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STATE CHARITY REGISTRATION LAW COMPLIANCE

TONY MARTIGNETTI

State charity registration laws—different in every state and the District of Columbia—require most nonprofits to inform states that they plan to solicit donations from their residents. These laws protect residents from fraudulent solicitations and prevent misuse or misappropriation of donations earmarked for charitable purposes.¹ Recent activities involving these laws have had a significant impact on compliance for nonprofits.

Basic considerations

The most basic consideration for a nonprofit is a determination of whether it solicits charitable gifts that may bring it within the reach of state registration laws. Such gifts come in many forms—cash, checks, stock, or purchases of raffle tickets or gala dinner tickets. A charitable gift may take the form of tangible personal property, real property, or another in-kind gift. Any transfer in which a portion is designated for a charitable purpose or to a charitable organization, including any variety of trust with a charitable remainder or lead interest, implicates state registration laws.

A second important consideration is whether the nonprofit must file Form 990, because that form requires information about compliance with these state laws. Currently, every nonprofit with gross receipts of at least \$500,000 or total assets of \$1.25 million or more (other than churches and certain church-related entities) must file Form 990.² In 2011 (for tax year 2010), those thresholds will be down to \$200,000 and \$500,000.³ For most nonprofits below the filing thresholds, there is a

Form 990-EZ filing requirement; this form also inquires about registration compliance.

Because both Form 990 and Form 990-EZ inquire about compliance with state registration and reporting laws, nonprofits that are required to file one of these forms have an additional impetus for “getting right” with the state laws in every jurisdiction from which the nonprofit solicits charitable gifts. Nonprofits subject to these federal filing requirements must file four and a half months after the close of each fiscal year, although extensions are readily available and commonplace. Form 990 must be signed by an officer of the organization and is signed under penalty of perjury.

Changes to Form 990

The Service’s vastly revised Form 990, with a hundred or so new questions and a score of new schedules, came into effect for the 2008 tax year. This first update in about 30 years includes two items asking explicitly about an organization’s compliance with state charity registration laws. They are in Part VI, line 17 and Schedule G, line 3 of the 2009 Form 990.

The first question asks for the states in which the nonprofit is required to file Form 990. That is a basic element of registration in many states, and something all states have in common. Essentially, it is asking for a list of states in which the organization is subject to the charity registration requirements and needs to register. The previous version of Form 990 asked for the states in which the form had been filed. This seemingly small difference signals a noteworthy change. It is a good deal easier to report where the Form 990 has been filed than where it ought to be filed.

Second, Part I of Schedule G requests: “List all states in which the organization is registered

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or licensed to solicit funds or has been notified it is exempt from registration or licensing." This is required if the organization reported more than \$15,000 in "professional fundraising services" expenses in Part IX, line 11e, column A of the core Form 990. There is an alternative other than registration or notification of exemption. A fair number of states—including Alabama, California, New Jersey, and New Mexico—allow the organization to determine on its own whether it is exempt, without notification of exemption acceptance from state officials.⁴

These two questions new to Form 990 require the charity to know where it must register under—or be exempt from—state charity registration laws. Where does a charity pursue registration or exemption?

What constitutes a solicitation?

All states require that charities register in states where they solicit,⁵ but "solicitation" means different things in different states. The definitions fall into a few categories.

A number of states—including Alabama, Alaska, Arizona, the District of Columbia, Florida, Illinois, Kentucky, Maine, New Jersey, New York, and Ohio—take the position that the existence of a Web site that accepts donations is considered a solicitation. If a nonprofit has a "Donate Now" button on its site, the nonprofit must register in those states and others.⁶ It should be noted that this information about online giving comes from contact with state officials. State laws have not yet

been updated to address the proliferation of online giving.

The Web sites of small organizations that expect to receive gifts locally can specify from which states they can accept gifts.⁷ It is recommended that such organizations use a pull-down menu and provide a list of the acceptable states, so as to clarify that they are not seeking charitable gifts from other states. Registration would be required only in those states, and then only in those states in which the "Donate Now" button is deemed a solicitation.

