

LEGAL ISSUES INVOLVED IN CHARITABLE FUNDRAISING

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Robert A. Wexler
Erik Dryburgh

INTRODUCTION

This paper will cover a series of topics related to fundraising, some of which will be considered during the oral presentation. The first six issues involve primarily state law questions; the final topic involves tax law.

- I. State and Local Regulation of Charitable Solicitations
- II. Commercial Fundraisers and Fundraising Counsel
- III. Third-Party Fundraising Agreements
- IV. Internet Fundraising
- V. Special Fundraising Vehicles: Bingo and Raffles
- VI. Endowment Issues
- VII. Tax Law Issues Specific to Fundraising
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I. STATE AND LOCAL REGULATION OF CHARITABLE SOLICITATIONS

Many states, including California, have enacted comprehensive statutory schemes regulating charitable solicitations of the public. Those statutes vary from state to state, but they require, in general, registration by the charitable organization and its fundraising agents and certain disclosures in the course of solicitation, with monetary penalties imposed for noncompliance.

California law has two main Codes that govern fundraising and registration of fundraising efforts:

- In 1959, California enacted the “Supervision of Trustees and Fundraisers for Charitable Purposes Act.” Calif. Government Code Sections 12580 *et seq.*, as recently modified by the Nonprofit Integrity Act of 2004.
- In 1972, the California legislature decided that the best protection against solicitation fraud was a well-informed public. To promote public education about charitable solicitation costs through disclosure to the donor, California passed the “Charitable Solicitation Disclosure Law.” Calif. Business & Professions Code Sections 17510 *et seq.*

Games of chance, such as bingo and raffles, are also subject to specific regulation under the California Penal Code (see Section V below).

A charity should check with the Attorney General of any other states in which it intends to conduct fundraising.

SUPERVISION OF TRUSTEES AND FUNDRAISERS FOR CHARITABLE PURPOSES ACT GOVERNMENT CODE SECTION 12580-12599.7

The Supervision of Trustees and Fundraisers for Charitable Purposes Act (the “Act”) prohibits charitable organizations from engaging in misrepresentation and certain other acts when soliciting donations.

Control over Fundraising.

The Act makes plain that charitable organizations must “establish and exercise control,” not only over their own fundraising activities, but over fundraising activities conducted by others for their benefit. That control must include approval of all written contracts, and the charitable organization must assure that fundraising activities are conducted without coercion of potential donors.¹

A charitable organization may not contract with any commercial fundraiser unless that fundraiser has registered as required with the Attorney General’s Registry of Charitable Trusts

¹ Section 12599.6(b).

(“Registry”), nor may Charity A raise funds for Charity B unless Charity B is registered as required.²

Misrepresentations.

Charitable organizations (and commercial fundraisers) may not misrepresent the purpose of the charitable organization or the nature or purpose or beneficiary of a solicitation. Misrepresentation may be established by word, by conduct, or by failure to disclose a material fact.³

Prohibited Practices.

The Act sets forth twelve prohibited acts and practices in the planning, conduct, or execution of any charitable solicitation or sales promotion. The prohibitions apply, according to the Act, “regardless of injury”:⁴

1. Operating in violation of this Act or order of the Attorney General, or after registration is no long valid.
2. Engaging in fraud or using any unfair or deceptive act or practice that creates a likelihood of confusion or misunderstanding.
3. Using any name or any other representation that misleads a reasonable person as to the identity of the charitable beneficiary.
4. Misrepresenting or misleading anyone to believe that the beneficiary of a solicitation or sales promotion is a charitable organization when it is not.
5. Misrepresenting or misleading anyone to believe that another person sponsors, endorses, or approves a charitable solicitation or sales promotion when that person has not given consent in writing to the use of the person’s name.
6. Misrepresenting or misleading anyone to believe that goods or services have endorsement, sponsorship, approval, characteristics, ingredients, uses, qualities, or benefits that they do not have, or that any person has any endorsement, sponsorship, approval, status, or affiliation that the person does not have.
7. Exploiting registration required by law to imply endorsement or approval by the Attorney General.

² Section 12599.6(c), (d).

³ Section 12599.6(a).

⁴ Section 12599.6(f).

8. Representing that a charitable organization will receive more than the amount reasonably estimated.
9. Distributing or offering to distribute – in connection with charitable solicitations by commercial fundraisers for police, fire, and other public safety personnel – membership cards or stickers, emblems, plates, or other items that could be used for display on a motor vehicle and that suggest affiliation with or endorsement by any public safety personnel or group.
10. Soliciting for advertising related to a charitable purpose to appear in a for-profit publication without making, at the time of solicitation, these disclosures: (a) the publication is for-profit, (b) the name of the solicitor and the fact that the solicitor is a professional solicitor, and (c) the publication is not affiliated with any charitable organization.
11. Representing that any part of contributions solicited by charity A will be given to charity B unless charity B has agreed in writing prior to the solicitation to the use of its name.
12. Representing that tickets to events will be donated for use by another unless certain requirements are met to prevent abuse.

**CHARITABLE SOLICITATION DISCLOSURE LAW
CALIFORNIA BUSINESS & PROFESSIONS CODE SECTIONS 17510 *ET SEQ.***

The California legislature was concerned about solicitations for charitable purposes in which an insignificant amount, if any, of the money solicited and collected was actually received by the charity. The purpose of this law, therefore, is “to safeguard the public against fraud, deceit and imposition, and to foster and encourage fair solicitations and sales solicitations for charitable purposes, wherein the person from whom the money is being solicited will know what portion of the money will actually be utilized for charitable purposes.”⁵

A charity includes “any person who, or any nonprofit community organization, fraternal, benevolent, educational, philanthropic, or service organization, or governmental employee organization which, solicits or obtains contributions solicited from the public for charitable purposes or holds any assets for charitable purposes.”⁶

A “solicitation for charitable purposes” means any request, plea, entreaty, demand, or invitation, or attempt thereof, to give money or property, in connection with which:

1. Any appeal is made for charitable purposes;
2. The name of any philanthropic or charitable organization is used or referred to in any such appeal as an inducement for making any such gift;

⁵ Section 17510.

⁶ Section 17510.2(d).

3. Any statement is made to the effect that such gift or any part thereof (or any part of the proceeds from a “sales solicitation” – see below) will go to or be used for any charitable purpose or organization; or
4. The name of any organization of law enforcement personnel, firefighters, or other persons who protect the public safety is used or referred to as an inducement for transferring any money or property, unless the only expressed or implied purpose of the solicitation is for the sole benefit of the actual active membership of the organization.

A “sales solicitation for charitable purposes” means the sale of, offer to sell, or attempt to sell any advertisement, advertising space, book, card, chance, coupon device, magazine subscription, membership, merchandise, ticket of admission or any other thing or service in connection with which any of the above applies.

The state rules described below do not preempt city or county ordinances. Compliance with any city or county ordinance is sufficient, provided the disclosure of information relating to solicitations or sales solicitations for charitable purposes is substantially similar to and no less than the state disclosure requirements.⁷

Disclosure Provisions for Personal Solicitations – Section 17510.3.

Prior to any solicitation or sales solicitation for charitable purposes, the solicitor or seller shall exhibit to the prospective donor or purchaser a card entitled “Solicitation or Sale for Charitable Purposes Card.” The card shall be signed and dated under penalty of perjury by an individual who is a principal, staff member, or officer of the soliciting organization. The card shall give the name and address of the soliciting organization or the person who signed the card and the name and business address of the paid individual who is doing the actual soliciting.

In lieu of exhibiting a card, the solicitor or seller may distribute during the course of the solicitation any printed material, such as a solicitation brochure, provided such material complies with the standards set forth below, and provided that the solicitor or seller informs the prospective donor or purchaser that the information as required below is contained in the printed material.

Information on the card or printed material shall be presented in at least 10-point type and shall include the following:

1. The name and address of the combined campaign, each organization, or fund on behalf of which all or any part of the money collected will be utilized for charitable purposes.
2. If there is no organization or fund, the manner in which the money collected will be utilized for charitable purposes.

⁷ Section 17510.7.

3. The non-tax-exempt status of the organization or fund, if the organization or fund for which the money or funds are being solicited does not have a charitable tax exemption under both federal and state law.
4. The percentage of the total gift or purchase price that may be deducted as a charitable contribution under both federal and state law. If no portion is so deductible, the card shall state that "This contribution is not tax deductible."
5. If the organization making the solicitation represents any nongovernmental organization by any name, which includes, but is not limited to, the term "officer," "peace officer," "police," "law enforcement," "reserve officer," "deputy," "California Highway Patrol," "Highway Patrol," or "deputy sheriff," which would reasonably be understood to imply that the organization is composed of law enforcement personnel, the solicitor shall give the total number of members in the organization and the number of members working or living within the county where the solicitation is being made and, if the solicitation is for advertising, the statewide circulation of the publication in which the solicited ad will appear.
6. With certain exceptions, if the organization making the solicitation represents any nongovernmental organization by any name, which includes, but is not limited to, the term "veteran" or "veterans," which would reasonably be understood to imply that the organization is composed of veterans, the solicitor shall give the total number of members in the organization and the number of members working or living within the county where the solicitation is being made. (This requirement does not apply to any community-based corporation that provides direct services to veterans and their families and qualifies as a tax-exempt organization under Section 501(c)(3) or 501(c)(19) of the Internal Revenue Code.)

NOTE: The California legislature recently adopted legislation that deleted the following additional requirements because they were unconstitutional under the Supreme Court's decision in Riley (see "Are These Fundraising Statutes Constitutional?" below). Prior to 2006, the disclosure card also required the following information:

The amount, stated as a percentage of the total gift or purchase price, that will be used for charitable purposes.

If paid fundraisers are paid a set fee rather than a percentage of the total amount raised, the card shall show the total cost that is estimated will be used for direct fundraising expenses.

If the solicitation is not a sale solicitation, the card may state, in place of the amount of fundraising expenses, that an audited

financial statement of these expenses may be obtained by contacting the organization at the address disclosed.

Exception: Non-sale Solicitations by Volunteers – Section 17510.3(c).

When the solicitation (i) is not a sales solicitation and (ii) is made by an individual volunteer who receives no compensation of any type in connection with the solicitation, the solicitor may comply with the disclosure provisions by (a) providing the name and address of the charitable organization on behalf of which all or any part of the money collected will be utilized for charitable purposes, (b) stating the charitable purposes for which the solicitation is made, and (c) stating that information about revenues and expenses of the organization, including its administration and fundraising costs, may be obtained by contacting the organization’s office at the address provided. The organization must provide this information to the person solicited within seven days after receipt of the request.

Note that the financial records of a soliciting organization shall be maintained and disclosed on the basis of generally accepted accounting principles (“GAAP”).⁸

Exception: Solicitations by Minor Volunteers – Section 17510.3(d).

