

UCLA

UCLA Law & Economics Series

Title

Board Control of a Charity's Subsidiaries: The Saga of OpenAI

Permalink

<https://escholarship.org/uc/item/5p23j13b>

Journal

Law & Economics, 26(2)

Authors

Aprill, Ellen P.

Loui, Rose Chan

Horwitz, Jill R.

Publication Date

2024

BOARD CONTROL OF A CHARITY'S SUBSIDIARIES: THE SAGA OF OPENAI
BY

ELLEN P. APRILL

JOHN E. ANDERSON PROFESSOR EMERITA AT LMU LOYOLA LAW SCHOOL

AND

ROSE CHAN LOUI

FOUNDING EXECUTIVE DIRECTOR, LOWELL MILKEN CENTER FOR PHILANTHROPY AND NONPROFITS

AND

JILL R. HORWITZ

DAVID SANDERS PROFESSOR OF LAW AND MEDICINE

FOUNDING FACULTY DIRECTOR, LOWELL MILKEN CENTER FOR PHILANTHROPY AND NONPROFITS

Board Control of a Charity's Subsidiaries: The Saga of OpenAI

by Ellen P. Aprill, Rose Chan Loui, and Jill R. Horwitz



Ellen P. Aprill



Rose Chan Loui



Jill R. Horwitz

Ellen P. Aprill is the John E. Anderson Professor Emerita in Tax Law at LMU Loyola Law School, Rose Chan Loui is the founding executive director of the Lowell Milken Center for Philanthropy and Nonprofits at UCLA School of Law, and Jill R. Horwitz is the David Sanders Professor of Law and Medicine and the founding faculty director of the Lowell

Milken Center for Philanthropy and Nonprofits at UCLA School of Law.

In this article, the authors demonstrate how OpenAI's corporate structure was designed to protect the primacy of the nonprofit corporation's charitable purposes and tax-exempt status. They also identify the continuing need for board oversight and explain the various legal mechanisms available to protect OpenAI's charitable, tax-exempt interests.

Copyright 2024 Ellen P. Aprill,
Rose Chan Loui, and Jill R. Horwitz.
All rights reserved.

Media coverage was hard-pressed to keep up with the fast-moving drama of Sam Altman's ouster and reinstatement as CEO of OpenAI. But the focus was on the wrong actor. OpenAI is not just another tech behemoth. It is a set of entities constructed to advance the legal purposes of a nonprofit, tax-exempt charitable corporation. The nonprofit and its tax-exempt charitable purposes, rather than Altman, should have been the star of the show.