To the list of states that require registration for "un-supplemented" online giving (i.e., a "Donate Now" button without the inducements listed below) must be added California, Idaho, Kansas, Maryland, Massachusetts, Mississippi, New Mexico, North Carolina, and Utah if an e-mail is sent or if donors are otherwise encouraged to go to a Web site where they can make a donation.⁸ Other inducements to give through the Web site would include those delivered via the U.S. Mail, advertisements, meetings, and events.

E-mail that requests a gift whether or not a Web site link is given is considered a solicitation in just about every state, and registration is required. Texas is an exception. The state does not consider Web or e-mail a solicitation, though it is to be noted that state authorities have expressed in informal discussion their desire to update those statutes.⁹

Paper mail requesting a donation is considered a solicitation in all states,¹⁰ no matter what that state determines about online giving.

¹ See, e.g., Florida Statutes § 496.402; New Jersey Statutes § 45:17A-19.

² See "Form 990 Series—Which Form to File (Filing Phase-In)," available at www.irs.gov/charities/article/0,,id=184445,00.html

³ *Id.*

⁴ Alabama Code § 13A-9-71 (f); California Government Code § 12583 (exemptions for charitable solicitations; the Franchise Tax Board exemption application may nonetheless be required); New Jersey Statutes § 45:17A-26 (exemptions under Charitable Registration and Investigation Act; registration with the Department of the Treasury, Division of Revenue as a foreign corporation doing business may nonetheless be required); New Mexico Statutes 57-22-4.

⁵ "The Charleston Principles: Guidelines on Charitable Solicitations Using the Internet" (hereinafter, "the Charleston Principles" or "the Principles"), 3/14/01, page 1, available at www.nasconet.org/Charleston%20Principles,%20Final.pdf.

⁶ It is still unclear in most states whether online acceptance of donations through a "Donate Now" button constitutes soliciting. Even officials in many states do not know the answer to this question themselves. The Charleston Principles, see *id.*, suggest standards, but which states adhere to the Principles is uncertain in most cases.

⁷ "The Charleston Principles," *supra* note 5 at page 18, #11. As stated in note 6, *supra*, which states adhere to the Principles is uncertain. If an organization explicitly limits solicitations to a number of states and uses simple technology to block donations from all other states, it clearly is not soliciting everywhere else, so need not register everywhere else.

⁸ This is information from direct contact with state officials, via phone and e-mail.

⁹ *Id.*

¹⁰ See, e.g., California Government Code § 12581.2; Florida Statutes § 496.404(20)(a); Massachusetts General Law Chapter 68, § 8, definition of "solicit"; New York Executive Law § 171-a(10); Pennsylvania Statutes, Title 10, Chapter 4B, § 162.3, definition of "solicitation."

¹¹ It is logical that if a for-profit foreign corporation selling goods or services in a state is transacting business, then a nonprofit soliciting gifts is doing likewise. Risk aversion is advisable over risk-taking, although a foreign nonprofit's small number of solicitations may land it outside the threshold of the state's "doing business" definition and, likely, outside its jurisdiction, based on the minimum contacts analysis in cases like *International Shoe v. State of Washington*, 326 U.S. 310 (1945).

Categories of registration

As soon as a nonprofit engages in a charitable solicitation as defined in the applicable state, it must register. The basics of registration therefore entail the organization's knowing where it solicits, determining its exemptions, and complying where exemptions do not apply. Registration typically requires amassing a number of documents and filling out a sheaf of forms.

As the above discussion indicates, the details of these rules vary significantly from state to state.

There is registration under what most states call a Charitable Solicitations Act, and there is registration as a foreign corporation doing business in the state (usually with a state's secretary of state). Both are an act of registration essential to soliciting donations. A "foreign corporation" is one incorporated (presumably as a not-for-profit corporation) in another state or country. It may be resident (domiciled) in many states, but it can be incorporated in only one. Many activities can fall within "doing business in the state" and, in most states, soliciting charitable gifts is among them. Thus, if one's clients are soliciting in states other than where they are incorporated, they are foreign corporations doing business in those other states and must register as such.

