NONPROFITS: CALIFORNIA ATTORNEY GENERAL

The Charity Oversight Role of the California Attorney General: An Introduction

04.24.15 | Linda J. Rosenthal, JD

California charities and trustees know that there are multiple government agencies poking around in their affairs.

We explained in "Say What? We're Monitored by How Many Agencies?" that the Internal Revenue Service is clearly the poker-in-chief. The federal tax exemption – with charitable deductions tacked on – are huge perks that provide the IRS permission to poke.

Jostling for the top spot on the state level are three contenders. The Secretary of State's office issues nonprofit corporation charters and the Franchise Tax Board doles out exemptions from state income tax.

But the winner among all of these in the poking department is the Attorney General's Office. Its Charitable Trusts Section, including the Registry of Charitable Trusts, is granted broad legal powers to poke and prod: not just charitable organizations, but also any person or entity holding or soliciting charitable funds or assets.

The Special Focus of the California Attorney General

Is all of this butting in by federal *and* state agencies entirely necessary? Is there duplication?

Yes and no. There's a good deal of overlap, but there are important distinctions in scope and focus.

The IRS (and the Franchise Tax Board) zoom in on the charitable organization itself: whether it's organized and operated exclusively for charitable purposes so that it merits an exemption from

income taxes. The governing laws are Section 501(c)(3) of the Internal Revenue Code and Section 23701(d) of the California Revenue and Taxation Code. These tax agencies scrutinize the applicant-organizations when they first get going, and then periodically afterward via audits and reviews of information returns.

In recent years, the IRS has plunged more deeply into review of organizational governance – although that is traditionally the province of state law and regulators. The justification for this expansion is that examining how the organization is governed may give clues to possible violations of Section 501(c)(3)'s prohibitions against inurement of net earnings to individuals, and more than incidental private benefit.

The AG's Charity Oversight Role

"The Attorney General regulates charities and the professional fundraisers who solicit on their behalf. The purpose of this oversight is to protect charitable assets for their intended use and ensure that the charitable donations contributed by Californians are not misapplied and squandered through fraud or other means."

The key authorizing legislation is the Supervision of Trustees and Fundraisers for Charitable Purposes Act, California Government Code sections 12580-12599.8.

(With some exceptions, notably religious and educational institutions), it applies to "all charitable corporations, unincorporated associations, trustees, and other legal entities holding property for charitable purposes, commercial fundraisers for holding property for charitable purposes, fundraising counsel for charitable purposes, and commercial coventurers, over which the state or the Attorney General has enforcement or supervisory powers."

It applies as well to all non-California 501(c)(3) corporations that raise funds, do business, or hold property in California.

There are several elements to this oversight role:

Registry of Charitable Trusts

All charitable trustees and fundraising professionals – as broadly defined in this law – must register initially and on a continuing basis, and must file annual financial disclosure reports and report certain major events and transactions. Also subject to these requirements is any nonprofit organization that conducts raffles for charitable purposes. There are serious penalties and consequences for failing to comply.

Audits and Investigations

The Charitable Trusts Section attorney and auditors investigate misuse of charitable assets or fraudulent fundraising activities. They get leads from required document filings filed as well as tips and complaints by the general public, the media, or interested groups. The Attorney General "has broad authority under State statutes to regulate charitable organizations and trusts and to commence law enforcement investigations and legal actions to protect the public interest." The Attorney General represents the public beneficiaries of charities, and acts on their behalf. What types of activities might the Attorney General's office investigate? Here are some:

- self-dealing transactions by insiders, including loans and excessive compensation
- substantial losses of funds or assets in a single year
- losses from speculative investments
- unauthorized and unfair sale or conversion of the charity or assets for profit or to a profit-making entity
- illegal use of money
- channeling funds and assets away from their intended, charitable purposes to unauthorized, non-exempt purposes; and
- possible criminal activities

Conclusion

The AG's Office also publishes resources "to help charities stay within the law" including the *Attorney General´s Guide for Charities, pdf* and information for donors in the *Guide to Charitable Giving for Donors, pdf*.

There are also searchable databases for specific California charities and charitable fundraising professionals. Among the databases are Registry Search, for registrants generally, and CFR Search, which provides information and documents regarding commercial fundraisers for charitable purposes.

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