
Christopher R. Sullivan

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Christopher R. Sullivan†

I. INTRODUCTION

Charitable organizations¹ employ a variety of methods for

† J.D. Candidate 2005, William Mitchell College of Law; B.A. University of Minnesota, English Literature, Computer Science.

¹ BLACK’S LAW DICTIONARY 228 (7th ed. 1999) (defining charitable organization as “[a] tax-exempt organization that (1) is created and operated
raising funds and educating the public about their causes and activities.\textsuperscript{2} The act of asking individuals for money is common to most charities.\textsuperscript{3} While there is nothing inherently fraudulent about charitable solicitation, the potential for fraud and abuse has led most states to enact legislation regulating fundraising.\textsuperscript{4} The ability exclusively for religious, scientific, literary, educational, athletic, public-safety, or community service purposes.


\textsuperscript{3}Charitable giving is a complex behavior that involves the financial resources of the individual, the need of the organization, and the cause or program being supported. Tax incentives such as deductibility of contributions may influence the amount given. Donations to organizations granted tax-exempt status under I.R.C. § 501(c)(3) are deductible to taxpayers who itemize, with some limitations. See I.R.C. § 170 (West 2004) (granting a deduction for "charitable contributions," which are defined as "a contribution or gift to or for the use of . . . [a corporation] organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes . . . ").

to regulate charitable solicitation is not without limits, however. During the 1980s, state and local officials attempted to enact legislation that sought to protect the public from fraud and required open, accountable, and effective charitable organizations. In a series of decisions, the Supreme Court decided that some of these regulations impinged on the First Amendment rights of the charity to educate the public about its cause.\(^5\)

Because the Court held that charitable solicitation had an educational and advocacy component, the regulation of which was subject to strict scrutiny,\(^6\) it was unclear whether a fraud cause of action could proceed against a professional fundraiser acting on behalf of a charity.\(^7\) By its unanimous decision in *Illinois ex rel.*...
Madigan v. Telemarketing Associates, Inc., the Court determined that the First Amendment did not protect fraudulent charitable solicitations. 8

This holding reflects the culmination of previous cases adjudicating the First Amendment rights of fundraisers. The decision also guides state and local regulators to a means of achieving their public policy goals of protecting the public from fraudulent charitable solicitations. The decision is meant to balance the protection of the public from fraudulent solicitations with a charity’s right to speak, educate, and solicit funds.

The regulatory landscape has changed in the ten years leading up to the Telemarketing Associates decision. Disclosures by charities of their overall finances as well as their contractual relationships with professional fundraisers are the norm. Public disclosures of that information, particularly on the Internet, provide donors and regulators with a generous amount of information on which to base decisions. As a result, regulators and the public have more information with which to combat fraud.

There is irony in the fact that the best means of preventing fraud may be a fraud cause of action itself. By focusing on fraud, the Court has highlighted an area of speech that does not deserve the same level of protection as charitable solicitation. Fraud prosecution, then, can be wielded as a tool to combat unscrupulous fundraisers. Fraud litigation against charities and paid professional fundraisers in the wake of the Telemarketing Associates decision indicate that the most egregious offenders can be stopped through coordinated anti-fraud campaigns.

This Note first examines the history of the relevant law in the areas of fraud, charitable solicitation, and prior restraints. 9 Specifically, it examines the three leading cases on regulation of charitable fundraising speech: Schaumburg, Munson, and Riley. 10

Next, the Note discusses the history and holding of Illinois ex rel. Madigan v. Telemarketing Associates, Inc. 11 Next, this Note will

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8. 538 U.S. 600 (2003) (Scalia, J., concurring). “What the First Amendment and our case law emphatically do not require, however, is a blanket exemption from fraud liability for a fundraiser who intentionally misleads in calls for donations.” Id. at 621.
9. See infra Part II.
10. Id.
11. Id.
explore the holding in *Telemarketing Associates* in light of *Schaumburg* and its progeny. This analysis includes a survey of recent and pending fraud litigation against charities and their fundraisers, and a review of the Federal Trade Commission’s “Operation Phoney Philanthropy.” Finally, the Note concludes with some regulatory considerations for charities, fundraisers, and regulators as they proceed in the post-*Telemarketing Associates* era.

II. HISTORY OF RELEVANT LAW

A. The Charitable Solicitation Regulatory Environment Before *Schaumburg*

    Fraud is “[a] knowing misrepresentation of the truth or concealment of a material fact to induce another to act to his or her detriment.” Specifically, fraud in the charitable context involves soliciting funds in the name of a charity with the intention that little, if any, of the funds raised would go to the charity for program activities as the donor intended. The Supreme Court has regularly found fraudulent speech to be of low value, and therefore unprotected.

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12. See *infra* Part IV.

13. *Id.* This play on words was lost on the Connecticut Attorney General’s Office. *See infra* note 140.

14. BLACK’S, *supra* note 1, at 670. The elements of the intentional tort of fraud (or deceit) are generally 1) false representation with 2) knowledge that the representation is false 3) that the plaintiff relies on 4) to his or her detriment. W. PAGE KEETON ET AL., PROSSER AND KEETON ON TORTS ch. 18 § 105 (5th ed. 1984). *See also* 37 AM. JUR. 2D Fraud and Deceit § 1 (2003) (discussing the broad nature of fraud as the “multifarious means that human ingenuity can devise and that are resorted to by one individual to gain advantage over another by false suggestions or by suppression of truth”).


regard. \(^{17}\)

Charitable solicitation is principally regulated by the states through their representative attorneys general\(^{18}\) as an exercise of the police power.\(^{19}\) In some cases, counties\(^{20}\) and cities\(^{21}\) have instituted charitable regulations. Typically, charity regulators attempt to protect the public from fraud by imposing disclosure requirements.\(^{22}\) Many of the attempts by states and municipalities

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\(^{17}\) Cantwell v. Connecticut, 310 U.S. 296, 306 (1940) (noting that a state may use its penal laws to protect its citizens by punishing fraudulent solicitations committed “under the cloak of religion”); Schneider v. State, 308 U.S. 147, 164 (1939) (denouncing fraud, including appeals “made in the name of charity and religion” as offenses punishable by law). \(But see United States v. Brandt, 196 F.2d 653, 657 (2d Cir. 1952)\) (labeling intent as a “practically crucial” element of fraud despite less than seven percent of $120,000 raised being used for charitable purposes).