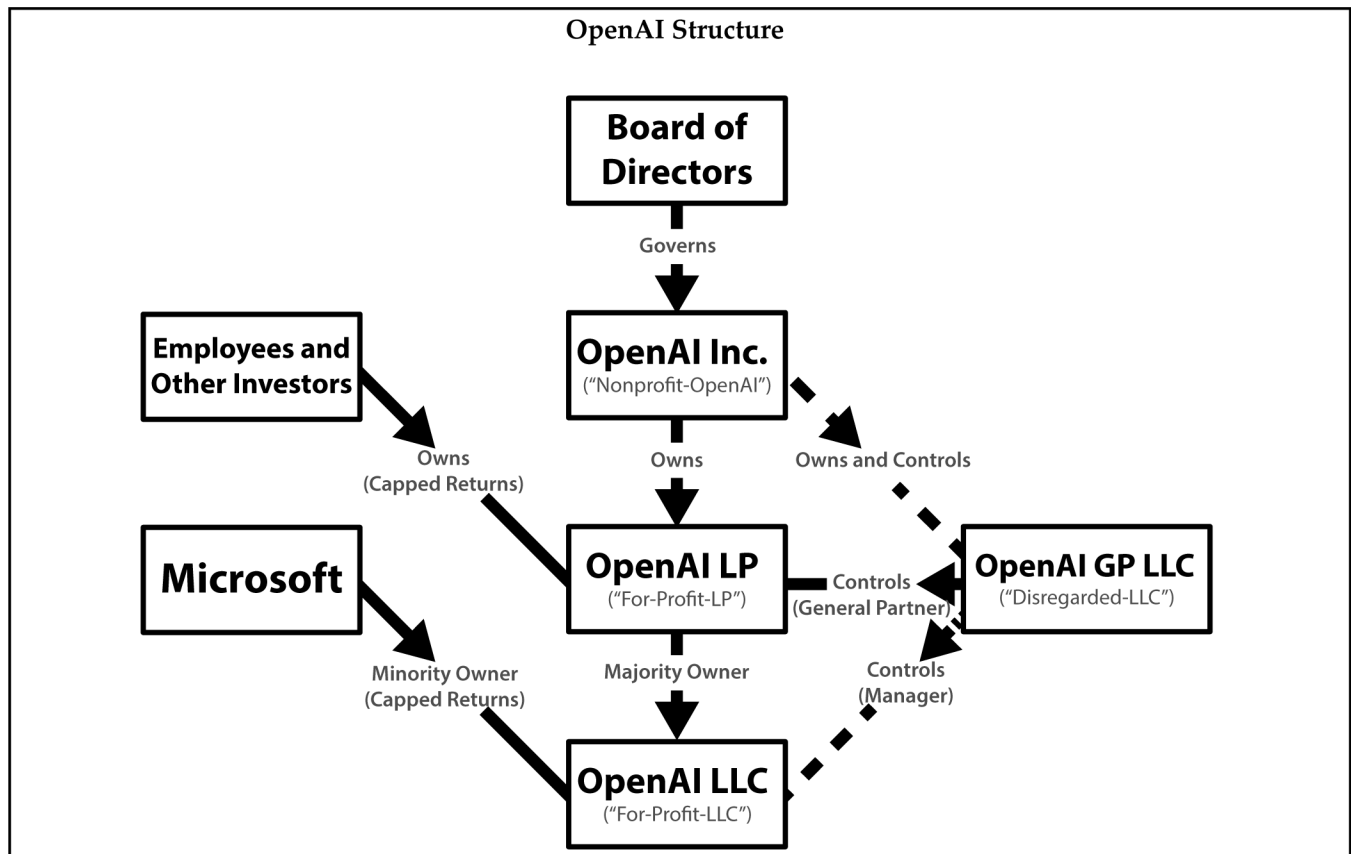
Fairly evaluating the board's decision to fire its CEO, as well as to reinstate him, requires knowing something about the collection of interlocking entities popularly known as OpenAI. OpenAI started as a tax-exempt, nonprofit company organized in Delaware (let's call that "Nonprofit-OpenAI").¹ The board later determined that charitable gifts and grants were insufficient to achieve Nonprofit-OpenAI's charitable purpose. It therefore created a structure designed to allow for private investments and, at the same time, to protect its charitable purposes. The protection of those purposes will depend on how the members of the board exercise their fiduciary duties.

Protecting Charitable Purposes

The relationships between the entities known as OpenAI were designed to ensure that charitable purposes drove the entire enterprise. (See figure.) Central to that structure is OpenAI LP, a for-profit limited partnership (let's call that "For-Profit-LP"), reportedly now worth \$80 billion to \$90 billion.² When outsiders and employees invested in For-Profit-LP, they all agreed to cap their

¹ See OpenAI's website describing the founding of Nonprofit-OpenAI in 2015. OpenAI, "Our Structure" (last accessed Dec. 20, 2023). See also the certificate of incorporation for OpenAI Inc. (2015) (on file with the California Office of the Attorney General Registry of Charitable Trusts).

² Deepa Seetharaman and Berber Jin, "OpenAI Seeks New Valuation of Up to \$90 Billion in Sale of Existing Shares," *The Wall Street Journal*, Sept. 26, 2023.



maximum financial returns.³ These caps were intended to advance nonprofit purposes — including safety and sustainability — over commerciality and profit maximization.⁴ In addition to the capping of returns to initial investors, future investors would be subject to lower caps, and any excess returns would go to

Nonprofit-OpenAI.⁵ Notably, outside investors and employees all signed a partnership agreement specifying that For-Profit-LP would be both governed by Nonprofit-OpenAI's board and operated in accordance with Nonprofit-OpenAI's charitable purposes.⁶

OpenAI also created a subsidiary of For-Profit-LP, OpenAI LLC (let's call that "For-Profit-LLC"), of which Microsoft is a minority owner

³ Greg Brockman and Ilya Sutskever, "OpenAI LP," OpenAI Blog, Mar. 11, 2019.