A volunteer who is 18 years of age or younger and who receives no compensation of any type in connection with any solicitation on behalf of a charitable organization qualified under Section 501(c)(3) of the Internal Revenue Code is not required to make any disclosures.

Exception: Sales to Membership or on Premises; Bingo – Section 17510.6.

The disclosure rules do not apply to solicitations, sales, offers, or attempts to sell within the membership of a charitable organization or upon its regular occupied premises. No disclosure is required for funds raised from bingo games.

Disclosures Not Involving Direct Personal Contact – Section 17510.4.

If the initial solicitation or sales solicitation is made by radio, television, letter, telephone, including over the Internet, or any other means not involving direct personal contact with the person solicited, the solicitation must clearly disclose the information required for personal solicitations, described above. This disclosure requirement is not required for any radio or television solicitation of 60 seconds or less.

If the gift is subsequently made or the sale is subsequently consummated, the solicitation or sale for charitable purposes card shall be mailed to or otherwise delivered to the donor, or to the buyer with the item or items purchased.

⁸ Section 17510.5.

Fiduciary Relationship – Section 17510.8.

A fiduciary relationship exists between a charity or any person soliciting on behalf of a charity, and the person from whom a charitable contribution is being solicited.⁹

Charitable Trust – Section 17510.8.

The acceptance of charitable contributions by a charity or any person soliciting on behalf of a charity establishes a charitable trust and a duty on the part of the charity and the person soliciting on behalf of the charity to use those charitable contributions for the declared charitable purposes for which they are sought.¹⁰

Retention of Funds Solicited for Charitable Purposes – Section 17510.87.

[This Section ruled unconstitutional by U.S. District Court, Northern District of California.]

Any individual, corporation, or other legal entity who, for compensation, solicits funds or other property in this state for charitable purposes is prohibited from retaining more than 50 percent of the net proceeds collected as a fee for fundraising services.

Other Financial Disclosure Requirements – Section 17510.9.

If a charity that is engaged in any solicitation or sales solicitation for charitable purposes (i) collected more than 50 percent of its annual income and more than one million dollars (\$1,000,000) in charitable contributions from donors in California during the previous calendar year, and (ii) spent more than 25 percent of its annual income on “nonprogram activities” (the sum of (a) total salaries of all persons employed by the charity, (b) fundraising, (c) travel expenses, and (d) overhead and other expenses related to managing and administering the charity), the charity must annually file certain financial information with the Attorney General’s Registry of Charitable Trusts.

The following information must be included in the filing (on Form CT-694):

1. Total revenue and contributions received of the charity.
2. The dollar amount and the percentage of total revenue and charitable contributions allocated to funding each of the following administrative functions:
 - a. total salaries of all persons employed by the charity;
 - b. fundraising;
 - c. travel expenses;

⁹ Section 17510.8.

¹⁰ Section 17510.8.

- d. overhead and other expenses related to managing and administering the charity; and
 - e. the salaries of the five highest compensated persons employed by the charity.
3. The dollar amount and percentage of total revenue and charitable contributions allocated to programs.

The charity also must make this filing available following a request made in person, by telephone, or by mail, and the Attorney General also will make the filing available for public review at the Registry of Charitable Trusts in Sacramento and in the San Francisco and Los Angeles offices of the Attorney General. The Attorney General also publishes a report including this information for all reporting charities, available to public main libraries and to any person upon request and the payment of a reasonable fee to cover the costs of publication and distribution.

ARE THESE FUNDRAISING STATUTES CONSTITUTIONAL?

Solicitation of charitable contributions is protected speech under the First Amendment, and state laws cannot infringe upon this protected speech. The Supreme Court has rejected as unconstitutional attempts by states to compel charities or their professional fundraisers to disclose their fundraising costs to potential donors during telephone solicitations.

Riley v. National Federation of the Blind, 487 US 781 (1988).

The Supreme Court found unconstitutional: (i) the State of North Carolina's requirements that professional fundraisers disclose the percentage of charitable contributions collected during the previous year that were actually turned over to the charity, (ii) the state's regulation of charitable solicitation practices by defining the reasonableness of fees based on the percentage of receipts collected, and (iii) the state's statutory licensing requirement for professional fundraisers prior to solicitation.

The solicitation of charitable contributions is protected speech...using percentages [of receipts collected] to decide the legality of the fundraiser's fee is not narrowly tailored to the State's interest in preventing fraud. Riley at 789.

The Court also found that a state may not require a charity fundraiser to tell each person solicited about the costs of the solicitation campaign, because this information might discourage people from giving money to charity and interfere with the free speech rights of charity solicitors. The California legislature (finally in 2005) amended the Section of the California Business and Professions Code (S. 17510.3) to conform it to the Constitutional standards articulated in Riley.

Illinois ex rel Madigan v. Telemarketing Associates, Inc., 538 US 600 (2003).

The Illinois Attorney General charged a professional fundraising firm with fraud, claiming the fundraiser made intentionally misleading statements in its charitable solicitations. Rather than relying solely on the percentage of donations that the fundraiser would retain, as in

Riley, the Attorney General alleged that the telemarketers affirmatively represented that a significant amount would be paid over to the charity for charitable purposes, when they knew this was not true. The Court concluded that the First Amendment “does not shield fraud” and that fraudulent charitable solicitation is unprotected speech. Therefore, the Attorney General was not prohibited from pursuing a fraud action against the professional fundraiser for making statements intentionally misleading donors.

People v. Orange County Charitable Services, 73 Cal. App. 4th 1054 (1999).

This California court held that an injunction against inaccurate and misleading disclosures by a professional fundraiser in connection with charitable solicitations was not a First Amendment violation. Distinguishing Riley, the court emphasized that the injunction did not require spontaneous disclosure of the percentage information before the solicitation; rather, the speaker only needed to give percentage information if the donor *asked*. The court held that requiring the commercial fundraiser to respond to a donor’s question with information the fundraiser is required by law to keep is not the equivalent of compelled speech and does not constitute an undue burden on free speech.

See also:

Gospel Missions v. Bennett, 951 F. Supp. 1429 (CD Cal 1997).

The court found that certain provisions of Los Angeles City and County ordinances that imposed certain registration, licensing, and financial disclosure on charitable solicitations were not narrowly tailored to achieve a legitimate state interest and therefore were unconstitutional.

Watchtower Bible and Tract Society of New York, Inc. v. Village of Stratton, 536 US 150 (2002).

The Supreme Court invalidated a local Ohio ordinance that required door-to-door “canvassers” both to obtain a permit before canvassing and to display that permit when canvassing. The amount of speech covered by the ordinance was overly broad, and the ordinance was not tailored to protect the village’s state interests.

Other Considerations.

1. The USA Patriot Act imposes disclosure requirements on telemarketers that are also applicable to charities and should be reviewed.
2. Adopt a privacy policy to address the use of donor information. A new California privacy law, Senate Bill 27, places additional disclosure requirements on organizations that propose to share customer information with third parties that intend to use the information for direct marketing purposes. This law may extend to charities.
3. Charitable trust issues. Be careful not to restrict the use of charitable funds to a specific narrow purpose as a result of the solicitation.

4. California also regulates the solicitation of salvageable personal property for charitable purposes (any type of property other than money, such as a vehicle). See California Welfare & Institutions Code Section 148, Revenue and Taxation Code Section 17201.

Local Regulation.

Charities that engage in fundraising also must comply with any local charitable solicitation laws. The charity should check on city and county requirements with either the office of county counsel, the county treasurer, the sheriff, the license department, the police department, or the city clerk. In some cases, the charity may need to obtain a permit or license; in others, particular disclosures or filings are required. These requirements vary a great deal from location to location.

A short description of certain San Francisco and Los Angeles requirements is provided below. For a complete list of more than 200 cities and counties that have solicitation ordinances, see Appendix C of CEB, *Advising California Nonprofit Corporations*.

San Francisco.

See San Francisco Police Code Article 9.6 Regulations for Solicitation for Charitable Purposes:

- No charitable organization may solicit, directly or through an agent or employee, any contribution for any charitable purpose or conduct any sales solicitation for charitable purposes activity on the streets, sidewalks, parks or other property under the control of the City and County of San Francisco unless such charitable organization shall have first obtained a Certificate of Registration from the Chief of Police.
- Upon request from the person solicited for information about the organization, the solicitor shall provide to the person a card entitled “Solicitation for Charitable Purposes Card.” The card shall be of a size to be prescribed by the Chief of Police or his or her designate, signed and dated under penalty of perjury by an individual who is a principal or officer of the charitable organization on whose behalf the solicitation is made.
- An individual engaging in sales solicitation for a charitable purpose by means of selling goods, products or services from a stationary display on the streets or sidewalks or other places held open to the public must also display a sign containing the name and address of the person on whose behalf the charitable solicitation is being made, and the fact that more information about the charitable organization is available upon request.

Los Angeles.

See Section 44.00 of the Los Angeles Municipal Code. General Information provided by the Los Angeles Police Commission, Commission Investigation Division, Charitable Services Section:

- The Los Angeles Municipal Code requires any person or organization soliciting or holding a special event in the City to obtain an Information Card (IC) from Charitable Services Section of the Los Angeles Police Commission prior to the event or appeal. The Report of Results of Activity form needs to be completed and submitted at the conclusion of the event/appeal
- If an organization is not established with Charitable Services Section, specific documents must be submitted and reviewed before an Information Card can be issued. The documents are (1) Corporation Articles (and Amendments), (2) Bylaws, (3) Internal Revenue Service letter of income tax exemption and (4) Franchise Tax Board (State of California) letter of income tax exemption, and (5) the Charitable Trust (CT) number issued by the State of California, Office of the Attorney General.
- For more information, the LAMC internet address is www.lacity.org; then single click on the left-hand side of the page: City Charter, Rules & Codes; scroll down on the page to Municipal Code and click once; then single click on the left-hand side of the page: Municipal Code; then single click on the left-hand side of the page: Municipal Code; then single click on Chapter IV; then click on the page Article 4 Philanthropy.

II. COMMERCIAL FUNDRAISERS AND FUNDRAISING COUNSEL

California law, and in particular the Nonprofit Integrity Act of 2004 (the “NIA”) as embodied in the Government Code, imposes specific registration, reporting, and disclosure obligations on persons or firms that are identified as either “commercial fundraisers” or “fundraising counsel.”

Commercial Fundraiser.

A commercial fundraiser for charitable purposes is defined as any individual, corporation, or other legal entity who for compensation does any one or more of the following:¹¹

1. Solicits funds, assets, or property in California for charitable purposes.
2. As a result of a solicitation of funds, assets, or property in California for charitable purposes, receives or controls funds, assets, or property solicited for charitable purposes.
3. Employs, procures, or engages any compensated person to solicit or control funds, assets, or property for charitable purposes.

