



Nonprofit Alert®

Alerting nonprofit leaders to key legal developments and responsive risk management steps.

1. Nonprofit Overview


1.1 Tithes From Bankrupt Couple Go Another Round After Supreme Court Ruling. The Supreme Court has instructed the 8th Circuit to reconsider its ruling as to whether a church can keep the tithes it received from a bankrupt couple. The 8th Circuit previously ruled that the church could keep the tithes because returning them would burden the debtor's free exercise of religion under the Religious Freedom Restoration Act (RFRA). But when the Supreme Court overturned RFRA in June, it altered the foundation of this case since the 8th Circuit relied on RFRA in making its original ruling. A court-appointed bankruptcy trustee brought suit in 1994 to recover the tithes under federal bankruptcy law, which allows a court to invalidate any transfer of assets that occurs during the year before bankruptcy if nothing was received in return for the assets. Those assets can then be used to satisfy creditors. Here, the bankruptcy trustee asked the court to recoup the couple's tithes, noting that the bankruptcy law covers charitable contributions and makes no exceptions for contributions to religious organizations. (NPA, June '96). The 8th Circuit must now reconsider the case in light of the Supreme Court's ruling overturning RFRA.

★ **The church must now show that even without RFRA, it is entitled to keep the tithes. One argument will likely be the impossible burden that all charities would face if required to conduct financial due diligence on donors before accepting their donations to avoid the risk of returning the donations later.**

1.2 Congress Passes New Relief Bill for Charitable Annuities. After more than two years of litigation, an antitrust suit filed against hundreds of charities that offer gift annuities is still pending in federal court, but the end may now be in sight now that Congress has passed legislation exempting charities from antitrust claims. The law follows similar legislation passed in 1995 that was intended to bring the antitrust suit to a close, but a federal appeals judge in Texas refused to dismiss the suit. *Ozee v. American Council on Gift Annuities*, 110 F.3d 1082 (5th Cir. 1997). Plaintiffs in the suit claim that charities issuing gift annuities conspired together in setting low rates on the annuities, triggering antitrust violations. (NPA, Dec.'95). Congress passed a 1995 law exempting charities from antitrust statutes, but the federal judge overseeing the case ruled the defendants had to prove their charitable status to qualify for the exemption. (NPA, Mar.'96). This latest measure grants immunity from antitrust suits

to all parties "involved in the planning, issuance, or payment of charitable gift annuities." It completely removes the issue of a party's charitable status.

★ **Officials with Charitable Accord, the coalition of charities defending gift annuities, hailed this latest law and said the issues that previously stalled the antitrust suit in Texas should now be a moot point.**

 **More information about charitable annuities and how they can work for your organization is available in NP9403-2, *Guidelines for Charitable Gift Annuities*. See back page to order.**


1.3 Looking to 1998: Postal Service Eyes More Rate Increases. Another postal rate increase is just around the corner if the Postal Rate Commission approves a request made last month by the Postal Service to increase nonprofit mail rates by 4.5%, plus a one-cent increase in first class mail. Nonprofits that don't use bar codes to sort their mail would be hit the hardest with their rates increasing significantly more than the projected 4.5%, but other nonprofits that use sorting techniques could see their rates decrease slightly, according to the plan.

★ **The Postal Service is requesting permission to make the increase effective sometime next year, with the earliest proposed date in May 1998.**

2. Liability & Risk Management

2.1 SEC Accuses Three Ministers in Securities Scandal. The Securities & Exchange Commission has filed charges against three ministers for swindling \$3.5 million from church members in an illegal securities scheme. The three allegedly sold bogus investments to more than 200 people in 16 states through an investment company founded by Wendell Rogers, one of the ministers. The other two ministers began selling securities after they met Rogers through the Assemblies of the Lord Jesus Christ.