\(^{18}\) See John W. Vinson, \(The Charity Oversight Authority of the Texas Attorney General, 33 St. Mary’s L.J. 243, 246-50\) (2004) (describing the early English and American common law authority of charitable regulation). In most states this has been written into statute. \(See statutes cited supra note 4.\) In addition to regulation of charitable solicitations, most charity regulators have broad powers to enforce the fiduciary duties of directors and officers. \(See, e.g., Minn. Stat. § 317A.467 (2003)\) (describing the attorney general’s power to seek broad equitable relief for any violation of chapter 317A).

\(^{19}\) Nat’l Found. v. City of Fort Worth, 415 F.2d 41, 45 (5th Cir. 1969) (citations omitted). “The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.” U.S. Const. amend. X. “It is a traditional exercise of the States’ ‘police powers to protect the health and safety of their citizens.’” Hill v. Colorado, 530 U.S. 703, 715 (2000) (quoting Medtronic, Inc. v. Lohr, 518 U.S. 470, 475 (1996)). \(See also Cantwell, 310 U.S. at 304\) (stating that a state can regulate the time, place, and manner of charitable solicitation as a means to “safeguard the peace, good order and comfort of the community . . . .”).


\(^{21}\) \(See, e.g., Martin v. City of Struthers, 319 U.S. 141 (1943)\) (describing a city ordinance that prohibited ringing doorbells or knocking on doors of residences); Hynes v. Mayor of Oradell, 425 U.S. 610 (1976) (reviewing a municipal ordinance that required validation of the cause by the police before solicitation could occur); Nat’l Found., 415 F.2d at 43 nn.1-2.

\(^{22}\) Charities interested in soliciting funds may be required to register and provide information, including the names and salaries of directors, purposes and methods of solicitation, and copies of contracts between the charity and professional fundraisers. \(See, e.g., Minn. Stat. § 309.52 (2003)\). Charities may also be required to provide detailed financial information on an annual basis. \(See, e.g., id. § 309.53.\) Professional fundraisers may be required to post a bond and state affirmatively the percentage of funds raised received by the charity. \(See, e.g., id. § 309.531.\)
to regulate or restrict the ability of charitable and religious groups to solicit, advocate, or canvass have conflicted with the First Amendment. Because the charitable solicitation was the most likely source of fraud within the charity’s operations, a common regulatory technique involved limiting the percentage cost of fundraising relative to the amount raised.24

Unfortunately, state and federal courts were unable to reach consensus about whether such limits were appropriate exercises of the police power of the states and their political subdivisions25 or prior restraints on speech that violated the First Amendment rights of charities and religious groups.26 In three separate decisions

23. U.S. CONST. amend. I; Hynes, 425 U.S. at 621-23 (holding as vague an ordinance that required police notice before canvassing); Martin, 319 U.S. at 153-54 (voiding an ordinance that prohibited door knocking or doorbell ringing in order to deliver handbills to residents); Jamison v. Texas, 318 U.S. 413, 413-14 (1943) (overturning an ordinance prohibiting “distribution” of handbills); Cantwell, 310 U.S. at 307 (prohibiting a state determination of what constitutes a religious cause before granting a license for the “perpetuation of religious views or systems”); Schneider, 308 U.S. at 163-64 (nullifying a canvassing ordinance that targeted non-commercial speech such as religious, political, or social information); Lovell v. City of Griffin, 303 U.S. 444, 450-51 (1938) (characterizing as overly broad an ordinance that required city manager permission before literature distribution).

24. See, e.g., Nat’l Found., 415 F.2d at 43 n.2 (authorizing the city secretary to deny fundraising permits to organizations when the cost of fundraising exceeds 20 percent of funds raised); Krishna Consciousness, 437 F. Supp. at 667 (imposing a rebuttable presumption of fraud on fundraising costs exceeding twenty-five percent of charitable solicitations conducted at county airports); Hillman v. Britton, 168 Cal. Rptr. 852, 860 (Cal. Ct. App. 1980) (describing a Fresno ordinance that held fundraising costs over 15 percent to be unreasonable). See also Don F. Vaccaro, Annotation, Validity and Application of Governmental Limitation on Permissible Amount or Proportion of Fundraising Expenses or Administrative Costs of Charitable Organizations, 15 A.L.R.4th 1163 (1995).

25. Nat’l Found., 415 F.2d at 46 (providing an opportunity for the charity to show the reasonableness of its high fundraising costs was flexible and acceptable); Krishna Consciousness, 437 F. Supp. at 671 (finding the fundraising costs provision constitutionally sound, but requiring a speedy appeals process for permit denials); People ex rel. Scott, 376 N.E.2d at 674 (upholding a state statute requiring seventy-five percent of gross receipts collected be used for charitable purposes).

26. Fernandes v. Limmer, 465 F. Supp. 493 (N.D. Tex. 1979) (concluding that an airport restriction on solicitation was a prior restraint without proper safeguards); Swearson v. Meyers, 455 F. Supp. 88, 90-94 (D. Kan. 1978) (granting of a license to solicit based on a determination of what is a religious cause is unconstitutional); Hillman, 168 Cal. Rptr. at 858-61 (discussing prior restraints in the area of charitable solicitation without deciding on their exact contours). Prior restraints interfere with the content of speech before it is delivered or published. Near v. Minnesota, 283 U.S. 697, 722-23 (1931). In the charitable solicitation context, there is concern for licenses that may be denied arbitrarily without due process. See Fernandes, 465 F. Supp. at 501-02 (citing Freedman v. Maryland, 380
dating from the 1980s, the Court struck down legislation and ordinances that sought to prevent fraud by regulating charitable solicitation based on percentage of donations used for fundraising costs. In each case, the means of protecting legitimate state or municipal interests such as preventing fraudulent solicitation of its citizens were insufficiently narrowly tailored to withstand strict scrutiny.

