Dealing with Embezzlement

PLUS: Responding to Negative Social Media & Employment Updates for the New Year

Fraud, Embezzlement and Theft: How to Respond

As background for its recent investigation, “Inside the Hidden World of Thefts, Scams and Phantom Purchases at the Nation’s Nonprofits,” the Washington Post sought to establish the extent to which 501(c)(3) organizations experience “significant diversions of assets.” Reporters scrutinized four years of IRS Form 990 information returns which, since 2008, require filers to report “any unauthorized conversion or use of the organization’s assets other than for the organization's authorized purposes, including but not limited to embezzlement or theft.”

Though the Post identified more than one thousand affected charities with collective losses totaling hundreds of millions of dollars, these represent but a fraction of such incidents. Only larger nonprofits file Form 990, and disclosure of loss is not required unless the amount exceeds a threshold of $250,000 or 5 percent of an organization’s annual gross receipts or total assets. Smaller nonprofits that file either the 990EZ or 990N are not required by those forms to make any kind of asset diversion disclosure.

Of course, charitable asset diversion in any amount is serious. Embezzlement in particular can damage donor trust and agency reputation, thereby undermining a nonprofit’s good work. In extreme cases, it can lead to revocation of tax exempt status. Therefore, it is critical that the board and management of an affected nonprofit formulate a thoughtful plan of action that complies with fiduciary duty and law. Recommended elements of such a plan for a California 501(c)(3) organization include:

- Full disclosure to the board if the diversion was first discovered by management.
- An internal investigation of loss conducted by a qualified investigator(s). (Both financial fraud and employment law issues may be involved.)
- A decision whether to file a police report against the perpetrator. (This may be required for insurance purposes).
- A plan to recover funds, possibly including a civil collection suit. If willing to allow a "forced resignation" (vs. termination with cause and criminal prosecution) based on full restitution, the nonprofit should obtain a signed plan and schedule for payment.
- Disclosure to Auditors/CPA. Will likely need assistance in filing IRS Form 4720 if an officer or director is involved and excess benefit rules apply.
- Disclosure on Form 990 for appropriate filers.
- Review of insurance policy for claims procedure if employee embezzlement has occurred.
- Establishment and/or review of internal controls and documentation of such policies.
- Decision whether and how to announce publicly.

A fuller discussion of the legal and fiduciary obligations triggered when nonprofits experience asset diversion will be posted in a new client alert on the Public Counsel website in January 2014.

The Community Development Project has advised clients about how to respond to theft or embezzlement issues and can assist you if this is a matter of concern. For more information, please call our intake line at (213) 385-2977 ext. 200 or email cdp@publiccounsel.org.

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### Responding to Negative Social Media: Employee Postings (Part II)

In our last newsletter we discussed how to respond when a client or supporter writes a negative online review of your nonprofit organization. Now imagine one of your employees goes home from work and posts a variety of complaints about low salaries, incompetent management, and lazy co-workers on his or her personal Facebook account. A few other co-workers chime in, agreeing with some of the comments about your organization. This posting, available to hundreds of the employee’s friends and the general public, obviously upsets the board and damages the nonprofit's reputation. Before management rushes to respond, however, it is important to consider the fact that disciplining the employee for his or her employment-related posts may constitute a violation of federal labor law.

Employee terminations resulting from postings on social media sites, known as "Facebook firings," have been gaining widespread attention in recent years, including from the National Labor Relations Board (NLRB), the federal
agency charged with enforcing the National Labor Relations Act (NLRA). The NLRA is a federal law designed to protect the rights of private-sector, including nonprofit, employees and employers. The NLRB has taken the position that firing an employee for his or her social media activity may be a violation of Section 7 of the NLRA, which protects employees’ rights to communicate with one another regarding the terms and conditions of their employment without fear of retribution. Generally speaking, all "concerted" activity by individual employees who are united in pursuit of a common goal is protected. In the scenario above, the mere fact that the employee’s co-workers read and responded to the post may protect the initial posting activity under the NLRA.

Determining if a particular posting is protected under the NLRA requires analysis of the specific facts and circumstances and is beyond the scope of this article. It is important, however, for employers to understand that firing or taking disciplinary action as a result of a protected activity may constitute an unfair labor practice in violation of the NLRA. There have been a number of recent cases where employees were reinstated or awarded monetary damages following "Facebook firings" in situations where the postings were considered protected.

