
Articles

Crossing the Tax Code's For-Profit/Nonprofit Border

Susannah Camic Tahk*

Abstract

The federal tax code erects and enforces a firm border between for-profit and nonprofit organizations. Multiple provisions of the code monitor the boundaries of the tax-exempt, or nonprofit, sector to ensure that no nonprofit organization slips across the border to become a for-profit organization. Other code provisions restrict entry into the tax-exempt sector by for-profit organizations. Despite serious legal impediments, however, organizations on both sides of the boundary have increasingly found means by which to cross the border. Arrangements such as corporate social responsibility, for-profit philanthropy, and social enterprise illustrate this recent trend. Through these arrangements, for-profit organizations are beginning to embrace social goals, while nonprofit organizations have started to use methods more traditionally associated with efficient business organizations. Research in organizational sociology provides tools by which to understand these

* Assistant Professor of Law, University of Wisconsin Law School. Thanks to the Graduate School at the University of Wisconsin for funding, to Charles Camic, Casey Faucon, Keith Findley, Alexandra Huneus, Megan McDermott, John Ohnesorge, Mitra Sharafi, Alex Tahk, and William Whitford for comments and suggestions, and to Lauren Fangmann for truly extraordinary research assistance. All errors are of course my own.

new cross-border developments. This body of research has shown that organizational sectors, or fields, evolve according to well-understood patterns, whose significance tax scholars have overlooked. Furthermore, federal tax law has failed to recognize and to make productive use of these organizational trends. This Article proposes that tax law should acknowledge the cross-sector movements of for-profit and nonprofit organizations, as well as the major advantages that these movements can produce. Tax law could then harness border-crossing activity to create social benefits. To achieve this result, federal tax law should loosen the for-profit/nonprofit boundary. This change would enable the tax code to encourage cross-sector “collaborations” between for-profit and nonprofit organizations. This change to the tax law is one that Congress and the Internal Revenue Service could now accomplish through several basic measures. These measures would make it possible for federal tax law to realize the large potential for social good that lies at the changing for-profit/nonprofit border.

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I. INTRODUCTION

U.S. federal tax law draws the borders of the tax-exempt sector rigidly. An organization is either exempt from federal income taxation or it is not. Historically, qualifying for tax exemption has served an important signaling role. Most notably, organizations that are “organized and operated” for “charitable” purposes may qualify for tax exemption.¹ Such organizations receive the additional tax benefit of being able to receive tax-deductible contributions. Tax-exempt or “exempt” organizations must comply with the complex legal framework that Congress and the Internal Revenue Service (“IRS”) have developed. The official exempt designation from the IRS signifies to the public that the organization serves a purpose that Congress or the IRS has identified as socially beneficial.

In contrast, organizations that do not qualify as exempt fall within the category of for-profit organizations for the purposes of tax law. Non-exempt organizations may choose among several organizational forms that the tax code offers.² The tax code sets forth different legislative and regulatory frameworks for the different types of for-profit organizations.³ However, all of these frameworks assume that the organizations they govern are organized and operated to make profits.

Tax law patrols the nonprofit border carefully.⁴ The tax code, its regulations, and members of its administrative bodies view sectorial

1. See I.R.C. § 501(c)(3) (2012) (stating that entities may qualify for tax exemption and deductibility of contributions if they are “organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition . . . , or for the prevention of cruelty to children or animals”). “Charitable” organizations organized and operated for one of these purposes are the most favorably treated and perhaps most common of the organizations exempt from federal income tax. While this Article will refer frequently to “exempt organizations,” its focus will be on the “charitable” subgroup.

2. See generally ROBERT J. PERONI & STEVEN A. BANK, TAXATION OF BUSINESS ENTERPRISES: CASES AND MATERIALS 671–867 (4th ed. 2012) (including, most prominently, the sole proprietorship, the C corporation, the S corporation, or the partnership; most LLCs are taxed as partnerships).

3. *Id.*

4. The tax law does not explicitly refer to “nonprofit” organizations. “Nonprofit” status is generally found in state corporate law. Frequently, scholars and commentators will refer to tax-exempt groups as “nonprofit organizations.” However, tax exemption and nonprofit status normally designate overlapping but non-equivalent sets of

border-crossings with suspicion. Most of the complex body of exempt-organization tax law attempts to ensure that organizations on the nonprofit side of the border do not enter for-profit territory. Moreover, from the standpoint of tax law, for-profit companies always exist as entirely for-profit companies. Tax law offers no opportunity for for-profit organizations to cross the exempt border and attain any of the tax law's markers of exemption.

The stark line that tax law draws between charitable and for-profit organizations is artificial. This is becoming increasingly true. In contemporary American society, many organizations do not fit neatly into either the nonprofit or for-profit category. Instead, organizations regularly move back and forth over the for-profit/nonprofit border.

Exempt organizations engage successfully in activities aimed at making profits.⁵ Simultaneously, exempt organizations sometimes attempt to enhance their individual positions.⁶ Then, exempt organizations often distribute profits to individuals in ways that, while different in form, resemble in substance distributions from for-profit companies.⁷

On the other side of the border, for-profit companies often engage in substantial charitable activities.⁸ Sometimes, for-profit companies

characteristics. As this Article will discuss, a nonprofit organization is not necessarily exempt from tax. The tax code actually exempts a wider range of groups than the "nonprofit" label implies. For more on these two points, see BORIS I. BITTKER & LAWRENCE LOKKEN, *FEDERAL TAXATION OF INCOME, ESTATES & GIFTS* ¶ 100.1.1 (2014), available at 1997 WL 440008 (Westlaw). However, the "nonprofit" label is quite common in the academic literature, and corresponds easily to the tax law's concept of "for-profit" entities. For these reasons, this Article will use the phrase "nonprofit border" to signify the line that the tax code draws around charitable organizations as described in section 501(c) of the tax code.

5. See Rachel Culley & Jill R. Horwitz, *Profits v. Purpose: Hybrid Companies and the Charitable Dollar* 13 (Univ. of Mich. Law Sch. Pub. Law & Legal Theory Working Paper Series, Paper No. 272, 2012), available at <http://bit.ly/1a1XWzB>. See generally Eleanor Brown & Al Slivinski, *Nonprofit Organizations and the Market*, in *THE NONPROFIT SECTOR: A RESEARCH HANDBOOK* 140 (Walter W. Powell & Richard Steinberg eds., 2d ed. 2006);

6. See generally Richard Steinberg, *Economic Theories of Nonprofit Organizations*, in *THE NONPROFIT SECTOR: A RESEARCH HANDBOOK*, *supra* note 5, at 117.

7. James R. Hines Jr. et al., *The Attack on Nonprofit Status: A Charitable Assessment*, 108 MICH. L. REV. 1179, 1193–97 (2010).

8. See, e.g., M. Todd Henderson & Anup Malani, *Corporate Philanthropy and the Market for Altruism*, 109 COLUM. L. REV. 571, 573–40 (2009). See generally, e.g., Doug Guthrie, *Corporate Philanthropy in the United States: What Causes Do Corporations Back?*, in *POLITICS AND PARTNERSHIPS: THE ROLE OF VOLUNTARY ASSOCIATIONS IN AMERICA'S POLITICAL PAST AND PRESENT* 183 (Elisabeth S. Clemens & Doug Guthrie eds., 2010). For two specific examples, see also *Charity, NEWMAN'S OWN*, <http://bit.ly/1ff5YV5> (last visited Jan. 29, 2014), and, from this author's personal favorite snack food company, Nicole Dawes, *A New Season of Summer Camp Begins & Late July*

explicitly pursue social benefits as part of their missions.⁹ Disentangling and parceling out the charitable and non-charitable components of a company's mission can prove very challenging. For-profit companies often distribute substantial profits in the service of charitable purposes.¹⁰ Further, for-profit companies often partner with exempt organizations in the service of the same goals.¹¹

Contemporary scholarship from a range of disciplines, aside from law, has described and analyzed the many ways in which these border-crossings can occur.¹² Border-crossings between organizational sectors challenge deeply entrenched legal views about business, charity, and the boundedness of sectors that have come to dominate American society. For this reason, organizational border-crossings have, in the past several

Teams with the American Camp Association to Send Kids to Camp!, LATE JULY ORGANIC SNACKS (June 23, 2011, 12:00 PM), <http://bit.ly/1fnCULQ>.

9. See JAMES E. AUSTIN, *THE COLLABORATION CHALLENGE: HOW NONPROFITS AND BUSINESSES SUCCEED THROUGH STRATEGIC ALLIANCES* 30 (2000) (discussing collaborative alliance between CARE and Starbucks).

10. Guthrie, *supra* note 8, at 183–85.

11. See generally AUSTIN, *supra* note 9 (discussing how and why for-profit companies collaborate with exempt enterprises); SHIRLEY SAGAWA & ELI SEGAL, *COMMON INTEREST, COMMON GOOD: CREATING VALUE THROUGH BUSINESS AND SOCIAL SECTOR PARTNERSHIPS* (2000).

12. For treatment of the issue in legal scholarship alone, see generally, for example, Brian Galle, *Keep Charity Charitable*, 88 TEX. L. REV. 1213 (2010) [hereinafter Galle, *Keep Charity Charitable*]; Brian Galle, *Social Enterprise: Who Needs It?*, 54 B.C. L. REV. 2025 (2013) [hereinafter Galle, *Social Enterprise*]; Henderson & Malani, *supra* note 8; Hines et al., *supra* note 7; Garry W. Jenkins, *Who's Afraid of Philanthrocapitalism?*, 61 CASE W. RES. L. REV. 753 (2011); Thomas Kelley, *Law and Choice of Entity on the Social Enterprise Frontier*, 84 TUL. L. REV. 337 (2009); Robert Lang & Elizabeth Carrott Minnigh, *The L3C, History, Basic Construct, and Legal Framework*, 35 VT. L. REV. 15 (2010); Benjamin Moses Leff, *The Case Against For-Profit Charity*, 42 SETON HALL L. REV. 819 (2012); Anup Malani & Eric A. Posner, *The Case for For-Profit Charities*, 93 VA. L. REV. 2017 (2007); Lloyd Hitoshi Mayer & Joseph R. Ganahl, *Taxing Social Enterprise*, 66 STAN. L. REV. 387 (2014); Martha Minow, *Partners, Not Rivals?: Redrawing the Lines Between Public and Private, Non-Profit and Profit, and Secular and Religious*, 80 B.U. L. REV. 1061 (2000); Antony Page & Robert A. Katz, *Freezing Out Ben & Jerry: Corporate Law and the Sale of a Social Enterprise Icon*, 35 VT. L. REV. 211 (2010); David E. Pozen, *We Are All Entrepreneurs Now*, 43 WAKE FOREST L. REV. 283, 294–300 (2008); Dana Brakman Reiser, *Blended Enterprise and the Dual Mission Dilemma*, 35 VT. L. REV. 105 (2010) [hereinafter Reiser, *Blended Enterprise*]; Dana Brakman Reiser, *Charity Law's Essentials*, 86 NOTRE DAME L. REV. 1, 39–40 (2011) [hereinafter Reiser, *Charity Law's Essentials*]; Dana Brakman Reiser, *For-Profit Philanthropy*, 77 FORDHAM L. REV. 2437 (2009) [hereinafter Reiser, *For-Profit Philanthropy*]; Dana Brakman Reiser, *Theorizing Forms for Social Enterprise*, 62 EMORY L.J. 681 (2013) [hereinafter Reiser, *Theorizing Forms*]; Matthew F. Doeringer, Note, *Fostering Social Enterprise: A Historical and International Analysis*, 20 DUKE J. COMP. & INT'L L. 291, 322 (2010); Ashley Schoenjahn, Note, *New Faces of Corporate Responsibility: Will New Entity Forms Allow Businesses to Do Good?*, 37 J. CORP. L. 453, 470 (2012); Culley & Horwitz, *supra* note 5; Victor Fleischer, "For Profit Charity": *Not Quite Ready for Prime Time*, 93 VA. L. REV. IN BRIEF 231 (2008), available at <http://bit.ly/1nlwws1>.

years, become a particularly fruitful and dynamic area of legal scholarship. Legal scholars have, inter alia, considered the larger social and philosophical ramifications of border-crossings,¹³ proposed major reforms of tax and business law to address this phenomenon,¹⁴ and argued against those reforms.¹⁵

However, in debating the pros and cons of border-crossings in the abstract and considering potential overhauls to address this development, existing legal scholarship has overlooked two key points. First, regardless of whether they should do so, contemporary organizations do cross sectorial borders. In recent decades, organizational sociology has recognized that this is the case—that modern social organizations often span the borders of what sociologists call “fields.” When organizations engage in field-crossings, the entities tend to change significantly. The second point overlooked by legal scholars is that, insofar as border-crossings take place, tax law can provide a powerful tool for directing and shaping the nature of those border-crossings.

My observations here suggest that, instead of obstructing border-crossings, federal tax law not only should accept the reality that organizations cross sectorial borders, but should also consider how to direct those crossings in ways that produce social benefit. Thus, the challenge—which the tax law literature has not yet addressed—is to examine existing organizational practices and to identify which practices the tax law should productively encourage.

Drawing on organizational sociology scholarship, this Article will directly tackle this challenge. In particular, this Article will illustrate how existing federal tax law has defined sectorial boundaries too rigidly and how that law has failed to account for the actual functioning of both for-profit and exempt organizations. Given this state of the law, this Article argues that federal tax law should make the for-profit/nonprofit border more flexible. More specifically, tax law should identify and stimulate border-crossing practices that create social value. This Article identifies one such practice—that of cross-sector collaborations—that has substantial potential to generate benefits for society. Bearing this objective in mind, this Article proposes and details several concrete ways by which federal tax law might encourage such beneficial collaborations.

13. See generally, e.g., Galle, *Keep Charity Charitable*, *supra* note 12; Hines et al., *supra* note 7; Leff, *supra* note 12; Minow, *supra* note 12.

14. See generally, e.g., Henderson & Malani, *supra* note 8; Jenkins, *supra* note 12; Lang & Minnigh, *supra* note 12; Malani & Posner, *supra* note 12; Reiser, *Theorizing Forms*, *supra* note 12.

15. See generally, e.g., Galle, *Social Enterprise*, *supra* note 12; Hines et al., *supra* note 7; Leff, *supra* note 12; Mayer & Ganahl, *supra* note 12; Culley & Horwitz, *supra* note 5; Fleischer, *supra* note 12.

To develop this analysis, this Article proceeds in three parts. Part II describes how tax law currently constructs the border of the tax-exempt organizational sector vis-à-vis the for-profit sector. Part III proposes that we should understand institutions as organizations that cross sectorial borders. This Part describes ways in which organizations do cross sectorial boundaries. It then examines border-crossing in light of research in organizational sociology, making use of that research to expose the problems and practical consequences that result from the overly rigid sectorial border that tax law currently imposes. Part IV then uses this research to consider ways in which to reorganize or redesign federal tax law to reckon with boundary-crossing organizations and to steer them in socially beneficial directions. In particular, this Part spells out several methods by which the tax code could stimulate cross-sector collaborations or alliances.

II. BORDERS OF THE TAX-EXEMPT SECTOR

Federal tax law defines the tax-exempt sector precisely and rigidly. This Part examines the way that federal tax law draws the sector's boundaries.¹⁶ This is a large topic, so the section does not purport to provide a full exegesis of exempt organization law. It aims to set forth, however, an account sufficient to support two claims. First, federal tax law carefully monitors the border of the tax-exempt sector to make sure that no exempt organization slips across the border to become a for-profit organization. Second, tax law offers for-profit organizations no entry into the exempt sector. These claims match the view of a prominent practitioner who writes:

[T]he entire legal and regulatory structure that governs U.S. businesses and nonprofits is designed to ensure that the charitable sector and the business sector stay fundamentally distinct. . . . [C]harity is supposed to be all about mission and not about money, whereas for-profit businesses are supposed to be all about money and not about mission. As a result, business and charities are regulated and operated according to fundamentally different principles, and any crossing of the lines is viewed with skepticism by regulators and the public.¹⁷

16. For similar overviews of exempt organization law, see generally, for example, Malani & Posner, *supra* note 12; Mayer & Ganahl, *supra* note 12.

