MEMORANDUM

To: K. King Burnett, John Sebert

From: Laura Chisholm

Date: December 18, 2009

Re: Uniform Oversight of Charitable Assets Act – Post Meeting Memorandum

The drafting committee met on October 23-24, 2009 in Washington, D.C. to discuss a preliminary draft of the statute and to further consider policy issues that had not been resolved at the committee's prior meeting.

Attending the meeting were: K. King Burnett (Chair), Laura B. Chisholm (Reporter), Carl Lisman (Member), Mary Jo Dively (Member), James Bopp, Jr. (Member), Lyle Hilliard (Member), Thomas Jones (Member), John J. McAvoy (Member), Hon. Frederick Stamp, Jr. (Member), David Walker (Member), Barry Hawkins (Member, Division Chair), Lisa A. Runquist (ABA Business Law), John P. Burton (ULC, Observer), Eric Carriker, Mark Pacella, Janne Gallagher, John McCormally, and Nancy A. McLaughlin. Also attending were Robert Stein (ULC President), Michael Houghton (Chair, ULC Executive Committee), John Sebert (ULC Executive Director), and Kieran Marion (ULC Legislative Counsel).

I. Goals of the Project

In the discussions throughout the two days, the drafting committee reconfirmed that there are three main goals for the statute. The first is to articulate that the attorney general oversight function is to protect charitable assets. In most states, whether or not that function is embodied in a statute, the authority is inherent in the common law powers of the attorney general. In at least a few states, though, it has been held that no such common law authority exists, and in some other states, whether it exists and what it consists of is not so clear. The uniform or model act that results from this project will establish the authority that most states recognize in those states that don't and clarify its content in states where there is some question. Even in states where the common law authority is recognized (or, at least, no court has said that it is not), the act will make that authority visible and eminently more clear. One important aspect of this function of the act is to provide language that articulates, or at least suggests, the appropriate boundaries of attorney general authority, that is:

- to correct abuses, but not to step in and take over governance or substitute the attorney general's judgment for the legitimate judgment of the charity's board or trustees;
- to look out for the interests of the indefinite beneficiaries of charitable assets, but to keep sight of the private nature of the assets, rather than treating them as quasi-public assets; and
- to protect the donor's expressed intent and hold the charity to its expressed purposes, while avoiding the temptation to impose subjective (and, perhaps, politically attractive) ideas about a donor's implicit intent.

The second goal is to make sure the attorneys general's offices have the information they need to carry out their appropriate oversight functions. The statute will seek to facilitate the acquisition of the right information, enough information, but not too much (that is, to facilitate oversight without overburdening either the regulators or the regulated), and timely information, so that the regulators can react effectively to something going awry.

The third goal is to collect all of these provisions in one place in a state's code – to present it as a coherent whole. At present, provisions relating to attorney general oversight of charitable assets, if they appear in statutes at all, may be found scattered in a variety of sections of a state's statutes.

An ancillary goal of the project is to clarify and solidify the states' proper role in oversight of charitable assets in light of recent and proposed expansion of federal charity oversight provisions. This object is driven not only by principles of federalism. States have a different history, focus, experience, understanding, and reason for caring that charitable assets be protected, and that interest should be supported by functional statutes. In addition, the project reflects a desire to contribute to considered, coherent development of the law in this area as it responds to the evolving realities of the charitable sphere. Ideally, the statute that comes out of the Uniform Law Commission will mesh with the ALI Principles of the Law of Nonprofit Organizations project and other considered, forward-thinking developments in charity law, such as UPMIFA.

II. Working Draft of the Statute

The policy decisions made at the first meeting of the committee in October 2008 were incorporated into a working draft of statutory language. No one existing state statute served as a model or baseline for the draft. However, much of the language of specific sections was adapted from language currently used in one or more states. This draft was intended to serve as a starting place for the process of serious legislative drafting. The Reporter's intent was to provide the committee with a broad array of specific provisions that might respond to the policy preferences identified by the committee in its earlier meeting, with the idea that deleting would likely be easier than adding.

The committee arrived at a number of key decisions that will inform the revisions that will be incorporated into the next draft, to be considered in February 2010. For example, one of the central features of the 1954 act, identified as a continuing objective for a new act in the study committee report and supported by the drafting committee at its October 2008 meeting, is to provide a mechanism and requirement for registration of charities with the attorney general, so that the state's charity regulators will be alerted to the existence and location of the charitable assets over which they are supposed to watch. In the second meeting of the committee, extended discussion of this aspect of the act ended with a tentative decision that registration should require only the most basic information, and is perhaps unnecessary altogether. The issue of periodic reporting, also a key feature of the 1954 act and left unresolved at the committee's first meeting, was left still unresolved at the end of the second meeting; the direction of the discussion about registration, though, suggests that there will not be much enthusiasm for anything but minimal periodic reporting, if any at all. The shift away from registration and periodic reporting may be explained, perhaps, by the fact that the draft statute provides a fairly

extensive list of organizational "life events" and proceedings concerning charitable assets that require advance notice to the attorney general. The thought is that a regime that requires all charities to report regularly threatens to burden both charities and regulators unreasonably and unnecessarily. A statute that focuses on getting information to the regulators about the specific kinds of events that are most likely to create opportunities for deliberate or innocent diversion of charitable assets in time to avert or correct a problem is better tailored to facilitate appropriate supervision. These provisions are coupled with specification of the attorney general's investigation authority and provisions to facilitate cooperation among charity regulators from different states and the federal government.

