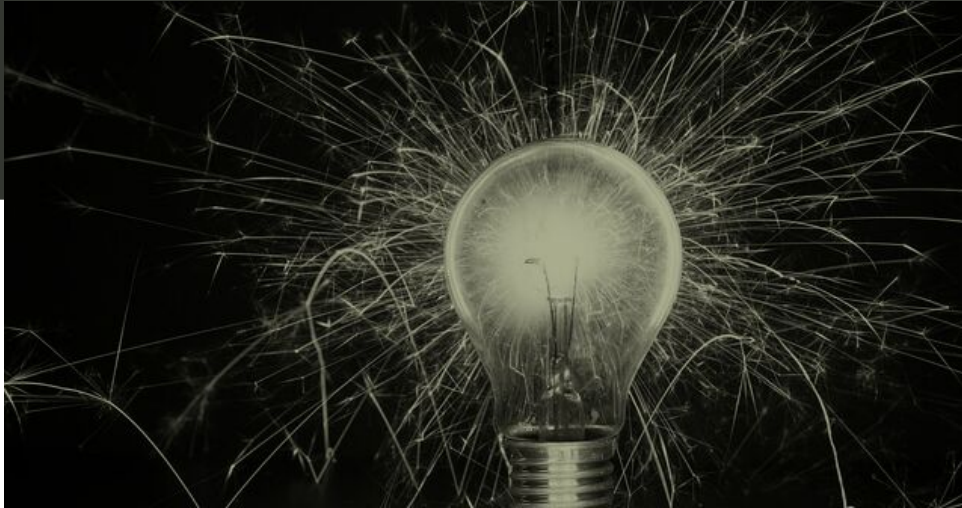


Report Critical of State Charity Regulation Sparks Controversy

03.02.23 | Linda J. Rosenthal, JD



The “nonprofit community” often presents a unified voice on key matters affecting philanthropy. But not always: Like American society at large, their individual views on the proper role for government can vary.

In late January, 2023, the [Philanthropy Roundtable](#), a prominent and influential “group of foundations and donors that advocates for a hands-off approach to regulating charities and giving,” published a report on state charity regulation that set off an immediate “firestorm of controversy.” The backlash comprised objections from many quarters – including the National Association of State Charity Officials as well as leading experts and commentators. The criticisms were based on both the methodology and conclusions of the report.

In response, the Philanthropy Roundtable has backed off a bit from full-throttled support for the research that seeks to tie less government oversight with a more thriving nonprofit sector. The organization now emphasizes that the report is a “... starting point for further research” with hopes that it will help “...lawmakers at the state level craft legislation that will free nonprofits of regulations.”

The New Study

The report in issue is a “state-by-state ranking of the rules state governments place on charities.” See [50-State Index of Charity Regulations](#), (January 31, 2023), a 44-page downloadable publication authored by Wayne Winegarden, Ph.D.

The document begins with four “key points”:

- “While there is a need for regulations on the charitable sector to foster accountability and trust in charities, excessive levels of regulation impose a burden on charities that outweighs the benefit of the regulation.
- Little research has been done to examine the impact of overregulation on the charitable sector. This study is a first step toward gaining a better understanding of the regulatory burden imposed on charities.
- By comparing states along five categories of charitable regulations, one can see that overregulation is correlated with relatively fewer charities in a state.
- Our society and those in need depend on a thriving, vibrant charitable sector. The evidence in this study suggests excessive levels of regulation are counterproductive to fostering a positive environment for charities and those they serve.”

According to Elizabeth McGuigan, senior director of policy and government affairs for Philanthropy Roundtable: “When you regulate something to an excessive degree, you’re going to get less charitable vibrancy.” See *New Report on State Charity Regulation Touches Off Debate About What Helps Nonprofits Thrive* (February 9, 2023) Alex Daniels, *The Chronicle of Philanthropy*.

“To determine their rankings,” Mr. Daniels explains, “Philanthropy Roundtable scored states in five categories: start-up regulations, annual reporting requirements, rules for paid solicitors, and audit mandates, as well as other types of oversight, including whether states use using a multi-agency approach to enforcement”

“Pennsylvania places the most stringent regulations on charities, according to the Roundtable’s report, while Montana sits on the other end of the spectrum.” Researchers “found that states with relatively low regulatory hurdles had a greater concentration of nonprofits.”

Swift Reactions

On February 8, 2023, the board of the National Association of State Charity Officials issued a statement, cautioning “that the that the data on state-level regulations in the report may be incomplete” and that “... the report’s key assumption that the number of charitable organizations is a good measure for the volume of actual charitable activity needs further analysis and study.”

