The Importance of Transparency in the Governmental Regulation of the Nonprofit Sector: Room for Improvement?

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A popular Government, without popular information, or the means of acquiring it, is but a Prologue to a Farce or a Tragedy; or, perhaps both. Knowledge will forever govern ignorance: And a people who mean to be their own Governors, must arm themselves with the power which knowledge gives.

- Letter from James Madison to W.T. Barry (July 4, 1822)

Sunlight is said to be the best of disinfectants; electric light the most efficient policeman.

- Louis D. Brandeis, Harper’s Weekly (Dec. 20, 1913)

I. INTRODUCTION

The above quotations from Founding Father, Political Theorist, and our 4th President James Madison, and Justice Louis D. Brandeis, underscore and vividly bring to life, the importance that transparency plays in the accountability of our Government, Society, and its institutions in general. The concept of transparency also plays an important role in the self-regulation of the charitable sector, and in the government regulation of the charitable sector, that reports $2.7 trillion in assets and $1.5 trillion in revenue. The Internal Revenue Service’s (“IRS”) 2009 redesign of IRS Form 990 was heralded at that time as subjecting the tax exempt

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1 One definition of “transparent” is “free from pretense or deceit . . . easily detected or seen through.” www.miramwebster.com

sector to a heightened standard of transparency, in the hopes of promoting self-regulation, assuring good governance, and promoting the prevention and detection of malfeasance. The National Association of State Charity Officials (“NASCO”) provided input on revisions to Form 990 and initially expressed criticism about increasing the filing threshold for the new form. The IRS maintains that the redesigned Form 990 enhances accountability in a variety of ways:

How does the new form enhance transparency of an organization’s mission, financial information and operations?

The new form’s summary page provides a snapshot of key financial, governance and operating information, including a comparison of the current year’s revenues, expenses, assets, and liabilities, with those of the prior year. The reordered core form provides a description of the organization’s program service accomplishments immediately after the summary page, to provide context before the user proceeds to sections on tax compliance, governance, compensation, and financial statements. The Checklist of Required Schedules also provides a quick view of whether the filing organization is conducting activities that raise tax compliance concerns, such as lobbying or political campaign activities, transactions with interested persons, and major dispositions of assets, and indicates which schedules the organization is required to file with the form.

Likewise, the IRS’s board governance practices published guidance also provide that “[b]y making full and accurate information about its mission, activities, finance, and governance publicly available, a charity encourages transparency and accountability to its constituents.”

The focus of this paper is not on the role of transparency in the self-regulation of the nonprofit sector (clearly that could consume an entire paper in itself). However, the widespread public availability of a charity’s financial and operational data in searchable form provides the important “electric light” or “policeman” described by Justice Louis Brandeis, that allows the IRS and state charity regulators to be a more efficient police force, aided by a militia of the “informed citizenry” Madison envisioned. Clearly, one important public policy reason why the

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3 “A major step in transparency is unfolding in the nonprofit world. The vehicle delivering this change is the newly revised IRS Form 990, "Return of Organization Exempt from Income Tax," which nonprofit organizations have begun filing for the 2008 tax year. The impact that the increased transparency will have on nonprofit organizations has been severely underestimated.” See, http://www.guidestar.org/rxa/news/articles/2009/the-door-has-opened-new-form-990-creates-strategic-opportunities-and-risks-for-nonprofit-organizations.aspx.

4 In comments submitted to the IRS dated September 14, 2007, NASCO objected to the IRS’s proposal to raise the threshold to file IRS Form 990EZ to $50,000. Subsequently, in a letter dated December 17, 2007, NASCO strenuously objected to the IRS’s proposal to raise the filing threshold for IRS Form 990 to $1 million (decreasing to $250,000 over time). See Appendix A and B


IRS Form 990 itself is public is the scarce resources the IRS possesses to audit and examine these “information returns.” Most recently available data indicates that the IRS examines less than .04 percent of the returns filed by 858,865 reporting tax exempt charitable organizations. Thus, the public availability of IRS Form 990 data allows donors, members of the public, the media, and other stakeholders to be the “eyes and ears” of the IRS in detecting malfeasing, and incomplete or inaccurate Form 990s. Moreover, charitable organizations that take the extra step to promote transparency by publishing the data on the Internet often short circuit what could be potentially costly and embarrassing investigations by governmental regulators by allowing experienced charity regulators to fend off unwarranted complaints almost immediately.

The core purpose of this paper is to examine the extent to which “transparency” plays in the government regulation of the nonprofit sector, with a particular emphasis on the extent to which a charity’s financial and operational data is electronically available on a widespread basis by government regulators, the extent to which government regulators make available on a widespread basis the results of investigations and enforcement actions, and to present and discuss the results of a survey of state charity regulator offices on the extent to which registration and other data is searchable and publicly available on the Internet. This paper will also examine how more liberalized information sharing between the IRS and state charity regulators can promote transparency, and thereby accountability, by our Nation’s tax exempt charitable organizations.

II. DISCUSSION

A. Federal Charity Regulation: The Internal Revenue Service

1. The IRS Website: Who Moved My Cheese?

As stated above, the IRS devoted significant time and effort into a complete redesign of IRS Form 990 to promote transparency and thereby accountability, for which it should be commended. It has expended significant resources since the initial re-design of the form to “tweak” it to continue to improve the form. Yet, in a roll-out of a new and re-vamped IRS Website in August of 2012, the IRS removed “charities” or the tax exempt sector from its main Internet landing page, thereby making it difficult for state regulators, donors, the media,


8 As stated recently by a State of Missouri Charity regulator in the Chronicle of Philanthropy:

An organization that tries to follow the best practices on transparency can prevent government investigations. On more than one occasion, when I have received a nasty complaint about a Missouri charity, I have decided that the allegation might be true. But upon doing a preliminary review online, I have found that the nonprofits in question were so transparent that I could verify that the complainers had it wrong, all without leaving my desk. Those nonprofits have no clue how close they came to large and embarrassing investigations.

academics, and the regulated sector itself to find important IRS guidance and information. This includes but is not limited to information on the IRS’s automatic revocation program, among other things. The IRS’ main Internet “landing page” formerly appeared like this:

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9 According to the IRS redesigned its website to make it easier for users to get to the information users most look for information about filing, payments, refunds, credits and forms. See http://www.irs.gov/help/article/0,,id=259023,00.html?portlet=101
The IRS Main landing page now appears like this:

Where does one interested in charities regulation or technical guidance navigate to find that treasure trove? It now takes two mouse “clicks” on the IRS website (first hidden under the cryptic moniker “Filings” and second under “charities and nonprofits”) to begin to obtain meaningful information about the tax exempt charitable sector\(^\text{10}\) (excluding private foundations) that reported $2.7 trillion in total assets and $1.5 trillion in revenue.\(^\text{11}\) Formerly, charities and nonprofits were prominently featured on the IRS Internet landing page. This IRS Website redesign, in this author’s view, has resulted in an abrupt “about face” in the IRS’s effort to promote transparency within the sector.\(^\text{12}\)

\(^{10}\) Alternately, a user may also click on “Information For” in the upper right hand corner of the Website to display a pull down menu that includes “Charities and Nonprofits.”

\(^{11}\) See 2012 Statistics of Income Bulletin.
The IRS website redesign has also made it more difficult for state charity regulators to obtain information about those charitable organizations that have had their tax exempt status automatically revoked in their state. Formerly, users were able to download an Excel file from a prominent area of the IRS website of all automatically revoked organizations by state of domicile. It is now far more difficult to obtain this information in a form that can be more readily used by state charity regulators to protect and safeguard charitable assets and donor restricted gifts made to organizations whose tax exempt status has been automatically revoked.

It is my view that the IRS must “walk the talk.” If the IRS demands greater transparency of the 1.7 million tax exempt organizations it regulates, it should hold itself to the same standard and more prominently feature exempt organizations and charities on its Internet site. Technical guidance, educational guidance, more powerful and robust search and customizable search engines with real time data on exempt organizations would give regulators, stakeholders, donors, academics, and the media better tools to assist the IRS in policing the “outliers” that fail to stay within the lines of statutory and regulatory requirements. On its Website, the IRS could provide direct access to Form 990 data that is filed by those reporting charitable organizations that are required to e-file their information returns and thereby leverage its scarce resources. In addition, greater transparency by the IRS would allow the many ethically governed charities and underperforming ones, better access to educational guidance and technical guidance to assist all them to employ best governance practices.

2. The IRS “Information Sharing” Program with State Charity Regulators

For many years, state charity regulators have urged the IRS to seek Congressional amendments to liberalize section 6103 of the Internal Revenue Code (“IRC”) to authorize the IRS to more freely communicate the results of audits of charitable organizations, the imposition of federal excise taxes on private foundations, and intermediate sanctions imposed on foundation managers, and related enforcement information, among other things. Section 6103 of the IRC generally guarantees confidentiality of tax returns, thereby encouraging the citizenry to voluntarily report and “self-assess” their income taxes to the IRS. Without confidentiality the voluntary nature of the Nation’s tax collection system would be jeopardized. Regrettably, the confidentiality mandate of section 6103 also includes charitable organizations that file “information returns.”

Taxpayer confidentiality, at least with state regulators, should not come into play for tax exempt organizations. Despite the fact that IRS Form 990 now reports robust public information about a charity’s finances, operations, lobbying, fundraising, governance, program services, executive compensation, functional expenses and income, and a myriad of other information about a charity, until the Pension Protection Act of 2009 (“PPA”), it was very difficult, if not illegal, for the IRS to share audit and enforcement data with state charity regulators. A last minute amendment to the PPA attempted to liberalize information sharing with state charity

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12 The author understands that the Exempt Organizations Division of the IRS was not pleased with the way the redesign downgraded the prominence of charities and tax exempt organizations on the website.

13 The entire list of revoked organizations remains available on the IRS Website, but not organized by state of domicile.
regulators, but it also subjected state charity regulators to criminal penalties and “Safeguard Procedures” that are explained in over 128 pages in IRS Publication No. 1075, “Tax Information Security Guidelines for Federal, State and Local Agencies” that are more properly designed for safeguarding tax data supplied to the IRS by individuals, corporations and partnerships, than on the tax exempt sector, whose tax returns themselves are publicly available on the Internet and who must provide public access to their Form 1023 and other data.

The effect of these draconian information sharing procedures is that only 4 states have entered into information sharing agreements with the IRS. For example, information that is produced to state charity regulators in “paper” form by the IRS may not be inputted or ‘typed” into any Networked computer system by a state charity regulator without the agency’s computer network being subject to another extremely difficult set of security procedures. Thus, state charity regulators must write the charitable organization that is subject to an IRS disclosure and request any communications from the IRS to free the regulator from the “shackles” of the IRS security requirements (See the ethical quandary caused by this discussed below).