One still unresolved issue is a very basic one – how to articulate the universe of entities that are appropriately subject to a particular state's attorney general oversight. The committee has generally taken the position that there should be no categorical exclusions from the reach of the statute, although there may be reasons to exempt some kinds of entities from particular requirements of the act. As the committee becomes more and more inclined to minimize the demands of registration and periodic reporting and to focus instead on gathering information about particular situations to which the attorney general ought to be alerted, there is less and less reason to exempt categories of organizations. Another aspect of this question, still to be resolved, is to delineate the universe of entities that "belong" to a particular state's regulators. Jurisdictional rules and conflict of laws principles provide for a broad reach to address wrongdoing that touches a state. The question here, though, is how to define the group of entities for which a particular state has appropriate regulatory reach. The underlying object here is to avoid subjecting multi-state entities to duplicative reporting and notice requirements, while being sure that some interested charity regulator is alerted to organizational events that merit oversight.

Discussions of specific sections of the draft act are summarized below:

Section 2. Definitions.

The committee agreed that the definitions will need to be reworked carefully to mesh with the substantive provisions of the act when those provisions are finalized.

Section 3. Attorney General Authority.

There was discussion about the use of the term "due application" in subsection (a), with concern expressed that the term is too broad, and might be interpreted to grant too much discretion. The committee agreed that the objective of this subsection is to articulate the general understanding of attorney general authority in this area, but not to invite overreaching. The committee and the Reporter agreed to continue to think about whether there is a better choice of words to accomplish this result.

A question was raised about whether subsections (a) and (d) could be combined. However, the two subsections serve different functions. Subsection (a) articulates the basic substance of attorney general authority with respect to charitable assets. Subsection (d) sets out remedies available to the attorney general as tools to carry out the duty set out in subsection (a). Based on this discussion, the Reporter believes that subsection (d) does not need to repeat the language of subsection (a) and should probably

be revised so as not to be addressed just to bringing an action, but rather, should include reference to other courses of action available to the attorney general.

There was discussion about whether subsection (b) is necessary. It was the sense of the group that it is. One important function of the statute is to codify and enable attorney general authority to protect charitable assets; there is no intention to limit attorney general authority by suggesting that the statute replaces other expressions of attorney general authority that appear either in common law or other statutes. Some states have taken the position that, absent a provision like this one, the inference is that the statute replaces other law. Thus, the committee decided that it is important to keep the provision in the statute.

Some participants expressed unease about subsection (e), which provides for authority to adopt rules and regulations reasonable and necessary for the administration of the act, because they saw it as giving the attorney general wide-ranging authority to generate regulations having to do with almost any aspect of charity governance. The group decided that subsection (e) should be removed from the statute and to consider later whether some more focused reference to rulemaking authority is necessary or desirable. For instance, if the final statute does incorporate a registration requirement, it will likely make sense to reference attorney general authority to use rulemaking to operationalize the registration regime.

Section 4. Registration.

Because no policy decision had been made by the committee in its earlier meeting, the first draft of the statute was compiled to incorporate the full range of possibilities, borrowed from states that have the most extensive requirements.

A variety of participants expressed great concern that registration should not be very burdensome. A question was raised about how much routine bother should be imposed on all charities in order to screen for the few instances that might be problematic. It was noted in the discussion that charities shouldn't have to hire a lawyer to register, or even to know that they are required to register, and that a global registration scheme imposes a burden not only on charitable organizations, but on attorney generals' offices, as well. The charity regulators in the room noted in response that availability of information to the public, not just the attorney general, serves an important function. Further, if the information system is electronic, some of the burden issue dissipates.

The sense of the group at the end of the discussion was to keep any registration requirement simple, set a size threshold so as to alleviate the concern about small grassroots organizations not having the resources to know they need to register, and to continue to try to figure out how to avoid making a large organization that operates in many states take on the burden of multiple registrations.

Discussion of particular subsections yielded the following decisions and open questions:

Subsection (c) lists the information to be included in the registration. There was agreement that requiring an inventory of the assets of the charitable entity was overly burdensome. There was less

agreement about requiring filing of the organization's by-laws, with some in the room expressing the strong opinion that the requirement is too intrusive, and others pointing out that the by-laws have to be submitted with the organization's Form 1023 application for recognition of federal tax exempt status.

The committee agreed that subsections (e) and (h) are unnecessary and should be deleted. Subsection (g), which refers to state and local tax exemption applications, should be changed to require tax authorities to provide the attorney general with a list of applications that have been approved, rather than "received." Further thought needs to be given to which tax exemptions this subsection should reference – just property tax exemptions, or others (e.g., sales tax exemptions) as well?

It was noted that subsection (f) may not be necessary, because it might be duplicative of section 7 and/or section 8 provisions. Subsection (i) should be deleted altogether or moved to section 6.

