March 12, 2021

Gary Trechel
Department of State
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Re: Comments on Proposed 19 NYCRR Part 146

Dear Mr. Trechel,

We write to provide comments on Proposed 19 NYCRR Part 146, on behalf of Lawyers Alliance for New York, Nonprofit New York, Perlman+Perlman LLP, and Pro Bono Partnership. The proposed regulations implementing Executive Law 172-b impose a completely unnecessary Annual Financial Report filing requirement on thousands of charitable nonprofit organizations. These reports will provide the State with no new information that is relevant to its authority under Article 7 of the Executive Law. Lawyers Alliance urges the Department to instead create a single filing portal with the Charities Bureau for the submission of Annual Financial Reports, adopt a realistic filing deadline for those reports consistent with the Charities Bureau's deadline, eliminate the extra-statutory IRS 1023 filing requirement, clarify that 990 Schedule B's submitted with the Annual Financial Reports are not subject to FOIL and that the Department will protect the confidentiality of those reports, and revise the Regulatory Impact Statement and Regulatory Flexibility Analysis to accurately reflect the costs imposed on the many regulated entities.

A. Single Filing Portal

We strongly urge the Department of State ("DOS") to amend its rule to provide that filing an Annual Financial Report with the Charities Bureau pursuant to Executive Law 172-b will satisfy a nonprofit organization's obligation to file the same report with DOS. This would save state government resources by eliminating the administrative expenses involved in operating two completely redundant filing portals, and it would save scarce charitable funds by eliminating the requirement that nonprofits must file the same report in two separate places. The dual-portal system that DOS' regulation envisions is particularly irrational at a time when state government is trying to streamline operations to save money and the nonprofit sector is under unprecedented financial pressures and attempting to meet unprecedented community need.

B. Observe Extensions Granted by the Charities Bureau

DOS should add a provision clarifying that the deadline for filing an Annual Financial Report with DOS pursuant to Executive Law 172-b is the same as the deadline for filing the same report with the

Charities Bureau. The proposed rule does not mention filing deadlines. Under Executive Law 172-b, the Charities Bureau has discretion to grant extensions of the statutory filing date; the law does not grant the Department of State discretion to ignore that extension. During the pandemic, the Charities Bureau has granted an automatic 12-month extension to all registered charities.[1] Well before the pandemic, the Charities Bureau granted an automatic 6-month extension to all registered charities, so that the earliest a report would be due is the 15th day of the 11th month after the end of the fiscal year.[2]

The Charities Bureau's automatic extension is necessary to enable nonprofit organizations to prepare the financial and other information associated with 172-b filings. Among other things, in order to prepare such filing a nonprofit organization must close its books for the fiscal year, work with a tax professional to prepare the IRS 990 (for which the IRS also grants a six-month extension), undergo either an audit or review conducted by an independent accountant, and wait for the auditor to produce the report. An audit can cost as much as $20,000,[3] and if a nonprofit has to pay for an otherwise unnecessary expedited service it may well cost even more.[4]

C. Remove Extra-Statutory IRS 1023 Filing Requirement

The proposed regulations would require charitable organizations to file:

> a statement of the filing entity's mission that is consistent with what was or would be provided to the Internal Revenue Service, with a filing entity's application for recognition of exemption as a 501(c)(3), all charitable categories identified in such application, any narrative description of the filing entity's activities provided with such application, and any supporting details to the narrative description provided with such application.

This requirement appears nowhere in Executive Law 172-b, and the State Register notice contains no justification. The only conceivable purpose of this requirement is to carry out the Department's obligation under Executive Law 93-a to determine whether certain in-kind contributions or communications are "inconsistent with the charitable purposes" of the contributor or speaker. However, the Department has no obligation to review the charitable purposes of most of the organizations required to make Executive Law 172-b financial reports. Under Executive Law 93-a, the Department must review a filer's charitable purposes only if that organization is: a) a 501(c)(3) that makes an in-kind donation worth $10,000 or more to a 501(c)(4) organization, and then only if the 501(c)(4) spends $15,000 or more in a 12-month period on lobbying and the lobbying expenditures constitute at least 3% of the 501(c)(4)'s total revenues, or b) a 501(c)(4) that spends more than $10,000 in a calendar year on certain kinds of advocacy communications.

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[1] Charities Bureau, Guidance for Charitable Nonprofit Organizations Facing the Challenges of the COVID-19 Pandemic (April 2020), https://www.charitiesnys.com/pdfs/charitiesbureauguidance.pdf

[2] Office of the Attorney General, Extension Request Procedure Change: 180 Day Extension of Time to File is Granted (March 17, 2015), https://www.charitiesnys.com/pdfs/extensiongranted.pdf

[3] National Council of Nonprofits, What Is an Independent Audit?, https://www.councilofnonprofits.org/nonprofit-audit-guide/what-is-independent-audit

[4] National Council of Nonprofits, How Much Should an Independent Audit Cost?, https://www.councilofnonprofits.org/nonprofit-audit-guide/how-much-should-independent-audit-cost (noting that "if your fiscal year-end is December 31, but your nonprofit is willing to file its IRS Form 990 later in the year on extension, the audit firm may be willing to negotiate a lower fee because your nonprofit's field work will not occur during the firm's busy season").