These byzantine security requirements led 43 State Attorneys General to write a National Association of Attorneys General (“NAAG”) “Sign On” letter to Congress on October 28, 2011, asking Congress to free state charity regulators from the yoke of security requirements applicable to individual taxpayers. In the sign on letter co-authored by Hawaii Attorney General David M. Louie and Colorado Attorney General John W. Suthers, NAAG explained the problem created by the PPA as follows:

As a result of the Act subjecting information sharing between the IRS and state charity officials to IRC §7213’s criminal penalties, the IRS has had to subject state charity officials, including state attorneys general, to the same informational safeguards imposed on the tax and revenue agencies of the 50 states. A copy of the 106-page IRS Publication No. 1075 that describes the multitude of safeguard procedures to which state charity officials must adhere may be found at the following URL: http://www.irs.gov/pub/irs-pdf/p1075.pdf.

These procedures not only create the ethical and legal conflicts described below, they are simply unworkable given the limited resources of state charity officials and should not apply to information regarding the revenue, expenses and governance data of charitable organizations already required to publicly report their financial and operational data. The IRS’s understandable safeguards for the protection of confidential federal income tax information should be inapplicable.

These safeguards, for example, do not permit state charity officials to enter any shared data through a word processing program on any networked computer for inclusion in a civil complaint without complying with a myriad of security requirements that state charity officials do not have the resources to implement.

14 The author of this paper wishes to acknowledge that the IRS Exempt Organizations Division has made more than good faith efforts to educate state charity regulators on how to comply with these requirements.

15 See Appendix C.
Consequently, despite years of diligent efforts by state attorneys general to obtain information from the IRS, only three state Attorney General offices—New York, California and Hawaii—have entered into information-sharing agreements with the IRS since the adoption of the Act nearly five years ago.

Even the three states that have entered into information-sharing agreements have had to construct an uncomfortable “fiction” to use the data.\(^{16}\)

The NAAG Sign on letter closed noting that information applicable to tax exempt charitable organizations should, as a matter of public policy, be more freely available to State regulators, given the complementary role played by State Attorneys General in policing the sector:

We see no reason why IRC notices of refusals to grant tax-exempt status, proposed revocations of exempt status, or proposed deficiency taxes for prohibited transactions under chapters 41 or 42, such as intermediate sanctions, taxes on self-dealing transactions and similar matters involving public charities and foundations, should be subject to the same criminal penalties and security procedures applicable to individual and corporate income tax return information. This is all extremely valuable and important information that allows state charity officials to fulfill their statutory mandate. The safeguard requirements have proven unsuccessful and unworkable.\(^{17}\)

Congress has taken no action to liberalize the information sharing provisions of the PPA in response to the NAAG Sign On letter, nor does it appear that the IRS has advocated for such liberalization. Given that it is the primary role of State Attorneys General to safeguard donor expectations and charitable assets regardless of the form in which they are held, a role distinctly different from the “board patrol” role played by federal tax regulations, it is of vital importance that there be far more transparency in the relationship between the IRS and state charity regulators.

B. Transparency by State Charity Regulators: Is Source Data Public?

After having participated in the prosecution of one of the largest breach of trust cases by a tax exempt charitable trust—the “Bishop Estate Controversy” that lasted from 1996 to 2000, I set about to re-enact a registration requirement for charitable organizations that solicit contributions in Hawaii. From 1969 to 1994, Hawaii had a registration law, but only about 125 charities were registered (whether mainland-based or Hawaii domiciled with the State at the time of the law’s repeal)

After two unsuccessful attempts to re-codify a registration law in Hawaii, and after a three-part newspaper series in the Honolulu Advertiser\(^{18}\) entitled “Hawaii’s Rules Lax on

\(^{16}\) Id.

\(^{17}\) Id.

\(^{18}\)
Oversight of Charities,” then Hawaii Attorney General Mark Bennett ("AG Bennett") supported my efforts to yet again introduce a registration law. AG Bennett, however, demanded as a condition of bill introduction that the law be effective—that registration forms and related submissions not simply be boxed away and not be reviewed or subject to scrutiny. Therefore, in drafting a new registration law, I included a requirement that the registration and annual financial reporting by registered charities be done electronically so that: (a) Hawaii’s registration process would be “paperless” and (b) source registration and financial data would be freely available to all to search and review via the Internet. In response to the three-part newspaper series in 2007, Hawaii’s Democratic Senate Caucus adopted the Attorney General’s registration bill as its own, it was passed and enacted effective January 1, 2009.

Hawaii’s Internet accessible charity registry\(^\text{19}\) provides all users with a searchable database of all registration statements filed by registered charities and the data can be searched in a variety of ways:

![Search for a Registered Charitable Organization](https://ag.ehawaii.gov/charity/search.html)

The registry allows any donor, regulators, and other persons to determine who controls the charity, how it solicits funds, how much it spends on program services, and fundraising, management and general expenses. Users of the registry can determine whether there are personal relationships among management and whether the organization has been subject to regulatory discipline, among other things:


\(^{19}\) [http://ag.ehawaii.gov/charity](http://ag.ehawaii.gov/charity)
A complete example of such a registration statement is included in Appendix E. In addition, Hawaii’s charity registry provides complete access to a registered charity’s IRS Form 990.

An electronic or Internet based registration process promotes far better compliance by the nonprofit sector than a paper-based registration process and yields more complete and accurate data. For example, online registration systems quickly reject and return incomplete registration forms. Electronic registration systems also result in less clerical and review time by agency staff and paper storage costs. It also allows regulators, or any person to quickly search for and retrieve a registered charity’s financial and operational data and well designed systems will “remember” a charity’s data and streamline registration renewals. At the time the original registration law was repealed in 1994, Hawaii had approximately 125 registered charities based on “paper” registration process. Today, there are over 2400 registered charities in Hawaii, the majority of which are domiciled on the mainland. The direct public availability of registration data to some extent forces un-registered charities to operate in the Sunshine—whether because their professional advisors suggest compliance, or because third parties report their non-registration status to the State. Such third parties could be charitable “competitors” or donors, stakeholders or board members themselves. Hawaii, however, was fortunate to paint on a “blank canvas” while other states with registration laws are somewhat wedded to paper based registration systems. Only Arizona, California, Colorado, Hawaii, Ohio, Tennessee, New Mexico, South Carolina, and Utah have Internet based registration systems and only Hawaii, Ohio, Colorado, and New Mexico mandate electronic registration.
Hawaii is in the process of implementing an online registration system for professional fundraisers, thus allowing direct public access to their registration forms, and financial reports which detail how much was raised, the percentage of proceeds the charity actually received and itemizing all other costs of charitable fundraising campaigns and contracts. Thus, it will be possible, for example, to examine how efficient a particular fundraiser was for all of its charity clients and to compare and contrast efficiencies of different professional fundraisers.

As stated above, Hawaii and those few states that provide direct access to a registered charity’s registration form and annual financial reports (IRS Form 990)—not just extracted or summary data from such submissions, allow donors, stakeholders, the media and others to view the activities of the registered charity under a microscope—this serves an important deterrence effect and builds donor confidence in wise giving.

Although 39 state have registration laws in some form or another, a 2012 survey of state charity regulators that includes Attorneys General, Secretaries of State, and Consumer Protection Offices shows that very few provide direct access to registration forms and financial reports. Only nine states provide direct access to registration forms, and one of them, Texas, only for law enforcement organizations. Thirty states provide public access only to extracted data from registration forms. Nine states provide Internet access to a registered charity’s Form 990 or annual financial report.

States charity regulators, even those that don’t register charities, could improve their transparency by making available to the public, via the Internet, information on the results of their investigations and enforcement actions, including cease and desist orders, judgments, appeals from registration suspensions or revocations, and injunctive orders, etc. The Hawaii Attorney General’s Office provides direct online access to administrative orders, judgments and other enforcement documents.

At present, only nine state charity regulatory agencies make such enforcement data available via the Internet. The public availability of such data not only has the “electric light” deterrent effect that Justice Brandeis described, but it also serves as an effective educational tool for the non-profit sector and charities to learn more about the types of cases and abuses State Attorneys General pursue and don’t pursue. I submit that it also promotes donor confidence because donors know that someone is policing the sector.

Beyond the Internet posting of enforcement action data, the Hawaii Attorney General’s office has also provided internet access to redacted “summaries” in situations where a charity agreed to implement remedial actions or reforms in response to inquiries or formal investigations.

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20 See www.multistatefiling.org

21 See Appendix F

22 Id. California, Colorado, Hawaii, New Mexico, New York, North Carolina, Texas, Utah and Washington.

23 Id. California, Colorado, Hawaii, Illinois, Massachusetts, New Mexico, New York, North Carolina, and Utah.

by the Hawaii Attorney General’s Office. Mississippi also posts such redacted summaries. My theory is that providing access to such redacted information protects the charitable organization (and more importantly its charitable purpose) from needless embarrassment, yet also providing the educational/deterrent effect discussed above.

III. CONCLUSION

Transparency plays an important role in the self-regulation of the charitable sector, however, both federal and state charity regulators should re-double their efforts at making their regulatory programs more accessible and transparent, leveraging the power of the Internet. States and the IRS could go farther in making source data available for public searches and examination. The IRS should seek to liberalize restrictions that needlessly interfere with a more efficient and robust system to detect and prevent malfeasance and protect charitable assets that are placed at risk. The regulation of charities and data about the sector could be more freely available on the IRS’s website. Shining Brandeis’ “electric light” on IRS and State regulatory data and enforcement activity could help charities better understand the regulatory environment and empower donors and funders to make better educated decisions, both of which assist to avoid fraudulent activity and help government agencies use its enforcement resources more wisely.
September 14, 2007

Mr. Ron Schultz  
Ms. Theresa Pattara  
Form 990 Redesign  
Internal Revenue Service  
Washington, DC  
Form990Revision@irs.gov

Re: National Association of State Charity Officials (“NASCO”) Comments

Dear Mr. Schultz and Ms. Pattara:

NASCO strongly supports the IRS’s efforts to redesign the Form 990 to meet not only its needs to enforce federal tax laws, but to serve the form’s many stakeholders, which include state regulators. The redesign recognizes that in the nearly thirty years since the form was last redesigned, the nonprofit sector has evolved. Exempt organizations are more frequently engaged in complex business-like activities and relationships with other entities. Advances in communications technology in the past twenty years have made it possible for nonprofits to widely expand the geographic area in which they conduct programs, make grants and solicit funds. NASCO supports IRS goals to improve transparency and compliance and to reduce the burden on filing organizations.

NASCO supports the concept of a core form, a summary page and schedules that will be filed by organizations as they apply to their activities.

Data collected on the Form 990 is vitally important to state officials charged with the responsibility to oversee charitable assets, charitable organizations and fundraising. As you know, NASCO has been formally collaborating with the IRS on the design of the Form 990 since 1981, when states agreed to accept the Form 990 for state registration and reporting purposes provided that information the states needed would be collected by the IRS.

