

# NONPROFIT MATTERS



A Bulletin for Nonprofit Organizations Distributed by the Public Law Center

Volume I, Issue I

January 2006

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## Message from the Executive Director

With this issue, we're unveiling *Nonprofit Matters*, a new newsletter designed for Orange County's nonprofit community. Every year, nonprofit organizations face an increasingly complex regulatory environment. That's true in the area of nonprofit management and governance; it's also true in the many areas of substantive laws that impact the clients served by local nonprofit groups. Our goal for this semi-annual newsletter is to make some of the laws and regulations that impact nonprofits and their clients a little more understandable. We hope you find it helpful.

Ken Babcock

**Nothing in this newsletter should be construed as legal advice. For more information about complying with the various laws mentioned in this newsletter, please consult a legal or tax professional.**

## Fundraising in the New Year and Beyond

Fundraising is an essential part of every charitable nonprofit organization. Pretty basic principle, but getting more complicated as fundraising has become more sophisticated and fraud continues to exist. While nonprofit organizations are encouraged to be more creative, competitive and determined with fundraising activities, legal issues may arise or violations may occur without prudent planning.

January 2005 brought about new regulations for California nonprofit organizations. With the

passage of the [California Nonprofit Integrity Act](#) ("Act"), many nonprofit organizations are subject to new corporate standards, and all nonprofit organizations are subject to new fundraising regulations. For 2006 and beyond, nonprofit organizations need to be aware of fundraising regulations implemented by the Act, California Attorney General ("Cal AG"), or taxing authorities.

One of the enduring key issues in fundraising is oversight and accountability for fundraising activities. For example, the Act now requires all nonprofit

organizations to have written contracts with



any commercial fundraiser or fundraising counsel. All commercial fundraisers and fundraising counsels are required to register with the Cal AG. Here are the

*Continued on page 4*

## New California Law to Provide Greater Protection to Victims of Human Trafficking

Human trafficking is modern-day slavery and its victims often are undetected in our communities. Although the idea of slavery may seem historical or third-world, human trafficking victims have been rescued here in Orange County. It is often only with the assistance of front-line social service and health providers or concerned neighbors that

a victim is able to seek assistance to leave their slave-like circumstances.

Human trafficking is the recruitment of another person, by means of threats, coercion or fraud. This recruitment is done for the purpose of controlling, exploiting and depriving another person of personal liberty. Examples are often found in the

context of worker and sexual exploitation. For example, a human trafficking victim may be someone who is forced, by use of threats and/or physical abuse, to work as a maid and is paid little or no money and given no freedom to leave their workplace. Another example of a human trafficking victim

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## HIPAA Privacy Awareness for Employer Health Plans

Most small employers were subject to HIPAA Privacy Rules in April 2004, while the new HIPAA eSecurity rules take effect in April 2006. Virtually every employer that has two or more employees and offers an employee benefit health plan is subject to HIPAA Privacy Rules.

HIPAA creates a curtain around the employer's Health Plan, so that any medical information (called "protected health information" or "PHI") cannot be disclosed without authorization. The new eSecurity rules effective in April 2006 address the employer's computer networks and systems protocols where any PHI exists in an electronic format. For example, Excel spreadsheets, emails, and text files that contain PHI must be safeguarded under a completely different set of policies and procedures. In addition, a Security Officer within the organization must be appointed.

The good news is that fully insured employer Health Plans that

maintain no PHI (except for census data and enrollment information) has limited compliance requirements under HIPAA Privacy Rules. The bad news is that a Section 125 medical flexible spending account (FSA) is considered a self-funded Health Plan, which requires full compliance.

eSecurity requires IT personnel to examine all computer access, security, data integrity, and storage features associated with any electronic PHI (or ePHI). The requirements set forth three basic areas to safeguard: administrative, physical, and technical. The rules require written documentation of the employer's risk analysis, sanction policy, disaster recovery plans, and emergency mode operation criteria. Additionally, there should be limited computer access for people specifically working with ePHI, device/media disposal procedures, and procedures established to determine who accessed systems during the course of normal business.