17. Allen R. Bromberger, *A New Type of Hybrid*, STAN. SOC. INNOVATION REV., Spring 2011, at 49, 50.

A. *Qualifying as a Nonprofit Organization*

Organizations “organized and operated” for certain purposes may qualify for tax exemption.¹⁸ The federal income tax code has included exemption provisions since its 1894 incarnation.¹⁹

The most prominent group of exempt organizations is that composed of “charitable, religious, educational, and scientific entities,” otherwise known as “charitable organizations,” “charities,” or “§ 501(c)(3) organizations.”²⁰ Organizations “organized and operated” for one of these purposes receive two major tax benefits. First, these charities are exempt from federal income tax on all or almost all of their net income. Second, individuals and corporations may deduct, within certain limits, contributions to charities.²¹ When discussing “tax-exempt organizations,” the remainder of this Article will be referring to charities.

To qualify for exemption as a charity, an organization must be “organized and operated” exclusively for charitable purposes. This category encompasses “religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition . . . , or for the prevention of cruelty to children or animals[.]”²² The IRS regulations accompanying the federal tax code amplify this list of purposes to include:

Relief of the poor and distressed or of the underprivileged; advancement of religion; advancement of education or science; erection or maintenance of public buildings, monuments, or works; lessening of the burdens of Government; and promotion of social welfare by organizations designed to accomplish any of the above purposes, or (i) to lessen neighborhood tensions; (ii) to eliminate prejudice and discrimination; (iii) to defend human and civil rights secured by law; or (iv) to combat community deterioration and juvenile delinquency.²³

This list is exhaustive.

The statutory “organized and operated” language points to an additional set of requirements for an organization seeking to qualify as a

18. See I.R.C. §§ 501(c), 527–28 (2012).

19. Act of Aug. 27, 1894, ch. 349, § 32, 28 Stat. 509, 556 (“[N]othing herein contained shall apply to . . . corporations, companies, or associations organized and conducted solely for charitable, religious, or educational purposes . . .”).

20. See BITTKER & LOKKEN, *supra* note 4, at ¶ 100.1.2.

21. I.R.C. § 170 (2012); see also STAFF OF J. COMM. ON TAXATION, 109TH CONG., HISTORICAL DEVELOPMENT AND PRESENT LAW OF THE FEDERAL TAX EXEMPTION FOR CHARITIES AND OTHER TAX-EXEMPT ORGANIZATIONS (Comm. Print 2005), available at <http://1.usa.gov/1d8t5wf>.

22. I.R.C. § 501(c)(3).

23. Treas. Reg. § 1.501(c)(3)-1(d)(2) (2008).

charity. This language gives rise to what tax practitioners and scholars commonly refer to as the “organizational” and “operational” tests for charitable status.²⁴ An organization is “organized” for charitable purposes if its charter or other organizing document: (1) limits its purposes to one or more of the above-described permissible purposes, and (2) does not authorize the organization to engage in any substantial activities that do not further one of those purposes.²⁵

This “organizational test” also limits what a charity may do with its assets when it stops operating. If the organization were to distribute assets to its members or shareholders when it liquidates, those assets would not serve one of the exempt purposes. Accordingly, to satisfy the “organizational test,” the organization must demonstrate that, when it ceases to exist, it will distribute its assets either in service of one of the permissible purposes or to a government.²⁶

B. *Operating as a Tax-Exempt Organization*

As the tax-exempt charity begins to carry out the activities authorized in its charter, the organization must also satisfy the “operational test.”²⁷ Under this additional test, the charity must engage “primarily in activities which accomplish one or more of [the] exempt purposes specified in section 501(c)(3).”²⁸ The organization fails the test “if more than an insubstantial part of its activities is not in furtherance of an exempt purpose.”²⁹ The purpose of this test is to ensure that, as an organization carries out its activities, it does not stray from its permissible purpose.

In addition to the operational test, the charity must comply with a series of other requirements aimed at keeping the charity firmly on its own side of the nonprofit border. Very importantly, the charity’s net earnings must not “inure[] to the benefit of any private shareholder or individual[.]”³⁰ Some authorities refer to this private inurement rule as the “nondistribution constraint.”³¹ This rule means that a charity may not

24. BITTKER & LOKKEN, *supra* note 4, at ¶ 100.2.

25. Treas. Reg. § 1.501(c)(3)-1(b)(1).

26. *Id.* § 1.501(c)(3)-1(b)(4).

27. *Id.* § 1.501(c)(3)-1(c).

28. *Id.* § 1.501(c)(3)-1(c)(1).

29. *Id.*

30. I.R.C. § 501(c)(3) (2012); *see also id.* § 4958; Treas. Reg. § 1.501(c)(3)-1(f)(2)(ii).

31. For the origin of this phrase, see Henry Hansmann, *The Rationale for Exempting Nonprofit Organizations from Corporate Income Taxation*, 91 YALE L.J. 54, 56–57 (1981). For its subsequent use, see, for example, Malani & Posner, *supra* note 12, at 2024; Mayer & Ganahl, *supra* note 12, at 404.

distribute any of its assets as profits to shareholders.³² Further, the charity may not pay any of its directors or staff at above-market rates.³³

The nondistribution constraint attempts to ensure that a charity does not distribute its assets in any way that might resemble a for-profit company disbursing its profits. One well-known treatise lists a variety of practices banned under this constraint: “excessive salaries, excessive rental payments, unwarranted payments or reimbursements of personal expenses, unsecured interest-free loans, leases of the organization’s property to insiders for less than fair rental value, unexplained transfers, and outright theft, often combined with sloppy bookkeeping and an inextricable commingling of assets.”³⁴ Charities may purchase goods or services from organizational insiders if the organizations pay fair market value for the goods and services.³⁵ However, as mentioned above, charities may not compensate the organizational insiders for goods or services at above-market rates. For this reason, the nondistribution constraint allows the IRS to scrutinize charity compensation arrangements carefully.³⁶ The IRS particularly monitors any salaries paid to charity directors or staff members that might depend on the

32. I.R.C. §§ 501(c)(3), 4958. *See also* Mayer & Ganahl, *supra* note 12, at 407. In 1996, new legislation enacting I.R.C. § 4958 imposed “intermediate sanctions” on organizations that violate this “private inurement” rule in ways not egregious enough to warrant losing exemption. Taxpayer Bill of Rights 2, Pub. L. No. 104-168, § 1311(d), 110 Stat. 1452, 1476 (1996). For more on Congress’s intent to use these provisions to provide “intermediate sanctions,” see H.R. REP. No. 104-506, at 55 (1996). The Treasury Department subsequently issued detailed regulations regarding this legislation. Together, the legislation and its regulations prohibit specific “excess benefit” transactions that Congress deemed inappropriate for charities. For more on these rules, see Evelyn Brody, *Business Activities of Nonprofit Organizations: Legal Boundary Problems*, in *NONPROFITS & BUSINESS* 83, 101 (Joseph J. Cordes & C. Eugene Steuerle eds., 2009); Pamela S. Kaufmann, *The Intermediate Sanctions Regulations Are Final—No More Excuses*, 96 J. TAX’N 240 (2002).

33. I.R.C. §§ 501(c)(3), 4958.

34. BITTKER & LOKKEN, *supra* note 4, at ¶ 100.4.1 (citing *Orange Cnty. Agric. Soc’y, Inc. v. Comm’r*, 893 F.2d 529 (2d Cir. 1990); *Church of Scientology v. Comm’r*, 823 F.2d 1310 (9th Cir. 1987); *Basic Unit Ministry v. Comm’r*, 670 F.2d 1210 (D.C. Cir. 1982); *Harding Hosp., Inc. v. United States*, 505 F.2d 1068 (6th Cir. 1974); *Cleveland Chiropractic Coll. v. Comm’r*, 312 F.2d 203 (8th Cir. 1963); *Birmingham Bus. Coll., Inc. v. Comm’r*, 276 F.2d 476 (5th Cir. 1960); *Easter House v. United States*, 12 Cl. Ct. 476 (1987), *aff’d*, 846 F.2d 78 (Fed. Cir. 1988); *John Marshall Law Sch. v. United States*, 228 Ct. Cl. 902 (1981); *Founding Church of Scientology v. United States*, 412 F.2d 1197 (Ct. Cl. 1969); *Variety Club Tent No. 6 Charities, Inc. v. Comm’r*, 74 T.C.M. (CCH) 1485, 1493 (1997); *Lowry Hosp. Ass’n v. Comm’r*, 66 T.C. 850 (1976); *Texas Trade Sch. v. Comm’r*, 30 T.C. 642 (1958), *aff’d*, 272 F.2d 168 (5th Cir. 1959)).

35. *See, e.g., Founding Church of Scientology*, 412 F.2d at 1197.

36. *See* Consuelo Laudo Kertz, *Executive Compensation Dilemmas in Tax-Exempt Organizations: Reasonableness, Comparability, and Disclosure*, 71 TUL. L. REV. 819, 823 (1997).

organization's revenues.³⁷ Salaries based on revenues start to resemble distributions of organizational profits—the exact practice that the nondistribution constraint prohibits.

Beyond the nondistribution constraint, the charity must comply with the ban on “private benefit” as it carries out its activities.³⁸ Under this rule, in addition to the purpose it serves according to the statutory list above, the organization must “serve[] a public rather than a private interest.”³⁹ This means that the organization may not serve a private individual or group and instead must serve the broader public.

Treasury regulations give three examples of hypothetical organizations whose services would violate this test.⁴⁰

The second example pertains to an art museum that displays the works of promising local artists. The museum's contracts specify that it may sell these works and give 90 percent of the proceeds to the artists. The regulations specify that this organization would serve the private interests of artists rather than the broader public interest.⁴¹

The third example relates to an organization that runs a training program that a for-profit company previously ran. The president of the for-profit company still owns the program. The for-profit company licenses the use of its name, sets program tuition, and provides program materials and trainers to the charity in exchange for royalty payments. The charity may develop its own program materials, but must transfer them back to the for-profit company if the license agreement between the two ever terminates. According to tax-exempt organization regulations, the charity here serves the private interest of the for-profit company rather than the broader public interest.⁴²

The ban on private benefit as amplified in these examples is yet another way in which the tax law erects a rigid border between for-profit and nonprofit entities. Nonprofit organizations are, under this ban, institutions that cannot benefit private individuals, whereas for-profit organizations do benefit private individuals. If a nonprofit organization crosses the hard-and-fast sectorial border and starts to benefit private

37. See, e.g., *Church of Scientology*, 823 F.2d at 1312; *Birmingham Bus. Coll., Inc.*, 276 F.2d at 478–79; *Kemper Military Sch. v. Crutchley*, 274 F. 125, 127 (W.D. Mo. 1921); *Sonora Cmty. Hosp. v. Comm'r*, 46 T.C. 519, 526 (1966); *Gemological Inst. of Am. v. Comm'r*, 17 T.C. 1604, 1609–10 (1952), *aff'd*, 212 F.2d 205 (9th Cir. 1954).

38. I.R.C. § 501(c)(3); Mayer & Ganahl, *supra* note 12, at 407.

39. Treas. Reg. § 1.501(c)(3)-1(d)(1)(ii) (2008). This language applies to all exempt organizations that serve purposes enumerated in that section. See, e.g., *Am. Campaign Acad. v. Comm'r*, 92 T.C. 1053, 1078–79 (1989).

40. Treas. Reg. § 1.501(c)(3)-1(d)(1)(iii).

41. *Id.*

42. *Id.*

interests, it has violated the membership rules for the nonprofit sector and will be ejected.

The private-inurement and public-benefit tests described above are not the only ways that the tax law strives to keep nonprofit organizations firmly on their side of the border. In addition, charitable organizations must adhere to certain limits on their political activities and obey the “public policy” doctrine. The political constraints are relatively straightforward. A charity may not allow a “substantial part” of its “activities” to consist of “carrying on propaganda, or otherwise attempting, to influence legislation” or to involve participating or intervening in a “political campaign.”⁴³

A more complex standard emerges from the “public policy” doctrine. This doctrine stems from the landmark case *Bob Jones University v. United States*.⁴⁴ In that case, Bob Jones University, a charity, had in place a ban on interracial dating. The IRS revoked the university’s exemption on the grounds that the ban violated “public policy.” The Supreme Court agreed, holding that “entitlement to tax exemption depends on meeting certain common law standards of charity—namely, that an institution seeking tax-exempt status must serve a public purpose and not be contrary to established public policy.”⁴⁵

This case now stands for the rule that charities may not operate in ways that run contrary to “public policy.”⁴⁶ Fortifying the exempt boundary still further, the Supreme Court in *Bob Jones* specifically grounded its ruling in the charitable sector’s distinctive character. Charitable organizations may not operate contrary to public policy because, unlike other organizations, they serve “public purpose[s].”⁴⁷ No equivalent to the *Bob Jones* case exists for for-profit organizations.⁴⁸

Another border-reinforcing requirement for charities prohibits them from becoming overly “commercial.”⁴⁹ Under this rule, the IRS may

43. I.R.C. § 501(c)(3); see also Johnny Rex Buckles, *Not Even a Peep? The Regulation of Political Campaign Activity by Charities Through Federal Tax Law*, 75 U. CIN. L. REV. 1071, 1077 (2007); Laura B. Chisolm, *Exempt Organization Advocacy: Matching the Rules to the Rationales*, 63 IND. L.J. 201, 220–23 (1987); Miriam Galston, *Lobbying and the Public Interest: Rethinking the Internal Revenue Code’s Treatment of Legislative Activities*, 71 TEX. L. REV. 1269, 1278 (1993); Joseph S. Klapach, Note, *Thou Shalt Not Politic: A Principled Approach to Section 501(c)(3)’s Prohibition of Political Campaign Activity*, 84 CORNELL L. REV. 504, 508–09 (1999).

44. *Bob Jones Univ. v. United States*, 461 U.S. 574 (1983).

45. *Id.* at 586.

46. *Id.*

47. *Id.*

48. For-profit organizations merely may not take business-expense deductions for expenses that violate public policy. See *Tank Truck Rentals, Inc. v. Comm’r*, 356 U.S. 30, 35 (1958).

49. See, e.g., *Asmark Inst., Inc. v. Comm’r*, 101 T.C.M. (CCH) 1067 (2011).

deny or revoke exemption from an organization whose activities resemble those of a “commercial” organization. Activities that the IRS has deemed excessively commercial include competing with commercial firms, providing services to for-profit businesses, maintaining a client base of for-profit firms, attempting to increase that client base, and offering services at the same prices as for-profit entities.⁵⁰ Under this commerciality doctrine, the IRS has denied exempt status to, inter alia, organizations training amateur baseball umpires,⁵¹ providing consulting services to artists for fees,⁵² writing grants for community organizations in exchange for payments,⁵³ and using mobile technology from a particular company to facilitate charitable donations.⁵⁴ In these cases, the IRS has explained that the organizations in question were carrying out “commercial activities” and, as a result, could not obtain the benefits of tax exemption.⁵⁵ However, charities may engage in only a modest amount of commercial activity without forfeiting tax exemption. In that case, however, they may have to pay unrelated business income tax (“UBIT”).⁵⁶

The ban on overly commercial activities further buttresses the border of the exempt sector. The IRS views commercial activities as the domain of for-profit organizations. The organizations denied exemption under the commerciality doctrine made claims to serve public purposes, but ventured too far across the border into what the IRS deemed for-profit territory.

