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Nonprofit *Alert*®

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

Inside This Issue of NPA

President's Budget Plan Holds Promise

There's good news and bad news for nonprofits in the budget plan that President Bush unveiled before Congress last month. Overall, the plan provides more federal dollars for nonprofits than had been expected, given the increased spending required for the nation's ongoing antiterrorism efforts and potential war against Iraq. But some social service dollars would be cut in an attempt to eliminate wasteful programs.

The Losers

Federal money earmarked to prevent domestic violence would be eliminated. Money to certain child abuse programs would also be cut because the Justice Department has consolidated projects aimed at helping battered women and children. The consolidations are intended to make these programs operate more efficiently.

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Funds for public housing and rent subsidies would also be reduced. However, the budget calls for increased funding to homeless programs and "sweat-equity" programs like Habitat for Humanity that help low-income families build their own homes.

The Winners

Volunteer and mentor training programs would get a significant boost with an additional $100 million for training and recruiting, plus an additional $50 million for mentoring programs designed for children with an incarcerated parent.

$200 million is directed toward existing programs that offer vouchers for substance abuse victims to use at treatment programs of their choice. The vouchers are good at any treatment center that meets certain federal guidelines, including treatment centers operated by religious institutions.

Education programs would receive several new funding sources, including $25 million for history programs and $47 million to upgrade technology resources at museums and libraries.

Focus on Giving

The President's plan also proposes a change in the tax laws that would allow taxpayers who do not itemize on their tax returns to claim a deduction for some of their charitable cash gifts.

In a proposal that has broad support within the charitable community, the President wants to give non-itemizers a tax deduction up to a maximum amount of $250 per year for individuals ($500 for married couples) if they donate at least that amount to charity in a given tax year.

This proposal has perhaps the best chance of passage, since the Senate has already passed a similar proposal under the CARE Act. The only real difference between the two versions is that the President proposes to make the deduction permanent, while the Senate allows the deduction just in 2003 and 2004.

Another proposal aimed at stimulating charitable giving is the President's plan to allow those aged 65 or older to withdraw money from their Individual Retirement Accounts (IRAs) and donate the funds to charity without incurring any income tax consequences. The Senate also has a similar version of this proposal, but it puts the eligible age at 70½.

Estate Tax Repeal

The charitable community has been less receptive to the President's proposal to permanently repeal the estate tax. Currently, the estate tax

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Liability & Risk Management

Court Upholds Cancer Society Exec's Punishment Due to Social Harm and Tarnished Reputation

You do the crime, you do enhanced time, the Sixth Circuit told a former American Cancer Society executive who was sentenced to embezzling funds totaling more than $7.8 million in 2000. (See *NPA*, Oct. '00). Daniel S. Wiant admitted he scammed the organization through bank fraud, money laundering, mail fraud, and the illegal use of credit cards after the FBI discovered he had wired money to an Austrian bank with instructions to distribute the funds as a charitable research grant to a fake beneficiary. He was sentenced to 13 years in prison, with five years supervised release, under an "enhanced" sentence allowed by federal sentencing guidelines. He was also fined nearly $600,000. The guidelines permitted the stiffer sentence because Wiant's crime involved misrepresentation to a financial institution. Wiant now challenges the sentence, claiming it applies only in cases where the offender actually solicited funds by misrepresentation. In his case, Wiant claimed he only misrepresented his status and exploited the charity's funds, using the bank as a conduit. The court was unpersuaded, however, and let his original "enhanced" sentence stand. "The social harm Wiant caused by tarnishing the reputation of the American Cancer Society is closely analogous to the social harm caused by scam artists...both discourage donations and diminish charitable impulses." *USA v. Wiant*, No. 01-3443 (6th Cir, 1/2/03).

The judiciary is increasingly intolerant of executives who abuse the public trust.

This case demonstrates the increasing skepticism and intolerance of the judiciary (reflective of public attitudes) toward nonprofit executives who abuse their public and charitable trust. Help your organization avoid this kind of fraud by adopting and implementing sound fiduciary and accounting policies. For examples of such policies, order Nonprofit *Alert*® Memos, *Accounting and Fiduciary Guidelines for Nonprofits* and *Annual Audits: Vital Risk Management*. See back page for ordering instructions.