Note that “commercial fundraiser” does not include an employee or trustee of a charitable organization, among others.¹²

Fundraising Counsel.

A fundraising counsel for charitable purposes is defined as any person who is described by **all** of the following:¹³

1. For compensation plans, manages, advises, counsels, consults, or prepares material for, or with respect to, the solicitation in California of funds, assets, or property for charitable purposes.
2. Does not solicit funds, assets, or property for charitable purposes.
3. Does not receive or control funds, assets, or property solicited for charitable purposes in California.
4. Does not employ, procure, or engage any compensated person to solicit, receive, or control funds, assets, or property for charitable purposes.

¹¹ Gov Code. §12599.

¹² Gov. Code §12599(a).

¹³ Gov. Code §12599.1.

Note that “fundraising counsel” does not include an attorney, or an employee or trustee of a charitable organization, among others.¹⁴

Charitable Organizations, Commercial Fundraisers, and Fundraising Counsel: Prohibitions.

The law sets forth twelve prohibited acts and practices in the planning, conduct, or execution of any charitable solicitation or sales promotion. The prohibitions apply, according to the law, “regardless of injury,” the same as those that apply to charities themselves, discussed in Section I above.¹⁵

Commercial Fundraisers and Fundraising Counsel: Registration Requirements.

Similarly, the NIA addresses registration with the Registry from three distinct perspectives: (1) as a requirement of commercial fundraisers and fundraising counsel,¹⁶ (2) as a prohibition on charitable organizations, barring them from contracting with a commercial fundraiser or fundraising counsel if not registered as required,¹⁷ and (3) as a remedy for charitable organizations, allowing them to void contracts with commercial fundraisers and fundraising counsel if not properly registered.¹⁸

Commercial Fundraisers: Constructive Trustee.

The NIA makes all commercial fundraisers constructive trustees as to all funds collected pursuant to solicitations for charitable purposes, and it requires the fundraiser to account to the Attorney General for all funds. The NIA subjects the fundraiser to the Attorney General’s supervision and enforcement over charitable funds to the same extent as a trustee for charitable purposes.¹⁹

Commercial Fundraisers: Notice to Attorney General.

The law requires that before beginning any charitable solicitation, a commercial fundraiser must file a notice with the Registry setting forth information identifying the fundraiser and the charitable organization, the fundraising methods to be used, the dates when fundraising will begin and end under the contract, and identifying information about the person responsible for directing and supervising the work of the fundraiser.

¹⁴ Gov. Code §12599.1(b).

¹⁵ Gov. Code §12599.6(f).

¹⁶ Gov. Code §§12599(m) and 12599.1(c).

¹⁷ Gov. Code §12599.6(c).

¹⁸ Gov. Code §12599.3(a).

¹⁹ Gov. Code §12599(g).

The notice must be filed not less than 10 days before the beginning of each solicitation campaign, event, or service, except for solicitations to aid victims of emergency hardship or disasters, in which case the notice must be filed not later than when the solicitation begins.²⁰

Commercial Fundraisers: Misrepresentations.

Commercial fundraisers (and charitable organizations) may not misrepresent the purpose of the charitable organization or the nature, purpose, or beneficiary of a solicitation. Misrepresentation may be established by word, conduct, or failure to disclose a material fact.²¹

Commercial Fundraisers: Deposit of Contributions.

For each contribution in the control or custody of a commercial fundraiser, the NIA requires the fundraiser, within five working days of receipt, (1) to deposit the contribution in an account in a bank or other federally insured financial institution solely in the name of the charitable organization and over which the beneficiary charitable organization has the sole right of withdrawal, or (2) to deliver the contribution to the charitable organization in person, by Express Mail, or by another method providing for overnight delivery.²²

Commercial Fundraisers: Prohibitions.

A commercial fundraiser for charitable purposes may not solicit in California on behalf of a charitable organization unless the organization has registered with the Registry or is exempt from such registration.²³

No person may act as a commercial fundraiser if that person (or any officer or director of that person's business or any person with a controlling interest in the business or any person employed or paid to solicit funds by the fundraiser) has been convicted in state or federal court of a crime, punishable as a misdemeanor or felony, arising from the conduct of charitable solicitation.²⁴

Commercial Fundraisers: Record Retention.

Commercial fundraisers must maintain, for at least 10 years, two categories of records: (1) solicitation campaign records, including donor information, revenue and expense data, the names and addresses of employees, and the name and number of each bank or other account in which funds were deposited by the fundraiser, and (2) ticket sale records for charitable events, including the number of tickets purchased and donated by each contributor and a list of all organizations receiving donated tickets for use by others.²⁵

²⁰ Gov. Code §12599(h).

²¹ Gov. Code §12599.6(a).

²² Gov. Code §12599.6(e).

²³ Gov. Code §12599(m).

²⁴ Gov. Code §12599(l).

²⁵ Gov. Code §12599.7(a), (b).

Fundraising Counsel: Notice to Attorney General.

The law requires that fundraising counsel must register with the Registry. In addition, before performing any services for a charitable organization, fundraising counsel must also file a notice with the Registry, not less than 10 working days before services start. The notice must include the name and address of fundraising counsel and of the charitable organization, and the dates when the performance of services begins and ends.²⁶

²⁶ Gov. Code §12599.1(e).

III. THIRD PARTY FUNDRAISING AGREEMENTS

Commercial Fundraisers: Contracts with Charitable Organizations.

The NIA requires that a commercial fundraiser and a charitable organization must enter into a written contract for each solicitation campaign, event, or service. The contract must be signed by an authorized contracting officer for the commercial fundraiser and by an official authorized to sign by the charitable organization's governing body. The mandatory provisions of the contract, which may be inspected by the Attorney General, include:

1. A statement of the charitable purpose of the fundraiser.
2. A statement of the "respective obligations" of the commercial fundraiser and the charitable organization.
3. If the fundraiser is to be paid a fixed fee, the contract must state the fee and provide a good faith estimate of what percentage the fee will be of total contributions, disclosing the assumptions on which the estimate is based, which must reflect all relevant facts known to the fundraiser.
4. If the fundraiser is to be paid a percentage fee, a statement of the percentage of total contributions that will be remitted to or retained by the charitable organization or, if the sale of goods is involved, the percentage of the sales price remitted to or retained by the charitable organization. In determining the percentage, the fundraiser's fee, as well as any other amounts the charitable organization is required to pay as fundraising costs, must be subtracted from contributions and sales receipts received.
5. The starting and ending dates of the contract and the date solicitation activity will begin in California.
6. The contract must require the fundraiser to handle contributions in accordance with the NIA's requirements (discussed above) on the deposit or delivery of funds to the charity.
7. A statement that the charitable organization shall exercise control and approval over the content and frequency of any solicitation.
8. If the fundraiser proposes to pay any person or legal entity, in cash or in kind, to attend, sponsor, approve, or endorse a charity event, the maximum dollar amount of those payments must be stated.

The contract must also contain three distinct provisions relating to cancellation of the contract. *First*, the contract must allow the charitable organization to cancel the contract without cost, penalty, or liability for a period of 10 days after signing, by giving written notice in a specified manner. Any funds collected by the fundraiser after notice of cancellation shall be held in trust for the benefit of the charitable organization without deduction for costs or expenses. *Second*, the contract must permit a charitable organization to terminate the contract on 30 days'

written notice to the fundraiser, effective five days after the notice is mailed. The charitable organization remains liable for the fundraiser's services during the 30-day period. *Third*, the contract must provide that, after the initial 10-day cancellation period, the charitable organization may terminate the contract at any time by giving written notice, without payment of any kind to the fundraiser, if (1) the fundraiser makes material misrepresentations in solicitations or about the charitable organization, (2) the charitable organization learns that the fundraiser or its agents have been convicted of a crime punishable as a misdemeanor or felony, arising from charitable solicitation, or (3) the fundraiser otherwise conducts fundraising activities that cause or could cause "public disparagement of the charitable organization's good name or good will."²⁷

Fundraising Counsel: Contracts with Charitable Organizations.

The NIA also makes clear that there must be a written contract between the fundraising counsel and the charitable organization for each service to be performed. The contract must be signed by the authorized contracting officer for fundraising counsel and by an official who is authorized²⁸ to sign by the governing body of the charitable organization.²⁹ Current law sets forth extensive provisions that must be included in the contract.³⁰

The contract must also contain two distinct provisions relating to cancellation of the contract. *First*, the contract must allow the charitable organization to cancel the contract without cost, penalty, or liability for the first 10 days after signing, by giving written notice in a specified manner. *Second*, the contract must permit the charitable organization to terminate the contract on 30 days' written notice to fundraising counsel. The notice is effective five days after the date of mailing; termination is effective 30 days after that. The charitable organization is liable for the services of fundraising counsel up to the effective date of termination.³¹

Charitable Organizations: Right to Cancel or Void Contracts with Commercial Fundraisers or Fundraising Counsel.

Contract cancellation rights of charitable organizations are addressed twice in the NIA. First, they appear as mandatory provisions of contracts between charitable organizations and commercial fundraisers or fundraising counsel, as discussed earlier. Second, they appear as separate rights, entirely apart from the terms of any contract. Thus, even if contracts fail to spell out the required rights of cancellation, the NIA provides that charitable organizations nevertheless have those rights by law.³² The NIA also provides that charitable organizations may void contracts with commercial fundraisers or fundraising counsel if they are not properly

²⁷ Gov. Code §12599(i).

²⁸ See Penal Code Sections 19 and 319-337.

²⁹ Gov. Code §12599.1(f).

³⁰ Gov. Code §12599.1(d).

³¹ Gov. Code §12599.1(f)(8),(9).

³² Gov. Code §12599.3(b), (c), (e), (f), (g).

registered.³³ Finally, whenever a charitable organization cancels a contract, it must mail a duplicate copy of the notice of cancellation to the Registry.³⁴

³³ Gov. Code §12599.3(a).

³⁴ Gov. Code §12599(d).

IV. INTERNET FUNDRAISING

Charities increasingly accept donations via the Internet. It is currently unclear when Internet activity will result in jurisdiction in a particular state. If a charity is passive and donors visit its web site, a state may not impose its charitable solicitation requirements. On the other hand, a state may exert jurisdiction in cases where a charity actively reaches out to donors in that state. A strict reading of many states' solicitation laws would require that a charity maintaining a web site including a request for contributions register in that state.

THE CHARLESTON PRINCIPLES: ON CHARITABLE SOLICITATIONS USING THE INTERNET

The Charleston Principles (the "Principles") reflect the informal, nonbinding advice of the Board of Directors of the National Association of Attorneys General/National Association of State Charity Officials ("NAAG/NASCO") to NASCO members. The topic of charitable solicitations using the Internet was the focus of the NASCO 2000 Seminar in San Diego, California. The final version was approved by the NASCO Board as Advisory Guidelines on March 14, 2001.