Previously, a charity that solicited contributions on a national basis was required to complete dozens of unique financial reporting forms to comply with state regulations. The agreement by the states to accept the Form 990 as a standardized, multipurpose information return and financial reporting form was intended to ease the filing burden on nonprofits and improve the accuracy and reliability of exempt organization financial information filed with both state officials and the IRS. We believe that there has been success in meeting both objectives, but as always, we strive to continue to seek further improvements. NASCO has appreciated the IRS’ responsiveness to NASCO’s needs and we look forward to continuing this valuable relationship.
The governance questions will generate questions from nonprofits as to whether they are appropriate areas of inquiry for the IRS, as state officials traditionally pursue violations of fiduciary duty and failures in governance. If IRS engages in educational activities on “best practices” for charity directors and trustees, NASCO is willing to collaborate.

The proposed implementation date is ambitious, and will require many states to completely revamp their charities registration databases. This may pose significant challenges for some states.

Set forth below are NASCO’s comments on the draft redesign.

1. **Raising the Filing Threshold**

The IRS is considering raising the minimum filing threshold from $25,000 in annual revenue to $50,000. This recognizes that the current value of $25,000 is much less than it was in 1979. Of the 39 states that regulate charities and fundraising, nearly all maintain minimum registration and reporting thresholds of $25,000, and under. As an example, New Hampshire requires all charities, regardless of size or income, to register and report. California requires all charities that receive assets of any amount to register. South Carolina, Maine and Utah require charities to register without regard to a minimum. Alaska’s minimum is $5,000; Michigan’s is $8,000 for charities that solicit, and no minimum for charitable trusts. Virginia’s law currently provides that a charity that does not file a Form 990 must file an audited financial statement, if revenues are at least $25,000. Texas, which does not register charities at all, relies on Form 990 data obtained from public sources when it evaluates complaints against charities. New York, Minnesota and many other states have a $25,000 threshold by statute. Charities with revenues between $25,000 and $50,000 must register and file an annual report.

NASCO surveyed its membership on this question and asked whether there is support for the notion that the states should similarly raise the minimum threshold in tandem with the IRS. We find that no state statute specifically ties its threshold to that of the Form 990. In fact, many states require small charities that are not required to file the Form 990 with IRS complete the return and file it with the state.

NASCO members state that they believe that retention of the minimum thresholds is important because of the high incidence of mismanagement, self-dealing, misappropriation and waste of charitable assets at these lower asset levels, which most states are mandated to protect for the benefit of the public. While we do not have specific data on this issue, NASCO members state that a relatively high proportion of complaints they receive relate to the operations of smaller organizations.
We recognize that to achieve its goal to reduce burden, the IRS believes it may need to raise the threshold for the filing the Form 990. We note, however, that comments proposed by Independent Sector and others express concern about the lack of public information that will be lost about the tens of thousands of smaller organizations should this occur.

If the threshold must be raised, NASCO would prefer that the small organizations be required to file at least a short form of sorts. If NASCO members need to revert to a state-specific form for registration and reporting purposes, the uniformity we have gained through the Form 990 will be lost. NASCO stands willing to work with the IRS and others to achieve a compromise.

2. Core Form, Summary Page

NASCO supports the concept of a summary page that provides a snapshot of an organization’s identity, its size by income and assets, its purpose and program focus, and its governance structure. The states appreciate the addition of new data such as the state of legal domicile, and the year of formation. It could also be helpful to know the organization’s form (corporation, LLC, unincorporated association, trust) and whether it is a membership organization.

Many nonprofit charitable organizations have alternative identities. For instance, C.C.R.F. is known as Children’s Cancer Research Fund. American Lebanese Syrian Associated Charities is more widely known as St. Jude Children’s Research Hospital. A space for alternative corporate identities would be helpful.

Part I, Line 1. Substitute purpose for mission. The mission statement could be added to Part III, line 11 which asks how the organization makes certain documents and information available to the public.

Part I, Line 2. Provide additional space. Add program before the word activities, so that it states “list the organization’s three most significant program activities and the activity codes.”

Part I, Line 4. “Independent” must be adequately defined in the instructions and not merely in the glossary.

Part I, Line 6. Compensation threshold. This requires a listing of the number of individuals receiving compensation in excess of $100,000. Many NASCO members believe that the compensation disclosure threshold should be lower.

Part I, Lines 11-16. Line 12 should require reporting of contributions and grants from all sources, excluding government. Include a separate line for government grants.
Part I, Lines 25 & 26. Generally, NASCO is not convinced that it is necessary to include the Gaming and Fundraising data on the summary page so long as the detail is provided on a schedule. Gaming is a specific activity that bears little resemblance to other types of fundraising and placing these two activities together on the summary page is confusing.

Removing this from the summary page will free up space that can used for more information about programs and activities, and perhaps for certain expense information that could help to make the summary page a universal reporting form for small organizations.

NASCO encourages the IRS to add another line to Part I that requests the total number of volunteers. This is important information that is not captured elsewhere.

3. Summary Page Metrics, Part I, Lines 8b, 19b, 24b

We understand that the proposed inclusion of the percentage calculations on lines 8b, 19b, and 24b have prompted a fair amount of objection in comments received thus far. NASCO is sensitive to the notion that prominently featuring such percentages on the summary page connotes that these are important measures of a nonprofit organization’s performance and that one can use these formulas to draw meaningful comparisons between entities. The diversity of the nonprofit sector is such that often these comparisons are not meaningful when applied broadly.

Individuals who are using nonprofit data to evaluate an organization’s performance can choose which numbers to compare and perform the calculations as they see fit. A lender will consider certain ratios to be particularly relevant, while a potential funder may consider other financial indicators.

NASCO encourages the IRS to reconsider whether the ratios proposed in the draft are those that provide the most value to the public and are not likely to lead to misunderstanding or distortion.

In our experience, potential donors who contact state regulators for information want assurance that their contribution will be well-spent. They want to know to what degree their financial support will advance the nonprofit’s stated purposes. Prior year financial data can be helpful in demonstrating the proportion of the organization’s resources that were spent on program services and other expenses, both by function and object category. It may be relevant, for instance, to a donor if the program expenses are chiefly in salaries or in printing, postage and caging expenses. We routinely encourage donors to review at least summary data taken from the Form 990, and to consider that information against their own standards and values. Percentages can be helpful in that analysis. For those citizens who respond to direct mail and telemarketing
donation appeals, and who are making choices among dozens of requests for contributions, it may be especially helpful to compare the total of joint costs of conducting an educational and fundraising activity to total expense or to program service expense.

Thus, a ratio that in NASCO’s experience is valuable to readers of the Form 990 is the percentage of program service expense to total expense.

Part I, 8b. Asks that the total amount of money spent on program services be divided by compensation paid to officers, directors, trustees, and other key employees. The vast majority of charitable programs services are carried out by persons other than officers, directors, trustees and other key employees. NASCO doubts that this metric will provide meaningful information.

Part I, 19b. Asks that total fundraising expenses be divided by total contributions. This figure can be helpful to donors when the charity is reliant on one or two methods of raising funds. Most established entities generate revenue and contributions through a diversified approach, seeking both large and small contributions and grants. Newly established charities may experience high fundraising costs initially until the organization is able to secure a number of faithful donors. But for those charities that do not have multiple sources of revenue, this number may be of value to some donors.

Part I, 24b. Seeks to compare the total of current operating expenses to the organization’s fund balance. Generally, the individual who is evaluating this ratio is going to be able to do so without having the calculation performed by the reporting entity.

4. Part II, Compensation

The proposed reporting threshold for compensation disclosure is $100,000, up from $50,000. NASCO members generally believe that the current $50,000 threshold should be retained.

On line 1a instructions, it might be helpful to insert “in the aggregate” after reportable compensation.

NASCO concurs with Jack Siegel’s recommendation that individuals be listed in descending order (trustees and directors first, institutional trustees and directors, then officers, then employees). That would result in all individuals within one classification being grouped together.

NASCO prefers that the disclosure of the position title and number of hours devoted weekly to position be retained.
Because compensation for former employees who receive less than $100,000 in compensation does not need to be reported on this schedule, the form only reveals former employees paid in excess of $100,000. Column B is helpful because it permits all relevant individuals to be included in one comprehensive schedule.

NASCO has traditionally supported the disclosure of the city and state of residence of directors, trustees and officers. We recognize, however, that many organizations engaged in controversial programs, or which assist those in abusive relationships, have a strong interest in maintaining privacy to avoid harassment or threats. NASCO members concede that the safety of volunteer directors, trustees and officers from harm will occasionally override the need for public disclosure of the city and state of residence.

5. Part II, Section B

Entities that respond “yes” to lines 5a - 5e should be required to complete Schedule R and the Line 5f table should be moved to Schedule R. Rather than ask for a description of the transaction, there should be a list of categories to allow a check-off rather than a description, such as those that are currently captured on Form 990, Schedule A. You may wish to add “substantial contributor” to line 5 as well. Generally, NASCO prefers the business relationships definition that currently applies to Schedule A, Part III, Line 2.

Line 10a requires the listing of the top five independent contractors that received compensation of more than $100,000. The instructions clarify that professional fundraisers are to be excluded since they are to be listed on Schedule G. It could be helpful to mention it on the form.

6. Part III, Statements Regarding Governance

Steven T. Miller, Commissioner, Tax Exempt and Government Entities has engaged the tax-exempt sector regarding the appropriate role for the IRS with respect to governance. He has taken the stance that, at a minimum, the IRS should educate on basic standards and practices of good governance and accountability. The states concur with observations made by Senators Max Baucus and Charles Grassley that governance is at the core of every charity scandal. In addition to carrying out our registration and enforcement functions, NASCO members have been extensively involved in promoting accountability and proper stewardship of charitable assets. State offices have published and freely distributed truckloads of materials on fiduciary duties of directors, and through forums, meetings and telephone calls, we have had countless educational contacts with community leaders and nonprofit board members. As an organization, NASCO is committed to continuing these important activities and welcomes the educational nature of the inquiries on the redesigned form. With that said, however, it may be important for the IRS to continue to state its reasons for asking the governance-related questions and dispel any notion
that it intends to conduct enforcement activity solely based on responses. It would also be useful to note that the organization should refer to the applicable state law for specific legal requirements.

Independent Sector suggests that separating statutory compliance questions from “best practices” questions would help to make the distinction that certain questions are meant to be educational in nature. This suggestion is worthy of consideration.

The instructions should clarify that non-voting members are not to be included in the number of persons on the governing body. Some organizations list honorary trustees or directors on the IRS return. When prominent individuals are so listed, it gives a reader the misleading impression that these persons have an active role and vote in the management of an organization.

Question 75a of the current Form 990 asks how many officers, directors, and trustees can vote at board meetings. However, we do not see that question on the draft return. Because some organizations will list honorary, non-voting directors, this information is useful in determining if that is the case. In addition, an instruction for Part II should clarify that those non-voting, honorary directors should not be listed.

The checkboxes to question 8 ask if an independent accountant provided certain services. Since there is no opinion or other form of assurance provided by an accountant who prepares a compilation, this choice should be eliminated to avoid any misleading conclusions.