⁴ *Id.* Brockman and Sutskever explain: "The fundamental idea of OpenAI LP is that investors and employees can get a capped return if we succeed at our mission, which allows us to raise investment capital and attract employees with startup-like equity. But any returns beyond that amount — and if we are successful, we expect to generate orders of magnitude more value than we'd owe to people who invest in or work at OpenAI LP — are owned by the original OpenAI Nonprofit entity."

⁵ *Id.* The OpenAI website says that its employee and investor paperwork starts with big purple boxes that proclaim:

The Partnership exists to advance OpenAI Inc.'s mission of ensuring that safe artificial general intelligence is developed and benefits all of humanity. The General Partner's duty to this mission and the principles advanced in the OpenAI, Inc. Charter take precedence over any obligation to generate a profit. The Partnership may never make a profit, and the General Partner is under no obligation to do so. The General Partner is free to re-invest any or all of the Operating Entity's (or the Partnership's) cash flow into research and development activities and/or related expenses without any obligation to the Limited Partners. See Section 6.4 of the Operating Entity's Limited Partnership Agreement for additional details. *Id.*

⁶ *Id.* Brockman and Sutskever state: "OpenAI LP's primary fiduciary obligation is to advance the aims of the OpenAI Charter, and the company is controlled by OpenAI Nonprofit's board. All investors and employees sign agreements that OpenAI LP's obligation to the Charter always comes first, even at the expense of some or all of their financial stake."

and For-Profit-LP is the majority owner.⁷ Similar to the partnership agreement for For-Profit-LP, the operating agreement for For-Profit-LLC includes a conventional disclaimer warning that investing is a high-risk investment; but it also includes an unusual warning, that “the Company may never make a profit, and the Company is under no obligation to do so.”⁸ For-Profit-LLC’s operating agreement further cautions that “investors could lose their capital contribution and not see any return,” and, both less common and more dramatically, that “it would be wise to view an investment in [For-Profit-LLC] in the spirit of a donation, with the understanding that it may be difficult to know what role money will play in a post-AGI [artificial general intelligence] world.”⁹

Importantly, all these entities are controlled by the board of Nonprofit-OpenAI through its ownership and control of OpenAI GP LLC (let’s call this “Disregarded-LLC”), a disregarded entity for tax purposes and the general partner (with some ownership share that we do not know) of For-Profit-LP, as well as the manager of For-Profit-LLC.

In short, Nonprofit-OpenAI’s charitable purposes were meant to guide the whole operation.¹⁰ Those purposes, found in Nonprofit-OpenAI’s Delaware certificate of incorporation, are “to provide for research, development and distribution of technology related to artificial intelligence. The resulting technology will benefit the public and the corporation will seek to open source technology for the public when applicable.”¹¹ Other sources shed light on what those purposes mean. For example, according to both its first (2016) and its most recent publicly available (2021) Form 990, “Return of Organization Exempt From Income Tax,” Nonprofit-OpenAI’s mission is to build artificial

general intelligence that benefits humanity.¹² Nonprofit-OpenAI has made similar representations in its annual filings with the attorney general of the state of California, where it conducts much of its business.¹³

Protecting Tax Exemption

Nonprofit tax-exempt entities may create for-profit subsidiaries that can secure investment capital to scale “a business beyond what might be possible if conducted inside the nonprofit parent.”¹⁴ That is clearly the case here. At the same time, the relationships among the family of OpenAI entities appear to have been painstakingly structured to protect Nonprofit-OpenAI’s status as a nonprofit and tax-exempt charity.

