



Philanthropic NEWS

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ACRFR FIGHTS FUNDRAISING SOLICITATION LAWS IN UTAH

The American Charities for Reasonable Fundraising Regulation (“ACRFR”) has sued the Director of the Utah Division of Consumer Protection in federal court alleging that Utah’s registration requirement for out-of-state fundraising consultants is unduly burdensome and unconstitutionally stifles free speech. The lawsuit, filed November 12, 2008, further alleges that fundraising consultants do not have sufficient minimum contacts with Utah for the state to exercise jurisdiction over them consistent with constitutional notions of fair play and substantial justice.

Utah’s law requires fundraising consultants to register even though the client and fundraising consultant do not have offices in Utah, do not perform services in Utah, and do not solicit business or charitable contributions in Utah. The only indirect contact these fundraising consultants may have with Utah is that their clients may send materials into Utah. Additionally, many professional fundraising consultants are not aware of the locations to which their charitable clients mail educational and fundraising materials, and therefore do not purposefully direct solicitation materials towards Utah or any other state.

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IRS ANNOUNCES FY 2009 COMPLIANCE INITIATIVES

The Internal Revenue Service’s 2009 compliance projects will include a new charitable spending study, a review of non-cash gift valuation, and an examination of the relationship between governance and IRS compliance.

Charitable spending study. The IRS will conduct a long-range study to learn more about how exempt organizations’ revenue sources and expenditures affect their ability to accomplish their charitable purposes. Some of the sources of revenue to be examined include public contributions, grants, and related and unrelated business income. Types of expenditures to be reviewed include fundraising expenses, officer compensation, and direct and indirect unrelated business income expenses. The IRS is interested in how the different types and amounts of revenue and expenses affect the amount of funds that are available for charitable program activities. Lois Lerner, director of the IRS’s exempt organizations division, has stated that this study is not an attempt to develop a formula for determining if charities are spending enough to accomplish their exempt activities. She stated that the IRS has not yet decided how it will use the information it gathers. The first stage of the initiative will focus on organizations that raise unusually large amounts of money, have unrelated business income, and spend relatively little on their programs.

Gifts in Kind Valuation. The IRS will also look at valuation of certain types of non cash (in-kind) gifts, including pharmaceutical donations, used clothing, and excess inventory of discontinued products. They will also look at how much of these gifts are

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ACRFR FIGHTS LAWS IN UTAH

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ACRFR filed the lawsuit in conjunction with fundraising consultant Rainbow Direct Marketing, LLC (“RDM”). RDM is a professional fundraising counsel whose only office is located in the State of New York. It claims that it has no direct contact with Utah, has no contract with Utah entities and does not market its services or solicit funds in Utah. Nonetheless, the Utah Division of Consumer Protection advised RDM that it must register in the State because one of RDM’s clients had registered in Utah to solicit charitable contributions, and threatened administrative action against RDM if it failed to register.

This case could have serious ramifications for all fundraising consultants and the nonprofit organizations that hire them. Currently, most states have similar laws requiring professional fundraising counsel to register even if the consultant has not directed their clients’ solicitations toward any particular state or geographic area. ACRFR claims that exempting professional fundraising counsel of such registration burdens would greatly reduce costs.

ACRFR is a nonprofit organization whose members and supporters include many charities, professional fundraisers, and fundraising counsel and consultants. The organization’s mission is to combat excessive regulation of nonprofits and fundraising by means of litigation.

ACRFR previously brought a case in federal court in Florida over a county ordinance that required fundraising consultants who work with charities seeking donations from county residents to register. In that case, the 11th Circuit did not find sufficient evidence in the record to establish that the consultants had the minimum contacts required for the county to assert legislative jurisdiction over them, noting that none of the fundraising consultants’ activities indicated that they “purposefully aid[ed] the solicitation of funds from the citizens of Pinellas County, in particular as opposed to general solicitations conducted more or less nationally. An abstract, indirect, and unaimed level of involvement with the [jurisdiction] would not be sufficient for the [jurisdiction] to regulate the consultants.”

This case could set a precedent in changing state fundraising and solicitation laws and their overbroad application by state regulators. This firm will be closely following this case and will report any significant developments that may affect charities’ and fundraising consultants’ obligations in complying with state solicitation laws.

IRS ANNOUNCES INITIATIVES

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then donated to other charities. The IRS will focus on the valuation of the non-cash gifts, the expenditures involved in the transactions, and the accuracy of the reporting on Form 990.

Governance and compliance. The IRS will continue emphasizing improved nonprofit governance by focusing on three areas. First, it will develop a checklist that will help examiners determine whether an organization’s governance practices affect its tax compliance. The checklist will also serve as an educational tool for organizations to learn about recommended governance practices. Second, the IRS will train its employees about how nonprofit governance affects determinations, rulings and agreements. Third, the IRS will look for ways to correlate responses to Form 990 governance questions with other Form 990 information in possible compliance initiatives. For example, the IRS may look at whether an organization has adopted procedures for reviewing executive compensation when reviewing the amount of executive compensation reported in the Form 990. The IRS may also look at how organizations regularly monitor and enforce compliance with their conflict of interest policy, particularly if they reported making significant loans to officers or employees.

To review the full summary of these compliance initiatives, go to http://www.irs.gov/pub/irs-tege/finalannualrptworkplan11_25_08.pdf.

