

# REGULATION OF CHARITIES BY THE CALIFORNIA ATTORNEY GENERAL



# Outline of Presentation

- ★ Overview of AG's Oversight Responsibilities
  - AG's Registry of Charitable Trusts
  - Enforcement Program
- ★ Duties of Charities and their Directors, Officers, and Trustees
- ★ Charity Fundraising
- ★ Donor Tips
- ★ Raffles

# Overview

- ★ AG has primary responsibility for overseeing charities and charitable solicitations
  - Includes charitable corporations, unincorporated associations and charitable trusts; also fundraising professionals
  - AG responsible for protecting charitable assets because they benefit all Californians

# Overview

- ✦ Charitable Trusts Section carries out the AG's responsibilities
- ✦ Composed of
  - ✦ Registry of Charitable Trusts
  - ✦ Legal and Audits Unit

# The Registry's Role

- ☀ Manages registration and annual reporting requirements
  - Initial registration within 30 days of receiving assets (money, real property, or other assets)
  - Initial registration requires a copy of governing instrument, IRS Form 1023, and bylaws (see Registration Checklist at [www.oag.ca.gov/charities](http://www.oag.ca.gov/charities))
  - Annual reporting (IRS Form 990 and RRF-1)
  - Exempt from registration and reporting, but not oversight: religious corporations, educational institutions, hospitals, health care service plans

# The Registry's Role

Receives and reviews notices of specific transactions required to be submitted to AG:

- Sale/disposition of substantially all assets
- Voluntary dissolution
- Merger
- Conversion (to mutual benefit or for-profit )
- Self-dealing transactions
- Loans to directors/officers
- Sale/transfer of nonprofit hospital facilities  
(Corp. Code, § 5000 *et seq.*)

# Transactions Requiring AG Notice or Consent\*

## ☀ Consent:

- ☀ Voluntary dissolution – requires AG waiver of notice
- ☀ Conversion to mutual benefit or for-profit corporation
- ☀ Merger involving a nonprofit public benefit corporation and a for-profit corporation
- ☀ Loans to directors and officers (with exceptions)
- ☀ Sale or transfer of nonprofit health facility

## ☀ 20-Day Notice Only:

- ☀ Sale or disposition of substantially all assets
- ☀ Merger involving two nonprofit public benefit, or religious, corporations

\*See Nonprofit Transactions Guide at [www.oag.ca.gov/charities](http://www.oag.ca.gov/charities)

# Enforcement Program

- ★ AG safeguards, preserves, and recovers charitable assets through investigations, audits and legal actions
- ★ Focus: mismanagement and diversion of charitable assets from intended use
- ★ Cases developed from complaints received and review of annual filings



# Types of Enforcement

- ✦ Informal contact; audit letter
- ✦ Subpoena
- ✦ Corrective action letter
- ✦ Assurance of voluntary compliance
- ✦ Administrative action
- ✦ Civil litigation
- ✦ Criminal charges

# Attending to Governance

- ☀ Directors and Officers are responsible for managing and preserving charitable assets
- ☀ CA Nonprofit Public Benefit Corporation Law governs Board duties and responsibilities
- ☀ Activities and affairs of a corporation must be conducted, and all corporate powers exercised, by or under the direction of the Board
- ☀ This ultimate decision-making role cannot be delegated to anyone else

\*See parts VI and VII of Form 990, and Guide to Form 990 at [www.oag.ca.gov/charities](http://www.oag.ca.gov/charities)

# Attending to Governance: Board Duties and Responsibilities

- ★ Statutory standard: a director must perform his/her duties
  - In good faith
  - In a manner the director believes to be in the best interest of the organization
  - With such care, including reasonable inquiry, as an ordinarily prudent person would do in the same position under similar circumstances



# Attending to Governance: Critical Principles

- ✦ Be actively engaged and attentive: ask questions and demand answers!
- ✦ Scrutinize budgets and keep an eye on potential risks
- ✦ Avoid conflicts of interest and self-dealing transactions
- ✦ Scrutinize executive compensation
- ✦ Make sure Officers and key employees are doing their jobs
- ✦ Closely examine and monitor fundraising practices and activities

