STATE CHARITY REGISTRATION LAWS: WHAT DIRECT MARKETERS SHOULD TELL THEIR CLIENTS

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As you prepare your direct mail, email, website or other solicitation for your nonprofit clients, you will add considerable value to your work if you alert your clients to the implications of new IRS requirements and state charity registration laws. All states have laws that require charities to register with officials when they solicit. Your clients cannot stop fundraising—it's their lifeblood. Yet they should know how to operate their programs in compliance with the laws.

State charity registration laws have been ignored for decades. Until earlier this year, I wouldn't have been allotted space to write about them. There is no penalty for breaking most of them and the few states that have penalties rarely enforce them, so there has been no incentive to comply. That is, until the IRS stepped in.

This year, the Service's vastly revised Form 990 comes into effect, with a few hundred new questions and a score of new schedules. Form 990 is the information return filed annually by nearly all nonprofits. With this first update in about 30 years come two questions asking explicitly about your clients' compliance with laws where they must register.

While it is just two questions, there is a great deal of work that goes into answering them completely. Do your clients know where their organizations must register or seek exemption?

The state registration laws—different in every state and the District of Columbia—agree on one thing: nonprofits register in states where they solicit. 'Solicitation' means different things across the states, but the various definitions fall into a few categories.

In many states, like Arizona, Florida, Illinois, New Jersey and New York, the mere existence of a website that accepts donations is a solicitation. Do your clients offer their donors online giving options? If so, they must register in the above listed states as well as others.

Add California and Utah to the list if your clients send emails or otherwise encourage donors to go to a website where they can make a donation. Add in Texas if your clients encourage online giving through direct mail or by phone.

Email that requests a gift irrespective of a website is a solicitation that triggers registration in all of the above states plus Massachusetts, Oregon and Washington.

Direct mail requesting a donation is a solicitation in all states and that may have the most significance for your company's nonprofit clients.

In order to answer those Form 990 questions, charities must research the requirements in every state in which they solicit donations. In Part VI of the 990 charities are asked for a list of states where they must file the 990. It's a part of the registration requirements in nearly every state. Schedule G asks in which states the charity is registered or if the states have notified them of exemption from registration.

All this brings us to an interesting point. Exemptions exist in close to all the states; some are quite broad while others are rather narrow. In many of the states that offer exemption, the organization must apply for it and receive a decree that they qualify. In others, the institution decides it is exempt and moves on to the next state.

Where you sit usually determines where you stand in these areas. If you are a state or federal regulator, you would most likely see narrow exemptions in the best interest of the public. Narrow exemptions provide the broadest protection from charity fraud, but then you would have to process more registrations. Registration is typically processed through a state's attorney general or secretary of state. Florida is an exception, where registration is processed through the Department of Agriculture and Consumer Services. In D.C., charities work with the Department of Consumer & Regulatory Affairs and the Office of Tax and Revenue.

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Regulators and legislators alike might favor limited exemptions because they increase revenue. There are fees for registration, which, for the largest nonprofits, can run as high as $400 in Florida and $300 in California. Like many others, fees in those states are graduated based on gross revenue in a year. A few thoughtful states base the fee on revenue from within their borders. Surprisingly, New York's price tag is a low $25 for all comers, plus another $25 for the largest. Perhaps I shouldn't publicize that…

Not surprisingly, nonprofits are looking for the widest exemptions. Nonprofits come in all stripes and include broad charitable missions like education, health care and religion. In Arizona, though, your clients are required to register unless they are a government body or fundraising for a political cause. But that's not the most onerous state—or should I say 'comprehensive?' Some jurisdictions, including D.C., Idaho and Indiana, offer no exemptions at all.

The federal Form 990 exemptions will shrink over the next few years. Currently, every nonprofit with gross receipts of at least $1 million or total assets of $2.5 million or more must file the 990. In two years, those thresholds will be down to $200,000 and $500,000. If it's not already there, the Form 990 is coming to a nonprofit near you. Those exempt from the 990 are not forgotten. There's a 990EZ, with one registration-lite inquiry.

The nonprofit 990 filing requirement is an impetus for 'getting right' with state registration laws where your nonprofit clients solicit donations. The 990 is filed four-and-a-half months after the close of the fiscal year and one of your client's officers signs it under penalty of perjury.

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And while enforcement at the state level is near nonexistent, do they want to take the chance that they will end up a test case? Do their board members know they are asking them to take that chance? If their charity is not registered where they solicit, it is breaking the law. Under the principles of fiduciary duty, the charity's board members can be held individually liable.

Most states don't have penalties but some do. Furthermore, in some states the penalty is part of the criminal code. In Florida you are looking at a 3rd degree felony and an up to $5,000 fine. There is the potential for jail time as well—it's a felony. And Florida offers very limited exemptions: soliciting for a named individual (think child's cancer treatment fund) or only from the organization's members. That's it. Likewise, in Arizona, Pennsylvania and Washington, noncompliance is criminal. In most states the penalties are civil, so while there will be no perp walk for your clients' CEOs and CFOs, the fines can be hefty. For instance, fines run as high as $25,000 in Georgia.

To stay on the right side of these laws requires more than initial registration. Notice that I slipped an adjective in to introduce the foreboding new phrase 'initial registration.' In the majority of states, an organization will have to renew registration annually, and file a financial report as well.

Renewal isn't typically as memorable as their first time, but they do have to remember the anniversaries and spend some time together.

There is a long-term, less palpable consequence of being outside the laws. Your clients risk a gift challenge down the road from a family member or heir who has some (probably pecuniary) motive for making trouble over a solicitation. An attorney will look for any way to invalidate a gift and by having it ruled illegal—because the nonprofit was not registered at the time—will go pretty far in that endeavor. There is no end to the mischief that can be made when a disgruntled heir hires an enterprising attorney.

State charity registration laws are a messy web with which to tangle. They are not complex, but they are time consuming and cost some money. As soon as your nonprofit clients have a website with a donation page, or email a request for a gift, or mail a solicitation, they are in the thick of it.

Here is a plan for how your clients can get started. Charity begins at home, so they should register first in their home state. I trust by now you recognize this does not mean incorporating in the state. This is also not registering a Charitable Gift Annuity program, for your clients that have one and if their state requires it. Those having been completed, your clients must comply with this additional layer of home-state regulation.

Then I recommend the charity look at where they (or you) send the largest number of solicitations. If their fundraising is mostly from online giving, I am talking about web based solicitations. Rank the states in descending order of population and start at the top, working through the states where the website is considered a solicitation. California is the most populous state. I described their definition of 'solicitation' above. (I am sorry, but I cannot go into detail state-by-state because if I apply the law to direct a specific action then I am giving legal advice. In an article, I can only go so far as to tell you what the law says.)

I suggest a government source for population ranking for greater reliability. I would look to the U.S. Census Bureau (www.census.gov) as the source.

As soon as your nonprofit clients have a website with a donation page or email a request for a gift they are in the thick of it.

If the solicitations are not primarily through a website then I would presume they are mostly using email or direct mail. Rather than relying on an outside source, they should start with their own database. Select those they solicit and query for state of primary residence, getting output ranked in descending order by state frequency. Start the registrations at the top, with the state where they (or you) send the most solicitations.

With time devoted to taking on a few new states every month, your clients will achieve compliance. And remember, they might enjoy exemption in some places. Remember too, there are some exemptions for which they must apply.

Whether or not your clients adopt my plan or proceed down another path, they must get started. In order to protect their organization's good name, their board and their officers, your nonprofit clients need to operate on the right side of state charity registration laws. They cannot ignore them any longer.

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