★ **According to the SEC's complaint, Rogers previously served a three-year jail term for writing bad checks before starting the investment company.**

 **A simple criminal records check would likely reveal Roger's questionable past. Learn how and when to perform these checks with NP9402-1, *Minimizing Liability by Developing a Comprehensive Hiring Process*.**

2.2 Charitable Immunity Overcome By Volunteer's Suit. A volunteer's lawsuit against Habitat for Humanity is proceeding after the New Jersey Supreme Court ruled the state's charitable immunity statute afforded no protection against the claim. Lambert DeVires, a volunteer construction worker, sued Habitat after falling from a ladder while performing electrical work during construction of a Habitat home in 1992. Habitat claimed protection under the state's charitable immunity statute, but the lower courts ruled the statute only protects a charity against lawsuits by those who receive benefits from the charity. Habitat claimed DeVires was a beneficiary of the charity since one of its missions is to provide opportunities for volunteers to give their time and efforts in service to others. However, the lower courts ruled, and the court agreed, that the test is whether the injured party is *bestowing* a benefit upon the charity or *receiving* one. By the court's estimation, DeVires was clearly bestowing a benefit. His claim against Habitat now goes forward on the merits. *DeVires v. Paterson Habitat for Humanity*, 689 A.2d 142 (NJ 1997).

★ **The doctrine of charitable immunity generally forbids recovery against a charity by a beneficiary of that charity, but many court rulings like this one have gradually eroded the doctrine in recent years.**

2.3 Catholic Diocese Ordered to Pay \$1.2 Million Judgement.

A Dallas court has imposed what is, to date, the largest judgement ever against the Catholic Church in a sexual abuse case. After a jury trial last month, the court awarded \$1.2 million in damages to 10 former alter boys and the parents of another boy who committed suicide. The boys were allegedly abused by a Roman Catholic priest hundreds of times over an 11 year period. The jury held the diocese liable because it ignored warnings about the priest and even covered up evidence in the case.

★ **The diocese bore more responsibility than the priest, the jury ruled, because it committed gross negligence, malice, conspiracy and fraud in failing to take corrective action against the priest when complaints were first lodged.**

3. Employees & Volunteers

3.1 Job Seekers Lie to Land a Job, Survey Shows. More than 95% of college graduates entering the job market in 1997 say they are willing to tell at least one lie to get a job, reports a study by Reid Psychological Systems, a Chicago company that conducts annual surveys and tracks job market trends. Forty-one percent of survey respondents admitted they had already lied when applying for a job. The majority of false statements occur in areas that are hard for employers to verify, such as personality and competence.

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Less likely areas for falsification were verifiable facts, such as past salary and work experience. (See related story at ¶8.1 below).

★ **The traits most often exaggerated or falsified are: (1) involvement in school activities; (2) title of past job positions; (3) previous employer's comments/evaluations; (4) computer skills; and (5) willingness to assume new duties.**



Helpful screening techniques to use when considering new job applicants are available in NP9101-1, *Minimizing Liability for Negligent Hiring*

3.2 Ashcroft Bill Protects Against Volunteer Liabilities.

Following on the heels of the Volunteer Protection Act signed into law in June (NPA, June '97), Sen. John Ashcroft (R-MO) has introduced the Liability Reform for Volunteer Services Act, which would provide additional protection to nonprofits that use volunteers. The bill would change the standard of proof needed to show liability from "clear and convincing evidence" to the more difficult standard of a "preponderance of the evidence." The bill would also cap punitive damages against nonprofits at \$250,000 or two times the loss, and it would hold nonprofits liable only for damages that are directly proportionate to their degree of fault.



Concerned about your own volunteer program? Get tips for reducing the risk of liability with NP9301-1, *A Prudent Volunteer Program for Nonprofits*. See back page to order.

