquor license as an incorporated unit of a national veterans’ organization.

However, should the Board take the position that Home Associations do not in fact constitute incorporated units of national organizations, Posts can clearly apply for a license as such and thereafter transfer the license to an affiliated organization, i.e. a Home Association or Home Corporation. Based on my review of the P.L.C.B. v. Craft American Legion Home case and the current statute, I would recommend that Home Associations continue to apply as an incorporated unit of a national veterans’ organization. However, it may be wise for Home Associations to be structured so as to meet all of the requirements of an affiliated organization in case their application is refused. Under these circumstances the Post itself would apply for the license and could then transfer it to a Home Association. Clearly a Home Association that qualifies as a “club” under 47 Purdon’s Statute §4-102 can be an organization holding a liquor license. The requirements to constitute a “club” under 47 Purdon’s Statute §1-102 are set forth in that section. These may be summarized as follows:

1. The members must be a “reputable group of individuals”.

2. They must associate together on a non-profit basis.
3. They must associate for legitimate purposes of mutual benefit, entertainment, fellowship or lawful convenience and have some primary interest and activity to which the sale of liquor or malt and brewed beverages is only secondary. A Home Association formed for the purpose of mutual benefit, entertainment, fellowship and lawful convenience to further the goals and aspirations of the American Legion would I believe, so qualify. (Note – the purpose must also comply with the requirements of the Internal Revenue Code under which tax-exempt status is sought).
4. The Home Association must hold regular meetings.
5. It must conduct its business through officers regularly elected and must admit members by written application, investigation and ballot.
6. Finally it must maintain such records, as the P.L.C.B. shall from time to time prescribe.

Some Home Associations having a liquor license have been granted a club license while others a catering club license. By special opinion obtained from the Pennsylvania Liquor Control Board, all entities holding a catering club license must qualify as a club, the privilege to serve alcohol to groups of non-members using the club's facilities by prior arrangement being only an additional privilege granted to an organization that already qualifies as a club under Section 102 of the Liquor Code. (47 P.S. §1-102).

It is also important to note that under Section 4-461.1 of the Liquor Code, 47 P.S. §4-461.1, the liquor license of a Home Association can be rescinded on three (3) bases directly associated with its affiliation with a Post of the American Legion. Initially, if the Post loses its Charter, the Home Association would lose its liquor license. Likewise, if the Home Association's relationship to the national veterans' organization is severed, its license would be lost. Finally, the license of the Home Association would also be rescinded upon request of the American Legion, Department of Pennsylvania.

Section 4-461.1 (e) also precludes both the Post and its affiliated Home Association from having a license.

## **V. BY-LAWS.**

While no standardized By-Laws exist for Home Associations like those for Posts, it is recommended that Home Association By-Laws address certain matters.

### **A. Purpose.**

The purpose of the Home Association should be set forth. In drafting the purpose, it must meet the requirements of the Pennsylvania Liquor Control Board for a club. This means that it must be established for legitimate purposes of mutual benefit, entertainment, fellowship or lawful convenience and have some primary interest or activity to which the sale of the liquor or malt or brewed beverages is only secondary. The purpose clause must also conform to the purpose requirements of the section of the Internal Revenue Code under which the Home Association seeks federal income tax-exempt status. Providing entertainment, social and recreational activities and fellowship for the mutual benefit of its members would appear to meet the requirements of both the Liquor Code and Sections 501 (c) (7) and (c) (19) of the IRC.

### **B. Membership.**

To qualify as a club under the Pennsylvania Liquor Control Board, the Association must admit members by written application, investigation and ballot. For anyone seeking membership in the Home Association, they must do so by written application, which must be investigated and voted upon.



Since under ARTICLE XI only members of the Post with which the Home Association is affiliated and which are in good standing may vote in the Home Association or hold office therein, any action on a member's application will be voted upon by the same individuals voting on membership in the Post. This will likewise be the case for elections to office. Therefore, in order to meet the requirements of the Liquor Control Board that membership applications be voted on after written application and investigation, and in order to avoid duplicating the same actions for membership in the Home Association, it is recommended that every application for membership in the Post conspicuously state that it is a dual application, whereby the individual seeks membership in the Post **AND** membership in the Home Association. It should also make known that a vote on the member's application is a dual vote by the members of the Post **AND** the voting members of the Home Association. The vote must be entered separately in the minutes of both organizations. In this way, applications to the Post and Home Associations can be handled in a single proceeding. Applications for a membership in the Home Association by others not seeking membership in the Post must be by written application, followed by investigation and a vote upon their admission. If members of the Auxiliary and members of the Sons over the age of twenty-one (21) are to be members of the Home Association they must, in order to meet the requirements of P.L.C.B. make separate written application followed by investigation and vote. This is likewise the case for other individuals seeking membership in the Association.