One approach many employers are taking is to establish a separate HR server to house all HR related materials. Then, both HR and IT staff are screened to determine the appropriate people who will be given specific access to ePHI via the network.

The Department of Health and Human Services (HHS) is responsible for investigating complaints and enforcing sanctions. Persons responsible for violation of HIPAA Privacy Rules may face sanctions that include prison terms ranging from one to ten years. Employers should not take HIPAA compliance lightly. Employers should take steps, document progress and implement safeguards to assure the security and integrity of an employee's PHI.

*This has been excerpted from an article published in the December 22, 2005, Public Interest Clearinghouse Legal Services Bulletin. It was written by Victor A. Deksnys, EVP with Gallagher BPI in Larkspur, CA.*

## Corporate Governance Update

### New California Legislation Relating to Corporate Governance

[SB 119](#) allows board action to be taken without a meeting if all members consent in writing and explains how "interested directors" can participate in this process. The bill amended sections 5211, 7211, 9211, and 12351 of the California Corporations Code, and added section 307.

[SB 702](#) makes unincorporated associations subject to new governance standards, including provisions relating to termination of membership, member voting, merger, and dissolution.

### California Nonprofit Integrity Act Now a Year Old

On January 1st, 2006, the Nonprofit Integrity Act had its first birthday. The law overhauled charitable registration with the Attorney General, raffle registration and reporting, financial audit requirements, executive compensation review, and the use of commercial fundraisers and fundraising counsel. To help make the law clearer, the Attorney General publishes this [Summary of Key Provisions](#).



### Congressional Support for Major Nonprofit Corporate Governance Reforms on the Wane

Several notable reports on nonprofit corporate governance were published in 2005, including the Panel on the Nonprofit Sector's [final report](#) and the John Hopkins Listening Post Project Report's [final results](#). According to [John Buckley](#), minority chief tax counsel for the House Ways and Means Committee, these independent reports, among others, have substantially decreased support for Sarbanes-Oxley type nonprofit reforms in Congress.

## Laws Affecting Your Clients in 2006

**Civil Rights:** California law [AB 1400](#) expanded the bases of discrimination prohibited by the Unruh Civil Rights Act to include marital status and sexual orientation.

The Domestic Partner Rights and Responsibilities Act of 2003 came into effect January 1, 2005. The law grants registered domestic partners the “same rights, protections, and benefits,” and imposes upon them the “same responsibilities, obligations, and duties” as are granted to and imposed upon spouses under California law.

In a series of landmark opinions, including [Elisa B. v. Superior Court of El Dorado County](#), the Supreme Court of California granted equal parental rights to same-sex parents. According to a [San Francisco Chronicle article](#), the court ruled that “lesbian and gay partners who plan a family and raise a child together should be considered legal parents after a breakup, with the same parental rights and responsibilities as heterosexual parents.”

**Consumer Rights:** If you’re involved in consumer rights, it would have been hard to miss the passage of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (S.256.ENR), which went into effect October 17, 2005. The Act overhauled bankruptcy laws for both individuals and businesses. Specifically, it changed the legal test to assess whether debtors have enough money to repay some or all of their debts. It also imposes credit counseling and money management class requirements for individuals seeking bankruptcy. For more information on the Act, read CNN’s [The New Bankruptcy Law & You](#).

AB 68, the [Car Buyer’s Bill of Rights](#), was signed by the governor in July 2005 and will go into effect July 1, 2006. The act expands the

rights of car buyers and restricts certain unfair practices of car dealers. Specifically, the law allows used car buyers who purchase a cancellation option (for up to \$250) to return a used car valued under \$40,000 within two days of purchase for any reason.

[SB 20](#), which goes into effect April 2006, extends a low-cost car insurance program for low-income good drivers to Orange County.

**Housing:** Section 1946.1 of the California Civil Code, which provided for a 60-day notice to terminate a residential tenancy, expired at the end of 2005. Thus, the law returns to the 30 day period previously required to terminate a tenancy. State Senator Sheila Kuhl authored a bill that would have made the 60 day requirement permanent. It passed the state Senate, but was defeated in the Assembly.



