

CHARITABLE ORGANIZATION REFORM LEGISLATION BECOMES LAW

By Jonathan Z. May

IN THIS ISSUE:

Reform Legislation	1
Q & A: Volunteer Officers	2
Fax Advertising	2
Fundraising Regulations	3
Q & A: Conflict of Interest	4
Policies	

Charitable Giving

- Rules for obtaining tax deductions for charitable contributions of easements on buildings in registered historic districts have changed to require such easements to preserve the entire exterior of the building, and to prohibit any change that is inconsistent with the historical character of the exterior.
- Clothing and household items donated to a charity must be in good 'used' condition or better for their value to be tax deductible.
- Contribution documentation for monetary donations is more important than ever. Starting in the 2007 tax year, taxpayers must document all monetary donations through bank records or written confirmation from the donee organization.
- Penalties for substantial and gross overstatements of valuations of charitable deduction property have increased.

CONTACTS

Please address all inquiries to:
 Mary Claire Chesshire, Editor
 Whiteford, Taylor & Preston, LLP
 7 St. Paul Street
 Baltimore, MD 21202
 410.347.9465
 mchesshire@wtplaw.com

CONTRIBUTORS

Eileen M. Johnson
 Kevin A. Kernan
 Jonathan Z. May

To be removed from this mailing list, please send an email to: dhill@wtplaw.com or call Diana Hill at 443.263.8290.

A number of reforms directed at charitable organizations are contained in the Pension Protection Act, signed into law on August 17, 2006. Highlights of these reforms are noted below.

- For tax years 2006 and 2007, taxpayers over the age of 70 and 1/2 may transfer up to \$100,000 from their IRAs to charities without having to include the transferred amount in gross income for Federal tax purposes.

Reporting and Access to Information

- Starting in 2007, organizations with annual incomes under \$25,000 that do not file a Form 990 will be required to annually report certain basic infor-

mation to the IRS in electronic form. This information will become publically available. Tax-exempt organizations that fail to file their reports as required for three consecutive years will be subject to automatic revocation of their tax-exempt status.

- In 2007, transfer pricing rules will be applied to determine the tax treatment of payments of interest, rents, annuities, and royalty payments made to a tax-exempt organization from affiliated for-profit organizations in which it has a controlling interest.
- Penalties on charitable organizations increased in the areas of: self-dealing and excess benefit transactions; failures to distribute income; excess business holdings; investments that jeopardize charitable purpose; and taxable expenditures (e.g., political activities).
- The IRS may now disclose to certain state officials, upon request, information to aid in the enforcement of state laws regarding charitable organizations. Such information includes: the names, addresses, and taxpayer identification numbers of organizations that have applied for 501(c)(3) status, a notice of 501(c)(3) status refusal, and a notice of proposed revocation of an organization's tax-exempt status.
- Any organization's Form 990-T (reflecting unrelated business income) is now subject to public disclosure.

Credit Counseling Organizations

- New standards and requirements are imposed on credit counseling organizations (CCOs) seeking to obtain or maintain tax-exempt status under IRC Section 501(c).
- Tax-exempt CCOs may not refuse to provide counseling services to a consumer due to the inability of the consumer to pay, the ineligibility of the consumer for debt management plan enrollment, or the unwillingness of the consumer to enroll in a debt management plan.
- CCOs must have a policy that requires any fees charged to a consumer for services to be reasonable, allows for fees to be waived if the consumer is unable to pay, and prohibits the charging of fees based on a percentage of the consumer's debt, the consumer's plan payment, or projected savings (unless permitted by applicable state law).
- A CCO's Board of Directors must be controlled by

continued on page 2

persons who represent the broad interest of the public, and not more than 20 percent of the Board's voting power may be vested in employees or people who directly or indirectly benefit from the organization's activities.

- A CCO may not solicit contributions from consumers during the initial counseling process or while the consumer is receiving services from the organization.
- If a substantial purpose of an organization is providing credit counseling services, to be tax-exempt under Section 501(c)(3), its aggregate revenues from payments by creditors of consumers of the organization's or services may not exceed a percentage of the organization's total revenues (80% for 2008, 70% for 2009, 60% for 2010 and 50% for 2011 and thereafter).

Donor Advised Funds

- Donor advised funds face tough new standards for the deductibility of charitable contributions and increased penalties for excess benefit transactions.

- New penalty taxes are imposed on sponsoring organizations related to certain distributions made from donor advised funds.

Taxable distributions from a donor advised fund will result in a 20% excise tax on supporting organizations and a 5% tax on fund management. The amount of the tax is limited to \$10,000 for any one taxable distribution.

