NONPROFIT LAW
COURSE SYLLABUS: FALL 2008

Course Coverage:

This is a course in the legal issues raised in governing a nonprofit organization, primarily a charity. We will focus on the appropriate considerations of State corporate and trust law and Federal tax law, as well as some State tax issues and Federal election law issues if we have time. We will also study First Amendment protections relating to association and charitable solicitation. Additional legal issues implicated in running a nonprofit, such as employment law and torts, are generally beyond the scope of this course.

Class Assignments:

Because the law in this area is so rapidly evolving, both in prescription and practice, we will rely heavily on works-in-progress and materials available on the Web. Initially, you need:


   This Guide is supplemented by a CD-ROM containing primary sources – case law, statutes and regulations, and other material. See index to assigned material, by class number, after this Syllabus.

2. ALI Nonprofit Law Draft: We will read selections from the draft I’m preparing as Reporter for the American Law Institute’s project on Principles of the Law of Nonprofit Organizations. Caveat: Only some portions of this draft have not yet been submitted to the ALI (and even those portions are subject to revision); however, all of it reflects feedback from the project’s Advisers, ALI Members Consultative Group, and others. Your suggestions will be most timely and welcome!

3. My photocopied set of Supplemental Material: Besides this Syllabus, this packet contains additional authorities, forms, commentary, and news stories. These pages are numbered by the Assignment to which they relate; unless otherwise indicated, each numbered assignment will take about one class hour. We will, of course, slow down or speed up as necessary.

   Note: You have two ways to access the assigned Internal Revenue Code sections we will read: at the beginning of the Supplementary Material is a document called “Code & Regs”, and the Guide’s CD-ROM, under Chapters 6 and 7, contains longer versions. By contrast, only two of the Treasury Department regulations (one amended in 2008) appear in the Supplement; the rest are only on the CD-ROM.
4. **Course Website:** Additional assigned documents are available as Online Course Materials (http://www.kentlaw.edu/classes/ebrody). The Course Webpage also has links to the following key sites, which you should access where assigned and monitor for developments:

   - http://www.irs.gov/charities (with material on all types of tax-exempt organizations)
   - http://www.charitygovernance.com (maintained by Jack Siegel)
   - http://www.sos.state.il.us/services/services_business.html (Ill. Sec. State)
   - http://www.ag.state.il.us/charities (Illinois Attorney General, Charities Division)
   - http://www./philanthropy.com/news (links to news stories on nonprofits)
   - http://www.guidestar.org (all filed IRS Form 990s for charities) (free registration)

**Buddy System:**

To make your preparation for class more effective, you must form into groups of two or three. Pick your own co-counsel, or, if you wish, come to me and I’ll pair you off. Let me know who your co-counsel are. You should meet with each other regularly to discuss the material.

**Assignments, Attendance, Preparation, Exam, and Grade:**

We meet three times a week, on Mondays, Tuesdays, and Wednesdays, from 1:55 - 2:50.

Given the size of our class, I will rotate you and your co-counsel(s) through the assignments to be prepared to be “lead discussant” on the day’s topics. Of course, all of you are required to prepare the material assigned for each class, and to be ready to discuss the material. If you’re unprepared, at least come to class, but let me know.

The grade will be based primarily on your exam. The exam will be 3 hours long, and completely open-book. I reserve the right to raise or lower your grade up to one full grade point based on the quantity and quality of your class participation. You may take this course pass/fail.

Get organized; *keep up*; and contact me with questions (preferably with your co-counsel).

**LEGAL LANDSCAPE FOR NONPROFIT ORGANIZATION**

1. **Overview of the Legal Landscape for Nonprofit Organizations**


Charities,” Supp. at 1-13 through 1-16.
To see what information we can readily learn about a charity, skim the
Smithsonian Institution’s 2006 Form 990, Supp. at 1-17 through 1-32.

2. Private Associations: Constitutional and Policy Issues
(This topic will take two class hours.)

ALI Draft: § 110 (Autonomy and Public Policy Limitations).

