2012 Annual Legal Review

An Association ***TRENDS*** Special Focus sponsored by VENABLE LLP

Venable is pleased to sponsor again the Association TRENDS Annual Legal Review. This Legal Review contains updates on major developments of the last year as well as summaries of articles and presentations that the Venable team has made on legal topics of importance to the trade association and nonprofit community. I hope you will find them of interest and invite you to subscribe to future alerts and articles at www.Venable.com/SubscriptionCenter. You can also access a complete collection of past articles at Venable.com/services/industries/nonprofits and associations/publications.

Brock R. Landry, Chairman, Government Division, Venable LLP

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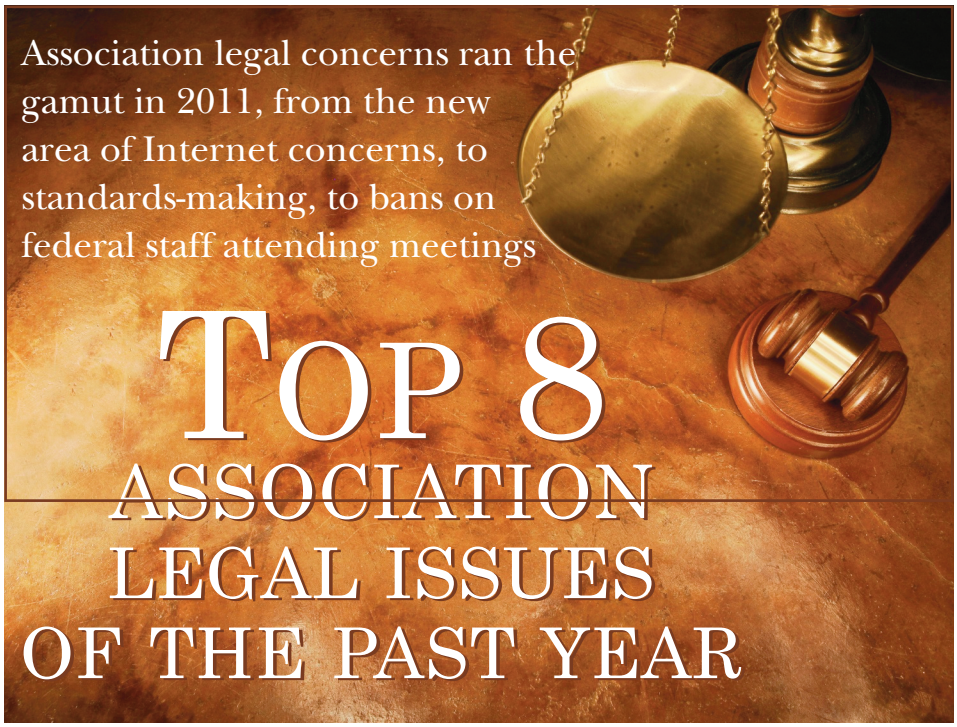

Association legal concerns ran the gamut in 2011, from the new area of Internet concerns, to standards-making, to bans on federal staff attending meetings

Top 8 Association Legal Issues of the Past Year

Lobbying: Meet you in St. Louis – or not. The Federal Election Commission and Office of Government Ethics have proposed significant new restrictions on the interaction of federal employees with trade associations. Existing House and Senate gift rules restrict legislative personnel from attending events unless they are "widely attended events (more than 25 people)" and if they have a speaking role or if it will 'further the interest of the government.' An Executive Order similarly restricts political appointees from meetings although "widely attended gatherings" in the Order's parlance are not defined by number. The new proposals would extend these restrictions to all executive branch employees. The association community has vehemently opposed the proposal arguing that this will inhibit free interaction of government employees with the trade association community at events such as trade shows and other events that would educate the federal employees about their members.

Taxation: Revocation of nonprofit tax exemptions. In June 2011, the Internal Revenue Service revoked the tax exemption of more than 275,000 nonprofit organizations, almost 17% of those previously exempted. This action impacts those entities that have failed to file required returns for three consecutive years. The IRS made significant efforts to inform the community of the new requirements for filing and indeed even extended the deadlines for compliance. Although many of the nonprofits that lost their exemption are likely defunct, the change will hit many that either did not know or ignored the requirements for filing. Those organizations wishing to re-obtain tax exemption must start from scratch – filing a new Form 1023 or 1024 and submitting appropriate users' fees. Loss of exemption can be significant: the entities may incur income tax liability and contributions to erstwhile (c)(3)s may not be deductible.