These cases built upon each other in two significant ways. First, as each rule or statute was struck down, attempts were made to bring existing laws in line with the Supreme Court decisions without sacrificing the desire for broad protections against fraudulent solicitation. Second, the holdings in each case broaden the First Amendment protection of charitable solicitation, while making attempts at regulation based on fundraising expenses more difficult, if not impossible. It was within the existing contours of these decisions that the Supreme Court decided \textit{Telemarketing Associates}.

\textbf{B. Village of Schaumburg v. Citizens for a Better Environment}

The first of the three major cases to present the issue of prior restraints on charitable solicitation was \textit{Village of Schaumburg v. Citizens for a Better Environment}. In that case, the Village of Schaumburg (“Schaumburg”) adopted a measure that required charities obtain a permit prior to soliciting funds either door-to-door or in the public streets. Furthermore, the ordinance required that permit applications include “[s]atisfactory proof that at least seventy-five percent of the proceeds of such solicitations will be used directly for the charitable purposes of the organization.”

U.S. 51 (1965)) (discussing procedural safeguards for speech regulation); \textit{Hillman} 168 Cal. Rptr. at 858-61 (same).


28. \textit{See} cases cited \textit{supra} note 27.


32. \textit{Id}. at 624 (quoting \textit{SCHAUMBURG, ILL., CODE § 22-20(g)} (1974)). Organizations were required to submit a certified audit or similar documentation detailing the distribution of funds raised. \textit{Id}. at 624 n.4 (quoting \textit{SCHAUMBURG, ILL., CODE § 22-20}). The ordinance required charities to exclude from the
The Court analyzed the Schaumburg ordinance with respect to some basic principles set down by previous decisions. The Court reiterated the fundamental protection the First Amendment provides to charitable solicitations. The Court characterized the speech aspects of charitable solicitation as:

Involv[ing] a variety of speech interests—communication of information, the dissemination and propagation of views and ideas, and the advocacy of causes . . . .

[S]olicitation is characteristically intertwined with informative and perhaps persuasive speech seeking support for particular causes or for particular views on economic, political, or social issues, and for the reality that without solicitation the flow of such information and advocacy would likely cease . . . . Furthermore, because charitable solicitation does more than inform private economic decisions and is not primarily concerned with providing information about the characteristics and costs of goods and services, it has not been dealt with in our cases as a variety of purely commercial speech. Reasonable regulation of such speech is allowable only to the extent that it is sufficiently specific and narrowly tailored to avoid acting as a prior restraint on such speech.

The Court examined Schaumburg’s interest to determine if it was sufficiently strong to justify the restriction of protected speech charitable purpose “[s]alaries or commissions paid to solicitors [and] [a]dministrative expenses of the organization.” Id. (quoting SCHAUMBURG, ILL., Code § 22-20(g)).

33. Id. at 628-33. See Hynes v. Mayor of Oradell, 425 U.S. 610 (1976) (recognizing the power of a municipality to enforce reasonable regulations when appropriately narrow and specific); Jamison v. Texas, 318 U.S. 413 (1943) (barring an absolute prohibition against the distribution of handbills involving a religious purpose because of the solicitation of funds); Cantwell v. Connecticut, 310 U.S. 296 (1940) (holding a statute requiring a license to solicit funds for religious, charitable, or philanthropic purposes as an invalid prior restraint on the free exercise of a religion); Schneider v. New Jersey, 308 U.S. 147 (1939) (acknowledging the potential for fraud in charitable or religious solicitations, but holding nonetheless that licensing requirements constitute an unconstitutional abridgement of freedom of speech).

34. Vill. of Schaumburg, 444 U.S. at 632.

35. Id. This characterization was by no means unanimous. Id. at 644 (Rehnquist, J., dissenting). “While such activity may be worthy of heightened protection when limited to the dissemination of information . . . a simple request for money lies far from the core protections of the First Amendment as heretofore interpreted.” Id. (citations omitted). The dissent analogized future governmental attempts to regulate charitable solicitation as task worthy of Sisyphus. Id. at 639.

36. Id. at 637.
prompted by the seventy-five percent fundraising requirement.\textsuperscript{37} The Court considered that Schaumburg had a legitimate interest in preventing fraud, but held that there was an insufficient relationship between the fundraising prohibition and the seventy-five percent threshold.\textsuperscript{38} High fundraising costs can result from “a wide range of variables, many of which are beyond the control of the organization.”\textsuperscript{39} Instead, the Court encouraged efforts that sought to punish fraudulent misrepresentations directly or by promoting disclosures that inform the public about the charity’s finances.\textsuperscript{40}


The Court next took up the issue of restrictions on charitable solicitation in \textit{Secretary of State of Maryland v. Joseph H. Munson Co.}\textsuperscript{41} The statute at issue was similar to the Schaumburg ordinance in that it sought to limit fundraising expenses to twenty-five percent.\textsuperscript{42} However, the statute differed significantly because it offered charities a means to avoid the twenty-five percent ceiling if the limit would prevent the organization from fundraising.\textsuperscript{43} The parties in

