neo Nonprofit & Exempt Organizations
LAW GROUP

Emerging Legal Questions in Today's Boardroom

BoardSource Leadership Forum
September 22, 2011

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Current Status of Nonprofit Governance

Overall Board GPA*

Chief Executive: 2.57
Board: 2.96

* BoardSource Nonprofit Governance Index 2010

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Current Status of Nonprofit Governance

% of Boards well-informed of their legal and governance responsibilities

Chief Executive: 58%
Board: 56%

* BoardSource Nonprofit Governance Index 2010

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Board Basics

- Governance and oversight
- Fiduciary duties of care and loyalty
- Authority to act as a group

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Agenda

- Technology and Social Media
- Transparency
- Earned Income and Social Enterprise
- Nonprofit Advocacy

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Technology and Social Media

- Social Media
- Internet Solicitations
- E-mail Voting

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Social Media

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Example: American Red Cross

Image source: Todd Wasserman, *Red Cross Does PR Disaster Recovery on Rogue Tweet* (Feb. 16, 2011)

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Social Media Risks Example: Labor Law

- Hispanics United of Buffalo, Inc. and Carlos Ortiz (9/2/11)
- NLRB Resources:
  - A Survey of Social Media Issues Before the NLRB (8/5/11)
  - NLRB Social Media Report (8/18/11)

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Other Social Medial Legal Risks

- Defamation
- Intellectual property violations (e.g., copyright)
- Inaccurate information
- Privacy violations
- Harassment
- Breach of confidentiality
- Anti-trust

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Social Media Policy Tips

- Moderation guidelines
- Process for removing content
- Training
- Community guidelines/Terms of use

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Internet Solicitations

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Charitable Solicitation Registration

- 40 states have charitable solicitation statutes
- NASCO – Charleston Principles
- Resources:
  - Nasconet.org
  - Multistatefiling.org

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E-mail Voting

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Board Action

Board may take action:

- At a duly held meeting; or
- By signed written consent

Resource: "Can Nonprofit Boards Vote by E-mail?" (Blue Avocado)

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E-mail Voting Concerns

- Actual consent
- Validity of current and/or past board actions
- Hasty decision-making
- Lack of thorough conversation

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E-mail Voting Tips

- Check state laws
- Establish guidelines
- Use sparingly
- Encourage discussion prior to vote
- Return signed written consents

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Transparency

- Form 990
- Private Benefit/Inurement
- Excess Compensation

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Form 990

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Form 990 – Recent Developments

- Pension Protection Act 2006
  - 6/8/11 announcement: 275k orgs lost exempt status
- 2008 Redesign
  - Governance-related questions
- More widely accessible

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Form 990 – Tips

- Review with other publicly available information
- Take care with narratives
- Use the perspective of a critic
- Review by a variety of experts

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Form 990 – Governance Questions

- Conflict of interest policy
- Executive compensation approval process
- Document retention and destruction policy
- Gift acceptance policy
- Meeting minutes documentation practices

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Form 990 – Governance Questions (cont.)

- Review process of Form 990 by the board
- Whistleblower policy
- Expense reimbursement policy
- Joint venture policy
- Policies regarding chapters, affiliates, and branches

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Form 990 – Governance Policies Tips

- Don't check "yes" just to check yes
- Don't adopt a policy you're not going to follow
- Regularly review adopted policies
- Talk about it!

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Private Benefit & Private Inurement

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No Private Benefit

- Org must serve a public interest and cannot be operated to serve private interests
- Incidental benefit to individuals may be okay

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No Private Inurement

- Net earnings cannot inure to an "insider"
- Penalty: Revocation of exempt status

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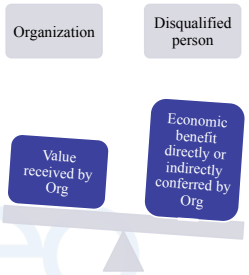
No Excess Benefit Transactions



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Excess Benefit Transaction

Penalty: Intermediate Sanctions

- 25%, 200% (disqualified person)
- 10% (up to $10,000) (board, if knowing and willing participation)

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Excess Compensation

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Reasonable Compensation

- For like services
- By like enterprises
- Under like circumstances
- On the date the contract is made

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Rebuttable Presumption of Reasonableness

- Approval in advance by disinterested board (or committee)
- Appropriate comparability data
- Concurrent documentation

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Common Issues

- Approval process of bonuses and severances
- Compensation for past services
- Fundraising-based compensation

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Earned Income and Social Enterprises

- Tax Implications
- Business Considerations
- Hybrid Legal Structures

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Tax Implications

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IRS – Tax Perspective

Related Business Income	Unrelated Business Income
• Generally exempt income	• May be subject to corporate taxes

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Related v. Unrelated

An unrelated business is:

1) A trade or business;
2) Regularly carried on; and
3) Not substantially related to furthering the exempt purpose of the organization.