Litigation. In October 2011, the Obama administration continued its restriction on interaction with lobbyists by prohibiting registered lobbyists from serving on federal advisory committees such as the Industry Sector Advisory Committees, which advise

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TOP 8 ASSOCIATION LEGAL ISSUES OF THE PAST YEAR

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the U.S. trade representative and the Commerce Department on international trade matters. Six lobbyists for various trade association groups have sued the administration claiming that the new policy denies their constitutional right of freedom of speech and the equal protection guarantees. The complaint also alleges that the policy would have the effect of encouraging people to avoid registration. The government has filed a motion to dismiss, arguing among other grounds that the plaintiffs have no standing since all advisory committee members serve at the pleasure of the president.

New corporation rules in D.C.
On Jan. 1, 2012 the new D.C. Non-Profit Corporation Act went into effect. This law is considerably more detailed than the previous statute, but overall the act generally provides flexibility to alter the statutory "default rules" through specific, different provisions adopted in a corporation's articles or bylaws. The act also recognizes and accommodates 21st century forms of communication in doing business such as Internet or other electronic meeting technology and notice. There are a number of significant areas of change: The act codifies the common law fiduciary duties of care and loyalty imposed upon directors and officers and specifies the nature of conflict situations that must be disclosed. Indemnification requirements are detailed. It streamlines the process and requirements for incorporation. Recordkeeping provisions are expanded significantly, requiring permanent retention of the minutes of meetings of boards and members. A variety of other records must be maintained at the corporation's principal office and are subject to inspection by directors and members. These changes will require review and revision of existing corporate documents of D.C. corporations.

Litigation heats up on standards-making. In a case that has now stretched for over five years, an insulation manufacturer alleges that the American Society of Heating, Refrigerating and Air Conditioning Engineers improperly developed standards for metal building insulation systems that restrained trade, foreclosed competition, and facilitated price increases. The plaintiffs originally sought injunctive relief to prohibit circulation or publication of a standard that had been in effect for nearly 10 years. The crux of the complaint is that the standards-making process was unfair and manipulated by ASHRAE and other unnamed persons. It is alleged that the resulting standards disadvantaged its product in the market (although did not bar it). The plaintiff also originally claimed violations of the Lanham Act, continued to assert a common law claim of unfair competition against the association. No other defendants have been named in the suit. Trial is set for later in the year.
This case will be watched for further guidance as to the claims that can withstand scrutiny related to associations' standards-making activities.

Internet: dot whatever. The furor over generic Top Level Domain Names raged through 2011 and continues this year. After years of consideration, in June 2011, ICANN – the entity charged with administration of the top-level domain names – announced the process by which applicants could seek new web address suffixes. In addition to the familiar few, such as .org, .com, .edu, .net, ICANN will open the floodgates to any new designations that it approves. Applications will be accepted until later in March. The process, however, is expensive. Application fees are $185,000 and this is just the start of establishing and maintaining a registry program for the domain name. Proponents of the change note that some countries are likely to start their own systems if the new proposals are thwarted. Widespread opposition has gathered. The Association of National Advertisers has established a coalition with more than 160 members, including ASAE, National Association of Manufacturers and the U.S. Chamber. The coalition is concerned about the confusion, cost and potential cyber-squatting that could ensue. Various legislators also have weighed in. It all spells a controversy for the rest of 2012.

Membership/accreditation restriction. Association members who determine or unduly influence another member's accreditation status can be dicey. In K&S Associates v. American Association of Physicists in Medicine, the court found that the plaintiff stated an unreasonable restraint of trade claim against the association for improperly withholding an economically critical accreditation. The factual allegations were important in denying a motion to dismiss. The chairpersons of the committee charged with evaluating the application recommended acceptance of K&S, but another ad hoc group was convened that included the applicant's two direct competitors. The complaint alleges that the accreditation was denied largely because of the improper involvement of the competitors. The case is set for trial later this year.