\begin{itemize}
\item \textsuperscript{37} \textit{Id.} at 686.
\item \textsuperscript{38} \textit{Id.} at 637. “[C]haritable solicitation is not so inherently conductive to fraud and overreaching as to justify its prohibition.” \textit{Id.} at 638 n.11.
\item \textsuperscript{39} \textit{Id.} at 637 n.10.
\item \textsuperscript{40} \textit{Id.} at 637-38. “Illinois law, for example, requires charitable organizations to register with the State Attorney General’s Office and to report certain information about their structure and fundraising activities.” \textit{Id.} at 638 n.12 (citing ILL. REV. STAT., ch. 23 § 5102(a) (1977)).
\item \textsuperscript{41} 467 U.S. 947 (1984) [hereinafter \textit{Munson}]. Other cases decided in the interim interpreted the Court’s holding in \textit{Village of Schaumburg} differently. See Nat’l Black United Fund, Inc. v. Campbell, 494 F. Supp. 748, 759 (D.C. 1980) (finding a twenty-five percent administrative and fundraising expense cap to be reasonable on its face, but “applied in a manner which sweeps quite broadly, precluding participation by organizations well within the proper purpose of the [fundraising campaign].”); Holloway v. Brown, 403 N.E.2d 191, 196 (Ohio 1980) (distinguishing the instant ordinance from that at issue in \textit{Village of Schaumburg} because of a higher percentage limit on costs and a rebuttable presumption of unreasonableness).
\item \textsuperscript{42} \textit{Munson}, 467 U.S. at 951. “A charitable organization . . . may not pay or agree to pay as expenses in connection with any fund-raising activity a total amount in excess of 25 percent of the total gross income raised or received by reason of the fund-raising activity.” \textit{Id.} (quoting MD. CODE ANN. § 103D(a) (1982)).
\item \textsuperscript{43} \textit{Id.} “The Secretary of State shall issue rules and regulations to permit a charitable organization to pay or agree to pay for expenses in connection with its fund-raising activity . . . in those instances where the 25% limitation would effectively prevent the charitable organization from raising contributions.” \textit{Id.} n.2
Munson also differed from those in Schaumburg. The Joseph H. Munson Co. ("Munson") was not a charitable organization, but a professional fundraising business that solicited funds on behalf of Maryland nonprofit organizations, specifically the Fraternal Order of Police.

In Munson the Court found the availability of a discretionary waiver from the Secretary of State was not sufficient to meet the First Amendment challenge. The Court did not find the statute a suitable means for achieving the goal of preventing fraudulent charitable solicitation. The Court described the poor fit between the goal of the statute and the potential misapplication as:

operat[ing] on a fundamentally mistaken premise that high solicitation costs are an accurate measure of fraud. That the statute in some of its applications actually prevents the misdirection of funds from the organization’s purported charitable goal is little more than fortuitous. It is equally likely that the statute will restrict First Amendment activity that results in high costs but is itself a part of the charity’s goal or that is simply attributable to the fact that the charity’s cause proves to be unpopular. On the other hand, if an organization indulges in fraud, there is nothing in the percentage limitation that prevents it from misdirecting funds. In either event, the percentage limitation, though restricting solicitation costs, will have done nothing to prevent fraud.

The waiver notwithstanding, the Maryland statute, like the Schaumburg ordinance, was insufficiently narrowly tailored to avoid a First Amendment challenge.

The dissent in Munson, however, saw a more substantial link between high fundraising costs and fraud. Calling the statute a form of economic regulation, the dissent found only an indirect

(Quoting Md. Code Ann. § 103D(a) (1982)).

44. See id. at 950; Vill. of Schaumburg, 444 U.S. at 620.
45. Munson, 467 U.S. at 950. Because Munson was a for-profit, professional fundraising organization not directly targeted by the statute, the Court had to address the issue of Munson’s standing to sue. Id. at 954-60. The Court held that Munson satisfied the “case or controversy” requirement and satisfactorily framed the issues for an over breadth challenge to the statute. Id. at 958-60. See also U.S. Const. art. III, § 2.
46. Munson, 467 U.S. at 962-69.
47. Id. at 966-67.
48. Id.
49. Id. at 970.
50. Id. at 980 (Rehnquist, J., dissenting).
impact on protected expression. The regulation would impose a price control on the market that may drive marginal producers out of the charitable solicitation business, but protected expression would not be fundamentally harmed.

Moreover, the dissent argued that the statute should withstand even heightened scrutiny because strong government interests are present. Such a statute coincides with the public’s expectation of how the charity uses donated charitable dollars, thereby bolstering confidence. In those cases where a donor is unaware that only a small portion of the funds raised actually goes to the charity, the dissent would find “an element of fraud.” Regardless of whether or not the percentages retained by the fundraiser are disclosed to the donor, the state has an interest in keeping charitable solicitation costs low and protecting charities from being “overcharged by unscrupulous professional fundraisers.”

D. Riley v. National Federation of the Blind of North Carolina

At issue in the third case of the charitable solicitation trio, Riley v. National Federation of the Blind of North Carolina, was the state’s amended Charitable Solicitation Act. The Act contained two provisions that a coalition of fundraisers and charitable organizations challenged on First Amendment grounds. The first provision provided for a three-tiered scale of reasonableness for fundraising expenses. The Act deemed fees reasonable if they were under twenty percent of the total collected. Fees between twenty and thirty-five percent were presumed reasonable, while those in excess of thirty-five percent were presumed unreasonable. The second provision required professional

51. Id. at 978.
52. Id. at 979-80.
53. Id. at 980.
54. Id.
55. Id. (internal quotations omitted). “[A] high fundraising fee itself betrays the expectations of the donor who thinks that his money will be used to benefit the charitable purpose in the name of which the money was solicited.” Id. at 980 n.2.
56. Id. at 980.
58. Id. at 785-87.
59. Id. at 784-85 (citing N.C. GEN. STAT § 131C-17.2 (1986)).
60. Id.
61. Id at 785. As in Munson, the statute contained a provision that allowed the presumption to be rebutted if the fee could be proved necessary “either (1)
fundraisers to affirmatively disclose the amount of funds retained for themselves.\textsuperscript{62}

Aware of the Court’s previous holdings that charitable solicitations are protected speech and that fee percentage-based restrictions were not sufficiently related to fraud prevention, North Carolina posited two distinctions for its regulatory scheme: guaranteeing reasonable fees to maximize funds flowing to the charity and the flexibility of the tiered approach.\textsuperscript{65} For the first distinction, the Court examined two possible premises.\textsuperscript{64} First, the Court considered whether charities are “economically unable to negotiate fair or reasonable contracts without governmental assistance.”\textsuperscript{65} The Court disposes of this possibility by citing a lack of evidence of inequitable contracts and a failure to narrowly tailor a regulation that restricts speech.\textsuperscript{66}

The second possible premise for the “reasonable fee” requirement was a state interest in regulation protecting the charity from an undertaking that would be harmful to its own interest.\textsuperscript{67} This premise did not survive even a superficial First Amendment analysis.\textsuperscript{68} Moreover, the court examined “legitimate reasons” for a charity to reject the state’s interest in ensuring “reasonable” fundraising fees.\textsuperscript{69} The Court acknowledged that a charity might make trade-offs regarding the type of fundraising drive, the costs of because the solicitation involved the dissemination of information or advocacy on public issues directed by the charity, or (2) because otherwise the charity’s ability to raise money or communicate would be significantly diminished.” \textit{Id.} at 785-86 (paraphrasing N.C. Gen. Stat. § 131C-17.2(d)(1)-(2) (1986)).