Guide: Chapter 3, Organization Basics, part (c), “Members,” at pp. 43-51;
skim Chapter 8, Other Benefits, “Federal Funding for Faith-Based
Organizations,” at pp. 403-10.

Supp.: State ex Rel. Grant v. Brown and Association for the Preservation of
Freedom of Choice v. Shapiro, Supp. at 2-1 through 2-10;
excerpts from Boy Scouts of America v. Dale., Supp. at 2-11 through 2-26;

CD-ROM: Under Ch. 3, you can the full text of Boy Scouts (at \Associative Rights);
under Ch. 6, skim Bob Jones University (at \Charitable), especially pp. 11-13 (majority opinion) and pp. 20-21 (Powell’s famous concurrence).

3. Charitable and Nonprofit Purposes

ALI Draft: § 210 (Charitable Purposes and Activities).

Web: Read Article 3 (Purposes and Powers) in the Illinois Not-for-Profit
Corporation Act, available on the Secretary of State’s website (from the
course Website, go to http://www.sos.state.il.us/departments/business_services/home.html and
click on “Business Organization Acts,” and then click on

Guide: Chapter 6, Tax Exemption: Introduction and “Tax Exempt Entities,” at
pp. 219-29; and “Terrorism and the Non-Profit Sector,” at pp. 325-27.

Note: We consider tax exemption beginning with Assignment 19.
We will cover political and lobbying activity in Assignment 22 and
the prohibition on “private inurement” in Assignment 20.

Supp.: Marsh v. Frost National Bank, Supp. at 3-1 through 3-6; news stories on
terrorist activities, Supp. at 3-7 through 3-14; Helmsley dog trust, Supp. At 3-15 through 3-17; anti-immigration group, Supp. at 3-18 through 3-20.

4. **Organizational Form: Comparing Charitable Trusts and Nonprofit Corporations**

   **ALI Draft:** § 200 (Choice of Form and State of Organization).

   **Guide:** Chapter 3, *Organization Basics*: pp. 23-31 (choice of form; the players) and pp. 35-43 (directors and officers).

   **CD-ROM:** Under Ch. 4: Director Removal, *Oberly v. Kirby* – especially footnote 15.

   **Supp.:** Brody and Brody & Fremont-Smith on the Model Nonprofit Corporation Act, Third Edition (Jan. 2008 Exposure Draft), Supp. at 4-1 through 4-12.

5. **The Corporate Form: Registration and Reporting.**

   *This topic will take two class hours.*

   **ALI Draft:** § 320 (Board Responsibilities, Functions, and Composition). (We examine board duties more thoroughly in the next few classes.)


   **Web:** Go to the Charities Bureau on the Illinois Attorney General’s website (from our Course Website, click on http://www.ag.state.il.us/charities).

   **Read:**
   1. FAQs;
   2. Filing Requirements;
   3. Registration and Annual Report Forms;
   4. Rules and Statutes (just skim the Charitable Trust Act; recall from Assignment 3 that the Not-for-Profit Corporation Act is on the Secretary of State’s website);
   5. Forming a Charitable Organization;
   6. Volunteer Board Members of Illinois Not-for-Profit Orgs.

   Go to the Secretary of State’s website (from the Course Website, click on http://www.sos.state.il.us/services/services_business.html), go to “Business Organizations Act,” and then to “Nonprofit Corporations.” Read the Illinois requirements for the articles of incorporation. Now go
back to the homepage, click on Publications and Forms, and then click on Not-for-Profit Corporations. Read “Articles of Incorporation” (and “A Guide for Organizing Not-for-Profit Corporations” (May 2008)) and “Not-for-Profit Annual Reports” (May 2008)

Take advantage of the Ford Foundation’s laudable amount of disclosure – go to http://www.fordfoundation.org/about/governance, and explore the links to the Foundation’s Charter/Articles of Incorporation, Bylaws, Committee Charters and Membership, and procedures for the receipt, retention and treatment of complaints regarding accounting, internal accounting controls, and auditing matters.

