



Philanthropic NEWS

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JOHNSON & JOHNSON SUES AMERICAN RED CROSS OVER CROSS TRADEMARK

Johnson & Johnson has filed a federal lawsuit against the American Red Cross and four of its licensing partners over the rights to the red cross symbol.

The dispute arose when the American Red Cross began licensing its trademark to commercial partners to use on various emergency preparedness products. Johnson & Johnson claims that the American Red Cross only has the right to use the mark in connection with its voluntary relief services and is infringing on their exclusive right to use the cross mark on commercial products being sold in retail stores. The American Red Cross has responded that "Congress and the Federal government have long recognized the right of the charity to use the Red Cross emblem on products sold to support its mission."

Johnson & Johnson filed the lawsuit after months of informal discussions failed to resolve the dispute. Johnson & Johnson had no objection to the American Red

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IRS ISSUES PRIORITY GUIDANCE PLAN

The Department of Treasury and Internal Revenue Service announced their priority guidance plan for 2007-2008. The items relating to tax-exempt organizations are summarized below. This firm will continue to update you as these regulations and guidance are issued in the coming year.

Some of the regulations and rulings the IRS plans to issue include:

- Final regulations under Code Sections 501(c)(3) and 4958 relating to revocation standards for organizations engaging in excess benefit transactions. These regulations will supersede the proposed regulations published on September 9, 2005;
- Final regulations on excise taxes on prohibited tax shelter transactions;
- Regulations relating to the Form 990 revisions;
- Regulations under Code Section 170 regarding substantiation and reporting requirements for charitable contributions adopted by recent legislation;
- Proposed regulations relating to new requirements for supporting organizations as a result of the Pension Protection Act of 2006 ("PPA") and proposed regulations on excise taxes on donor-advised funds resulting from the PPA;

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JOHNSON & JOHNSON SUES AMERICAN RED CROSS

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Cross's sale of products bearing the symbol as part of its fundraising efforts in the past. However, the conflict began in 2004 when the American Red Cross began licensing the red cross mark to commercial partners selling products in retail stores, including emergency preparedness kits and grooming kits. Johnson & Johnson claims that its goal in filing the lawsuit is "to restore the long-held legal boundaries surrounding the use of the Red Cross trademark."

The American Red Cross maintains that providing first aid, health, safety and emergency preparedness products that people can conveniently purchase at places where they regularly shop helps to advance their mission. The organization receives part of the proceeds from sales of those products, currently amounting to less than \$10 million per year, and uses the funds to further support its mission of helping Americans prevent, prepare for, and respond to disasters and emergencies.

CAR SHOW CHARITY EVENT ENDS IN TRAGEDY AND LAWSUITS

A nonprofit's worst nightmare came true in Tennessee in June when six people were killed and a dozen more injured at a Cars for Kids car exhibition and drag race, an annual fundraising event held for the past 18 years. Cars for Kids, now facing a dozen lawsuits and the threat of numerous others, is uninsured. In addition, Cars for Kids is currently under investigation by the state's Division of Charitable Solicitations and Gaming for failing to register with the state and the local District Attorney is contemplating criminal charges against its organizers.

So far, twelve lawsuits seeking \$85 million in damages have been filed on behalf of injured spectators against the charity, the car's driver, the car owner and the city. At least one wrongful death suit has also been filed by the family of a teenager killed seeking \$10 million in damages.

The organizers claimed that they never felt insurance was necessary because they were simply raising money for kids. This tragedy serves as a reminder to nonprofit organizations of all varieties to have the right type of insurance in place to minimize risks of liability.

For more information on insurance coverage for your organization, please contact Cliff Perlman at cliff@perlmanandperlman.com.

IRS PRIORITY GUIDANCE PLAN

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- Proposed regulations under Code Section 170(f)(12) relating to donations of qualified vehicles;
- Proposed regulations under Code Section 664(c) to reflect 2006 legislation concerning the effect of unrelated business income on charitable remainder trusts; and
- Rules pertaining to the e-Postcard notification requirement for organizations not required to file with the IRS.

SUPREME COURT RULES IN FAVOR OF ISSUE ADVOCACY BY NONPROFITS

Last June, the Supreme Court held that the ban on electioneering communications under the Bipartisan Campaign Reform Act (also known as BCRA or, the McCain-Feingold Act) is unconstitutional when applied to issue advocacy advertisements.

The case entitled *Federal Election Commission v. Wisconsin Right to Life, Inc.* involved a 501(c)(4) nonprofit organization, Wisconsin Right to Life ("WRTL"), that was planning to air ads encouraging voters to contact specific Senators to oppose a filibuster blocking federal judicial nominees. WRTL intended to run the ads in the period leading up to the 2004 federal primary election. The Federal Election Commission (FEC) claimed the ads violated the "electioneering communication" ban under BCRA, which makes it a federal crime for any corporation to broadcast any communication that names a federal candidate for elected office and is targeted at the electorate shortly before an election.