C. Management Structure.

Since Home Associations are to be incorporated pursuant to the Pennsylvania Non-Profit Corporation Act, their affairs should be managed by a Board of Directors. The day-to-day operations should be under the management of elected officers. Occasionally, where Home Associations and Posts have had totally dissimilar managing bodies, disagreements have arisen between the Post and the Home Association. While both entities are separate Non-Profit Corporations, it is recommended the structure of the Home Association be such as to minimize the likelihood of disagreements between the management of the Post and the management of the Home Association. This can be minimized by having individuals serve in similar capacities in both the Post and Home Association. It is therefore suggested that the Commander of the Post be the President of the Home Association. Likewise, the Vice-Commanders of the Post should serve as Vice-Presidents of the Home Association, while the Adjutant and Finance Officer of the Post serve as Secretary and Treasurer respectively of the Home Association Corporation.

Under the standardized By-Laws, the affairs of the Post are managed by an Executive Committee made up of the Post's officers and an even number of at large Executive Committeemen, at least four (4) in number. It is likewise recommended that the Board of Directors for the Home Association also have at large Directors in addition to the officers. It is strongly recommended however, that the number of at large Directors and the individuals holding those positions be different than the number and

individuals holding comparable positions in the Post. The reasoning for this is that the Post's protection from liability of the Home Association depends on the two (2) entities, in fact, being separate organizations. By having a Board of Directors of the Home Association and an Executive Committee of the Post which are not one hundred percent (100%) identical, the likelihood of disagreements is minimized but the separateness and differentness of each entity is preserved.

Under the Liquor Code requirements for a club, the officers and directors of the Home Association must be elected. The Post and Home Association can conduct completely separate elections. A single combined election for both the Post and Home Association could also be held. When this structure is utilized it should be clear that nominations and elections for the officesorial positions in the Post also constitute a nomination and election for the equivalent position in the Home Association.

Ballots prepared for voting on those officesorial positions, which are integrated between the Post and Home Association, must reflect that the party being voted for is actually being elected by the voting members of the two (2) entities to two (2) separate positions, i.e. the Post office and the comparable office in the Home Association. For example, the ballot might read as follows:

For Post Commander and Home Association President

John Smith (  )

Mary Doe (  )

Robert Jones (  ).

(pick one)

Combined ballots will also have to have separate sections for candidates being elected to a position in only one of the entities, for example at large Executive Committeemen for the Post and at large Executive Directors for the Home Association.

As with Posts, no single individual should hold more than one (1) of these management positions. The applicable results of the nominations and elections must be separately entered in the minutes of each organization.

Other provisions of the By-Laws can be adapted to meet the particular needs of the Home Association and its operation.

## **VI. OPERATIONS.**

### **A. Use of Post Real Estate.**

Since the real estate in which Home Associations will operate cannot be owned by the Home Association some written arrangement between the Post and the Home Association for use of the Post owned real estate by the Home Association should be entered into. This can be via a Lease or some other operating agreement. The Post and Home Association are free to allocate responsibility for the real estate between them. For example, the Home Association can be made responsible for the payment of mortgage payments, taxes, maintenance and insurance. These responsibilities can also be placed with the Post, or some with each.

Since aside from the dues, the major sources of funding for a Post's programs and activities will probably be generated by the Home Association, the lease/arrangement should provide for a transfer of monies from the Home Association to the Post. Obviously, this can be done as rent or some other transfer to the Post. Since the Post has 501 (c) (19) tax-exempt status, gifts to the Post may be deductible contributions. This should be checked and verified by the Home Association's accountant. Under such circumstances, monies can be moved from the Home Association to the Post with no income tax ramifications.

**B. Unrelated Business Income Tax.**

Care must be taken so that activities of the Home Association are not categorized as Unrelated Business Income. The term "trade or business" includes any activity carried on for the production of income, whether from selling goods or performing services. Business activities are regularly carried on if they are conducted frequently or continually and are pursued in a manner similar to comparable commercial activities of non-exempt organizations. Unless the business activities, apart from the income generated, contribute importantly to the accomplishment of the organization's exempt purposes they are not substantially related and may generate taxable unrelated business income.

Once it has been determined that a business activity is unrelated there are several special rules that apply to computing the amount of the income that would be taxable. Certain dividends, interest, annuities, royalties and rents

may be excluded in whole or in part. The expenses, depreciation and similar items directly connected with the conduct of the unrelated business may also be deducted. Whether a specific activity is taxable often depends on the section of the Code under which a veteran's organization is exempt. Also, certain activities have been specifically excluded from the definition of unrelated trade or business. The exclusions that apply to veterans' organizations include:

- a. Volunteer Labor: Any business in which substantial sales or work is performed by volunteers without compensation.
- b. Selling Donated Merchandise. A business that consists of selling goods substantially all of which have been received as gifts or contributions. For example, the income generated from thrift shops selling donated goods with the proceeds going to the exempt organization.
- c. Certain Bingo Games. A bingo game must be legal and must be conducted in a jurisdiction that does not permit commercial bingo. The game must be one in which wagers are placed, the winners determined and prizes are distributed in the presence of all persons placing wagers in that game.
- d. Low Cost Articles. For organizations eligible to solicit charitable contributions, the distribution of low cost articles, such as stationery or candies, incidental to the solicitation is not an unrelated trade or business.
- e. Exchange or Rental of Member Lists. The exchange or rental of member or donor lists between Posts of war veterans eligible to receive tax deductible contributions are not considered an unrelated trade or business.

