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7 **STATE OF CALIFORNIA**
8 **BOARD OF EQUALIZATION**

9
10 In the Matter of the Petitions)
Appealing the Denial of Claims for)
11 Organizational Clearance Certificates for)
12)
13)
14 **ALLIANCE MEMBER SERVICES, INC.**)
2006 -2009)
15)
16 **NONPROFITS' INSURANCE ALLIANCE**)
OF CALIFORNIA)
2008-2009)
17)
18 Petitioners)

APPEALS DIVISION
REVISED HEARING SUMMARY
FOR ORAL HEARING ON
PROPERTY TAX PETITIONS

Appeal No: WEC 08-003
Case ID No: 472460

Appeal No: WEC 08-004
Case ID No: 472465

19 For Petitioners:

Barbara A. Goode, Esq.

20 For Property and Special
21 Taxes Department:

Andrew Jacobson
Tax Counsel

22 For Appeals Division:

Louis A. Ambrose
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23 **ISSUE PRESENTED**

24
25
26 **Whether petitioners Alliance Member Services, Inc. (AMS) and Nonprofits' Insurance Alliance of**
27 **California (NIAC) (collectively, "petitioners") have established that respondent County-Assessed**
28 **Properties Division (respondent) erred in its determination that petitioners do not qualify for**
organizational clearance certificates (OCC) because petitioners are not organized and operated
exclusively for charitable purposes pursuant to Revenue and Taxation Code (R&TC) section 214.

1 (NIAG)¹. In 2001, NIAC's board formed another liability risk pool, Alliance of Nonprofits for
2 Insurance – Risk Retention Group (ANI-RRG), for tax-exempt entities located outside California.
3 Initially, NIAC shared the same personnel with ANI-RRG but was advised that, for accounting
4 purposes, the better practice would be for NIAC and ANI-RRG to contract with a third party for staffing
5 and other support services. As a result, AMS, a nonprofit corporation, was formed to provide staff,
6 services and support to NIAC and ANI-RRG as the third-party company. AMS has been granted both
7 federal and state income tax exemptions. (Pet. Reply Br., exhibit B.) In 2006, AMS executed Amended
8 and Restated Articles of Incorporation. NIAC owns the property located on Front Street in Santa Cruz
9 which is used for NIAC's headquarters and the property is operated by AMS. (Resp. Open. Br., pp. 3-4.)

10 On December 11, 2003, respondent updated NIAC's existing welfare exemption status in
11 accordance with the new statutory provisions for administration of the welfare exemption and issued an
12 OCC to NIAC as a nonprofit corporation organized and operated for charitable purposes within the
13 meaning of the property tax welfare exemption. On March 5, 2006, AMS filed a claim for an OCC
14 which respondent denied based on a finding that AMS was not organized and operated for charitable
15 purposes in accordance with R&TC section 214, subdivision (a). On that same date, respondent also
16 revoked NIAC's OCC on the grounds that it had been granted in error and based on a finding that it was
17 not organized and operated for charitable purposes in accordance with R&TC section 214, subdivision
18 (a). Petitioners timely filed petitions to appeal the denial of their OCC claims. (Resp. Open. Br., pp. 4-
19 5.)

20 Parties' Contentions

21 Petitioner's Contentions

22 Charitable Purpose

23 Each petitioner contends that it qualifies for an OCC because it is organized and operated for
24 charitable purposes. Petitioners dispute respondent's position that they operate for the benefit of their
25 member organizations and that their operations provide a general community benefit. (Petition, p. 1.)
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27

28 ¹ The other two members of NIAG are Alliance of Nonprofits for Insurance, Risk Retention Group, Inc. (ANI-RRG) and the National Alliance of Nonprofits for Insurance (NANI).

1 Petitioners disagree with respondent’s contention that petitioners’ activities are not necessary for
2 the welfare of the community, not a service that government would be otherwise compelled to provide
3 and are “predominantly” a private sector function. Petitioners argue that the fact that activities may be
4 performed by the private sector has no bearing on whether those activities benefit the community as a
5 whole. In support of their argument, petitioners cite their exhibit A, an agreement between San Diego
6 County and a nonprofit group home provider for children which includes liability insurance provisions
7 mandated by the county. Based on these provisions, petitioners contend that the group homes could not
8 exist without liability insurance so that those services are possible as a result of the provider’s
9 participation in petitioners’ risk sharing pool. Thus, petitioners contend that the provider’s ability to
10 purchase insurance from a commercial, for-profit company is irrelevant to a determination of
11 petitioners’ charitable purpose. Petitioners conclude that, through the nonprofit risk pool, the group
12 home services are available to San Diego County and with “the assistance of accident reduction, safety
13 and counselor training programs”, the group home provider and petitioners improve the entire San
14 Diego County community. (Pet. Reply Br., pp. 6-8.)