- There are also new penalty taxes for excess benefit transactions involving donor advised funds and excess benefit holdings of donor advised funds.

- An organization must report annually on the total number of its donor advised funds, the aggregate value of assets held in such funds, and the aggregate contributions to, and grants made from, such funds.

Supporting Organizations

- Supporting organizations [tax-exempt organizations under IRS Section 501(c)(3) that are also non-private

foundations under IRS Section 509(a)(3) because they "support" another tax-exempt charity] face increased distribution requirements, increased penalties for excess benefit transactions, and new reporting requirements.

- Certain types of supporting organizations must now provide information (yet to be determined by the IRS) to each of their supported organizations to ensure that the supporting organization is responsive to the needs or demands of the organization it is supporting.
- A supporting organization is now required to list the organization it supports, indicate the type of supporting organization it is, and certify on its Form 990 that it is not controlled by disqualified persons.

Q *Are my organization's volunteer officers considered employees of my organization?*

A According to a recent federal court case, the answer is no. In that case, the court determined that a nonprofit organization's volunteer officers were not employees of the organization for purposes of the Employee Retirement Income Security Act of 1974 (ERISA). This holding applied even though volunteer officers administered the day-to-day operations of the nonprofit, and state law ruled that officers of an organization are employees. The ruling was especially significant because the organization would have been required to provide continuing health insurance coverage to terminated employees if the volunteer officers had counted as employees. Specifically, the court looked to whether the nonprofit controlled the manner in which the individuals performed their work, the location of the work, and whether the organization supplied the tools for the work. But most important to the court was the fact that the officers were not paid a salary, although they received enhanced membership benefits at no charge.

FAX ADVERTISING AND NONPROFIT ORGANIZATIONS

By Kevin A. Kernan

In April 2006, the FCC issued amended regulations to the Junk Fax Prevention Act of 2005 that expressly recognize, or codify, an "Established Business Relationship" (EBR) exemption.

The FCC regulations now allow unsolicited facsimile advertisements to be exchanged between entities or persons who enjoy an ongoing relationship formed by a voluntary two-way communication regarding products or services offered by either party. The new FCC rules require senders of facsimile advertise-

ments to provide a free "opt-out" mechanism (toll free telephone or fax number, e-mail address, or web site) on the fax that is available 24/7 to allow recipients to cease future fax transmissions. The request to end transmissions must be honored within 30 days from the date of request.

Although the Act explicitly authorized the FCC to exempt nonprofit organizations from the opt-out notice requirements for all fax advertisements sent to their mem-



bers to further their association's tax-exempt purpose, the FCC declined to do so. However, the Commission determined that non-commercial messages sent by nonprofit organizations (such as requests for a donation to a political campaign, political action committee or charitable organization) do not constitute "unsolicited advertisements," and are not covered by the facsimile advertising prohibition. But unsolicited facsimile advertisements from nonprofits that promote a commercial product or service, such as ones that solicit advertisements for member publications, are subject to the regulations.

FUNDRAISING REGULATIONS IN THE 21ST CENTURY

By Eileen M. Johnson

While most managers know that their organization must be registered to solicit charitable contributions in the state where their office is located, many do not realize that registration and reporting obligations may extend beyond state lines (e.g.: mailing solicitations to donors and members in another state, publicizing fundraising events in another state, or displaying solicitation requests on the organization's web site).

What is Regulated?

There is no national consensus on the requirements for registration, reporting, or even the terminology that is used. Generally, a professional fundraising counsel is someone who assists a charity in planning a fundraising campaign. A professional solicitor is someone who contacts prospective donors and asks them to make a donation. A professional fundraiser serves a combination of functions, from helping to plan a campaign to implementing it with paid solicitors.

It is important to understand how each state defines and regulates fundraising activity. Generally there is an initial registration application and annual reports due thereafter. States usually impose additional reporting requirements on charities that use professional fundraising counsel, professional solicitors, and/or professional fundraisers.

Exemptions from registration and reporting vary by jurisdiction. Some states exempt parent-teacher organizations, religious organizations, or those that only solicit from their members. Other states exempt any organization that raises less than a specified dollar amount, commonly \$25,000. Membership dues and fees are often

exempt by definition and not considered to be fundraising.

Managers may not realize the breadth of the charitable solicitation regulations that may impact their organization. For example, a concert or golf tournament may be considered a fundraising activity if admission is charged. The sale of products to support an organization may be considered fundraising. Raffles, sweepstakes and contests may require an additional permit or license, often issued at the local government level.