C. *Qualifying and Existing as a For-Profit Organization*

Organizations that fall on the for-profit side of the border face an entirely different set of tax rules than nonprofit organizations. As legal scholars Lloyd Hitoshi Mayer and Joseph Ganahl have observed, “The federal income tax system, and to a lesser extent the various state tax

50. *See id.* at 1073. For additional discussion of the “commerciality doctrine,” see, for example, FRANCES R. HILL & DOUGLAS M. MANCINO, *TAXATION OF EXEMPT ORGANIZATIONS* ¶ 3.02, at 45–46 (2014), available at 2003 WL 1891101 (Westlaw); W. Marshall Sanders, *The Commerciality Doctrine is Alive and Well*, *TAX’N EXEMPTS*, Mar./Apr. 2005, at 209.

51. I.R.S. Priv. Ltr. Rul. 201217020 (Feb. 1, 2012).

52. I.R.S. Priv. Ltr. Rul. 201218023 (Jan. 12, 2012).

53. I.R.S. Priv. Ltr. Rul. 201247017 (Aug. 30, 2012).

54. I.R.S. Priv. Ltr. Rul. 201235021 (June 4, 2012).

55. I.R.S. Priv. Ltr. Rul. 201247017 (Aug. 30, 2012); I.R.S. Priv. Ltr. Rul. 201235021 (June 4, 2012); I.R.S. Priv. Ltr. Rul. 201217020 (Feb. 1, 2012); I.R.S. Priv. Ltr. Rul. 201218023 (Jan. 12, 2012).

56. I.R.C. §§ 511–513 (2012). Charitable organizations must pay UBIT on any “unrelated business taxable income” (“UBTI”). *Id.* § 512. UBTI is any income that a charity derives from carrying on a trade or business unrelated to its exempt purpose. *Id.* *See, e.g., id.* §§ 512(b), 513(a)(3).

systems, treat entities organized to generate profits for the benefit of investors very differently from the vast majority of entities organized as nonprofits.”⁵⁷

Most notably, unlike with tax-exempt organizations, tax law assumes that all for-profit entities can and will distribute their resources to private individuals. Businesses that fall on the for-profit side of the border do not necessarily have actual profits. Instead, for tax purposes, the ability to *distribute* funds to private parties is what distinguishes a for-profit organization from a nonprofit organization. Then, the various tax organizational forms ensure that the relevant private individuals will pay any income tax owed on income from the for-profit entity.⁵⁸

Tax law governing for-profit entities is a massive subject. Very briefly, for-profit entities, including LLCs and a variety of other forms, may choose among one of four principal organizational forms: the C corporation, the S corporation, the sole proprietorship, or the partnership.⁵⁹ The C corporation pays an entity-level tax on its income. With the other three forms, the tax law imposes tax on the entity’s owners rather than on the entity itself. All four organizational forms face hundreds of laws governing how they must conduct their affairs and distribute their resources. These laws all operate under the assumption that the entities are trying to make and distribute profits. The laws then tell the entities how to calculate those profits and how to treat their profit-making activities for tax purposes.

Tax law does recognize that for-profit organizations might donate money to charitable organizations. Corporations may, within limits, deduct most contributions to organizations qualifying for exemption under § 501(c)(3).⁶⁰ Specifically, corporations may deduct their contributions as long as the deducted amount is less than ten percent of taxable income.⁶¹ Under slightly different rules, individual taxpayers may deduct their similar contributions as long as their deducted amount is less than 50 percent of taxable income.⁶² When partnerships or sole proprietorships make charitable contributions, the tax law operates as if the individual owners of those businesses had made the contributions.⁶³ The individual owner in that case must add the contributions from his or her business to his or her personal contributions and then deduct that

57. Mayer & Ganahl, *supra* note 12, at 404.

58. *Id.* at 404–05.

59. See PERONI & BANK, *supra* note 2, at 16–17. The tax law also offers specialized forms to entities in particular industries. See, for example, I.R.C. § 856, which describes a form for real estate firms, the real estate investment trust (“REIT”).

60. I.R.C. § 170(a)(2).

61. *Id.* § 170(b)(2)(A).

62. *Id.* § 170(b)(1).

63. Treas. Reg. § 1.702-1(a)(4) (2005).

amount, subject to the 50 percent limit and to various other minor constraints under the charitable-deduction rules.⁶⁴

However, if the corporation or individual donates to a charitable organization for any sort of business purpose, the corporation or individual may generally deduct that amount in full.⁶⁵ Federal tax law allows businesses to deduct all “ordinary and necessary expenses” incurred “in carrying on” the business’s “trade or business.”⁶⁶ If a charitable contribution meets that standard, the for-profit entity may deduct it without facing the percentage and other limits of the charitable deduction.⁶⁷ However, companies may not use the business-deduction rules to escape percentage- or timing-related limits of the charitable deduction.⁶⁸

This complex set of tax regulations governing for-profit entities is entirely separate from the set governing nonprofit organizations. If an entity does not qualify for exemption under the rules described in the previous subsection, it is subject to the regulations designed for for-profit companies. Regardless of what the organization does, or how much of a profit it actually makes, if it does not pass the various exemption tests, it must operate within the regulatory framework that applies to all for-

64. *Id.* For the other minor constraints, see generally I.R.C. § 170 and the regulations promulgated thereunder.

65. A for-profit entity may not deduct as a business expense a charitable contribution that provides only an “incidental benefit” to the taxpayer’s business. See *Brooks v. Comm’r*, 10 T.C.M. (CCH) 1094 (1951); see also *Hartless Linen Serv. Co. v. Comm’r*, 32 T.C. 1026, 1029–31 (1959).

66. I.R.C. § 162(a). As a practical matter, for-profit entities often may choose whether they would prefer to deduct certain contributions as charitable gifts or as business deductions. Mayer & Ganahl note that:

Generally speaking, businesses will prefer, and so will usually try, to deduct expenses under § 170(a) for two reasons. First, there is the advantage of appearing to be concerned with social responsibility, thereby garnering consumer goodwill. Second, the forced capitalization of some expenses under § 263 may make it more advantageous to characterize expenses as charitable contributions under § 170 as long as the charitable contributions of the corporation do not exceed the ten percent of taxable income limit on C corporations deducting such contributions.

Mayer & Ganahl, *supra* note 12, at 409 (citing *United States v. Transamerica Corp.*, 392 F.2d 522, 523 (9th Cir. 1968); Nancy J. Knauer, *The Paradox of Corporate Giving: Tax Expenditures, the Nature of the Corporation, and the Social Construction of Charity*, 44 DEPAUL L. REV. 1, 43–44 (1994)).

67. I.R.C. § 162(a).

68. *Id.* § 162(b); Treas. Reg. § 1.162-15(a)(2) to -15(c) (as amended in 1965). For efforts to distinguish between charitable contributions and business expenses, see, for example, *Singer Co. v. United States*, 449 F.2d 413, 423 (Ct. Cl. 1971) (citing Rev. Rul. 67-446, 1967-2 C.B. 119); *Jefferson Mills, Inc. v. United States*, 259 F. Supp. 305, 310–12 (N.D. Ga. 1965), *aff’d per curiam*, 367 F.2d 392 (5th Cir. 1966); Rev. Rul. 72-314, 1972-1 C.B. 44; Rev. Rul. 63-73, 1963-1 C.B. 35.

profit companies. Under no circumstance can the for-profit company pass over into the tax-exempt world.

III. CONTEMPORARY ORGANIZATIONS AS INSTITUTIONS THAT CROSS SECTORIAL BORDERS

Part II of this Article described two very different legal frameworks that regulate the taxation of organizations: one for nonprofit entities that serve public purposes and the other for for-profit entities that serve private purposes. From the standpoint of federal tax law, any organization falls within either one or the other of these categories. Tax law does not conceive of organizations that regularly traverse this boundary. Nor, for the purposes of tax law, can organizations be subject partly to one tax framework regime and partly to the other.

Looking beyond the categories of federal tax law and considering the social reality in which organizations operate reveals, however, that organizations cross borders all the time. Part III begins by examining some significant instances in which organizations do so. It then uses tools from organizational sociology to understand these border-crossings and to identify the ways in which tax law fails to reflect these organizational realities.

A. *Corporate Social Responsibility, For-Profit Philanthropy, and Social Enterprise*

In actuality, organizations often do cross the for-profit/nonprofit border. Harvard Law School Dean Martha Minow described the boundary between the for-profit and nonprofit sectors as “rapidly fading, shifting, and criss-crossing.”⁶⁹ A substantial volume of scholarship, legal and otherwise, has documented instances in which this is the case.⁷⁰ This subsection very briefly describes some of these common border-crossings. Three major types include: (1) corporate social responsibility, (2) for-profit philanthropy, and (3) social enterprise. These border-crossings have received particular attention in recent years, although all three trends have their root in historical phenomena.⁷¹

To take the first of these, one of the most commonly discussed border-defying undertakings is “corporate social responsibility” (“CSR”). Business scholars and CSR experts C.B. Bhattacharya and Sankar Sen define CSR as a company’s “status and activities with

69. Minow, *supra* note 12, at 1062.

70. See generally sources cited *supra* note 12.

71. See generally Peter Dobkin Hall, *A Historical Overview of Philanthropy, Voluntary Associations, and Nonprofit Organizations in the United States, 1600–2000*, in THE NONPROFIT SECTOR: A RESEARCH HANDBOOK, *supra* note 5, at 32.

respect to its perceived societal or, at least, stakeholder obligations.”⁷² They point out that “more companies than ever before are backing CSR initiatives such as corporate philanthropy, cause-related marketing, minority support programs, and socially responsible employment and manufacturing practices[.]”⁷³ Bhattacharya and Sen contend that for-profit companies are currently pursuing CSR “with real financial and marketing muscle[.]” noting that, as of 2004, “[t]he web sites of more than 80% of the *Fortune 500* companies address[ed] CSR issues[.]”⁷⁴ Law professor Dana Brakman Reiser explains that CSR embodies the idea that “corporations and their leaders be *permitted* or *required* to consider interests beyond those of shareholders in their everyday business decisions.”⁷⁵

In the same vein, University of Chicago law professors Todd Henderson and Anup Malani describe how prevalent CSR initiatives are and how much they impose in costs on for-profit companies:

Firms now produce “green goods,” voluntarily reduce environmental emissions, and directly help provide medicines to the uninsured. . . . [C]onsider corporate commitments to reduce carbon dioxide emissions, which we estimate to cost firms tens of billions of dollars per year. Since there is currently no law or regulation requiring these reductions, there is no significant difference between a firm donating \$100 to an environmental charity and a firm spending \$100 to voluntarily reduce carbon dioxide emissions; both reduce the firm’s profit by \$100 with the goal of improving social welfare.⁷⁶

Related to CSR is what Brakman Reiser refers to under the second header of “for-profit philanthropy.”⁷⁷ Companies engaged in for-profit philanthropy direct the methods and resources of their for-profit enterprises toward social missions.⁷⁸ Brakman Reiser’s paradigmatic example is Google’s experiment with the for-profit philanthropy Google.org. Google.org is Google’s “philanthropic division,” which “stands alongside divisions for engineering, sales, and finance, but is

72. C.B. Bhattacharya & Sankar Sen, *Doing Better at Doing Good: When, Why, and How Consumers Respond to Corporate Social Initiatives*, 47 CAL. MGMT. REV. 9, 9 (2004) (internal quotation marks omitted) (quoting Tom J. Brown & Peter A. Dacin, *The Company and the Product: Corporate Associations and Consumer Product Responses*, 61 J. MARKETING 68, 68 (1997)).

73. *Id.*

74. *Id.*

75. Reiser, *For-Profit Philanthropy*, *supra* note 12, at 2446 (emphasis added).

76. Henderson & Malani, *supra* note 8, at 574 (footnotes omitted).

77. Reiser, *For-Profit Philanthropy*, *supra* note 12, at 2438.

78. *Id.* at 2437–38.

tasked with addressing climate change, poverty, and emerging diseases.”⁷⁹

Third and finally, one of the best-known manifestations of boundary-blurring organizations is “social enterprise.” Brakman Reiser defines social enterprise as “an organization formed to achieve social goals using business methods.”⁸⁰ She goes on to give examples: “Think companies that use one-for-one models like TOMS shoes and Warby Parker, or hire ‘hard-to-employ’ low-income or foreign-born individuals like Greyston Bakery and Hot Bread Kitchen. Think of your favorite green or locally-sourced business or of one serving customers at the bottom of the pyramid.”⁸¹ Of one famous social enterprise, Ben & Jerry’s ice cream company, legal scholars Antony Page and Robert F. Katz have observed:

It was a for-profit corporation that seemingly did not put profits first. Rather, it pursued, in the parlance, a “double bottom” line, seeking to advance progressive social goals, while still yielding an acceptable financial return for investors. It advanced its social mission in many ways, such as by committing 7.5% of its profits to a charitable foundation; conducting in-store voter registration; and buying ingredients from suppliers who employed disadvantaged populations.⁸²

Importantly, social enterprise encompasses not just for-profit entities with social missions, but also nonprofit entities using business tools to solve social problems. These nonprofit social enterprises undertake a variety of endeavors. In a recent article, practitioner Robert Wexler describes a few common types.⁸³ Wexler identifies organizations that employ and teach job skills to members of a disadvantaged group,⁸⁴ organizations that provide technical assistance to existing nonprofits,⁸⁵ microfinance organizations,⁸⁶ and organizations that “produce products or services in a businesslike fashion, but then sell and distribute those products and services at a deep discount to the poor.”⁸⁷ Organizations of these kinds include Pedal Revolution, which “helps at-risk youth learn how to develop job skills by working in a bicycle repair shop[.]”

79. *Id.*

80. Reiser, *Theorizing Forms*, *supra* note 12, at 681.

81. *Id.* at 681–82 (footnotes omitted).

82. Page & Katz, *supra* note 12, at 211. Ben & Jerry’s has not yet announced Free Cone Day for 2014.

83. Robert A. Wexler, *Effective Social Enterprise—A Menu of Legal Structures*, 63 EXEMPT ORG. TAX REV. 565 (2009).

84. *Id.* at 570.

85. *Id.*

86. *Id.* at 573.

87. *Id.* at 571.

CompassPoint Nonprofit Services, which “provides technical assistance to exempt organizations[,]” and the Institute for OneWorld Health, which “helps develop new medicines to help the poor and works with companies to help disseminate the medicines.”⁸⁸

All of these ventures represent organizations that cross the for-profit/nonprofit boundary. In all of them, organizations are pursuing elements of private and public benefit in tandem. The organizations carrying out these ventures hope to accumulate resources and perhaps even distribute resources, while also benefiting the public. For these border-crossing groups, all of these goals are linked.

B. The Organizational Dynamics of Border-Crossings

Organizational border-crossings present a challenge for tax law as a result of its sharp division between for-profit and nonprofit organizations. However, research from sociology enables us to understand the growth of organizations that cross these borders and, for purposes of tax law, to understand the dynamics of these organizations as well. This body of research highlights the difficulty of grouping organizations rigidly into sectors. Instead, sociological scholarship has shown that organizations from different sectors regularly exert powerful influences over each other. Part III.B will summarize a few of the most important conclusions from this research, as they can be used to analyze the nonprofit/for-profit border.

Sociologists studying organizations refer to those organizations as existing in “fields.”⁸⁹ The concept of a “field” corresponds to that of an organizational sector.⁹⁰ Sociologists generally prefer to speak of “fields,” rather than of “sectors,” because the field concept is broader and applicable not only to sectors of the economy, but also to political, religious, educational, and other institutions. A field is a “community of organizations that coexist and interact in some area of institutional life and share common systems of meaning, values, and norms.”⁹¹ From this

88. Wexler, *supra* note 83, at 571.

89. *See generally* NEIL FLIGSTEIN & DOUG MCADAM, A THEORY OF FIELDS (2012).