[SB 137](#) prevents a homeowners association from foreclosing on a home for unpaid assessments of less than \$1,800 or 12 months’ delinquency.

**Health Care:** The new “voluntary” Medicare Prescription Drug Plan, called Medicare Part D, came into effect January 1, 2006. The program replaced prescription drug coverage under Medicaid. According to the [National Senior Citizens Law Center](#), 4.26 million Californians will be affected by this change, including one million low-income individuals. You may refer elderly and disabled clients to the U.S. Department of Health & Human Service’s [Medicare webpage](#). Information is available in English, Spanish, Chinese, Korean, Vietnamese, and Russian.

As of October 7, 2005, basic dental and periodontal services are

available for all pregnant Medi-Cal beneficiaries regardless of immigration status. [SB 377](#) was passed to improve maternal health and reduce the number of premature deliveries, low birth weights, and children born with disabilities, problems that can result from poor dental health.

The governor also approved a measure to restore \$2.4 million in funding to the IMPACT program. With the passage of [SB 650](#), low-income men and immigrants who have no access to health care will continue receiving free, high-quality prostate cancer treatment and care.

On July 1, 2006, [AB 1195](#) will go into effect and ensure that doctors and surgeons who provide direct patient care are better equipped to address racial, ethnic, linguistic and gender-based disparities in medical treatment and diagnosis. This law will require continuing education courses to include cultural and linguistic competency training and creates a voluntary program that provides doctors with the opportunity to learn a foreign language.

[AB 22](#) requires health insurers to explain in writing why an individual was denied coverage or granted coverage at a higher rate than standard.

With the passage of [AB 1586](#), insurers may no longer refuse to pay for an organ or tissue transplant solely because the intended recipients is HIV-positive.

**Access to Justice:** On January 1, 2006, the jurisdiction of the [Small Claims Court](#) will be increased to allow claimants to recover judgments of up to \$7,500. The new law applies to cases filed by individuals and does not apply to small claims lawsuits filed by business entities.

“Fundraising” cont. from page 1

definitions for the two types:

**Commercial Fundraiser—**

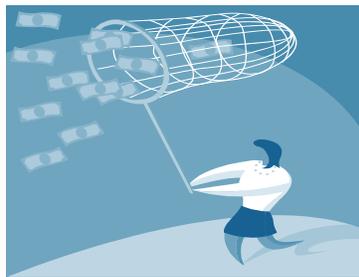
Defined as any individual, corporation, or other legal entity that, for compensation, solicits funds, assets, or property in California for charitable purposes on behalf of a nonprofit organization. A common commercial fundraiser is a telemarketing company that solicits on behalf of a nonprofit organization.

**Fundraising Counsel—**Defined as any person, corporation, or other legal entity that, for compensation, plans, manages, advises, counsels, consults or prepares material for the solicitation in California of funds, assets, or property for charitable purposes. Fundraising counsel can range from an independent grant writer to a charitable event coordinator.

While a commercial fundraiser usually collects and controls charitable funds for a nonprofit organization, fundraising counsel does not, and cannot, control any charitable assets under California law. Both types of fundraisers must register with the Cal AG, and a nonprofit organization should check the Cal AG’s registry to

verify that the fundraiser has registered before signing a contract. The registry can easily be accessed at the [Cal AG’s Charitable Trust Division’s website](#).

Having a written contract with your commercial fundraiser or fundraising counsel is not only good business practice, but it also provides oversight by the Board of Directors. First, a written contract provides documentation of each party’s expectations and obligations and provides



enforcement mechanisms better than an oral contract. Second, most nonprofit organizations require the Board of Directors to approve, or at least review, a contract for services. (If your organization does not require the Board of Directors to approve of fundraising contracts, then the organization should consider amending the bylaws to add that level of oversight.) The Board of Directors should exercise its Duty of Care to carefully examine the contract, understand the terms, and ask questions of officers or staff members.