Registration and Reporting

To ease reporting burdens on organizations with multi-state fundraising activities, many states accept the Unified Registration Statement (URS). This form collects information about the organization's governance, programs, and fundraising activities, and is usually filed with a copy of the organization's Form 990 (or a financial statement if the organization is not required to file a Form 990). Additional documents required to be submitted include copies of fundraising materials or contracts with professional fundraisers or solicitors.

In D.C., charities must obtain a master business license and report biannually, and D.C. accepts the Unified Registration Statement (URS) although additional requirements exist for charities using paid solicitors. Contact the Department of Consumer and Regulatory Affairs at 202.442.4400.

In Maryland, charities must register and report annually. Maryland accepts the URS, and exempts any organization that does not employ a professional solicitor from registration, if it only solicits contributions only from its members or does not receive more than \$25,000 from the public in any one year, or only receives contributions from for-profit corporations and private foundations. Contact the Secretary of State, Charities Division at 410.974.5534.

Charities must register and report annually in Virginia. Virginia also accepts the URS although there are additional requirements for charities using paid solicitors. Charities and those who solicit charitable donations on their behalf must use required disclosures. Contact the Department of Agriculture and Consumer Services, Office of Consumer Affairs at 804.786.1343.

Disclosures

Many states require organizations soliciting contributions from their residents to provide disclosure statements to prospective donors at the point of solicitation. Organizations that solicit in multiple states with disclosure

continued on page 4

requirements will usually include all of the disclosure statements, often on a separate card inserted into a letter or at the bottom of a solicitation letter.

Fundraising and the Internet

Care should be taken in multi-state fundraising because the definitions, regulations, and exemptions are inconsistent. If an organization based in one state conducts fundraising activities on its web site or through the use of e-mail, it may be subject to regulation in other states. As a general rule, if a charitable organization has a place of business in a state and uses the Internet for fundraising, it must register for charitable solicitation activity in that state (if that state regulates fundraising). A charity may be subject to a registration requirement in a state where it does not have a physical presence if it conducts fundraising activities on its web site. Examples of fundraising activity are a general appeal on its web site for donations or the use of e-mail requesting donations directed to residents of that other state. A sale of a product or service on a charity's web site or even another party's web site might subject the charity to a charitable solicitation registration requirement if prospective purchasers are told that the charity benefits from the sale.

The disclosure statements that are required to be given to prospective donors at the point of solicitation must also be used in conjunction with Internet fundraising. Many organizations will use a generic disclosure notice on their web appeal pages and then link them to another page with the specific state disclosure notices that are required for that organization.

Special care should be exercised when conducting raffles, sweepstakes or contests on the Internet as these are

heavily regulated in some states. An organization may have to use disclaimers such as "This is not an offer to residents of XX" on their web site to avoid running afoul of other state laws.

Charities conducting fundraising activities on their web sites or through e-mail should review the laws of the other 49 states and the District of Columbia and determine if they qualify for any available exemptions or have a registration and reporting obligation in any of those states where their message is received.

Q *Does our nonprofit board of directors need a conflict of interest policy?*

A A conflict of interest policy is like insurance: you want to have it in place *before* you need it. After the past decade's corporate scandals, board members should be thinking about conflicts of interest because they protect both the organization and its board members. Possible conflict situations include: an organization contracting with a board member; a close relative of a board member being involved in a business deal with, or employed by, an organization; or a board member recommending investments or services in which the board member has an interest. Need another reason for a policy? The IRS now asks charities applying for tax exemption to provide a copy of their policy or to identify in writing their conflict procedures.

THE NONPROFIT ORGANIZATIONS GROUP

We advise and counsel nonprofit organizations on a variety of legal issues, including obtaining tax-exempt status, fundraising, private foundation and public charity status, unrelated business income issues, corporate governance, intermediate sanctions, and labor and employment issues. For more information about our Nonprofit Organizations Group, please contact Jonathan Z. May at 410.347.8781 or jmay@wtplaw.com.

Jonathan Z. May, Chair	410.347.8781
Glenn R. Bonard	202.659.6773
Mary Claire Chesshire	410.347.9465
William M. Davidow, Jr.	410.347.8767
Julianne E. Dymowski	202.659.6795
Robert D. Earle	410.347.8773
Howard R. Feldman	410.347.8793

Ann M. Garfinkle	202.659.6819
Peter D. Guattery	410.347.9431
Eileen M. Johnson	202.659.6780
Kevin A. Kernan	202.659.6818
Herman B. Rosenthal	410.347.9488
Eric A. Vendt	202.659.6814

The Nonprofit Report is a Whiteford, Taylor & Preston service to clients and other friends of the firm.

It is designed to provide general information on specific developments and issues; it is not intended to provide legal advice or opinion.

©2006 Whiteford, Taylor & Preston, LLP.