Some practitioners believe nonprofits need only register under charity solicitation acts. State authorities disagree. They expect foreign nonprofits to register to "do business" in their state if they engage in any activities within their state, including charitable solicitation.¹¹

The bottom line is that wherever a nonprofit solicits is where it must register, both as a foreign corporation doing business in the state and, unless exempt, to solicit contributions.

Once the organization knows where it must register, it must next gather documents, including articles or certificate of incorporation, bylaws, its IRS tax-exempt determination letter, Forms 990, professional fundraiser contracts, financial statements, and a list of board members.

Next, the organization must find the right forms for every state. For foreign corporation registration, the required, relatively simple forms are usually available on the Web site of the state secretary of state. For charitable solicitation registration, 35 states accept the Unified Registration Statement (URS), which is a product of the National Association of State Charity Officials. It helps considerably to have this common form that satisfies all these states. Beyond this common form there are variations in additional information requested, supplement-

tal forms, renewal requirements, periods covered, and fees. As an example, some states ask for an audited financial statement with the URS, others will accept an un-audited financial statement, still others will accept an accountant's opinion letter, and some do not require any financial substantiation. Some states vary in what financial substantiation is required according to gross revenue and others vary it based on fundraising revenue, which may be either measured in-state or nationwide.

After all the requirements get sorted out, applications are submitted, and the organization waits to hear back from state officials. Often, rules have changed or were misinterpreted or something is incomplete, requiring the provision of additional information. Delays, therefore, often ensue, but normally approval letters eventually arrive.

The most basic consideration for a nonprofit is whether it solicits charitable gifts.

Determining where to start

How does a nonprofit know which states to start with? An organization accepting online gifts or relying heavily on e-mail or paper mail, depending on the type of organization, could have to register in all 51 jurisdictions—an intimidating task to contemplate.

Here is a plan to share with clients for breaking the job into reasonable pieces. Charity begins at home, so suggest that they register first in their home state. It should be emphasized to the client that this registration is separate from state incorporation. It also is not registering a charitable gift annuity program, if the organization has one and their state requires registration. Those presumably having been previously completed, the client must now ensure compliance with this additional layer of home-state regulation.

Then the client should look at where the largest number of solicitations goes. If fundraising is mostly from online giving, this is considered Web-based solicitation. In this case, rank the states in descending order of population and start at the top, working through the states where a Web site is considered a solicitation. California is the most populous state. It is advisable to use a government source for population ranking for greater reli-

ability, such as the U.S. Census Bureau (www.census.gov).

If the charity's solicitations are not primarily through a Web site, it is to be assumed they are mostly using e-mail or paper mail. Rather than relying on an outside source, they should start with their own database to determine which states to focus on first. Select the constituents they solicit and query for state of primary residence, getting output ranked in descending order by number of constituents. Start the registrations at the top. Where the most people live is where they send the most solicitations.

By taking on a few new states each month, an organization will be in compliance in an efficient way. It is to be remembered that they might enjoy exemption in some places, but also that some exemptions have to be applied for.

Exemptions

Exemptions exist in a number of states. Some are quite broad and others rather narrow. The most typical grant of exemption is by charitable mission—exemptions for religious, health care, and educational organizations are most commonly seen in the states that offer exemptions.¹² In a good number of states, the organization must apply for its exemption and receive back a decree that it

qualifies.¹³ In others, the institution alone decides it is exempt and it moves on to the next state.