90. *Id.* at 9.

91. Shauhin Talesh, *Lost in Translation: How Competing Organizational Field Logics Mediate the Meaning of Rights 7* (2013) (unpublished manuscript) (on file with author). *See generally* W. RICHARD SCOTT ET AL., INSTITUTIONAL CHANGE AND HEALTH CARE ORGANIZATIONS: FROM PROFESSIONAL DOMINANCE TO MANAGED CARE (2000); W. RICHARD SCOTT, INSTITUTIONS AND ORGANIZATIONS (2d ed. 2001); Paul J. DiMaggio & Walter W. Powell, *The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields*, 48 AM. SOC. REV. 147 (1983); Lauren B. Edelman, *Overlapping Fields and Constructed Legacies: The Endogeneity of Law*, in PRIVATE EQUITY, CORPORATE GOVERNANCE AND THE DYNAMICS OF CAPITAL MARKET REGULATION 55, 55–90 (Justin O’ Brien ed., 2007); Mark C. Suchman & Lauren B. Edelman, *Legal*

point of view, for-profit organizations constitute one field, while nonprofit organizations constitute another.

Particular organizations act within fields. According to sociologists, especially those who consider themselves members of the “new institutionalist” school, fields shape and constrain organizational behavior. As sociologists Walter Powell and Paul DiMaggio explain, in a field “organizational actors making rational decisions construct around themselves an environment that constrains their ability to change further in later years.”⁹² Within fields, organizations establish their own “routines,” which include “the forms, rules, procedures, conventions, strategies, and technologies around which . . . and through which they operate.”⁹³ These routines are among the factors that influence how organizations operate.

Significantly, sociologists have found that the borders between different organizational fields are “not fixed but shift depending on the definition of the situation and the issues at stake.”⁹⁴ In fact, one of the primary characteristics of fields is the extent to which their boundaries shift. In their recent book on the subject, sociologists Neil Fligstein and Doug McAdam characterize organizational fields by saying that “[fields] are continuously contested and constantly oscillating between greater and lesser stability and order[,] . . . [and are always] in some sort of flux[.]”⁹⁵

What causes the boundaries of a field to fluctuate? Many things, but particularly powerful among these is the force that other fields exert. Fligstein and McAdam explain that it is difficult to understate “just how complicated and potentially consequential . . . the ties [are] that link any given . . . field to its broader field environment.”⁹⁶ Accordingly, they emphasize the need “to take seriously the constraints (and opportunities) imposed on [given fields] by the myriad ties they share to other fields.”⁹⁷

Elaborating these observations, Powell and DiMaggio describe how “[o]rganizations in a structured field . . . respond to an environment that consists of other organizations responding to their environment, which consists of organizations responding to an environment of organizations’ responses.”⁹⁸ Over time, however, organizations not only shift their

Rational Myths: The New Institutionalism and the Law and Society Tradition, 21 LAW & SOC. INQUIRY 903 (1996).

92. DiMaggio & Powell, *supra* note 91, at 148.

93. Barbara Levitt & James G. March, *Organizational Learning*, 14 ANN. REV. SOC. 319, 320 (1988).

94. FLIGSTEIN & MCADAM, *supra* note 89, at 10.

95. *Id.* at 12.

96. *Id.* at 19.

97. *Id.*

98. DiMaggio & Powell, *supra* note 91, at 149. See generally THOMAS C. SCHELLING, MICROMOTIVES AND MACROBEHAVIOR (1978).

activities, but they also alter their foundational identities and beliefs. Indeed, scholars of organizational learning Barbara Levitt and James March describe how “some of the more powerful phenomena in organizational change surround the transformation of givens, the redefinition of events, alternatives, and concepts through consciousness raising, culture building, . . . or paradigm shifts.”⁹⁹

Then, this line of sociological research emphasizes that organizations that interact with each other become more like each other over time. DiMaggio and Powell call this phenomenon “*institutional isomorphism*.”¹⁰⁰ Drawing on a number of case studies, they find that, for organizations, “powerful forces emerge that lead them to become more similar to one another.”¹⁰¹ Even organizations that start out with different purposes morph into organizations resembling one another through contact with each other.

DiMaggio and Powell and the scholars that follow them recognize that different types of isomorphism emerge in different contexts. However, certain factors are more likely to give rise to all types of isomorphism. Among these factors, DiMaggio and Powell find that if organizations are dependent on each other, they are more likely to become similar in “structure, climate and behavioral focus.”¹⁰² Important additional factors are the intensity, frequency, and mechanism of organizational contact. Sociologists David Strang and Sarah Soule describe inter-field influences as “flowing along the lines of close social relations.”¹⁰³ They point as well to how “[f]requent interaction engenders much exchange of information about the character, motivations, and effects of diffusing practices.”¹⁰⁴ Writing from what they call an “organizational-ecology” perspective, Levitt and March liken the flow of practices and understandings across different organizational fields to the movement of diseases. Levitt and March call this isomorphic mechanism “diffusion,” comparing it to the “spread of a disease through contact between a member of the population who is infected and one who is not, sometimes mediated by a host carrier.”¹⁰⁵

99. Levitt & March, *supra* note 93, at 324. See generally CHRIS ARGYRIS & DONALD A. SCHON, ORGANIZATIONAL LEARNING (1978); Nicole Woolsey Biggart, *The Creative-Destructive Process of Organizational Change: The Case of the Post Office*, 22 ADMIN. SCI. Q. 410 (1977); Richard Harvey Brown, *Bureaucracy as Praxis: Toward a Political Phenomenology of Formal Organizations*, 23 ADMIN. SCI. Q. 365 (1978).

100. DiMaggio & Powell, *supra* note 91, at 150 (emphasis added).

101. *Id.* at 148.

102. *Id.* at 154.

103. David Strang & Sarah A. Soule, *Diffusion in Organizations and Social Movements: From Hybrid Corn to Poison Pills*, 24 ANN. REV. SOC. 265, 272 (1998).

104. *Id.*

105. Levitt & March, *supra* note 93, at 330.

Through diffusion, “[o]rganizations capture the experience of other organizations through the transfer of encoded experience in the form of technologies, codes, procedures, or similar routines.”¹⁰⁶ Levitt and March cite examples of “routines diffused by contacts among organizations” that are “transmitted through socialization, education, imitation, professionalization, personnel movement, mergers, and acquisitions.”¹⁰⁷ Other mechanisms, according to law professor Lauren Edelman and sociologist Mark Suchman, include “‘softer’ organizational phenomena such as inter-organizational cooperation, community-building, public relations, and reputation.”¹⁰⁸

In related research, sociologists Joel Podolny and Karen Page have argued that various network connections among organizations “allow participating [organizations] to learn new skills or acquire knowledge, gain legitimacy, improve economic performance, and manage resource dependencies.”¹⁰⁹ This learning process occurs because inter-field links “can encourage learning by promoting the rapid transfer of self-contained pieces of information.”¹¹⁰ Further, such linkages “may foster learning by encouraging novel syntheses of information that are qualitatively distinct from the information that previously resided within the distinct nodes.”¹¹¹

Drawing specifically on research about the linkages between for-profit and nonprofit organizations in the biotechnology field, Podolny and Page report that, by “facilitat[ing] the transfer of information between two nodes [i.e., organizations], the existence of an enduring exchange relation may actually yield new knowledge . . . [because] the network [that spans fields] becomes the locus of innovation rather than

106. *Id.* at 329; see also John M. Dutton & William H. Starbuck, *Diffusion of an Intellectual Technology*, in COMMUNICATION AND CONTROL IN SOCIETY 489, 489–511 (Klaus Krippendorff ed., 1979).

107. Levitt & March, *supra* note 93, at 320, 330.

108. Lauren B. Edelman & Mark C. Suchman, *The Legal Environments of Organizations*, 23 ANN. REV. SOC. 479, 494 (1997). See generally CLIFFORD GEERTZ, LOCAL KNOWLEDGE (1983).

109. Joel M. Podolny & Karen L. Page, *Network Forms of Organization*, 24 ANN. REV. SOC. 57, 62 (1998).

110. *Id.* See generally Farok J. Contractor & Peter Lorange, *Why Should Firms Cooperate? The Strategy and Economics Basis for Cooperative Ventures*, in COOPERATIVE STRATEGIES IN INTERNATIONAL BUSINESS 3 (Farok J. Contractor & Peter Lorange eds., 1988); Bruce Kogut, *A Study of the Life Cycle of Joint Ventures*, 28 MGMT. INT’L REV. 39 (1988); Franklin R. Root, *Some Taxonomies of International Cooperative Arrangements*, in COOPERATIVE STRATEGIES IN INTERNATIONAL BUSINESS, *supra*, at 69.

111. Podolny & Page, *supra* note 109, at 63. See generally Walter W. Powell & Peter Brantley, *Competitive Cooperation in Biotechnology: Learning Through Networks?*, in NETWORKS AND ORGANIZATIONS: STRUCTURE, FORM, AND ACTION 366 (Nitin Nohria & Robert G. Eccles eds., 1992).

the nodes that comprise the network.”¹¹² Sociologists Elisabeth Clemens and James Cook similarly observe that “ties, connectedness, visibility, and proximity facilitate the adoption of new organizational forms or policies.”¹¹³ This inter-field arrangement leads to “innovation as actors seek to accommodate newly adopted institutional rules to existing practices, resources, and competing schemas.”¹¹⁴

But how does law enter this picture? According to organizational sociologists, legal institutions constitute yet another social field, but one that is closely linked to organizational sectors or fields. As such, law has an important role to play in shaping the boundaries of organizational fields and how organizations within fields change. Explaining this process, Edelman and Suchman¹¹⁵ observe:

[O]rganizations look to the law for normative and cognitive guidance, as they seek their place in a socially constructed cultural reality. Law provides a model of and for organizational life, defining roles for organizational actors and meanings for organizational events—and imbuing those roles and meanings with positive or negative moral valence.¹¹⁶

Strang and Soule echo this argument, drawing out the point that “much recent organizational analysis treats the state and the professions”—the field of law included—“as change agents that spread new practices and facilitate particular lines of innovative action.”¹¹⁷

The most “profound” way in which law shapes organizational fields and the boundaries between them is by establishing what Edelman and Suchman refer to as a “constitutive environment.”¹¹⁸ Law “constructs

112. Podolny & Page, *supra* note 109, at 63 (citing Powell & Brantley, *supra* note 111; Walter W. Powell et al., *Interorganizational Collaboration and the Locus of Innovation: Networks of Learning in Biotechnology*, 41 ADMIN. SCI. Q. 116 (1996)).

113. Elisabeth S. Clemens & James M. Cook, *Politics & Institutionalism: Explaining Durability and Change*, 25 ANN. REV. SOC. 441, 451 (1999).

114. *Id.* at 452.

115. Edelman & Suchman, *supra* note 108. See generally YASEMIN NUHOGLU SOYSAL, LIMITS OF CITIZENSHIP: MIGRANTS AND POSTNATIONAL MEMBERSHIP IN EUROPE (1994); D. ELEANOR WESTNEY, IMITATION AND INNOVATION: THE TRANSFER OF WESTERN ORGANIZATIONAL PATTERNS TO MEIJI JAPAN (1987); John L. Campbell, *Institutional Analysis and the Role of Ideas in Political Economy*, 27 THEORY & SOC'Y 377 (1998); Robin Stryker, *Legitimacy Processes as Institutional Politics: Implications for Theory and Research in the Sociology of Organizations*, in 17 RESEARCH IN THE SOCIOLOGY OF ORGANIZATIONS: ORGANIZATIONAL POLITICS 179 (Samuel B. Bacharach & Edward J. Lawler eds., 2000).

116. Edelman & Suchman, *supra* note 108, at 482.

117. Strang & Soule, *supra* note 103, at 271.

118. Edelman & Suchman, *supra* note 108, at 483.

and empowers various classes of organizational actors and delineates the relationships between them.”¹¹⁹ Edelman and Suchman note:

The constitutive legal environment is comprised primarily of *definitional categories*—those basic typologies that identify the legally cognizable components of the social world and that explain the natures and attributes of each. Constitutive law generally functions almost invisibly, providing taken-for-granted labels, categories, and “default rules” for organizational behavior; however, by establishing the background understandings that frame social discourse, constitutive law helps to determine what types of organizations come into existence and what types of organizational activity gain formal recognition. Thus, for example, the constitutive legal environment describes how various classes of organizations are born and how they die¹²⁰

In other words, for organizations, law is “a pervasive belief system that permeates the most fundamental morals and meanings of organizational life[.]”¹²¹ Consequently, organizations that the law sorts into distinct categories come to regard themselves differently than organizations sorted into other categories. In contrast, if law allows “a common legal environment” to extend *across* organizational fields, law can exert a further homogenizing influence over organizational “behavior and structure.”¹²²

C. *Border-Crossings and Tax Law*

The kinds of border-crossings between nonprofit and for-profit organizations described in Part III.A correspond to the inter-field dynamics that organizational sociology has observed. While organizational sociology has not specifically studied CSR, for-profit philanthropy, or social enterprise, this body of research would nevertheless lead one to expect these recent organizational developments. Indeed, sociological scholarship on fields offers an illuminating way to understand correctly the shifting nature of the for-profit/nonprofit border. The boundaries between the field of nonprofits and the field of for-profits “oscillat[e].”¹²³ As organizations in both fields adopt missions that, at different points in time, seek to combine

119. *Id.*

120. *Id.* (emphasis added).

121. *Id.* at 493.

122. DiMaggio & Powell, *supra* note 91, at 150.

123. FLIGSTEIN & MCADAM, *supra* note 89, at 12.

components of for-profit and nonprofit entities, these two fields seem “always [to] be in some sort of flux[.]”¹²⁴

Further, the forces currently loosening the boundaries between the for-profit and nonprofit fields arose because of the “broader field environment” in which each exists.¹²⁵ The for-profit sector can adopt social missions and undertake activities that create social benefit because the nonprofit sector already did those things. In fact, the practice that immediately predated the rise of CSR was the advent of business charitable contributions.¹²⁶ Initially, the for-profit sector confined its publicly oriented mission to sharing resources with organizations that had publicly oriented missions.¹²⁷ Only over time did organizations within the for-profit field begin to encompass social goals into their *own* missions.¹²⁸

Conceptualizing for-profit and nonprofit entities as “complex social actors whose behavior is shaped by their cultural environment”¹²⁹ helps to explain why organizations have begun to cross the for-profit and nonprofit borders with increasing frequency, notwithstanding the tax code’s impediments. As the for-profit and nonprofit sectors orient themselves in new directions, the organizations within those fields adopt new orientations. Nonprofit and for-profit organizations are each “in a structured field, . . . respond[ing] to an environment that consists of other organizations responding to their environment, which consists of organizations responding to an environment of organizations’ responses.”¹³⁰ This is exactly how organizations in both fields began to cross borders. A few nonprofits experimented with market technologies; at the same time, for-profits began to work on projects promoting social good. A few high-profile innovators on both sides of the fluctuating boundary attracted positive attention and provided models for other organizations.¹³¹ Small steps by existing organizations, combined with innovations from new organizations, tilted both sectors toward each other. As the two fields gradually tilted, other organizations responded by tilting along with these fields. Then, just as DiMaggio and Powell’s argument about isomorphism would predict, still other organizations responded to the new tilts observed in organizations around them.

124. *Id.* at 12–13.

125. *Id.* at 19.

126. Reiser, *Theorizing Forms*, *supra* note 12, at 692.

127. *Id.* at 686; Henderson & Malani, *supra* note 8, at 573.

128. Henderson & Malani, *supra* note 8, at 573.

129. Talesh, *supra* note 91, at 7.

130. DiMaggio & Powell, *supra* note 91, at 149.

131. *See, e.g.*, Page & Katz, *supra* note 12, at 213.