4. Tax-Exempt Issues

4.1 Presidential Campaign on Internet Fictional, Not Political.

A private foundation that sponsored a simulated political campaign on the Internet did not endanger its exempt status by engaging in prohibited political activity, the IRS has ruled. The campaign was purely fictional, based on a computer simulation designed by a software developer for the private foundation to use in stimulating issue awareness in the context of a hypothetical presidential election. No part of the fictional campaign advocated any political position, and the foundation remained strictly nonpartisan. The IRS ruled the activity was "educational" and well within the foundation's exempt purpose. Furthermore, the IRS ruled that revenue the foundation received from licensing fees paid by the commercial company that provided access to the Internet campaign did not result in taxable unrelated business income, since it was substantially related to the foundation's exempt purpose. IRS LTR 9723046.

★ **Nonprofits are prohibited from partisan political activity on the Internet or anywhere else, but the issue-oriented, fictional nature of the political campaign in this case helped demonstrate its educational merit.**



If the lines between permissible and prohibited political activity seem blurry, read NP9101-3, *Nonprofit Lobbying and Political Activity—Know Your Limits*. See back page to order.

4.2 Retail Value Offers Best Assessment of Donations. What's an old poster from a James Bond film worth these days?

Enough to trigger a dispute with the IRS if you happen to overstate its value, as Gerald and Catherine Leibowitz discovered. The Leibowitzs donated hundreds of old movie posters and other memorabilia to the American Museum of Moving Image in 1985. The Leibowitzs then claimed a charitable deduction of \$188,085, but the IRS said that amount was grossly overvalued. The case ended up before the Tax Court, where both sides produced experts who gave radically varying valuations. Recognizing that the valuation of such unique collectibles was an inexact science, the court said the more accurate value should be based on fair market data and other factors such as the “mint” condition of the collection. Making its own valuation, the court priced the collection at \$50,412. The court relieved the Leibowitzs of penalties, however, after they presented compelling evidence of their good faith in relying on expert assessors and tax preparers when they initially made the claim. *Leibowitz v. Commissioner of Internal Revenue*, T.C. Memo 1997-243, 73 TCM 2858.

5. Federal Rules & Regulations

5.1 IRS Considers Raising Threshold for Filing Form 990s.

With few exceptions, nonprofits must file informational tax returns, known as Form 990s, if they normally collect more than \$25,000 in annual receipts. But a plan under consideration by the IRS would raise that threshold to \$40,000. The \$25,000 cut-off has not been adjusted for

inflation since 1982. Officials estimate up to 60,000 organizations would be relieved of filing if the threshold changes.

★ **Some practitioners oppose the change because they claim it is only motivated by the IRS’s desire to save money, and in so doing, would weaken the accuracy of the IRS’s charity data base that many states and consumer organizations use.**

5.2 Appreciated Gifts Deduction Survives Pending Tax Bills.

Tax legislation currently under consideration by a House-Senate Conference Committee includes a provision that extends the deadline for deducting gifts of appreciated, publicly-traded stock to private foundations. The deduction previously expired on May 31, pursuant to a provision in the Small Business Job Protection Act, passed last year. (*NPA*, Sept. '96). But advocates pushed the measure into new tax legislation, which now has an excellent chance of becoming law.

★ **If passed, the bill would extend the deduction provided under §170(e)(5) of the tax code to the end of 1998 or 1999, depending on which year conference members eventually agree upon. This would allow donors to make gifts of appreciated stock to private foundations and claim deductions for the full appreciated amounts up until the new deadline.**



For further explanation on the treatment of appreciated property donations, see NP9109-6, *Gifts of Property*. See back page to order.