Philanthropy Roundtable’s Elizabeth McGuigan disagreed, saying that “... the report didn’t suggest that lots of regulations directly stifled nonprofits but that there was a correlation between the two.”

It was that point about correlation, though, that received particularly sharp criticism from a variety of quarters. One executive of a leading nonprofit tweeted “a few design tips” for the Philanthropy Roundtable’s future research endeavors: “[A]ways know the difference between correlation and implied causation, and ... always consider more than one explanatory variable in an equation.”

The Daniels article notes that “some nonprofit experts and regulatory officials questioned the premise that regulations inhibited the creation of nonprofits and voiced concerns about the Philanthropy Roundtable’s methodology, saying that it mischaracterized how the average nonprofit in each state is actually affected by government oversight. The report, they said, improperly concluded that the proliferation of nonprofits in a state is a result of light regulation.”

Key Academic Critiques

Among those experts mentioned in the Daniels article is Erynn Beaton, a professor at the Ohio State University John Glenn College of Public Affairs, who serves on the Ohio Attorney General's Charitable Advisory Council. "State regulation of nonprofits is necessary to squash fraud and maintain donors' trust in the charities they support," she told Alex Daniels. "The question is whether there is a sweet spot in the amount of government oversight that can ensure confidence in how nonprofits operate without making life too difficult for charity leaders,..."

Professor Beaton also "took issue with the Philanthropy Roundtable index, saying it didn't collect current data on state nonprofit rules and used a 'blunt' approach to assign states with high or low levels of regulation." She added: "...[T]he number of charities in a given state likely had little to do with the regulatory environment. Other factors, such as the level of government funding to support nonprofit work and the needs of a state's residents, drive how many charities set up in each state."

"This report," she concludes, "makes some very large claims that the methodology just doesn't support. The size of the nonprofit sector has much more to do with need and resources in the state than it does the regulatory burden."

Another expert quoted in Mr. Daniels article is Professor Cindy Lott, director of the philanthropic leadership doctorate program at Indiana University's Lilly Family School of Philanthropy. She "has studied state regulation of nonprofits for years" and "spearheaded an effort to develop another study of state charity rules, called the Regulatory Breadth Index of state charity regulation."

"It is difficult to capture the nuances of how charities actually experience regulations," said Professor Lott. While not commenting directly on the new Philanthropy Roundtable index, she explained in detail how the two indexes differed considerably, noting as well that the Regulatory Breadth Index "was not created with the assumption that regulations hindered the growth and effectiveness of nonprofits." She added: "Methodology matters, and legal data is notoriously difficult to translate into accessible quantitative data....Nuance matters as well," explaining that "... a state can have a lot of regulations, but it is difficult to measure how tightly they are enforced or if smaller charities or specific types of nonprofits are exempt from some rules."

"In response," McGuigan stressed to Mr. Daniels that "... more work was needed to assess the impact of state regulation on charities." She said the "study is a starting point for further research, adding that she hopes it helps lawmakers at the state level craft legislation that will free nonprofits of regulations."

Letter to the Editor

On February 16, 2023, Elizabeth McGuigan and the report's author, Dr. Wayne Winegarden, submitted a letter to the editor of The Chronicle of Philanthropy titled "More Research Is Needed on State Regulation of Charities." They indicated they are "... pleased to see the robust conversation reflected in last week's Chronicle of Philanthropy article.... Such a dialogue is long overdue and is ultimately the purpose of the Philanthropy Roundtable report."

They continued: "Starting a discussion about which regulations create net benefits and which regulations impose net costs is essential. However, as the study emphasizes multiple times in

issuing its state scores, 'this is an imperfect ranking based on imperfect variables.' That does not mean it isn't a worthy endeavor. Much more can be learned about this topic, and additional research is needed."

They further explained their reasoning and purposes: "It's widely accepted that state regulations on charities can create important benefits: promoting trust and discouraging fraud. But how these regulations are implemented matters. The notion that regulations will impose net costs when taken to excess should not be controversial....Research is needed on when regulations transform from being beneficial into a financial burden, and into how they affect a charity's financial viability."

Conclusion

For a variety of reasons, the primary focus of charity regulation in the United States has, in recent years, shifted from the Internal Revenue Service to the activity of the state attorneys generals. It's a trend we've covered considerably over the last year or so.

An ongoing conversation about the appropriate scope and breadth of state charity oversight, and any legitimate conclusions that can be reached about it, is a critical one for the nonprofit sector going forward.

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