GOVERNANCE: STATE FIDUCIARY LAW

6. Fiduciary Duties in General
   (This topic will take two class hours.)
   
   ALI Draft: Introductory Notes to Chapter 3 (Governance); § 300 (Fiduciary Duties); § 305 (Modification of Fiduciary Duties); § 310 (Duty of Loyalty); § 315 (Duty of Care); § 340 (Informational Rights and Obligations of Governing-Board Members).
   
   Guide: Chapter 4, Legal Duties & Obligations: pp. 77-99.
   
   CD-ROM: Under Ch. 4: Breach of Duties: Stern v. Lucy Webb Hayes National Training School (known popularly as the “Sibley Hospital Case”).

7. Exploring the Duty of Loyalty: Conflicts of Interest
   
   
   
   Supp.: Ostrower, “Findings on Financial Transactions between Nonprofits and Board Members” (2007), Supp. at 7-1 through 7-6; Smithsonian Institution materials (2007 through 2008), Supp. at 7-7 through 7-23.
   
   Web: Continue exploring the Ford Foundation’s website – at http://www.fordfoundation.org/about/governance – specifically, the Foundation’s Standards of Independence, Trustee Code of Ethics, Staff
8. **Exploring the Duty of Care: Delegation vs. Abdication and Investments**

   **ALI Draft:** § 325 (Committees and Delegation); and § 335 (Investment Management and Spending Policy).

   **Guide:** Chapter 3, *Organizational Basics*: “Board Committees,” at pp. 31-35; and Chapter 4, *Legal Duties and Obligations*: “A Further Look at Investments,” at pp. 99-115. (We also cover UMIFA/UPMIFA in Assignment 12.)

   **CD-ROM:** Ch. 4\Bielfeldt Foundation\Ill. AG Complaint.

9. **Understanding Nonprofit Financial Statements**

   *(This topic will take two class hours.)*


   **Web:** See Jack Siegel’s list of 101 questions on governance, financial controls, and safeguards that he posts on his website:
   
   www.charitygovernancelaw.com/Courses/101%20Questions%20for%20Your%20Consideration/player.html.

   Read his “Ten Financial Controls that Every Charity Should Put in Place”:
   

10. **Sanctions for Breach and Enforcement of Fiduciary Duties**

   *(This topic will take two class hours.)*

   **ALI Draft:** Chapter 3 (Governance), Introductory Note to Topic 2; § 350 (Enforcement of Fiduciary Duties by Charity or Co-Fiduciary); § 360 (Remedies and Sanctions for Breach of Duties).
Note: Assignment 13 covers suits by donors. I’ll describe there the difficulties of the current legal regime for private standing and “derivative” litigation on behalf of nonprofit organizations.

CD-ROM: Under Ch. 4: John v. John (at Breach of Duties); and King Foundation Jury Instructions and Jury Questions (at King Foundation).

Guide: Chapter 6, Federal Tax Exemption, discussion of King Foundation, at pp. 276-77; and of Maddox Foundation, at pp. 279-80 (note: Maddox settled in May 2007 – by splitting into two, one in each state).


11. Limitations on Fiduciary Liability

ALI Draft: § 365 (Business Judgment Rule); § 370 (Limitations on Monetary Liability for Breach); § 375 (Establishing and Defending a Claim for Breach); and § 380 (Immunity from Third-Party Suit, Indemnification, and Insurance).


CHARITABLE CONTRIBUTIONS

12. Exploring Fiduciary Duties: Restricted Gifts

ALI Draft: Chapter 4 (Gifts), Introductory Note; § 400 (Effects of Gifts to Charity); § 405 (Creation of Gift Restrictions or Conditions); § 410 (Permitted Terms in a Gift Instrument); § 415 (Unenforceable Gift Provisions).


CD-ROM: Ch. 7\Restrictions\PLR 200202032.