# Governance: Critical Principles (con't.)

- ★ Charity Officers and Directors are accountable for charitable assets
- ★ Officers/Directors may be personally financially liable for harm their actions/inaction caused the charity

# Caution: Use of Restricted Assets

- ✦ Assets are restricted by charity's governing documents, donor designation, or content of solicitation
- ✦ Duty to use in accordance with restriction
- ✦ Must be able to account for use in accordance with restriction
- ✦ Avoiding problems:
  - ✦ Segregate
  - ✦ Scrutinize charity's solicitation language

# Complying with Requirements of Other Government Agencies

- ★ SOS

- ★ FTB

- ★ IRS

- ★ Local jurisdictions may regulate solicitation [see list on AG website Resources page]

- ★ Multi-state solicitation campaigns [information available at [www.multistatefiling.org](http://www.multistatefiling.org) ]

# The Independent Audit Requirement

★ Applies to the following entities with \$2 million or more in gross revenue\*

- Nonprofit Corporations
- Unincorporated Associations
- Trusts

[Unless exempt from registration and reporting]

\* Audit FAQ's are available on AG's website



# Independent Audit Requirement: Definition of “Gross Revenue”

- Follow instructions for Line 12 of IRS Form 990 and Line 12, column (a) of IRS Form 990PF.
- Non-cash and one-time contributions, and income from special events are included in the definition.
- Revenue from government grants and contracts for services for which an accounting is required are excluded from the definition.

# Independent Audit Requirement (con't.)

- ✱ Independent audited financial statements must be made available to the Attorney General and the public
- ✱ Includes all statements and notes but NOT the management letter
- ✱ Complete no later than 9 months after close of fiscal year

# Audit Committee Requirement

- ☀ If required to conduct independent audit, must have an audit committee
  - ☀ Appointed by governing Board
  - ☀ May be only one person
  - ☀ Can be non-governing Board members
  - ☀ Cannot include 50% or more of members of Finance Committee
  - ☀ Cannot include President/CEO, Treasurer/CFO, staff members, or employees

## Duties and Responsibilities of the Audit Committee

- ★ Recommend hiring and firing of auditor to the Governing Board
- ★ Confirm that financial affairs are in order
- ★ Review and accept/reject audit
- ★ Approve non-audit services by auditor

# Executive Compensation Review

- ✦ Review and approval of executive compensation is a critical responsibility
- ✦ “Compensation” includes salary, bonuses, and retirement and all other benefits
- ✦ Compensation review requirement applies to all
  - ✦ Nonprofit corporations
  - ✦ Unincorporated associations
  - ✦ Charitable Trusts

Gov. Code, § 12586, subd. (g)

# Executive Compensation Review (con't)

- ★ Must be reviewed and approved by Board or authorized committee of Board for the following positions:
  - ★ President or CEO
  - ★ Treasurer or CFO
  - ★ Or others with comparable powers and duties

# Executive Compensation Review (con't.)

★ Review and approval required at 3 points:

- ★ Initial hiring of the Officer
- ★ Upon renewal or extension of the Officer's employment term
- ★ Modifying the Officer's compensation
- ★ Compensation must be "just and reasonable" (consider comparables, officer's qualifications, & other factors)

# Executive Compensation Review (con't.)

- ★ Review is ALSO required for at-will Officers on initial hiring and whenever compensation modified
- ★ No review required for staff or Officers paid more than President or CEO, and Treasurer or CFO, but the charity must ALWAYS exercise due care to ensure that the compensation is just and reasonable
- ★ Excessive executive compensation is considered a waste of charitable assets and can result in liability for Board members and Officers; it can also jeopardize tax-exempt status



