

Attorney General's Guide for Charities: Review and Discussion



Presenter: Tania Ibanez



Senior Assistant Attorney General
Charitable Trust Section

Introduction

- ▶ The Attorney General's Guide for Charities provides information to directors, officers, trustees, volunteers, fundraisers, and accountants in the nonprofit sector, which helps them to understand their responsibilities.
- ▶ This presentation highlights and elaborates on some of the important topics covered in the Guide based on the Attorney General's Office day-to-day regulatory experience – review the Guide for complete information and details.
- ▶ The Guide and this presentation are not legal advice, and should not be cited as legal authority.

Key and New Points in the Guide

- ▶ Significant Changes in the Guide:
 - ▶ Chapter 4 - Charities as Employers.
 - ▶ Chapter 6 - Is a new chapter which covers reporting obligations to the IRS, Franchise Tax Board, the Attorney General's Registry of Charitable Trusts, the Secretary of State, and the Board of Equalization (Cal. Dept of Tax & Fees Administration).
 - ▶ Chapter 7- Directors and Officers.
 - ▶ Chapter 9- Charitable Fundraising.

Attorney General Oversight of the Nonprofit Sector (Guide Chapters 6, 9-12)

- ▶ The Attorney General has primary responsibility for supervising charities, charitable trusts, and charitable fundraisers in California.
- ▶ There is a difference between our office, Franchise Tax Board and Secretary of State.
- ▶ Charities operating in California are required to **register** and **file annual financial reports** with the Attorney General's Registry of Charitable Trusts unless exempt by statute. (Chapters 6 & 9)
 - ▶ And there are other additional registration and reporting requirements for raffles. (Chapters 6 & 9.)
- ▶ Charitable fundraisers soliciting or operating in California are also required to register and report, and submit to contract requirements.
- ▶ Certain transactions require notice to and approval by the Attorney General.

Registration and Reporting Requirements

- ▶ The Attorney General's Registry of Charitable Trusts (Registry) oversees the registration and reporting requirements of charities, charitable trusts, and charitable fundraisers. (Gov. Code, § 12580 et seq.)
- ▶ The Guide links to the required registration and reporting forms.
 - ▶ The registration forms and instructions are also available on the Attorney General's website (oag.ca.gov/charities).
- ▶ Once a charitable organization registers, and remains in good standing, it can renew its registration online.
- ▶ All registrants also have a continuing obligation to update the Registry with change of address information.

The Consequences for Failing to Register or Becoming Delinquent in the Annual Filing and Reporting Requirements May Result in Punitive Actions

- ▶ A charitable organization cannot legally operate if it is not in good standing with the Registry. The organization's registration must be current to operate; delinquent or suspended organizations may not solicit or disburse charitable funds. (Cal. Code Regs., tit. 11, § 999.9.4.)
- ▶ The failure to register or failure to annually renew the registration may result in the assessment of late fees of \$25 per month, penalties, and/or cease & desist orders. (E.g., Gov. Code, § 12586.1.)
- ▶ If an organization is delinquent in its annual reporting requirements, the Registry may suspend its registration, and it may lose its tax exemption with the Franchise Tax Board.

The Guide covers all of the Attorney General's reporting requirements, and also touches upon the reporting requirements of other state and federal agencies.

The Attorney General's Registry Provides Public Access to Registration and Reports

- ▶ The Registry is required to provide public access to all reports filed with the Registry. To that end, the Registry maintains a searchable database for the public's benefit.
- ▶ The public uses this database to research whether a charitable organization is registered or not.
- ▶ If an organization is registered and listed as "delinquent" this information is posted on the Registry's public searchable database.

The Nonprofit Sector Is Under the Oversight of and Subject to Examination by the Attorney General

- ▶ The Attorney General has the primary responsibility for supervising charities in California. The Attorney General seeks to protect charitable assets and donations, and ensure compliance with articles of incorporation, and other governing documents.
- ▶ The **legal and audit staff** at the Attorney General's Office investigate charities, charitable trusts, and fundraising professionals, and brings enforcement actions. The audit process, what triggers an investigation, and the areas of concern to the Attorney General are discussed in the Guide (Chapter 10).

