



Nonprofit *Alert*[®]

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

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Update on EO Legislative Reform Proposals

Although Congress approved the Tax Reconciliation bill (H.R. 4297, the Senate version of which originally included charitable organization provisions) without any significant charitable incentives and reforms (a provision stiffening penalties on charities participating in prohibited tax shelters was included), Senate Finance Committee (SFC) Chairman Chuck Grassley (R-IA) and House Ways and Means Chairman Bill Thomas (R-CA) have agreed to add a package of charitable incentives and reforms to the Pension Reform bill (H.R. 2830) that is currently in Conference Committee.

When asked about the charitable reforms and incentives that Grassley and Thomas are considering for this package, one House staffer responded that "everything is on the table," including reform proposals that Grassley first entertained in 2004, as well as those previously included in the Senate version of the Tax Reconciliation bill. The staffer indicated that the official timetable for finalizing the Pension Reform bill was originally Memorial Day, but in part because of the fluid nature of the charitable incentive and reform proposals, conferencing may not be completed until the Fourth of July or after.

NHTSA Reissues 15-Passenger Van Safety Advisory

In 2005, the National Highway Traffic Safety Administration (NHTSA) reissued what is now the fourth safety advisory in five years that focuses on the increased rollover risks for 15-passenger vans. The advisory concluded that 15-passenger vans with more than 9 occupants have rollover rates nearly three times the rate of vans with fewer than 10 occupants.

Many churches, as well as other nonprofits, own and use 15-passenger vans to carry passengers on sponsored events. **In light of this most recent advisory, any organization that continues to use its van must realize that they are now assuming an elevated risk of liability.**

Consider the following scenario: The staff at Cherry Falls Church is ecstatic about the number of youths signed up to attend their annual beach week retreat. This year, attendance has swelled to 74 attendees. While it will be a tight fit, Cherry Falls Church has decided that they need not rent extra transportation. Using the seven 15-passenger vans already belonging to the church, the staff spread out attendants in groups of 12 to 14 amongst the fleet, allowing for extra luggage storage in the back row and on the van's top. On the morning of the trip, there is not a cloud in the sky. However, misfortune strikes: One of the vans carrying 13 passengers rolls over after swerving to miss another church van. Although there

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NHTSA...continued

are no fatalities, one youth has suffered serious trauma to his face and scalp, while the driver has fractured his collarbone.

It is important to realize that not only may a Court find such vehicle use negligent, but that it could also conclude Cherry Falls Church, and its governing board, “grossly negligent” as a result of their disregard of four NHTSA safety advisories warning of the multiplied risk of carrying more than 9 passengers.

A finding of “gross negligence,” which constitutes an indifference to, and a blatant violation of, a legal duty with respect to the rights of others, differs from negligence not only in degree of inattention, but also in its implications for the plaintiff. Such a finding could expose Cherry Falls Church to “punitive damages” that are likely not covered under its liability insurance policy. What’s more, the members of the board of directors could be personally liable on the basis of gross negligence, which may not be covered by state immunity laws.

If your church owns one or more 15-passenger vans, consider restricting its use to only carrying cargo, or replacing it with smaller vans or “small school buses.” If you do decide to retain your van, please be sure to strictly comply with the most recent NHTSA safety advisory recommendations:

1. Keep your passenger load light—Research shows that 15-passenger vans have a rollover risk that increases dramatically as the number of occupants increase.
2. Check your van’s tire pressure frequently, at least once a week—Studies have found that 74% of all 15-passenger vans have improperly inflated tires; this can change handling characteristics, increasing the prospect of a rollover crash in 15-passenger vans.
3. Require all occupants to use their seatbelts or the appropriate child restraint—nearly 80% of those who have died nationwide in 15-passenger vans were not buckled up.
4. If at all possible, seat passengers and place cargo forward of the rear axle—and avoid placing any loads on the roof—by doing so, you’ll lower the vehicle’s center of gravity and lower the chance of a rollover crash.

5. Be mindful of speed and road conditions—analysis shows that the risk of rollover increases significantly with speeds over 50 mph and on curved roads.
6. Only qualified drivers should be behind the wheel—Special training and experience are required to properly operate a 15-passenger van.

Note: While compliance with the above recommendations may provide some defense to liability, it may not be enough. If you decide to continue using your 15-passenger van, make sure to:

- ⇒ Never ride more than 9 occupants in the 15-passenger van.
- ⇒ Adopt a written policy mandating compliance with all NHTSA recommendations.
- ⇒ Install the NHTSA hangtag in every van. (<http://www.nhtsa.dot.gov/cars/problems/studies/15PassVans/15PassCustomerAdvisory.htm>).