In response to the proliferation of web site solicitations, state charity officials addressed the issue of who has to register where and developed consistent guidelines addressing online charitable solicitations. The Principles provide guidance to state charity officials with respect to when charities and their fundraisers may be required to register or may be subject to enforcement action, and in what jurisdictions, with regard to charitable solicitations via the Internet.

Suggested Registration Requirements for Internet Solicitation.

- A. An entity that is domiciled within a state and uses the Internet to conduct charitable solicitations in that state must register in that state. This is true without regard to whether the Internet solicitation methods it uses are passive or interactive, maintained by itself or another entity with which it contracts, or whether it conducts solicitations in any other manner. An entity is domiciled within a particular state if its principal place of business is in that state.
- B. An entity that is not domiciled within a state must register in accordance with the law of that state:
 1. If its non-Internet activities alone would be sufficient to require registration;
 2. If
 - a. the entity solicits contributions through an interactive web site; and

- b. either the entity:
- (i) specifically targets persons physically located in the state for solicitation; or
 - (ii) receives contributions from the state on a repeated and ongoing basis or a substantial basis through its web site;

or

3. If the entity solicits contributions through a site that is not interactive, but either specifically invites further offline activity to complete a contribution, or establishes other contacts with that state, such as sending e-mail messages or other communications that promote the web site; and the entity satisfies (b)(2)(i) or (ii) above.

To “specifically target persons physically located in the state for solicitation” means to either (i) include on its web site an express or implied reference to soliciting contributions from that state or (ii) otherwise affirmatively appeal to residents of the state, such as by advertising or sending messages to persons located in the state (electronically or otherwise) when the entity knows or reasonably should know the recipient is physically located in the state. Charities operating on a purely local basis, or within a limited geographic area, do not target states outside their operating area if their web site makes clear in context that their fundraising focus is limited to that area, even if they receive contributions from outside that area on less than a repeated and ongoing basis or on a substantial basis.

An “interactive web site” is a web site that permits a contributor to make a contribution, or purchase a product in connection with a charitable solicitation, by electronically completing the transaction, such as by submitting credit card information or authorizing an electronic funds transfer. Interactive sites include sites through which a donor may complete a transaction online through any online mechanism processing a financial transaction, even if completion requires the use of linked or redirected sites. A web site is interactive if it has this capacity, regardless of whether donors actually use it.

An entity that solicits via e-mail into a particular state shall be treated the same as one that solicits via telephone or direct mail if the soliciting party knew or reasonably should have known that the recipient was a resident of or was physically located in that state.

Exclusions from Registration:

- Maintaining or operating a web site that does not contain a solicitation of contributions but merely provides program services via the Internet (such as through a public information web site) does not, by itself, invoke a registration requirement. This is true even if unsolicited donations are received.

- Entities that provide solely administrative, supportive, or technical services to charities without providing substantive content, or advice concerning substantive content, are not required to register

Fraud.

NASCO advises states to enforce the law against any entity whose Internet solicitations mislead or defraud persons physically located within a particular state, without regard to whether that entity is domiciled in the state or is required to register in that state pursuant to the Principles.

V. SPECIAL FUNDRAISING VEHICLES – BINGO AND RAFFLES

California generally prohibits games of chance, but makes certain exceptions for charitable bingo and raffles, subject to specific requirements. Note that if a game of chance is conducted over the Internet, other states may also seek to impose jurisdiction.

BINGO

Bingo is governed by California Penal Code (“Pen C”) Section 326.5. Cities and counties can adopt ordinances permitting certain organizations to hold bingo games for charitable purposes if certain requirements are met.

“Bingo” means a game of chance in which prizes are awarded on the basis of designated numbers or symbols on a card that conform to numbers or symbols selected at random. The winning cards shall not be known prior to the game by any person participating in the playing or operation of the bingo game. All preprinted cards shall bear the legend, “for sale or use only in a bingo game authorized under California law and pursuant to local ordinance.”³⁵

Certain restrictions applicable to bingo games include:

- Any organization authorized to conduct bingo games must conduct the game only on property owned or leased by it, or property whose use is donated to the organization, and which property is used by that organization for an office or for performance of the purposes for which the organization is organized.³⁶
- All bingo games shall be open to the public, not just to the members of the authorized organization.³⁷ However, no minors are allowed to participate.³⁸
- A bingo game shall be operated and staffed only by members of the authorized organization that organized it. Those members shall not receive a profit, wage, or salary from any bingo game.³⁹
- No individual, corporation, partnership, or other legal entity, except the organization authorized to conduct a bingo game, shall hold a financial interest in the conduct of a bingo game.⁴⁰

³⁵ Pen C §326.5(o).

³⁶ Pen C §326.5(f).

³⁷ Pen C §326.5(g).

³⁸ Pen C §326.5(e).

³⁹ Pen C §326.5(h).

⁴⁰ Pen C §326.5(i).

- Charities must keep all profits derived from a bingo game in a special fund or account and shall not be commingled with any other fund or account. Those profits shall be used only for charitable purposes.⁴¹
- No person shall be allowed to participate in a bingo game unless the person is physically present at the time and place where the bingo game is being conducted.⁴²
- The total value of prizes awarded during the conduct of any bingo games shall not exceed two hundred fifty dollars (\$250) in cash or kind, or both, for each separate game which is held.⁴³

RAFFLES

Old Regime.

Lotteries are generally prohibited under Section 319 of the California Penal Code and are defined as follows:

A lottery is any scheme for the disposal or distribution of property by chance, among persons who have paid or promised to pay any valuable consideration for the chance of obtaining such property or a portion of it, or for any share or any interest in such property, upon any agreement, understanding, or expectation that it is to be distributed or disposed of by lot or chance, whether called a lottery, raffle, or gift-enterprise, or by whatever name the same may be known.

With the exception of the State-sponsored lottery, and certain charity raffles discussed below, a “lottery,” as defined above, is illegal, and any person convicted of operating a lottery could be convicted of a misdemeanor and subject to a \$10,000 fine or six months in jail, or both.⁴⁴

A lottery has three essential elements: (1) distribution of a prize, (2) the element of chance, and (3) consideration paid for a chance at the prize.⁴⁵ The absence of any one of these three elements makes the event something other than a lottery and, thus, legal. Although the first two elements, prize and chance, will exist in any fundraising lottery or raffle conducted by a charity, charities could eliminate the third element, consideration, to make the event legal.

⁴¹ Pen C §326.5(j).

⁴² Pen C §326.5(m).

⁴³ Pen C §326.5(n).

⁴⁴ See Pen C §§19 and 319-337.

⁴⁵ *Cal. Gasoline Retailers v. Regal Petroleum Corp.*, 50 Cal. 2d 844, 851 (1958).

Consideration is established if any of the players have to pay in order to have a chance at winning the prize.⁴⁶ For example, if some are required to pay for a chance to participate in the lottery, and others are allowed to participate for free, the element of consideration is nevertheless present.⁴⁷ If, however, there is general and indiscriminate distribution of raffle tickets free to any and all who ask for one, and if those receiving the tickets are then permitted to participate and claim the prize if they win, the element of consideration is missing and the game is legal.⁴⁸ Accordingly, under current law, charities have been able to conduct lawful raffles by ensuring general and indiscriminate distribution by offering tickets in exchange for a suggested donation.

Most charities conducting raffles, however, either through ignorance or willful disregard of the law, have made little effort to conform to the law. Other charities have made good faith efforts to conform to the law, but in all likelihood, have failed to meet the gratuitous, general, and indiscriminate distribution standard. Opinions from the California Attorney General demonstrate that certain requirements must be met in order to meet such standard.⁴⁹

First, there must be public disclosure that the donation is voluntary. The opinions suggest that the organization should convey to all participants, at the time the donation is requested, that the donation is voluntary and that tickets are available for free. Second, there must be equal participation for all participants.⁵⁰ Those receiving the tickets for free must be able to participate in the raffle to the same extent as persons making “gratuitous” donations. Thus, in practice, one player should be able to obtain as many free tickets as another is permitted to purchase. In other words, if one participant is permitted to purchase five tickets, then any participant should be able to obtain up to five tickets for free.

The requirement of equal participation essentially requires the charity to set some limit on the number of tickets a participant can acquire. Setting the number too low will result in not enough tickets being sold. On the other hand, setting the number too high requires the charity to give out free tickets to that extent to anyone who asks. This “free-loader” problem may have dissuaded many charities from conducting raffles or lotteries in a manner that met the strict requirements of the law.

New Regime.

Effective July 1, 2001, qualified tax-exempt organizations may conduct raffles under Pen C Section 320.5. Under the statute, the raffle may be conducted only by an organization that has been qualified to conduct business in California for at least one year and that is tax-exempt under Rev & T C Section 23701a, Section 23701b, Section 23701d, Section 23701e, Section 23701f, Section 23701g, Section 23701k, Section 23701l, Section 23701t, or Section 23701w.⁵¹ Section 23701(d) is the California equivalent of Section 501(c)(3) of the

⁴⁶ *People v. Shira*, 62 Cal. App. 3d 442, 451, 460-61 (1976).

⁴⁷ *Id.* at 460, and fn. 11.

⁴⁸ *Id.* at 459-60.

⁴⁹ 68 Op. Atty. Gen. Cal. 275 (1985); 82 Op. Atty. Gen. Cal. 12 (1999).

⁵⁰ *See* 60 Op. Atty. Gen. Cal. 130 (1977).

⁵¹ Pen C §320.5(c).

Internal Revenue Code. Furthermore, the organization must use the raffle funds for directly supporting a beneficial or a charitable purpose in California.⁵² For purposes of Pen C Section 320.5, a raffle is defined as a scheme for the distribution of prizes by chance among persons who paid money for paper tickets that provide the opportunity to win such prizes, and which meets all of the following requirements:⁵³

- Each ticket is sold with a detachable coupon or stub, and both the ticket and its associated coupon or stub are marked with a unique and matching identifier.
- Winners of the prizes are determined by draw from among the coupons or stubs.
- The draw is conducted in California under the supervision of a natural person who is 18 years of age or older.
- At least 90 percent of the gross receipts generated from the sale of raffle tickets for any given draw are used by the eligible organization conducting the raffle to benefit or provide support for beneficial or charitable purposes; alternatively, the organization may use those revenues to benefit another private, nonprofit organization, provided that an organization receiving these funds is itself an eligible organization under the statute. In no event may funds raised by raffles be used to fund any beneficial, charitable, or other purpose outside of California.