As noted, For-Profit-LP was organized as a partnership with Disregarded-LLC as the general partner. According to the Forms 990 of OpenAI-Nonprofit, For-Profit-LLC elected to be treated as a corporation rather than a partnership for tax purposes.¹⁵ As a result, neither For-Profit-LP nor For-Profit-LLC is bound by the requirements of Rev. Rul. 2004-51, 2004-1 C.B. 974, regarding limited liability company joint ventures between nonprofits and for-profits. Still, as described below, Nonprofit-OpenAI followed the ruling’s guidance on how to write agreements that ensure those endeavors are consistent with a nonprofit’s charitable purposes.

Rev. Rul. 2004-51 requires that when a charity contributes a portion of its assets to and conducts a portion of its activities through an LLC treated as a partnership, the charity must establish that

⁷ OpenAI, “Our Structure,” *supra* note 1, at “Overview.”

⁸ *Id.*

⁹ *Id.*

¹⁰ *Id.* (explaining the intent of the structure: “The Nonprofit would remain central to our structure and control the development of AGI, and the for-profit would be tasked with marshaling the resources to achieve this while remaining duty-bound to pursue OpenAI’s core mission. The primacy of the mission above all is encoded in the operating agreement of the for-profit, which every investor and employee is subject to.”)

¹¹ *Id.*

¹² See ProPublica, OpenAI 2016 Form 990, Part III (last accessed Dec. 20, 2023) (“OpenAI’s goal is to advance digital intelligence in the way that is most likely to benefit humanity as a whole, unconstrained by a need to generate financial return.”). *But see* ProPublica, OpenAI 2021 Form 990 (last accessed Dec. 20, 2023) (stating the mission slightly differently: “OpenAI’s mission is to build general-purpose artificial intelligence that benefits humanity, unconstrained by a need to generate financial return.”).

¹³ See, e.g., California Office of the Attorney General Registry of Charitable Trusts, OpenAI 2016 Form RRF-1.

¹⁴ See David Avrum Levitt and Steven Richard Chiodini, “Taking Care of Business: Use of a For-Profit Subsidiary by a Nonprofit Corporation,” *Business Law Today* (June 22, 2014).

¹⁵ See, e.g., ProPublica, OpenAI 2021 Form 990, Schedule R, Part IV (last accessed Dec. 20, 2023).

the activities of the joint venture contribute to the tax-exempt nonprofit entity's exempt purposes.¹⁶ The revenue ruling described a university that is tax exempt under section 501(c)(3) and that formed an LLC with a for-profit specializing in interactive video training to develop interactive training sessions for teachers. The university's participation in the LLC represented an insubstantial part of the university's activities. (The LLC did not make an election to be treated as a corporation and thus was treated as a partnership for federal tax purposes.) The university and the for-profit each held a 50 percent ownership interest in the LLC, which was proportionate to their capital contributions. The LLC was managed by a governing board, with three directors chosen by the university and three by the for-profit.

Although the nonprofit university and the for-profit partner shared equal ownership interests and the right to pick board members, the university preserved the exclusive right to approve the curriculum, the training materials, the instructors, and the standards for successful completion of the courses in the LLC's governing documents. The governing documents also provided that all contracts and transactions would be at arm's length and fair market value. With all these safeguards, the ruling concludes that teacher training conducted by the LLC contributed importantly to the accomplishment of the university's educational purposes and that its activities were substantially related to those educational purposes. Thus, participation in the LLC did not endanger the university's exempt status or subject it to the unrelated business income tax.

Unlike the joint venture at issue in Rev. Rul. 2004-51, here For-Profit-LP is not an LLC but a limited partnership. As a limited partnership and unlike an LLC, it is governed by its general partner, Disregarded-LLC. Its status as a

disregarded entity means that it is an LLC with Nonprofit-OpenAI as its single member.¹⁷ As Nonprofit-OpenAI explains on its most recent Form 990, it maintains control of For-Profit-LP "through control of its general partner."¹⁸ There is favorable case law on this sort of arrangement. *St. David's Health Care Systems* addressed requirements when a nonprofit tax-exempt entity enters a partnership.¹⁹ In that case, St. David's had contributed all its hospital assets to a partnership with a for-profit entity. The court wrote that "if the non-profit organization enters into a partnership agreement, and retains control, we presume that the non-profit's activities via the partnership agreement primarily further exempt purpose."²⁰