# Top 9 Ways to Get Investigated

- ✦ Failing to ensure all regulatory filings are current
- ✦ Allowing CEO/Executive Director sole control
- ✦ Failing to hold regular Board meetings
- ✦ Failing to regularly evaluate performance of CEO/Executive Director
- ✦ Failing to properly record Board actions in meeting minutes [and poor record-keeping in general]\*
- ✦ Failing to implement adequate internal controls
- ✦ Allowing self-dealing transactions without the analysis required by law
- ✦ Failing to aggressively monitor the organization's fundraisers
- ✦ Failing to ensure restricted gifts are used only per restriction

\* Note: the AG has a 10-year statute of limitations

# Top Excuses That Will Only Make it Worse

- ✦ We've always done it that way.
- ✦ I didn't know I had to register/No one told me.
- ✦ "So and So" was supposed to do that.
- ✦ We're a volunteer Board and don't have time to...
- ✦ I completely trusted ...
- ✦ Only our Treasurer gets to see the financial records.
- ✦ We threw those records away. No one told us we had to keep them.

# Charity Fundraising: Commercial Fundraisers

## ★ Definition:

- ★ Any individual/entity who does any of the following for compensation:

- Solicits assets for charitable purposes
- Receives or controls such assets
- Employs any compensated person to do either

- ★ All CFRs must be registered with the AG's Registry

# Charity Fundraising: CFR's Notice of Intent to Solicit

- ☀ All CFRs must file Notice of Intent to Solicit
  - ☀ Filed with Attorney General's Registry
  - ☀ 10 working days before the start of a solicitation campaign or event
  - ☀ *Exception* for disaster solicitations – provide notice concurrent with commencement of campaign

# Charity Fundraising: Written Contract Requirement

- ★ Charity and CFR must enter into written contract for every solicitation campaign or event
- ★ Contract is voidable unless the commercial fundraiser is registered with the Attorney General
- ★ Must be signed by an official authorized by the charity's governing Board
- ★ See model contract on AG's website

# Terms Required in Fundraising Contracts with CFRs

- ★ The written contract must state:
  - Charitable Purpose
  - Obligations of both parties
  - Fee arrangement
  - Effective, start, and termination dates
  - 5-day limit to transfer contributions from CFR to charity
  - Charity control of content and frequency
  - Maximum amount to secure attendance at, or sponsorship of, an event
  - Cancellation rights

Gov. Code, § 12599, subd. (i)

# Charity Fundraising: Fundraising Counsel

## ☀ Definition:

- ☀ A Fundraising Counsel is any individual or entity who for compensation
  - ☀ Plans, manages, consults or prepares material for solicitation of assets for charitable purposes
  - ☀ Does *not* solicit assets for charitable purposes
  - ☀ Does *not* receive/control such assets
  - ☀ Does *not* employ persons who solicit assets or receive/control such assets

Gov. Code, § 12599.1

# Requirements for Charity Fundraising using FRCs

- ✦ Fundraising counsel must be registered with the AG's Registry
- ✦ Notice of Intent to Solicit required of FRCs is the same as with CFRs
- ✦ Written fundraising contract required
  - ✦ Required terms are the same as for CFR's with one addition: must state that FRC will not solicit, receive, or control donated funds, assets, or property or employ another to do so



# Charity Fundraising: Contract Cancellation Rights

- ★ Applies to all fundraising professionals
- ★ Contract voidable if CFR or FRC not registered with Attorney General
- ★ Right to cancel for any reason w/in 10 days of execution

Gov. Code, § 12599.3

# Charity Fundraising

## Remember:

- ☀ Charities are required by law to exercise control over fundraising activities
  - ☀ Approve written contracts
  - ☀ Approve content of solicitation
  - ☀ Assure no coercion
  - ☀ Honor “Do Not Call” requests
- ☀ Charities and their fundraisers must all be registered with the Attorney General
- ☀ CFRs must transfer donated funds to charity or to account controlled solely by charity within 5 days of receipt

Gov. Code, § 12599.6

# Charity Fundraising: Prohibited Acts

- ✱ Violations of the registration and reporting requirements (for charities & fundraisers)
- ✱ Unfair or deceptive acts or fraudulent conduct
- ✱ Using any name or symbol that suggests a contribution is for a particular charitable organization when that is not true
- ✱ Representing that a contribution will be used for a charitable purpose when that is not true