As this reiterative process moved forward, various organizational learning mechanisms came into play, just as the sociological literature would anticipate. As Levitt and March describe, organizational “givens” were transformed and “paradigm[s] shift[ed].”¹³² Companies that may have taken the pursuit of profit as a given started to consider objectives that had little to do with profit. Nonprofit organizations that had never evaluated market methods began to do so. The national media “rais[ed] consciousness” about the ways in which organizations could cross borders.¹³³ Consciousness-raising then inspired organizations on both sides of the mutating field-boundary to try out new practices and goals. These experiments stimulated shared “culture building” around CSR, for-profit philanthropy, and social enterprise.¹³⁴ In turn, shifts in organizational cultures fostered additional border-crossing activities.

1. How Federal Tax Law Treats Border-Crossing Organizations

Despite the increase in for-profit/nonprofit border-crossings that has occurred, federal tax law was ill equipped to deal with this phenomenon when it began to emerge. This situation has not improved. Adhering to its rigid line between for-profit and nonprofit organizations, tax law had—and, to date, still has—no viable way to treat entities that span this gulf. As prominent exempt-organizations practitioner Robert Wexler recently observed, it is “cumbersome to design a social enterprise under the dense and unaccommodating passages of the [tax] code.”¹³⁵ Border-crossing ventures simply do not fit neatly into either the for-profit or the nonprofit frameworks of tax law. Each framework creates consequential hurdles for organizations attempting CSR, for-profit philanthropy, or social enterprise.

That is not to say that such organizations necessarily run afoul of tax law. Tax lawyers have crafted creative—and complex—legal devices and vehicles that allow these ventures to carry out their activities while complying with the law. However, designers of these vehicles have had to contend with operating outside of the tax law’s existing frameworks. Their vehicles all have been forced to use an apparatus that was not intended to accommodate the new inter-field developments and that has not been retooled to do so. Fitting CSR, for-profit philanthropy, or social enterprise into that apparatus has been challenging and cumbersome. As a result, organizations that cross the for-

132. Levitt & March, *supra* note 93, at 324.

133. *Id.*

134. *Id.*

135. Robert A. Wexler, *Social Enterprise: A Legal Context*, 54 EXEMPT ORG. TAX REV. 233, 244 (2006).

profit/nonprofit border must, at a minimum, confront considerable administrative complexity. They must also deal with the uncertainty that comes from using novel devices that neither Congress nor the IRS has approved.

As Wexler notes, because Congress and the IRS have not adjusted the tax law's for-profit/nonprofit boundary to accommodate border-crossers, there is no defined legal structure that they can use. To fill the void, tax lawyers and academics have posited a variety of different options, three of which I will describe briefly.¹³⁶

One option involves border-crossing organizations that attempt to stay on the nonprofit side of the for-profit/nonprofit border. These organizations apply for exempt status.¹³⁷ However, the exempt-organization tax code provisions often prove overly restrictive for the would-be border-crosser. For example, existing for-profit companies, no matter how socially responsible, cannot qualify for tax exemption without shedding their primary businesses.¹³⁸ Moreover, the nondistribution constraint prevents tax-exempt organizations from distributing returns to investors.¹³⁹ As a result, border-crossing ventures that plan to remain tax-exempt cannot raise money from investors who expect returns. Additionally, charitable organizations that only raise money from a handful of sources will constitute "private foundations" under the tax code. The tax code substantially restricts the activities of private foundations.¹⁴⁰ Among other requirements, private foundations must distribute at least five percent of their net assets a year for charitable purposes.¹⁴¹ Similarly, the nondistribution constraint and private-benefit rules prevent the owners of an organization from benefiting from it. Consequently, an organization whose owners may want to sell part of it eventually may not use the tax-exempt form. Then, a venture whose mission includes for-profit and nonprofit elements always runs the risk that the IRS will conclude that the organization has strayed too far from an exempt purpose, distributed too much to private parties, elevated the interests of some other group over those of the

136. For a very useful overview of the different options, see generally Wexler, *supra* note 83. For a treatment of these options in the popular press, see Esha Chhabra, *A Social Entrepreneur's Quandary: Nonprofit or For-Profit?*, N.Y. TIMES, July 10, 2013, <http://nyti.ms/1brx62i>.

137. Wexler, *supra* note 83, at 569. Sometimes the organizations will also choose to apply for exemption not as a charity but as an organization described in I.R.C. § 501(c)(4) (2012). *Id.*

138. Existing for-profit businesses would likely run afoul of the organizational and operational tests, the private-inurement and private benefit rules, and the commerciality doctrine.

139. See discussion *supra* Part II.B.

140. See I.R.C. §§ 4940–4945 (2012).

141. *Id.* § 4942(e).

public, or become excessively commercial. For these reasons, some border-crossing ventures simply abandon any hope of qualifying for tax exemption.¹⁴²

Turning, however, to a second option, that of using a for-profit entity for the border-crossing project, also has downsides. Most notably, of course, for-profit entities cannot receive tax-deductible contributions.¹⁴³ As a result, for-profit forms impede border-crossing efforts that need to raise money for charitable activities through grants or contributions. Further, some grant-making agencies or other potential collaborators that themselves are not for-profit companies may be unwilling to work with for-profit entities.¹⁴⁴ Relatedly, some social innovators believe that the “tax-exempt” label is an essential element of their endeavor’s brand.¹⁴⁵ They think that this label produces a “halo effect” that is necessary to signal the venture’s public-benefit orientation to the public.¹⁴⁶ Additionally, unlike a tax-exempt organization itself, either the for-profit entity or its investors will be required to pay tax on any income the entity earns.

Finally, as a third option, some border-crossing ventures split themselves in two. They operate using both a for-profit and a tax-exempt entity.¹⁴⁷ These two entities then pursue the organization’s mission together. The “goals, objectives, and strategies of the nonprofit and the business are coordinated to serve mutual interests.”¹⁴⁸ When, as is common, the two entities coordinate by entering into a series of contracts with each other, some commentators refer to the resulting arrangement as a “contract hybrid” structure.¹⁴⁹

The contract hybrid presents its own set of challenges, however. For one, to make use of this option a border-crossing venture must be able to separate its activities cleanly into exempt and non-exempt categories.¹⁵⁰ Then, the venture must ensure that all of the dealings between its two components satisfy the complex rules regarding self-dealing that are part of the ban on private benefit. These “intermediate sanctions” rules constrain the behavior of tax-exempt organizations that enter into transactions with related parties.¹⁵¹ Congress originally enacted these rules because its members were suspicious of tax-exempt

142. Wexler, *supra* note 83, at 569.

143. I.R.C. § 170.

144. Wexler, *supra* note 83, at 575.

145. *Id.*

146. *Id.*

147. *Id.* at 569; *see also* Bromberger, *supra* note 17, at 49.

148. Bromberger, *supra* note 17, at 51.

149. *Id.* at 49.

150. Wexler, *supra* note 83, at 575.

151. *See* I.R.C. § 4958 (2012).

organizations with related parties.¹⁵² Specifically, Congress viewed these deals as posing a substantial risk of private inurement to the related party. Under the contract hybrid structure, the tax-exempt organization has to transact with a related entity, its for-profit component, on a regular basis. The two entities must document that they have negotiated each of these deals at arm's length and that the for-profit business compensates the exempt organization with the fair market value of anything the exempt organization provides.¹⁵³ As a result, "there are so many formalities to be observed, overhead may go up; and the structure can be complex and hard to understand, which may impair the venture's ability to attract philanthropic and private capital."¹⁵⁴

Additionally, with the contract hybrid structure, the individuals controlling the exempt entity may not benefit financially from the for-profit business. This effectively means that the board of directors and leadership of the exempt organization need to consist primarily of individuals who care enough about the venture to run the exempt entity, but are distinct from the people who will do well if the for-profit company does well.¹⁵⁵ Correspondingly, investors in the for-profit enterprise need to be comfortable pursuing a shared mission with an exempt organization they do not control.¹⁵⁶

2. How Tax Law Might Approach Border-Crossings More Realistically

The challenges that all of these potential tax structures present highlight the difficulty of fitting such ventures into a tax code set up to regard movements across sectorial boundaries with "skepticism."¹⁵⁷ As just discussed, each of the different structures imposes costs on organizations that seek to span the for-profit/nonprofit boundary. These costs arise from the overarching fact that each of the potential tax structures that accommodate border-crossings is artificial. Each one fails to recognize what happens in practice when organizations cross field-boundaries.

The first option, which posits that organizations can stay on the tax-exempt side of the border, fails because "tax-exempt" does not adequately describe border-crossing ventures. Such ventures, as described above, involve elements of private and public benefit. The

152. H.R. REP. NO. 104-506, at 55 (1996).

153. Bromberger, *supra* note 17, at 52.

154. *Id.*

155. Wexler, *supra* note 83, at 576.

156. *Id.*

157. Bromberger, *supra* note 17, at 50.

mix of the two may shift over time, depending on how the project evolves. An exempt organization is supposed to pursue public benefit. Congress and the IRS imposed legal constraints on exempt organizations specifically to make sure exempt organizations remain publicly oriented. In contrast, border-crossings may not always stay publicly oriented.

As to the second option, for-profit tax forms also fail to describe border-crossing efforts. Again, by definition, organizations crossing the for-profit/nonprofit border are not just pursuing profit. They differ fundamentally from the prototypical for-profit business. They have socially beneficial purposes in mind. They are carrying out the same types of publicly oriented activities as exempt organizations.¹⁵⁸ The for-profit forms do not deal with these key facts.

Third and lastly, the contract hybrid fails to describe border-crossing ventures. An undertaking geared toward a mixed private/public goal is by no means two separate undertakings. It is a single project with a blended mission—for instance, to identify local artisans and to sell their products. The contract hybrid expects members of such a project to pretend that this is not true. The participants have to document that they are engaging in transactions on the same terms that unrelated parties would negotiate in the absence of a common objective. Accordingly, the two component entities must choose leaders, many of whom do not, in fact, share interests. Organizations must comply with this requirement even though it is highly questionable whether individuals who have not jointly embraced an organization's dual purpose can effectively lead an organization created to serve that very purpose. Although the contract hybrid may be the easiest of the three options for many border-crossing projects to adopt, it is also a problematic fit.

But the practical problems do not end here. Rather, the border that the tax code currently imposes between for-profit and nonprofit fields delegitimizes border-crossings altogether. As Suchman and Edelman have observed, “[l]aw constructs and legitimates organizational forms . . . [and] helps to constitute the identities and capacities of organizational ‘actors.’”¹⁵⁹ Federal tax law conveys to organizations that they should be either for-profits or nonprofits. As a result, organizational undertakings that overflow these categories appear more transgressive than endeavors that are tidier. For this reason, for-profit organizations tend to adopt, as tax law dictates, a for-profit profile. Viewed in light of organizational sociology, however, tax law actually discourages for-

158. For a detailed discussion of how this is the case, see generally Malani & Posner, *supra* note 12.

159. Edelman & Suchman, *supra* note 108, at 493.

profit companies from entertaining socially beneficial projects that run counter to that profile.

To correct these interlinked practical problems, this Article proposes that, instead of holding to the fiction that organizations do not cross field boundaries, tax law should recognize that *the long-accepted boundary between for-profits and nonprofits has undergone significant change as organizations have crossed between these fields*. As discussed above, growing numbers of organizations simply no longer stay on opposite sides of an impenetrable sectorial wall.

By neglecting to acknowledge these realities of organizational behavior, tax law misses a rare and important opportunity. As a powerful legal tool, tax law might actually shape the nature of border-crossings. Not all organizational border-crossings will yield substantial public benefits, but some might. Tax law has the capacity to differentiate socially promising border-crossings from dangerous ones, creating a hospitable environment for the former and stemming the latter. I will discuss below some examples of the former.

Along these lines, Edelman and Suchman refer to the importance of “legal symbols in evoking desirable normative commitments.”¹⁶⁰ If tax law currently furnishes symbols—categories, terms, rules—that delegitimize organizational border-crossings, redesigned symbols might legitimize those boundary-crossings that are desirable. Tax law can “imbu[e] . . . roles and meanings with positive or negative moral valence.”¹⁶¹ If certain kinds of border-crossings are socially beneficial, tax law can imbue those with the positive moral valence that Edelman and Suchman describe. However, to do this, tax law must begin to loosen the borders it has maintained between organizational fields. Sociologists Elisabeth Clemens and Doug Guthrie speak of the “promise of replacing the framework of ‘the nonprofit sector’ as a distinct domain governed by its own rules and logics of appropriateness with greater attention to the role of nonprofit organizations as mediating among a variety of different actors and institutions.”¹⁶²

However, existing legal scholarship on how the federal tax code treats different kinds of organizations has not yet investigated which border-crossings might create social value and how tax law might encourage those particular border-crossings. This is likely true because, while border-crossings have been noticed in the tax literature, that

160. *Id.* at 495.

161. *Id.* at 482.

162. Elisabeth S. Clemens & Doug Guthrie, *Boundary Crossing: Contemporary Recombinations of Markets, States, and Nonprofit Organizing*, in *POLITICS AND PARTNERSHIPS: THE ROLE OF VOLUNTARY ASSOCIATIONS IN AMERICA'S POLITICAL PAST AND PRESENT*, *supra* note 8, at 205, 206.

literature is still relatively new. Most of it has actually appeared only in the past six years (in the wake of Malani and Posner's 2007 analysis of the subject).¹⁶³ For this reason, the available tax scholarship has yet to engage some of the most important questions that border-crossings raise.

Indeed, up to this point, the relevant tax literature has generally confined itself to two overlapping issues. One concerns the normative merits of border-crossings generally.¹⁶⁴ The other, more recent stream of scholarship proposes drastic reforms to the tax treatment of tax-exempt organizations so as to accommodate border-crossings.¹⁶⁵ The literature on both of these topics has made important contributions. The way tax scholars think about border-crossings has progressed substantially in just the past six years. Even so, this Article seeks further to advance the conversation about CSR, for-profit philanthropy, social enterprise, and other potential boundary-crossing ventures by suggesting that the IRS should encourage some of them.

Again, this is not the case because border-crossings are all normatively worthwhile, but because some could be. Not all border-crossings produce social good, but, as I will discuss below, some have the potential to do so. By acknowledging that border-crossings exist and regulating them as such, tax law can sort among them and become a more refined instrument with the flexibility to react to various types of border-crossing activities that occur.

IV. FACILITATING SOCIALLY BENEFICIAL BORDER-CROSSINGS THROUGH ORGANIZATIONAL COLLABORATIONS

Part IV of this Article confronts the questions that Part III raises. How might tax law come to terms with organizational border-crossings? What kinds of border-crossings should tax law encourage?

These are large questions, and my plan is for this Article to be the first in a series devoted to them. Considered abstractly, there are numerous ways that Congress and the IRS could identify organizational border-crossings that create social value and subsequently facilitate and

163. See generally Malani & Posner, *supra* note 12.

164. See generally, e.g., Galle, *Keep Charity Charitable*, *supra* note 12; Hines et al., *supra* note 7; Jenkins, *supra* note 12; Minow, *supra* note 12; Page & Katz, *supra* note 12; Pozen, *supra* note 12; Reiser, *Blended Enterprise*, *supra* note 12; Reiser, *For-Profit Philanthropy*, *supra* note 12; Doeringer, *supra* note 12.

165. See generally, e.g., Galle, *Keep Charity Charitable*, *supra* note 12; Galle, *Social Enterprise*, *supra* note 12; Henderson & Malani, *supra* note 8; Hines et al., *supra* note 7; Lang & Minnigh, *supra* note 12; Leff, *supra* note 12; Malani & Posner, *supra* note 12; Mayer & Ganahl, *supra* note 12; Reiser, *Charity Law's Essentials*, *supra* note 12; Reiser, *Theorizing Forms*, *supra* note 12; Culley & Horwitz, *supra* note 5; Fleischer, *supra* note 12.

promote them.¹⁶⁶ Tax policymakers and scholars should, accordingly, strive to bring a variety of perspectives to bear on determining how Congress and the IRS might move forward here.