United Way Adopts Accountability Standards

United Way leaders from around the country met in Phoenix last month and adopted stricter accountability measures designed to make sure local United Way organizations accurately report overhead and program costs. Shaken by numerous controversies in recent years, United Way leaders sought to improve the organization's integrity and reputation. The new standards will now require local United Ways to conduct periodic self-assessments of their management and governance, and submit the reports and data from the assessments, including documentation of all revenues and expenses to the national United Way office. The national office will monitor the self-assessments, and an outside third party will review the financial data. In addition, 170 of the larger United Way organizations will be required to submit supplemental financial papers, including federal tax information.

This reform effort was already underway when the latest scandal made news last fall at the United Way in Washington, DC. (See *NPA*, June '02). To learn more about the United Way's new tighter standards, go to www.unitedway.org.

Employees & Volunteers

Employees' Time at Safety Course Not Compensable

Employers aren't responsible for compensating employees during training courses that are prerequisites for employment, the Sixth Circuit says. Tradesman, Inc., a skilled labor leasing company, required employees to complete a 10-hour safety course as a condition for employment. Some candidates were also hired on condition they complete the course within 60 days. The Department of Labor sought an injunction against Tradesman to stop this practice and compensate employees for 10 hours of unpaid overtime. A lower court granted the injunction, but Tradesman appealed, arguing its employees attended the course voluntarily. The Sixth Circuit noted that employees did not perform work while attending class, and the subject matter was not directly related to their job skills. Because completion of the training was fully disclosed as a precondition for employment, the court concluded that attendance was purely voluntarily, and therefore not compensable work time. *Chao v. Tradesmen Int'l, Inc.*, 2002 WL 31527264 (6th Cir., 2002).

Avoid this confusion in your organization by making clear to prospective employees, through employment publications and other communications, what training is a prerequisite for particular positions.

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Tax-Exempt Issues

IRS Issues Audit Checklist for Religious and Social Service Groups to Identify Weaknesses

As part of its “market segment” reviews, the IRS has published a 39-question checklist for its auditors to follow in auditing religious and social service organizations. Questions center on issues such as an organization’s size and purpose, number of constituents, organizational structure, fundraising income, lobbying, and executive compensation. The results of the reviews will be compiled into “profiles” that the IRS will use to identify areas of non-compliance common to those organizations. The goal is to develop better auditing practices and help educate organizations on points of weakness in their legal compliance. The IRS plans to develop similar checklists for the entire exempt organizations community. It has divided nonprofits into 35 different categories for “market segment” reviews.

Religious and social service groups are amongthe first to undergo IRS market segment reviews. Churches are generally not included in the review because they’re not required to file tax forms (unless they're generating unrelated business income).

Win-Win Situation: Sale of Apartment Complex Won't Affect Organization's Tax Exemption

A tax exempt organization may sell its interest in an apartment complex without incurring any adverse tax consequences or jeopardizing its exempt status, the IRS has ruled. The organization entered into an agreement to sell its entire interest in the building, contingent on a favorable ruling from the IRS. The sale was to be completed in a single transaction, at fair market value. There was no outstanding debt on the building. The only unusual aspect of the agreement was that the organization first granted a purchase option to the buyer. The organization agreed to assist the buyer in meeting various requirements to obtain financing for the purchase, but the buyer handled all expenses associated with obtaining financing. The IRS accepted the arrangement and said the organization would not incur unrelated business income tax (UBIT) on the sale proceeds. Furthermore, the IRS said any option payment income that the organization might receive, should the sale not reach completion, would also be free of UBIT because this was an isolated liquidation of unencumbered assets rather than a regularly conducted business of selling appreciated property. IRS LTR 200246032.

NPA Highlight of the Month

The Media: Friend or Foe to Nonprofits?