NASCO suggests that IRS consider adding a question to elicit whether the entity experienced theft and/or embezzlements during the year: Theft and embezzlement are often indicators of poor internal controls and/or lack of board oversight. Many entities currently report such losses in overall operating loss without explanation.

As stated above, the mission statement could be added to Part III, line 11, which asks how the organization makes certain documents and information available to the public.

7. Part IV, Revenue

Additional data regarding sources of contributions, such as aggregate amounts raised from individuals, foundations, and corporations, would be desirable and of interest to the public.

8. Part V, Statement of Functional Expense

For lines 1 and 2, request that the amounts of cash and non-cash grants be separately disclosed. Line 3 should include a reference to complete Schedule F.
Line 11 e. The Form calls for the amount of professional fundraising fees to be reported on Line 11e. The Instructions state that the organization should report not only the fee, but the amount of money paid for fundraising services, including payments for printing, paper, envelopes, postage, mailing list rental, etc. be included in professional fundraising fee. The fee portion of what an organization pays to a professional fundraiser should be separated from the amounts it pays to the fundraiser for other services, such as graphic design, printing, or postage. However, both pieces of information should be factored in for purposes of the Schedule G trigger. The dollar level of the trigger, as we state below, may be too low at $10,000.

The states ask that costs for printing, postage, and telephone costs be retained as object or natural expenses that can be allocated to the appropriate function. Line 13 combines supplies, telephone, postage and shipping, and printing and publications into “office expense.”

Line 12, Advertising. The instructions state that in-house fundraising costs and printing should be reported as advertising expense. This is confusing.

NASCO heartily endorses the 5% limitation for other expenses imposed by Line 23.

NASCO understands that the absence of the joint cost disclosure in the redesigned form is an oversight and will be included in the final draft. NASCO wishes to express its strong preference for this information. We request that the joint cost information currently required be added back into the redesigned form.

The overview leaves the impression that the joint cost disclosure would be replaced with the requirement that organizations exempt under section 501(c)(3) and 501(c)(4) follow AICPA SOP 98-2 in allocating joint costs of conducting a fundraising and educational activity. NASCO supports requiring all tax-exempt organizations that allocate joint costs to follow AICPA SOP 98-2.

It must be emphasized that these are two separate issues. Requiring organizations to follow SOP 98-2 is a welcome development that NASCO has long advocated. But it is not a substitute for the disclosure of the actual joint cost expense allocation. Without that, a reader of the Form 990 would not be aware that such allocations took place, and would not be aware of the effect of those allocations on the functional expense statement.

We agree with the movement of payments to affiliates to Part V, line 21 of the draft 990.

It is not clear if organizations holding both conservation land and conservation easements are required to fill out both Part V and Part VII. These parcels are “program related” so it would appear both parts must be completed by the conservation organization: Part V requires the cost
and book values of the conservation land while Part VII lists the easements only and does not require cost/book values. A clarification would be welcome in the form or in the instructions.

9. Part VI, Balance Sheet

Line 10 does not require a description/value of the investments on Schedule D. Some public charities have significant publicly-traded stock and bond holdings that are not being properly administered and which could jeopardize the financial health of the organization; this therefore becomes an important piece of information for regulators.

Part VII, line 16 refers to “assets in permanent endowments.” Part VI, lines 28, 29, and 30 of the core form 990 refer to SFAS 117. Schedule D, Part XII refers to “endowment funds.” Schedule D, Part XIII refers to reconciliation of Net Assets including unrestricted, temporarily, restricted, and permanently restricted assets. It seems there should be some cross-reference among these four elements since all four refer to “endowment” funds which are permanently restricted assets as defined by SFAS 117. Senators Grassley and Baucus specifically mention endowment funds in correspondence to Treasury. The new 990 should allow the reader to understand the value and size of permanently restricted funds held by a public charity.

10. Part VII, Statements Regarding General Activities

The instructions for lines 7 a-b, which serve as a trigger for Schedule R, need to be very clear. The definition of “control” is not consistent between the core form glossary and that for Schedule R. The core form refers to “tax-exempt” entities, while Schedule R refers to “nonprofit” entities.

The reference to “related organization” should be changed to related parties. The definition of related parties that appears in the 2006 Form 990 should be retained. The draft redesign definition is not as comprehensive and does not include a critical element, namely, person(s) who exercise substantial influence. The definition of substantial influence should also be retained from the 2006 instructions.

The form uses the term “permanent endowment.” In the glossary the term endowment, permanent is defined as, “Assets held subject to stipulations that they be invested to provide a permanent source of income.” A better definition (from the University of California) might be: “Endowment funds are funds to which the donor has stipulated that the fund principal shall remain inviolate and that only income be expended.” Public charities, unlike private foundations, often misunderstand what an “endowment fund” really is and tend to include unrestricted funds in their permanent investment funds. The definition should be very clear for purposes of the form 990 in order to reduce the confusion among public charities and to give an accurate accounting of “true endowment” funds.
Line 12 appears to promote the notion that an entity serving as a fiscal agent should have a written agreement to protect its tax-exempt status. NASCO agrees that written fiscal agency contracts are desirable and would help to minimize legal disputes that often arise between the sponsor and the sponsored organization regarding expenditure authority. Additional discussion of the objectives of this question should be added to the instructions.

11. **Part IX, Statement of Program Service Accomplishments**

The Statement of Program Service Accomplishments should be moved to the forward section of the core form, preferably the second page. The signature block can be appended to Part VIII, Statement Regarding Other IRS Filings.

12. **Schedule D**

NASCO recommends adding a section for publicly traded investments. The instructions for VI should encourage disclosure of all “other assets” and “other liabilities.” The instructions will need to provide a brief overview of FIN 48.

13. **Schedule G Fundraising and Gaming**

In our experience, entities that engage significantly in gaming are not likely to have the fundraising activity that would be reported on the proposed Schedule G. NASCO agrees that the fundraising and gaming activities are sufficiently distinct, particularly from the IRS’ tax enforcement perspective and the states’ fundraising regulatory posture to warrant separation of the disclosure and reporting functions.

The schedule trigger, at more than $10,000, on Part 4, line 11a (gross income from fundraising events) or Part 5, line 11e (professional fundraising expenses), is quite low. It would potentially encompass every school PTO carnival held in the United States. Perhaps a trigger of $25,000 should be considered.

Part I, Fundraising Activities. 1a. While it is helpful to know the method by which a charity solicits contributions from the public, it would be more relevant to know what proportion of revenues received were from each method. Other methods to be added to the description are door-to-door solicitations, electronic or print media solicitations, as well as a space for “other.”

For purposes of Schedule G, it would be more useful if the tax-exempt organization indicated only the fundraising activities for which it paid a fundraiser for services rendered.
Part I, Fundraising Activities 1b. This question asks if the organization had a written or oral agreement with any individual (including officers, directors, trustees, or key employees listed in Form 990, Part III) or organization in connection with these or other fundraising activities. If yes, they must be listed on the table, disclosing the name of the individual/organization, the type of activity, the gross receipts, amount paid to or retained by individual, and the amount paid to the organization.

First, reference to the insiders within the parentheses almost suggests that the main purpose in asking this question is to determine if those insiders are being paid to conduct fundraising activities. This notion is reinforced by question 2. Only after reading the question more than once, it becomes evident that the question is eliciting information about any contracts the tax-exempt organization has related to fundraising. Second, characterizing the contracted, compensated fundraiser as an “organization” is confusing. It would be preferable to refer to the fundraiser as an individual or third party or entity. A definition that closely resembles common state definitions for professional solicitor, fundraising counsel, or professional fundraiser should be considered.

NASCO asks that the address of the third party or entity be disclosed.

This request for disclosure is perhaps much broader than is necessary. Many states require that contracts between charities and professional fundraisers be filed or described. The states generally do not require contracts with graphic designers, lettershops, printers, entertainers and other vendors that provide services connected to the fundraising activity to be filed as part of the registration process. If the situation warrants, those contracts can be obtained by investigative requests.

It would be desirable to separate out the fee portion of the amount paid to an outside professional from the other amounts an organization pays to its vendor for related costs, such as printing, design, telemarketing services, or postage.

The wording of columns (iv) and (v) in the table, “amount paid to or retained by individual or organization listed in (a); and amount paid to organization,” raises the issue of custody and control of the contributions solicited from the public.

The information provided in response to Question 3 might be improved by a list of the states with which the organization is registered (or may be recognized as exempt from the requirement) and checkboxes for each state.

Only a few NASCO member states actively regulate gaming activities in addition to regulating charitable fundraising. Most states have a separate agency or division that enforces state laws governing bingo, pull tabs, raffles and other games of chance. NASCO received a few
comments from its members regarding the gaming section of this schedule. Instructions for Part III: The definition of gaming does not include Texas Hold ‘Em Poker or other card games which are rapidly replacing Bingo among the larger charities engaging in games of chance. Additional information may be required if an organization contracts with a third party for gaming revenue. Line 19b is not clear with respect to the amount of distributions required under state law that were distributed to other organizations. It is not clear if the actual amount distributed or the minimum required to be distributed is requested. Both amounts may be of value.

14. Schedule H, Hospitals

The data collected on the hospital schedule will be valuable to government, to healthcare policy-makers and to the broader public. We acknowledge the vigorous debate within the industry as to what should be included in community benefits. No matter what the final schedule looks like, the data obtained through its uniformity across the spectrum of tax-exempt hospitals will be an achievement.

New Hampshire and many other states have specific community benefits reporting laws for hospitals. Part I, sections 1-4 of Schedule H refers specifically to charity care activities. New Hampshire nonprofit hospitals are not required to provide charity care as part of their community benefits obligations and the Part I emphasis therefore has the potential to unfairly portray those hospitals that do provide community benefits listed under “other benefits” but do not provide charity care.

Defining actual hospital cost has been a challenge for every state seeking information on community benefits. The worksheets attempt to quantify the charges in a consistent manner, but there are a number of variables that make uniformity and cross-sector comparisons very difficult. For example, under Medicare, patients are sorted into DRGs or Diagnostically Related Groups that weigh several factors in determining the reimbursement rate paid to the hospital. Hospital A in New York City may charge more for a certain procedure than Hospital B in Concord, New Hampshire, but not receive a greater Medicare reimbursement even though the New York hospital’s labor and physical plant costs are legitimately higher. In addition to working with the Catholic Health Association, the IRS may also consider speaking with state regulators in those states with community benefits reporting requirements in order to understand the difficulty of valuing/quantifying the benefits provided by nonprofit hospitals. There is no opportunity for a hospital to report those community benefits that may be qualitative and impossible to quantify.

