



# Nonprofit *Alert*®

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

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Rebates That Yield Deductions

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## ➤ Ministerial Exception Inapplicable;

### Clergy Harassment Case Upheld

Courts typically dismiss harassment and discrimination lawsuits filed by clergy against churches because any court involvement in a church's internal affairs would constitute government entanglement. But a three-judge panel of the 9th Circuit now says religious organizations are subject to the same harassment laws as all other entities when sued by their leaders.

The case involves \$1-million in damages claimed by a former Jesuit seminarian (called a "novice" in the Jesuit order) who alleges his superiors sent him pornographic material, made unwelcome sexual advances, and conducted inappropriate sexual discussions for six years.

The novice complained but saw no corrections. As a result, he claims he was forced to leave before becoming a priest.

A lower court dismissed his case, citing the ministerial exception, but the 9th Circuit said it didn't apply. Since the Jesuit order "doctrinally disavows the harassment, the danger that the application of Title VII in this case will interfere with religious faith or doctrine is particularly low," the court concluded.

➤ **This case represents a growing trend among courts that allow prevailing public policy to trump religious activity, especially if the objectionable activity can be shown to have little or no nexus with religious beliefs.**

### Donor's Racist Will Leaves \$28 Million in Limbo

A Baltimore nursing home has put \$28-million at stake over an unusual but highly controversial discrimination clause in a donor's will. The Keswick Multi-Care Center refused to honor a stipulation in Dr. Jesse C. Coggins will that would have required the nursing home to restrict care only to white patients.

Coggins' 1962 will named the nursing home as the beneficiary of his trust upon the death of his heirs. The last of Coggins' heirs died in 1998, leaving the trust at nearly \$30-million. The nursing home board considered the discrimination clause illegal and refused to honor it, but a Baltimore Circuit Court judge ruled they had to follow the donor's intentions or lose the trust altogether. The will names the University of Maryland Medical System as a

secondary beneficiary if the nursing home cannot accept the terms of the trust, but it doesn't place any stipulations on the university.

The nursing home is appealing the ruling. Managing deferred giving issues like this is challenging because a nonprofit is often unaware of the donor's will or other deferred gift until after the donor's death, when revision is too late.

➤ **To lessen risks, planned giving staff should routinely ask for file copies of wills when they learn their charity is a beneficiary. Retain counsel to review all wills received and identify any problems while correction is still possible. Always encourage donors to use their own counsel in preparing charitable trusts and estate documents.**

### \$\$\$+\$+\$ Per Diem Rates Rise \$\$\$+\$+\$

Federal per diem rates increased on January 1 for "high-cost" areas from \$185 per day to \$201. Rates for all other areas increased from \$115 to \$124 per day. Several areas were added to the "high-cost" list, including Silverthorne/Keystone, CO, Prince George's County, MD, Loudoun County, VA, and Big Sky, MT. Nonprofits often use these rates to reimburse employee travel, reducing detailed expense documentation. See details in **Nonprofit Alert**® Memo 9103-3, *Expense Reimbursement for Volunteers and Employees*.

## Liability & Risk Management

### *Greenpeace Board Reaction: Not So Peaceful*

The entire board of the environmental activist group, Greenpeace USA, has resigned when differences between management philosophies couldn't be reconciled. For over a year, the board debated the direction the organization should pursue. Finally, in December, all the board members turned in their resignations, leaving the organization to elect new directors later this year. Just two years ago, the organization closed 11 regional offices and laid off more than three-fourths of its staff. The executive director insists the mass resignations "are not a sign of drift in Greenpeace's mission," citing a number of recent achievements including balancing its \$20-million budget for the first time in five years and hiring on several new staff members. She says the organization now has some 300,000 members nationwide. Its parent organization, Greenpeace International, has about 2.4 million members and operates an annual budget of \$100-million.

➔ **Nonprofit Alert® Memo 9107-1, *Responsible Governance by Nonprofit Board Members*, contains helpful tips for keeping your board working well together. Why not provide copies for all your board members? Ordering instructions are on the back page. Call for discounts on five or more copies.**

### *Brochure Promise Could Create Premises Liability*

Two men died of hypothermia when their boat capsized in the freezing waters of Unity Lake, a secluded lake in Missouri, owned by a private religious school. One man was an employee at the school, and the other man was his guest. Both men had been fishing. An investigation determined their boat capsized because it was overloaded. School policy permitted employees and their guests to fish on the lake, but employees had to sign a waiver indicating they did so at their own risk. The appropriate waiver had been signed in this case. Nevertheless, family members sued the school, claiming it was negligent in providing security at the lake. They pointed to a brochure published by the school, which emphasized the availability of 24-hour building and grounds security. The brochure also stated that a dispatch team was "ready to respond to any emergency 24-hours a day." Based on the brochure statements, the family claimed the school owed the men a duty. The court rejected their argument,

however, finding that the brochure created a promise only if there was reliance on it. Since there was no evidence the men even knew the brochure existed, there could be no promise, the court said. *Green v. Unity School of Christianity*, 991 S.W. 2d 201 (1999).