Social activities, such as the operation of a bar and restaurant are appropriate for veterans' organizations exempt under I.R.C. 501 (c) (19) and (c) (7) as long as the activities are limited to members and their bona fide guests. A guest is an individual accompanying a member who pays for food, beverages, etc.

Permitting non-members use of these facilities is not related to the accomplishment of exempt purposes and will result in the income from non-members being taxable. For an I.R.C. 501 (c) (7) organization, non-member income that exceeds thirty-five (35%) percent of gross receipts may jeopardize exemption.

Charging admission for **REGULARLY** conducted fundraising activities, such as dinners, breakfasts and dances, is a trade or business. Admissions paid by members may be considered related income if social or recreational activities further exempt purposes. An activity that is “regularly carried on” and is open to non-members would not be considered substantially related to the exempt purposes of a veteran’s organization under any Code section. Therefore, unless one of the exceptions such as the Volunteer Labor Exception applies, the income from these types of regularly carried on activities is taxable.

Selling tickets to social functions to non-members is an unrelated activity for all veterans’ organizations. If this activity only occurs occasionally, it may not be considered “regularly carried on” and will not be taxable. If the activity is regularly carried on, however, it would be taxable unless it is excluded under one of the above set forth exceptions such as the “Volunteer Labor Exception”.

Whether the rental of banquet facilities on a regular basis is an unrelated business depends on the Code section under which the organization is exempt. The rental of such facilities to members may be related to the permissible purposes of organizations exempt under I.R.C. 501 (c) (19) and 501 (c) (7). The rental of the facilities to non-members is always considered unrelated to the

exempt purposes of such organizations. If the rental of the facility is unrelated to the organization's exempt purposes the rental income may or may not be taxable. The rents from real property are excluded in computing the tax. If the rent includes personal services, such as catering or decorating, it is not considered rent from real property and would be taxed. Rents from personal property rented with the real property (mixed lease) may also be excluded, if the rents attributable to the personal property do not exceed ten (10%) percent of the total rent. The rental exclusion does not apply to the rental of personal property.

The unrestricted use of Home Association facilities by non-members is not related to its exempt purposes. The sale of food and drink to non-members may result in the income being taxed unless the Volunteer Labor Exception applies. Likewise, selling liquor and food for consumption off the premises does not further the exempt purposes of a veteran's organization. All income from off-premises sales is subject to UBIT (Unrelated Business Income Tax) unless a specific exception applies.

For further examples of activities which may generate unrelated business income tax, Home Associations should refer to the IRS Tax Guide for Veterans' Organizations, copies of which are obtainable from the Internal Revenue Service and their accountants.

#### C. Limitations On The Service of Alcohol.

Any club licensee which is either an incorporated unit of a national veterans' organization or an affiliated organization, as defined in Section 461.1 of the Liquor



Code [47 P.S. §4-461.1], is permitted to sell liquor or malt or brewed beverages to any active member of another unit which is chartered by the same national veterans' organization or to any member of a nationally chartered auxiliary associated with the same national veterans' organization.

Section 461.1 of the Liquor Code defines an "affiliated organization" as a home association, home corporation, auxiliary, "sons of" or similar organization that is directly affiliated with an incorporated unit or a national veterans' organization.

However, the term "active member" does not include a social member. Because of this, social members of other Home Associations do not have the same rights and privileges as an active member of a particular Home Association and, therefore, cannot purchase alcoholic beverages at another Home Association. Individuals that are active members of an auxiliary or "sons of" chartered by a national veterans' organization, or a nationally chartered auxiliary associated with the same national veterans' organization may be sold liquor and malt or brewed beverages by a Home Association.

Since the American Legion has only one class of membership, a Home Association may sell alcoholic beverages to any American Legion member. The American Legion Auxiliary being a nationally chartered auxiliary associated with the American Legion, the Home Association may legally sell alcoholic beverages to any active members of it. The same applies to any "squadron of the sons" of the

American Legion. Of course, alcoholic beverages may only be sold to those twenty-one (21) years of age or older.

As a caveat, section 5.81 of the Board's Regulations states that a club licensee shall adhere to the provisions of its constitution and bylaws. [40 Pa. Code §5.81]. As such, should the bylaws of the Home Association prohibit sales to other than Home Association members such provision must be observed.

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D. Separate Meetings and Records, etc.

All Home Associations **MUST** hold meetings separate from the Post, maintain separate minutes and records from the Post and always make clear that actions being taken by it are not actions of the Post. Separate letterhead and a distinctly separate address such as a different box number or a box number where the Post has a street address and a separate phone number are encouraged.

Obviously, governmental filings should be clear. Finally, both the Post and Home Association must have separate Federal Employer Identification Numbers (F.E.I.N numbers).

This Guide is intended solely as a general overview of matters impacting the formation and operation of a Home Association. Every Home Association should consult legal counsel and accountants for specific application of these concepts to a particular Home Association.

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