Moreover, the Department already has in its possession the best evidence of charitable purposes – the purposes clause of the Certificate of Incorporation of every nonprofit corporation formed or authorized to do business in New York. That purposes clause remains in effect unless and until it is changed via a Certificate of Amendment filed with the Department of State. In contrast, the application for 501(c)(3) status (called an "IRS 1023") that the Department seeks only reflects an organization's intentions at the time that the form is filed. Indeed, in recognition of the fact that nonprofit organizations grow and change over time, the IRS requires them to describe on their annual IRS 990 "any new significant program services" and "any significant changes ... in how it conducts its program services to further its exempt purposes."[5] Since the Form 990 is part of the Annual Financial Report, you are already in possession of every charities' mission description.

Many nonprofits will be unable to comply with the requirement to submit portions of an IRS 1023. 501(c)(3)s formed prior to 1969 were not required to file 1023s.[6] Prior to 1988, 501(c)(3)'s were not required to retain their 1023's.[7] While a 501(c)(3) organization may be able to request a copy of its 1023 from the IRS, for older 1023s the IRS frequently responds that it does not have a copy on file. And, there are many charitable organizations that never filed a 1023, for instance because they are a 501(c)(4), a religious organization exempt from the requirement to file a 1023, or a member of a group exemption.

D. Confidentiality

The regulations must include provisions requiring the Department to maintain the confidentiality of the identities of the major donors of 501(c)(3) public charities – the information contained on the IRS 990 Schedule B that is filed as part of an organization's Annual Financial Report under Executive Law 172-b. The Charities Bureau has careful protocols in place to strictly maintain the confidentiality of the names and addresses of major donors reported on the 990 Schedule B.[8] The only other state charities regulators who require the filing of Schedule B, New Jersey and California, also have promulgated regulations with strong legal protections governing when the information will be made public, when it will be shared with other government officials, and how long it will be kept.[9]

[5] IRS, 2020 Instructions for Form 990, Section III lines 2 and 3, https://www.irs.gov/pub/irs-pdf/i990.pdf.
[6] IRS, Pub. 557 (Jan. 2020), https://www.irs.gov/publications/p557
[7] IRS, Notice 88-120 (1988) ("If an organization filed its application before July 15, 1987, it is required to make available a copy of its application only if it had a copy of the application on July 15, 1987."), https://www.irs.gov/charities-non-profits/notice-88-120-1988-2-cb-454
[8] Citizens United v. Schneiderman, Brief of the Attorney General (April 7, 2017), p. 51 n.19 (describing the Charities Bureau's "'consistent practice' of keeping Schedule B's confidential and substantial protocols in place to maintain confidentiality").
[9] NJSA 45:17A-31 ("the names, addresses and telephone numbers of contributors and amounts contributed by them ... shall not be considered a matter of public record and shall not be made available for public inspection, shall not be used for a purpose inconsistent with [New Jersey's charitable registration law], and shall be removed from the record in the custody of the Attorney General at such time that such information is no longer necessary for the enforcement of [that law]"); 11 Code of CA Regs. § 310 ("(b) Donor information exempt from public inspection pursuant to Internal Revenue Code section 6104 (d)(3)(A) shall be maintained as confidential by the Attorney General and shall not be disclosed except as follows: (1) In a court or administrative proceeding brought pursuant to the Attorney General's charitable trust enforcement responsibilities; or (2) In response to a search warrant.").

The Department's proposed regulations appropriately do not include Executive Law 172-b Annual Financial Reports in the category of documents that will be "made publicly available or disclosed when requested under Article 6 of the Public Officers Law."[10] However, they should also include the 990 Schedule B's submitted with those reports in the list of specific documents that will not be provided under that law, which currently includes only "information provided in a statement of relevant facts pursuant to paragraph (b) of section 146.4 or 146.5 of this Part."[11]

We urge the Department to also mirror the provisions of the New Jersey and California regulations that require the government to destroy the reports when they are no longer "necessary for the enforcement" of the law, and to prohibit the use of the records for any use other than enforcement of the underlying law.