A fair number of states have very few exemptions, and some have none at all. Interesting are Arizona (insignificant),¹⁴ District of Columbia (slight), Florida (very few),¹⁵ Idaho (slight), Indiana (none), Nevada (none), and New Hampshire (slight: churches, and those for which compliance constitutes a financial burden, which must be substantiated).¹⁶

One may conjecture that states having the most interest are those in which the most money is raised or a large number of people donate. There are no exemptions for having a small number of donors in a state, however, although a proposal for exemption based on number of donors does exist. The Charleston Principles¹⁷ are a set of recommended registration guidelines developed by the National Association of State Charity Officials at a meeting in South Carolina in 1999. The Principles are a sound and reasonable way of determining which charities should have to register based on the degree of exposure, or contact, they have in a state, even though it is difficult to determine which states have adopted the Principles.

State regulators would likely see narrow exemptions as in the best interest of the public to provide the broadest protection from fraudulent solicitations and misuse of charitable monies, but one would also have to process more regis-

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trations. Registration is typically through a state's attorney general or secretary of state. Florida is an exception, where organizations register with the Department of Agriculture and Consumer Services. In the District of Columbia, organizations work through the Department of Consumer & Regulatory Affairs and Office of Tax and Revenue. The latter has jurisdiction because the District requires charities to apply for exemption from income, sales, and property taxes.

Regulators and legislators alike might favor limited exemptions because they increase revenue. There are fees for registration that, for the largest nonprofits, can run to \$400 in Florida and \$300 in California. The fee in Hawaii is \$750, the highest in the nation. Fees in those states are graduated based on gross revenue in a year; smaller organizations pay less.

Ohio, Oregon, and a few other states base the fees on revenue from within their borders. New York's price tag is \$50 for all nonprofits with gross revenue over \$250,000. Five states (Arizona, Arkansas, Kentucky, Michigan, and New Mexico) are fee-free and 32 charge \$100 or less.

In part because of the fees, nonprofits look for the broadest exemptions. Their other motivation is avoiding the storm of paper and details inherent in registration.

Over the next few years, more organizations will seek exemptions. More will also likely be registering, because of the need to answer the new questions on the Form 990.

More stringent enforcement of regulations

State charity registration laws have been around for decades but they have not always been strictly enforced. There is evidence of that having started to change even before the changes to the Form 990.¹⁸

In October 2009, the Georgia Secretary of State fined a nonprofits founder \$25,000—the maximum penalty in Georgia and among the highest in the country—for failure to register the foundation's charitable solicitations. A Georgia court agreed with the Secretary of State that the founder should suffer personal liability for the foundation's failure to comply with state registration requirements.¹⁹

A more recent enforcement action came in January 2010 in Florida, a popular fundraising state with its population of retirees and part-year residents. There, a charity raising money for police officers and families in Florida, with an \$11,000 annual budget, was sued for \$10,000 in a civil action.²⁰

More recently still, New Jersey authorities fined an individual administrator \$17,500 because the organization for which she worked—Ray of Hope—was an unregistered charity when it operated in the state between 2005 and 2009. This case is noteworthy because a former volunteer used the charity's name to commit fraud unrelated to registration requirements. The charity was, in essence, a victim, having come to the Attorney General's attention because of the fraud, but was fined for noncompliance nonetheless.²¹

Turning back to Florida, note that not all the penalties there are civil. There is a criminal fine of up to \$5,000²² and the potential of prison time for having committed a third-degree felony. It is unlikely that anyone will go to prison over charity registration, absent other criminal acts such as fraud. But as to that fine, Florida offers very limited exemptions—soliciting for a named individual, such as a child's cancer treatment fund, or only from the organization's members.²³ In Arizona (\$2,500

¹² See, e.g., Alabama Code § 13A-9-71 (f); Arkansas Code Annotated § 4-28-404; Hawaii Revised Statutes § 467B-11.5; Louisiana Administrative Code, Title 16, Part III, § 515 C; Michigan Code of Laws § 400.263, sec. 13 (exemption for religious-owned facilities for the aged and chronically ill); North Carolina General Statutes § 31F-3; West Virginia Code § 29-19-6.

