



NON-PROFIT MANAGEMENT UPDATE

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CASE DEVELOPMENTS

Provided by

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CASE DEVELOPMENTS

OPEN MEETINGS AND PUBLIC RECORDS LAWS

Nonprofit corporations may be subject to the disclosure requirements in the Tennessee Public Records Act (“the Act”) if, based on the totality of the circumstances, the organizations are the functional equivalent of a governmental agency. The Act requires access to public or state records, i.e., “all documents made or received pursuant to law or ordinance or in connection with the transaction of official business by any governmental agency.” A nonprofit medical foundation was found to be the functional equivalent of a governmental agency – and thus subject to the records disclosure requirements in the Act – where, among other things, the Foundation provided educational and administrative services that a public medical university would otherwise perform, received significant funding from a public medical university, and engaged in additional activities that furthered the university’s mission. *See Gautreaux v. Internal Med. Educ. Found., Inc.*, No. E2008-01473-COA-R3-CV, 2009 Tenn. App. LEXIS 729 (Tenn. Ct. App. Oct. 30, 2009).

JUDICIAL DEFERENCE TO MEMBERSHIP DISCIPLINE BY PRIVATE NONPROFIT CLUB

A Kansas appellate court found that courts generally should defer to social clubs in matters of membership discipline provided there is substantial compliance with the club’s bylaws. After a former member of a nonprofit country club was expelled due to loud and offensive language, he filed suit against the club. When appealing the lower court’s grant of summary judgment for the club, the former member asserted that there had been a violation of his due process rights, breach of contract, and breach of the

implied duty of good faith and fair dealing. The Court of Appeals of Kansas first found that the former member had not shown any state (governmental) action which caused his expulsion, and therefore concluded that no violation of due process had occurred. Second, the court concluded that the club conducted its disciplinary proceedings in substantial compliance with its bylaws, rules, and regulations, and that the former member had therefore failed to show a breach of contract. Third, with respect to the claim for breach of implied duty of good faith and fair dealing, the court concluded that, because no grounds existed for judicial questioning of the regularity or sufficiency of the club board’s decision to expel the former member, summary judgment upholding the club’s decision to expel the member was appropriate. *See Pollock v. Crestview Country Club Ass’n*, 205 P.3d 1283 (Kan. Ct. App. 2009).

STANDING TO SUE NONPROFIT PUBLIC BENEFIT CORPORATION

The primary responsibility for protection of assets held by charitable trusts and public benefit corporations in California resides in the state Attorney General. A California appellate court therefore concluded that plaintiff, a staff doctor with a nonprofit benefit corporation, did not have standing to sue the nonprofit for a full accounting of its assets and/or for a declaration that a hospital operated by the nonprofit could not be sold to a for-profit entity. The court also noted that the doctor did not have a special interest in the management of the nonprofit’s affairs, and was not a trustee, director, or special donor with any continuing property interest in his donations to the nonprofit and thus had no other unique basis to assert standing to sue the nonprofit. *See Klein v. Anaheim Mem. Hosp. Ass’n*, No. G040829, 2009 Cal. App. Unpub. LEXIS 8072 (Cal. Ct. App. Oct. 8, 2009).

EXCESS COMPENSATION OF NONPROFIT CORPORATION BOARD MEMBER

A Texas appeals court upheld a jury's order that a former president of the board of directors of a nonprofit corporation and tax-exempt charitable private foundation, disgorge \$5.3 million in excess compensation that he and other board members allegedly authorized for themselves. The court found a contract requiring the foundation to pay the Board President compensation in excess of reasonable compensation for services rendered was void as a matter of public policy. The court also found that the contract was void as its enforcement would injure the public good by rewarding the Board President for participating in fraudulent or illegal activity. However, the court overturned the trial jury's award of \$10.3 million in punitive damages, finding that the jury had failed to find clear and convincing evidence that the Board President had acted with malice. See *Yeckel v. Abbott*, No. 03-04-00713-CV, 2009 Tex. App. LEXIS 3881 (Tex. App. June 4, 2009).

NONPROFITS AS BUSINESSES

The Supreme Court of Pennsylvania has determined that the term "business" under the Pennsylvania Public Official and Employee Ethics Act ("the Act") should be interpreted to include nonprofit entities. The Act, among other things, prohibits public officials from engaging in conduct that constitutes a conflict of interest. The court reasoned that a liberal interpretation of the term "business" was necessary to assure citizens that the private financial interests of public officials would not undermine the honest discharge of those officials' duties. See *Rendell v. Pa. State Ethics Comm'n*, Nos. 82 MAP 2008, 83 MAP 2008, 2009 Pa. LEXIS 2491 (Pa. Nov. 30, 2009).

NONPROFIT EXPENDITURES ON ELECTION-RELATED ACTIVITIES

A federal appellate court has ruled that the First Amendment permits nonprofits, like individuals, but unlike political parties, to spend unlimited amounts out of their soft-money accounts for election-related activities. The court explained that the United States Supreme Court has generally approved statutory limits on contributions to candidates and political parties as consistent with the First Amendment, but has rejected expenditure limits on individuals, groups, candidates, and parties, even though expenditures may confer benefits on candidates. Therefore, the court agreed with a plaintiff nonprofit group that challenged various Federal Election Commission ("FEC") regulations dictating that nonprofits pay for most election-related activities out of their hard-

money accounts as violating the First Amendment. The court further found that three of the challenged regulations exceeded the FEC's authority under the Federal Election Campaign Act. See *Emily's List v. FEC*, 581 F.3d 1 (D.C. Cir. 2009).

LEGISLATIVE DEVELOPMENTS

EDWARD M. KENNEDY SERVE AMERICA ACT

The Edward M. Kennedy Serve America Act ("the Act") was signed into law by President Obama on April 21, 2009. See Pub. L. No. 11-013, HR 1388. The legislation is a milestone for the national service movement and the largest expansion of civilian service since the Depression. According to its proponents, the Act will dramatically expand national and community service programs and strengthen the infrastructure for volunteerism within the nonprofit community. The Act includes a Nonprofit Capacity Building Program, a \$50 million, 5-year federal matching grant program under which nonprofit intermediaries that raise \$200,000 in matching grant funds can apply for a federal matching grant to provide organizational developmental assistance to small and midsize nonprofits. While the Act took effect on October 1, 2009, many new authorizations must undergo rulemaking before they go into effect. Other authorizations will become effective immediately, but the processes for implementing these provisions will require rulemaking. A list of effective dates of various provisions of the Act is available at:

<http://www.nationalserviceresources.org/effective-dates-serve-america-act-provisions>.

IRS GUIDANCE ON FORM 990 SCHEDULES A and L

The IRS recently compiled Frequently Asked Questions ("FAQs") and answers regarding Schedule A and Schedule L filings on its website. The IRS guidance addressed concerns about how to properly report an organization's public support or public charity classification or transactions with interested persons. The guidance for Schedules A and L is available at: http://www.irs.gov/pub/irs-tege/schedulea_faqs_11_2009.pdf and http://www.irs.gov/pub/irs-tege/sch_l_faqs_tips.pdf

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