With regard to the 90 percent of gross receipts distribution requirement, Pen C Section 320.5(b)(4)(A) provides that an eligible organization may use funds from sources other than the sale of raffle tickets to pay for the administration or other costs of conducting a raffle. Therefore, it appears that the statute permits an eligible organization to use its funds to cover raffle expenses as long as 90 percent of the gross revenue from the raffle is used for charitable or beneficial purposes. Penal Code Section 320.5 was enacted as enabling legislation for the amendment to the California Constitution that was passed as Proposition 17 in March 2000. The amendment provides that at least 90 percent of the gross receipts from the raffle shall be used for beneficial or charitable purposes in California, but it is silent on the issue of the eligible organization's using other resources to cover the expenses of the raffle. It is thus uncertain whether Pen C Section 320.5, as enacted, extended the parameters of a legal raffle as prescribed by the amendment approved as Proposition 17.

Only an employee of the eligible organization is entitled to receive compensation in connection with the operation of a raffle.⁵⁴ No raffle may be conducted by any gaming machine, apparatus, or device.⁵⁵ No raffle may be conducted, and no tickets may be sold, within an

⁵² Pen C §320.5(a).

⁵³ Pen C §320.5(b).

⁵⁴ Pen C §320.5(d).

⁵⁵ Pen C §320.5(e).

operating satellite wagering facility or racetrack. A raffle may not be advertised, operated, or conducted in any manner over the Internet, and no raffle tickets may be sold, traded, or redeemed over the Internet; “advertisement,” however, does not include the announcement of a raffle on the web site of the eligible organization.⁵⁶ No individual, corporation, partnership, or other legal entity, besides the eligible organization, may have a financial interest in the conduct of a raffle.⁵⁷

An eligible organization may conduct a raffle only if it registers annually with the Department of Justice and completes the necessary registration forms provided by the Department of Justice.⁵⁸ Further, once registered, an eligible organization must annually provide the Department of Justice with the following information on a form provided by the Department of Justice (Pen C Section 320.5(h)):

- The aggregate gross receipts from the operation of raffles;
- The aggregate direct costs incurred by the eligible organization from the operation of raffles; and
- The charitable or beneficial purposes for which proceeds of the raffles were used, or the identity of the eligible recipient organization to which proceeds were directed, and the amount of those proceeds.

The registration form, Form CT-NRP-1, is prescribed by the California Attorney General. A completed registration form and a filing fee must be submitted by September 1 of each year (*i.e.*, September 1 through August 31) during which a raffle is expected to be conducted. If registration is not made by September, an eligible organization must submit the registration form and fee at least 90 days before the raffle is held.⁵⁹ Every registered eligible organization must also file a nonprofit raffle report each year on or before September 1 on Form CT-NRP-2. The Forms CT-NRP-1 and CT-NRP-2 can be found at the Attorney General’s web site: caag.state.ca.us/charities/statutes.htm.

The registration and reporting requirements do not apply to a religious corporation, a charitable corporation organized primarily as an educational institution or a hospital, a health care service plan licensed under Health & S C Section 1349, or a cemetery corporation regulated under Chapter 19 of Division 3 of the Business and Professions Code.⁶⁰

⁵⁶ Pen C §320.5(f).

⁵⁷ Pen C §320.5(g).

⁵⁸ Pen C §320.5(h).

⁵⁹ Department of Justice Regulations for the Non-profit Raffle Program, Chap 4.

⁶⁰ Pen C §320.5(h)(7).

A raffle is exempt from the requirements of Pen C Section 320.5 if it satisfies all of the following requirements:⁶¹

- It involves a general and indiscriminate distribution of the tickets;
- The tickets are offered on the same terms and conditions as the tickets for which a donation is given; and
- The scheme does not require any of the participants to pay for a chance to win.

The requirements for exempting a raffle from Pen C Section 320.5 are consistent with the factors previously used by the Attorney General in determining the illegality of raffles prior to the enactment of Pen C Section 320.5.

Note that no charitable contribution deduction is available for the purchase of raffle tickets or for a donation in connection with which the donor received a raffle ticket. The recipient of the ticket is deemed to have received a return benefit of equal value.

THE CALIFORNIA ATTORNEY GENERAL'S QUESTIONS AND ANSWERS REGARDING RAFFLES

1. May charities now hold raffles to raise funds?

Recent changes to the state constitution and Penal Code provide a narrow exception to the prohibition against gambling in California. After July 1, [2001] certain tax-exempt groups such as charities may hold fund-raising raffles.

2. What is a raffle?

A raffle is a type of lottery in which prizes are awarded to people who pay for a chance to win. Each person enters the game of chance by submitting a detachable coupon or stub from the paper ticket purchased. A raffle must be conducted under the supervision of a natural person age 18 or older. At least 90 percent of the gross receipts from raffle ticket sales must be used by the eligible tax-exempt organization to benefit or support beneficial purposes in California.

Groups are prohibited from awarding raffle prizes by use of a gaming machine, apparatus or device such as a slot machine. A raffle also may not be advertised, operated or conducted over the Internet. However, the organization conducting the raffle may place on its web site an announcement of a raffle. See Penal Code section 320.5.

⁶¹ Pen C §320.5(m).

3. Who may hold raffles?

Only eligible private, tax-exempt nonprofit groups qualified to conduct business in California for at least one year prior to conducting the raffle may conduct raffles to raise funds for the organization and charitable or beneficial purposes in California.

Eligible organizations are charities and religious or other organizations that were exempted from state taxation by the Franchise Tax Board under the following Revenue and Taxation Code sections: 23701a (labor, agricultural, or horticultural organizations other than cooperative organizations); 23701b (fraternal orders); 23701d (corporations, community chests or trusts operating exclusively for religious, charitable or educational purposes); 23701e (business leagues, chambers of commerce); 23701f (civic leagues, social welfare organizations or local employee organizations); 23701g (social organizations); 23701k (religious or apostolic corporations); 23701l (domestic fraternal societies); 23701t (homeowners' associations); and 23701w (veteran's organizations).

If you need a copy of your tax-exempt letter, submit an e-mail request to the Franchise Tax Board or write to: Exempt Organizations Unit, Franchise Tax Board, P.O. Box 942840, Sacramento, CA 94240-0040.

4. Does an organization already registered as a charity need to register separately to conduct a raffle? Are there separate reporting requirements?

Yes. Raffle registration is a separate requirement from charity registration. A report on raffle activities is required during the year (September 1 through August 31) in which any raffle is held.

5. Must all eligible organizations register and report?

Nonprofit religious organizations, schools and hospitals are exempt from the registration and reporting requirements; however, even though they are not required to register and report, those organizations must still comply with all other provisions of Penal Code section 320.5.

6. Can my organization hold a raffle immediately?

No. Before conducting a raffle, your group must be registered with the Attorney General's Registry of Charitable Trusts. Your group also must receive written confirmation of your annual registration before holding the initial raffle.

7. If an organization gives away raffle tickets, does it have to register and report?

Registration is not required if all tickets for a drawing are free, and solicitations of voluntary donations to the organization are in no way connected to distribution of tickets, and this is made clear to all participants. If you require a “donation” in return for a ticket, you must register.

8. How do I register to conduct a raffle?

Complete the raffle annual registration form (ct-NRP-1) and mail to the Registry with your \$20 registration fee by September 1 of the year (September 1 through August 31) in which you expect to hold a raffle. Checks should be made payable to the Department of Justice.

Please note, you must receive written confirmation of your registration before holding a raffle. Raffle registration forms are available on the [Attorney General’s web site] or may be requested by mail, fax, or telephone.

9. How long is a raffle registration valid?

A raffle registration is good for 12 months – from September 1 through August 31 – and must be renewed annually.

10. If my organization registers but decides not to hold a raffle, is the fee refundable?

No.

11. What information must we provide for raffle registration?

An eligible nonprofit group must furnish on the registration form:

- a. Name of organization;
- b. Address of organization;
- c. One or more of the following:

Federal Tax/Employer Identification Number

(assigned by the Internal Revenue Service and usually found on the IRS letter granting exemption from federal taxes. Contact the Exempt Organization Section of the IRS at (877) 829-5500; or <http://www.irs.gov/> with questions); or

Corporate Number

(assigned by the Secretary of State at the time the Articles of Incorporation are endorsed and filed); or

Organization Number

(assigned by the Franchise Tax Board to associations, trusts, and organizations that are not incorporated in California but do business in California); or

California Charitable Trusts Identification Number

(assigned by the Registry of Charitable Trusts to organizations required to register and report with the Registry).

- d. Name and title of a “fiduciary,” which is a person such as a director, officer, trustee or other individual occupying a similar position of responsibility in the organization.

12. As a chapter of a statewide organization, do I have to register to hold a raffle?

Yes. Each individual chapter of an organization that plans to conduct a raffle must register and complete a Nonprofit Raffle Report for each raffle conducted.

13. My organization has changed the raffle date noted on the registration form. Do we need to contact the Registry?

No. You can indicate the revised date on the Nonprofit Raffle Report when it is completed and filed.

14. When is the Nonprofit Raffle Report disclosing raffle activities required to be filed?

A separate disclosure report is required for each raffle held by the organization. The reports may be filed with the Registry of Charitable Trusts anytime after the conclusion of a raffle, but must be filed by no later than September 1 of each year for activities in the current registration period.

15. What kind of record keeping is required?

The required information appears on the Nonprofit Raffle Report form (ct-NRP-2). Basically, the organization must report the date and location of the raffle held; total funds received from the raffle; total expenses for conducting the raffle; the charitable or beneficial purpose for which raffle proceeds were used or the amount and organization to which proceeds were directed. (See Nonprofit Raffle Report form at forms.)

16. Are there limits on raffle prizes?

State law does not specify any limits on the value of raffle prizes.

17. Does an organization report individual buyers of raffle tickets?

No.

18. When can an organization expect to receive confirmation of registration?

Depending on volume, it could be up to 60 days after receipt of the registration form.

19. Can I complete the registration and report forms on the Internet?

Yes. However, upon completion, you must print it, sign and mail it along with the fee to the Registry of Charitable Trusts.

VI. ENDOWMENTS

UMIFA: THE LAW OF ENDOWMENTS

A. What Is An Endowment?

- To a donor, an endowment is a sum of money given to a charity for charitable purposes, with only the “income” being spent and “principal” being preserved.
- To an accountant, it is a fund which is “permanently restricted”.
- To a lawyer, it is an institutional fund not wholly expendable on a current basis under the terms of the gift instrument.
- Thus, a “true” endowment is one established or created by the donor. A board-restricted endowment (or “quasi-endowment”) is created when the Board takes unrestricted funds and imposes a spending restriction.