The group did not resolve the question: If the act does incorporate a registration requirement, what is the appropriate nexus between an entity and a particular state to justify an obligation to register in that state? While it is desirable to avoid unnecessary duplication and undue burden on charities that operate in more than one state, a state's charity regulator has a legitimate interest in being aware of charitable assets that are being held or applied within that state, even if the entity is based elsewhere. How should the statute describe the universe of organizations subject to the registration requirement in a particular state?

Section 5. Public inspection of register.

In the discussion of this section, it was suggested that subsections (a) and (b) be dropped and replaced by adding the clause "unless otherwise provided by law other than this act" to the first section of the section. The Reporter's further thoughts on that suggestion are that, while the substance of subsection (a) can be addressed with that streamlined language, subsection (b) would not be captured. However, subsection (b) may belong in a different section, because it is not about the register, rather, it is about notice.

A general thread of the discussion concerned making donor lists public. This concern was premised on the idea that, in the interest of simplicity, registration and periodic reporting might be based on the Form 990 that organizations already submit to the federal government. It should be noted that this problem will arise only if registration and reporting is linked to the Form 990, and that no decision to do that has been reached by the committee. Indeed, no decision to impose any periodic reporting requirement at all has been reached, although it has not been rejected, either. In any case, the concern about donor lists will be borne in mind as drafting proceeds. A more general issue, which requires more background research, relates to the interface of any exclusions from public inspection that the committee wishes to incorporate into this statute and a given state's public records act. This interface might be addressed in a comment, or otherwise worked into the statute in a way that a particular state can tailor to its own code's approach.

Section 6. Investigation.

A basic policy issue that was discussed, but not resolved, was whether the initiation of an investigation by the attorney general should need to be based on a sworn complaint, court approval, or just reasonable belief that there is something to investigate. Participants had a variety of opinions on this question (as do states that currently have statutory provisions addressing attorney general investigations). The impact of an investigation on a charity was noted, along with concern about the potential for overreaching or ill-motivated attorneys general. On the other hand, it was noted that cause for investigation often does not arise out of a sworn complaint, for example, when a newspaper story raises a concern about a charity. It was agreed that there is a need to protections against abuse of process, but no agreement was reached on whether that protection should be provided by putting barriers in the way of the attorney general asking for information or by providing mechanisms for a charity to block the demand for information after it has been issued. It was agreed that the fact of going to court to enforce a demand for information should not be public information, since the demand for information is not.

The group agreed that section 6(a) should be congruent with section 3(b). The ability to investigate should not be broader than the reasons the attorney general can go to court. It was also agreed that the provisions about procedure (subsections (b) through (f) should probably be left out of this statute and replaced with state-specific references to more general statutes that describe attorney general investigative powers and processes.

Section 7. Notice to Attorney General.

Some concern was expressed about the use of the word "material" in subsection (a). Some in the room felt that the term is too vague to give notice to organizations about when notice is required. Others thought that the word is not problematic, as it is used in a variety of legal standards, and because examples could be provided in the comments. One solution that was proposed was to require the filing of amended articles or other organic document any time there is an amendment. The charity regulators in the room favored this approach, and it has the advantage of certainty.

It was suggested that subsection (b), relating to notice of dissolution, should be extended beyond corporations to take in other forms of organization, particularly LLCs and unincorporated associations. This may be unnecessary, as subsection (c) covers disposition of all or substantially all assets. No decision was reached on this point.

There was discussion of whether to define "substantially all" in subsection (c) by setting a percentage threshold or including some other definition. No resolution of this issue was reached.

The timeframes included in several of the section 7 subsections were discussed, but not decided.

It was pointed out that the statute provides no consequences for failure to notify the attorney general as required in section 7, and agreed that provisions spelling out consequences must be included in the act. No resolution was reached on what those consequences should be.

The committee agreed that provisions to parallel subsection (b)(2) should be provided for subsections (c), (d), and (e). It was also agreed that a provision should be added to require notice of the creation of an irrevocable inter vivos trust that includes one or more charitable interests and the nature of those interests.

There was discussion about adding a provision requiring notice of a contemplated change in purpose or contemplated change in use of a restricted gift. There was more agreement on the latter point than on the former, because of the difficulty of defining when a change of purpose that is not tied to any formal action or document would trigger the requirement.

Section 8. Proceedings Concerning Charitable Entities.

It was suggested that the subsection (a) reference to "no later than commencement of proceedings" would result in notice being too late to be useful. States' rules of civil procedure vary; it was suggested that the timing of this provision should match a state's rules. This issue was not fully resolved. Perhaps the best approach is to bracket it, with a note that it should be congruent with the state's civil procedure rules.

It was agreed that the list in subsection (a)(3) should not be introduced with "including but not limited to." Care will need to be taken to make the list sufficiently inclusive, but avoid inadvertent overbreadth. It will be necessary to make sure the language focuses on actions concerning charitable assets or a charitable entity in a way that has an impact on charitable assets. For example, subsection (a)(3)(E), which now requires notice of "an action to determine matters relating to the probate and administration of an estate involving a charitable trust" is clearly too broad as written.