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Legal Issues of Creative Fundraising

NC Center for Nonprofits

Nonprofit Legal Compliance Workshop

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Disclaimer

This presentation is provided solely for educational purposes and is not intended to be, nor should it be relied upon, as legal or tax advice.

The views expressed are my own.

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Presentation Overview

1. The “New” Tax Law and Why it Matters For Fundraising
   a) Basic Overview of Charitable Deduction
   b) Review of Changes in New Tax Law Affecting Nonprofits

2. Creative Fundraising
   a) Commercial Coventures
   b) Other Developments

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Basic Overview of Charitable Deduction and New Tax Laws

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Charitable Deduction

A donation to a 501(c)(3) organization entitles a donor to a tax deduction

- You can deduct the value of the amount contributed from your taxable income
- But it only works if you “itemize” (i.e. don’t take the standard deduction)
  - E.g. A donor itemizes on her tax return and gives $9,000 in a given year to charities and has taxable income of $50,000. Because she itemizes, the taxable income is reduced by the amount of the donation; so taxable income goes down from $50,000 to $41,000.
  - Giving a dollar to charity does not eliminate a dollar of income tax you must pay; the savings calculation is based on your tax bracket
  - For the example above each dollar to charity is about $.25 in income tax reduction

“New” Tax Law

Impact of Tax Cuts and Jobs Act

- Doubled standard deduction for income tax ($24.4k for married couples and $12.2k for individuals)
- New limits on key itemizations- SALT ($10k), mortgage interest deduction (based on home value), etc.
- Doubled estate tax exclusion to $11 and $22 million (inflation adjusted)
- Only 10-14% of taxpayers will itemize, down by about 20%
- Some donors will begin “bunching”

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“New” Tax Law

- Will bunching mean less direct giving and more to DAFs?
- Competition from 501(c)(4)s in grassroots fundraising?
- Fewer estates with tax planning
- Will Charitable Deduction only be useful for very wealthy?

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“Newest” Tax Law- Only for 2020-2021

- For itemizers
  - Adjusted cash contributions made in 2020 are eligible for 100% AGI deduction (used to 60%)- Likely only will matter for a very few people
- For non-itemizers
  - Up to $300 deduction for cash gifts to charity ($600 for couples)
  - Some push to make something like this a permanent change
- NC decoupled from both provisions in 2020. 2021?

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2019 Data

Fundraising Effectiveness Project

Year to date nonprofit sector trends
01/01/2019 to 12/31/2019

Revenue

Year to-date revenue metrics indicate the value of general, mid-level, and major donors.

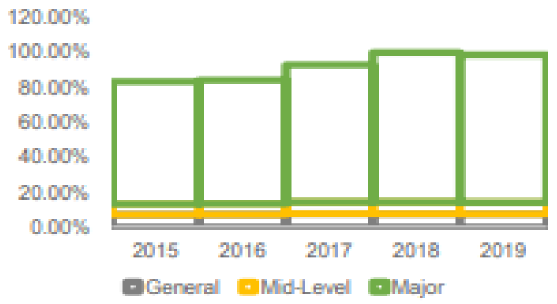
Revenue YTD

98.64% (% of Revenue at end of 2018)

Revenue YTD by Donor Level

General Donors (Under $250)	Mid-Level Donors ($250 - $999)	Major Donors ($1,000 & Up)
7.51%	6.66%	84.47%
-1.1% YTD Change	-1.0% YTD Change	-1.4% YTD Change
5.36% Upgraded Donors	45.4% Mid-Level Joins	36.0% Major Joins

Revenue YTD by Donor Level



Revenue YTD by Gift Range

Year	General	Mid-Level	Major
2015	7.06%	6.19%	70.12%
2016	7.19%	6.23%	70.81%
2017	7.64%	6.73%	78.64%
2018	7.59%	6.73%	85.68%
2019	7.51%	6.66%	84.47%

FUNDRAISING EFFECTIVENESS project

Upgraded Donors = % of under $250 donors that increased their giving.
Mid-Level Joins = % of $250-$999 donors with first gift in that range.
Major Joins = % of $1,000+ donors with first gift in that range.

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Standard Deduction Doubles: How to Adjust

- Consider “bunching” donations in one year and using standard deduction in other years
    - For example: Donor, a taxpayer who itemizes deductions, normally gives $10,000 to various charities per year. The donor could create a donor advised fund (DAF) with $40,000 and then advise DAF to distribute $10,000 per year to those charities. If the donor wished to support a single charity on an annual basis and wanted that annual support to continue, the donor could create an (or support an existing) organizational endowment at a community foundation to support the single charity with annual distributions from the endowment.
    - In the year the donor makes the $40,000 donation to a DAF or organizational endowment, the donor’s itemized deductions will exceed the standard deduction. In intervening years, the donor can take the standard deduction.