B. What Was UMIFA And Why Was It Adopted?

The Uniform Management of Institutional Funds Act (UMIFA) is a uniform law which provides rules regarding how much of an endowment a charity can spend, for what purpose, and how the charity should invest the endowment funds. UMIFA was the governing law in California through December 31, 2008. It was adopted because charities and their lawyers were unsure how to define “income” in the context of an endowment. Many looked to trust law, which generally defines “income” as including interest, dividends and the like, but defines gains as “principal”. Thus, charities invested endowments in bonds and high-dividend stocks, but passed by investments with favorable growth prospects if they had a low current yield. Consequently, long-term yield suffered. The drafters of UMIFA thought charities should be able to spend a prudent portion of the gains earned by an endowment.

C. So What Is UPMIFA?

1. UMIFA is thought to be out of date, particularly as to management, investment, and spending issues. In particular, the post-dot.com “down” market resulted in many “underwater” endowments, exposing the flaws in the UMIFA spending rules.
2. UPMIFA was approved by the National Conference of Commissioners on Uniform State Laws in July 2006, and has been adopted by approximately one-half of the states.

3. California adopted UPMIFA (Senate Bill 1329) effective January 1, 2009. It applies to funds created after that date, and to decisions made after that date for existing endowments (i.e., it will be “retroactive”).

D. How Does An Endowment Get Created?

1. An endowment fund is a fund not wholly expendable by the institution on a current basis under the terms of the applicable gift instrument. UPMIFA makes it clear that the term “endowment fund” does not include funds that the charity designates as endowment (these are “quasi-endowment” funds).
2. UPMIFA defines a gift instrument as being a “record” – information inscribed on a tangible medium or stored electronically – including an institutional solicitation, under which property is given. UPMIFA thus makes it clear that a gift instrument must be in writing, but expands the definition to include email. Governance documents, such as Bylaws, may be part of the gift instrument. A record is part of the gift instrument, however, only if the donor and the charity were, or should have been, aware of its terms.

E. How Should A Charity Invest Its Endowment?

1. Investment is a matter of state law. In California, the Board is subject to the rules on prudent investments as set forth in both the Corporations Code and UPMIFA (which unfortunately are not entirely consistent).
2. The Corporations Code provides that in making investments, a Board must “avoid speculation, looking instead to the permanent disposition of the funds, considering the probable income, as well as the probable safety of funds.” This is an “old fashioned” and fairly conservative statement of the prudent investor rule.
3. UPMIFA articulates a standard of care for both managing and investing an endowment. It requires the charity to consider the charitable purposes of the charity, and the purposes of the endowment fund. It requires the Board (and others responsible for managing and investing) to act in good faith and with the care of an ordinary prudent person, and notes that the charity may incur only appropriate and reasonable costs.
4. The charity must consider:
 - a. General economic conditions,
 - b. Effects of inflation and deflation,
 - c. Tax consequences,
 - d. The role of each investment in the overall portfolio,

- e. Expected total return from income and appreciation,
 - f. The charity's other resources, and
 - g. The needs of the charity and the fund to make distributions and preserve capital.
5. UPMIFA provides that an individual investment must be analyzed in the context of the total portfolio and the overall risk-reward objectives, and that a charity can invest in any kind of property that is not inconsistent with the standard of care.
 6. UPMIFA imposes a duty to diversify.

F. How Much Of An Endowment Can A Charity Spend?

1. UMIFA provided that "The governing board may appropriate for expenditure for the uses and purposes for which an endowment fund is established so much of the net appreciation, both realized and unrealized, in the fair value of the assets of an endowment fund over the historic dollar value of the fund as is prudent"

Net appreciation includes realized gains and unrealized gains.

Historic dollar value is "the aggregate fair value in dollars of (1) an endowment fund at the time it became an endowment fund, (2) each subsequent donation to the endowment fund at the time it is made, and (3) each accumulation made pursuant to a direction in the applicable gift instrument at the time the accumulation is added to the endowment fund."

Although UMIFA did not explicitly so state, most attorneys concluded that "income" (e.g., interest and dividends) could be spent as well (even with an "underwater" endowment).

2. UPMIFA makes a radical change and does away with the concept of "historic dollar value". UPMIFA allows a charity to appropriate for expenditure, or accumulate, so much of an endowment fund as the charity determines is prudent for the purposes for which the fund was established.
3. The charity must consider:
 - a. The duration and preservation of the endowment fund,
 - b. The purposes of the charity and the fund,
 - c. General economic conditions,
 - d. Effects of inflation and deflation,
 - e. Expected total return from income and appreciation,

- f. The charity's other resources, and
 - g. The charity's investment policy.
4. California's UPMIFA includes the optional provision stating that an appropriation of greater than 7% of the average FMV of an endowment (averaged over the last three years) is be presumptively imprudent.

G. What About Delegation?

UPMIFA allows a charity to delegate management and/or investment decisions to agents. The charity must act prudently in selecting the agent, establishing the scope of the delegation, and reviewing the agent's actions. A charity that does so is not liable for the actions of the agent. However, the agent is held to a "reasonable care" standard and is expressly made subject to appropriate court jurisdiction.

H. What About Changing A Restriction?

1. UPMIFA allows a charity to release or modify a restriction regarding management, investment, or purpose of a fund if the donor consents in writing.
2. If a purpose or use restriction becomes unlawful, impracticable, impossible to achieve, or wasteful, the court may modify the restriction in a manner consistent with the donor's intent. The Attorney General must be notified.
3. The court can modify a management or investment restriction if it has become impracticable or wasteful, impairs the management or investment of the fund, or (if due to unforeseen circumstances) the release would further the purposes of the fund. The Attorney General must be notified.
4. If a fund is less than \$100,000 in value and over 20 years old, and the charity determines that a restriction on the management, investment, or use of the fund is unlawful, impracticable, impossible to achieve, or wasteful, the charity can (after notice to the Attorney General) release or modify the restriction. It must thereafter use the funds in a manner consistent with the donor's charitable purposes.

I. What About Enforcing Spending Or Purpose Restrictions?

1. The Attorney General can bring an action to enforce the terms of a restricted gift. Depending on the law governing the internal affairs of the charity, an officer, director, or even a voting member may be able to challenge a breach of trust. *See, e.g.,* Cal. Corp. Code §5142 (for California nonprofit public benefit corporations).
2. What if the donor believes the institution is violating the use restriction? Some states have held that unless the donor reserves a right to enforce in the gift instrument, only

the state Attorney General has legal standing (*Carl Herzog Foundation v. University of Bridgeport*, 699 A.2d 995 (1997)). Other states have concluded that a donor may have standing (*LB Research and Education Foundation v. UCLA Foundation*, 130 CalApp 4th 171 (2005); *Smithers v. St. Luke's Roosevelt Hospital Center*, 723 N.Y.S.2d 426 (2001)).

3. A donor may consider building donor standing into the gift instrument. A power of reversion is likely to render the gift incomplete and non-deductible for income tax purposes; consider including a power to redirect the gift to another charity willing to abide by the restrictions in the event of default.

J. What About Those Accountants?

1. In general, for accounting purposes, funds received as “true” endowments are classified as permanently restricted. Funds subject to a restriction that the Board can satisfy – such as a timing restriction or purpose restriction – are classified as temporarily restricted. Funds received with no donor-imposed restrictions are classified as unrestricted.
2. FASB Staff Position 117-1 sets forth guidelines for reporting endowments governed by UPMIFA. It states that a charity should classify “all or a portion” of an endowment as permanently restricted net assets, based upon explicit donor restrictions (if any) or what the Board determines must be retained permanently. For example, a Board could determine that UPMIFA requires it to maintain the “historic dollar value” of its endowments. The value of an endowment in excess of the amount reported as permanently restricted is to be reported as temporarily restricted, until such time as some amount is “appropriated for expenditure”, at which time that amount becomes unrestricted. FASB Staff is not encouraging charities to report as permanently restricted the purchasing power of an endowment (e.g., initial value increased by the rate of inflation, not reduced for losses or expenditures). FSP 117-1 also requires more disclosure, including information regarding a charity’s spending policy and investment policy.
3. FASB 124 requires that distributions from the endowment, and losses suffered by the endowment, be taken from the endowment portion of the temporarily restricted asset class first (until it goes to zero), then from the unrestricted asset class. Put another way, the amount reported as permanently restricted funds would not change if there is a significant investment loss; the loss would reduce the temporarily restricted and the unrestricted asset classes.

VII. TAX LAW

State law regulates fundraising solicitations, fundraisers, and fundraising counsel. Federal tax law speaks to situations in which a donor can take a tax deduction and what steps are necessary to secure the deduction. In this section, we address, in question-and-answer format, some of the key questions that donors and Charities face in understanding the ability of the donor to take a tax deduction.

We do not discuss the rules applicable to corporate donors in this paper, nor do we address the deductibility of contributions made to private foundations.

CAN THE DONOR ALWAYS DEDUCT THE FAIR MARKET VALUE OF A GIFT?

Subject to percentage limitations discussed below, an individual donor may always deduct the face value of cash donations made to a Charity. With respect to gifts of property, a donor may be able to deduct either the fair market value of the property or the donor's tax basis in the property, depending on the facts.

In order to understand the extent of the donor's potential deduction, we must always ask a series of questions:

1. What type of property is the donor giving (*e.g.*, cash, stock, real estate...)?
2. Has the donor held the property for more than one year? Property held for more than one year is considered long-term capital gain property. Property held for one year or less is short-term capital gain property.
3. What is the donor's basis in the property? Basis is usually the amount the donor paid for the property, less any depreciation taken on the property.
4. What is the fair market value of the property? We talk later about how to value certain types of property.
5. How will the charity use the property? For example, there is a different deduction for art donated to an art museum that will display the art than for art donated to a soup kitchen that will sell the painting.

Once we know the answers to these five questions, we can determine whether the donor will be able to deduct the fair market value of the gift or simply his or her basis, as follows:

- For gifts of cash, the donor can deduct the face value of the cash.
- For gifts of long-term capital gain real estate, stock, and other intangible property, such as partnership interests, the donor can deduct the fair market value of the item donated.

- For gifts of tangible personal property (such as artwork) to a Charity that will use the item as part of its charitable function (*e.g.*, art to a museum), the donor can deduct the fair market value of the item.
 - If the donor made the donated item, however, the donor can only deduct his or her basis.
- Most other donations are limited to basis, with some minor statutory exceptions.
- If an item is worth less than the donor's basis, the donor may never deduct more than basis. For example, if a computer costs the donor \$2,000 and is worth \$1,000 at the time of donation, the donor deducts \$1,000 only.
- Certain items such as vehicles are subject to special rules limiting the deduction to the amount the Charity receives on sale of the item (unless the Charity uses the item).

CAN THE DONOR DEDUCT THE ENTIRE AMOUNT OF THE GIFT IN THE YEAR MADE?

