



Nonprofit *Alert*®

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

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➤ Legislative Developments

Congress Attaches More Strings to Federal Funds

It could've been much worse when Congress passed an appropriations bill last month containing several new restrictions for charities that receive federal funds, but by the time the measure emerged from a House-Senate Conference Committee, the most stringent provisions were eliminated or at least watered down enough to make them palatable to most nonprofits.

What remains is a requirement that prohibits charities from using certain federal funds to lobby. A further provision requires the chief executive officer of any entity receiving federal funds to certify that none of the funds has been used to

lobby the federal government or litigate against the United States.

At press time, the President was expected to sign it into law in the coming weeks. The intent behind this legislation is clear: Congress wants to significantly curb nonprofit lobbying with federal money. This has been an ongoing theme in Congress since the 1980's when new lobbying rules were first made applicable to nonprofits.



Read about more limitations in Nonprofit Alert® Memo 9101-3, *Nonprofit Lobbying and Political Activity—Know Your Limits*. See back page to order.

Web Worries: No Jurisdiction From Internet Ads

A web site that functions purely as advertising doesn't subject its maker to potential lawsuits in any jurisdiction other than the maker's own, the Fifth Circuit has ruled. The case gave the court its first opportunity to opine on the issue of Internet jurisdiction. It involved a Texas resident who sued a Vermont company for alleged copyright infringement. Because the company's web site contained a print-out mail order form, a toll-free phone number, mailing address, and an email address, the plaintiff argued the company was "doing business" in Texas and was, therefore, subject to lawsuits there. The court noted, however, no orders were actually taken through the web site; instead, users had to download the order form and fax or mail it to the company. Thus the site was only a "passive advertisement," the court wrote, which was not enough to create jurisdiction. *Mink v. AAAA Development*, No. 98-20770 (5th Cir. 1999).