15 General Community Benefit

16 In addition to their liability risk pool activities, petitioners state that they sponsor an Internet-
17 based newsletter called the “Blue Avocado” which provides support and information to community
18 nonprofits by offering resources for all nonprofits. Petitioners also offer free training and educational
19 materials in risk management that are available to the larger nonprofit community. As further evidence
20 that they have a charitable purpose, petitioners point to the support that they have received from private
21 foundations and state agencies. Petitioners state that they have received over \$10 million from the Bill
22 and Melinda Gates Foundation and the David and Lucile Packard Foundation, which shows that these
23 foundations recognize that petitioners directly benefit the community and that the activities of
24 petitioners, as well as the participant nonprofits’ activities, need to be supported financially. Petitioners
25 also state that funds for the purchase of their offices came from tax-exempt bonds issued by the
26 California Communities Development Authority (Authority) which issues bonds for qualifying
27 California tax-exempt entities. Petitioners state that the Authority requires that each nonprofit applicant
28

1 and the proposed project “demonstrate a clear public benefit to the community in which the project will
2 reside.” (Pet. Reply Br., pp. 9-10.)

3 Petitioners argue that the California Supreme Court has consistently interpreted the term
4 “charitable” broadly and has broadly construed activities that confer a general community benefit. As
5 support for that proposition, petitioners cite *Lundberg v. Alameda County* (1956) 46 Cal.2d 644 and
6 *Stockton Civic Theatre v. Board of Supervisors* (1967) 66 Cal.2d 13. Petitioners assert that the *Stockton*
7 *Civic Theatre* case is “especially instructive” in that a community theater was engaged in the same
8 activity as commercial theaters, the community theater’s productions were enjoyed only by ticketholders
9 and the theater charged ticket fees to offset operating expenses. Petitioners contend that the Supreme
10 Court rejected a narrow interpretation of charitable intent and community benefit and “found a
11 charitable purpose and benefit to the larger Stockton community simply because there was a community
12 theater.” In view of that holding, petitioners argue that their activities must also be considered as
13 benefiting the larger community regardless of the fact that there are commercial enterprises that insure
14 nonprofits. Moreover, petitioners argue, they are unlike commercial insurers in that their directors come
15 from the nonprofit community and they offer services not provided by commercial insurers. Finally,
16 petitioners maintain that charitable foundations are willing to donate based on petitioners’ commitment
17 to the nonprofit community and the larger community and the fact that the only beneficiaries of
18 petitioners’ activities are nonprofit tax-exempt organizations and the communities they serve. (Pet.
19 Reply Br., pp. 10-11.)

20 Post-Conference Briefing

21 In post-conference briefing, petitioners provide documentation which they contend supports their
22 position that “NIAC and AMS are unique charitable organizations that support the public good.” The
23 information provided is intended (1) to show how NIAC and ANI-RRG establish their premiums and
24 how that process is different than commercial insurers and (2) to explain the NIAC dividend plan which
25 is the process by which premium monies are returned to participants. (Pet. Post-Conf. Br., pp.1-2.)

26 With respect to the premium-setting process, the document explains that industry-generated
27 recommended rates are used as a starting point for determining pricing but NIAC’s underwriting and
28 pricing practices are different from commercial carriers in that NIAC’s underwriters are encouraged to

1 learn how each nonprofit operates so as to provide full coverage for its activities, rather than looking for
2 ways to exclude certain hazards. In addition, petitioners state that, unlike a commercial insurer, NIAC's
3 loss control director will work with a nonprofit with frequent claims to avoid future claims and will
4 increase a premium as a result of claims activity only as a last resort. Petitioners further explain that a
5 premium is increased (and occasionally a nonprofit is not renewed) for repetitive claims activity only
6 when the nonprofit has not shown an interest in preventing future claims. (Pet. Post-Conf. Br., exhibit
7 A.)