In what follows, I offer one proposal. I base this proposal on the empirical findings of organizational sociology about the dynamics of inter-field border-crossings. Although not every plan for how tax law might treat border-crossings needs to build on organizational sociology, research from that area does provide a concrete basis for tax policy recommendations. Nevertheless, I want to emphasize that my recommendation is only one of many steps that Congress and the IRS could fruitfully take to make the for-profit/nonprofit border more flexible for the purposes of tax law.

My own proposal centers on what, in reference to the federal tax code, I will call cross-sector *collaborations* or alliances. Alliances between for-profit and nonprofit organizations offer one particularly promising type of structure by which to enable and support border-crossing activity. By making use of this structure, tax law would recognize and signal its willingness to legitimize organizational border-crossing practices more generally. In this sense, promoting collaborative organizational ventures furnishes an ideal place to begin this signaling process. By encouraging such collaborative undertakings, Congress and/or the IRS can harness their power to create social value. At the same time, lawmakers can facilitate and stimulate border-crossing practices that are already occurring—and already generating public benefits.

Part IV.A describes generally how cross-sector collaborations would work and the ways in which they could improve social welfare. Part IV.B considers seven concrete ways by which Congress and the IRS might loosen the for-profit/nonprofit border in order to promote such collaborations. Part IV.C anticipates and addresses objections to the argument that lawmakers should enable and encourage these partnerships.

A. *The Nature and Advantages of Cross-Border Collaborations*

By *cross-border collaboration*, I refer to a venture in which an entity that current federal tax law treats as a for-profit organization and an entity that the tax law treats as a tax-exempt organization work together toward a shared mission. Cross-border collaborations offer substantial potential for public benefit for two reasons. First, these

166. For an identification of several ways in which Congress and the IRS could accommodate such border-crossings, see Mayer & Ganahl, *supra* note 12, at 439–42.

alliances allow organizations with different resources and capacities to bring their diverse strengths together to tackle particular social problems. Second, cross-border collaborations can reorient for-profit organizations toward public purposes. The following subsections discuss these advantages and examine some specific examples of each.

1. Addressing Social Problems and Achieving Public Goals

The first major advantage of cross-border collaborations is their potential to combine diverse and disparate organizational capacities to address recognized social problems and accomplish public goals. For-profit and nonprofit organizations each have particular sets of tools at their disposal. Bringing these tool-sets together to pursue a socially oriented project allows each organizational collaborator to achieve more for the cause than either one could achieve separately.

Business-school scholars have long been cognizant of this possibility and have examined it in depth, drawing on many case studies. In his seminal study of cross-field collaborators, Harvard Business School professor James Austin foresaw¹⁶⁷ that “[t]he twenty-first century will be the *age of alliances*. In this age, collaboration between nonprofit organizations and [for-profit] corporations will grow in frequency and strategic importance.”¹⁶⁸ He explains that “these emerging strategic alliances [will] go far beyond check writing in order to leverage the competencies of each partner and create two-way value[.]”¹⁶⁹ Harvard Business School professor Rosabeth Moss Kanter echoes this view, writing:

A big new idea is emerging in America: that business models and social values provide a powerful combination. The realization is dawning that new alliances between private and social sectors can get things done that were never done before to energize businesses and transform communities.

Everywhere I look, businesses are discovering social values, and social purpose organizations are discovering business principles. And both are finding that they can create new benefits for their stakeholders by reaching out to the other. . . .

It’s about time we bridge the gap between businesses and nonprofits. For too long, they have lived in separate world. For too long, they have been viewed as opposites on so many dimensions. And for too long, American individualism, supported by a contract-oriented

167. AUSTIN, *supra* note 9.

168. *Id.* at 1.

169. *Id.* at 2.

adversarial legal system, helped erect a series of walls that made every organization a fortress unto itself. . . .

. . . .

Finding the common interests that businesses and nonprofits share is a path toward producing the common good—that is, *benefits to society*¹⁷⁰

In a similar vein, business scholars Ida Berger, Peggy Cunningham, and Minette Drumwright, who have conducted a number of case studies of what they call “social alliances,” report:

Social alliances can be designed, structured, nurtured, and maintained in a manner that will enable them both to contribute to solving pressing social problems and to fulfilling important strategic objectives for companies and nonprofits. As such, they can be important generators of value for companies, nonprofits, and society at large.¹⁷¹

Speaking more broadly, sociologists have observed that, in the current period, organizations of various types seem increasingly eager to work together. In their book on inter-organizational partnerships, Catherine Alter and Jerald Hage go so far as to claim that “cooperative behaviors—the growing number of partnerships, alliances, joint ventures, consortia, obligational and systemic networks . . . represent a stunning evolutionary change in institutional forms of governance [A] new culture is developing, the culture of cooperation.”¹⁷² Specifically focusing on alliances that span organizational fields, sociologists Joseph Galaskiewicz and Michelle Sinclair Colman write that “there has been a blurring of the boundaries across sectors and an expansion of the interface between nonprofits and business. . . . They have strategic, commercial, and political partnerships [and] . . . [t]he lines separating the sectors appear to be blurred[.]”¹⁷³

Elaborating these findings, Austin’s study of cross-border collaborations describes the multiple “synergies”¹⁷⁴ that emerge from

170. Rosabeth Moss Kanter, *Foreword* to SAGAWA & SEGAL, *supra* note 11, at xi, xii–xiv (2000) (emphasis added).

171. Ida E. Berger et al., *Social Alliances: Company/Nonprofit Collaborations*, 47 CAL. MGMT. REV. 58, 88 (2004).

172. CATHERINE ALTER & JERALD HAGE, *ORGANIZATIONS WORKING TOGETHER* 12, 17 (1993) (citation omitted).

173. Joseph Galaskiewicz & Michelle Sinclair Colman, *Collaboration Between Corporations and Nonprofit Organizations*, in *THE NONPROFIT SECTOR: A RESEARCH HANDBOOK*, *supra* note 5, at 180, 196. *See generally* Michelle Sinclair & Joseph Galaskiewicz, *Corporate-Nonprofit Partnerships: Varieties and Covariates*, 41 N.Y.L. SCH. L. REV. 1059 (1997).

174. AUSTIN, *supra* note 9, at 10.

arrangements of this kind between for-profits and nonprofits. In part, such synergies arise from the sheer gathered force that comes with a joint effort.¹⁷⁵ Austin labels these the synergies of “critical mass,” observing that some alliances seek deliberately to create a “*critical mass*—the cooperating groups . . . share a common concern about the particular problem. They come together to assemble sufficient collective confidence, knowledge, financial resources, or political power to enable them to be effective.”¹⁷⁶ Still further, there is what Austin calls this “inescapable interdependence” because “no single entity has all the inputs necessary to address an identified social need effectively.”¹⁷⁷

As to the success of such synergies in actually addressing “social need effectively,” a brief overview of a few prominent cross-sector alliances illustrates the public achievements of these kinds of collaborative efforts. In one instance, the nonprofit urban youth service corps City Year partnered with outdoor apparel company Timberland to expand City Year nationally.¹⁷⁸ In another, Pioneer Human Services, a rehabilitation nonprofit, teamed with airline manufacturer Boeing to create Pioneer Industries, a light metal and finishing factory that trains and employs recovering substance abusers and ex-offenders to manufacture products for Boeing’s use.¹⁷⁹ In yet another, The College Fund, the United States’ largest and oldest educational assistance organization for African-American students, collaborated with pharmaceutical company Merck on a science internship program that places African-American student-interns at Merck and assigns mentors to them.¹⁸⁰ A further example is that of the nonprofit low-income housing providers and for-profit developers who have successfully worked together to create low-income housing in Cleveland with the assistance of federal low-income housing tax credits.¹⁸¹ Likewise, home-supply company Home Depot joined with inner-city playground charity KaBOOM! to build a series of playgrounds in economically depressed areas around the country.¹⁸² In another instance, the American Humane Association has collaborated with pet-food producer Ralston Purina to

175. *Id.*

176. *Id.*

177. *Id.* (emphasis omitted).

178. *Id.* at 1.

179. SEGAL & SAGAWA, *supra* note 11, at 24.

180. AUSTIN, *supra* note 9, at 2.

181. See Michael McQuarrie, *Nonprofits and the Reconstruction of Urban Governance: Housing Production and Community Development in Cleveland, 1975–2005*, in *POLITICS AND PARTNERSHIPS: THE ROLE OF VOLUNTARY ASSOCIATIONS IN AMERICA’S PAST AND PRESENT*, *supra* note 8, at 237, 237–68.

182. SEGAL & SAGAWA, *supra* note 11, at 17.

create the Pets for People program, which increases adoption of homeless pets.¹⁸³

Other examples also attest to the positive social impact of alliances in the form described above as the contract hybrid.¹⁸⁴ In these cases, parties to the arrangement design their collaborating organizations with a purpose that is shared by both the nonprofit and the for-profit partnering organizations. As a result, much of what the organizations do is part of a joint endeavor, and their workings are interdependent. This collaborative structure has been at the frontier of social enterprise, and it is currently enabling the projects of some of the most innovative socially oriented entrepreneurs.¹⁸⁵

In a variant of this arrangement, one particularly impressive collaboration has involved paper company Georgia-Pacific and the environmental organization The Nature Conservancy.¹⁸⁶ This alliance was notable because these two organizations have historically stood in opposition to one another.¹⁸⁷ Before entering into their alliance, the two organizations “pursued competing agendas for common lands. The former wanted to preserve the land untouched, the latter to use it intensively.”¹⁸⁸ In 1994, however, the two organizations decided to experiment with managing together, according to a set of agreed-upon environmental commitments, a parcel of jointly owned land in North Carolina.¹⁸⁹ Each entity had a role in this alliance for jointly developing and monitoring the project and bearing associated costs. Georgia-Pacific’s role was “ownership, operation, upkeep, and maintenance of the properties, . . . and monitoring the ecosystem management plan.”¹⁹⁰ The Nature Conservancy’s role was “protecting the properties; monitoring and managing plant and animal populations, plant communities, and natural habitats; and jointly developing the ecosystem management plan.”¹⁹¹ Both organizations were committed to the ecosystem management plan, one provision of which stated:

This plan will ensure the highest level of conservation, and, if compatible, timber production. Timber harvesting is prohibited within 660 feet of the channel of any permanent stream or estuary,

183. AUSTIN, *supra* note 9, at 3. Goldie, the rescue cat who joined the author’s family this summer, did not come through Pets for People, but, to stimulate cross-sector partnerships further, maybe the next one will.

184. *See supra* Part III.C.1.

185. *See generally* Bromberger, *supra* note 17.

186. AUSTIN, *supra* note 9, at 3.

187. *Id.*

188. *Id.* at 4.

189. *Id.*

190. *Id.* at 83.

191. AUSTIN, *supra* note 9, at 83–84.

and [that] all timber will have to be removed by helicopter (the environmentally least damaging method, albeit four times more costly).¹⁹²

At first, this collaboration was challenging, because “old mind-sets and perceptions restricted, and continue[d] to restrict, realization of their relationship’s full potential.”¹⁹³ As Rob Olszewski, Georgia-Pacific’s director of environmental affairs, emphasized to Austin: “Some of the conservative foresters tend to group the environmental community together, rather than sorting through the vastly different organizations. There are still some cowboy foresters out there who feel like it’s none of anybody’s business what we do out there on the landscape.”¹⁹⁴ Nonetheless, this socially beneficial alliance has flourished. Since undertaking the North Carolina project, Georgia-Pacific and The Nature Conservancy have entered into increasingly high-stakes environmental endeavors involving larger parcels of land.¹⁹⁵ The public value that these organizational collaborations created through their first-shared effort has multiplied.

2. Changing Organizational Orientation

In addition to their capacity to achieve socially beneficial goals, cross-sector alliances offer another major advantage: they can channel for-profit organizations away from private interests and toward public ones. A close, collaborative relationship with a nonprofit partner has the power to transform the for-profit entity into one with more publicly oriented routines, cultural norms, and values, while at the same time that the for-profit entity transmits some of its own efficiency practices to the nonprofit.

As discussed in Part III.B, one of the primary processes that organizational sociology has documented is “institutional isomorphism,” i.e., the fact that organizations that are in contact tend to become more like each other over time.¹⁹⁶ Indeed, sociological research has repeatedly found that organizations that interact with each other are more likely to homogenize.¹⁹⁷ This is so, again, because the more frequently and intensely organizations interact with each other, the more their practices and values diffuse across field-boundaries.¹⁹⁸ “Socialization,”¹⁹⁹

192. *Id.* at 84.

193. *Id.* at 52.

194. *Id.*

195. *Id.* at 72.

196. DiMaggio & Powell, *supra* note 91, at 149.

197. *Id.* at 156.

198. *See* discussion *supra* Part III.B.

199. Levitt & March, *supra* note 93, at 320.

“imitation,”²⁰⁰ and common “culture building,” all of which arise from close and frequent contact, are among the primary accompaniments of isomorphism. What is more, these strong isomorphic tendencies become even more powerful when the linked organizations share a common goal. Levitt and March explain: “[p]ressure on organizations to demonstrate that they are acting on collectively valued purposes in collectively valued ways leads them to copy ideas and practices from each other.”²⁰¹

One take-away lesson of this organizational research is that when for-profits and nonprofits interact closely and frequently—as collaborations of the kind I am proposing will cause them to do— isomorphic forces will drive them to become more like each other. Collaborating organizations, particularly those with “collectively valued purposes,” are more likely to “copy ideas and practices from each other.”²⁰² Accordingly, in cross-border collaborations, for-profit organizations not only may adopt some of the nonprofit’s routines, but may also adopt over time some of the nonprofit’s foundational beliefs and values, thereby reorienting themselves more fully toward public purposes. After all, to qualify for tax exemption, nonprofits have to operate primarily for a public purpose. In this context, the more for-profits collaborate with nonprofits, the more for-profits are likely to regard themselves as operating for public purposes as well.

The business-school case studies, cited in Part IV.A.1, of existing collaborations between for-profit and nonprofit organizations attest to the power of such cross-sector alliances to alter the missions of the for-profit contributors. For example, Timberland, as its collaboration with City Year developed, “added the theme of ‘beliefs’ to the company’s prevailing themes of ‘boots’ and ‘brand.’”²⁰³ One Timberland executive told Harvard’s James Austin that “[t]his new dimension holds that the company and its employees should make a positive difference in society at large and that the corporate culture should foster involvement in confronting and solving problems within and outside the company.”²⁰⁴ Likewise, a Georgia-Pacific executive explained that, as the company’s collaboration with The Nature Conservancy evolved, “a reorientation of our mission and strategy . . . led us into a much more aggressive partnership effort.”²⁰⁵ This “reorientation” galvanized far more ambitious shared environmental projects that the two entities eventually undertook together.

200. *Id.*

201. *Id.* at 330.

202. *Id.*

203. AUSTIN, *supra* note 9, at 24.

204. *Id.*

205. *Id.* at 80 (internal quotation marks omitted).

Another revealing instance of for-profit reorientation comes from the international level. Looking at cross-sector alliances abroad, Galaskiewicz and Colman found that collaborations with nonprofit organizations caused for-profit companies working in developing countries to incorporate concern with the social problems within those countries into own their missions.²⁰⁶ Indeed, the researchers claim that the “significance of business/nonprofit collaborations is perhaps most clear in the international arena.”²⁰⁷ Here, collaborations of this kind have “begun to move beyond simple philanthropy to such concerns as sustainable development, human rights, and the quality of life within host countries.”²⁰⁸ This is so because nonprofits working with for-profits in developing countries “can strongly influence corporate behavior[,]”²⁰⁹ inspiring for-profits “to take a leadership role in solving social and environmental problems, to be transparent and reveal to others their environmental and social performance, and to live by an accepted standard of corporate social performance and accountability that does not exploit power advantages.”²¹⁰

Significantly, in all of these examples the cross-sector collaboration transforms the for-profit company’s mission rather than that of the nonprofit. To observe this is not to deny that such a collaboration may alter some of the non-profit’s practical routines or norms. Tellingly, however, the research on cross-sector collaborations has not reported any changes in the fundamental public-goal orientation of nonprofit organizations.