Taxation: IRS announces its focus for enforcement. The 2012 Work Plan published by the IRS Exempt Organizations Division highlighted significant areas of scrutiny that the association community will face. The substantial changes to the Form 990 were promulgated for the express purpose of providing information to better evaluate tax compliance of nonprofits. Data for tax years 2008 and after are being evaluated to construct "risk models to identify the likelihood of noncompliance." For example, questions on the form regarding corporate governance are being used to identify potential noncompliance. Political activity is another area of emphasis. The IRS will also look to outside sources as well as returns to identify potential noncompliance with political activity and lobbying tax issues. Unrelated business income tax is always a hot topic with the IRS – in 2012 the EO will analyze associations that report significant gross receipts from unrelated activities, but declare no tax due.

Employees: Their Facebook page said what about the association?

Because nonprofits are typically not unionized, they often overlook the fact that the National Labor Relations Act can apply to them and limit their right to discipline or terminate employees for social media activity.

A report by the NLRB's acting general counsel issued last August and a subsequent ruling of an NLRB administrative law judge provide very helpful guidance for nonprofits on what policies and punishment for postings might be problematic. For example, the NLRB report discusses the following findings in particular cases:

- Employees were unlawfully discharged for responding to the Facebook posting of a coworker discussing working conditions, even though the employee who initiated the cyber conversation considered her coworkers' comments to be cyberbullying and harassment.
- An employee was discharged lawfully after posting profane comments on Facebook critical of store management because the employee's postings were merely an expression of individual gripes, as opposed to protected concerted activity. In this case, at least two coworkers responded to the posting; however, their messages reflected that the posting was individual and not group activity.
- A policy prohibiting employees from making disparaging comments when discussing the employer or its supervisors was unlawful because the policy did not make clear that it did not prohibit protected concerted activity.
- The discharge of a recovery specialist in a residential facility for homeless individuals who posted demeaning comments concerning her employer's clientele was lawful because there was no evidence of protected concerted activity: the comments did not mention any terms or conditions of employment, the posting was not discussed with any coworkers, and the comments were not for the purpose of inducing group activity or an outgrowth of collective concerns of the employee or her coworkers.

On Sept. 2, 2011, an NLRB administrative law judge issued the first adjudicated decision involving social media-based discipline. In the case, Hispanics United of Buffalo Inc., a nonprofit that renders social services to economically disadvantaged clients in Buffalo, N.Y., was found to have committed unfair labor practices when it discharged several employees for Facebook postings – made on their own computers outside of working hours – that expressed criticism of their working conditions and of a person who worked for the nonprofit. The employees were terminated based on the contention that the postings constituted cyberbullying and harassment in violation of the nonprofit's policies. The ALJ found the comments protected and rejected the contention that the employees were bullying the other worker or that they harassed her in violation of the nonprofit's policies. Consequently, the ALJ concluded that the employees had not engaged in conduct that converted their concerted activity from protected to unprotected status.

The NLRB's recent report and the Hispanics United of Buffalo decision provide helpful guidance to nonprofits not wishing to become potential NLRB cases, including the following:

- Communications that are not concerted are generally not protected. However, the cases highlight that a finding of concerted activity might turn on evidence not readily available to the employer, so caution is warranted.
- Communications that are concerted (i.e., that are not merely an individual gripe) on matters of mutual concern to employees are likely to be found to be protected by the NLRA.
- Communications that are protected do not become unprotected simply because the comments are communicated via the Internet and/or because they might be read by nonemployees as well.
- Communications that are protected do not become unprotected just because they contain some critical (about the employer) or otherwise objectionable language.
- An association policy that, reasonably interpreted, would tend to "chill" employees in the exercise of their rights under the NLRA is likely to be found unlawful by the NLRB if it is challenged.

Given this new focus on social media, nonprofits should: 1) review their relevant employment policies to ensure that they are not overbroad and do not constitute potential unfair labor practices; and 2) proceed cautiously when determining whether to discipline an employee because of his or her comments in postings on Facebook, Twitter or other social media.

Read the full article by Ron Taylor and Jeff Tenenbaum at www.Venable.com.

FEC advisory opinion opens PAC doors

The FEC has issued an advisory opinion (AO) to the Utah Bankers Association that provides new opportunities for associations to solicit contributions from the general public to candidates. The AO will allow the Utah Bankers PAC to establish a project that will identify candidates who support the banking industry. One advisory council will identify those candidates and a second will determine which candidates will receive support from the project. The councils will be staffed by association employees and also by volunteers from member banks.