8 The dividend plan document explains that the "company wide dividend" is determined as a
9 percentage of total gross written premiums for the calendar year ended three years prior to the most
10 recent calendar year. Member dividends are payable only as a credit against renewal premiums and
11 computed based on "loyalty credit" and "loss ratio credit" and members with loss ratios exceeding 60
12 percent for the period are not eligible for member dividends for that period. The document further
13 explains that the dividend plan allocates the benefits of better-than-expected financial results to
14 members on an equitable basis. (Pet. Post-Conf. Br., exhibit B.)

15 Petitioners state that they conduct many public activities with benefits to the general public and
16 the nonprofit community at large which are available without becoming a member of NIAC or ANI-
17 RRG. As evidence of such activities, petitioners attach a schedule of public presentations by staff of
18 NIAC and ANI-RRG. Petitioners also present as exhibit D to the brief a document that presents three
19 additional ways in which they serve the general public, as follows: (1) an on-line magazine called the
20 Blue Avocado, (2) the Nonprofit Congress, and (3) BOARDnetWORK, which is described as a publicly
21 available tool to assist nonprofit boards of directors. (Pet. Post-Conf. Br., exhibits C and D.)

22 Petitioners also state that the legislative history of IRC section 501(n) evidences a public policy
23 to assist in the formation of nonprofit liability risk pools and quotes a U.S. House of Representatives
24 report that states that the legislation "will help make liability insurance more affordable to charitable
25 organizations." Petitioners assert that NIAC and ANI-RRG were formed at times during which liability
26 insurance was either difficult for nonprofits to obtain or the variability of the cost of commercial
27 insurance was difficult for nonprofits to manage. (Pet. Post-Conf. Br., p. 3 and exhibit E.)
28

1 In a supplemental brief, petitioners contend that the legislative history of the bill under which
2 NIAC was created, Assembly Bill 3545 of the 1986 Regular Session (AB 3545), shows that the bill had
3 broad support by local governments that considered risk pools as a means of making public services
4 more available and by charities that viewed them as a benefit to the public. Petitioner cites support for
5 the bill from local governments which considered the legislation to be a means of enabling community-
6 based organizations to provide services and, thereby, conserve general revenue monies. Petitioners note
7 that nonprofit organizations supported the legislation and quote the United Way of California which
8 stated that “[t]he current crisis in the availability and affordability of liability insurance has had a broad
9 and erosive impact on health and human services in our communities”. Petitioners also note that the
10 United Way proposed a three-pronged approach to the crisis by supporting the legislation, conducting
11 risk management training and examining the feasibility of alternative insurance arrangements. By
12 comparison, petitioners contend that their activities are “three-pronged” and that, more importantly,
13 more than 9,500 charitable organizations obtain the benefits of petitioners’ liability risk pools. (Pet.
14 Supp. Br., pp. 1-3 and exhibits.)

15 **Respondent’s Contentions**

16 Respondent contends that petitioners’ insurance underwriting and sales activities do not meet the
17 community benefit test necessary to qualify as charitable under R&TC section 214, subdivision (a).
18 Respondent explains that in order to qualify as “charitable” under R&TC section 214, subdivision (a), an
19 organization’s activities must provide a general community benefit or, if those activities provide a
20 specific benefit to a limited portion of the community, then they must serve to lessen the burdens of
21 government. Respondent contends that petitioners’ commercial insurance underwriting and sales
22 activity does not provide “a benefit to the community as a whole or an unascertainable and indefinite
23 portion thereof” and that those activities do not “lessen the burdens of government”. Respondent points
24 out that the California Court of Appeal has qualified the test by holding that “a more direct and
25 demonstrable benefit to the community at large” is required in order to qualify as a charitable purpose, if
26 “the institution’s purpose has received relatively little recognition in judicial decisions and governmental
27 programs.” (*Clubs of California for Fair Competition v. Kroger* (1992) 7 Cal.App.4th 709, 716-717.)
28

1 Respondent further contends that the courts have not allowed the welfare exemption to
2 organizations that perform services with “no measurable benefit to the broader community” and cites, as
3 examples, the denial of the welfare exemption to a junior college with a one-year course for morticians
4 and funeral personnel and a vocational training school for construction industry workers. Respondent
5 argues that petitioners’ activities provide a service to other nonprofit organizations and are not open to
6 the community as a whole. Respondent disputes petitioners’ characterization of their member nonprofit
7 organizations as “the community” for purposes of welfare exemption law. Respondent asserts that
8 petitioners were created by their “member insureds to provide a reliable source of insurance for
9 themselves” and respondent describes the “beneficiaries” of petitioners’ activities as the members who
10 are entitled to receive dividends. On those bases, respondent concludes that petitioners are more similar
11 to the industry trade schools that confer only private benefit. (Resp. Open. Br., pp. 11-13.)