In order to steer clear of restricting protected activity under the NLRA, but still prevent negative postings and have a clear framework for discipline in the event the postings are made regardless, employers should implement a social media policy as part of their employee handbook. An employer drafting or reviewing a social media policy should consider the following five tips:

1. **Avoid overly broad policies and restrictions.** A social media policy should include the employer’s policy objectives and provisions should be tailored narrowly to not prohibit "concerted activity" via social media, meaning, for instance, discussion among co-workers regarding terms and conditions of employment. Overly broad policies have been found to violate the NLRA.

2. **Focus on preventing the dispute.** The primary focus should be on preventing a dispute from arising. Even a simple reminder that any posting may be public, or seen by other employees, may be enough to prevent an employee from venting through social media.

3. **Consider what happens if an issue does arise.** Having a defined process for discipline for violations of the social media policy will ensure that the employer treats all employees fairly and is able to react to negative social media postings quickly and effectively.

4. **Educate your employees.** Give a detailed description of which speech is protected, and which is not. Employees should be aware of their rights but also aware that they cannot post with impunity.
5. **Keep the policy up to date.** In light of the increasing and changing use of social media and NLRB scrutiny, employers should regularly review their policies to ensure compliance with the most recent developments.

The NLRB has released reports detailing the results of investigations in dozens of social media cases. These reports are available at the NLRB website.

*If you would like to request legal assistance in crafting or reviewing a robust Internet use and social media policy for your organization, please call our intake line at (213) 385-2977, ext. 200 or email cdp@publiccounsel.org.*

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**Employment Law Developments for 2014**

Earlier this year, California Governor Jerry Brown signed into law a number of bills that significantly impact California nonprofit employers. Below is an overview of a few of these new laws, effective January 1, 2014. **In light of these important legal changes, it is advisable to review and update your organization's employment policies and procedures.** If your organization needs legal assistance with reviewing and updating its employment manual and policies, or other employment law issues, please visit our website.

**Protection for Exercising Rights under the Labor Code**

AB 263 amends California Labor Code section 98.6, making it illegal to retaliate against an employee who has complained to the employer, orally or in writing, that he or she is owed unpaid wages, and creating a civil penalty of up to $10,000 per violation. Previously, the law only explicitly prohibited discharge and discrimination as a result of a complaint.

**Criminal Penalty for Failing to Remit Withholdings**

California Labor Code section 227 makes it a crime for an employer to willfully or with the intent to defraud fail to remit agreed-upon payments to health and welfare funds, pension funds, or other various benefit plans. A violation is punishable as a misdemeanor, but rises to a felony where the amount the employer fails to remit exceeds $500. SB 390 amends this law, **making it a crime for an employer to fail to remit withholdings from an employee's wages** that were made pursuant to state, local, or federal law (e.g., taxes).

**Sexual Harassment Definition Clarified**

SB 292 amends the California Fair Employment and Housing Act (FEHA) to clarify that sexually harassing questions relating to forming a nonprofit and obtaining tax exemption.

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**Advance registration is required.** For more information and to register for the seminar, please visit our website.

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**CDP eNewsletter Archive**

Have you recently joined our mailing list and feel like you've been missing out on great information? If so, we have good news! Previous issues of the CDP eNewsletter are available on our website.

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**Legal Services for Nonprofits**

The Community Development Project builds strong foundations for healthy, vibrant and economically stable communities by providing comprehensive legal and capacity building services to organizations serving people with lower-incomes in the Los Angeles area. CDP provides assistance on a wide range of matters to community organizations, including:

- **Contract & Lease Renegotiation**
- **Modification & Reduction of Workforce**

**Does your nonprofit need to terminate or renegotiate contractual or lease obligations? Do you know whether your nonprofit is legally permitted to sublet unused space?**

**Sexual Harassment Definition Clarified**

SB 292 amends the California Fair Employment and Housing Act (FEHA) to clarify that sexually harassing
conduct may be considered sex harassment **even if not motivated by sexual desire.** While this new law is most applicable to claims of same-sex harassment, it applies to different-sex harassment claims as well.

