



The Attorney General and Nonprofits

University of Missouri-St. Louis

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Ask questions!
Interrupt freely!



The Attorney General's Mission & The Public's Interest

- The Attorney General oversees all charitable entities and solicitations in Missouri
 - The Attorney General is the guardian of charitable trusts and assets.
 - In short, the Attorney General can pursue almost every violation of the laws governing nonprofits.
- Goal: Strengthen Missouri's nonprofit sector
 - Of course, we need to use our unique powers



Attorney General's Mission

1. An efficient and successful nonprofit sector is absolutely essential to Missouri's well-being
 - What we do supports that goal
2. We believe the nonprofit sector represents some of the best people and ideas in Missouri
3. You do an incredible job – does not get said enough.



Attorney General's Powers

1. Nonprofit corporations, Chapter 355, RSMo
 - Require or stop a particular action, § 355.141
 - a/k/a *Ultra Vires*
 - Includes violations of federal law
 - Remove Directors, § 355.356
 - Includes breach of duty
 - Dissolve the corporation, § 355.726
 - Other actions to remedy violations of law
2. Charitable Trusts, Chapter 456, RSMo
 - Remove Trustees, § 456.10-1001
 - Action for breach of fiduciary duty
 - Necessary party for modification, termination, etc.
 - Other actions, common law is quite broad.



Attorney General's Powers

3. Attorney General oversees charitable solicitations
 - As Guardian of Charitable Assets, and
 - Under Missouri Merchandising Practices Act, Chpt 407, RSMo (*aka* consumer fraud laws).
 - Aggressively pursue fraudulent solicitations and other deceptive practices.
 - Maintain registration of nonprofits and professional fundraisers who solicit donations.
4. Endowment Funds, Chpt. 402, RSMo
 - Stop mismanagement of endowments



Attorney General's Powers

More practical list

- Commence investigations
 - Review all records
 - Interview anyone
- Take action against just about anyone who has acted illegally
- Remedies are as broad as our powers
- Federal law counts too
 - Ultra vires act
 - Reference for what is reasonable conduct



What happens when the Attorney General gets involved?

- We want to cooperate
 - Will want information, and expect to get it
 - Will give you an opportunity to respond before we take drastic or aggressive action
 - There are exceptions
 - Egregious violations
- The best way to make the Attorney General go away is to cooperate fully.
- Goals: Rehabilitate, Remove, Punish



What causes AGO involvement?

- Policy goal: Protect the integrity of the sector and maintain donors' faith in nonprofits
- More Practical Goals:
 - Recover diverted or misapplied assets (and stop the activity that led to the diversion)
 - Prevent nonprofits from ceasing to serve their communities
 - Stop fraudulent solicitation activity
- Constantly triage cases and priorities
- How do we choose? Top 10 list is below



Top 10 ways to get investigated

1. Clear failure to follow mission
2. Conflicts of interest
3. Fraud and Embezzlement, failing to respond and prevent
4. Paying excess compensation
5. Failing to operate with the needed transparency.



Top 10 ways to get investigated

6. Directors & Senior leadership failing to be sufficiently active
7. Not filing what you should with government agencies.
8. Violate fundraising laws.
9. Misusing your endowment and restricted assets.
10. Convert from Nonprofit to For-Profit



Top 10 ways to get investigated

5 more for charitable trusts

1. Excess compensation and fees (covered in #4 on Top 10 list)
2. Self-dealing (#4)
3. Failure to distribute sufficient amounts (#1)
4. Distributing to incorrect beneficiaries (#1)
5. Poor investments (#9)



#1 Failure to follow mission

“asleep at the wheel”

- Have a duty to actively work towards fulfilling your mission
 - Can you say what your organization does?
 - Examples: the animal shelter and the micro-lender
- Best practice: should have tangible, critical assessments of efficiency and program successes.
- Bad excuse #1 “Technically, it's legal.” (but what will your donors and constituents say).