15. Schedule M, Noncash Contributions

NASCO shares the concern of the IRS that overvalued non-cash contributions on charity income and expense statements run the risk of distorting what is reported on the Form 990. Therefore, we welcome the addition of Schedule M.
Schedule M requirements may add an administrative burden for some charities that have not been properly accounting for donated items. However, NASCO believes that a long history of lax accounting for non-cash goods does not justify continuing the practice. A review of many comments filed with the IRS fails to acknowledge that the charity is valuing the items for purposes of reporting them as income. A possible solution to this dilemma would be to require charities that report “non-cash contributions” to keep these records. If they do not report them, then there may be no need for tracking. This would not be true for any item for which the organization provided a Form 1098 to the donor. Any organization providing a 1098 should be required to report and account for all such donations.

There is a need for more detailed instructions on what to report, how to report and record-keeping requirements for all items listed on Schedule M.

We encourage the IRS to also capture information on the donors of the non-cash goods and their disposition. We also believe that the schedule should include the disposition of non-cash donations received in a prior period.

For columns b and d it would be beneficial if there were a total amount listed after line 26. This will allow the reader to determine if all items listed on Schedule M have also been accounted for in Part IV (Revenue) and Part VI (Balance Sheet).

There are several suggestions that Schedule M should be eliminated and this information combined with Schedule B. However, Schedule B is not publicly disclosed and not required to be filed with most states. NASCO does not support combining Schedule M into Schedule B.

16. **Schedule N, Termination or Significant Disposition of Assets**

The information captured on Schedule N will be highly welcomed by state offices that oversee dissolutions and transfers of assets. NASCO applauds the IRS for the addition of Schedule N.

17. **Schedule R, Related Organizations**

The language and definitions between the core form and Schedule R need to be consistent and clear. The reference to “related organization” should be changed to related parties. The definition of related parties that appears in the 2006 Form 990 should be retained. The draft redesign definition is not as comprehensive and does not include a critical element, namely, person(s) who exercise substantial influence. The definition of substantial influence should also be retained from the 2006 instructions.
Part II, B, Line 5f should be moved to Schedule R. Rather than ask for a description of the transaction, there should be a list of categories to allow a check-off rather than a description, such as those that are currently captured on Schedule A.

Finally, a question has arisen as to the proper reporting of contributions or grants made to an organization that is acting as a fiscal agent. We understand that a grant made by a fiscal sponsorship arrangement is legally a gift to the exempt organization and it must retain control over its expenditure to the sponsored organization and not act merely as a pass through.

NASCO asks that the language currently in General Instruction E be retained. It helps to underscore our authority to question whether the form has been properly completed and submitted.

Where the instructions make reference to allocations between program, management and general and fundraising, the IRS should refrain from implying or stating that certain costs are always allocated to program.

Thank you for considering NASCO’s comments. Congratulations to the IRS team on engaging the sector so well through this period of comment and for moving this important project forward.

Very truly yours,

JODY WAHL
President, National Association of State Charity Officials

(651) 297-4607 (Voice)
(651) 296-7438 (Fax)
APPENDIX B
December 17, 2007

Via Express Mail and Email

Ms. Lois Lerner
Director, Exempt Organizations Division (T:EO:RA:T)
Internal Revenue Service
1750 Pennsylvania Avenue, NW, Room 6631
Washington, DC 20224

Dear Ms. Lerner:

The Board of Directors of the National Association of State Charity Officials (NASCO) strongly believes that the IRS' apparent intent to raise the filing threshold for the new IRS Form 990 to $1 million in gross income, phased down over three years to $250,000 is extremely unwise. We wanted to take the opportunity to explain NASCO's position on this issue.

1. The IRS' apparent decision seems directly at odds with the national sentiment to require charities to report more, not less information, and to become more, not less transparent. Even the IRS' own discussion draft of good governance practices recommends full transparency. One only need read the Wall Street Journal (WSJ) special report December 10th and the scores of other recent articles in national publications to divine national sentiment. The 2006 study quoted in the WSJ article shows that 71% of those surveyed believed that charities waste a

"We very much appreciate you sharing the IRS apparent intentions in a phone call to me in my capacity as NASCO President. This information remains solely within the board's knowledge at this time. "By making full and accurate information about its mission, activities, and finances publicly available, a charity demonstrates transparency."
great deal or a fair amount of their money.

Likewise a 2006 Harris Poll found:

One-third of U.S. adults (32%) have less than positive feelings toward America's charitable organizations and the same number (32%) thinks that the nonprofit sector in America has pretty seriously gotten off in the wrong direction, according to a survey by Harris Interactive. While a majority of adults may have positive feelings toward nonprofits (68% give them a score of 51 or higher out of 100) and most (92%) households have contributed to a charity in the last year (up from 80% in October 2005), only one in 10 (10%) strongly agrees that charitable organizations are honest and ethical in their use of donated funds. Almost half (48%) somewhat agrees with this sentiment, while slightly more than one-quarter (27%) somewhat or strongly disagrees that these organizations use donated funds honestly and ethically, and another 15 percent are not sure.

2. As your partner in the regulation of charities, we understand that the IRS is getting "push back" from the nonprofit sector. NASCO believes that the WJ article said it best:

"I think we get irrational pushback from nonprofits who say, 'You can't measure mission-centered work,' " says Brian Gallagher, chief executive of United Way of America and chairman of Independent Sector, a coalition of charity and philanthropy leaders. "You must certainly can. The question is, 'Are you committed to do it?' And then, 'Are you committed to report on it?'" 

Without such information, says philanthropist Gerald Greenwald, the retired chairman of United Airlines, "those that are really succeeding don't get the applause and money they should, and those that aren't doing very well seem to just live on forever."

3. The United States House of Representatives, Committee on Oversight and Government Reform, held a hearing on December 13, 2007. Even though the stated purpose of the hearing was an assessment of veterans' charities via their expenditures on fundraising, it became apparent during the hearing that the Committee was concerned, in general, with disclosure issues affecting the sector. In addition, the U.S. Senate Finance Committee has expressed concern about disclosure issues. Clearly, we should be focused on requiring more disclosure, not less.

4. Many state charity officials may have to require or will require charities below the $1 million threshold to file the new 990 form anyway because state law requires it. For example, Michigan approximates that 95 percent of charities will not be required to file the Form 990 and it will have to impose additional filing requirements on these charities.

5. The IRS' apparent intention will have vast consequences to those 11 or so states that do not register charities at all, where the 990 form is the only public and regulatory "window" into the charitable organization. Using Hawaii as an example, there are 8,200 true charities\(^1\) and only 1,825 file 990 forms at present. Approximately 1,700 of these organizations have income below $1 million meaning that 93 percent of Hawaii reporting charities would file a 990-F. This is not sufficient to allow state regulatory or public accountability.\(^2\)

6. In some states, charities register but do not file the Form 990, instead filing much briefer state financial forms on the premise that more detailed information is available on the Form 990, which can usually be found on Guidestar. If the number of Forms 990 available on Guidestar were to drop significantly, then indeed the state filing burden on charities could increase substantially, since charities under the IRS threshold would then be forced to file a Form 990 with the state (even if it was not required by the IRS) or file a dramatically longer state financial form.

\(^1\)http://nccsdataweb.urban.org/NCCS/Public/index.php
\(^2\)http://nccsdataweb.urban.org/NCCS/Public/index.php. I admit that a small number of the 1,700 may be private foundations.
7. These new filing thresholds could adversely affect the cost-benefit analysis for states considering plugging into the IRS state retrieval system, which was seen at one time as a promising vehicle for promoting e-filing on the state level and developing tax software that would ease the filing burden on charities that register in more than one state.

8. The IRS has proposed a core form with various schedules completed only by those to whom they apply, so it is already geared to having a 990 form in various forms rather than just 990 and 990EZ. Why doesn't the IRS have smaller filers submit the core form with the information currently collected on Schedule A?

9. IRS statistics indicate that it examines less than 2,400 990 forms. As a result, the IRS must necessarily rely on state charity officials to serve on the frontline "trenches" of charity oversight and enforcement. The Form 990 is one of the most significant tools that state charity officials use to identify the misuse of funds or malfeasance. According to most recently available statistics, sixty-two percent of State referrals to the Exempt Organizations' Division resulted in significant corrective actions being taken, including revocation of exempt status. If you expect us to be your "eyes and ears" we cannot do this job blindfolded and with ear plugs in.

10. Most importantly, widespread use of the new Form 990 will increase donor confidence in charities and which will in turn promote philanthropy. According to Independent Sector, there has been a substantial drop in charitable giving due to a public loss of confidence in the nonprofit sector. Charitable giving per organization fell from $382,000 in 1982 to $277,000 in 2006.

Rather than having charities under the expected new threshold file a 990EZ, several member states of NASCO have expressed the view that the IRS should simply require those charities to continue to file the old form which provides more information, rather than a form that provides substantially less. Those charities should be able to file the form they have been filing all along, without implementing any new record keeping or accounting procedures.
We hope the IRS reconsiders what we believe is an ill-advised decision that is not in the best interests of the Nation's charities, their donors, those they serve, and state charity regulators, nor even the IRS.

Thank you for considering our view.

Very truly yours,

HUGH A. JONES
President, NASCO
APPENDIX C
October 28, 2011

The Honorable Max Baucus  The Honorable Orrin Hatch
Chairman  Ranking Member
Committee on Finance  Committee on Finance
United States Senate  United States Senate

via fax

Dear Chairman Baucus and Ranking Member Hatch:

Re: Pension Protection Act of 2006 Provisions Regarding Information Sharing Between the Internal Revenue Service (IRS) and State Charity Regulators (Attorneys General)

I. INTRODUCTION
We write to express our collective desire that Congress amend the provisions of sections 6103, 6104 and 7213 of the Internal Revenue Code (IRC). This request is intended to enhance the effectiveness of state charity regulators as well as the IRS by enabling state regulators to more freely use information shared by the IRS.

II. BACKGROUND INFORMATION
State attorneys general typically have both common law and statutory oversight responsibilities over the charitable assets administered in their respective states including, but not limited to, testamentary and inter vivos trusts and foundations, individual and corporate fiduciaries, unincorporated associations, nonprofit corporations and their professional fundraisers and fundraising consultants. See Ex. A. There is a continuum of common law and statutory authorities that provide state attorneys general with broad regulatory responsibilities over the charitable sector. Indeed, the common law authority vesting state attorneys general with these oversight authorities dates back to the Statute of Charitable Uses in 1601, predating by centuries our own federal tax code. Similarly, secretaries of state and state charity officials in other agencies responsible for consumer protection, licensing, or securities oversight in their respective states are vested with statutory authority over the activities of charitable organizations and their professional fundraising consultants and solicitors.

1 See STATE ATTORNEYS GENERAL POWERS AND RESPONSIBILITIES (Emily Myers & Lynne Ross, eds., 2007).
Although the specific functions of the IRS and state charity officials are distinct, they share a number of important objectives. While the IRS accomplishes its mission through the enforcement of our federal tax laws and state attorneys general apply state trust, nonprofit corporation, consumer protection, and charitable solicitations laws, the goals of these state and federal regulatory schemes often intersect—both state and federal regulators have material concerns about ensuring against excess compensation, private inurement, waste, fraud, conflicts of interest and other abusive practices. Despite these shared interests, however, a variety of constraints discussed more fully below on the IRS’s ability to share “tax return information” with state charity officials frustrate the synergies that would otherwise enhance the effectiveness of the limited enforcement resources available at both the state and federal levels.