The project will then create a website and emails that will encourage people to contribute to the candidates. The council members may forward the emails to their personal contacts, and ask that they be forwarded along to others. It is important to note that the emails and websites are not used to collect contributions for the candidates. Rather, they encourage people to contribute directly to the candidates involved (by directing people to the candidate's websites). In addition, this activity will not be coordinated with the candidates.

The costs involved for creating content (including staff time), paying Internet vendors, etc. will be paid by the PAC. In addition, the PAC will pay its affiliated associations (those in other states) $50 annually to cover the costs associated with staff from those associations forwarding emails. The association itself will pay any administrative costs, such as accounting, legal, and phone costs.

This AO makes clear that associations may use their PACs to solicit contributions to candidates from those outside of the association's restricted class. This frees up PAC resources, helps to elect candidates whom the association supports, and likely will help the association raise more money for its PAC since it can rely on contributions from those outside of the restricted class to contribute to candidates.

Read the full article by Ron Jacobs at www.Venable.com.

Is your chapter a franchise?

A recent Seventh Circuit appeals court decision held that the national Girl Scouts organization violated a Wisconsin franchise law when it attempted to take away territory from a local "chapter" as a part of the national's reorganization of affiliates. In Girl Scouts of Manitou the Manitou council sought to enjoin the national organization from transfering all of its territory in Wisconsin, arguing that it was a "dealer" under Wisconsin law and that such action would violate the Wisconsin Fair Dealership Law. While the transfer of all of the Manitou council's territory would not have served to dissolve the Manitou council as an entity, it would have prevented it from representing itself as a Girl Scouts organization and from otherwise using Girl Scouts trademarks, which the court characterized as a "constructive termination."

In 2004, the national Girl Scouts organization decided to cut back drastically the number of local councils and expand the surviving councils' boundaries. Each council is party to a charter agreement. According to the court's decision, the agreement with the Manitou council did not permit the national organization to change its territory at the time the national organization attempted to take away the council's territory, though the council had agreed to be subject to a rule that allowed the national organization to have the final say over "all matters concerning jurisdictional lines."

The Wisconsin Fair Dealership Law forbids a franchisor from terminating, canceling, failing to renew or substantially changing "the competitive circumstances of a dealership agreement without good cause." A "dealer" is defined as a "grantee of a dealership," and the applicable "dealership" definition is an agreement that grants "the right to sell or distribute goods or services, or use a trade name, trademark, service mark, logotype, advertising or other commercial symbol, in which there is a community of interest in the business of offering, selling or distributing goods or services." Girl Scout cookies played a big part in the decision!

The national organization raised several unsuccessful arguments. First, it claimed a First Amendment right of free expression would be violated if it wasn't allowed to reorganize. Second, it argued that the Wisconsin law does not apply to nonprofit entities due to an absence of commercial activities. The court gave that short shrift, stating that, "[f]rom a commercial standpoint, the Girl Scouts are not readily distinguishable from a Dunkin' Donuts." Ultimately, the court held that although the national organization's board of directors had the authority in its chartering agreement with the Manitou council to make final decisions "in all matters concerning jurisdictional lines," when attempting "to use that authority to terminate the franchise altogether," the national organization violated the Wisconsin Fair Dealership Law.

While the facts involved in this case are somewhat unique – given how significant and recognizable the Girl Scouts' cookie sales and other activities are – the decision of the court was a broad one that could be construed as applying to more traditional nonprofits that might have less visible commercial activities. The contractual relationship between the Girl Scouts and its councils (which the court viewed as akin to that of "franchisor to franchisee") appears to be very similar to relationships that associations and other nonprofit organizations have with their state and local chapters, and other affiliates. As a result, this decision could pave the way for state dealership and franchise laws to be imposed on nonprofit organizations' relationships with their chapters and affiliates. About 20 states have dealership or franchise laws that could now come into play for nonprofit organizations across the country.

Consequently, nonprofit organizations with chapters should review their organizational structure, charter agreements and related documentation, as well as state dealership and franchise laws, to determine whether changes to these documents may be necessary or prudent.

Read the full article by George Constantine at www.Venable.com.