#2 Conflicts of interest

- A nonprofit corporation should be above reproach.
- If any transaction gives even the appearance of a conflict of interest, it should be avoided.
 - Would the media and your Mom understand?
- Includes any person you would call an insider or family members.
- IRS, donors, media, and the general public all have different views of conflicts.
 - None are good
- Law ≠ public perception



Conflict of Interest

Legal definition

- A conflict of interest transaction is a transaction with the corporation in which a director of the corporation has a material interest. § 355.416, *RSMo*
- A conflict of interest transaction is not voidable or the basis of imposing liability on a non-compensated director if the transaction was not unfair to the corporation or is approved by the board. § 355.416, *RSMo*



Conflict of Interest Approval of Conflict

- A transaction in which a ***non-compensated director*** has a conflict ***may*** be approved in advance if the board, excluding the director with an interest, votes to approve, believes in ***good faith*** that the transaction is not unfair and ***all material facts are known***. § 355.416, RSMo
 - *Emphasis added*
 - It is still a bad idea



#3 Fraud and Embezzlement, Failing to respond and prevent

- Nonprofit corporations, and their directors, have a fiduciary duty to protect their assets.
- Why important?
 - They're stealing from you!
 - Overall cost, sector-wide, was \$40 billion for 2006, or some 13% of the roughly \$300 billion given to charity that year. (Source: NY Times, March 29, 2008)
- Many, many organizations are victims and do not know it



#3 Fraud and Embezzlement, Failing to respond and prevent

- You are vulnerable
 - Embezzlement can happen to you
- Examples:
 - Nancy O'Donnell sentenced on January 24, 2013 for embezzling \$209,000 from the St. Vincent de Paul Society at St. Joseph's in Cottleville. Source: stltoday.com 1/25/2013
 - Fred W. Robinson convicted of embezzling from Paideia Academy on March 27, 2013. Source: stltoday.com 3/27/2013
 - These are just the ones charged and reported



#3 Fraud and Embezzlement, Prevention: What I tell nonprofits

Must take all reasonable steps to prevent

1. Depends on organizational size
 - Even the smallest organizations **MUST** take steps
2. What would Mad Eye Moody do?
 - Constant Vigilance!
 - Culture and small steps go a long way
 - Discuss and create policies.
3. Remember, audits are generally not designed to catch fraud.





#3 Fraud and Embezzlement, Prevention, basic steps I tell nonprofits

- **Culture** is most important
 - Internal tips find most fraud
- **Systems** that are replicable, repetitive procedures that produce predictable results.
 - Internal controls
 - Policies and procedures
 - Checks and balances
- **Oversight** (hard to do too much)
 - Financial reporting
 - Feedback loops



#3 Fraud and Embezzlement, Response

- Embezzlement will happen to someone here.
- Must take all reasonable steps in response
 1. Punish offender
 - 72% of nonprofits frauds resulted in termination
 - 6% of nonprofits DID NOTHING, *source: Greenlee, et al. An Investigation of Fraud in Nonprofit Organizations*
 2. Report to law enforcement (and cooperate!)
 3. Get your money back
- Close whatever hole was exploited
 - Use opportunity to strengthen your organization
 - ACORN example



#3 Fraud and Embezzlement, failing to respond and prevent

- Bad excuse #3 “We completely trusted _____”
- Bad excuse #3A “We didn’t want our donations to suffer, so we didn’t tell anyone”
- Bad excuse #3B “We thought our auditor would catch that”
- Not a coincidence that #3 has the most bad excuses!



#4 Paying Excess Compensation

- All of your assets must go to your charitable purposes, and compensation must be reasonable.
- Everything should be reasonable and justified
- Avoid paying substantially more than similar organizations and lavish expense accounts.
 - Remember IRS excess compensation rules
 - Expense accounts matter
- Bad excuse #4 “We had left over money so figured we would go to Vegas, buy a Vette, etc.”



#4 Paying Excess Compensation

Part 2

- IRS forbids “excess benefit transactions”
 - Any transaction in which a nonprofit insider receives more than they should have for a particular task or service.
 - Can be taxed at 200% of the value received.
- Independent Contractors’ compensation must also be reasonable
 - Professional fundraisers who charge a high percentage of funds raised are red flags



#5 Failing to operate with the needed transparency.

- Donors and the Public expect complete transparency
 - Expectations get higher and higher
 - Remember the over-sharing friend on Facebook/Twitter/etc.
- Top complaint generator
 - People will leap to conclusions if lack information
- Best Practice: A nonprofit should operate with as much transparency as possible
 - All records should be open AND easily accessible.
 - Example: all minutes, financial statements, and Form 990's should be posted online



#5 Failing to operate with the needed transparency.