Nonprofit-OpenAI did even more to ensure the advancement of the charitable purposes. Echoing Rev. Rul. 2004-51, although not required to do so, the Form 990 describes the partnership agreement as requiring the partnership "to give priority to exempt purposes over maximizing profits for the other participants, preventing the partnership from engaging in activities that would jeopardize the organization's exemption, and requiring all contracts entered into with the organization to be on terms that are at arm's length or more favorable to the organization."²¹

Neither does Rev. Rul. 2004-51 apply to For-Profit-LLC. Although formed as an LLC, it elected to be treated as a corporation, not a partnership, for tax purposes,²² and the revenue ruling applies only to LLCs treated as partnerships for tax purposes. As a corporation for tax purposes, it serves as a blocker for attribution of any unrelated income from it to Nonprofit-OpenAI through

¹⁷ OpenAI 2021 Form 990, Schedule R, *supra* note 15; reg. sections 301.7701-1 to -6. See also Ellen P. Aprill, "Section 501(c)(3) Organizations, Single Member Limited Liability Companies, and Fiduciary Duties," 52 *Real Prop. Tr. & Est. L.J.* 153 (2017); Robert R. Keatinge, "LLCs and Nonprofit Organizations — For Profits, Nonprofits and Hybrids," 52 *Suffolk U. L. Rev.* 553 (2009).

¹⁸ ProPublica, OpenAI 2021 Form 990, Schedule O (last accessed Dec. 20, 2023).

¹⁹ *St. David's Health Care Systems v. United States*, 349 F.3d 232 (5th Cir. 2003). See also *Redlands Surgical Services v. Commissioner*, 113 T.C. 47, 92-93 (1999), *aff'd*, 242 F.3d 904 (9th Cir. 2001); Rev. Rul. 98-15, 1998-1 C.B. 718.

²⁰ *St. David's Health Care Systems*, 349 F.3d at 238.

²¹ OpenAI 2021 Form 990, Schedule O, *supra* note 18 (also saying that the organization does not have a written joint venture policy with its controlled partnership).

²² See reg. section 301.7701-3; OpenAI 2021 Form 990, Schedule R, *supra* note 15. See also Heather Field, "Checking In on Check the Box," 42 *Loy. L. Rev.* 451 (2009).

¹⁶ *Id.*

Nonprofit-OpenAI's ownership interest in For-Profit-LP. (Although we do not know the exact ownership of Nonprofit-OpenAI in For-Profit-LP, the disclosure on Nonprofit-OpenAI's Form 990 that For-Profit-LLC is not a section 512(b)(13) controlled entity tells us that its interest is 50 percent or less.)

Still — and importantly — For-Profit-LLC remains an LLC for state law purposes. As a result, it can be governed through a management agreement. Disregarded-LLC, itself an LLC for state law purposes, is that manager, according to the OpenAI website, and the operating agreement includes the restraints and restrictions described above intended to ensure the primacy of the nonprofit's mission.

Thus, Nonprofit-OpenAI carefully structured its operations so that it retains ultimate control of both For-Profit-LP and For-Profit-LLC, the former by virtue of Disregarded-LLC serving as general partner and the latter by virtue of Disregarded-LLC serving as its manager. In short, Nonprofit-OpenAI put on the belt and suspenders intended to ensure that both For-Profit-LP and For-Profit-LLC would adhere to Nonprofit-OpenAI's nonprofit, charitable purposes.

Governing OpenAI

All of this demonstrates the primacy of the company's charitable purposes, under both substantive state nonprofit law and federal tax law. However, unless the members of the board fulfill their fiduciary duties, which run to the nonprofit entity in light of its charitable purposes,²³ even the most carefully thought-out structures are for naught. The board members who ousted Altman, the majority of whom were independent with no interest in OpenAI's for-profit entities, seemed to be concerned with their increasing inability to supervise the CEO, including determining whether Altman was advancing the nonprofit purposes.