It is commonly known that the IRS audits or examines less than one-half of one percent of all charitable organizations exempt under section 501(c)(3) of the Internal Revenue Code. It is also widely accepted that the IRS suffers limited resources to police the sector, in which, according to the National Center for Charitable Statistics, there are 1,127,287 tax exempt 501(c)(3) charities and private foundations administering over $2,495,197,897,281 in charitable assets. Although federal law requires such organizations to make their informational returns (IRS Forms 990, 990EZ or 990 PF) available for public inspection and to state charity officials upon request, prior to the Pension Protection Act of 2006, the IRS was precluded from sharing any other tax return information with state charity officials, including any instances in which the IRS may have discovered or received information or complaints concerning violations of state law. Widespread public access to the income, expenses and governance information of the charitable sector already allows the public and state charity officials to be the “eyes and ears” of the IRS by reporting abuses. In truth, the 50 state attorneys general and other state charity officials are on the “front lines” in regulating charities and annually refer many significant cases of abusive practices to the IRS Exempt Organizations Division.

The National Association of State Charity Officials (“NASCO”), which is affiliated with the National Association of Attorneys General (“NAAG”), has long advocated liberalizing the provisions of IRC §§ 6103 and 6104 to allow the IRS to freely share what is considered protected “tax return information” relating to charitable organizations. Such information-sharing would allow state attorneys general and other state charity officials to pursue cases that the IRS may lack the resources or authority to undertake, including the diversion of charitable assets by organizations in their respective jurisdictions where charitable assets are required to be deployed for the benefit of the public-at-large. In June 2004, NASCO testified to this effect before the Senate Finance Committee. See http://finance.senate.gov/imo/media/doc/062204mptest.pdf

III. THE PENSION PROTECTION ACT OF 2006

The Pension Protection Act of 2006 (the “Act”) was intended to respond to the circumstances described above and allowed the IRS to unilaterally share tax return information with state charity officials and share other such information upon request. Regrettably, section 1224(b)(5) and (6) amended IRC §7213(a)(2) to make it a criminal offense for any state official to disclose

2 Federal treasury regulations also require private foundations to provide their IRS Forms 990PF to state attorneys general in their state of domicile or registration.
information shared by the IRS under IRC §6104(c)(2). Despite the good faith efforts of the IRS Exempt Organizations Division to implement these amendments, what was intended to facilitate the rigorous oversight of the charitable sector by state charity officials has failed to achieve its intended purpose.

IV. EXPLANATION OF THE PROBLEM

As a result of the Act subjecting information sharing between the IRS and state charity officials to IRC §7213’s criminal penalties, the IRS has had to subject state charity officials, including state attorneys general, to the same informational safeguards imposed on the tax and revenue agencies of the 50 states. A copy of the 106-page IRS Publication No. 1075 that describes the multitude of safeguard procedures to which state charity officials must adhere may be found at the following URL: http://www.irs.gov/pub/irs-pdf/p1075.pdf.

These procedures not only create the ethical and legal conflicts described below, they are simply unworkable given the limited resources of state charity officials and should not apply to information regarding the revenue, expenses and governance data of charitable organizations already required to publicly report their financial and operational data. The IRS’s understandable safeguards for the protection of confidential federal income tax information should be inapplicable. These safeguards, for example, do not permit state charity officials to enter any shared data through a word processing program on any networked computer for inclusion in a civil complaint without complying with a myriad of security requirements that state charity officials do not have the resources to implement. Consequently, despite years of diligent efforts by state attorneys general to obtain information from the IRS, only three state Attorney General offices—New York, California and Hawaii—have entered into information-sharing agreements with the IRS since the adoption of the Act nearly five years ago.

Even the three states that have entered into information-sharing agreements have had to construct an uncomfortable “fiction” to use the data:

1. When the IRS makes a disclosure to the state charity office, an official reviews the data, logs the receipt of the information, and must place the data in a file secured by at least two barriers (doors, cabinets, etc).

2. In order to take investigatory or enforcement action, however, the state charity official must then rely upon an independent source, such as a telephone directory or advertisement, as the ostensible basis for contacting the subject charitable organization and requesting any recent communication to or from the IRS. Following this sort of procedure does not violate the safeguard provisions at issue because

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4 State attorneys general acknowledge and commend the IRS’s earnest efforts to administer these changes, educate state charity officials about the new requirements and make information sharing a reality. The IRS and state charity officials continue to enjoy an open dialogue about ways to improve charitable oversight. The comments expressed herein are in no way intended to criticize the IRS’s implementation of the Act. The failure of this experiment is not the IRS’s doing.

5 Other than on unrelated business income, charities are exempt from income tax under IRC § 501(c)(3).
information provided directly by the charitable organization is not subject to IRC §§ 6103, 6104 and 7213.

3. If asked, a state charity official is prohibited from disclosing that the inquiry was premised on the information received from the IRS and must hope that the organization voluntarily produces all relevant information and, if not, issue a subpoena for the information.

In addition to the above, the rules of discovery are generally very broad and require disclosure of the tax return information in many, if not most, state jurisdictions. Although discovery rules are only applicable whenever civil or criminal proceedings are instituted, the fact that such disclosure may be required warrants careful consideration about the propriety of states withholding section 6104 tax return information and/or the fact of an IRS referral. The requirement that states must withhold disclosure of section 6104 tax return information will be especially sensitive whenever that information has prompted the state's inquiry. Most well-represented defendants demand to know all of the details underlying a state's enforcement action and are quick to exploit any suggestion of selective prosecution or prejudice due to a lack of candor concerning the identity, timing, or source of a complaint or the basis for the commencement of the action. Although state attorneys general are permitted to disclose and utilize section 6104 tax return information in judicial and administrative proceedings, discovery often occurs well in advance of such proceedings and the prejudicial effect of withholding such information from defendants until the time of trial is likely to risk court-imposed sanctions prohibiting the use of the information. From a practical standpoint, the discovery process will also result in the disclosure of information to third parties beyond the state's control (witnesses, court reporters, etc.).

Moreover, the security requirements create problems even when the shared information is not used to pursue an investigation or enforcement action. Some states have record retention laws that govern the return or destruction of state records which are likely to conflict with the provisions of section 6103(p)(4). Many states have their own versions of the federal Freedom of Information Act (FOIA) which may be sufficiently broad in scope to encompass the shared section 6104 return information. To the extent that return information under section 6104 is included within the scope of such statutes, states may be obliged to produce the information when requested.

In light of all of the above, states receiving section 6104 tax return information that cannot be used more straightforwardly are confronted with both ethical and legal dilemmas.

We see no reason why IRC notices of refusals to grant tax-exempt status, proposed revocations of exempt status, or proposed deficiency taxes for prohibited transactions under chapters 41 or 42, such as intermediate sanctions, taxes on self-dealing transactions and similar matters involving public charities and foundations, should be subject to the same criminal penalties and security procedures applicable to individual and corporate income tax return information. This is all extremely valuable and important information that allows state charity officials to fulfill their statutory mandate. The safeguard requirements have proven unsuccessful and unworkable,
however, and even the three states that have attempted to “play by the rules” feel as if the information obtained directly from the affected charity is akin to fruit of a poison tree.\(^6\)

As officials that represent state revenue and taxation agencies, we fully appreciate the fundamental public policy reason for the protection of confidential taxpayer return information—to encourage taxpayers to freely and voluntarily report their income and pay their fair share of taxes. Similar considerations should not apply to organizations that are exempt from income tax, that operate with the public subsidy of tax-exempt status, and who must already publicly report their income, expenses, governance data, disqualified person transactions, excess benefit transactions, changes in exempt purpose and governing documents, embezzlements and losses of funds, etc.—information that is then publicly available online at [http://www2.guidestar.org](http://www2.guidestar.org).

We urge Congress to remedy this situation by amending the federal laws to allow state attorneys general and other state charity officials to more freely obtain and use information possessed by the IRS to protect and promote the public interest we all share – that is, to ensure that charitable assets are lawfully administered at all levels of government.

Sincerely,

John W. Suthers  
Colorado Attorney General

Luther Strange  
Alabama Attorney General

Tom Horne  
Arizona Attorney General

Kamala Harris  
California Attorney General

Joseph R. “Beau” Biden III  
Delaware Attorney General

Lawrence Wasden  
Idaho Attorney General

David Louie  
Hawaii Attorney General

John J. Burns  
Alaska Attorney General

Dustin McDaniel  
Arkansas Attorney General

George Jepsen  
Connecticut Attorney General

Lenny Rapadas  
Guam Attorney General

Lisa Madigan  
Illinois Attorney General

\(^6\) Recently proposed IRS regulations (IRS REG-140108-08) will not address any of the substantive issues presented.
Tom Miller
Iowa Attorney General

Jack Conway
Kentucky Attorney General

Douglas F. Gansler
Maryland Attorney General

Derek Schmidt
Kansas Attorney General

William J. Schneider
Maine Attorney General

Martha Coakley
Massachusetts Attorney General

Lori Swanson
Minnesota Attorney General

Chris Koster
Missouri Attorney General

Jon Bruning
Nebraska Attorney General

Michael Delaney
New Hampshire Attorney General

Gary King
New Mexico Attorney General

Roy Cooper
North Carolina Attorney General

Mike Dewine
Ohio Attorney General

Linda L. Kelly
Pennsylvania Attorney General
*No Signature Available*
Guillermo Somoza-Colombani
Puerto Rico Attorney General

Marty J. Jackley
South Dakota Attorney General

Mark Shurtleff
Utah Attorney General

Rob McKenna
Washington Attorney General

Greg Phillips
Wyoming Attorney General

Alan Wilson
South Carolina Attorney General

Robert E. Cooper, JR.
Tennessee Attorney General

William H. Sorrell
Vermont Attorney General

Darrell V. McGraw, JR.
West Virginia Attorney General
Hawaii's rules lax on oversight of charities

Video: Dwight Kealoha talks about what to look for in a charity

• Knowing where every penny goes every day StoryChat: Comment on this story

By Rob Perez
Advertiser Staff Writer

Alphabetland Preschool & Kindergarten, a Waipahu charity, drew investigation from the state because of irregularities such as a $264,000 salary to one official and a loan to another – a husband and wife who were also its only board members.

ANDREW SHIMABUKU | The Honolulu Advertiser

Today
Charities in Isles get scant state scrutiny

Tomorrow
The fate of legislation

Tuesday
Mining the phone lines of charity call centers

Wednesday
Models for oversight of charities
HOW ARE YOUR DONATIONS USED? WAYS TO FIND OUT

Do you know how much of your charitable donation goes to the actual good deeds the charity is supposed to perform? Or how much the top executive of your favorite charity is paid? Or what that charity spends on overhead? Find out through our custom-built searchable database of more than 650 Hawai‘i charities, with information gleaned from the charities’ tax forms through http://www.guidestar.org/.