- The Law (and not necessarily Best Practices)
 - Law: Missouri statutes list required corporate records and inspection rights for members
 - Sections 355.821 – 355.841, RSMo
 - Law: Directors get everything
 - IRS: Make Forms 990 and 1023 publicly available
 - Law = bare minimum
 - The public expects much more than the law requires.
 - Will run out of donors and have embarrassing headlines
- *Law is not reflective of current donor expectations*



#5 Failing to operate with the needed transparency, example

- Nonprofit created to support Agency on Aging
 - (c)(3) pass-through + own real estate
 - Poorly drafted operating agreements + separate management
- NP refused to provide regular updates on donations and details about real estate to Agency on Aging
- Agency on Aging comes to Attorney General
 - Not sure what is going on, money is going into black hole, can't get info, think CEO/ED is stealing...
- AG investigates
- Zero laws broken but:
 - NP is now dissolved
 - CEO/ED had horrible press



#6 Directors or Senior leadership failing to be sufficiently active

- Directors have a fiduciary duty to be active and obtain sufficient information to make informed decisions.
- Directors must understand the organization's financial health.
- There must be regular reporting to the Board.
 - The directors must know all of the nonprofit's activities
 - Directors must actively seek the information they need.
 - Ask questions!!!!!!
- Bad excuse #6 “We're a volunteer board and don't have the time to _____.”



#6 Directors or Senior leadership failing to be active - example

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Monday, May 17, 2010 | Modified: Tuesday, May 18, 2010

KCUMB claims former CEO Pletz fraudulently obtained stipends

Kansas City Business Journal - by [Mike Sherry](#) Staff Writer

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[Stanton resigns from Kansas City University of Medicine and Biosciences](#)

[Arts Council of Metropolitan Kansas City misses fund-raising goal](#)

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Kansas City University of Medicine and Biosciences says it may have overpaid nearly \$1.5 million in salary stipends to its former CEO, Karen Pletz.

The revelation came as part of the school's most recent tax

A portrait of Karen Pletz, a woman with short blonde hair, wearing a dark top.

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Kansas City University of Medicine and Biosciences sues its former president, alleging fraud, mismanagement

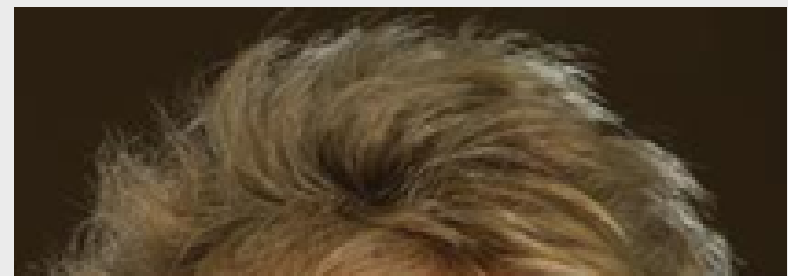
Kansas City Business Journal - by Mike Sherry, Staff Writer

Date: Monday, March 22, 2010, 10:50am CDT - Last Modified: Tuesday, March 23, 2010, 10:08am CDT

Related: [Health Care](#), [Education](#)

The former president of Kansas City University of Medicine and Biosciences systematically defrauded the university out of millions of dollars for a decade, the school alleged in a civil suit filed Monday in Jackson County Circuit Court.

[Enlarge Image](#)



Grand jury indicts Pletz in alleged \$1.5M fraud

Kansas City Business Journal - by Steve Vockrodt, Staff Writer

Date: Thursday, March 31, 2011, 10:21am CDT - Last Modified: Thursday, March 31, 2011, 2:37pm CDT

Related: [Banking & Financial Services](#), [Health Care](#), [Insurance](#), [Education](#), [Legal Services](#)

A grand jury has charged **Karen Pletz**, former CEO of [Kansas City University of Medicine and Biosciences](#) [+](#), with money laundering and filing fraudulent tax returns, among other charges.