Unless the Department adopts these measures, the risk of public disclosure will discourage giving to nonpolitical 501(c)(3) organizations by potential donors who prefer to remain anonymous, whether out of modesty, a religious imperative, a wish for privacy, or fear of retaliation or ostracism. Moreover, in the absence of adequate protection for the confidentiality of charities' donor information it is likely unconstitutional for the Department to collect that information. In 2018 the U.S. Court of Appeals for the Second Circuit rejected a constitutional challenge to the Charities Bureau's Schedule B filing requirement, relying heavily on its finding that "applicable law prevents the Attorney General from publicizing lists of donors."[12] However, the court warned that "[w]e would be dealing with a more difficult question if these disclosures went beyond the officials in the Attorney General's office charged with enforcing New York's charity regulations."[13] That is precisely what the Department of State filing requirement does.

E. The Regulatory Impact Statement and Regulatory Flexibility Analysis Are Deficient

The Regulatory Impact Statement and Regulatory Flexibility Analysis violate the State Administrative Procedures Act ("SAPA") and DOS' own Rule Making Criteria by failing to accurately assess the cost (including any professional services that will be required), alternatives that would avoid unnecessary duplication, and the number of regulated entities that will be affected.[14]

1. Cost: Contrary to the Regulatory Impact Statement's assertion that the regulations "will not impose any additional costs on the regulated entities,"[15] the Department's decision not to operate a single filing portal with the Charities Bureau for Executive Law 172-b Annual Financial Reports will cause the regulated entities to spend additional time on their filings and to pay an additional filing fee. In addition, the Department's failure to adhere to the Charities Bureau's filing deadline for those reports may require charities to pay extra to their tax preparers and outside auditors to expedite preparation of the organization's IRS 990,

[10] Proposed 19 NYCRR sec. 146.10.
[11] Id.
[12] Citizens United v. Schneiderman, 882 F.3d 374, 384 (2d Cir. 2018). The Supreme Court has granted certiorari in a similar case, in which the 9th Circuit upheld the California charities regulator's Schedule B filing requirement in the face of a constitutional challenge. Americans for Prosperity v. Becerra, 903 F.3d 1000 (2019), cert granted.
[13] Citizens United v. Schneiderman, 882 F.3d 374, 384 (2d Cir. 2018).
[14] SAPA 202-a, 202-b; NY Department of State, Regulatory Flexibility Analysis for Small Business and Local Governments, https://www.dos.ny.gov/info/pdfs/FMT-RFA.pdf; NY Department of State, Rule Making Criteria, https://www.dos.ny.gov/info/rulemakingmanual.html#appc
[15] State Register, Feb. 3, 2021, p. 15.

CHAR 500 and audit or auditor's review report. Moreover, while the Department asserts that the IRS 1023 information it requires organizations to submit is "ordinarily maintained by charitable organizations," as explained above that is not always true. Those organizations that cannot obtain their 1023, because it was filed so long ago that neither they nor the IRS has a copy, or that never filed a 1023, will have to try to describe the purposes, activities and charitable categories that they "would [have] provided to the Internal Revenue Service, with a filing entity's application for recognition of exemption as a 501(c)(3)." These organizations would be well advised to consult with an attorney or tax professional, which will further increase the cost of compliance.

The Department also fails to accurately assess the cost imposed on the Department itself. The Department's statement that "[t]he proposed regulations do not impose any additional costs on the Department of State" is incorrect, since the cost of establishing and operating its own filing portal for Executive Law 172-b Annual Financial Reports could be eliminated if the Department of State were to operate a single portal with the Charities Bureau.

2. Alternatives to Avoid Duplication: Contrary to the Regulatory Impact Statement's claim that "[t]hese proposed regulations do not duplicate any existing requirements of the state or federal governments,"[16] the requirement to file the exact same documents with two different government agencies is obviously duplicative. In light of this duplication, the Department must "identify all efforts which the agency has or will undertake to resolve, or minimize the impact of, such duplication... on regulated persons, including, but not limited to, seeking waivers of or exemptions from such other rules or legal requirements, seeking amendment of such other rules or legal requirements, or entering into a memorandum of understanding or other agreement concerning such other rules or legal requirements."[17] The Regulatory Impact Statement fails to do so, admitting that "[n]o significant alternatives were considered...."[18]

3. Number of Regulated Entities: The Department provides no estimate of the number of regulated entities, and this information is not publicly available. However, the number of entities required to file a duplicative Annual Financial Report is surely in the many thousands. An analysis of the IRS' Exempt Organizations Business Master File reveals that there are approximately 12,800 New York 501(c)(3) organizations with revenue of $250,000 or more that are schools, hospitals, or are publicly supported, and therefore are likely required to file Annual Financial Reports with the Department under Executive Law 172-b. The actual number of regulated entities is likely much higher, since there are many other types of organizations that are also required to file, including some private foundations and 501(c)(4)'s, as well as the many organizations that are based in other states and conduct charitable solicitations in New York.

[16] Id. p. 16.
[17] SAPA 202-a(3)(f).
[18] State Register, Feb. 3, 2021, p. 16.

Thank you for your consideration of these comments.

Sincerely,

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