➔ **Note how the school could have been found liable if only a few facts had been different in this case. Have you conducted a risk management review of your promotional literature and web site that could detect the potential for these risks?**

## Employees & Volunteers

### *Have Car, Will Travel for FLSA Overtime Comp*

The Fair Labor Standards Act does not require overtime pay to compensate employees for their travel to and from work, even when the time spent is significant, so long as the commute is "normal travel." What's normal is another matter, however, as a refrigerator mechanic discovered when he tried to claim overtime for the long hours spent driving between his home and the Grand Union grocery stores where he performed services. The mechanic had no fixed work location. Grand Union issued his work assignments by telephone each morning, requiring him to be at an assigned site in Connecticut or New York no later than 8 a.m. Grand Union paid him for time spent traveling between sites during the day but did not compensate the additional travel before or after his first and last assignments of the day. The mechanic claimed he traveled an average of seven to eight hours per day, but was only partially compensated for those hours. He filed suit under the FLSA seeking overtime wages, but the lower court sided with Grand Union, and the Second Circuit affirmed. The court based its decision on a provision of the Portal-to-Portal Act, which specifically provides that normal travel is not compensable under the FLSA unless there is either (1) a written contract stating that such travel is covered, or (2) a custom or practice in effect at the place of employment, which covers such travel. Grand Union had neither a contract nor a practice of covering such travel. The court noted the unfairness of the situation, but could not offer a remedy under the law. *Kavanagh v. Grand Union Co., Inc.*, 1999 WL 760202 (2nd Cir 1999).

➔ **Assess your organization's compliance with the FLSA rules on employee travel and overtime. Order Nonprofit Alert® Memo 9208-1, *Nonprofit Employers & the Fair Labor Standards Act* for help. See back page to order.**

### *Womens Health Act Requires New Notice of Surgery*

A new law, which passed in 1998 and took effect last year, now requires employers with group health plans to notify employees that their plans will pay for reconstructive surgery if they also cover mastectomies. Mandated by the Women's Health and Cancer Rights Act, the notice requirements apply to both employers and insurers, but notice need only be given by one party. If the insurer provides the notice, for example, then the

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employer is relieved of the duty. Notice must be provided in writing upon enrollment in a health plan and every year thereafter.

 **The Department of Labor offers sample notice provisions and additional information at its web site, <http://www.dol.gov/dol/pwba>.**

## Tax-Exempt Issues

### ***Beyond Books: Library Fees Don't Threaten Status***

A nonprofit, §501(c)(3) library may keep its tax exemption despite offering additional services that go beyond its traditional mission. The reason: all the additional services are “by-products” of the library’s exempt activities, the IRS said. The library maintains one of the largest and oldest collections of business-related resources in the U.S. To enhance public accessibility, the library proposed offering the collection electronically via a remotely accessible “virtual interactive library.” The library also planned to offer fee-based searching, reference, and educational training services related to the collection. Because all these activities furthered the library’s purpose, the IRS ruled that its tax-exemption was not in jeopardy, and no unrelated business income (UBI) would result. The IRS was careful to point out, however, that if the library staff provided assistance beyond those activities described, resulting in “the actual development of business plans” and/or “the making of business judgments” for its customers, then UBI would apply. But even such UBI would not jeopardize the library’s exempt status unless the scope of the activity became large in relation to its other exempt activities, the

IRS concluded. IRS LTR 199945062.

**This ruling is a good example of how far a nonprofit can go in providing products or services before UBI becomes a problem. Even after UBI arises, a nonprofit can still function relatively free of worries about its exempt status, so long as the UBI-producing activity remains proportionately insubstantial to its overall charitable programs. For details, refer to Nonprofit Alert® Memo 9110-1, *UBI Primer for Nonprofits*.**

### ***Disclosure Requirements Encompass Foundations***

The IRS released final regulations last month that outline public disclosure requirements for private foundations. The regulations are virtually the same as the disclosure rules that cover public charities, but because the original law did not mention foundations, a separate law was passed last year, extending the coverage to some 48,000 private foundations in the United States. Foundations must provide copies of their three most recent tax returns and their initial application for exemption upon request. They may charge a “reasonable fee” for copying or avoid the copying burden altogether by making the documents “widely available” through the Internet.