Court Upholds DAF’s Denial of Tax Exemption

The Federal Court of Claims has upheld the IRS denial of the tax exemption application of New Dynamics Foundation. NDF was established as a donor advised fund (DAF) that accepted contributions into accounts from which donors were permitted to make advisements as to ultimate use by NDF. While there are numerous DAFs that have been recognized as 501(c)(3) tax exempt organizations, and several DAFs rank among the top charitable organizations in assets held, the Court found that NDF failed to operate exclusively for exempt purposes, but was characterized “at the least by willful neglect, and, more than likely, an active willingness to participate in a scheme designed to produce inappropriate tax benefits.” Key among the evidence presented by the IRS was NDF promotional materials that claimed that NDF donors could “warehouse wealth,” and advise up to 95 percent of amounts in a fund for “administrative” expenses of the donors, travel, and payment to their children of a “reasonable wage” for participating in volunteer activity. Based on these facts and others, the Court concluded that NDF donors did not truly relinquish ownership and control

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DAF Tax Denial....continued

over funds and property donated to NDF, but were allowed to use NDF as a conduit for the accomplishing the twin tax avoidance goals of building up their assets tax free and then siphoning off the accumulated wealth to pay for personal expenditures.

➔ Some legislators have cited egregious cases of private benefit, such as the types of schemes promoted by NDF, as rationale for promoting new statutory requirements on donor advised funds. However, the NDF case highlights that the IRS, under current law, has the means to find and prohibit abuse of donor advised funds without burdening legitimate DAFs with additional requirements.

Texas-based Charity and its President Violated Fiduciary Duties in Ohio, Court Rules

An Ohio Appellate Court ruled that a Texas-based charity and its president violated their fiduciary duties by failing to oversee professional solicitors. The Court directed the appointment of a receiver to receive the organization's charitable contributions in Ohio.

The American Deputy Sheriff's Association (ADSA) presents itself as a charitable organization raising funds for equipment and training of local law enforcement personnel, and to provide scholarship and death benefits for their families.

CEO Larry Smith entered into a controversial relationship with several soliciting organizations owned by Michael Gold. Gold and his organizations failed to register as professional solicitors in all states required and subcontracted solicitations to as many as 7,500 solicitors without getting ADSA approval. The solicitors used unapproved and misleading scripts, failed to turn over collected funds as required and retained approximately 96% of the contributions for costs and fees. In spite of these irregularities, Smith continued renegotiating new contracts with Gold while having no confidence that he would perform responsibly.

The Ohio court found that both Smith and ADSA breached their fiduciary duties by failing to exercise reasonable care and oversight over solicitation activities.

Charity Official Charged with Theft

Cheryl McEwan, a grants administrator for the Rockefeller Foundation, and her husband, Anthony McEwan, have been charged with stealing hundreds of thousands of dollars from the foundation that employed her.

The pair stole \$232,500 in triple-matching grants through a scheme where she approved awards to a fake charity managed by her husband. The funds were used to pay credit card and mortgage bills and to make a down payment on a house.

The husband-and-wife duo, along with Frank Melli, a director of an environmental nonprofit, were also charged in a similar scheme with stealing \$188,500 from the Rockefeller Foundation.

Denying any wrongdoing, Melli and Cheryl McEwan are being held on bail. Anthony McEwan has not yet been arraigned.

➔ Rigorous applicant screening, including use of secondary references and criminal records checks, is an essential element in prudent risk management. It is especially crucial for employees with direct control of funds. For information on risk management steps to avoid a similar occurrence in your organization, order *Nonprofit Alert® Memo, Hiring & Supervision: Managing Employee Liability*.

Michigan A.G. Starts Controversial Investigation into the Ford Foundation

Michigan Attorney General Mike Cox has started an investigation into the Ford Foundation. "The foundation has drifted away from Michigan," says Nate Bailey, a spokesman for the A.G.'s office. "One of our goals," he continues "undoubtedly is to bring some of Henry Ford's money home." Mr. Bailey, who believes the Foundation has a "higher fiduciary responsibility" to its hometown and state, contends that the fund has ignored the Ford family's philanthropic wishes by reducing support for charities in Michigan.

While the inquiry primarily focuses on whether the grant maker gives enough of its \$11.6-billion largess to charitable causes in Detroit and other parts of Michigan, further questions have been raised concerning the giving of funds

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Ford Foundation....continued

to nonprofits with connections to board members, and excessive administrative costs.

“We have a long and proud history of grant making in Michigan,” replies Marta L. Tellado, Ford’s Vice President of communications who points out that the Foundation still provides generous support, along the lines of \$38-million since 1996, to groups in the state. Ms. Tellado dismisses the A.G.’s additional claims, citing Ford’s 13 international offices as the cause for higher administrative costs. As to the \$830,000 donated to the World Wildlife Fund when Kathryn Fuller was CEO of the group and also a Ford board member—a conflict-of-interest oft-cited by the Attorney General’s office—Tellado attests to the Foundation’s support of the Fund since 1957. She also maintains that Board members strictly adhere to a policy of recusing themselves from any grant decisions involving charities they have worked for.

Sam Singh, chief executive of the Michigan Nonprofit Association noted, “The question is what’s an appropriate investment to the state you were created in? That’s a question for the board to answer. To me, it’s not a legal question.”