\textsuperscript{62} \textit{Id.} at 786. Unchallenged portions of the statute required the disclosure of the professional fundraiser’s name, his or her employer’s name, and the employer’s address. \textit{Id.}

\textsuperscript{63} \textit{Id.} at 789-90.

\textsuperscript{64} \textit{Id.} at 790.

\textsuperscript{65} \textit{Id.}

\textsuperscript{66} \textit{Id.} During oral arguments the Court indicated that each of the sixty charities that stated a position voiced their opposition to the statute, prompting North Carolina to label them as “misinformed regarding the pro-charity nature of the statute.” \textit{Id.} at 790 n.6 (citing Tr. of Oral Arg. at 20-21).

\textsuperscript{67} \textit{Id.} at 790 (calling the premise “paternalistic”).

\textsuperscript{68} \textit{Id.} at 790-91.

\textsuperscript{69} \textit{Id.}
the drive, short-term benefits, educational opportunities, and any other benefits that the charity may achieve through its fundraising.\textsuperscript{70} The Court regarded opportunities for advocacy and education to be sufficient to justify a sacrifice in the amount of funds raised.\textsuperscript{71}

North Carolina cited the flexibility of its tiered approach to “reasonableness” as a key distinction between this Act and previous regulatory frameworks struck down by the Supreme Court.\textsuperscript{72} However, having found the “generalized interest in unilaterally imposing its notions of fairness on the fundraising contract [to be] both constitutionally invalid and insufficiently related to a percentage-based test,” the Court returned to familiar territory: was the flexibility of the regulation sufficiently narrowly tailored to the particular interest of protecting a charity from fraud?\textsuperscript{73} Not surprisingly, the Court, citing \textit{Munson}, denied the presence of a “nexus between the percentage of funds retained by the fundraiser and the likelihood that the solicitation is fraudulent.”\textsuperscript{74} Even the rebuttable presumption of the top tier was insufficient to convince the Court that this Act would not have a chilling effect on speech.\textsuperscript{75} The Court was unwilling to allow the possibility that a factfinder might decide that costs or fees were excessive despite any advocacy or educational content of the speech.\textsuperscript{76}

The second statutory feature that the Court examined was the requirement of an affirmative disclosure of the percentage of charitable contributions retained by the professional fundraiser.\textsuperscript{77} Acknowledging that the commercial and educational aspects of charitable solicitation are intertwined, and relying on its previous

\begin{itemize}
  \item \textsuperscript{70} \textit{Id.} at 792.
  \item \textsuperscript{71} \textit{Id.}
  \item \textsuperscript{72} \textit{Id.}
  \item \textsuperscript{73} \textit{Id.}
  \item \textsuperscript{74} \textit{Id.} at 793.
  \item \textsuperscript{75} \textit{Id.} “Whether one views this as a restriction on the charities’ ability to speak, or a restriction of the professional fundraisers’ ability to speak, the restriction is undoubtedly one on speech, and cannot be countenanced here.” \textit{Id.} at 794 (citations omitted).
  \item \textsuperscript{76} \textit{Id.} at 793.
  \item \textsuperscript{77} \textit{Id.} at 795. Intervening court decisions pointed to a split on the issue of affirmative disclosures. \textit{Heritage Publ’g Co. v. Fishman}, 634 F. Supp. 1489, 1505 (D.Minn. 1986) (upholding the disclosure portions of the charitable solicitation statute while finding other portions unconstitutional in light of \textit{Schaumburg} and \textit{Munson}); \textit{State v. Events Int’l, Inc.}, 528 A.2d 458, 461-62 (Me. 1987) (striking down a disclosure provision that was linked to a seventy percent fundraising cost threshold).
\end{itemize}
holdings in *Schaumburg* and *Munson*, the Court refused to “parcel out the speech, applying one test to one phase and another test to another phase.” As a result, the Court applied the heightened test for a regulation that addresses a compelling state interest through narrowly tailored means.

The Court did not find North Carolina’s interest in enlightening potential donors about the costs of a fundraising campaign to be compelling. As in the previous cases, the Court reminded the state that “the charity reaps a substantial benefit from the act of solicitation itself.” The Court also pointed to the unchallenged portions of the statute that required affirmative disclosure of the professional capacity of the fundraiser, and the requirement to provide the percentage information to donors who inquire. Nor did the Court find the statute sufficiently narrowly tailored to avoid chilling otherwise protected speech.

Significantly, the Court suggested other methods of achieving a narrowly tailored response to the state’s concerns. Most relevant to this discussion is the Court’s urging to the state to “vigorously enforce its antifraud laws to prohibit professional fundraisers from obtaining money on false pretenses or by making false statements.” So, on the one hand, the Court put legislative and rulemaking bodies on notice that charitable solicitation was highly

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78. *Id.* at 796.

79. *Id.* at 798. The Court recognized that there was a different interest involved in compelled speech and compelled silence, but found the distinction “without constitutional significance” in the realm of protected speech. *Id.* at 796.

80. *Id.* at 798.


82. *Id.* at 799. The Court gave a clear indication of its opinion of such positive disclosures when it stated, “[N]othing in this opinion should be taken to suggest that the State may not require a fundraiser to disclose unambiguously his or her professional status. On the contrary, such a narrowly tailored requirement would withstand First Amendment scrutiny.” *Id.* at 799 n.11. Other states have similar affirmative disclosure requirements. See, e.g., 225 ILL. COMP. STAT. 460/17 (2003) (requiring prompt disclosure of paid professional fundraiser status); MINN. STAT. § 309.556, subd. 2 (2003) (requiring disclosure of the name of the professional fundraiser and their status as “professional fund-raiser” prior to any oral contribution request).