In fact, from public reports, the board members who voted to fire Altman were concerned about his lack of transparency, obstructing their ability to oversee the operations

²³ See generally American Law Institute, *Restatement of the Law: Charitable Nonprofit Organizations*, section 2.02, "Duty of Loyalty," and section 2.03, "Duty of Care" (2021).

and ensure the charitable purposes were being advanced.²⁴ *The New York Times* reported that "some board members worried that Mr. Altman was too focused on expansion while they wanted to balance that growth with A.I. safety,"²⁵ an issue that goes directly to the charitable purposes.

Although former board member Helen Toner said that the board was not "motivated by a desire to slow down OpenAI's work,"²⁶ a prominent prior conflict appears to have arisen over a report she published that, in part, expressed concern about the rapid development of AI. The report described how the release of ChatGPT inadvertently created urgency among its competitors, who in response sought to accelerate or "circumvent internal safety and ethics review processes."²⁷ If this understanding of the conflict is correct, the board members, given their fiduciary duties, were acting responsibly, fulfilling those fiduciary duties by assessing whether Altman was managing the company to advance its legal purposes. It seems as if the board members who left in the wake of the drama did not think so. Regardless of whether their assessment of Altman was substantively correct, it seems as though Altman amassed so much power within the company and Silicon Valley that he was in charge and not the board.

Why have the nonprofit and tax-exempt purposes been lost in public discussion about the OpenAI debacle? Perhaps the sheer size of the dollars at stake makes it hard for observers as well as interested parties — outside investors and employees — to focus on the purposes listed in documents drafted seemingly long ago. As striking as it was that almost all of OpenAI's employees threatened to quit if Altman was not reinstated,²⁸ their protest letter may have meant

²⁴ Helen Toner (@hlntr), X, formerly known as Twitter (Nov. 29, 2023) ("To be clear: our decision was about the board's ability to effectively supervise the company, which was our role and responsibility.").

²⁵ Cade Metz, Tripp Mickle, and Mike Isaac, "Before Altman's Ouster, OpenAI's Board Was Divided and Feuding," *The New York Times*, Nov. 21, 2023.

²⁶ Toner, *supra* note 24.

²⁷ Andrew Imbrie, Owen Daniels, and Toner, "Decoding Intentions: Artificial Intelligence and Costly Signals," Center for Security and Emerging Technology, at 29 (Oct. 2023).

²⁸ Will Knight, "95 Percent of OpenAI Employees Threaten to Follow Sam Altman Out the Door," *Wired*, Nov. 28, 2023.

more if those employees did not have an interest in cashing in on the company's \$80 billion to \$90 billion valuation.²⁹ The outside investors, of course, face similar incentives. That Microsoft sprang into action and hired Altman and Greg Brockman (OpenAI's president/CEO and chief technology officer, respectively, and both board members and co-founders) so quickly after Altman was fired suggests that the company sees terrific profit potential in OpenAI's work.

Given the history, it's unclear whether the reconstituted board can or will want to advance the company's charitable purposes. The only remaining independent board member to have voted for removing Altman is Adam D'Angelo, a tech entrepreneur who made his fortune at Facebook, Quora, and similar companies. The two new independent board members, Chair Bret Taylor (a tech entrepreneur and former CEO of Salesforce) and Larry Summers (who has extensive nonprofit experience), are presumably friendlier to Altman and the employees' interests than those who left. Microsoft, which owns 49 percent of For-Profit-LLC, will have a nonvoting observer in the room when the Nonprofit-OpenAI board makes its decisions.³⁰ This new board also plans to appoint an unspecified number of additional members;³¹ their number and backgrounds could well give an indication of the priority the current and future board gives to the charitable purposes.

Overseeing a Giant

How can charitable purposes and interests be protected in the face of such strong incentives to profit? A reconstituted board could decide they want to take Nonprofit-OpenAI in a direction inconsistent with its charitable purposes and dissolve the charity, as some observers have suggested.³² They could decide to alter the charitable purposes to ease the for-profit ends.

²⁹ See Seetharaman and Jin, *supra* note 2. See also Kate Clark, Aaron Holmes, and Jon Victor, "OpenAI's \$86 Billion Share Sale in Jeopardy Following Altman Firing," *The Information*, Nov. 18, 2023.