The Supreme Court found that WRTL's ads did not constitute express advocacy and that the FEC did not have a sufficiently compelling governmental interest to justify burdening WRTL's speech. In its decision, the Supreme Court distinguished between permissible "issue advocacy" ads, which address public issues in general and are allowed as part of a grassroots lobbying campaign, and "express advocacy" communications, which promote a specific candidate's election or defeat and are prohibited under BCRA in the period immediately prior to an election. Ruling in favor of WRTL, the Court found that the FEC ban on electioneering communications was unconstitutional as applied to WRTL's ads because it

violated WRTL's free speech rights to broadcast issue advocacy advertisements.

To implement the Supreme Court's decision, the FEC has published proposed revisions to its rules governing electioneering communications to exempt this type of issue advocacy from the prohibition. Final rules are expected to be published by the end of November 2007.

IRS RECOMMENDS GOOD GOVERNANCE PRACTICES

The IRS recently released a list of nine proposed "good governance" practices for Section 501(c)(3) organizations. While the list is currently only a draft, and it does not have the force of law, the IRS has stated publicly that it strongly recommends groups adopt these practices. The IRS has also stated that in any review of an organization's tax-exempt status, the extent to which it has voluntarily adopted these practices will be taken into consideration. The recommended practices are:

- **Mission Statement.** The board should adopt a clear mission statement that explains why the charity exists, what it hopes to accomplish, what activities it will undertake, and who it intends to benefit from those activities.
- **Code of Ethics and Whistleblower Policies.** The board should adopt ethics policies that communicate to all personnel a strong culture of legal compliance and ethical integrity. The board should also adopt policies and procedures for handling employee complaints and reports in confidence about suspected financial impropriety or misuse of the charity's resources.
- **Due Diligence/Duty of care.** The Board should see to it that each director: (a) is familiar with the charity's activities and knows whether those activities in fact promote the charity's mission; (b) is fully informed about the charity's finances; and, (c) has the information needed to make informed decisions.
- **Duty of Loyalty/Conflicts of Interest.** The Board should adopt a conflict of interest policy that: (a) requires directors and staff to act solely in the interests of the charity without regard for personal interests; (b) includes written procedures for determining whether a relationship, financial interest, or business affiliation results in a conflict of interest; and, (c) prescribes a certain course of action in the event a conflict of interest is identified. Directors and staff should also be required to disclose annually in writing any known financial interest that the individual, or a member of the individual's family, has in any business entity that transacts business with the charity.
- **Transparency.** The charity's Form 990, annual reports, and financial statements should be complete and accurate, posted on the organization's website, and be made available to the public upon request.
- **Fundraising Policy.** The board should make sure that fundraising solicitations meet federal and state law requirements and solicitation materials are accurate, truthful, and candid. Charities should keep their fundraising costs reasonable. Performance of professional fundraisers should be monitored.
- **Financial Audits.** The Board of every 501(c)(3) organization should adopt a budget at the beginning of each fiscal year. If the charity has substantial assets or annual revenue, the board should insist on an annual audit, with an audit committee to select and oversee the auditor. The auditing firm should be changed periodically (e.g., every five years) to ensure a fresh look at the financial statements.
- **Compensation Practices.** Charities should never pay more than reasonable compensation for services rendered. Charities should generally not compensate persons for service on the board of directors except to reimburse direct expenses of such service. Director compensation should be allowed only when determined appropriate by a committee composed of persons who are not compensated by the charity and have no financial interest in the determination. Charities may pay reasonable compensation for services provided by officers and staff. In determining reasonable compensation, a charity should use one of the "safe harbor" procedures recommended by IRS.
- **Document Retention Policy.** An effective charity should adopt a written policy establishing standards for document integrity, retention, and destruction, including guidelines for handling electronic files. The policy should cover backup procedures, archiving of documents, and regular check-ups of the reliability of the system.

The full text of the draft can be found at:
www.irs.gov/pub/irs-tege/good_governance_practices.pdf

To discuss your current compliance status, please contact Allen Bromberger at 212-889-0575 or send an email to allen@perlmanandperlman.com.

CALIFORNIA ADOPTS NEW PROCEDURE FOR STATE TAX EXEMPTION

In September, California Assembly Bill 897 was adopted, which allows 501(c)(3) organizations that are tax-exempt for federal tax purposes to be treated as tax-exempt organizations for California tax purposes without the need to obtain separate approval from the state. Under existing state law, California requires organizations seeking tax exemption to submit a Form 3500 application for tax exemption and a filing fee. Form 3500 requires the organizations to submit formation documents and a balance sheet, in addition to other information that is duplicative of the requirements on the IRS Form 1023 application for federal tax exemption.

The new law eliminates the requirement for 501(c)(3) organizations that have received federal tax exemption to file a separate Form 3500 application for tax exemption with the California Franchise Tax Board (FTB) for requests made on or after January 1, 2008. Instead, such organizations will be required to submit a copy of their IRS tax-exemption determination letter along with a new Form 3500-A. The new Form 3500-A has not been released yet, however, the California FTB Exempt Organizations Office has told this firm that it would be in the form of a checklist.

The law requires organizations to notify the FTB of a revocation of its tax-exempt status by the IRS, which will automatically result in revocation of the organization's tax-exempt status in the state. In addition, the effective date of an organization's state tax-exempt status will be retroactive to the effective date of federal tax-exemption.

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