Other Transactions Requiring Attorney General Notice or Consent (Chapter 11)

Sale or Transfer of Assets

- ▶ The Attorney General must receive a 20-day advance notice before a nonprofit corporation sells, leases, conveys, exchanges, transfers, or otherwise disposes of all or substantially all of its assets. These requirements apply to California public benefit corporations, mutual benefit corporations (if holding charitable assets), and religious corporations. (Corp. Code, §§ 5913; 7238, 7913; 9633; see also Cal. Code Regs., tit. 11, §§ 999.1-999.4.)

Conversions

- ▶ A public benefit corporation cannot convert into a mutual benefit corporation, religious corporation, business corporation, social purpose corporation, or cooperative corporation unless the Attorney General provides written consent. The Attorney General requires certification that all charitable assets will be transferred to another charity as a condition to consent. (Corp. Code, § 5813.5; Cal. Code Regs., tit. 11, § 999.2, subd. (d).)

The Attorney General Has Primary Responsibility for Supervising Charities and Must Approve or Receive Notice of Certain Transactions that Have Significant Impact on the Charity and Its Assets

Dissolution

- ▶ The Attorney General must receive notice of voluntary (and involuntary) proceedings to dissolve. This requirement applies to public benefit corporations, mutual benefit corporations (if holding charitable assets), and religious corporations. (Corp. Code, §§ 6611-6612, 6615-6617, 6716, 7238, 8611, 8614, 8716, 9680.) Moreover, the Attorney General must be involved in providing a written waiver of the distribution of the charity's assets.

Mergers

- ▶ Nonprofit corporations may also require the Attorney General's written consent for a proposed merger depending on the corporate forms of the merging parties. For example, if a public benefit corporation seeks to merge with a mutual benefit corporation, the proposed merger requires the Attorney General's consent. (Corp. Code, §§ 6010, 8010.)

Professional Fundraising Registration, Reporting, and Contract Requirements (Guide Chapter 9)

- ▶ If a charitable organization is going to hire a commercial fundraiser or a fundraising counsel, these fundraising professionals need to be registered with the Attorney General's Registry. (Gov. Code, § 12599.6, subd. (c).)
- ▶ There has to be a written contract with fundraising professionals for each solicitation campaign. (Gov. Code, §§ 12599, subd. (i), 12599.1, subd. (f), 12599.3.) View the Registry's [Basic Components of a Fundraising Representation Agreement](#) for a model contract.
- ▶ There are notice requirements. Both commercial fundraiser and fundraising counsel must file a Notice of Intent to Solicit Form with the Registry. (Gov. Code, §§ 12599, subd. (h), 12599.1, subd. (e).)
- ▶ There are reporting requirements. Commercial fundraisers must file financial accountings for the solicitation campaigns. (Gov. Code, § 12599, subd. (c).) These reports must be signed by the charity's officials.
- ▶ Check the Attorney General's Commercial Fundraising report. <https://oag.ca.gov/charities/publications/commercial>

Charitable Organizations Must Control Their Fundraising (Guide Chapter 9)

- ▶ Charities and their agents may not misrepresent how they use solicited donations.
- ▶ Once funds have been donated for a specific purpose, charities have a fiduciary duty to spend those funds only on that purpose. (E.g., Bus. & Prof. Code, § 17510.8.)
- ▶ In retaining a fundraiser:
 - ▶ Learn how frequently potential donors are contacted and what practices are being implemented to prevent deceptive or coercive solicitation.
 - ▶ Determine who owns the donor list, and its terms of use.
 - ▶ Find out what practices the fundraising professional implements to protect donor privacy.
 - ▶ Clarify the fundraising professional's compensation and payment of campaign expenses.