13 & 14.  **Board Responsibilities With Respect to Donors; Consequences of Breach**

*(Note: As suggested, this topic will take us two class hours, but please prepare all indicated material before the first class.)*

**ALI Draft:** § 420 (Compliance With Gift Restrictions and Conditions); and § 470 (Ratification of Charity’s Breach).


15.  **Change of Purpose: Cy Pres and Equitable Deviation Charitable-Trust Doctrines; “Duty of Obedience”; Nonprofit “Conversions” to For-Profit Form**

*(This topic will take two class hours.)*

**ALI Draft:** § 240 (Effecting a Change in Charitable Purpose); § 250 (Effect on Assets from a Change in Charitable Purpose); § 430 (Procedures When Circumstances Require Modification of a Restriction)); § 440 (Proceeding to Modify a Restriction (Deviation and Cy Pres)); § 450 (Effect of Passage of Time), pp. 186-90

**Guide:** Chapter 10, *Fundraising*, “Changed Circumstances,” at pp. 466-68.

**CD-ROM:** CH. 10\Cy Pres: *In the Matter of Estate of Donald Othmer.*

16. Regulation of Charitable Solicitations


CD-ROM: Ch. 9*World Church of the Creator*. Under the Supreme Court Trilogy, read the most recent case, *Madigan v. Telemarketing Associates, Inc.*


17. Pledges

ALI Draft: § 480 (Donor’s Failure to Perform a Charitable Pledges).


CD-ROM: Ch. 10*Pledges: Woodmere Academy* (Saul Steinberg); and skim *Maryland National Bank*.

18. Tax Treatment of Charitable Contributions

*(This topic will take two class hours.)*


Ch. 7*Internal Revenue Code*: Skim § 170(a)(1), (c) and (f)(8), (f)(16) [not on CD-ROM] & (f)(17) [not on CD-ROM]. In class we will briefly discuss subsections (b) and (e) [not in the Supplement].

Skim § 6115 (quid-pro-quo contributions) and regs under *Regulations*.

In the cases, skim *Sklar v. Commissioner*, 282 F.3d 610 (9th Cir. 2002), where the Ninth Circuit not only rejected a claim by orthodox Jewish parents that they could deduct the portion of private-school tuition paid for...
religious training, but it also ruled that the settlement between the IRS and the Church of Scientology (not a party to this case) was unconstitutional! The taxpayer also lost in Tax Court in the subsequent case (a later year).


(This topic will take two class hours.)


CD-ROM: In Ch. 6, under 'Internal Revenue Code Provisions, read I.R.C. § 501(c), particularly subsection (3) [also in Supp. at Code & Regs 3-6]; and under 'Taxexempt Status_Generally\Tax Regulations, read Treas. Reg. § 1.501(c)(3)-1(a), (b), (c) & (d) [also in Code & Regs, in Supp.].


This website also has links to the annual information returns (Forms 990, 990-EZ, and 990-PF); and to Forms 990-T (UBIT) (which we cover in Assignment 23) and 1120-POL (which we cover in Assignment 22), as well as Form 8283 (covered in Assignment 18). For 2008, the IRS is phasing in a major re-design of the Form 990. The core form of the revision is also in the Supp. for Assignment 24, where we’ll focus on the governance questions.

Starting in 2007 (filings made in 2008), organizations too small to file a Form 990 or 990-EZ must file an e-Postcard – failure to file 3 years in a row causes loss of tax exemption. How many orgs will have to re-apply for exemption?! For FAQs on the e-Postcard, go to the IRS Website.

20. **Prohibitions on Private “Inurement”**

*(This topic will take two class hours.)*

**Private Inurement and Private Benefit:**


- **CD-ROM:** See Treas. Reg. § 1.501(c)(3)-1(c)(2) and -1(d)(1)(ii) (private benefit prohibition) [this Reg is also in the Code & Regs in the Supp.].