Although it is rarely an issue for most donors, individual donors can only deduct their aggregate cash charitable contributions to public charities in any year to the extent of 50% of their adjusted gross income for the year. Any balance can be carried forward for up to five years.

As an example, if a donor's adjusted gross income on his 2004 tax return is \$100,000, the donor can deduct up to \$50,000 in charitable contributions for 2004. If the donor made \$60,000 in charitable contributions, for example, he can deduct the remaining \$10,000 in the following year, provided he does not otherwise exceed his contribution limit for the following year.

This 50% limitation applies to cash gifts. Gifts of property, such as real estate and stock, are generally limited to 30% of adjusted gross income if the full fair market value of the gift is allowed, and 50% if the donor only deducts his basis in the item.

WHEN HAS THE DONOR MADE A DEDUCTIBLE GIFT?

The Supreme Court held that the test for determining whether a transfer was a gift or not was whether the transfer was made out of "detached and disinterested generosity"; *i.e.*, a transfer for no consideration and without the expectation of return benefit. Duberstein v. Comm'r., 363 US 278 (1960).

Regulation Section 1.170A-1(h) places a burden of proof on a donor who makes a gift and receives goods or services in return: In order to claim a deduction, the donor must show that his/her contribution exceeded the value of the goods or services received, and also that he/she intended to make the excess payment. Only the excess is deductible.

There are also special bargain sales rules where a donor contributes property that is subject to debt, and the charity assumes the debt. In these situations, the donor's gift will be a part gift and part sale, with basis allocations described in the IRC and Regulations.

WHEN IS THE GIFT COMPLETE?

Basic Tax Law.

Regulation Section 1.170A-1(b): Regulation Section 1.170A-1(b) says a contribution is made at the time delivery of the gift asset is effected. The general application of this rule often involves the question: “When did the donor relinquish dominion and control over the gift asset?”

Applications of the Basic Rules.

Gift by check or credit card.

The unconditional delivery of a check that clears in “due course” is deemed to be given on date of delivery to the charity. A contribution made by credit card is deductible in the year in which the charge is made, regardless of when paid. Rev. Rul. 78-38, 1978-1 CB 67.

Gift of stock.

A properly endorsed stock certificate (or stock certificate and signed stock power) donated to a charity (or its agent) is deemed given on date of delivery.

Alternative rule: The gift is complete when ownership of the stock is transferred on the corporation’s books and records. For shares held in street name, the gift is complete when ownership of the stock is changed on the broker’s records.

When is a check or stock certificate “delivered” – the “mailbox” rule.

A check (or stock certificate) that is *mailed* to the charity, and received in due course, is deemed to be *delivered* on date of mailing. It is not clear whether this longstanding “mailbox rule” applies to checks or certificates sent by Federal Express or other private carrier. When a donor puts a letter in a USPS mailbox, or when a letter is taken from a donor’s private mailbox by a postal worker, the donor can no longer take back the letter. The letter no longer belongs to the donor. On the other hand, when a donor sends a Federal Express envelope, Federal Express is the donor’s agent, and the donor can theoretically ask Federal Express not to deliver the package. In that case, the date of delivery is the date that the package is received by the charity.

Real property and tangible personal property.

Delivery of tangible personal property usually requires an actual transfer of possession. In some cases, constructive delivery can be shown (TG Murphy, TC Memo 1991-276), for example, by delivery of a signed bill of sale. Gifts of real estate require the delivery of a formally executed and acknowledged (notarized) deed.

WHAT DOES THE DONOR NEED TO DO TO BE ABLE TO TAKE A DEDUCTION?

The Recordkeeping and Appraisal Rules.

Regulation Section 1.170A-13 contains a wealth of useful information. Note that these rules apply to all gifts, regardless of whether the substantiation rules of IRC Section 170(f)(8) apply.

The “Basic” Rules for Gifts of Cash and Property.

For gifts of cash, the donor must maintain a canceled check, receipt, or other “reliable written records” evidencing each contribution (including name of charity, date, and amount). The burden of proof regarding the “reliability” of those records (*i.e.*, whether the IRS will accept them) rests with the donor.

For gifts of cash or property worth \$250 or more, the donor must have received from the charity a written receipt or thank you letter. Additional information about the required contents of this acknowledgment are set forth in IRS Publication 1771, which follows on page 40 of this paper.

For gifts of property to which the appraisal rules (described below) do not apply, the donor must maintain a receipt from the charity showing the name of the charity, the date and location of the gift, and a description (but not value) of the property. If the deduction for a gift of property exceeds \$500, the donor must maintain a written record including the above information plus manner and date of acquisition and cost basis, and the donor must complete and submit Form 8283 with the donor’s return.

Appraisal rules are discussed below. For a discussion of receipts that the charity should provide to the donor, see above.

WHEN IS AN APPRAISAL NECESSARY?

One of the requirements for gifts that include items *other than* cash, cash equivalents, or publicly traded stock with no restrictions as to transfer, is that these gifts, if worth more than \$5,000, must be appraised. The following rules apply to appraisals, for which the donor is responsible.

Qualified Appraisal.

To be a qualified appraisal, a document must:

1. Be made not earlier than 60 days prior to the date of the contribution, and be received by the donor no later than the due date (including extensions) of the return on which the deduction is claimed;
2. Be prepared, signed, and dated by a qualified appraiser; and
3. Not involve an appraisal fee that is based on the appraised value of the property.

A qualified appraisal must include the following information:

1. A description of the property that sufficiently identifies the property that was appraised as the property that was (or will be) contributed;
2. In the case of tangible property, the physical condition of the property;
3. The date (or expected date) of the contribution;
4. The terms of any agreement relating to the use, sale, or other disposition of the property contributed, including the terms of any agreement or understanding that restricts or earmarks donated property for a particular use;
5. The name, address, and identifying number of the qualified appraiser and of any entity or person who employs or engages the qualified appraiser;
6. The qualifications of the qualified appraiser who signs the appraisal, including the appraiser's background, experience, education, and membership, if any, in professional appraisal associations;
7. A statement that the appraisal was prepared for income tax purposes;
8. The date on which the property was appraised;
9. The appraised fair market value on the date of contribution;
10. The method of valuation used to determine the fair market value, such as the income approach, the market-data approach, and the replacement-cost-less-depreciation approach; and
11. The specific basis for the valuation, such as specific comparable sales transactions or statistical sampling, including a justification for using sampling and an explanation of the sampling procedure employed.

Qualified Appraiser.

A qualified appraiser is an individual who meets the following criteria:

1. Holds himself or herself out to the public as an appraiser or performs appraisals on a regular basis;
2. Is qualified to make appraisals of the type of property being valued, according to qualifications described in the appraisal;

3. Understands that an intentional overstatement of the value of the property described in the appraisal may subject the appraiser to civil penalty for aiding and abetting an understatement of tax liability;
4. Is not the donor, donee, or any party to the transaction in which the donor acquired the property;
5. Is not any person employed by or related to one of the above parties;
and
6. Is not someone primarily used by one of the above parties who does not perform a majority of his or her appraisals for other persons.

Appraisal Summary.

In addition to obtaining a qualified appraisal, the donor must attach an “appraisal summary,” which must be signed by both the appraiser and the donee, to his/her income tax return for the year in which the deduction is claimed. The IRS has provided Form 8283 for this purpose.

Sample Form.

The following is an all-purpose receipt where no return benefits are provided to the donor:

This letter is to gratefully acknowledge, for your tax records, our receipt of your generous gift of *[cash in the amount of \$_____][describe property donated in reasonable detail]*. We received your gift on *[date]* at *[location]*.

No goods or services were provided to you in exchange for this gift. Therefore, the full amount of your contribution is deductible.

Again, we thank you for your support.

IRS PUBLICATION 1771
CHARITABLE CONTRIBUTIONS –
SUBSTANTIATION AND DISCLOSURE REQUIREMENTS

IRS Publication 1771, *Charitable Contributions – Substantiation and Disclosure Requirements*, explains the federal tax law for organizations such as charities and churches that receive tax-deductible charitable contributions and for taxpayers who make contributions. There are two general rules that organizations need to be aware of to meet substantiation and disclosure requirements for federal income tax return reporting purposes:

- A donor is responsible for obtaining a **written acknowledgment** from a charity for any single contribution of \$250 or more before the donor can claim a charitable contribution on his/her federal income tax return;
- A charitable organization is required to provide a **written disclosure** to a donor who receives goods or services in exchange for a single payment in excess of \$75.

More on written acknowledgments and written disclosures is addressed in this publication. For information about organizations that are qualified to receive charitable contributions, see IRS Publication 526, *Charitable Contributions*. Publication 526 also describes contributions you can (and cannot) deduct, and it explains deduction limits. For assistance about valuing donated property, see IRS Publication 561, *Determining the Value of Donated Property*.

Written Acknowledgment.

Requirement.

A donor cannot claim a tax deduction for any single contribution of \$250 or more unless the donor obtains a contemporaneous, written acknowledgment of the contribution from the recipient organization. An organization that does not acknowledge a contribution incurs no penalty; but, without a written acknowledgment, the donor cannot claim the tax deduction. Although it is a donor's responsibility to obtain a written acknowledgment, an organization can assist a donor by providing a timely, written statement containing the following information:

1. Name of organization;
2. Amount of cash contribution;
3. Description (but not the value) of non-cash contribution;
4. Statement that no goods or services were provided by the organization in return for the contribution, if that was the case;
5. Description and good faith estimate of the value of goods or services, if any, that an organization provided in return for the contribution;

6. Statement that goods or services, if any, that an organization provided in return for the contribution consisted entirely of intangible religious benefits (described later in this publication), if that was the case.

It is not necessary to include either the donor's social security number or tax identification number on the acknowledgment.

A separate acknowledgment may be provided for each single contribution of \$250 or more, or one acknowledgment, such as an annual summary, may be used to substantiate several single contributions of \$250 or more. There are no IRS forms for the acknowledgment. Letters, postcards, or computer-generated forms with the above information are acceptable. An organization can provide either a paper copy of the acknowledgment to the donor, or an organization can provide the acknowledgment electronically, such as via an e-mail addressed to the donor. A donor should not attach the acknowledgment to his or her individual income tax return, but must retain it to substantiate the contribution. Separate contributions of less than \$250 will not be aggregated. An example of this could be weekly offerings to a donor's church of less than \$250, even though the donor's annual total contributions are \$250 or more.

Contemporaneous.

Recipient organizations typically send written acknowledgments to donors no later than January 31 of the year following the donation. For the written acknowledgment to be considered contemporaneous with the contribution, a donor must receive the acknowledgment by the earlier of:

1. The date on which the donor actually files his or her individual federal income tax return for the year of the contribution; or
2. The due date (including extensions) of the return.