➔ Increased state scrutiny of the charities highlights the need of Board members to know their legal obligations. For more information order *Nonprofit Alert® Memo, Directors’ Nonprofit Legal Duties*.

Indiana Judge Hands Control of Schwab Foundation over to a New Board

“Judge Hands Control of Schwab to New Board,” reports the Fort Wayne Journal Gazette. The Olin B. and Desta Schwab Foundation has been in recent news most notably and notoriously for the lawsuits brought against its board. Indiana Attorney General Steve Carter sued the board last January for mismanaging the Foundation’s assets and illegally relocating it to Nevada in 2004, where a similar lawsuit is currently on hold. Allegations from both states focus on the purchase of a \$1.5 million resort home outside Las Vegas—purportedly purchased as an investment—that served as a vacation spot for the now former board members. “I’m sure [the new board] will complete any sale in a way that withstands public scrutiny,” says Carter.

Gates Foundation Awards \$75,000 Grant to NCNA

The Bill and Melinda Gates Foundation has awarded a \$75,000 grant to the Washington, D.C.-based National Council of Nonprofits Associations. The grant will support a series of NCNA-sponsored town hall meetings among America’s nonprofit leaders in an effort to unite and organize that sector. Feedback generated from these meetings will be used to inform the development of a public-policy platform.

Audrey R. Alvarado, NCNA executive director notes, “These common ideals and concerns, which we’re uncovering now in our town halls, create the foundation that will ultimately articulate the vision and aspirations we have for the sector’s future.”

Muslim Charitable Organizations Raise Voices of Concern

A coalition of Muslim organizations has recently requested a meeting with Treasury Secretary John Snow to voice their concerns about the government’s counterterrorism efforts’ effect on Islamic religious obligations.

In a letter to Snow, the American Muslim Taskforce on Civil Rights and Elections suggested that the government’s crackdown on Islamic charities has hurt American Muslims’ ability to carry out religious obligations to the needy. The letter claims effects that have been both direct, through the government’s closure of several prominent Islamic charitable organizations, and indirect, through the intimidation of Muslim donors required by faith to give alms.

Since 9/11, the government has designated three major U.S. Muslim charities as likely sponsors of terrorism and has since frozen their assets.

➔ See the *January/February 2006 Nonprofit Alert®* for additional information on the U.S. Treasury’s voluntary guidelines for charitable organizations seeking to protect themselves from inadvertently aiding terrorist-related organizations.

At the IRS:

Intermediate Sanctions/Revocation Regulations

Final regulations explaining the circumstances under which the IRS would both impose intermediate sanctions on and / or revoke tax-exempt status from exempt organizations with excess benefit transactions might be released in the next few months, says David Fish, manager IRS Technical Guidance and Quality Assurance. However, while speaking at the March Nonprofit Legal and Tax conference in Washington he said, "You never know with how things happen at Treasury."

This year the IRS is adding 200 new organizations to the 1,800 currently under focus in the Service's executive compensation compliance project, which will now shift focus towards uncovering excessive loans made to tax-exempt organization officials, says Fish.

High-profile Disaster Relief Charities to be Investigated

An IRS official has indicated that tax-exempt hospitals and high-profile charities that participated in recent disaster relief efforts are among the organizations that the IRS plans to target in its compliance initiatives this year. Additionally, recent trends of abuse from private foundations have prompted the Service to launch major compliance efforts toward that sector.

Marvin R. Friedlander, speaking at the March Nonprofit Legal and Tax conference in Washington, told attendees that the IRS intends to efficiently mobilize its resources so that the public and Congress do not lose confidence that exempt organizations merit a tax preference...or are fulfilling their exempt purposes.

IRS Officials Discuss Common Filing Errors

Joyce Hoover of the IRS Exempt Organizations Special Review reports that 36.1 percent of Forms 990 and 51.7 percent of Forms 990-EZ are submitted with errors and that the most common of these errors are found at the beginning of the form where it asks for an organization's name and other identifying information.

Common mistakes cited by Hoover, along with several tips and guidelines include:

- ➔ When filing Forms 990 or 990-EZ, make sure to use the organization's legal name, not the name it uses to do business.
- ➔ If you want to use the "doing business as" name on the form, put that name in parenthesis.
- ➔ Make sure to check that the Employer Identification Number in Box D is accurate and that the correct year end for the organization is reported.
- ➔ Make sure that the accounting methods used on your organization's returns are the same methods regularly used to maintain your books and records.
 - Note that most states accepting Form 990 for charitable organization registrations require all amounts to be reported based on the accrual method.
 - However, Schedule A—the support schedule used for public charities—must be filled out using the cash method.
- ➔ Organizations with gross receipts below \$25,000 are not required to file. Those that do decide to file, however, must now complete the entire form instead of merely checking Box K.

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. Visit the [Nonprofit Alert Memo Page](#) for details. **To Subscribe:** The NPA is a free publication with no login or password required. Visit the [Nonprofit Alert Page](#) to view current and past issues. Send an email to NPA@GG-Law.com to be added to the new issue notification email list.

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