83. *Riley*, 487 U.S. at 799-800 (calling the measure “prophylactic, imprecise, and unduly burdensome”).

84. *Id.* at 800.

85. *Id.*
protected speech. On the other hand, the Court spotlighted a tool that states’ attorneys general could use to achieve the same end: fraud prosecutions.

Not surprisingly, commentators analyzed the three opinions and speculated on possible future regulatory challenges. There was a sense that the Court had gone too far to protect aspects of charitable solicitation to the detriment of regulators, donors, and the charities themselves. Potential solutions included mandatory disclosure requirements, public education campaigns to educate donors, and self-policing by the charitable sector. Fifteen years after the Court’s decision in *Riley*, the Supreme Court again addressed the interests of these constituencies as well as the
balance between protected speech and fraud.\textsuperscript{92}

\section*{III. CASE HISTORY}

\textbf{A. Facts}

VietNow is an Illinois charity that educates its members about issues important to veterans of the Viet Nam War such as homelessness and Agent Orange.\textsuperscript{93} Telemarketing Associates, Inc. ("Telemarketing") and Armet, Inc. ("Armet") (collectively, Telemarketers) are professional fundraising corporations solely owned by Richard Troia.\textsuperscript{94} From 1987 until 1996, VietNow contracted with Telemarketing to raise funds.\textsuperscript{95} VietNow received fifteen percent of the funds raised by Telemarketing, which retained the other eighty-five percent.\textsuperscript{96} Armet brokered additional out-of-state contracts with third-party professional fundraisers.\textsuperscript{97} Those contracts yielded ten to twenty percent of the funds to Armet and ten percent to VietNow.\textsuperscript{98} During the period of the contracts, Telemarketers raised over $7.1 million on behalf of VietNow with approximately $1.1 million of that amount going to the charity.\textsuperscript{99}

The Attorney General of Illinois filed the initial complaint in 1991,\textsuperscript{100} alleging common law fraud, breach of fiduciary duty, statutory fraud, and deceptive trade practices.\textsuperscript{101} Primarily, the complaint alleged misrepresentation of the use of the solicited funds.\textsuperscript{102} Because the charity received only fifteen cents of every dollar raised,\textsuperscript{103} representations to donors that VietNow would

\begin{thebibliography}{99}
\bibitem{94} People ex rel. Ryan v. Telemarketing Assocs., Inc., 763 N.E.2d 289, 291 (Ill. 2001).
\bibitem{95} Id.
\bibitem{96} Id.
\bibitem{97} Id.
\bibitem{98} Id.
\bibitem{99} Id. “VietNow does not complain that it did not receive the amounts for which it contracted . . . [or] expressed dissatisfaction with the fund-raising services provided by the defendants.” Id.
\bibitem{100} Id.
\bibitem{101} Id at 291-92.
\bibitem{103} In fact, there were additional allegations that "of the money raised by Telemarketers, VietNow in the end spent only about 3 percent to provide
benefit from significant portion of funds raised were false, deceptive, and fraudulent.\textsuperscript{104} Affidavits submitted along with the complaint alleged a variety of affirmative representations regarding the use of donated funds.\textsuperscript{105} Specific claims Telemarketers made to prospective donors involved Thanksgiving food baskets, job training, rehabilitation, and other services for veterans.\textsuperscript{106} One donor was allegedly told that ninety percent or more of her donation would be used for veterans, and that because VietNow was an all-volunteer organization, no labor costs would be incurred.\textsuperscript{107} The trial court granted Telemarketers’ motion to dismiss the fraud claims.\textsuperscript{108} At the subsequent appeals before the Illinois Appellate Court and the Illinois Supreme Court, Telemarketers prevailed.\textsuperscript{109} Not surprisingly, the Illinois Supreme Court relied heavily on the Supreme Court’s previous holdings in \textit{Schaumburg}, \textit{Riley}, and \textit{Munson}.\textsuperscript{110} While there was no specific regulatory provision at issue here, the Illinois Supreme Court considered the attempt to bring fraud claims against Telemarketers created the same sort of First Amendment issue raised by the previous cases.

The Illinois Supreme Court echoed each of the lessons learned from the charitable solicitation triad.\textsuperscript{112} Telemarketing’s statements were only fraudulent in light of the eighty-five percent solicitation fee.\textsuperscript{113} The fraud claim, therefore, was an attempt to regulate for-profit fundraisers using the same fee-based percentages struck down earlier.\textsuperscript{114} Like earlier Supreme Court decisions, the Illinois Supreme Court noted that high fundraising costs could have a variety of reasons.\textsuperscript{115} The court expressed concern about non-monetary or educational messages contained in charitable services to veterans.” \textit{Id.} at 607 n.1.

\begin{enumerate}
\item[104] \textit{Id.} at 609.
\item[105] \textit{Id.} at 608. Procedurally, such affidavits attached to the complaint become part of the complaint “for all purposes.” \textit{Id.} at 609 n.3 (quoting 735 ILL. COMP. STAT. 5/2-606 (2003)). As a result, an Illinois court can consider such evidence under a motion to dismiss.
\item[106] \textit{Id.}
\item[107] \textit{Id.} at 609.
\item[108] \textit{Id.}
\item[109] \textit{Id.}
\item[110] \textit{Id.} at 609-10.
\item[111] \textit{Id.} at 611.
\item[112] \textit{See id.} at 609-11.
\item[113] \textit{Id.} at 610.
\item[114] \textit{Id.}
\item[115] \textit{Id.}
\end{enumerate}
the solicitation process. Finally, the court read the Riley decision to bar a definition of fraud that “places on solicitors the affirmative duty to disclose to potential donors, at the point of solicitation, the net proceeds to be returned to the charity.”