Fiscal Management Is Important to the Survival and Success of the Charity (Guide Chapter 5)

- ▶ A charitable organization's internal controls are critical. Board members (directors) have a fiduciary duty to the organization, and must steward and provide oversight to the charity as to how its resources are used to fulfill its mission. Board members may be accountable for the loss or misuse of charitable assets if it resulted from deficient or nonexistent internal controls, or lack of due care or reasonable inquiry. As such, the charity's directors should establish internal controls for the charity.
- ▶ An effective internal control system includes an annual budget:
 - ▶ A realistic budget should be developed early enough so that the entire board can be involved in its review and approval before the beginning of the fiscal year.
 - ▶ Directors should monitor the budget. Any sizable differences between expected and actual revenue, or anticipated and actual expenses, should be investigated by directors or designated officers to obtain a full explanation.

Fiscal Management and Internal Controls (Continued)

- ▶ An effective internal control system segregates duties when handling funds. No single employee should receive, record, deposit, and reconcile the charity's receipt of funds.
- ▶ Adequate internal control systems also prevent embezzlement. Embezzlement is a crime of opportunity: if the same person opens the mail, and also makes deposits to the organization's bank accounts, what's to stop them from cashing the checks, or depositing them into an account that they control? Also, having one person approve payments of invoices and issue checks can lead to problems. This person can submit fake invoices for dummy entities and pay those invoices without anyone becoming aware.

Board Engagement Is Critical to the Success of a Charity (Guide Chapter 7)

Board members must be willing and able to exercise duties of care and loyalty towards the organization.

Tips for meeting the duty of care requirements:

- ▶ Directors should review the corporation's articles of incorporation and bylaws to better understand the corporation's mission, and their expected roles and responsibilities.
- ▶ Directors should be informed about the nonprofit organization's program and operations.
- ▶ Attend board meetings and be prepared. Don't be afraid to ask questions at board meetings or to request that matters be decided at a later date to allow for more in-depth deliberation.
- ▶ In making decisions related to the charity's finances, budgets, and compensation paid to staff, proactively demand and review financial reports and compensation studies. Review duty statements and performance evaluations.

Board Engagement and Fiduciary Duties (Continued)

- ▶ What does duty of loyalty mean? It means to act in the best interest of the corporation.
- ▶ With narrow exceptions, a director or officer cannot borrow money from a charity.
- ▶ If director lends money to a charity, the loan terms must be fair to the charity and the loan must be disclosed to the Registry and the IRS.
- ▶ Directors should not engage in self-dealing transactions unless every single step in Corporations Code section 5233, subdivision (d)(2), is closely followed.
- ▶ Directors also may be personally liable for authorizing or receiving a prohibited distribution of the charity's assets. Examples of prohibited distributions include:
 - ▶ Transfers of corporate assets without fair consideration;
 - ▶ Payment of excessive or unauthorized salaries, non-contractual benefits or bonuses;
 - ▶ Improper gifts of the corporation's assets to individuals; and
 - ▶ Other uses of corporate assets that violate the charitable trust under which they are held.

Conclusion

The Attorney General's Guide for Charities provides valuable information and assistance to directors, officers, trustees, volunteers, fundraisers, and accountants for charitable organizations that operate or fundraise in California.

For example:

- ▶ The Guide discusses the different steps in a charity's life span, from creation, to mandatory registration and reporting, transactions requiring either notice to or consent by the Attorney General, and dissolution procedures.
- ▶ Provides best practice recommendations for directors and officers in the daily operation of a charity and in conducting fundraising activities, among other topics.
- ▶ Gives practical information and answers to questions frequently asked of the Registry staff.

Conclusion

- ▶ For more information please visit <https://oag.ca.gov/charities>
- ▶ Registry contact information:
 - ▶ P.O. Box 903447
Sacramento, CA 94203-4470
(916) 210-6400
 - ▶ <https://oag.ca.gov/charities/contact>
- ▶ <http://www.calnonprofits.org/resources/nonprofit-compliance-checklist>