NPA Highlight of the Month

States Turn to Religious Nonprofits for Welfare Help

With federal welfare funds drying up, states have turned to nonprofits in recent years to take up the slack. What they found were excellent programs offered by religious-based nonprofits, but the constitutional separation between church and state prevented much government involvement. Now, states are slowly amending their laws to allow more flexibility. Two measures, recently signed by Texas Gov. George Bush, make it easier for religious nonprofits to help the state’s poor without violating prohibitions against mixing religious teaching with social services. Under one law, religious child care providers may receive accreditation from private organizations other than the state. A second law exempts drug and alcohol treatment centers, run by religious organizations, from state registration requirements. The exemption only covers counseling and support services, not medical care. Texas has also issued a resolution encouraging voluntary religious programs in the state’s prison system. Prison Fellowship, a national Christian ministry, has responded and is providing the model for a pre-release program. Michigan has taken a more novel approach by approving “welfare mentors” from faith-based organizations who counsel welfare recipients as they attempt to move off the public dole. The state compensates religious groups for providing mentors, but the mentors must have a “non-judgmental attitude.” They may encourage participants to attend Bible classes or church functions, however, without violating state laws.

★ **Officials in both states say the efforts are aimed at deregulating religious organizations in the hopes they will expand social services programs that help people move off welfare and reduce the states’ costly social burdens. Last year’s overhaul of the federal welfare program paved the way with a provision guaranteeing religious groups the right to compete for state welfare contracts without foregoing their religious practices or beliefs. Gammon & Grange explains how to take advantage of that new federal law in NP9702-1, *Charitable Choice— Availability of Government Funding to Religious Social Service Providers*.**

6. State Rules & Regulations

6.1 Minnesota Debates Tax Credit for Serving Poor. The state legislature is debating a measure that would grant taxpayers a state income tax credit up to \$125 for charitable contributions to organizations that serve the poor. To qualify, contributions must be made to groups that “primarily benefit persons whose household incomes are below the federal poverty line.”

6.2 North Carolina Legislation Would Increase Giving. Two bills before the North Carolina legislature gained wide support among the state’s nonprofits after studies showed passage of the measures would significantly increase private giving. The North Carolina Center for Nonprofits produced statistics showing that a 4.25% increase in the state tax credit for charitable contributions by non-itemizers would boost private contributions by \$109 million. State law currently allows non-itemizers a 2.75% credit.

7. Gifts & Fund Raising

7.1 Donor’s Estate Claims Deduction for Charitable Pledge. A donor named “Martin” signed an agreement with a state university foundation, pledging \$250,000 later than December 31, 1999. Two years later, Martin died without making any payments. The university then filed a claim, and Martin’s estate agreed to pay the entire pledge, but it first sought assurance from the IRS that the payment would be deductible. Claims against an estate are payable only if the decedent was obligated on them at the time of death; they are deductible only if they can be enforced against the estate. State law dictated that charitable pledges become claims enforceable against an estate only if the pledge agreement stated the specific purpose for which the pledge was to be used, and if the charity actually relied on the pledge. Here, the university proved to the IRS that the pledge agreement specified the funds were for constructing a new building. The

university also relied on the pledge, since it began construction shortly after the agreement was signed and applied for state matching funds based partly on the pledge. IRS LTR 9718031.

★ **A charitable pledge is a mere promise to make a future gift—which is something entirely different from making a deferred gift.**

8. Executive Items of Interest

8.1 Quote of the Month. “THE COMPETITIVE NATURE OF TODAY’S JOB MARKET PUTS A REMARKABLE AMOUNT OF PRESSURE ON GRADUATES TO DEVISE STRATEGIES THAT INCLUDE EMBELLISHING THE TRUTH...MANAGERS NEED TO INCORPORATE STRICTER PRE-EMPLOYMENT SCREENING METHODS TO AVOID HIRING SOMEONE WHO MAY END UP COSTING THEM IN THE FUTURE ...”— Stephen Coffman, President, Reid Psychological Systems, a recruitment company that conducts annual surveys of entry-level job seekers. (See related story at ¶3.1 above).

8.2 Government Consolidates Nonprofit Info on Web Site. A new web site created by the White House Office of Public Liaison offers a central location for nonprofits to collect



The web address for the site is: www.nonprofit.gov. This is one you’ll want to bookmark!

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