**Intermediate Sanctions:**


**Interaction Between § 501(c)(3) and  § 4958:**


- **Supp.:** Final regulations (issued in 2008), in Code & Regs in Supp. (the proposed version is in CD-ROM, under Ch. 6\Intermediate Sanctions\ at \Proposed Regulations _September 9 2005_Private Benefit.pdf).  

21. **Private Foundations**

Note: The full ramifications of “private foundation” status are beyond the scope of this course; just appreciate that it is carries more restrictions than the “public charity” alternatives under Code section 501(c)(3). All 501(c)(3)’s are presumed to be private foundations unless excluded under the rules of I.R.C. § 509.

22. **Advocacy, Lobbying, and Political Activities; 501(c)(3)/(c)(4)/PACs (§ 527) Affiliations**

(This topic will take two class hours.)


CD-ROM: In Ch. 6, I.R.C. § 501(h) [also in Supp.]. Note: The dollar limits are in § 4911 (not in your Code & Regs).

Also in Ch. 6, under Lobbying, read *Regan v. Taxation With Representation*.

Web: On our Course Website, read *Revenue Ruling 2007-41* (classifying activities by (c)(3)’s) (go to “politics-rr-2007-41”). Skim *Revenue Ruling 2004-6* (advocacy activities by (c)(4)’s, (c)(5)’s, and (c)(6)’s)).

Supp.: IRS, “2008 Political Campaign Season,” Supp. at 22-1 through 22-4; material relating to IRS investigation of the United Church of Christ, Supp. at 22-5 through 22-14; and “Pastors May Defy IRS Gag Rule” and other news, Supp. at 22-15 through 22-19.

23. **Commercial Activities and the “Unrelated Business Income Tax”**

(This topic will take two class hours.)


Supp.: In Code & Regs, read Code §§ 511(a) & (b); 512(a)(1) & (3) (social clubs), and (b)(1) through (12); § 513(a), (c), & (i); Treas. Reg. § 1.501(c)(3)-1(e) [also on CD-ROM].


Web: Go to the Metropolitan Museum of Art’s webpage at http://www.metmuseum.org/store/ and explore. Don’t miss “Luxury Fine Jewelry” in the left-hand column. Is the profit on these items exempt?!
24. **IRS and Peer Group Role in Charity Governance**

**Supp:** New Form 990 and news story and my comment letter on the draft form, Supp. at 24-1 through 24-22.


Explore other Websites of charity watchdogs and “peer regulators”:

* BBB Wise Giving Alliance Charity Standards, at http://www.give.org/standards/index.asp

* Association of Fundraising Professionals Ethics Guides, at http://www.afpnet.org/ethics

* Wall Watchers, at http://www.ministrywatch.com, and read a couple of “Donor Advisories.”

25. **IRS and Congressional Initiatives (a.k.a. “Grassley Love Letters”)**


26. **State Tax Benefits for Charities**


CD-ROM: In Ch. 8\Property Taxes, read the Providence, R.I., PILOTs agreement; and *Matter of Pacer* (re zoning approvals).


Web: On our Course Website, skim brody-EOTR-prop-tax.pdf.

27. **The “Non-(c)(3)’s” [IF TIME]**


Supp.: Table of types of exempt entities from Joint Committee on Taxation (July 2007), Supp. at 27-1 through 27-3.

28. **Exam Practice**

(We will spend two class hours on these.)

On our Course Website, you can find all my old exams. I’ll divide up the class into groups to prepare and present questions for us to discuss.

**EXAM**

The exam will be on Thursday, December 11, at 8:30 a.m. This will be a 3-hour, open-book exam.

Take into the exam all of your written course material and your notes, and any other written material you wish. Some of you might be living out of your notebook computers. You may bring your computer into the exam, including your notes and outlines, but you may not bring any CD-ROMs or go online. Anyone who prepares for class, attends regularly, and studies the material should be able to do well on the exam; by contrast, anyone who does not keep up should not be able to do well on the exam simply by having an electronic outline.