Whoever said, “There’s no such thing as bad press,” didn’t manage a nonprofit organization. Bad press can be ruinous, especially for organizations whose existence depends on public recognition and support. Knowing how to skillfully avoid and deflect negative publicity is just one crucial component in a dynamic media policy. Nonprofit leaders must also publicize the nonprofit’s positive message by taking advantage of the mass media’s enormous communications power.

The best approach is to be prepared. Determine in advance who among your staff will be a media contact, both in times of routine news events and in times of crisis. Draft simple fact sheets explaining everything from your organization’s mission and programs to its position on various issues. Develop and maintain good contacts with media representatives, especially those who often report on nonprofit events or other issues affecting your organization.

In a crisis, always tell the truth, but focus on getting your organization’s message out in the way you want it to be understood. This does not mean you should provide the media with every last detail of an incident or tell a reporter everything you know. In fact, doing so could create potential liabilities for your organization; check with an attorney, if in doubt. Other crisis tips to remember:

- Use a prepared statement and stick to it. Anticipate questions and prepare answers in advance. Have an attorney review the text if there is any possibility that legal issues could arise.
- If you don’t know, say so. Don’t try to schmooze an answer. Just offer to find the answer and get back to the reporter before his/her deadline.
- Don’t ever ignore the media. Practice the three “Rs”: return calls; respond to requests; and respect deadlines.

Using the media effectively can propel your nonprofit’s concerns and activities to the forefront of a community. The media is always looking for a story, and most organizations can benefit from positive publicity. Developing and implementing a comprehensive media policy is one way to insure your organization accomplishes this goal. Refer to Nonprofit Alert® Memo, *Making the Media Work for You* to develop a media policy. See back page to order.

Nonprofit's Web Site & Pubs Don't Produce UBIT if They Only Acknowledge Third-Party Providers

Listing information about third-party service providers on a nonprofit's web site or in its publications doesn't produce unrelated business income tax (UBIT), the IRS has ruled. The issue arose in a case involving a tax-exempt agricultural organization that published news materials and operated a web site for its members. It used these mediums to convey information to members and the general public about issues affecting the agricultural industry. The organization sold advertising space in its print publications. Income from these ad sales was taxable as UBIT, the IRS said. But the organization also provided acknowledgments in its print and electronic publications, including its web site, that referred to third-party service providers who offered special benefits for the organization's members. These acknowledgments did not produce UBIT, the IRS said, because the mere acknowledgment of the availability of those benefits to members did not constitute a trade or business. Furthermore, links on the organization's web site to other sites operated by the third-party providers also did not create any UBIT concerns. IRS LTR 200303062.

Additionally, the IRS said banner advertising on the organization's web site wouldn't trigger UBIT, so long as the advertising wasn't done on a periodic basis and wasn't just an online version of the organization's print materials, which do create UBIT. This is good news for nonprofits operating web sites, but a slightly different fact scenario (such as a small gratuity or stipend paid for the banner advertising) would be considerably more likely to produce UBIT. Nonprofits should consult legal counsel before placing any advertisements on their web sites, as this area of the law continues to evolve.

Labor Dept Provides Info for Deploying Military

With thousands of Reservists deploying to the Middle East, nonprofits are once again facing questions about their obligations to employees called up for military duty. The Uniformed Services Employment and Reemployment Rights Act (USERRA) prohibits discrimination against these employees and protects their rights to reemployment upon return from service. COBRA protects health care coverage for these employees and their families.

Review all these issues with employees who may be deploying. Find complete details on the Department of Labor's web site at www.dol.gov/pwba.

President's Budget Plan . . continued from p. 1

is set to reduce incrementally over the next several years, with a complete repeal in 2010. After 2010, the tax would automatically be restored unless Congress passes new legislation. Some nonprofits worry that a permanent repeal of the estate tax will stymie charitable giving, since wealthy donors would have less of a tax incentive to make contributions. Passage of this proposal is less certain than the President's other proposals, as the issue has spawned considerable controversy for several years.

To Order Memos: Memos referenced in the ***Nonprofit Alert*** can be purchased for $20 each ($10 for clients) from Gammon & Grange, P.C. Five or more copies of the same memo are bulk priced at $5 each. Call, write, or email us at the address below.

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