¹³ See, e.g., General Statutes of Connecticut § 21a-190d, 225 Illinois Compiled Statutes § 460.3(a); Maine Revised Statutes Annotated, Title 9, Chapter 385, § 5006(3); discussion with Ohio Attorney General's office, Charitable Law Section (if an organization determines that it is exempt from registering, a notarized letter requesting exemption and stating corresponding statute must be sent to the attorney general's office); South Carolina Code of Laws § 33-56-50(C); Wisconsin Department of Regulation & Licensing, "Worksheet Concerning Exemption from Registration as a Charitable Organization."

¹⁴ Arizona Revised Statutes § 44-6553.

¹⁵ Florida Statutes § 496.406.

¹⁶ New Hampshire Revised Statutes, Title 1, § 7:28 (III-c).

¹⁷ Note 5, *supra*.

¹⁸ IRS, "Form 990 Redesign for Tax Year 2008 Background Paper," 12/20/07.

¹⁹ "Fulton County Court fines Atlanta Councilman Willis \$25,000 for not registering charity," Atlanta Journal-Constitution, 10/6/09, available at www.ajc.com/news/georgia-politics-elections/fulton-county-court-fines-155836.html.

²⁰ "Florida Agency Sues Tampa Bay Area Police Charity Over \$75 Fee," St. Petersburg Times, 1/22/10, available at www.tampabay.com/news/publicsafety/florida-agency-sues-tampa-bay-area-police-charity-over-75-fee-1067189.

²¹ "State accuses Cedar Grove resident of car-donation scheme," Verona-Cedar Grove Times, 10/29/10, available at www.northjersey.com/news/business-town_business/106305673_State_accuses_Cedar_Grove_resident_of_car_donation_scheme.html.

²² Florida Statutes § 496.417.

²³ Florida Statutes § 496.406.

fine),²⁴ Pennsylvania (\$10,000 fine),²⁵ and Washington (\$5,000 fine),²⁶ too, noncompliance is a criminal offense. In most states—like California, Illinois, Maryland, New York, and Texas—the penalties are civil, so no “perp walk” for board members and the CEO, but the fines can be hefty, as is the case in Georgia.

Under basic principles of fiduciary liability, board members are liable for the deeds, errors, and omissions of the charities on whose boards they serve. It is important that clients’ board members know they could suffer personal liability for failure of the organization to register in each state where it solicits. It also is important that clients’ officers know they are taking that chance with their board members’ reputations. An enforcement letter shared with the author from the California Department of Justice, dated 12/24/09, reinforces these points.

Charitable assets cannot be used to pay these avoidable costs. Accordingly, directors, trustees, officers and return preparers responsible for failure to timely file the above-described report(s) are personally liable for payment of all penalties, interest and other costs incurred to restore exempt status. (Emphasis in original.)

In early 2009, the secretaries of state in Arizona and Washington sent letters to their do-

mestic unregistered charities reminding them of the requirements.

There are long-term, less palpable consequences of being outside the laws. A nonprofit risks a gift challenge down the road from a family member or heir who has some (most likely pecuniary) motive for making trouble over a solicitation. It is possible that an enterprising attorney will look for any way possible to invalidate a gift and have it ruled illegal. One possible way is the nonprofit’s not being registered at the time.

Donors, too, might be the unsatisfied parties. They might be disenchanted with new leadership, a change in mission, a new program, financial mismanagement, negative press, or a grandchild who was denied admission.

Keeping up-to-date and compliant

To stay on the right side of the law takes more than initial registration. In the majority of states, charities will have to renew registration annually and file a financial report as well. Among the renewal states, Georgia stands out as generous—only every two years.²⁷ A fair number of states do not require renewal, however.

Conclusion

Charity registration laws are a morass, but each nonprofit’s compliance is essential before it solicits donations if it is to keep its officers, trustees, bank account, and its own reputation on the right side of the laws and out of trouble. ■

²⁴ Arizona Revised Statutes § 44-6561, 13-802(A).

²⁵ Pennsylvania Statutes, Title 10, § 162.18.

²⁶ Revised Code of Washington § 19.09.275(1), 9A.20.021(2).

²⁷ Official Code of Georgia Annotated § 43-17-5(b)(9).