Before you sigh relief over this ruling, keep in mind that the court identified three levels of web use: (1) contracting with out-of-state residents through repeated transmissions of computer files over the Internet; (2) maintaining a web site that allows users to exchange information with a host computer; and (3) merely advertising or posting information on a passive web site. Only the third level escapes jurisdiction, according to the Fifth Circuit. If your organization engages in level one or two, then long-arm jurisdiction very likely reaches your organization, making your liability much greater.

~~~ What to Save . . . What to Trash ~~~

According to a University of Stanford study, U.S. workers never look a second time at 87% of the paperwork that crosses their desks. Most simply file it away or push it to a stack where it remains until some contingency, like cleaning or an employee transfer, causes it to be removed. If that number is accurate, then there's a lot of paper you and your employees could be eliminating the first time around!

Learn what to save and what to trash with **Nonprofit Alert®** Memo 9104-1, *Records Retention Requirements*. See ordering instructions on the back page.

Liability & Risk Management

Baptist Charity Investigated for Financial Dealings

The Arizona Attorney General's office and Corporation Commission have launched an investigation into the financial dealings of the Baptist Foundation of Arizona, claiming the organization allegedly misrepresented itself to over 13,000 investors. Officials allege that the foundation and certain subsidiaries promised investors unrealistic rates of return on their deposits. The foundation is the fundraising subsidiary of the Arizona Southern Baptist Convention. It sells investment products primarily to Southern Baptist members, but also operates dozens of subsidiaries that engage in everything from real estate to insurance. State officials are attempting to unscramble the interlocking connections between the subsidiaries and the foundation.

➔ **According to published reports, the foundation has already fired its three top executives in an attempt to address investor concerns. The state's investigation began after the *Phoenix New Times* published an expose last year.**

IRS Mistake Doesn't Relieve Church of Liability

The Indianapolis Baptist Temple is liable for more than \$5.3 million in employment taxes and assessments despite the IRS's mistake in using an incorrect employer identification number (EIN), a federal judge has ruled. The IRS used an EIN that had previously been assigned to the Temple when it functioned as a corporation prior to 1989. That year, the Temple dissolved its corporate form and reorganized as an unincorporated religious society. A new EIN was issued shortly thereafter. Since the Temple had actual knowledge of all the assessments and penalties that were sent in the name of the predecessor corporation, the court ruled that the IRS's mistaken use of the old EIN did not in any way prejudice the Temple; thus the church was fully liable for the back taxes, plus interest and penalties.

United States v. Indianapolis Baptist Temple, et al., No. IP 98-0498-C-B/S (S.D. Ind. 1999).

➔ **Cases like this offer a valuable lesson that all nonprofits can learn vicariously: one of a nonprofit's greatest liability exposures is often the underpayment of payroll taxes. This triggers the IRS' potent collection weapon known as the §6672 100% penalty tax against both the organization and its officers.**

Nonprofit Alert®

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Convention Contract Bowls a Strike for Association

A federal judge in New York has ruled that the Women's International Bowling Congress (WIBC) did not make an implicit promise to rent rooms from the Hyatt Regency Hotel in Buffalo during its 1996 annual championship tournament. The ruling relieves the organization of liability for some 2,400 rooms that were unoccupied during the tournament. The case centered around a contract that WIBC entered with the hotel, which named the hotel as WIBC's headquarters during the tournament and specified how many rooms the hotel would hold for WIBC attendees. However, the contract did not address WIBC's obligation to pay for any rooms that went unoccupied. Reading the contract's plain language, the court ruled that WIBC was not liable for any shortfall between the number of rooms held, versus those actually rented by WIBC attendees. The court distinguished the hotel's promise to "hold" the rooms, but not necessarily "reserve" them. This indicated both parties understood that all the rooms on "hold" might not actually be filled, the court said. *Hyatt Corp. v. Women's Int'l Bowling Congress*, CIV No. 97-CV-0767A(F) (W.Dist.NY, 1999).

➔ **All nonprofits enter contracts—leases, employment agreements, licenses, building contracts, annuities, etc.—and contract liability is a concern on every deal. The best way to limit your contract liability is through an internal or external review, followed by board review and approval.**

Employees & Volunteers

On the Road Again: Tricky Travel Deductions

Two recent court rulings highlight the complexity of employee travel deductions. In the first, a consultant worked for several publishing companies as an independent contractor. His principal place of business was his home office, but for four years, he worked several months of every year at a temporary location in California where he assisted the editor of a magazine. The IRS denied his expense deductions for a one-bedroom apartment in California, plus all travel connected with the temporary work. The reason: the work exceeded the one-year limit the IRS defined as "temporary." But the Tax Court overturned the ruling, noting that the work was "on again and off again" throughout the period. His work was renewed each year because of unexpected contingencies that the magazine experienced. The court also focused on several other indicia of his temporary work, including:

- the continued operation of the consulting business from his home office, even during periods when he was physically in California;
- the fact that he spent more time at his home office each year than he did at the temporary job in California; and
- he was not provided, nor did he maintain an office in California. *Mitchell v. Commr.*, T.C. Memo 1999-283.

In the second case, a federal bankruptcy court denied travel expenses to a couple who were self-employed artisans. The couple made decorative items, which they sold at craft shows around the country. They traveled to the shows in a mobile home, where they lived for a majority of the year. They also maintained

a house in Florida but only lived there about 35 to 40 days a year. The court ruled that the mobile home was their primary “tax home” because they spent the majority of their time there. The taxpayers admitted they only used their Florida house for storage and even slept in the mobile home when on the premises. As a result, the court denied their travel expense deductions for the mobile home. *In re Bechtelheimer*, No. 96-02352-8G3 (BC-DC FL, 1999).

➔ **The IRS is very parsimonious about travel-away-from-home deductions. This could be critical for your employees who travel regularly, such as consultants or trainers. Review with them the rules outlined in Nonprofit Alert® Memo 103-3, *Expense Reimbursement for Volunteers and Employees* so they know what deductions are available. See back page to order.**

Executive Salaries Increase at Top U.S. Nonprofits