While nonprofit organizations must follow the Act, other federal and state laws must be addressed. At the federal level, nonprofits need to wary of Unrelated Business Income and Charitable Giving regulations. Unrelated Business Income (“UBI”) is defined as earned income that is derived from a 501(c)(3) organization’s activities that are NOT substantially related to its charitable purpose. UBI is subject to normal corporate income tax rates. For example, if a nonprofit

organization earns income from operating a cafe, but its charitable purpose is to provide homeless services, then UBI might likely apply. The Internal Revenue Service (“IRS”) examines how the activity furthers the charitable purpose, not how the income will be used. (If your nonprofit is thinking of engaging in commercial activities or social enterprise, then you should consult PLC or a tax attorney.) Nonprofits must also be aware of changes in Charitable Giving regulations by the IRS. While individual taxpayers should consult a tax professional with how charitable donations are characterized, fundraising techniques can change yearly based on how the IRS treats various charitable transactions.

Under California law, nonprofit organizations need to be aware of the Act, as discussed above, as well as regulations issued by the Franchise Tax Board, Board of Equalization, and Cal AG. While most charitable fundraising is not taxed under California law, fundraising events that include gambling, raffles, and auctions have restrictions or impose taxes on the nonprofit organization. If you are thinking of using gaming or auctions in your fundraising activities, you should seek legal counsel or do research before proceeding.

While nonprofit organizations need to be diligent but as fundraising regulations continue to grow, nonprofit organizations should not feel overburdened with new regulations. Legal resources are available over the Internet or through legal counsel such as the Public Law Center, National Economic Development and Law Center, and other nonprofit legal service providers. Careful planning will help avoid new and old pitfalls.

### New USPS Rule

On June 1, 2005, the U.S. Postal Service issued a series of rule changes, some of which modified what can qualify for the Nonprofit Standard postal rate. For more information on the rule changes read this resource from the [Alliance for Nonprofit Mailers](#).

## Changes in Charitable Fundraising Laws

### Illegality of Charitable Gaming Activities

In November 2005, the California Attorney General issued a Fundraising Alert: [No Charity](#)

[Poker Games](#).

According to the alert, “While eligible tax-exempt organizations registered with the Attorney General’s Registry of Charitable Trusts may conduct [fundraising raffles](#),

charities and anyone other than a licensed gaming establishment are not allowed to offer poker tournaments, ‘Monte Carlo’ or ‘Casino Night’ events, or casino games such as craps or roulette.”

For more information, contact the Attorney General’s [Division of Gambling Control](#). The Los Angeles Daily News [reported](#) that California lawmakers will be looking to make a charitable exception to gaming law in the 2006 legislative session.



### New IRS Regulations on Excess Benefit Transactions

From the [IRS](#): “The IRS and Treasury Department [published proposed regulations](#) in the September 9, 2005 Federal Register which amend the existing regulations under section 501(c)(3) and add several examples to illustrate the requirement that an organization serve a public rather than a private interest. The proposed regulations also provide guidance on factors the IRS will consider in determining whether a 501(c)(3) organization that engages in one or more excess benefit transactions described in section 4958 will continue to be recognized as exempt under section 501(c)(3).”

*California SCR 21 designated the week of March 6-12, 2006 as California Nonprofit Organizations and Philanthropy Week.*

### New Guidance from the IRS Relating to Donor Tax Deductions

**Intellectual Property:** IRS [Notice 2005-41](#) provides guidance on the availability of charitable contribution deductions from qualified intellectual property donations.

**Vehicle Donations:** IRS [Notice 2005-44](#) of June 20, 2005 provides guidance on section 884 of the American Jobs Creation Act of 2004, which substantially changed the rules for determining the amount a donor can deduct for donating a vehicle. For more information on charitable donations of vehicles, visit [this IRS webpage](#).



“Human Trafficking” cont. from page 1

is someone who is forced to perform commercial sex acts. This victim may be unable to leave their forced prostitution situation because the traffickers are holding the victim’s immigration documents and/or threatening to harm the victim or his or her family if the victim attempts to leave or report the coercion to law enforcement.

In 2000, the Federal government enacted the Trafficking Victims Protection Act of 2000, which provides protection to human trafficking victims in the form of immigration relief, public benefits, enhancement of criminal penalties for traffickers and federal funding for victims services.

