

The Plain & Simple

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State Law Update

New York Attorney General Wins Judgment Against Grasso: The New York State Supreme Court ordered Richard A. Grasso, former head of the New York Stock Exchange, to return \$87 million (plus interest and other amounts) which he received as part of a \$139.5 million payout prior to his departure from the company. That payout reflected, to a significant extent, Mr. Grasso's alleged interest in retirement funds, which he withdrew in a lump sum. In a decision dated October 18, 2006, Honorable Charles E. Ramos found that Mr. Grasso's withdrawal of funds was improper (except for the monies which reflected deferred compensation, to which he was entitled), that Grasso had a fiduciary duty to disclose to the board the magnitude of his pension benefits, and that he breached that duty by failing to make the required disclosure. The court found that "[y]ear after year, [the board] made decisions to pay him without knowing his true compensation." It is anticipated that the imminent trial on the remaining legal issues, including the key question of whether Grasso's overall compensation package was unreasonable, will be delayed while the ruling is appealed.

New York's Dissolution Simplification Law Being Implemented: The New York State legislature passed a bill in June of 2005, proposed by New York Attorney General Spitzer with widespread support in the not-for-profit sector, which provides for simplification and streamlining of the dissolution process for New York charitable corporations. For almost a decade, New York charities (with the support of the Association of the Bar of the City of New York and the Nonprofit Coordinating Committee) had been urging the State to simplify New York's cumbersome dissolution process, which had required charities with assets to make two court appearances. The bill, signed into law by Governor Pataki in October of 2005, by its terms became effective as of April 9, 2006 (six months after enactment). The Attorney General has recently posted on its website updated forms and instructions implementing the new statutory provisions, which can be accessed at <http://www.oag.state.ny.us/charities/forms/charindex.html>.

Federal Law Update

Pension Protection Act Of 2006 Impacts On Charities: The Pension Protection Act of 2006 (the "Act"), signed into law by President Bush on August 17, 2006, has numerous provisions which could have a significant impact on charitable organizations. Some portions of the Act are unclear, ambiguous, or imprecise, suggesting that guidance from the IRS might be appropriate. We summarize here just a few of the significant aspects of the new legislation:

- A. IRA rollover: For two years, individuals age 70.5 and older may make charitable donations of up to \$100,000 from an IRA without the need to count the donation as taxable income.
- B. Expanded tax deductions are allowed for contributions of book and food inventory and certain conservation contributions.
- C. Unrelated business income tax returns must now be disclosed and made available for public inspection.
- D. Excise tax penalties for private foundations (including self-dealing, failure to make the minimum 5% annual payout, jeopardizing expenses, and taxable expenditures) and excess benefits are doubled.

E. New requirements are imposed on donor advised funds, supporting organizations (particularly type 3 SOs) and credit counseling organizations. For the first time, donor advised funds are defined in the Internal Revenue Code.

F. Charitable contribution deduction limitations are imposed with respect to contributions of money, clothing, household goods, and certain other items.

G. Exempt organizations with gross receipts under \$25,000 must file with the IRS an annual notice beginning in 2008.

Updated Treasury Department Financing Guidelines On Terrorist Activity: On September 29, 2006, the Treasury Department issued a revised version of its 2002 anti-terrorist financing guidelines describing "Voluntary Best Practices for U.S.- Based Charities." These guidelines assist United States based charities in complying with the various requirements restricting funding which directly or indirectly supports terrorist organizations. A copy of the guidelines is available through the following link <http://www.treasury.gov/press/releases/reports/0929%20finalrevised.pdf>. It is important for charities supporting international programs to be aware of these guidelines, and it is advisable for directors to consider adopting policies and undertaking due diligence in connection with any grant being made overseas. Such organizations must be aware of the various laws (such as the US Patriot Act of 2001) and executive orders (such as Executive Order 13224) which govern the making of grants overseas including, violations of which could lead to civil and criminal penalties as well as revocation of tax exempt status.

IRS Enforcement Action Reversed On Appeal: In Caracci, et al. v. Commissioner of Internal Revenue, the Fifth Circuit Court of Appeals reversed a prior US Tax Court ruling (118 T.C. 25) obtained by the IRS, which had supported the IRS' contention that "Sta-Home Health Agencies of Carthage, Greenwood, and Jackson, Miss., which provide home health care and other health services, had sold their assets too cheaply to for-profit corporations and ordered the corporations to repay the nonprofit groups \$5.2 million, plus penalties that could reach up to \$1.25 million." (Chronicle of Philanthropy, 11/14/02, p. 32) In a major setback for the IRS, the Fifth Circuit Court of Appeals, in a decision dated July 11, 2006 (reported at 456 F.3d 444) criticized certain factual and legal errors made by the IRS and the Tax Court. The Caracci case represented a major enforcement effort by the IRS under the intermediate sanctions law applicable to public charities (IRC Section 4958).

IRS Action Against Illegal Political Activity: The IRS has issued a reminder to charities that they must avoid involvement in political campaign activity during the 2006 elections, consistent with the legal prohibition of such activity under Code Section 501(c)(3). The Service had noticed an increase in such activity during the 2004 elections. The prohibition extends to a full range of charities, including religious and educational groups. The IRS has launched an enforcement program, the Political Activity Compliance Initiative, to investigate certain allegations of wrongdoing. In a separate development, it was announced that in August of 2006 the IRS had dropped its widely publicized investigation into possible illegal campaign activity by the NAACP prior to the 2004 presidential election. That investigation emanated from a speech highly critical of President Bush given by Julian Bond, Chairman of the group, in July of 2004.

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