**Protection for Military and Veterans**

AB 556 amends FEHA to add "**military and veteran status**" to the list of categories protected from employment discrimination. "Military and veteran status" includes members or veterans of the U.S. Armed Forces, Armed Forces Reserve, and National Guard, as well as the California National Guard. In addition, AB 556 specifically allows employers to inquire about an applicant's or employee's military or veteran status for the purpose of awarding a veteran's preference as permitted by law. Employers should review and revise their employment policies and handbooks to add this new protected category.

**Protections for Employees Who Are Crime Victims**

California Labor Code section 230 currently prohibits an employer from retaliating against an employee who is a victim of domestic violence or sexual assault for taking time off from work in connection with court proceedings or to seek medical attention and other specified services as a result of these crimes.

**SB 400 extends this protection to employees who are victims of stalking.** The new law also prohibits retaliation against an employee because of his or her status as a victim of domestic violence, sexual assault or stalking if the employee/victim provides notice to the employer or the employer has actual knowledge of this status. In addition, SB 400 requires employers to provide reasonable accommodations to employees who are victims of domestic violence, sexual assault or stalking and request an accommodation for their safety while at work. Employers are prohibited from retaliating against an employee who has requested a reasonable accommodation, whether the request was granted or not.

SB 288 adds California Labor Code section 230.5, which prohibits employers from retaliating against an employee who is a victim of certain crimes for taking time off from work to appear in any court proceeding in which a substantive right of the employee/victim is at issue. The time off is unpaid, but an employee has the right to use accrued vacation or other paid time off to cover the absence. The employee must give reasonable advance notice unless not practicable. The specified offenses covered by this law include vehicular manslaughter while intoxicated, hit-and-run causing death or injury, sexual assault, and various other felonies. The term "victim" includes the employee's spouse, parent, child, sibling, or guardian. Employers should adopt a procedure for responding to requests for time off that may be protected by this law and a procedure for obtaining appropriate documentation to verify the need for time off.

**you attempting to reclassify employees as independent contractors? Are you aware of the legal implications of all of these actions?**

**Corporate Governance**

Is your board aware of its duties during a period of financial difficulty? Do your board members know how to conduct financial and programmatic oversight? Has your organization adopted a conflict of interest policy? Are your directors aware of the situations where they could incur personal liability for the acts of the corporation, and do you have appropriate controls and procedures in place to protect them?

**Debt Reorganization & Cash Flow**

Does your nonprofit need to renegotiate debt repayment terms? Do you know what agreement terms you should pay special attention to if applying for or increasing a line of credit? Have any of your key vendors filed for bankruptcy?

**Fundraising & Social Enterprise**

Is your nonprofit considering alternative fundraising methods (e.g., loans from directors, starting a for-profit business, joint-ventures, etc.)? Do you know how to structure these activities to protect your tax-exempt status? Are you aware of the legal ramifications of using restricted or endowment funds to pay ongoing expenses?

**Mergers & Strategic Alliances**

Is your nonprofit considering a merger or consolidation to save or expand programs? Do you know the difference between a formal merger and other types of strategic
Protections for Undocumented Workers

AB 263 adds California Labor Code section 1019, which makes it unlawful for an employer to engage in an unfair immigration-related practice against a worker in retaliation for exercising a legal right under the Labor Code. Prohibited practices include: (1) requesting more or different documents than are required under federal immigration law, or refusing to honor documents that appear genuine on their face; (2) using the federal E-Verify system to check the employment authorization status of a person at a time or in a manner not required under federal law or not authorized under the system; (3) threatening to file or the filing of a false police report; or (4) threatening to contact or contacting immigration authorities. The law creates a rebuttable presumption that an adverse action taken within 90 days of the employee exercising a protected right is retaliatory.

SB 666 amends various sections of the California Business and Professions Code and Labor Code and makes it an "adverse action" for purposes of establishing discrimination or retaliation to report or threaten to report to a government agency the suspected citizenship or immigration status of an employee, a former employee or a prospective employee, or a member of their family, because the person has exercised a right under the Labor, Government or Civil Codes. Certain licensed businesses may have their licenses suspended or revoked for taking an adverse action.