B. Court Holding and Analysis

By taking up this case, the Court agreed to address an issue that had been referred to, but not explicitly dealt with, in its previous holdings. Unlike the prophylactic measures in Schaumburg, Munson, and Riley, this case involved fraud, which the First Amendment does not protect. The Court was quick to point out that fraud actions would not constitute a means to avoid the First Amendment problems with those previous measures. The Court warned off any state regulator who might attempt to “gain case-by-case ground [the] Court . . . declared off limits to legislators.” In other words, a coordinated campaign of fraud actions in order to impose a fee-based percentage limitation against those charities with high fundraising costs would not survive a constitutional challenge.

The Court acknowledged two distinctions in the pleadings that should allow the suit to proceed past the dismissal stage without interfering with the First Amendment. First, the complaint alleges that Telemarketers affirmatively represented that a major portion of donations would be used for specific programmatic purposes, despite their knowledge that only fifteen percent of each dollar donated was available to the charity. The second

116. Id. at 610-11.
119. Id. at 612.
120. Id. at 617. “Simply labeling an action one for ‘fraud,’ of course, will not carry the day.” Id.
121. Id.
122. See id. Even at the eighty-five percent retention level, the Court is unwilling to accept percentage-based enforcement measures. Id. at n.8.
123. Id. at 617-18. When considering the legal sufficiency of a defendant’s motion to dismiss, an Illinois court will assume the facts are true as pleaded and interpret them “in the light most favorable to the plaintiff.” Id. at 618 (emphasis omitted) (quoting Connick v. Suzuki Motor Co., 675 N.E.2d 584, 588 (Ill. 1997)).
124. Id. at 618.
justification the Court gave for allowing the fraud suit to proceed was that the charitable solicitation could be seen as a façade for the private inurement of Telemarketers. The complaint describes the funds raised for the charity as being “merely incidental to the fund raising effort.” The Court was persuaded that the fraud action was properly tailored to the facts as pleaded, and reversed and remanded the decision of the Illinois Supreme Court.

IV. ANALYSIS OF THE TELEMARKETING ASSOCIATES DECISION

A. A Proper Balance

In Telemarketing Associates, the Supreme Court reached an appropriate balance between all of the competing interests. By emphasizing the requirements of a narrowly tailored rule and a prohibition against “broad prophylactic” measures, the Court forced regulators to focus on the fraudulent component of the charitable solicitation. By emphasizing the protected nature of non-fraudulent charitable speech, the Court reaffirmed the importance of education and advocacy. And by allowing a fraud case to proceed against a professional fundraiser, the Court put the entire for-profit fundraising industry on notice that any fraudulent portion of their charitable solicitations would not be protected.

The Court never strayed from its endorsement of fraud as a means to regulate charitable solicitation. Indeed, the Court has appeared quite sympathetic to the oft-stated purpose behind many of these statutes and ordinances: protecting citizens from fraudulent charitable solicitations. In Telemarketing Associates,
however, the Court went further by giving insight into its reasons for preferring a “properly tailored fraud action” to “broad prophylactic rules.”

Fraud actions are attractive to the Court in this context because by their very nature they are narrowly tailored to “particular representations made with intent to mislead.” The Court considers the burden of proof of all of the elements of a fraud action to be sufficient protection for charitable speech. Despite fear by the Illinois Supreme Court that the cause of action in this case was an attempt to circumvent previous holdings of the Supreme Court, Telemarketing Associates stands for the proposition that the First Amendment does not offer protection when protected speech is intertwined with fraudulent speech.

Even though states may find the factual burden difficult to establish, now fraud actions against charities or professional fundraisers can proceed without having to address the thorny Constitutional issues. By succinctly settling the First Amendment issues of fraud and charitable solicitation, the Telemarketing Associates Court put regulators on firmer ground when taking action against unscrupulous fundraising practices. As a result, states can expect a number of cases to settle before trial is even necessary. In fact, Telemarketing Associates and its owner Richard Troia settled the Illinois action involved in Telemarketing Associates. The settlement bars Telemarketing Associates from soliciting funds from Illinois residents and from soliciting funds on behalf of Illinois charities.

130. Telemarketing Associates, 538 U.S. at 617 (citations omitted).
131. Id. at 621.
132. Id.
133. Id.
134. One commentator has suggested that states could implement a system for recording and auditing telephone solicitations by professional fundraisers. Kent D. Wittrock, Note, The End of Fraudulent Solicitation—Really?: The Supreme Court in Madigan v. Telemarketing Associates Provides That Fraudulent Statements in Charitable Solicitation are not Protected Speech, 72 UMKC L. Rev. 275, 294 (2003). While such a scheme would indeed provide the necessary factual basis for fraud suits, the additional costs to the states would probably make such a system unfeasible. Furthermore, having just escaped the specter of prior restraints, states may be hesitant to conduct random telephone audits that could give rise to litigation in the areas of privacy and wiretapping.
136. Id.
The most important question that remains after *Telemarketing Associates* is when a specific statement about the use of funds constitutes misrepresentation. The Court calls the actions of Telemarketing “a façade” and the amounts given to VietNow as “incidental to the fundraising effort.” The specific threshold that this represents is unclear. The Court does not specify whether any affirmative statement regarding the use of the funds received will be sufficient to meet this requirement. Having opened the door to fraud actions, the Court may have to specify what level of fraudulent speech is necessary to constitute a misrepresentation.

**B. Fraud Enforcement Actions**

While the statutory measures may yet remain the domain of Sisyphus, discrete fraud actions against professional fundraisers and charities will become a more popular route for regulating these enterprises. Coordinated fraud investigations along with a changing regulatory environment indicate that *Telemarketing Associates* was decided at the best time to provide guidance to regulators seeking to use fraud and related actions against professional fundraisers.

In the years between *Riley* and *Telemarketing Associates*, the Federal Trade Commission has become an important agency in the regulation of charitable solicitation and fraud. Beginning with discrete prosecutions and small coordinated campaigns, the FTC emerged as a federal partner for state regulators in the area of charitable solicitation fraud, particularly involving telephone solicitations. As if to reinforce fraud as the next battleground for regulators, the FTC announced Operation Phoney Philanthropy.