12 Respondent also contends that petitioners’ insurance activities are predominantly performed by
13 the private sector and, thus, not a service which “the government would otherwise be compelled to
14 provide for the community.” Respondent rejects petitioners’ argument that the liability risk pool activity
15 enables nonprofits to provide a community benefit as positing a relationship between petitioners and the
16 community that is “too attenuated to satisfy the community benefit test.” (Resp. Open. Br., p. 13.)

17 Post-Conference Briefing

18 With respect to the information about activities that petitioners claim provide a general
19 community benefit, respondent contends that those activities are services provided primarily to
20 petitioners’ members. Respondent argues that the Blue Avocado serves in part to advertise and increase
21 access to petitioners’ insurance services and provides a professional benefit to organizations, board
22 members and employees of the nonprofit industry rather than to the community as a whole or an
23 unascertainable and indefinite portion thereof. Despite evidence that NIAC made a grant of \$100,000 to
24 the Nonprofit Congress and Blue Avocado, which respondent states may be a charitable activity,
25 respondent contends that petitioners’ primary activity is not grant-making, but rather insurance
26 underwriting and sales to member nonprofits. Respondent also notes that NIAC’s support for these
27 activities “may also serve to increase awareness of petitioners’ insurance underwriting services.”
28

1 With respect to BOARDnetWORK, the document storage website, respondent states that
2 petitioners acknowledge that the service is generally available only to member insureds at petitioners'
3 cost. For that reason, respondent finds no general community benefit. Respondent also concludes that
4 access to petitioners' webinars, because of the fees charged and the technical subject matter, is mostly
5 restricted to petitioners' members and other nonprofits interested in purchasing petitioners' services
6 rather than members of the whole community. (Resp. Post-Conf. Br., pp. 2-6.)

7 With respect to petitioners' analysis of the legislative history of IRC section 501(n), respondent
8 contends that there is no indication from that history that Congress' primary concern was a scarcity of
9 liability insurance available to nonprofits. Respondent also asserts that an organization that meets the
10 requirements for a tax exemption pursuant to IRC sections 501(c)(3) and 501(n) does not necessarily
11 also meet the requirements for the welfare exemption. (Resp. Post-Conf. Br., p. 8.)

12 Applicable Law

13 Welfare Exemption

14 General Requirements

15 Under California law, property owned by qualifying nonprofit organizations and used
16 exclusively for religious, hospital, scientific or charitable purposes is eligible for the property tax
17 welfare exemption. (Calif. Const. Art. XIII, § 4(b); Rev. & Tax. Code, § 214 et seq.) For a nonprofit
18 organization to qualify, that organization must be both organized and operated such that the primary
19 purpose is for one or more exempt purposes, i.e., religious, hospital, scientific or charitable. (Rev. &
20 Tax. Code, § 214, subd.(a).) The standards for determining whether an organization has demonstrated
21 by its activities that it is organized and operated for charitable purposes have been developed by case
22 law.

23 Under R&TC section 214.8, subdivision (a) a welfare exemption may not be granted (with
24 specific exceptions not applicable here) unless the claimant organization is qualified as exempt from
25 federal income tax under IRC section 501(c)(3) or state income tax under R&TC section 23701d.
26 Subdivision (a) further provides that the section shall not be construed to enlarge the welfare exemption
27 to apply to organizations qualified under IRC section 501(c)(3) but not otherwise qualified for the
28 welfare exemption under other provisions of the R&TC.