# Charity Fundraising Prohibited Acts (con't.)

- ✦ Representing that a person endorses a charitable solicitation unless that person has agreed to do so in writing
- ✦ Representing that contributions solicited will be given to another charity unless that charity has given prior written consent
- ✦ Misrepresenting the net proceeds to be received by the charity
- ✦ Other prohibited acts (Gov. Code, § 12599.6)

# CONTRACTING WITH FUNDRAISING PROFESSIONALS

## ★ DO's:

- ★ Check charity and CFR/FRC registration status with the Registry
- ★ Review annual CFR report on AG's website for CFR's previous NET proceeds to charity
- ★ Ask for and check CFR's/FRC's references
- ★ Review model fundraising contract on AG's website before signing any contract

# CONTRACTING WITH FUNDRAISING PROFESSIONALS

## ★ DO's (con't.):

- ★ Review the script/pitch and fundraising materials carefully before approving
- ★ Before campaign starts, contact local government agencies to determine whether additional permits/licenses are required
- ★ Before signing any contract get an unambiguous and clear written estimate for all costs involved in the campaign and make sure that these estimates match those quoted in the contract
- ★ Keep copies of relevant documents (contract, invoices, bank records, etc.)

# CONTRACTING WITH FUNDRAISING PROFESSIONALS

## ★ DON'T

- ★ Be misled by “get-rich-quick” promises
- ★ Forget that donors care about the cost of fundraising - donors want a high percentage of their contribution to be used for program services, not for fundraising
- ★ Sign contracts for fundraising services without researching the company for complaints, etc.

# Record-keeping Requirements for CFRs

- ✦ Keep records for 10 years
- ✦ Document all revenue and expenses
  - ✦ Cash: date and amount
  - ✦ Non-cash: date, amount, name and address of donor
  - ✦ Name and address of each employee or agent involved
  - ✦ Bank account numbers, names, locations

Gov. Code, § 12599.7



# DONOR TIPS

## ★ DO's before donating:

- ★ Learn about the charity & review its financial disclosure reports (ask for written information or research on the internet)
- ★ Ask if the solicitor is being paid to solicit
- ★ Ask what percentage of the donations raised is paying for fundraising expenses
- ★ Make sure donation is tax deductible

# DONOR TIPS (con't.)

## ★ DO's (con't.):

- ★ Watch out for “copy-cat” names
- ★ Confirm law enforcement agency appeal
- ★ Consider cost of “freebies”

## ★ DON'Ts:

- ★ Make cash donations, or give SSN or credit card number to anyone
- ★ Give a donation when you feel pressured or uncomfortable

# Raffle Regulation Overview

- ✱ A raffle is a type of lottery
- ✱ Lotteries are illegal unless statutory exception
- ✱ Penal Code sec. 320.5
  - ✱ Creates a limited “charity-raffle” exception to California law prohibiting lotteries

# What Is A Raffle?

- ✦ A “raffle” involves the purchase of a chance to win a prize
- ✦ “Raffle” elements:
  - ✦ Pay money
  - ✦ Paper ticket with identifying number and detachable stub
  - ✦ Drawing held to determine winner

# Raffles

## Limits On Who Can Conduct

- ☀ Must be an “eligible” organization:
  - ☀ A private nonprofit organization;
  - ☀ Qualified to do business in CA for at least one year before raffle conducted; and
  - ☀ Tax exempt under specific Rev. and Tax. Code sections

\*Does not include public schools or other government entities

# Raffles

## Annual Registration

- ★ Must be registered with Attorney General **prior to** conducting raffle:  
September 1 – August 31
- ★ Separate from **charity** registration under Government Code
- ★ Must have confirmation letter from Registry **before** raffle conducted
- ★ Each chapter of statewide organization must register separately

*\*Exemption:* nonprofit religious organizations, educational institutions, hospitals, BUT must comply with all other provisions of § 320.5