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138. See, e.g., Press Release, Federal Trade Commission, Northern Virginia Telemarketers of Desert Storm Bracelets Agree to Pay $120,000 to Settle FTC Charges (July 13, 1992) (prohibiting the defendants from future misrepresentations of the nature of the charitable organization, the portion used for charity, and the public benefit derived from money raised).

mere fifteen days after the *Telemarketing Associates* decision. This FTC program showcases new and existing law enforcement actions against charities, for-profit fundraisers, and associated individuals. Such actions were by no means new to the FTC, but the scale and scope of this operation points to the ascendancy of fraud as a means of regulating charitable solicitation. The involvement of the FTC is crucial for targeting those fraudulent charitable solicitation operations that operate in multiple states or phone from one state into another. As a coordinating and information sharing resource, the role of the FTC bodes well for those regulators combating fraudulent solicitations.

The involvement of the FTC, however, will come at an unexpected cost in the form of additional litigation about the First Amendment nature of charitable solicitation. What may be considered settled law at this point could be reopened due to pending litigation involving the Federal Do-Not-Call List (DNC). Charitable solicitations are exempt from the requirements of DNC, but challenges to the law have begun assailing the distinction between charitable solicitations as protected speech and less-protected commercial speech. DNC did impose some limited requirements on for-profit fundraisers in the interest of combating...
fraudulent charitable solicitations. These have also become the subject of litigation. Such litigation could force the Supreme Court to more closely examine the commercial nature of charitable solicitations and the nature of the intertwining of education, advocacy, and commercial transactions.

C. Regulatory Changes Since Riley

Rather than prohibit charitable solicitation altogether, the Supreme Court expressed a preference for disclosure requirements that “help make contribution decisions more informed.” In the years since Schaumburg and Riley, public disclosure of a charity’s financial records has become commonplace. More importantly, public awareness of these disclosures through the Internet or the media has resulted in increased scrutiny from and accountability to the giving public.

I. IRS Disclosures

Requirements that a charity or its professional fundraiser disclose financial information remains a popular means for ensuring accountability of charities and preventing fraudulent solicitations. Adding to the existing disclosure requirements of charitable organizations, the 104th Congress expanded the disclosure requirements for all organizations exempt from taxation under I.R.C. § 501(c). After the amended law and its subsequent rulemaking, the application filed requesting tax-exempt status along with the organization’s annual information returns were open to public inspection. Such information returns contain important information regarding the finances and fundraising activities of the organization. 501(c)(3) organizations are required to provide copies of these returns for three years after the

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148. See supra note 22 and accompanying text.
149. See discussion and sources cited supra notes 4, 22.
151. 26 U.S.C. § 6104(d) (2004). Organizations are required to file an annual information return, the IRS Form 990, that specifies income, expenses, salaries, and program activities. 26 U.S.C. § 6033(b) (2004).
filing date of the return. Individual requests can be fulfilled collectively if the returns are widely available, specifically over the Internet.

These disclosure requirements are significant educational and accountability measures. They aid the regulatory battle against charitable solicitation fraud by disseminating information about organizations and educating and empowering donors to explore the programmatic and financial reporting of an organization that requests their donation.

2. Intermediate Sanctions

The second key regulatory change affecting charitable organizations does not directly address fraud, disclosure, and accountability. Instead, recent legislation seeks to “prevent wrongdoing by persons who have a special relationship” with charities. Along with additional public disclosure requirements, the Taxpayer Bill of Rights 2 imposed taxes on a class of individuals who engaged in a transaction with the charity that unreasonably benefited the individual. These taxes are labeled intermediate sanctions, and target excess benefit transactions between the charity and disqualified persons.

Revenue-sharing transactions such as those between charities and professional fundraisers resulting in a percentage division of funds raised may become part of intermediate sanctions law.

154. IRS Procedure and Administration Rule, 26 C.F.R. § 301.6104(d)-2 (2004). While it does not satisfy the “widely available” requirement due to a technical matter, Guidestar, in partnership with the IRS and the National Center for Charitable Statistics, maintains a database of approximately one million charities’ information returns. See http://www.guidestar.org. The Supreme Court examined a copy of VietNow’s IRS Form 990 as part of its decision. Illinois ex rel. Madigan v. Telemarketing Assocs., Inc. 538 U.S. 600, 607 n.1 (2003).
157. “The sanctions are considered intermediate because they are between the choices of revocation of tax-exempt status and inaction on the part of the IRS.” HOPKINS, supra note 155, at 3. An excess benefit transaction is one in which the economic benefit to the disqualified person exceeds the value of consideration received for providing the benefit. 26 U.S.C. § 4958(c)(1) (2004). A disqualified person is one “in a position to exercise substantial influence over the affairs of the organization.” Id. § 4958(f)(1). The full scope of this complex regulation is beyond this note. See generally HOPKINS, supra note 155.
158. See HOPKINS, supra note 155, at 149-50, 157-58 (describing the history of
While the IRS does not consider fundraising percentage fee arrangements to be excess benefit transactions \textit{per se}, future proposed rulemaking could target such transactions. By focusing on the private benefit to the fundraiser, rather than the language used to perform the fundraising, the IRS may be able to succeed where state regulators have failed. Rather than assume that a contract with a professional fundraiser with high fees is presumptively fraudulent, such a transaction could be presumptively one of excess benefit. The resulting regulation could have the same effect to regulate fundraising fees, but without involving prior restraints on the protected speech of the charities.

V. CONCLUSION

After \textit{Riley} it may have been unclear what options remained available to regulators who sought to protect the public from fraudulent charitable solicitation. Over the years between \textit{Riley} and \textit{Telemarketing Associates}, fraud actions and mandatory disclosures have worked together to provide the best means for regulating this area. Neither fraud actions nor most mandatory disclosures run afoul of the First Amendment in the same manner as broad prohibitions or strict licensing. The world has changed since \textit{Riley}. The widespread availability of information about charities has created a more informed donor, while abuses continue to attract the media and legislators. Charities and professional fundraisers face continued scrutiny over their fundraising and solicitation practices, but this is done in the hopes of maintaining a charitable sector that continues to attract donations by being open, effective, and accountable.

\footnote{revenue-sharing rulemaking and its application in the fundraising context).}

\footnote{HOPKINS, \textit{supra} note 155, at 149-50.}