Standard Deduction Doubles: How to Adjust

- Under the new law, donating certain appreciated assets will continue to be beneficial
  - Gifts to a public charity of certain appreciated assets, such as marketable securities or real estate, results in a deduction equal to full market value of such assets at time of transfer
  - But the donor does not have to recognize appreciation of assets as income

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Standard Deduction Doubles: Retirement Assets

- Individuals with an IRA account are generally required to take a minimum distribution from that IRA every year starting at age 70 ½
- Instead of taking the minimum distribution, an individual can undertake a “charitable rollover” of all or part of that required minimum distribution and no income tax will be due on the amount passing to charity
- The charitable rollover is limited to $100,000 per year
- The charitable rollover is only available for IRAs
- If an individual is 70 ½ but the retirement assets are in a 401(k) plan, if the plan permits, the individual can take in service withdrawal and rollover to an IRA in order to take advantage of charitable rollover in the future

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Estate Tax Changes

- The estate tax exclusion amount, that is the amount that can pass at death without estate tax, has doubled-
- Pre-2018: $5 million adjusted for inflation per person, and $10 million, also adjusted for inflation, per married couple
- 2018-Dec. 31, 2025- $10 million adjusted for inflation per person, and $20 million also adjusted for inflation, per married couple
- Gift tax and generation skipping tax exclusion amounts are the same as the estate tax exclusion amount
- SECURE ACT: Reduced “stretch” period to 10 years for non-spouse beneficiaries of retirement assets

Estate Tax: What Did Not Change

- Charitable gifts at death still result in an unlimited charitable deduction for estate tax purposes
  - E.g. John Doe dies with $50 million estate and directs all amounts not subject to estate tax to go to his alma mater and all amounts within the estate tax exclusion amount to his brother
  - If John dies in 2021, $11,180,000 goes to his brother, $38,820,000 goes to alma mater, and $0 is due in estate tax
  - The estate tax previously applied only to few people, but now to even fewer people

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Estate Tax Changes: How to Adjust

- With so few estates now subject to estate tax, consider soliciting gifts during life and allowing donors to take advantage of an income tax deduction
  - Remember “bunching” technique
- Consider discussing changes to existing estate plans of which you are aware that benefit your organization and notifying donors about how new changes will affect charitable intent
  - Consider Jane Doe, who made an estate plan many years when the estate tax exclusion amount was $1 million. During that year Jane had assets of $5 million. Her estate plan directed the maximum allowable exclusion amount to her daughter and any amount subject to estate tax to her favorite charity, the Salvation Army.
- Consider combining a retirement accounts and charitable remainder trusts to mimic lifetime stretch for beneficiaries

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Estate Tax Changes: How to Adjust

- Jane Doe example (cont.)
  - Jane dies in 2018 with $8 million in assets. Because her estate plan was based on any amount subject to estate tax passing to charity and anything not subject to estate tax to her daughter, her daughter now gets her entire estate and the Salvation Army gets nothing.
- What can Jane and her favorite charity do to avoid this?
  - Re-draft estate plan so that a minimum amount goes to charity
  - Give amounts during life and take income tax deductions
  - If the standard deduction is causing a problem, consider “bunching”
  - If 70 ½ or older, consider a charitable rollover

Summary of Steps for Charitable Organizations to Consider

- Given the tax law changes, what should charities consider doing:
  - PUSH FOR CASH DONATIONS IN 2021
  - Emphasize non-tax reasons for donations
  - Consider beneficial use of “bunching” and communication on this with donors as appropriate
  - Actively solicit donations of retirement plan assets, including charitable rollovers
  - To the extent that you are aware of donors planning to benefit your organization via the donor’s estate plan, review available documentation to see if donations are based on amounts passing per the estate tax exclusion amount and see if given current exclusion, that estate plan still meets the wishes of the donor

Summary of Steps for Charitable Organizations to Consider

- To get the tax reform law passed, Congress put a “sunset” date on almost all the tax provisions not related to corporate tax cuts
  - Generally, all the tax provisions mentioned in this presentation are scheduled go away on the last day of 2025
  - At that time, the pre-2018 tax law comes back into effect (e.g. the “old” standard deduction amount and “old” estate tax exclusion amount)
  - But… Congress can always extend some or all of the provisions

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Commercial Coventures and Other Developments

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What is a Commercial Coventure (CCV)?