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Earned Income Examples

- Woodland Park Zoo Doo
- Goodwill Industries stores

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Facts & Circumstances

IRS considers factors such as:

- Nature and size of business
- Fees
- Who is served
- Business operations

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Exclusions & Modifications

Including:

- Volunteer workforce
- Convenience of members
- Selling donated merchandise
- Passive income

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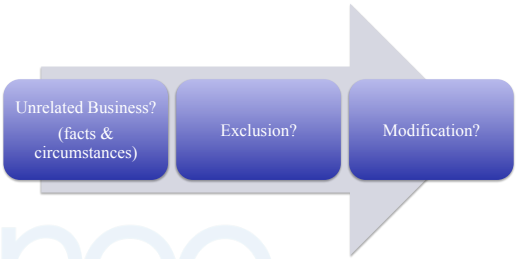
Application of the Rule



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Museum Examples:

- Café – Street entrance…
- Auditorium – Dual-use…
- Gift shop – Merchandise lines…

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Last but not least…

Unrelated business activity cannot be more than an **insubstantial amount** of the org's activity!

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Business Considerations

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Additional Considerations

- Mission
- Directors' fiduciary duties
- Taxes (e.g., sales, property, income tax)
- Potential private inurement or private benefit
- Capacity
- Culture compatibility
- Other costs

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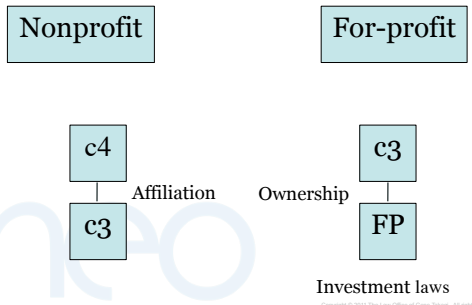
Subsidiaries



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Hybrid Legal Structures

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Hybrid Legal Entities

- Low-profit Limited Liability Company (L^3C)
  - *Resource: Americans for Community Development*
- Benefit Corporation
  - *Resource: B Lab*
- Flexible Purpose Corporation
  - *Resource: Businessforgood.blogspot.com*

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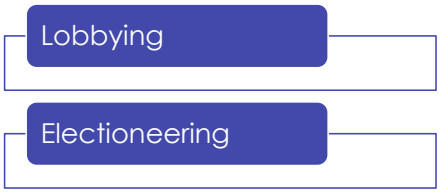
Nonprofit Advocacy



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Lobbying

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Lobbying

- Communication
- Principal purpose is to influence legislation
- Reflects a view on specific legislation

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Lobbying Examples

- Drafting legislation
- Influencing legislators to introduce legislation
- Distributing lobbying materials
- Telling others to contact legislators to support/ oppose legislation

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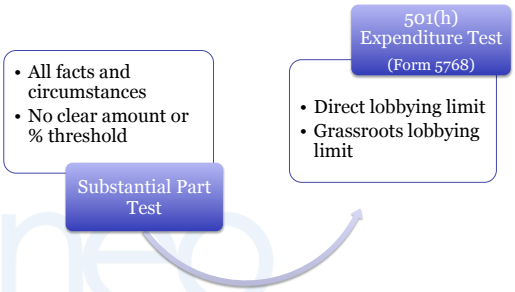
BUT must be insubstantial…



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501(h) Expenditure Limits

- Direct
  - 20% of first $500,000 of EPE
  - 15% of next $500,000 of EPE
  - 10% of next $500,000 of EPE
  - 5% of remaining EPE (over $1.5M) (up to $1 million)
- Grassroots
  - 25% of Total Lobbying Expenditure Limits

EPE = Exempt Purpose Expenditures

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501(h) Exceptions to Lobbying

- Nonpartisan analysis, study or research
- Exams of broad social, economic and similar problems
- Technical advice or assistance to governmental body
- Self-defense communications

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Electioneering

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No Electioneering

- No direct or indirect activities for or against a **candidate** for **public office**
- On all levels – **federal, state, and local**

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Facts and Circumstances

IRS considers factors such as:

- Content
- Timing
- Method of distribution

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Electioneering Penalties

- Revocation of tax-exempt status
- Intermediate penalty tax
- *Warning for minor or inadvertent mistakes?*

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Election-Related Activities

Permissible activities may include:

- Issue Advocacy
- Voter Registration
- Voter Education
- Candidate Education

Remember: IRS will consider all facts and circumstances!

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First Amend. Free Speech and Association

Must be acting in their **individual capacity** and not on behalf of the organization.

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Tips for Organizations

- No support/opposition at an org-sponsored event
- No publication of an individual's election choices
- No use of org's assets or facilities for an individual's electoral work
- Provide policies and training
- Use visible disclaimers

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Affiliated Organizations – Tips

- Have independent board members
- Consider a cost-sharing agreement (if sharing resources)
- Have clear separation between each org's activities
- Provide clear solicitation materials for each org
- Do not use 501(c)(3) assets toward activities not permitted if conducted within the 501(c)(3) itself

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Nonprofit Advocacy – Other regulations

Including:

- Federal, state, and local laws (e.g., Federal Lobbying Disclosure Act and Federal Election Campaign Act)
- Federal and state ethics rules

- Resources: Alliance for Justice
  - *Rules of the Game (2nd edition)*
  - *Influencing Public Policy in the Digital Age*

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