# Raffles Restrictions

- ★ 90% of gross receipts from ticket sales for each draw must either:
  - Be used by the organization conducting the raffle for its charitable or beneficial purpose
  - Or given to another eligible organization to use for its charitable or beneficial purpose

# Raffles

## Restrictions

- ✱ Proceeds must be used in California
- ✱ Non-restricted funds from sources other than tickets can be used to pay for costs
- ✱ None of the 90% restricted funds can be used to compensate a person in connection with operation of the raffle
- ✱ Can advertise, but not conduct raffles on the internet



# Raffles

## Restrictions

- ✱ Cannot use gaming machines to conduct raffles
- ✱ Cannot sell tickets or conduct raffle in a satellite wagering facility, at a racetrack or gambling establishment
- ✱ No legal entity or individual may hold financial interest in the raffle except eligible organization conducting, or receiving proceeds from, the raffle

# Raffles Reporting

- ★ **New:** A single aggregate report for all raffles held during the year
- ★ FAQs and reporting form on AG website
- ★ Report(s) filed no later than 10/1
- ★ Reporting requires precise financial records
  - ★ Total funds received
  - ★ Total expenses
  - ★ Charitable or beneficial purpose for which proceeds used
  - ★ Name of eligible organization receiving proceeds

# Raffles

## Exemption from Regulation

A raffle is exempt if it meets all of these requirements:

- ✦ It involves general and indiscriminate distribution of tickets;
- ✦ Tickets are offered on same terms and conditions as tickets for which donation given;  
AND
- ✦ Participants are not required to pay for a chance to win

Penal Code, § 320.5, subd. (m)

# Raffles: FAQ's

- ✦ Do we have to register if we call it an “opportunity drawing?”
- ✦ If participants are required to “pay to play” in order to have a chance to win a prize, the drawing is subject to the provisions of Penal Code section 320.5 and related regulations.

# Raffles: FAQ's

- ✦ Is a silent auction the same as a raffle?
- ✦ No. A silent auction is not the same as a raffle. In a silent auction only the person willing to pay the highest bid amount is able to obtain the item.

# Raffles: FAQ's

- ★ How do we register to hold a raffle?
  - ★ At least 60 days before the raffle submit:
    - Application for registration, \$20 fee, and copy of FTB exemption letter/entity status letter
  - ★ If less than 60 days before the raffle:
    - Applications are processed in the order they are received
    - No expedited services are available

(\*see raffle checklist on AG's website)

# Raffles: FAQ's

- ★ What happens if we don't register?
- ★ An eligible organization must be registered with the Attorney General prior to conducting any activity associated with a raffle. Failure to comply with the provisions of section 320.5 is a misdemeanor; violations may be forwarded to local law enforcement.

# RESOURCES

## ★ AG's Website

- ★ Charity & Fundraiser Filings
- ★ Forms & Publications:
  - Registration guide
  - Guide to submitting transactions
  - Guide for Charities
  - Forms and instructions
  - Laws and regulations
  - Model contract
  - Resources re: conduct of raffles
- ★ Contact information for other government agencies, legal services, & technical assistance



# Attorney General

## Contacts and Information

- ☀ Website resources (including registration & reporting, raffles, etc.) [www.oag.ca.gov/charities](http://www.oag.ca.gov/charities)
- ☀ Registration contact information:
  - [registration@doj.ca.gov](mailto:registration@doj.ca.gov); (916) 445-2021 ext. 4
- ☀ Registration Renewal contact information
  - [rff1@doj.ca.gov](mailto:rff1@doj.ca.gov); (916) 445-2021 ext. 5
- ☀ Delinquency contact information
  - [delinquency@doj.ca.gov](mailto:delinquency@doj.ca.gov); (916) 445-2021 ext. 6
- ☀ Raffle contact information:
  - [raffles@doj.ca.gov](mailto:raffles@doj.ca.gov); (916) 445-2021 ext. 9
- ☀ Other specific questions:
  - [tania.ibanez@doj.ca.gov](mailto:tania.ibanez@doj.ca.gov)