Organizational scholars have not speculated about why this is the case, but tax law actually provides a plausible explanation. Although markets provide powerful incentives for organizations to pursue private benefit, those organizations that have opted to eschew private benefit to the extent necessary to obtain a tax exemption are those that have already resisted a strong market pull in that direction. Thereafter, such organizations must stay publicly focused or they jeopardize their tax-exempt status. If tax-exempt organizations gravitate to private interests, they risk losing their tax exemption altogether. In this way, existing legal regulations in the United States prevent nonprofits from veering too far toward their for-profit partners. Tax law essentially bans nonprofits from allowing their cross-sector collaborations to reorient their missions

206. Galaskiewicz & Colman, *supra* note 173, at 194.

207. *Id.*

208. *Id.*

209. *Id.*

210. *Id.*; see also SOPHIA A. MUIRHEAD, CORPORATE CONTRIBUTIONS: THE VIEW FROM 50 YEARS, at 49–56 (1999).

in for-profit directions. At the same time, the isomorphic pressures of such alliances lead for-profits toward a more public reorientation.

B. Using the Federal Tax Apparatus to Enable and Encourage Cross-Border Collaborations

Assume now that congressional lawmakers and federal tax policymakers are persuaded by the advantages of collaborations between nonprofit and for-profit organizations. Given this fact, how might legislators and policymakers accomplish a loosening of the border that tax law now imposes between the two kinds of organizations by positively encouraging socially beneficial cross-sector collaborations? Part IV.B proposes seven possible methods in answer to these questions. In the subsections that follow, I list these methods in an order that runs from least to most drastic. This listing is certainly not exhaustive. Tax law is new to the business of identifying socially beneficial border-crossings, so I would suggest that the IRS experiment with doing so using one of the more flexible devices first and then, if appropriate, the federal government could proceed to one of the others.²¹¹

1. Speeches and Continuing Education

In the exempt organizations area, the IRS often relies heavily on speeches by IRS executives to communicate crucial information to members of the tax-exempt sector. For example, in recent years, the IRS officials decided that they wanted to embark on a major initiative to bring about changes in nonprofit governance practices.²¹² The IRS began this initiative by dispatching its top executives to high-profile venues to explain the IRS's newfound attention to governance. These speeches then received attention in the tax press, a major outlet that tax lawyers generally read to keep abreast of legal developments.²¹³ Likewise, the

211. In addition to proposing specific devices the federal government could use to identify and stimulate socially beneficial border-crossings, Part IV.B also raises issues about the various ways the IRS administers tax law. For a more general discussion of this issue, see generally, for example, Kristin E. Hickman, *IRB Guidance: The No Man's Land of Tax Code Interpretation*, 2009 MICH. ST. L. REV. 239; Kristin E. Hickman, *Unpacking the Force of Law*, 66 VAND. L. REV. 465 (2013).

212. See, e.g., Sarah Hall Ingram, Comm'r, Tax Exempt & Gov't Entities, Speech at Georgetown Law Center: Nonprofit Governance: The View From the IRS (June 23, 2009); Steven T. Miller, Comm'r, Tax Exempt & Gov't Entities, Speech Before the Western Conference on Tax Exempt Organizations, Loyola University: Nonprofit Governance (Nov. 20, 2008); Steven T. Miller, Comm'r, Tax Exempt & Gov't Entities, Speech at Georgetown Law Center: Nonprofit Governance and Effectiveness and Efficiency of Operations (Apr. 24, 2008).

213. See, e.g., Renato Beghe, *IRS to Ask About Internal Controls During EO Exams*, TAX NOTES TODAY, Nov. 21, 2008, available at LEXIS 2008 TNT 226-3; Steven T.

IRS posts the speeches of its executives on its website so that organizations and their lawyers can digest them more carefully.²¹⁴

Given these precedents, the IRS might use speeches by its officials to announce the agency's interest in seeing more cross-sector collaborations. IRS executives could explain that the IRS not only is open to, but actually welcomes, such alliances. Further, in their speeches, IRS staff members could explain how collaborative ventures might deal with some of the tax issues that these efforts raise, using these occasions to dispel some of the uncertainty that exists around these issues.

Along similar lines, the IRS's exempt-organizations division regularly publishes continuing professional education ("CPE") texts around topics that it deems important.²¹⁵ These texts instruct IRS agents and other staffers around the country on how to treat the tax-related practices of the organizations that the IRS regulates. While speeches tend to reach the practitioner community, CPE texts target IRS offices nationwide, and are also publicly available. The IRS could issue one or more CPE texts explaining the benefits of cross-sector collaborations and directing local IRS agents no longer to view these alliances with suspicion, and even to promote them insofar as possible.

2. IRS Forms

The IRS regularly uses tax forms to communicate relevant information to parties that must file these forms. The IRS has traditionally used the exempt organization returns for exactly this purpose. To illustrate, in 2008, the IRS overhauled Form 990 to take account of issues that the IRS had come to regard as important. As noted in the previous subsection, for instance, IRS officials had recently decided that the agency would like to encourage certain governance practices—such as conflict-of-interest policies—among tax-exempt organizations. To do this, the IRS started asking exempt organizations on Form 990 whether they have implemented these practices.²¹⁶ Including questions about governance routines on Form 990 indicated

Miller, *IRS Official Addresses EO Governance*, TAX NOTES TODAY, Apr. 24, 2008, available at LEXIS 2008 TNT 80-27; Fred Stokeld, *Exempt Organization Wrap-Up*, TAX NOTES TODAY, July 10, 2009, available at LEXIS 2009 TNT 130-4.

214. *Speeches*, INTERNAL REVENUE SERVICE, <http://1.usa.gov/1kPubmZ> (last updated Aug. 7, 2013).

215. *Exempt Organizations Continuing Professional Education Technical Instruction Program*, INTERNAL REVENUE SERVICE, <http://1.usa.gov/MscKwH> (last updated Nov. 14, 2013).

216. See generally Michael W. Peregrine, *Emphasis on Corporate Governance in Final Form 990*, 59 EXEMPT ORG. TAX REV. 139 (2008).

that the IRS valued these routines and wanted to know whether organizations were following them. The IRS administrators seem to have found that, like speeches and CPE texts, questions on IRS forms are a highly effective form of “soft regulation.”

For this reason, the IRS might incorporate form questions about cross-sector collaborations to highlight the significance of these alliances to both for-profit and nonprofit organizations. On tax forms for both kinds of organizations, the IRS could include, for instance, a question such as: “Are you currently participating in any collaborations with organizations outside your sector?” The IRS could also insert follow-up questions about the purposes and activities of the collaboration. Drawing on academic research about the features of successful inter-field projects, such questions would communicate information to all organizations about how to structure a cross-sector alliance that works effectively toward policy goals.

3. Guidance

Currently, IRS regularly issues substantial administrative “guidance.” The various types of guidance, including revenue rulings, general counsel memoranda, and private letter rulings, along with less-established formats, allow IRS officials to update the agency’s interpretation of tax law to account for new transactions or activities, especially in areas of the law that might be uncertain.

Guidance would be a firmer, more legally forceful way (than speeches and forms) for federal tax law to facilitate and encourage cross-sector collaborations. For example, the IRS could issue a revenue ruling highlighting the tax issues that such an alliance would face, addressing points of uncertainty, and indicating the agency’s intent to resolve these ambiguities in favor of the alliance’s partnering organizations. Such guidance would provide comfort to organizations whose leadership, like the Georgia-Pacific tax team,²¹⁷ seeks to avoid the tax risks of cross-sector collaborations. Guidance could also provide needed certainty to participants in contract hybrids, who are currently taking the risk of operating without any specific instructions from the IRS. The guidance would also send a broader signal to organizations, their lawyers, and IRS operatives about the IRS’s intent to accommodate and promote collaborative projects.

217. See *infra* note 236 and accompanying text.

4. Changes to Charitable-Deduction Rules

Above and beyond steps that the IRS itself might take, Congress can also legislate to enable and encourage cross-sector collaborations. The IRS could then follow the legislative activity with its own regulations.

One way Congress might accomplish this would be through changes to the charitable-deduction rules. For instance, as discussed in Part II, individuals and corporations currently face certain percentage limits on their charitable deductions—limits that might prevent for-profit partners in collaborations from deducting as charitable deductions the full amount they spend on these ventures.

To correct this problem, Congress might increase the percentage limits on charitable deductions. Congress could opt to do that generally or only for taxpayers participating in cross-sector collaborations. However, either way, these changes to the charitable-deduction rules would not have any effect on expenses that for-profit organizations incurred directly as part of shared endeavors.

5. Changes to Business-Deduction Rules

A related legislative change could affect the business-deduction framework. As discussed earlier, current federal tax law provides incentives for for-profit organizations to donate money to charitable organizations rather than to spend it directly on socially beneficial projects. Congress and the IRS could encourage cross-sector collaborations by simply removing this disparate treatment arrangement for organizations that participate in cross-border collaborations.

Congress and the IRS might accomplish this change in several ways. For instance, for-profit organizations now prefer to deduct expenses as gifts to charity in part for public-relations reasons. However, the IRS could ask for-profits to show on their tax returns what percentage of their deductible business expenses came out of a cross-sector alliance. A high figure might have the same public-relations value as a large “gift to charity” deduction.

As discussed above, another reason businesses prefer not to deduct charitable gifts under the business-deduction framework pertains to capitalization rules. If a business invests in an asset pursuant to a cross-sector collaboration, under current law the business might have to capitalize that expense rather than deduct it immediately. Congress could eliminate this possibility by allowing for-profit organizations to deduct immediately all expenses made in connection with a cross-border collaboration. Congress could allow this favorable treatment for all

collaboration-related expenses or just for the ones that serve a public purpose. In the alternative, Congress could provide a particularly generous accelerated-depreciation framework for these expenses. Business scholarship has actually provided a method for companies to value their cross-sector partnerships.²¹⁸ Such a method could, as another alternative, allow the IRS to ask companies to treat cross-sector collaborations as valuable assets subject to a particular favorable depreciation schedule.

This proposal somewhat resembles Malani and Posner's plan to permit both for-profit and nonprofit organizations to deduct amounts paid for public purposes²¹⁹—a plan that scholars have criticized on administrative grounds, saying that distinguishing between amounts paid for public purposes and for private ones would be too difficult.²²⁰ Allowing increased deductions for expenses associated with a cross-sector collaboration might raise some but not all of the same administrative issues. The IRS might have an easier time determining which expenses were made pursuant to the collaboration and which were not than the IRS would have in classifying expenses as publicly or privately oriented. Further, a cross-sector collaboration, by definition, includes a for-profit and a nonprofit partner. A tax form could ask both the nonprofit and the for-profit to list the expenses the for-profit sought to deduct. In this way, the IRS would essentially require the nonprofit to certify that the for-profit used the funds in the ways it claimed.

6. Changes to Exempt-Organization Restrictions

Some of the tax risks that cross-sector collaborations currently face arise from the various rules encumbering exempt organization behavior. For instance, as discussed, exempt organizations may hesitate to enter into shared projects with for-profits for fear of running afoul of the UBIT/joint-venture rules. Further, nonprofits may be more generally concerned that collaborating with a for-profit threatens their exempt status.

As described earlier, the IRS could assuage some of these concerns through speeches, CPE texts, forms or guidance. Congress could also address these fears by relaxing some of the restrictions on exempt-organization behavior, either in the specific context of collaborations or more generally. For example, Brakman Reiser has proposed allowing

218. See generally John T. Gourville & V. Kasturi Rangan, *Valuing the Cause Marketing Relationship*, 47 CAL. MGMT. REV. 38 (2004).

219. See generally Malani & Posner, *supra* note 12.

220. See Hines et al., *supra* note 7, at 1217.

charities to participate in more commercial activities.²²¹ Mayer and Ganahl second this recommendation, arguing that the plan would “serve to bolster the autonomy and flexibility of charities as they determine ‘how best to achieve their missions.’”²²² Congress could also loosen the private-benefit rules, again, either in the context of cross-boundary alliances alone or more generally. Lastly, Congress could reduce the number of situations in which exempt organizations can incur UBIT.²²³

7. Tax Credits

Finally, Congress could create positive tax incentives for cross-sector collaborations in the same way that Congress currently subsidizes so many favored activities: with a tax credit, potentially a refundable one. Congress could set forth the precise types of collaboration it wants to encourage, and could then allow a credit for any expenses spent as part of one of these collaborations.

A separate credit for these expenses would differ from merely expanding the charitable deduction. Unlike deductions, credits are not worth more to higher-income taxpayers. For this reason, a credit would provide the same incentive to organizations at all income levels to collaborate across sectors. Then, unlike the charitable deduction, a credit could be available for expenses that the for-profit itself incurred directly. If Congress was particularly determined to encourage cross-sector collaborations, it could even make the credit available to the nonprofit. The nonprofit could offset it against UBIT, and, in the case of a refundable credit, the nonprofit could even wind up getting a cash subsidy for activities of the collaboration. However, an additional credit would add complexity to the tax code, particularly relative to expanding a charitable deduction that already exists. On the other hand, Congress could consider converting the whole charitable deduction to a credit and, in the process, use the new legislation to stimulate cross-sector endeavors, but that plan goes beyond the scope of this discussion.

These seven mechanisms are just a few of the methods by which federal lawmakers and tax officials could encourage cross-sector collaborations. Informed by research on how border-crossing organizations actually work, members of Congress and IRS policymakers should certainly think creatively about how best to proceed in this area and may want to consider alternatives not discussed in this section.

221. See generally Reiser, *Charity Law's Essentials*, *supra* note 12.

222. Mayer & Ganahl, *supra* note 12, at 441 (quoting Reiser, *Charity Law's Essentials*, *supra* note 12, at 55).

223. *Id.*

C. *Counterarguments Considered*

The two previous subsections have described the advantages of cross-sector collaborations and some of the means that Congress and the IRS might use to promote them so as to make the for-profit/nonprofit border more flexible. Part IV.C discusses and briefly responds to ten objections that opponents of this proposal might make.

First, in regard to my contention that federal tax law should loosen the for-profit/nonprofit border, some critics might observe that tax law just has to draw some artificial lines. Organizational fields are always changing, so law necessarily has to make some distinctions among types of organizations. There is no reason, this line of thinking might continue, to be particularly concerned about the fact that the for-profit/nonprofit border is artificial. In this vein, in 2010, legal scholars James Hines, Jill Horwitz, and Austin Nichols wrote that “[c]haritable deductions are hardly the only activity governed by entity classifications. In the tax realm, business entities are taxed very differently based on whether they are partnerships, S corporations, C corporations, limited liability companies, foreign branches or foreign subsidiaries, and numerous other distinctions.”²²⁴

However, some distinctions are more artificial than others. Fields and organizations do not all change at once, but as they do, some mismatches between organizational realities and tax law will arise. If federal tax law never adjusts for the more egregious mismatches, it loses the opportunity to assume an active role in directing what organizations are doing. If law never catches up to how for-profits and nonprofits actually operate, it cannot differentiate between those organizational behaviors that are socially beneficial and those that are not, so as to encourage those border-crossings that are. In the meantime, tax law still has to devote resources to policing arbitrary lines. Interestingly, Hines, Horwitz, and Nichols bring up the example of partnerships. Before 1997, the IRS devoted substantial time to patrolling the border between C corporations and partnerships.²²⁵ However, as new state-law corporate forms, particularly LLCs, developed over time, C corporations and partnerships, which had once represented two distinct business models, started to converge in their structures and activities.²²⁶ Consequently, the IRS decided to loosen the C corporation/partnership boundary and allow most businesses to elect the category that worked best for them.²²⁷ The

224. Hines et al., *supra* note 7, at 1215.

225. See Heather M. Field, *Checking in on Check-the-Box*, 42 LOY. L.A. L. REV. 451, 492–93 (2009).

226. *Id.* at 457–63.