HonoluluAdvertiser.com/fyi

John Flanagan

Kelvin Taketa

Hugh Jones is the deputy attorney general assigned to keep watch on Hawai‘i's charity sector — along with his other duties in the department. He's the only official assigned even part-
Hawai'i is one of only 11 states that do not require charities to register, a gap that allows thousands of local nonprofits to raise millions of dollars from the public with virtually no regular oversight from regulators.

The lack of a registration requirement, considered the foundation of an effective monitoring system by many national experts, means charities can collect donations from residents without anyone from the state making even cursory checks to see how that money generally is spent.

"Charities aren't getting much oversight in Hawai'i," said Peter Swords, who has taught nonprofit law at Columbia University in New York for about 30 years. "With nobody looking at you, it means people can abuse the charity system. It's as simple as that."

Although the vast majority of Hawai'i's 5,000 public charities follow the rules and have financial safeguards in place, some organizations invariably stray from their tax-exempt missions — usually without drawing any scrutiny from the state.

Without a registration system that provides for annual reviews, regulators typically intervene only if someone complains or the questionable conduct is flagged some other way.

Take the case of Alphabetland Preschool & Kindergarten, a family-run, Waipahu-based charity that has an average monthly enrollment of 300 students and annual revenue of roughly $2 million, according to its tax returns.

For three consecutive years, starting in 2002, the Waipahu nonprofit paid one of its top executives more than $250,000 annually, far more than what officials earn at education institutions much larger in size. At KCAA Preschools of Hawai'i, a nonprofit that had double the enrollment and revenue as Alphabetland during that same period, its top executive earned less than $75,000 a year.

Over roughly that same period, Alphabetland also loaned more than $100,000 to another officer of the charity — the husband of the top-paid one — while he earned a salary of up to $120,000. Hawai'i law prohibits nonprofits from loaning money to their officers and directors. The husband served in both roles.

The wife's pay, which raised questions of excessive compensation, and the husband's loan were duly noted on Alphabetland's federal tax returns from 2001 to 2004.

But because Hawai'i has no registration system, which usually includes the filing of a charity's tax return, the Alphabetland transactions went unnoticed by state regulators — until one of them read a national story about questionable loans to nonprofit officials. The story had a brief Hawai'i reference, eventually leading the state attorney general's office to the Waipahu charity.

Authorities found more red flags once they started digging.

They learned, for instance, that the tax-exempt organization had paid its husband-and-wife management team, Gary and Amy Arizala, about $1 million from 2000 to 2003 (Gary Arizala died in 2004) and that the nonprofit was leasing two luxury cars, a Jaguar and Volvo, for $1,200 a month.

They also could see from the tax returns that the Arizalas were listed as Alphabetland's only board members during the period the husband was borrowing money and the wife's annual salary peaked at $264,000. The couple's daughter was added as a third board member in 2004, the returns show.
Such an arrangement runs afoul of standards that watchdog groups such as the Better Business Bureau recommend for governance of charities, including having a board that is independent, free of self-dealing and has at least five members.

Alphabetland declined comment except to say it was in discussions with the AG's office, has not admitted any liability and cautioned against jumping to conclusions about the issues raised by the state.

"We are confident that the matter should be resolved in the not-too-distant future to everyone's mutual satisfaction," the charity said in a June statement.

The AG's office declined comment because the case is still pending.

CRIMES AND MISDEEDS

The issue of charitable oversight has taken on greater significance in Hawai'i because of some relatively recent high-profile cases of misconduct or alleged misconduct. Among the cases:

- A Salvation Army official on O'ahu was fired last year after he stole more than $300,000 in money and property that elderly donors had intended to give to the charity. It was later disclosed that the official had been hired by the organization even though he had a previous conviction in Colorado for bilking an elderly couple. The man pleaded guilty to theft, forgery and other charges last week in connection with the Salvation Army case.
- A soccer league volunteer was sentenced to five years of probation last year for stealing more than $40,000 from her O'ahu nonprofit group.
- A former politician was accused in 2005 of improperly transferring $130,000 in campaign funds to a Waipahu charity he headed. The matter was referred to the AG's office for a criminal investigation.

Those cases and other publicized ones delivered some damaging public-relations blows to Hawai'i's industry, raising questions about whether the state and charities themselves have sufficient safeguards in place to protect against abuse.

The federal government grants tax-exempt status to charities, but it does so few audits — far less than 1 percent of all nonprofits nationally — that oversight has fallen largely to the states. The Internal Revenue Service did not have statistics on audits of Hawai'i nonprofits.

The quality of charity monitoring varies considerably from state to state, with some jurisdictions devoting entire divisions to it. Pennsylvania, for instance, has about 30 people, including attorneys and support staff, in its charitable trusts and organizations section. Oregon has nearly 20.

In Hawai'i, the AG's office, which is responsible for charity oversight, doesn't have even one full-time deputy assigned exclusively to that task.

That dearth of resources was reflected in a December 2004 survey by the National Association of State Charity Officials. Of the 30 states that responded, every one had more budgeted positions — from clerks to attorneys — dedicated to charity oversight and enforcement than Hawai'i, which at the time had none. Today, it has one.

"Oversight (around the country) generally is pretty lax," said Burnis Morris, a Marshall University journalism professor who specializes in nonprofit issues. "But at least some oversight is better than none."

Proponents say registration systems provide states with valuable information on what groups are out there collecting money, what they're collecting it for, how they're spending it in a broad sense and other aspects of a
charity’s operations. The information can help enforcement officials spot red flags, such as questionable transactions or compensation deals, and answer questions from the public.

Having regulators review annual filings also can serve as deterrents to abuse and is designed to give donors confidence that someone independent of the organization is watching to protect their interests.

National experts say Hawai‘i’s lax system, one of the weakest in the nation, is worrisome.

"I can’t think of another state that has less of a commitment to regulating charities and protecting the interests of donors," said Trent Stamp, president of Charity Navigator, a watchdog group based in New Jersey.

"It really sounds like a wild west atmosphere," said Daniel Borochoff, president of the American Institute of Philanthropy in Chicago.

**IN-HOUSE WATCHDOGS**

Industry officials, however, say Hawai‘i nonprofits generally have done a good job of protecting donor interests, spending money efficiently and keeping misconduct at bay.

"I’m not aware of any wholesale abuses," said John Flanagan, chief executive of the Hawai‘i Alliance of Nonprofit Organizations. "I think Hawai‘i nonprofits have a pretty good track record."

The board of directors of each organization provides some outside oversight, many charities hire outside accountants to review their books, and nonprofits that receive funding from government agencies and private foundations have to file reports accounting for how those dollars are spent, according to charity executives.

"The nonprofit sector here is subject to much greater scrutiny than any (government) agency," said Nanci Kreidman, executive director of the Domestic Violence Clearinghouse.

Adding to that dynamic, the tight-knit nature of the industry in an island community means word quickly spreads when a charity strays from its mission, so nonprofits go to great lengths to protect their integrity and the trust of donors, the executives say.

"Reputation is what they live by," said Kelvin Taketa, president of the Hawai‘i Community Foundation.

Taketa and other executives agree that the AG’s office doesn’t get nearly enough funding to provide oversight under the existing system, let alone under any expanded one. They particularly laud Hugh Jones, the deputy AG who provides the bulk of that oversight, including maintaining the office’s Web site on charity fundraisers. Jones, however, also has other, non-charity-related duties. The main responsibility of the tax division he heads is to provide representation to the state Department of Taxation.

"Hugh does a terrific job," Taketa said of Jones’ nonprofit duties. "But frankly we need four Hughs, not just one."

Guarding against abuse is critical to the industry because charities rely on public support, and donors will be reluctant to give if they don’t trust that their money will be used wisely.

The stakes are considerable.

Hawai‘i residents give hundreds of millions of dollars annually to philanthropic causes. In 2001, the most recent year for which statistics were available, local residents donated about $430 million in goods and money
to Hawai‘i and national charities, according to a 2002 study commissioned by the Hawai‘i Community Foundation.

The funds that go to local nonprofits help support a sizeable chunk of the state economy. Hawai‘i’s 5,000 charities control more than $12 billion in assets. Another 500 private foundations, formed by companies or wealthy families to help fund charitable services, control $1.2 billion in assets.

All told, these nonprofit organizations generate more than $2 billion in revenue, employ more than 41,000 people and pay wages topping $1 billion.

Given such weighty numbers, even if a tiny fraction of charities stray from their missions and divert assets for non-charitable purposes, the impact can be significant, according to regulators.

NO REGISTRATION SYSTEM

That was among the arguments the AG’s office made several years ago when it attempted to get a registration system resurrected in Hawai‘i. Registrations were required here until legislators repealed the law in the mid-’90s. But lawmakers were unwilling to support a new statute that the AG’s office proposed in 2001 and 2002.

While Hawai‘i has a strong law regulating paid solicitors for charities and another statute allowing the state to remove directors for fraud or gross abuse, Jones said a registration system would provide valuable information that would help the public separate the good charities — the vast majority — from the bad and enable the AG’s office to better monitor the industry.

One of the big drawbacks of not having an effective system is that consumers have no single place to turn to for comprehensive, timely information about charities seeking donations. Would-be donors, for example, can’t check to see if an organization that they’re unfamiliar with and that is asking for donations is a legitimate charity registered with the state. They also can’t see if the organization has provided the state with information on its finances.

Some watchdog groups, such as the Better Business Bureau (http://www.give.org/) or Charity Navigator (www.charitynavigator.org), provide online evaluations of certain charities, but the offerings tend to be limited or the participation of charities is voluntary.

A charity’s federal tax returns, called 990s, also are available online (http://www.guidestar.org/), but regulators and others often lament that the returns can be untimely, inaccurate or incomplete. Nonprofits with income of $25,000 or less and most faith-based groups are not required to file 990s.

TAX DEDUCTIONS AT RISK

Without a registration system, local donors who contributed more than $74,000 in 2006 and early 2007 to the Music Foundation of Hawai‘i likely wouldn’t have known that the charity was involuntarily dissolved by the state Department of Commerce and Consumer Affairs in 2004 and not re-incorporated until January 2007.

That meant the donors' contributions during that period were not tax-deductible, according to the AG’s office.

Under a typical registration system, a significant change in status — such as an involuntary dissolution — would have to be reported to the state AG's office, and that information likely would have been added to what was publicly available about the charity.
The Hawai'i AG's office came across the music foundation case only because the charity's paid fundraiser, Hawai'i Promotions, was required to register with the state under the charitable solicitations law. All paid solicitors fall under that law.

Hawai'i Promotions' license was suspended in May for 90 days, partly for providing misleading information to foundation donors, according to the AG's office. The company didn't contest the suspension and paid a $3,000 fine.

In providing receipts to the donors, Hawai'i Promotions included its federal tax identification number and a "Keep this portion for your records" statement, implying that donations were tax-deductible, Jones said in a May letter to the fundraiser.

