

## NEW LEGISLATIVE DEVELOPMENTS AFFECTING CHARITIES

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### Federal Tax Law.

The Senate Finance Committee is expected to hold hearings on April 5, 2005, regarding possible legislation affecting charities. Senate staff have suggested that press and Internal Revenue Service ("IRS") reports of abuses require prompt legislative action, which may also provide revenue raisers to help address the federal budget shortfall. The hearings will be a continuation of the Committee's June 22, 2004, hearings and the Committee Staff's "White Paper" on best practices and potential legislative reforms for tax-exempt organizations. That hearing and White Paper are available at the Senate Finance Committee's website ([www.finance.senate.gov/sitepages/2004HearingF.htm/hearings2004.htm](http://www.finance.senate.gov/sitepages/2004HearingF.htm/hearings2004.htm)).

Among the White Paper's suggestions which attracted the most attention are to:

- (1) extend to public charities the self-dealing rules now applicable to private foundations, which could effectively block many common contract and lease arrangements between public charities and their officers and directors, and
- (2) eliminate fair-market-value deductions for contributions to public charities of gifts of closely-held securities, partnership interests, real property, and tangible personal property. With limited exceptions, those gifts would be deductible only at the donor's cost basis, not a higher fair market value (as is currently allowed for gifts to public charities, provided the value is supported by a qualified appraisal). Many fear that this proposal could reduce charitable contributions, especially in communities where gifts other than cash and publicly-traded securities are popular.

On January 27, 2005, the Joint Committee on Taxation Staff released a report entitled "Options to Improve Tax Compliance and Reform Tax Expenditures," which contains over 100 pages on charity and charitable-deduction reforms. The Report is available on the Joint Committee's website ([www.house.gov/jct/s-2-05.pdf](http://www.house.gov/jct/s-2-05.pdf)). In addition to rolling back the fair-market-value deduction, the Report proposes to eliminate the rebuttable presumption of reasonableness now available to public charity officials seeking a safe harbor against excess-benefit transaction taxes.

On March 1, 2005, the Panel on the Nonprofit Sector convened by Independent Sector released its "Interim Report presented to the Senate Finance Committee." The Panel's Interim Report is available at its website ([www.nonprofitpanel.org/interim](http://www.nonprofitpanel.org/interim)). The 69-page Interim Report addresses suggestions from both the Senate Finance Committee Staff White Paper and the Joint Committee on Taxation Staff. Among other things, it comments on accountability and

governance, including suggestions regarding donor-advised funds, opposition to the Senate Staff proposal to repeal rather than reform certain supporting organizations, and an expression of "deep reservations" regarding the proposal to limit fair-market-value deductions for gifts to public charities. ("The effect of this proposal could be to eliminate a significant source of contributions to charities.")

IRS Commissioner Mark Everson has identified increased charities enforcement as one of his highest priorities. In a speech given on March 15, 2005, Commissioner Everson reiterated his administration's focus on discouraging and deterring noncompliance by tax-exempt entities and their misuse by third parties for tax-avoidance purposes. The text of his speech is available at [www.natptax.com/ir2005-30.pdf](http://www.natptax.com/ir2005-30.pdf). The IRS has recently stepped up audits of charities, especially regarding compensation and potentially abusive arrangements with donors, directors, and officers. If federal hearings proceed on April 5, Commissioner Everson might be expected to testify regarding preliminary findings from those audits.

We believe that the likelihood of new federal legislation is high. As recently as last week, however, Congressional staff indicated informally that they have not received much feedback from charities outside of the Panel on the Nonprofit Sector. This suggested to them that charities' concern about new legislation is low. Therefore, charities that do have concerns about potential legislation should consider the following steps:

- (1) identify the proposals from the White Paper, Joint Committee Report, and Interim Report of greatest concern to their organizations and communicate those concerns and constructive comments to legislative staff;
- (2) share concerns and comments with other similarly situated organizations and with staff of umbrella or affinity groups; and
- (3) monitor continuing developments.

New York State Law.

On March 7, 2005, New York State Attorney General Eliot Spitzer released his proposals to amend the Not-for-Profit Corporation Law and Article 7-A of the Executive Law (governing fundraising for charities). The five proposals are posted at [www.oag.state.ny.us/charities/legislation](http://www.oag.state.ny.us/charities/legislation).

We believe these proposals represent improvement over prior proposals. For example, the proposed legislation would encourage (but not require) boards to designate executive committees if they have more than 25 members, and audit committees if they have more than \$2 million in revenue and support and have audited financial statements. The proposals would also create a new provision requiring certain not-for-profit corporations to maintain a system of internal financial controls designed to reasonably ensure the identification of incorrect financial information in annual reports and the reporting of fraud against the corporation. The proposals

also include proposed revisions to the conflict-of-interest provisions to establish a presumption of fairness where appropriate disclosures are made and due diligence is performed.

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