LOS ANGELES ART MUSEUM FACES FINANCIAL TROUBLE

The Museum of Contemporary Art, Los Angeles (MOCA) made headlines recently when it was reported that the museum had been operating at a deficit for six of the last eight years and had spent down its endowment, valued at about \$40 million ten years ago, to \$6 million. According to a statement published by MOCA, the California Attorney General’s Office is conducting an audit to determine whether MOCA violated the terms of restricted gifts by using restricted funds for general operating purposes. As a 501(c)(3) tax-exempt charitable organization, the museum is required to use any restricted contributions only for the purposes specified by the donor. Failing to do so can subject a charity to scrutiny by state regulators as well as the Internal Revenue Service.

Facing severe financial trouble, MOCA’s Board has been considering its options for its long term existence. Among its options, the Los Angeles County Museum of

Art, a rival museum in the L.A.-area, made a formal proposal to merge the two institutions. However, MOCA recently announced that its Board of Trustees voted instead to accept a “challenge” grant from the Eli and Edyth Broad Foundation for endowment replenishment. Under the grant, the Broad Foundation will provide \$15 million over the next five years and will match up to \$15 million raised and received by the museum. In conjunction with the announcement of the grant, the museum kicked-off a major fundraising campaign for endowment and operating expenses and has publicized commitments of sizeable gifts from its trustees.

The Board also announced that the museum’s director, Jeremy Strick, has resigned after a nine-year tenure and a new chief executive officer, Charles Young, has been appointed to oversee the day-to-day operations of the museum. Mr. Young will work closely with a newly formed advisory committee comprised of leaders in the field of museum management and finance to address the challenges ahead.

CHARITY NAVIGATOR ANNOUNCES NEW RATING CRITERIA

Charity Navigator has announced that it will attempt to develop a measurement for charitable outcome to add to its rating system for evaluating charities. Ken Berger, President and CEO of Charity Navigator, defines “outcomes” as “the events, occurrences or changes in conditions, behavior, or attitudes that indicate progress toward achievement of the mission and objectives of the program. Thus, outcomes are linked to the program’s (and its agency’s) overall mission – its reason for existing.”

Charity Navigator awards charities a rating of zero to four stars based on criteria that purportedly reflects an organization’s financial health. Currently the ratings are based on two categories, organizational efficiency, which is largely determined by administrative and fundraising expenses, and organizational capacity, which measures an organization’s sustainability of its programs over time based on primary revenue growth, program expense growth, and the working capital ratio. These analyses are based on financial information derived from organizations’ IRS Form 990s.

Charity Navigator has always advised donors against using its ratings as the *only* factor in deciding whether to support a particular organization, and recommends donors also gather information from other sources about an organization’s programmatic impact. However, Charity Navigator is finally recognizing that donors are not taking

the additional steps recommended to assess outcomes, and are depending almost entirely on its ratings.

Charity Navigator is only beginning the process of developing this new outcome measurement, and stated that it could take not just months, but perhaps years to develop a meaningful tool that is broad enough to evaluate all types of charities without being overly complicated. An outcome measurement will take time to develop because there is no standardized data source, such as the Form 990, from which to gather this information, and Charity Navigator anticipates that it will probably need to gather the information directly from the charities it evaluates.

To read Ken Berger’s full blog on this new outcome measurement, go to <http://www.kenscommentary.org/2008/12/measure-of-outcome.html>.

IRS ENCOURAGES ADOPTION OF GOVERNANCE POLICIES

This firm sent out a Client Alert in October highlighting the redesigned Form 990’s new section on governance policies and disclosure requirements, which asks organizations to answer whether they have adopted written policies on conflicts of interest, whistleblower protection, document retention and destruction, gift acceptance, executive compensation, and joint venture participation. In order to answer these questions affirmatively in the 2008 Form 990, organizations must have adopted the policies by the end of its 2008 fiscal year. Organizations with a calendar fiscal year that did not adopt these policies by the end of 2008 should still consider adopting the policies in 2009 in order to respond affirmatively to the questions in the 2009 Form 990. While the IRS does not require organizations to adopt these policies, not having them in place could subject an organization to enhanced scrutiny by the IRS.

This firm can provide organizations with sample policies, procedures and guidelines that would allow an organization to respond affirmatively to the new governance questions on the redesigned Form 990, as well as assist in tailoring the policies to fit your organization’s individual needs. If you would like advice on whether adopting specific policies is appropriate for your organization, or need assistance in preparing any of these policies and procedures, please contact Karen Chang at Karen@perlmanandperlman.com.

UPCOMING SPEAKER EVENTS AND ANNOUNCEMENTS

SETH PERLMAN will be speaking at the Practising Law Institute about Internet Fundraising and Cause Related Marketing on February 4, 2009 in New York City. He will also be speaking at the Association of Fundraising Professionals Conference about State Oversight of Charity Activities on March 30, 2009 in New Orleans, Louisiana.

ALLEN BROMBERGER and **BARBARA NAGEL** will be giving a workshop about Financing Social Ventures at the Social Enterprise Alliance Summit on April 16, 2009 in New Orleans, Louisiana. Allen will also be participating in the Social Venture Network Annual Conference with Seth Perlman on April 23 - 29, 2009 in Itasca, Illinois.

CATHERINE OETGEN co-authored an article entitled "Conflicting Interests: Practical Tips on What to Do and How to Do It" published in the *Nonprofit Times* in November. The article discusses challenges charitable organizations face when dealing with conflicts of interest and gives ideas of how charities can handle conflict situations appropriately. Catherine also co-authored a chapter on legal issues facing volunteer board members in *Governance for Health Care Providers: The Call to Leadership* published by Productivity Press in December. For copies of these recent publications, please contact Catherine at catherine@perlmanandperlman.com.

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