The median executive salaries at the nation’s largest nonprofit organizations increased last year by 5.7%, according to an annual study conducted by *The Chronicle of Philanthropy*. That equates to a median salary of \$207,990. This marks healthy growth over the 1997 median increase of 2.9%. The study looked only at 246 of the nation’s largest and wealthiest nonprofit organizations, including private foundations, charities, hospitals, universities, and community foundations with incomes ranging from \$9.7 million to \$3.6 billion. The study also showed that most of these organizations spent between one and two percent of their total income to compensate their top two executives.

➔ **These generous salaries are not reflective of actual or reasonable salaries for the remaining two million U.S. nonprofits. Assess the reasonableness of your pay**

scales with Nonprofit Alert® Memo 9102-7, *Establishing Reasonable Compensation for Nonprofit Leaders*. See back page to order.

Tax-Exempt Issues

Baseball Exemption Is Just a Field of Dreams

An amateur baseball team does not qualify for exempt status, the Tax Court has ruled, because its activities do not support charitable goals. The team’s sole activity is playing regular games at a local field. It does not charge admission. The IRS argued, and the Tax Court agreed, that this amounted to nothing more than recreation. Allowing spectators to watch the games free of charge was only incidental and did not constitute a charitable goal. Although the “promotion, advancement, and sponsorship” of amateur baseball are exempt purposes, the court said nothing was being promoted here other than the team member’s “social and recreational” interests. *Wayne Baseball v. Commissioner*, T.C. Memo 1999-304.

➔ **The first and most important precept in establishing an exempt organization is that it must have a charitable purpose. Nonprofit Alert® Memo 9304-1, *Organizing the Nonprofit*, explains why. See back page to order.**

Gift Is Same in All Languages, Despite Confusion

A donor left \$1 million in U.S. securities to a foreign charity, but her will did not clearly specify whether the gift should go directly to the foreign charity or to its U.S. affiliate. In addition, the will was written in a foreign language, but not in the language of the

NPA Highlight of the Month

Historic AOL/Guidestar Venture Puts Charities in the Sunlight

One-stop shopping has arrived in the world of philanthropy, thanks to an historic venture between America Online and various nonprofits including the Philanthropic Research organization, which operates Guidestar.org. Together they have launched Helping.org, a new web portal that links users to a wealth of charity data that has never before been accessible in one place. Users can research tax forms and other information filed by charities, find news about volunteer opportunities, and even make charitable donations online. Since last year, Guidestar has posted on its web site the detailed tax returns that most nonprofits are required to file annually with the IRS (i.e. the Form 990). But under this new arrangement announced late last month, Guidestar’s database now serves as the search tool to research more than 600,000 charities through Helping.org. Most of the data comes from the Form 990’s, but Guidestar has included a “consumer-friendly format” that charities can use to update or expand the information contained in their Form 990’s, explains Debra Snider, Communications Director at Guidestar. For charities that aren’t required to file Form 990’s like churches and small nonprofits, Guidestar offers a registration process enabling them to post data so that potential donors and volunteers can access similar information about all charities. Eventually, Guidestar plans to provide three to five years worth of Form 990’s and related data for all charities, says Snider. “With all this information in one place, not only donors but nonprofits themselves can more easily benchmark by understanding what’s going on throughout the charitable community,” she says.

➔ **The site will also serve as an alternative means for nonprofits to comply with federal disclosure rules that require public accessibility to a charity’s Form 990. Visit the new web portal at <http://www.helping.org> or access Guidestar at <http://www.guidestar.org>. For more information about the disclosure rules, refer to Nonprofit Alert® Memo 9904-1, *Nonprofit Disclosure Rules*.**

country where the foreign charity was located! To clear up the confusion, representatives of the estate petitioned a foreign court to translate the will. The court then ruled that the donor's intent was for the U.S. affiliate to receive the gift. However baffling the will language may have been, it was purely a function of the translation, the court said, and not a problem with construction. Based on that ruling, the IRS granted the donor's estate a charitable deduction for the gift. IRS TAM 199925043.

➡ **The real issue is the necessity of making a gift to a qualified U.S. charity. To be deductible, the gift must be placed within the full and complete control of a U.S. charity, although the charity may ultimately honor a non-binding request of the donor to use the gift in advancing the compatible work of a foreign charity.**

Club's Sale of Property Tees Off UBIT Concerns

A social club wanted to sell 6.75 acres of land alongside a golf course that it operated, so the club first petitioned the IRS to determine whether the sale would create an unrelated business income tax (UBIT) liability. Golfers routinely used about 2.5 acres of the land to retrieve their stray golf balls. The club used the remainder of the property as a water basin and landscape storage. Except for the acreage used exclusively by the golfers, the IRS said the property was not used in performance of the club's exempt function and would, therefore, be subject to UBIT. However, any gain from the sale of the 2.5 acres used by the golfers would not create UBIT, the IRS ruled. IRS LTR 199929044.

➡ **Given the potential UBIT issues, always check with legal counsel before considering the sale of any property that your organization owns. *Nonprofit Alert*® Memo 9110-1, *A UBIT Primer for Nonprofits*, can also help answer basic questions about the tax liabilities created by such sales.**

Nonprofit Insurance Alliance Expands Nationally

With the help of a \$5 million donation from the Bill and Melinda Gates Foundation, the Nonprofit Insurance Alliance of California will offer its services nationwide starting next year. Services

include liability insurance, plus free risk management and training seminars for nonprofit executives. Operated as a nonprofit insurance pool, the Santa Cruz-based organization now provides liability insurance to some 2,000 California nonprofits, which equates to one out of every ten 501(c)(3)'s operating in the state.

➡ **Learn more about the Alliance and its plans by visiting its web site at <http://www.niac.org>.**

State Rules & Regs

Arkansas Stiffens Solicitations With DTPA Penalties

A new law revises the state's charitable solicitation requirements, providing much more detail to disclosure rules and making any violation of the new act also a violation of the state's Deceptive Trade Practices Act (DTPA). This means all DTPA penalties can also be applied against violators, including criminal sanctions, injunctions, and restitution awards. Ark.Act 1198.

Texas Opens Board Meetings Via Video & Internet

The state legislature recently amended its nonprofit corporation act to allow electronic board meetings via videoconferencing and/or the Internet so long as all participants agree and are able to participate by communicating concurrently with each other. TX H.B. 756.

➡ **Look for more states to make similar changes as technology presents convenient and economical alternatives to traditional board meetings.**

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