But even though the foundation had formally incorporated again, its previous tax-exempt status didn't apply to the new organization, meaning donations in 2006 and 2007 were not tax-deductible, Jones said in the letter.

Johnny Kai, the foundation's executive director, denied that the charity or the fundraiser was attempting to mislead anyone.

The foundation was involuntarily dissolved because of a technicality that Kai wasn't even aware of until the AG's office sent him a notice, according to Kai.

He also said the IRS recently told him the foundation's tax-exempt status still was good — the IRS Web site indicates as much — but the agency recommended that the charity reapply anyway because of the state's contention. Kai has done that.

"It was all innocent," he said. "We weren't trying to fool anybody."

The need to oversee charities is not just limited to the smaller, less obscure ones, analysts say.

High-profile, more mainstream organizations also can slip up, sometimes unknowingly.

That apparently was the case when the Honolulu Academy of Arts, as part of a compensation package to its newly hired president and director in 2003, loaned Stephen Little money to help him with a home purchase.

When the charity's board learned the following year about the AG's position on such lending practices, it immediately addressed the issue; the board and Little decided that he would step down as an officer of the academy but maintain his position as chief administrator.

"This was done to comply with the law and to prevent either a conflict (of) interest or the perception of a conflict of interest," Little said in an e-mail.

He repaid the loan in full in 2005.

Although the academy mentioned the loan on its tax returns the past several years, the AG's office wasn't aware of it until last week — when The Advertiser called to inquire about it.

Reach Rob Perez at rlperez@honoluluadvertiser.com.
Unified Registration Statement (URS) for Charitable Organizations® (v. 3.01)

☑ Initial registration  ☐ Renewal/Update

08/31/2007

This URS covers the reporting year which ended (day/month/year)

Filer EIN 99-0220777

State HI

1. Organization’s legal name

MAKE A WISH HAWAII INC

If changed since prior filings, previous name used ______________________________________________________

All other name(s) used Make-A-Wish Foundation of Hawaii

2.(A) Street address 745 Fort St. Suite 315

City Honolulu

State HI

County Honolulu

Zip Code 96813

(B) Mailing address (if different)

City Honolulu

State HI

County Honolulu

Zip Code 96805

3. Telephone number(s) (808) 537-3118

Fax number(s) (808) 536-5566

E-mail makeawish001@hawaii.rr.com

Web site www.makeawishhawaii.org

4. Names, addresses (street & P.O.), telephone numbers of other offices/chapters/branches/affiliates (attach list).

5. Date incorporated _______________________________ State of incorporation ________________________________

Fiscal year end: day/month ________________

6. If not incorporated, type of organization, state, and date established __________________________________________

7. Has organization or any of its officers, directors, employees or fund raisers:

A. Been enjoined or otherwise prohibited by a government agency/court from soliciting? Yes ☐ No ☐

B. Had its registration denied or revoked? Yes ☐ No ☐

C. Been the subject of a proceeding regarding any solicitation or registration? Yes ☐ No ☐

D. Entered into a voluntary agreement of compliance with any government agency or in a case before a court or administrative agency? Yes ☐ No ☐

E. Applied for registration or exemption from registration (but not yet completed or obtained)? Yes ☐ No ☐

F. Registered with or obtained exemption from any state or agency? Yes ☐ No ☐

G. Solicited funds in any state? Yes ☐ No ☐

If “yes” to 7A, B, C, D, E, attach explanation.

If “yes” to 7F & G, attach list of states where registered, exempted, or where it solicited, including registering agency, dates of registration, registration numbers, any other names under which the organization was/is registered, and the dates and type (mail, telephone, door to door, special events, etc.) of the solicitation conducted.

8. Has the organization applied for or been granted IRS tax exempt status? Yes ☐ No ☐

If yes, date of application ________________ OR date of determination letter 8/9/1983

If granted, exempt under 501(c) _____ . Are contributions to the organization tax deductible? Yes ☐ No ☐
9. Has tax exempt status ever been denied, revoked, or modified? Yes ☐ No ☑

10. Indicate all methods of solicitations:
- Mail ☐
- Telephone ☑
- Personal Contact ☐
- Radio/TV Appeals ☑
- Special Events ☐
- Newspaper/Magazine Ads ☐
- Other(s) ☐

11. List the NTEE code(s) that best describes your organization

P

12. Describe the purposes and programs of the organization and those for which funds are solicited (attach separate sheet if necessary).

See Statement 1

_____________________________________________________________________________________________
_____________________________________________________________________________________________
_____________________________________________________________________________________________
_____________________________________________________________________________________________
_____________________________________________________________________________________________

13. List the names, titles, addresses, (street & P.O.), and telephone numbers of officers, directors, trustees, and the principal salaried executives of organization (attach separate sheet). See Statement 2

14. (A) (1) Are any of the organization’s officers, directors, trustees or employees related by blood, marriage, or adoption to:
   (i) any other officer, director, trustee or employee OR (ii) any officer, agent, or employee of any fundraising professional firm under contract to the organization OR (iii) any officer, agent, or employee of a supplier or vendor firm providing goods or services to the organization? Yes ☐ No ☑
   (2) Does the organization or any of its officers, directors, employees, or anyone holding a financial interest in the organization have a financial interest in a business described in (ii) or (iii) above OR serve as an officer, director, partner or employee of a business described in (ii) or (iii) above? Yes ☐ No ☑
   (If yes to any part of 14A, attach sheet which specifies the relationship and provides the names, businesses, and addresses of the related parties).

(B) Have any of the organization’s officers, directors, or principal executives been convicted of a misdemeanor or felony? (If yes, attach a complete explanation.) Yes ☐ No ☑

15. Attach separate sheet listing names and addresses (street & P.O.) for all below: See Statement 3

- Individual(s) responsible for custody of funds.
- Individual(s) responsible for fund raising.
- Individual(s) authorized to sign checks.
- Bank(s) in which registrant’s funds are deposited (include account number and bank phone number).

16. Name, address (street & P.O.), and telephone number of accountant/auditor.

Name: Vivian Lai
Address: 1132 Bishop St. Suite 1000
City: Honolulu State: HI Zip Code: 96813 Telephone: (808) 536-0066

Method of accounting: Accrual

17. Name, address (street & P.O.), and telephone number of person authorized to receive service of process. This is a state-specific item. See instructions.

Name: Lyn Brown
Address: 745 Fort St. Suite 315
City: Honolulu State: HI Zip Code: 96813 Telephone: (808) 537-3118
18. (A) Does the organization receive financial support from other nonprofit organizations (foundations, public charities, combined campaigns, etc.)?  Yes ☐  No ☑

(B) Does the organization share revenue or governance with any other non-profit organization?  Yes ☐  No ☑

(C) Does any other person or organization own a 10% or greater interest in your organization OR does your organization own a 10% or greater interest in any other organization?  Yes ☐  No ☑

(If “yes” to A, B or C, attach an explanation including name of person or organization, address, relationship to your organization, and type of organization.)

19. Does the organization use volunteers to solicit directly?  Yes ☐  No ☑

Does the organization use professionals to solicit directly?  Yes ☐  No ☑

20. If your organization contracts with or otherwise engages the services of any outside fundraising professional (such as a “professional fundraiser,” “paid solicitor,” “fund raising counsel,” or “commercial co-venturer”), attach list including their names, addresses (street & P.O.), telephone numbers, and location of offices used by them to perform work on behalf of your organization. Each entry must include a simple statement of services provided, description of compensation arrangement, dates of contract, date of campaign/event, whether the professional solicits on your behalf, and whether the professional at any time has custody or control of donations.

21. Amount paid to PFR/PS/FRC during previous year: $41,000.00

22. (A) Total contributions: $1,515,284.00

(B) Program service expenses: $1,452,841.00

(C) Management & general expenses: $8,778.00

(D) Fundraising expenses: $50,844.00

(E) Total expenses: $1,512,463.00

(F) Fundraising expenses as a percentage of funds raised: 3.00% 4.00%

(G) Fundraising expenses plus management and general expenses as a percentage of funds raised: 96.00%

(H) Program services as a percentage of total expenses: ____________%

Under penalty of perjury, we certify that the above information and the information contained in any attachments or supplement is true, correct, and complete.

Sworn to before me on (or signed on) ________________, 20____

Notary public (if required) ____________________________________________

________________________________________

Name (printed) Tracey Keahi

________________________________________

Name (signature) Name (signature)

________________________________________

President Treasurer

________________________________________

Title (printed) Title (printed)

Consult the state-by-state appendix to the URS to determine whether supporting documents, supplementary state forms or fees must accompany this form. Before submitting your registration, make sure you have attached or included everything required by each state to the respective copy of the URS.

Attachments may be prepared as one continuous document or as separate pages for each item requiring elaboration. In either case, please number the response to correspond with the URS item number.

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Purpose and Programs

Purpose:
Wish Granting

Program(s):
1) Wish Granting
<table>
<thead>
<tr>
<th>Name and Address</th>
<th>Mailing Address (if different)</th>
<th>Title</th>
<th>Phone</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ryan Sakaguchi</td>
<td>1001 Bishop St. Pauahi 1800</td>
<td>President</td>
<td>808-541-5172</td>
</tr>
<tr>
<td>Honolulu, HI 96813</td>
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<tr>
<td>Marie Milks</td>
<td>1565 Kaminaka</td>
<td>Vice President</td>
<td>808-226-5633</td>
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<tr>
<td>Honolulu, HI 96816</td>
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<tr>
<td>Lori Lee</td>
<td>817 Ekoa Pl.</td>
<td>Secretary</td>
<td>808-983-8673</td>
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<tr>
<td>Honolulu, HI 96821</td>
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<tr>
<td>Tracey Keahi</td>
<td>999 Bishop St., Suite 1900</td>
<td>Treasurer</td>
<td>808-531-3481</td>
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<tr>
<td>Honolulu, HI 96813</td>
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<tr>
<td>Robert Q. Bruhl</td>
<td>828 Fort St. Mall, 4th Floor</td>
<td>Director</td>
<td>808-521-5661</td>
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<td>Honolulu, HI 96813</td>
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<tr>
<td>Carolyn Tom Davis</td>
<td>1132 Bishop Street, 16th Floor</td>
<td>Director</td>
<td>808-533-8267</td>
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<td>Honolulu, HI 96813</td>
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<tr>
<td>Brandt G. Farias</td>
<td>999 Bishop St.</td>
<td>Director</td>
<td>808-525-6112</td>
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<td>Honolulu, HI 96813</td>
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<tr>
<td>Michael P. Loo</td>
<td>567 S. King Street, PH 603</td>
<td>Director</td>
<td>808-523-6285</td>
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<tr>
<td>Honolulu, HI 96813</td>
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</tr>
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*Has PDF list of registered charities on website.
**Registers only nonprofits that are not tax exempt or that are exempt under provisions other than IRC §501(c)(3)
***Issues press releases regarding settlements with URL links to settlements, judgments or AVC’s.
****Website has a location for such information but nothing has been posted.