

Planned Giving News

FOURTH QUARTER 2004

2004 LEGISLATIVE HIGHLIGHTS

by Peter Boyle

The year 2004 was important for California non-profits. The state's legislature took significant steps in the area of non-profit governance and better donor protection, while at the same time aided the long-term viability of these institutions through changes in gift annuity regulation.

As Ken Dike explained in our Fall newsletter, *Senate Bill 1088* amended California's insurance code to allow gift annuities to invest up to 50% of their annuity reserves in stock. This is a significant increase from the former limit of 10% and will, in the long-term, likely result in additional funds for California's charities. Importantly however, simply because the code now allows this higher allocation, does not mean it is appropriate for every fund. Make sure to consult your investment professional before making any changes to your allocations. If you missed this article, let us know and we will send you another copy or you can visit our website at www.clifford1915.com.

The other areas of change involved non-profit corporate governance and the registration of trustees.

The *California Nonprofit Integrity Act of 2004*, which took effect on January 1, 2005, has a significantly broader scope than deferred giving,

but is certainly worthy of discussion. The intent of this legislation is to: 1) provide new protections against fraudulent fundraising practices and 2) require greater financial accountability by charities and commercial fundraisers. Some of the key points are:

- Accountability
 - Charitable organizations have 30 days, instead of six months, to register and file Articles of Incorporation with the Attorney General's Registry of Charitable Trusts.
 - Independent audits of annual financial statements are now required for charities with gross revenues of \$2 million or more.
 - Charities with gross revenues of \$2 million or more must establish and maintain an audit committee.
- Executive Compensation
 - Executive compensation by charitable corporations, unincorporated associations and charitable trusts must be reviewed and approved to ensure the payment is "just and reasonable."
- Commercial Fundraisers
 - Commercial fundraisers must notify the Attorney General before starting a solicitation campaign.
 - Commercial fundraisers must

have written contracts with the charitable organizations for whom they are working.

- Charitable organizations and commercial fundraisers for charitable purposes are prohibited from engaging in misrepresentation and certain other acts when soliciting donations.
- Fundraising counsel must have written contracts with charitable organizations.

There remain some exemptions from the registration, reporting and audit requirements so long as the "charitable corporation or unincorporated association [is] organized and operated primarily as a religious organization, educational institution, hospital..." The other provisions of the Act, however, appear to apply to these organizations.

Specific to planned giving, charitable lead trusts would seem to be covered by the Act, but remainder trusts are exempt so long as they remain future interests.

For further information on this legislation and its requirements, you can refer to the Attorney General's website @ <http://www.ag.ca.gov>.

The last important piece of legislation (Senate Bill 1248) expanded on

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"THE INTENT OF THIS LEGISLATION IS TO 1) PROVIDE NEW PROTECTIONS AGAINST FRAUDULENT FUNDRAISING PRACTICES AND 2) REQUIRE GREATER FINANCIAL ACCOUNTABILITY BY CHARITIES AND COMMERCIAL FUNDRAISERS."

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existing laws governing conservators and guardians. Since 2000, all professional conservators and guardians have been required to register with the California Attorney General. The intent of registration was to provide the courts with a centralized resource for appointing and possibly removing a fiduciary.

Beginning in 2005, this registration was expanded to include trustees. In a round-about manner this legislation includes non-profits acting as trustee of charitable trusts. While several categorical exemptions were written into the legislation, the statute is silent on the issue of charitable organizations acting as the trustee of charitable trusts. It is widely believed that the Attorney General's office will issue some guidance on this topic; as of this printing none has been forthcoming. Therefore, as a result of the financial penalties for non-conformance, we have been recommending that our clients consider registering their institutions.

Unfortunately, since this registration was originally designed to document an individual's qualifications to act in a fiduciary capacity, some of the required declarations, such as educational background, obviously do not apply to institutions. However, with little or no guidance from the State, several attorneys we consulted suggested filling-in the registration form as completely as possible. If you have specific questions on how we counseled our clients, please let us know. The registration fee is \$385 and is good for three years.

For further information, either contact our office or check the Attorney General's website at <http://caag.state.ca.us/conservator/index.htm>. §

WHAT'S IN A NAME?

by Jim Fox

Remember when sales people in the financial services industry were clearly identified as stockbrokers, registered representatives, insurance salesmen, or mutual fund salesmen? Over the last decade, there has been a tremendous marketing effort directed at camouflaging the sales focus of those professional activities. New business titles such as financial advisor, investment consultant, and wealth manager, along with a host of other labels, often are superficial attempts to disguise what is primarily a sales commission-driven function.

The reason for this is multifaceted but is essentially driven by an informed investor population that has seen the devastating impact caused by conflicts of interest and disgraceful abuses by unethical financial salesmen as noted by the press almost daily. The population of wealthy investors has grown, as has their access to information. The result has been a huge, growing appetite for competent, unbiased assistance.

How does a nonprofit institution exercise its fiduciary duty and select the real thing? Certainly a few questions directed at discovering all affiliated business interests could shed light on potential conflicts or lack of real training and professional competence. A fee-based Investment Counselor is technically an Investment Adviser registered with the Securities and Exchange Commission (SEC) under the Investment Advisers Act of 1940. Membership in the Investment Counseling Association of America

requires compliance with some of the highest standards for ethical business practices in the industry. Employees of member firms of the ICAA also are encouraged to earn professional certifications such as Chartered Investment Counselor or Chartered Financial Analyst, to name two.

Once the trustees determine the potential adviser is actually a registered advisor, it should request the mandatory disclosure statement. This is a regular filing with the SEC called Form ADV. It is composed of Part I and Part II. Investment Counselors are required to update the information at least annually and more often if a material change occurs. The counselor must provide a prospective client Part II before a service agreement is executed. Part I can be requested as a supplement or obtained from the SEC's website www.sec.gov, under "Check out Brokers & Advisors." This report discloses the background of the principals, identifies the owners, its sources of income, the specific competencies of the firm, any regulatory deficiencies that may exist, and a host of other details. It should be noted that very small, usually embryonic firms are exempt and register only with the state in which they are domiciled. These firms, however, rarely qualify for institutional advisory consideration.

From our perspective, it is rare that an interviewing board or committee will spend adequate time on this important background detail. We feel it should receive *at least* the attention that is customarily devoted to examining yesterday's performance record. §

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