1 Pursuant to R&TC section 254.6, subdivision (a) an organization that intends to claim the
2 welfare exemption shall file a claim for an OCC with the Board. Under subdivision (c), the Board staff
3 is charged with reviewing OCC claims to ascertain whether the claimant organization meets the
4 requirements of R&TC section 214. The items considered by staff include, among other factors,
5 whether “[t]he services and expenses of the owner or operator (including salaries) are excessive, based
6 upon like services and salaries in comparable public or private institutions” and whether “[t]he
7 operations of the owner or operator, either directly or indirectly, materially enhance the private gain of
8 any individual or individuals.” (Rev. & Tax. Code, § 254.6, subd. (b).)

9 Charitable Purpose

10 The California Supreme Court has broadly construed the charitable purpose aspect of the welfare
11 exemption to include a wide range of humanitarian activities, rendered at cost or less, the object of
12 which is the care of the physical and mental well-being of the recipients. (Assessors’ Handbook section
13 267, *Welfare, Church and Religious Exemptions* (Oct. 2004) (AH 267), p. 2, (citing *Fredericka Home*
14 *for the Aged v. County of San Diego* (1950) 35 Cal.2d 789, 793.) In *Lundberg v. Alameda County*,
15 *supra* at p. 649, the court held that “charity” is

16 a gift to be applied consistently with existing laws, for the benefit of an indefinite number
17 of persons—either by bringing their hearts under the influence of education, or religion,
18 by relieving their bodies from disease, suffering, or constraint, by assisting them to
19 establish themselves in life or by erecting, or maintaining public buildings or works, or
20 otherwise lessening the burdens of government. (*quoting Estate of Hahn* (1925) 196 Cal.
21 778, 781-782.)

22 In *Stockton Civic Theatre, supra*, at pp. 19-20, the court held that *charitable* was to be broadly
23 construed in line with previous decisions and concluded that charitable activities include “a wide range
24 of activities beneficial to the community.” The primary test is whether the activity provides a general
25 community benefit whose “ultimate recipients are either the community as a whole or an unascertainable
26 and indefinite portion thereof.”

27 In the *House of Rest of Presbyterian Church v. County of Los Angeles* (1957) 151 Cal.App.2d
28 523, a non-profit corporation was formed for the purpose of providing a “house of rest” for missionaries

1 and other Christian workers to stay in the United States. The corporation owned and operated an
2 apartment building that was used to house missionaries of the foreign and national boards of the
3 Presbyterian Church in the United States and for workers of the Young Men's and Young Women's
4 Christian Associations who were on furlough from their missions. The apartment units were completely
5 furnished and missionaries on furlough would pay a token rent, which included utilities and a cleaning
6 charge.

7 With respect to determining whether the property was "used exclusively for charitable
8 purposes", the court held that the test is whether the use of the property is "incidental to and reasonably
9 necessary" for the accomplishment of such purposes. In this regard, the court stated that "[t]he
10 integrated activities as a whole must be examined in determining the tax status of property for the
11 welfare exemption." The court found that the property was maintained as an integral part of the
12 religious and charitable operations of the Presbyterian Church because it was used solely to carry out the
13 program of spreading Christianity throughout the world. Thus, the court concluded that the property
14 was "incidental to and reasonably necessary for the accomplishment of plaintiff's religious and
15 charitable purposes and that it is used exclusively for those purposes." (Id. at pp.532 and 536.)

16 Community Benefit

17 With respect to the nature of the community benefit required, the court of appeal observed in
18 *Clubs of California, supra*, that courts are likely to require only an indirect public benefit if the
19 organization serves an interest historically regarded as being closely tied to the public welfare.
20 However, if the organization's purpose is not so recognized in judicial decisions and governmental
21 programs, then the courts will require a more direct and demonstrable benefit to the community at large.
22 (Id. at p. 717.) The community benefit test has been applied by the courts to exempt other activities as
23 charitable if the class benefited by the activity is sufficiently large that a gift to it may be considered to
24 benefit an indefinite portion of the community. However, an organization may still be considered
25 charitable even if its benefits are confined to the members of a certain segment of the public, such as a
26 particular race or creed, provided no special advantage is given to members of the organization or to
27 particular individuals. (AH 267, p.4.)
28

1 Charging of Fees

2 Any fees charged will not necessarily prevent a charitable purpose determination if used to pay
3 the expenses of the operation and not to profit the founders or shareholders and if the income is in the
4 normal pursuit of the organization's exempt purposes. However, the amount of the fees may affect the
5 degree to which the activity is open to the community as a whole. (*Clubs of California, supra* at p. 717.)