³⁰ Alex Heath, "Microsoft Joins OpenAI's Board With Sam Altman Officially Back as CEO," *The Verge*, Nov. 29, 2023.

³¹ See Jin, Seetharaman, and Tom Dotan, "OpenAI Got Its CEO Back. What Happens Next?" *The Wall Street Journal*, Nov. 23, 2023.

³² See Jennifer Williams-Alvarez, "OpenAI's Two-Tiered Structure Is Criticized," *The Wall Street Journal*, Dec. 8, 2023.

Either way, they must do so via procedures specified in the corporate bylaws and state nonprofit law. (Because Delaware does not have a separate nonprofit corporation act, Delaware nonprofits are formed under the state business corporations act.) Those procedures typically require notice to charity regulators and require oversight to protect any charitable interests.

Regardless of which of these two paths the board chooses, the existing charitable assets remain devoted to charitable purposes.³³ Whether the laws of Delaware or another state with jurisdiction require existing assets to remain devoted to OpenAI's particular charitable purposes depends on both the state and the nature of the restrictions on those assets.³⁴ There is Delaware case law, however, that considers a charity's general charitable assets to be devoted to that charity's purposes.³⁵

Operating in parallel, federal tax law requires exempt charities in Delaware to state in their certificates of incorporation that all assets remaining after payment of debts and liabilities be distributed to another section 501(c)(3) organization or a federal, state, or local government for public purposes.³⁶ That is, the charity would need to identify another section 501(c)(3) entity willing to accept these assets to further its own nonprofit and exempt purposes. Under federal tax law, and depending on Delaware corporate law, the nonprofit could sell its current assets and distribute the sales proceeds

³³ American Law Institute, *supra* note 23, at section 3.01, "Procedures for Changing a Charity's Purposes in Its Organizational Documents and the Application of Existing Assets to New or Additional Purposes."

³⁴ *Id.* at section 3.01; section 4.01, "Restrictions on Charitable Assets"; section 4.03, "Release or Modification of a Specific Restriction on a Charitable Asset." The Delaware Supreme Court explained that "the founder of a charitable corporation makes a gift 'outright to the corporation to be used for its corporate purposes' (citation omitted)." *Oberly v. Kirby*, 592 A.2d 445, 466-467 (Del. 1991).

³⁵ "In distinguishing an 'absolute gift to be used by the corporation for one or more of its corporate purposes' to a gift technically held in trust, the Delaware court stated that in the case of the former 'the resulting duty on the part of the corporation [is] to use the property solely for its corporate purposes and not to do an *ultra vires* act. . . . The corporation is only under a duty not to divert the property to anything other than one or more of the charitable purposes for which the corporation is organized.' *Denckla v. Independence Foundation*, 193 A.2d 538, 541 (Del. 1963)." American Law Institute, *supra* note 23, at section 3.01, Reporters' Note 2.

³⁶ See reg. section 1.501(c)(3)-1(b)(4); see also Rev. Proc. 82-2, 1982-1 C.B. 367.

to another section 501(c)(3) organization, provided the sale is for FMV.

Perhaps nothing so dramatic will occur. If the nonprofit does not dissolve or change purposes, then the risk is that the continuously operating for-profit entities will work to earn profits rather than to advance the charitable purposes, such as keeping the world safe from AI. There is no easily measurable outcome here, such as whether a subsidiary for-profit must make regular distributions of net income to the nonprofit.

Still, if there is another public showdown, it may be possible to identify a violation of the charitable purposes. In that case, there are a few paths to protect those purposes.³⁷ Most directly, the Delaware office of the attorney general³⁸ could apply its authority to regulate charitable assets to ensure that Nonprofit-OpenAI retains the assets to which it is entitled and that the members of the board correctly perform their fiduciary duties.³⁹ Alternatively, the Delaware attorney general or a Delaware court could authorize a private party to bring a claim protecting the charitable interests.⁴⁰ But as in the regulation of Delaware for-profits, the state is remarkably hands-off in its regulation of nonprofits. The California attorney general may also have authority to protect the charitable assets located in California because of the extensive business OpenAI conducts there. Legal questions about the composition of the nonprofit board and other matters of internal affairs, however, belong to Delaware alone.