- CCV- Basically, an arrangement where a nonprofit receives a percentage of a sale or an amount per sale made by a for-profit
  - E.g. You buy a beer at a brewery and the brewery advertises that it shall give $1 from each beer sale to Red Cross.
  - About half of the states, including NC, regulate CCVs
    - Regulations include requirements to have a written contract with certain provisions, registration with state authorities, and fees.
    - Exact regulation and what constitutes a CCV does vary widely state to state
- Traditionally, most CCVs benefit charities, but the steps here would also generally apply to a CCV benefiting a 501(c)(4)
- Who gets the tax benefit if any- Usually, for-profit.

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CCV in NC- Important Definitions

- “Charitable sales promotion” means an advertising or sales campaign that represents that the purchase or use of goods or services offered by a coventurer is to benefit a charitable organization. The provision of advertising services alone to a charitable organization does not constitute a charitable sales promotion.
- "Coventurer" means any person who, for compensation, conducts a charitable sales promotion or a sponsor sales promotion, other than in connection with the solicitation of contributions.
- "Sponsor" means a person who is or holds out to others as soliciting contributions by the use of any name that implies affiliation with emergency service employees or law enforcement officers and who is not a charitable organization. "Sponsor" includes a chapter, branch, or affiliate that has its principal place of business outside the State, if this chapter, branch, or affiliate solicits or holds out to be soliciting contributions in this State.
- "Sponsor sales promotion" means an advertising or sales campaign conducted by a coventurer who represents that the purchase or use of goods or services offered by the coventurer will be used for a sponsor purpose or donated to a sponsor. The provision of advertising services alone to a sponsor does not constitute a sponsor sales promotion.

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What to do Prior to Launching the CCV

- The for-profit entity needs to get written consent from the charity to engage in the CCV
  - The charity needs a solicitation license or exemption in NC and should report CCV accordingly
  - Sign a contract, which should provide:
    - Projected amount of gross sales, sales for each item sold, charity's share per item, charity's total income from contract
    - Start and end date of venture
    - Obligation for for-profit to provide a final accounting to charity and have accounting ready to provide to NC government authorities if requested
    - Consider having a minimum donation require- in part because doing a CCV requires resources and there may be no sales
    - IP rights- limited license to use IP by for-profit for agreement (consider value of your IP in making terms of deal)
    - What will the promotion look like- have veto rights maybe
    - Compliance with applicable law
    - Geographic concerns
    - Other typical contract terms- indemnification, limited liability, termination, no assignment, governing law

What to Do During and After the CCV

- During the CCV- Charity should:
  - Make sure contractual terms are being adhered to
  - Publicize event using its own channels
- After the CCV- Charity should:
  - Get accounting per contract
  - Think about economics of the CCV (staff time, resources dedicated to making the CCV work, compliance costs like involving a lawyer, accountant, etc.).
  - Think about follow up with for-profit, especially if the CCV was successful (e.g. should it be an annual event?)

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Compliance Considerations

- On the license application/renewal, NC requires reporting on any current CCVs or CCVs that occurred during the immediate preceding year.

1. Applicant Name:	
2. Contractor Name:	
3. Contractor Street Address:	
4. Contractor Telephone Number:	
5. Contractor Type:	☐ Coventurer | ☐ Fund-raising Consultant ☐ Solicitor
6. Contract Signing/Execution Date:	
7. Contract services Begin Date:	
8. Contract services End Date:	
9. Is this a continuing or multiyear contract?	☐ YES | ☐ NO
10. Are North Carolina residents solicited for contributions as a direct or indirect result of this contract?	☐ YES | ☐ NO

11. Does contract contain salary, rate, or fee terms? ☐ YES | ☐ NO
<u>If YES, state terms and conditions below:</u>

12. Does contract contain bonus terms? ☐ YES | ☐ NO
<u>If YES, state terms and conditions below:</u>

13. Does contract contain commission terms? ☐ YES | ☐ NO
<u>If YES, state terms and conditions below:</u>

14. Does contract contain expenses terms? ☐ YES | ☐ NO
<u>If YES, state terms and conditions below:</u>

15. Does contract contain other compensation terms? ☐ YES | ☐ NO
<u>If YES, state terms and conditions below:</u>

16. Amount of funds received resulting from contract since your last license application filing:
(For initial applicants: amount of funds received within past fiscal year or past 12 months):

Answer either or both line items: Gross Amount Received: $__________

Net Amount Received: $__________

QUESTIONS?

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