6 In *YMCA v. County of Los Angeles* (1950) 35 Cal.2d 760, the court held that rental fees charged
7 by the YMCA for lodging in its dormitory facilities was not a basis for denying the welfare exemption
8 because the operation of those facilities accomplished the organization's charitable purpose of
9 "providing for the welfare of young men and boys of moderate earning capacity and income, through the
10 maintenance of lodging quarters at a minimum cost so that they may have a place of study, recreation
11 and abode, under wholesome and decent influences and with proper protection and guidance designed to
12 foster good citizenship and inculcate Christian ideals and character." (Id. at p. 769.)

13 The court found that the YMCA's dormitory accommodations appeared to be reasonably
14 necessary to carry out its general program as "a base of operations" to disseminate its "commonly
15 recognized influences and teachings directed to the elevation and betterment of young men and boys"
16 and "provides complete recreational facilities as well as opportunities to participate in activities intended
17 to promote moral and spiritual well-being." (Id. at p. 767.) The court further found that the moderate
18 rental fees generated income that was used to defray operating expenses but that there was no real profit
19 motive as the lodging activity was integrated into plaintiff's recognized religious and charitable
20 objectives. (Id. at p. 771.)

21 Charitable Contributions

22 Although the level of contributions to an organization is an important criterion for determining
23 charitable purpose, the absence of contributions alone is not conclusive evidence that no charitable
24 purpose exists if it can be shown that the organization is providing a benefit or gift to the community.
25 In addition, a charitable purpose may be demonstrated if the organization receives a government subsidy
26 or funding which is used to provide benefit to the community as a whole or an unascertainable and
27 indefinite portion thereof. (AH 267, p. 5.)
28

Appeals Division Analysis and Comments

As the case law decisions show, the courts have broadly construed the types of activities that have a “general community benefit”. Petitioners argue that their primary activity of operating a liability risk pool is charitable based on the following:

- Liability insurance is necessary for the operation of the member nonprofits which, otherwise, could not provide their services.
- Petitioners were formed as a result of the lack of a reliable, reasonably priced market for liability insurance for nonprofit organizations.
- By participating in petitioners’ risk pool, the member nonprofits are able to provide their services which benefit the general community.
- In addition, the risk management procedures and practices engendered by petitioners’ activities help to reduce the number of accidents in the larger community and thereby provide a general community benefit.

Respondent believes that petitioners’ liability risk pool activity provides a benefit to its member insureds but does not provide a benefit to the community as a whole or an unascertainable and indefinite portion thereof. With respect to any indirect general community benefit, respondent argues that petitioners do not meet the test because the government would not otherwise be compelled to provide liability insurance to the member nonprofits. Respondent also suggests that, under the holding of *Clubs of California, supra*, petitioners should be required to show “a more direct and demonstrable” general community benefit because petitioners’ “purpose has received relatively little recognition in judicial decisions and governmental programs.”

In *House of Rest, supra*, the nonprofit corporation’s activities of maintaining and operating an apartment house directly benefited furloughed missionaries and their families but, as the court found, was incidental to and reasonably necessary for the accomplishment of and used exclusively for the religious and charitable purposes of the Presbyterian Church. The court reached that conclusion by examining “the integrated activities as a whole” which, it seems, involved tying the activities of a separate nonprofit corporation to the activities of the Presbyterian Church.

1 In the view of the Appeals Division staff, it appears that petitioners are similarly asking
2 respondent to view as “integrated” their liability risk pool activities and the activities of the member
3 nonprofits in determining whether petitioners’ activities have a charitable purpose. At the hearing, the
4 parties should be prepared to address the holding in *House of Rest, supra* and discuss whether it is
5 applicable to or distinguishable from the facts presented here.

6 With respect to respondent’s suggestion that petitioners’ “purpose has received relatively little
7 recognition in judicial decisions and governmental programs”, so that petitioners must establish a more
8 direct general community benefit. However, the Appeals Division staff notes that the legislative history
9 materials for AB 3545 indicate that the Legislature was made aware of the importance of liability risk
10 pool sharing for nonprofit organizations prior to passing this legislation. At the hearing, the parties
11 should be prepared to discuss the significance of that legislative history in the context of governmental
12 recognition for this purpose.

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