Goods and Services.

The acknowledgment must describe goods or services an organization provides in exchange for a contribution of \$250 or more. It must also provide a good faith estimate of the value of such goods or services, because a donor must generally reduce the amount of the contribution deduction by the fair market value of the goods and services provided by the organization. Goods or services include cash, property, services, benefits, or privileges. However, there are important exceptions as described below:

Token Exception – Insubstantial goods or services a charitable organization provides in exchange for contributions do not have to be described in the acknowledgment. Goods and services are considered to be insubstantial if the payment occurs in the context of a fundraising campaign in which a charitable organization informs the donor of the amount of the contribution that is a deductible contribution, and:

1. The fair market value of the benefits received does not exceed the lesser of 2 percent of the payment or \$76; or

2. The payment is at least \$38, the only items provided bear the organization's name or logo (*e.g.*, calendars, mugs, or posters), and the cost of these items is within the limits for "low-cost articles," which is \$7.60. Free, unordered low-cost articles are also considered to be insubstantial. Example of a token exception: If a charitable organization gives a coffee mug bearing its logo and costing the organization \$7.60 or less to a donor who contributes \$38 or more, the organization may state that no goods or services were provided in return for the \$38 contribution. The \$38 is fully deductible.

The dollar amounts are for 2001. Guideline amounts are adjusted for inflation. Contact IRS Exempt Organizations Customer Account Services at (877) 829-5500 for annual inflation adjustment information.

Membership Benefits Exception – An annual membership benefit is also considered to be insubstantial if it is provided in exchange for an annual payment of \$75 or less and consists of annual recurring rights or privileges, such as:

1. Free or discounted admissions to the charitable organization's facilities or events;
2. Discounts on purchases from the organization's gift shop;
3. Free or discounted parking;
4. Free or discounted admission to member-only events sponsored by an organization, where a per-person cost (not including overhead) is within the "low-cost articles" limits.

Example of a membership benefits exception: If a charitable organization offers a \$75 annual membership that allows free admission to all of its weekly events, plus a \$20 poster, a written acknowledgment need only mention the \$20 value of the poster, since the free admission would be considered insubstantial and, therefore, would be disregarded.

Intangible Religious Benefits Exception – If a religious organization provides only "intangible religious benefits" to a contributor, the acknowledgment does not need to describe or value those benefits. It can simply state that the organization provided intangible religious benefits to the contributor.

Unreimbursed Expenses.

If a donor makes a single contribution of \$250 or more in the form of unreimbursed expenses, *e.g.*, out-of-pocket transportation expenses incurred in order to perform donated services for an organization, then the donor must obtain a written acknowledgment from the organization containing:

- A description of the services provided by the donor;

- A statement of whether or not the organization provided goods or services in return for the contribution;
- A description and good faith estimate of the value of goods or services, if any, that an organization provided in return for the contribution;
- A statement that goods or services, if any, that an organization provided in return for the contribution consisted entirely of intangible religious benefits (described below), if that was the case.

In addition, a donor must maintain adequate records of the unreimbursed expenses. See Publication 526, *Charitable Contributions*, for a description of records that will substantiate a donor's contribution deductions.

Example of an unreimbursed expense: A chosen representative to an annual convention of a charitable organization purchases an airline ticket to travel to the convention. The organization does not reimburse the delegate for the \$500 ticket. The representative should keep a record of the expenditure, such as a copy of the ticket. The representative should obtain from the organization a description of the services that the representative provided and a statement that the representative received no goods or services from the organization.

What are "intangible religious benefits?" Generally, they are benefits provided by a tax-exempt organization operated exclusively for religious purposes, and are not usually sold in commercial transactions outside a donative (gift) context. Examples include admission to a religious ceremony and a *de minimis* tangible benefit, such as wine used in a religious ceremony. Benefits that are not intangible religious benefits include education leading to a recognized degree, travel services, and consumer goods.

Payroll Deductions.

When a donor makes a **single contribution of \$250 or more by payroll deduction**, the donor may use both of the following documents as the written acknowledgment obtained from the organization:

- A pay stub, Form W-2, *Wage and Tax Statement*, or other document furnished by the employer that sets forth the amount withheld by the employer and paid to a charitable organization; and
- A pledge card that includes a statement to the effect that the organization does not provide goods or services in consideration for contributions to the organization by payroll deduction.

Each payroll deduction amount of \$250 or more is treated as a separate contribution for purposes of the \$250 threshold requirement for written acknowledgments.

Written Disclosure.

Requirement.

A donor may only take a contribution deduction to the extent that his/her contribution exceeds the fair market value of the goods or services the donor receives in return for the contribution; therefore, donors need to know the value of the goods or services. An organization must provide a written disclosure statement to a donor who makes a payment exceeding \$75 partly as a contribution and partly for goods and services provided by the organization.

A contribution made by a donor in exchange for goods or services is known as a *quid pro quo* contribution. Example of a *quid pro quo* contribution: A donor gives a charitable organization \$100 in exchange for a concert ticket with a fair market value of \$40. In this example, the donor's tax deduction may not exceed \$60.

Because the donor's payment (*quid pro quo* contribution) exceeds \$75, the charitable organization must furnish a disclosure statement to the donor, even though the deductible amount does not exceed \$75.

A required written disclosure statement must:

- Inform a donor that the amount of the contribution that is deductible for federal income tax purposes is limited to the excess of money (and the fair market value of property other than money) contributed by the donor over the value of goods or services provided by the organization; and
- Provide a donor with a good faith estimate of the fair market value of the goods or services.

Examples of Written Acknowledgments.

- "Thank you for your cash contribution of \$300 that (organization's name) received on December 12, 2004. No goods or services were provided in exchange for your contribution."
- "Thank you for your cash contribution of \$350 that (organization's name) received on May 6, 2004. In exchange for your contribution, we gave you a cookbook with an estimated fair market value of \$60."
- "Thank you for your contribution of a used oak baby crib and matching dresser that (organization's name) received on March 15, 2004. No goods or services were provided in exchange for your contribution."

The following is an example of a written acknowledgment where a charity accepts contributions in the name of one of its activities:

- “Thank you for your contribution of \$450 to (organization’s name) made in the name of its *Special Relief Fund* program. No goods or services were provided in exchange for your contribution.”

*An organization must furnish a disclosure statement in connection with either the solicitation or the receipt of the *quid pro quo* contribution. The statement must be in writing and must be made in a manner that is likely to come to the attention of the donor. For example, a disclosure in small print within a larger document might not meet this requirement.

Exception.

A written disclosure statement is not required:

- Where the goods or services given to a donor meet the “token exception,” the “membership benefits exception,” or the “intangible religious benefits exception” described earlier; or
- Where there is no donative element involved in a particular transaction, such as in a typical museum gift shop sale.

Penalty.

A penalty is imposed on charities that do not meet the written disclosure requirement. The penalty is \$10 per contribution, not to exceed \$5,000 per fundraising event or mailing. An organization may avoid the penalty if it can show that failure to meet the requirements was due to reasonable cause.

Further Information.

Written acknowledgment – Detailed rules for contemporaneous written acknowledgments are contained in Section 170(f)(8) of the Internal Revenue Code and Section 1.170A-13(f) of the Income Tax Regulations. The “low-cost article” rules are set forth in Section 513(h)(2) of the Code. This information can be found on the IRS web site at www.irs.gov.

Written disclosure – Detailed rules for written disclosure statements are contained in Section 6115 of the Internal Revenue Code and Section 1.6115-1 of the Income Tax Regulations. The penalty rules are contained in Section 6714 of the Code. This information can be found on the IRS web site at www.irs.gov.

IRS publications – Order publications by calling the IRS at (800) 829-3676. Download IRS publications at www.irs.gov.

IRS customer service – Telephone assistance for general tax information is available by calling IRS customer service toll-free at (800) 829-1040.

EO customer service – Telephone assistance specific to exempt organizations is available by calling IRS Exempt Organizations Customer Account Services toll-free at (877) 829-5500.

EO web site – Visit Exempt Organizations web site at www.irs.gov/eo.

TOKEN AND MINIMAL BENEFITS – UPDATED NUMBERS FOR INFLATION

Item	Rev. Proc. 90-12	2007	2008	2009
A	\$25.00	\$44.50	\$45.50	\$47.50
B	\$50.00	\$89.00	\$91.00	\$95.00
C	\$ 5.00	\$8.90	\$9.10	\$9.50

1. If the *fair market value* of all benefits received from the charity in return for a contribution is not more than the *lesser* of 2% of the contribution or “B,” the benefits may be disregarded as insubstantial for purposes of return benefit disclosures.
2. If a contribution is at least “A” and the only benefits received in return are items *costing*, in total, no more than “C” and bearing the charity’s name or logo, the benefits may be disregarded as insubstantial for purposes of return benefit disclosure.

VIII. HYPOTHETICAL PROBLEMS

1. Bill is a wealthy entrepreneur. He decides to invite 100 of his closest friends to his incredibly large home for a party. He tells his friends that he hopes to raise funds for his favorite charity, Charity X, and asks each party attendee to write a check for \$100. Being a VIP, Bill cannot be bothered with the handling of the funds, so he hires an event planner to organize the party. The event planner collects the checks, some of which are made out in the name of Charity X and some of which are made out in the name of the event planner. The event planner deposits any checks made out to him, and writes a check for the total amount to Charity X. What are the legal issues?
2. The Development Director (“DD”) of Charity X has realized that Charity X needs to be more aggressive about securing its future needs. She proposes, in addition to the traditional annual fund drive, to start up a “Fund for the Reasonably Foreseeable Future” – the FRFF. Because her staff is overwhelmed, she proposes to hire an outside contractor to run FRFF. She will also seek the advice of a firm on how to put the campaign together, even though that firm will not actually raise funds for FRFF. The literature promoting the fund will say, “Help us fund the reasonably foreseeable future by establishing the FRFF endowment fund.” She wants the contractor to conduct the fundraising effort through direct mail and over the internet. The FRFF begins to receive contributions in 2008, continuing in 2009. Any issues?
3. The local Zoo charges adult admission of \$10 and children pay \$1.

You can become a member at different levels. For \$70 you get unlimited zoo admission and a poster. For \$100 you get the \$70 benefits, plus a cool mug. For \$500 you get all of the above, plus the right to have lunch with the Zoo Director. For \$10,000 you get the right to use the Zoo once a year for an evening, after-hours party. You have to pay for all of the food and entertainment, but not for use of the Zoo facilities.

What is the donor’s deduction at each level?

CONCLUSION

This paper and the accompanying presentation are intended to make development directors and fundraising staff aware of some of the key areas of regulation that affect charitable fundraising. We urge the reader to contact his or her legal counsel to review these rules as they apply specifically to his or her charity.