It may be possible for ousted board members to protect the charitable interests by bringing a

claim against the other board members in an action akin to a derivative action.⁴¹ It's unclear whether another party — besides a board member, a former board member, or a state attorney general — would have standing to bring a claim to protect the charitable interests. A Delaware court could take the rare step of authorizing another party to bring a claim if no one steps up to protect the charitable interests at stake.⁴²

Finally, at the federal level, the IRS can ensure that Nonprofit-OpenAI's interests remain devoted to a valid exempt purpose, but federal tax law is generally unconcerned about whether it is the precise exempt purpose set out in the certificate of incorporation. Although the IRS requires that an entity be operated in accordance with its stated exempt purposes, Form 990 enables the organization to notify the IRS of changes to the exempt purposes, whether or not they are the same as those at the time of its application for exemption. Moreover, as noted, OpenAI has been carefully structured to avoid several of the most common bases for revoking exemption — such as too much unrelated business taxable income or too much private benefit.⁴³

Conclusion

Whatever happens in OpenAI's next chapter, protecting the charitable interests is likely to be a heroic task in the face of those overwhelming profit-making incentives. The depleted budgets of state and federal regulators will make it hard for

³⁷ See generally American Law Institute, *supra* note 23, at Ch. 5, "Government Regulation of Charities," and Ch. 6, "Standing of Private Parties."

³⁸ *Id.* at section 5.01, "Role of the State Attorney General."

³⁹ *Id.* at section 2.02 explains: According to the Delaware Supreme Court, while the "formulation of the duty of loyalty" is a question of law, the application of the duty to any specific case is "fact dominated." *Cede & Co. v. Technicolor*, 634 A.2d 345, 360 (Del. 1993). It is a question of fact whether "an officer's or director's interest in a challenged board-approved transaction is sufficiently material to find the director to have breached his duty of loyalty and to have infected the board's decision." *Id.* at 364.

⁴⁰ *Id.* at Ch. 5-6.

⁴¹ *Id.* at section 6.02, "Standing of a Private Party to Bring an Action on Behalf of a Charity: The Derivative Action." Unlike other states, Delaware:

allows only members of a charity, and not members of a charity's board, to bring a derivative action. See DEL. CODE ANN. tit. 8, section 327 (West). . . . However, as a practical matter, the members and the directors of a Delaware nonstock corporation are often the same because the organizational documents of Delaware charities typically state that the directors shall be members; if the articles and bylaws are silent regarding membership, the members will be deemed to be those persons who elect the directors, who are commonly the incumbent directors. *Id.* at Reporters' Note 13.

⁴² *Id.* at section 6.03, "Standing of a Private Party to Enforce the Purposes to Which Charitable Assets Are Devoted and Administrative Terms Governing Charitable Assets"; section 6.04, "Standing of a Private Party to Bring or Intervene in a Cy Pres or Deviation Proceeding"; section 6.05, "Definition of a Private Party With a Special Interest for Purposes of Standing."

⁴³ See IRS, "How to Lose Your 501(c)(3) Tax Exempt Status (Without Really Trying)" (last accessed Dec. 20, 2023).

them to weigh in effectively. The tossed board members, who have remained rather tight-lipped about their reasons for leaving, likely will not have the stomachs to battle the powerful members of the reconstituted board — even if they believe the remaining board members have lost their way. And no one else may be in a legal or financial position to bring a claim. If OpenAI fails to follow the requirements of its state nonprofit and federal tax-exempt status, the risk is that For-Profit-LP and its for-profit subsidiary would subordinate the nonprofit purpose to their profit-making interests. Given the amounts likely at stake and the public interest in advancing charity, it is imperative that some authority remain alert. ■

taxnotes®

Federal | State | International



**Want to be renowned
in the tax community?**
Write for Tax Notes.

If you do, you will:

- ▶ Receive exposure in the world's leading tax publication
- ▶ Join a network of the best and brightest minds in tax

taxnotes.com/acquisitions

Your byline here.