 **The disclosure requirements for private foundations become effective March 13. Review the specifics of disclosure requirements for all exempt organizations in Nonprofit Alert® Memo 9904-1, *Nonprofit Disclosure Rules*. See back page to order.**

### ***One to Another: Gift Makes Lease Income Possible***

## ***NPA Highlight of the Month***

### **Rebate Helps Charity . . . and Yields Deduction**

The IRS has ruled that a coupon rebate program, offered by a manufacturer upon the purchase of certain items, will actually produce a charitable tax deduction for the participants in the program when they donate their rebates to charity. Participants receive a card when enrolling in the program. At that time, they designate whether they want to redeem the face value of the coupons for cash, which they keep, or whether they want all or a portion of the rebate to go to charity. Participants may change their rebate designation at any time. The manufacturer petitioned the IRS to rule whether participants could claim a charitable tax deduction for the rebate amounts that they donate to charity. Distinguishing this situation from other leading cases where a deduction had been denied, the IRS said participants in this program could claim deductions if they designate 100% of their rebates to charity. In other cases, participants in similar programs did not have the option of claiming the rebates for themselves. Instead, rebates automatically went to charity. Here, the payments are voluntary, since participants have the opportunity to collect the payments themselves or designate them for charity. Because of this feature, the IRS ruled the payments were deductible. IRS LTR 199939021.

 **To claim deductions, participants must substantiate their donations, of course. The manufacturer simplified this task by providing the donee charity with an accounting of each participant’s rebates. Then, the charity simply issued the required substantiation documents to participants. Stay current on substantiation rules with Nonprofit Alert® Memo 9505-1, *Demystifying the Receipting of Charitable Gifts*. See back page to order your copy.**

In a recent Letter Ruling, the IRS reiterated the basic rules for determining when taxes will apply to lease income earned by a charity. An exempt fraternal lodge proposed to transfer a piece of real estate and an undisclosed amount of cash to a charity that provided testing for learning disabilities in children. The cash was to help pay for constructing a building on the donated real estate in which the charity would conduct its mission. At least two-thirds of the building would be used by the charity, with the remainder of the space leased to the fraternal lodge or other nonprofit and/or for-profit entities at the going market value to be determined by an independent appraisal. The charity did not intend to incur any debt in erecting the building. Any building costs not covered by the fraternal lodge's cash donation would be raised from public donations. The IRS ruled that income from the lease of extra space in the building would not produce a tax liability because the charity would own the building debt-free and would use it primarily for exempt purposes. IRS LTR 199940034.

## State Rules & Regs

### Arizona: Land of Plentiful Charitable Giving

A new survey released by the Arizona Community Foundation indicates that Arizona households give an average of \$1,539 yearly to charity, more than double the national average of \$753. Three out of every four Arizona citizens donate to charity, surpassing the national average of 70.1 percent, as calculated by the charity coalition Independent Sector. The Arizona study analyzed trends for 1998, the most recent year for which statistics were available.

### California Changes Overtime Laws for Employers

Effective January 1, 2000, overtime in California begins after working eight hours in a day, rather than the more common practice of counting 40 hours in a work week. Sick leave rules have also changed, requiring employers to grant employees up to half their earned sick leave to care for sick family members.

 Several details and limitations apply. Check out the complete explanation at the California Chamber of Commerce's web site, <http://www.calchamber.com>.

### Ohio Unveils Trust Fund Law With More Options

A new state law, called the Institutional Trust Funds Act, widens investment options for trust funds maintained by third-party trustees on behalf of Ohio nonprofit organizations. The law allows trustees, like banks and financial institutions, to pay income to a trust's charitable beneficiaries based on appreciation of the trust's total assets, not just interest and dividends. Experts predict trustees will be more inclined under the new law to invest trust assets in stocks and other growth vehicles, whereas the old law favored conservative investments, like bonds and funds with guaranteed returns. The law covers only charitable trusts held by third-party trustees. Trusts held by charities themselves already enjoy many investment options.

 However, the law does not relieve the requirement that third-party charitable trusts may pay out only a percentage of the trust's total assets. Check with legal counsel for additional details.

### Tennessee Looks Past Exempt History to Impose Tax

The Tennessee Board of Equalization has levied a hefty tax lien against 13 YMCA fitness facilities, finding they operated merely to benefit their members, not for any charitable purpose that entitled them to tax exemption. The Board dismissed the YMCA's arguments about its long charitable history and even disregarded the YMCA's federal tax-exempt status, saying those aspects of the operation did not alter its primary purpose as a "secular membership organization" that "furnish[es] facilities and equipment to its members for exercise, recreation, and other physical fitness."

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