

The Plain & Simple

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Tax Exempt Law

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Additional Provisions of the Pension Protection Act of 2006 Now Effective

The Pension Protection Act of 2006 (the "Act"), signed into law by President Bush on August 17, 2006, contains a number of changes that will have a major impact on many nonprofit organizations. While some provisions became effective immediately upon enactment (such as the IRA charitable rollover, the biggest giving incentive in the Act), a number of important reforms just became effective on January 1, 2007, including the following:

1. **Public Charities.** The maximum penalty on organization managers for participation in excess benefit transactions is doubled, from \$10,000 per transaction (in the aggregate) to \$20,000 per transaction.
2. **Private Foundations.** For acts of self-dealing between a private foundation and a disqualified person, the Act doubles the initial tax on the self dealer from 5% to 10% of the amount involved. In addition, the Act doubles the initial tax on foundation managers from 2.5% to 5% of the amount involved, and doubles the amount of the taxes on foundation managers for self-dealing transactions to \$20,000 per act (in the aggregate).
3. **Donor Advised Funds.** The making of a "taxable distribution" (i.e. a distribution to a natural person, or to any other organization or entity for purposes that are not charitable) from a donor advised fund, as newly defined by the Act, will subject the sponsoring organization to an excise tax equal to 20% of the amount of the taxable distribution. The manager of the sponsoring organization is subject to an excise tax equal to 5% of the amount of the distribution (not to exceed \$10,000 per taxable distribution).

In addition to these and the IRA rollover provision, other important provisions in the Act which became effective immediately on the enactment date include: (i) increased reporting obligations are imposed on all 501(c)(3) organizations; (ii) certain grants to certain supporting organizations will no longer count as qualifying distributions toward a private foundation's minimum distribution requirement and instead will be treated as taxable expenditures unless expenditure responsibility procedures are applied; (iii) the thresholds for donors making substantial and gross overstatement of the valuations of property given to charity are lowered; (iv) the entire amount of compensation paid by a donor advised fund to a disqualified person (as defined under Section 4958 of the Code) will be deemed an excess benefit transaction; and (v) every supporting organization is now required to file an annual information return indicating which type of supporting organization it is and identifying its supported organization.

NYS Bar Association Approves Comprehensive Amendments to Not-for-Profit Corporation Law

On January 26, 2007, the NYS Bar Association's House of Delegates approved a proposal of the Business Law Section, Committee on Corporations, to substantially revise and modernize the NPCL. The approval was given with the understanding that the Committee will consult with the New York City Bar Association (which had reviewed and commented on the proposal) during the next 60 days to gain their support, and to seek input and acceptance from the broader nonprofit constituencies throughout the State.

This project began several years ago to conform the NPCL to certain of the changes made to the Business Corporation Law which would improve the NPCL if applied. The project grew in scope, and the goals were modified to address other provisions that have concerned practitioners and academics, and have made New York a less likely destination for the incorporation of not-for-profit corporations. The proposal will include basic changes deemed non-controversial such as making the statute gender neutral, changing the name of the statute, and allowing for electronic notice in certain circumstances. Proposed changes that may provoke debate include eliminating corporate types and altering methods of financing not-for-profit corporations.

Independent Sector Committee Proposes Self Regulation For Charities

Independent Sector's Advisory Committee on Self Regulation has recently published for public comment a list of 29 principles of effective practice for charitable organizations (the "Principles"). Comprised of 34 leaders from public charities, foundations and academic institutions, the Advisory Committee developed its draft after examining standards and principles established by more than 50 self-regulation and accreditation systems that monitor different types of charitable organizations. The public comment period ended on February 2, 2007, and it is anticipated that the Advisory Committee will finalize and recommend the Principles to Independent Sector's Panel on the Nonprofit Sector this Spring.

In 2004, the US Senate Finance Committee, led by its then Chairman Charles Grassley (R-Iowa), began holding hearings to consider sweeping legislation which would impose greater accountability, financial controls and governance reforms on charitable organizations. In the face of widespread opposition, Senator Grassley encouraged Independent Sector to establish the Panel on the Nonprofit Sector, an independent group of nonprofit leaders. The Panel issued a series of reports recommending action by Congress and the IRS, as well as voluntary best practices for charitable organizations to strengthen their transparency, governance, and accountability.

The Principles are arranged into four general categories: "Facilitating Legal Compliance," "Effective Governance," "Strong Financial Oversight," and "Responsible Fundraising." The Committee is recommending that all charitable organizations aspire to follow these principles, but particularly public charities with at least \$1 million in annual revenues and private foundations with at least \$25 million in assets. This edition of the Plain and Simple will highlight the category of Facilitating Legal Compliance; our next edition will address the three other categories.

In terms of legal compliance, the Principles recommend that charitable organizations (i) be knowledgeable about and comply with all applicable laws and regulations and international conventions, (ii) have a governing body that is responsible for reviewing and approving the annual budget, key financial transactions, compensation practices, and fiscal and governance policies, (iii) adopt and implement policies to ensure that actual or apparent conflicts of interest are appropriately managed, (iv) establish and implement policies and procedures that enable "whistle blowers" to come forward without fear of retaliation, (v) establish and implement policies and procedures to protect the organization's important documents and business records, and (vi) make information about its operations, board members, finances, programs and activities, and methods for evaluating performance publicly available.

For more information or detail about the Principles, or to discuss your organization's legal compliance responsibilities, please contact the Tax Exempt Organizations group.

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