In September 2005, Governor Arnold Schwarzenegger signed California

legislation to increase and expand protection of human trafficking victims. AB 22, the California Victims Protection Act, establishes human trafficking as a crime in California, requires cooperation from local law enforcement, and provides greater relief to victims through the Victims Compensation Fund and greater potential for civil lawsuits against the traffickers. In addition, Governor Schwarzenegger signed SB 180, which creates the California Alliance to Combat Trafficking and Slavery Task Force to research and report findings of California’s human trafficking data, models, programs and services by July 1, 2007.

PLC—in collaboration with Boat People SOS, St. Anselm’s Cross-Cultural Community Center, The Cambodian Family, and Catholic Charities of Orange County—has been awarded a

federal grant to provide free assistance to human trafficking victims in Orange County. Case managers from these social service agencies can provide victims with assistance in applying for health and housing benefits, job training, and access to ESL classes. PLC can provide victims with assistance in applying for immigration relief and, when appropriate, in cooperating with law enforcement in the investigation and prosecution of the traffickers.

*If you would like more information about human trafficking, would like to report a potential human trafficking situation, or would like to request training, please contact PLC at (714) 541-1010 or the Human Trafficking Hotline at (714) 251-4011.*



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601 Civic Center Drive West  
Santa Ana, CA 92701

Phone: 714-541-1010 Fax: 714-541-5157  
<http://www.publiclawcenter.org>

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We would like to thank the Volunteer Center of Orange County, CONNECT: Partnership for Nonprofit Solutions, Orange County United Way, and the Fieldstone Foundation for their help in distributing the inaugural issue of this newsletter.

[The Public Law Center](#), Orange County's pro bono law firm, is committed to providing access to justice for low income residents. Through volunteers and staff, the Public Law Center provides free civil legal services, including counseling, individual representation, community education, and strategic litigation and advocacy to challenge societal injustices. Now in its 25th year, PLC is sponsored by the Orange County Bar Association and is supported by lawyers throughout the county.

PLC may be able to assist your clients who are low-income Orange County residents and have certain types of immigration, family law and civil legal problems, including: landlord-tenant, homeownership, collection, bankruptcies, consumer, estate-planning, discrimination, employment, adoptions, guardianships, custody matters, divorces involving children or domestic violence, and immigration work that does not involve naturalization or work visas. To determine whether your clients are eligible for services, they may contact the [Legal Aid Society of Orange County](#), which regularly refers cases to PLC, or attend one of PLC's clinics at various [homeless shelters](#) and community organizations around Orange County.

## New COLAP Service in 2006

PLC's Community Organizations Legal Assistance Project (COLAP), through staff and pro bono volunteer attorneys, provides free transactional legal assistance to local non-profit organizations that face a variety of business law issues in areas such as contract law, employment law, and real estate law. COLAP also provides free legal assistance to those interested in starting new nonprofit organizations designed to benefit Orange County's low-income residents. Additionally, COLAP partners with community organizations to provide legal education seminars to already existing and start-up nonprofits. For more information on COLAP services, please visit our [webpage](#).



Starting in early 2006, COLAP will be assisting organizations through a legal audit program. Through this program, teams of volunteer attorneys and law students will conduct legal checkups on organizations to make sure they are complying with various state and federal laws. The service allows organizations to address legal issues before they become a problem. If nonprofits do not comply with legal requirements, they may be subject to administrative fines or they can even lose their tax-exempt status. This project helps organizations avoid these consequences.

To participate in the program, contact COLAP attorney [Shannon Anderson](#).

### Upcoming Workshop

PLC's Community Organizations Legal Assistance Project (COLAP), in collaboration with CONNECT: Partnership for Nonprofit Solutions, and the Honorable Claude Parrish of the Board of Equalization, will be offering a Tax Seminar for Nonprofits on JANUARY 30<sup>th</sup>, 2006. The seminar will provide expert information from government officials from the IRS, BOE, EDD, and FTB about tax laws, exemptions, and reporting requirements as they apply to nonprofits. To register for the workshop, contact [Shannon Anderson](#).