227. Treas. Reg. §§ 301.7701-2 to -3 (as amended by T.D. 8697, 1997-1 C.B. 215).

IRS could then focus on regulating actual LLC behaviors and stop dedicating resources to bolstering a boundary that no longer reflected actual organizational behavior. Circumstances such as these are exactly why Congress and the IRS are empowered to change the law—to update outmoded rules as conditions change.

A second argument against loosening the for-profit/nonprofit border concerns the distinctive qualities of the nonprofit sector. In her article sectorial boundaries, Martha Minow writes that “[b]lurring the borders between profit and non-profit organizations could undermine legal and political support for the non-profit sector and eliminate its distinctiveness. Loss of the non-profits would weaken civil society and democracy.”²²⁸ Other scholars have noted additional, particularly worthwhile qualities of nonprofits, which they believe that boundary-loosening could threaten.²²⁹

In responses to these claims, I argue that it is precisely because the nonprofit sector has such particularly beneficial qualities that the tax law should enable those qualities to diffuse more broadly. Infused with some of the traits that make nonprofits such a force for social good, for-profits too could work toward that end. For-profits too could provide some of the benefits to “civil society” and “democracy” that Minow touts. Encouraged to do so, for-profits can also direct some of their massive financial and human resources to social problems that desperately need such resources. Harvard and University of Michigan business school professors Joshua Margolis and James Walsh write:

The world cries out for repair. While some people in the world are well off, many more live in misery. . . . The sheer magnitude of problems, from malnutrition and HIV to illiteracy and homelessness, inspires a turn toward all available sources of aid, most notably corporations. Especially when those problems are juxtaposed to the wealth-creation capabilities of firms—or to the ills that firms may have helped to create—firms become an understandable target of appeals.²³⁰

In my view, some of this concern over the nonprofit sector’s distinctiveness relative to the for-profit sector derives from a belief that for-profit organizations will never do anything besides pursue profit. Even if they try to achieve some other goals, the organizations will

228. Minow, *supra* note 12, at 1084–85.

229. See, e.g., Galle, *Keep Charity Charitable*, *supra* note 12, at 1222–25 (noting the “warm glow” effect—that is, the good feeling that both donors and charity employees get from participating in charity); Hines et al., *supra* note 7, at 1204 (noting “moral” justifications for nonprofit organizations).

230. Joshua D. Margolis & James P. Walsh, *Misery Loves Companies: Rethinking Social Initiatives by Business*, 48 ADMIN. SCI. Q. 268, 268–70 (2003).

immediately swallow those up within the profit motive. This assertion, however, is questionable. There is a genuine debate in the business-school literature about whether for-profit companies hurt their bottom lines by engaging in social initiatives, and the jury is still out on that question.²³¹ As an empirical matter, we just do not know if public goals jeopardize profits, let alone whether businesses would try to attain increased profits even if the answer was yes.

Additionally, the fact that so many for-profit organizations have adopted social aims suggests that businesses can achieve at least some social good without substantially harming their bottom line. Insofar as many businesses may currently be neutral from a profit-making perspective as to whether they create some social benefit, tax law could nudge them toward producing that benefit.

Not only this, but viewing either for-profit or nonprofit organizations as single-purpose monoliths is also implausible. Individual actors compose both nonprofit and for-profit entities. It is generally impossible to reduce individual motivations to any one exclusive objective. Individuals, including those within for-profit and nonprofit organizations, are subject to multiple influences, many of which they do not recognize as such. These influences include institutional pressures in the direction of organizational isomorphism, along with numerous additional factors that sociology, psychology, behavioral economics, and other social sciences have brought to light. An implication of this is that even the most hard-nosed, profit-oriented executive is likely to change his or her outlook to some degree after repeated interactions with members of organizations that do not share his or her views. To the extent that tax law is structured to harness the diverse motivating factors that social scientific research has identified, tax law has particular power to create beneficial change.

A third and related objection to my proposal might come from the political left. Students of class conflict might point out that, because for-profit organizations own capital, they will always stand fundamentally opposed to nonprofit organizations that do not. Imagining that these two contrary organizational types might work together overlooks the great force of class conflict and, for that reason, is just not realistic. But three responses present themselves. One, some scholars have pointed out that nonprofits themselves are concentrations of capital. Consequently, encouraging two different capitalist sectors to work together on some

231. For a review of the literature on the relationship between corporate profits and social responsibilities, see generally Margolis & Walsh, *supra* note 230. See also Joshua D. Margolis & Hillary Anger Elfenbein, *Do Well by Doing Good? Don't Count on It*, HARV. BUS. REV., Jan. 2008, at 19–20.

project has little bearing on conflict between the capitalist class and an opposed class. Two, because, as described above, social organizations are groups of individuals rather than monolithic entities, reducing all of the inter-field dynamics among for-profits and nonprofits to one of class conflict tends to oversimplify. Three, in some ways, the proposal put forth in this Article is actually a radical one. Most commentators on the left regard the pursuit of private profit as a fundamental social evil. By reorienting private enterprise away from profit and toward public benefit, the proposal described here dilutes profit motive.

A fourth and somewhat obverse objection might emerge from the right. Galaskiewicz and Colman call attention to conservative economist Milton Friedman's admonition "that the business of business is business," noting that this perspective "was based on his understanding that corporate social responsibility puts firms in an awkward position."²³² Friedman wrote that "[i]f businessmen do have a social responsibility other than making maximum profits for stockholders, how are they to know what it is? Can self-selected private individuals decide what the social interest is?"²³³

In this case, four responses are in order. One, underlying Friedman's view is the tacit recognition that providing goods to the public at a market price does serve the most important social interest. Indeed, for-profits attempt to determine public preferences and serve them all the time. Hence, thinking about social goals may not represent as fundamental a departure for the for-profit organization as Friedman believes. Two, as a related point, organizations are not single-purpose monoliths. As the field of behavioral economics often points out, the individuals who make up for-profit organizations already think not just about how to satisfy market demand, but about how to attain a number of other objectives too. Encouraging private enterprises to pursue something other than profit is inviting them to do something they are already doing. Three, tax law already subsidizes tax-exempt organizations to enable them to identify social interests and determines how to serve them. As this Article has pointed out many times, nonprofit and for-profit organizations are increasingly becoming similar in the ways they operate. Given that tax law creates incentives for nonprofit organizations as they seek to produce social benefits, Friedman's critique offers no reason why similar tax incentives should not be available to for-profit organizations that strive toward the same objective. Four, the proposal outlined in this Article makes use of the fact that nonprofits

232. Galaskiewicz & Colman, *supra* note 173, at 193 (citing MILTON FRIEDMAN, CAPITALISM AND FREEDOM 133 (1963)).

233. *Id.* (quoting FRIEDMAN, *supra* note 232, at 133).

may be especially good at determining what is good for the public. This is among the reasons that my proposal encourages nonprofits to collaborate and to share that expertise with for-profits.

A fifth potential counterargument relates to the broader question, considered at length in the corporate law literature, of whether corporations violate their fiduciary responsibilities to shareholders by pursuing public purposes. What fiduciary duties should look like is essentially a corporate law issue, which falls outside the scope of this Article. Suffice it to say that current corporate law allows companies substantial leeway to embrace social goals.²³⁴ The law as it stands permits companies to move in some of the more publicly oriented directions toward which, as I have argued, they are already moving and which they should continue to pursue. Further, of the approximately 32 million businesses that filed tax returns in 2008, most are sole proprietorships or companies that, under current tax law, cannot have more than a limited number of shareholders.²³⁵ In those companies, shareholders who agree that the business should socially reorient itself should be able to take the organization in that direction. In fact, in a contract-hybrid situation, the entrepreneurs involved form the for-profit organization for the express purpose of working with a nonprofit. For these reasons, the dangers here are much greater in the non-closely-held context. For that reason, Congress or the IRS may in fact want to limit the extent to which non-closely-held companies may take advantage of incentives for border-crossing collaborations.

A sixth objection is that, from a practical standpoint, any effort to loosen the nonprofit/for-profit border increases the potential for abuse. That concern is exactly why I have not proposed that Congress and the IRS dismantle the framework that is already in place for eliminating abuse in the nonprofit sector. As described in Part II.A, tax law has elaborate rules aimed at preventing nonprofits from misusing public

234. See Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 763–813 (2005); Lisa M. Fairfax, *Doing Well While Doing Good: Reassessing the Scope of Directors' Fiduciary Obligations in For-Profit Corporations with Non-Shareholder Beneficiaries*, 59 WASH & LEE L. REV. 409, 430–63 (2002); Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 664–65 (2007); Judd F. Sneirson, *Green is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance*, 94 IOWA L. REV. 987, 1009–10 (2009).

235. See Table 3: *Number of Returns, Business Receipts, Net Income, and Deficit by Form for Business, Sector, Tax Year 2008*, INTERNAL REVENUE SERVICE, <http://1.usa.gov/1jWdf9t> (last visited Mar. 6, 2014) (showing data indicating that 31.6 million business filed tax returns in 2008, 22.6 million of which were sole proprietorships and 4 million of which were S corporations, which cannot have more than 100 shareholders).

subsidies. It is not clear how cross-sector collaborations raise such grave potential for abuse that the regime already in place to deal with abuse cannot do so. As with any other change to tax law, Congress and/or the IRS can design measures intended to stimulate cross-sector collaborations so that those measures also minimize abusive transactions. If problems arise, tax law is, as always, flexible enough to address them.

A seventh counterargument might raise concerns about my proposal to loosen the nonprofit/for-profit border specifically through cross-sector collaborations. In this regard, critics might claim that this proposal attempts to fix a structure that is not broken. After all, current tax law does not actually disallow cross-sector collaborations. Tax-exempt organizations can opt enter into them, as can for-profits. Presumably, for-profits can already deduct some of the expenses associated with cross-sector collaborations as charitable contributions under Section 170(a), and they can deduct the others as business expenses under Section 162(a).

However, as Part II argued in detail, federal tax law presently imposes substantial impediments to for-profit/nonprofit collaborations. To recall some important aspects of this problem, for-profit organizations can currently deduct charitable contributions only up to ten percent of taxable income. As a result, a particularly generous corporation in a cross-sector alliance now risks running afoul of those limits. Further, in most genuine partnerships, the for-profit entity itself winds up spending money directly on the project. Federal tax law does not clarify how businesses should treat socially targeted direct expenses. Members of existing collaborations have noted the tax uncertainty they face. For instance, in reference again to the Georgia-Pacific/The Nature Conservancy project, Austin observed:

[T]he Lower Roanoke River proposal, [The Nature Conservancy]'s and Georgia-Pacific's first effort at joint land management, did not receive universal support. Georgia-Pacific's law and tax departments and some managers resisted the change. "Our law and tax people like to keep everything very clean," recalled senior communications manager Lynn Klein. "They said, 'Why don't you just sell it to them or donate it, and that way it's clean and we're out of there?'" . . . "We ended up not yielding to the tax people," Klein recalled, "and the long-term benefits have been good. . . ."²³⁶

My proposal obviates these various obstacles to collaborations between for-profit and nonprofit organizations.

236. AUSTIN, *supra* note 9, at 52.

An eighth possible argument against encouraging cross-sector collaborations might claim that, in any such alliance, the for-profit organization will possess a power advantage and will use this advantage to co-opt the nonprofit. However, research on these alliances, as they have taken shape thus far, demonstrates that such co-optation has not tended to occur. In fact, in their study of cross-sector collaborations, Berger, Cunningham, and Drumwright found that, in some alliances, both parties acknowledged that the nonprofit actually wielded substantially more power.²³⁷ In other instances, the for-profit misestimated the significant power of the nonprofit at first, only to admit the mistake later.²³⁸

A ninth criticism of the cross-sector collaboration proposal is that it would not, after all, render federal tax law's nonprofit/for-profit border any more flexible; in other words, the proposal does not go far enough. Recall, however, that my proposal is meant only to provide a first step toward making the nonprofit/for-profit border less rigid. By encouraging cross-sector collaborations, Congress and the IRS would be licensing nonprofits and for-profits to embark on major joint ventures with shared goals, as well as acknowledging that social advantages can result from such collaborations. In this way, Congress and IRS tax law could set the stage for future, perhaps more radical efforts in the area of tax law. As discussed above, however, drastic change to exempt-organizations law is not now politically feasible. In contrast, the proposal advanced in the Article centers on steps that Congress or the IRS could take right now, without having to wait for major changes in the political environment.

A tenth and final criticism comes from a potential economic impact analysis. Perhaps the changes proposed here would impose greater costs on the public than the benefits they would produce. The foregoing sections of this Article suggest, however, substantial potential for social good arising from cross-border collaborations. Many of the ways that the federal government might regulate these shared endeavors are relatively low-cost. For example, a speech or a piece of guidance from the IRS is inexpensive to issue, and may spawn several major collaborations generating social good. However, as the IRS, and potentially Congress, proceed in this area, I encourage them to gather data on emerging collaborations and to stay flexible. This is one reason I would suggest that the IRS's first foray into the world of cross-border projects be one of the less drastic options. If the collaborations present unanticipated risks or costs, the IRS can then respond as they arise.

237. Berger et al., *supra* note 171, at 65.

238. *Id.*

V. CONCLUSION

The federal tax code has failed to keep pace with fundamental changes in the organizations that it regulates. Whereas in an earlier era for-profit and nonprofit organizations frequently stood on either side of a firm border between these two sectors, those organizations are currently traversing that border with increasing regularity, modifying their values and practices as they encounter each other along the way.

This change is widely acknowledged outside of tax law and tax scholarship. Research in sociology, in particular, has demonstrated that organizational sectors and the institutions within them are dynamic. Sectorial boundaries shift in ways that consequentially shape the interaction between for-profit and nonprofit organizations. Organizational isomorphism is one of the powerful forces driving this interaction across sectorial boundaries. Isomorphic pressures cause organizations from different fields and sectors to become more similar over time. This is exactly what has been happening with the nonprofit and the for-profit sectors, and the change has resulted in a growing tendency for for-profit organizations to embrace the social objectives of nonprofits.

However, federal tax law has neglected to recognize and to make beneficial use of these major organizational developments. Instead, in tax law, the for-profit/nonprofit border remains rigid. The firm boundary that tax law draws between for-profit and nonprofit organizations fails to take account of how organizations actually operate. Further, enforcing this boundary through the current provisions of the tax code seriously impedes the pursuit of joint projects between for-profits and nonprofits, which could produce substantial social benefits.

To correct these problems, tax law needs to make the for-profit/nonprofit border significantly more flexible. There are many ways to do this, but one promising means would be the facilitation and galvanization of cross-sector organizational collaborations by federal tax law. Cross-sector collaborations offer great potential to reorient the objectives of for-profit organizations and, thereby, to promote the attainment of public, rather than private, goals. Collaborations between nonprofit and for-profit organizations can harness isomorphic and other social pressures to create substantial social benefit. For this reason, tax law should loosen the nonprofit/for-profit boundary by encouraging cross-sectorial collaborations. This change to the tax law is one that Congress and the IRS could currently accomplish in several basic ways. Taken together, these measures would provide an overdue first step toward enabling federal tax law to realize the large potential for social good that lies at the ever-changing for-profit/nonprofit border.