A grand jury returned 24 criminal counts against Pletz, who ran KCUMB from 1995 until her [abrupt termination in December 2009](#), all of which relate to an alleged scheme to obtain more than \$1.5 million from the osteopathic university.

TIMELINE: [See a timeline of the events concerning Pletz](#)

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MARKETPLACE OF IDEAS

So where was the board during the KCUMB-Pletz debacle?

 Premium content from Kansas City Business Journal - by Michael Braude, Contributing Writer

Date: Sunday, April 25, 2010, 11:00pm CDT - Last Modified: Thursday, April 22, 2010, 6:33pm CDT

Related: [Education](#)

A number of people have asked me: "Why don't you write a column about the debacle at the Kansas City University of Medicine and Biosciences and its embattled former president?"

Frankly, an awful lot already has been written in this paper and others about the unfortunate situation surrounding Karen Pletz.



[Enlarge Image](#)

Michael Braude



#7 Not filing what you should with government agencies

- 3 core filings:
 1. Internal Revenue Service: Form 990
 - States review the revocation lists
 2. Secretary of State: Annual report
 3. Attorney General: Registration
 - If your nonprofit solicits donations (will cover in #8)
- Basic, but important
 - Illustrates the digital fishbowl nonprofits operate in



#7 Not filing what you should with government agencies, part 2

- Why important?
 - Severe sanctions from agency
 - Donors, potential donors, clients, and everyone else all see lack of filing.
 - All information is just a click away
 - Public will misinterpret
 - Will harm your digital footprint
 - Rating sites: BBB, Charity Navigator
 - 990 sites: Guidestar, Foundation Center
 - Online giving platforms: First Giving, Crowdrise, etc.



Actual text of email I received

It has come to my attention that the [name] has had it's not for profit status revoked by the IRS !!! Yet they are collecting funds for Joplin and just recently had a fund raising for Haiti!!!!???????????? PEOPLE NEED TO BE AWARE THAT THE MONEY THEY ARE GIVING AND HAVE GIVEN THIS PAST YEAR IS NOT TAX DEDUCTIBLE!!!! Anyone with an estate or any amount of money NEEDS TO BE AWARE THAT THEY WILL HAVE TO PAY TAX ON THE "DONATION". I believe that the law states that they cannot continue to act like they are not for profit as this fraudulently represents their position!!! ALL their [donors] need to be made aware of this!!



#8 Violate fundraising laws

1. Failure to register

- If you solicit donations, you may need to register

2. Misrepresentations in solicitations

- Obviously, misrepresentations in soliciting donations are forbidden

3. Violation of Do-Not Call rules

- Surprisingly easy to violate
- All are violations of Missouri's consumer fraud laws (Chpt. 407, RSMo)



#8 Violate fundraising laws

Who needs to register

1. All charitable organizations that solicit donations

- Definition: Any person or entity who solicits funds for any charitable purpose. § 407.453(2)
- Many exceptions (see next slide)

2. All Professional Fundraisers

- Definition: anyone compensated by a charitable organization primarily for the purpose of soliciting funds. § 407.453(4)
- Does NOT include: bona fide employees who receive regular compensation and aren't primarily employed for the purpose of soliciting funds. § 407.453(4)
 - Salaried development directors are usually exempt
- Few exceptions here



#8 Violate fundraising laws

Who does NOT have to register (§ 407.456.2)

1. Organizations recognized under § § 501(c)(3), (c)(7) or (c)(8)
 - Only in Missouri, other states still require registration
2. **Religious organizations**
3. **Educational institutions** (and their related foundations)
 - An institution with a defined curriculum, student body and faculty, and which conducts classes on a regular basis
4. **Fraternal, benevolent, social, and historical organizations,**
 - When solicitation is confined to the membership
5. **Hospitals**
 - Provided all fund-raising activities and solicitations are carried on by employees and not by any professional fund-raiser.



#8 Violate fundraising laws

How to register

- In Missouri
 - Fill out forms and mail in
 - www.ago.mo.gov/checkacharity/charityregistration
 - Contact Donna Rodenbaugh
 - 573-751-1197
 - donna.rodenbaugh@ago.mo.gov
- Other states
 - Contact them!



#8 Violate fundraising laws Other States

- Other states have different requirements
 - Most require 501(c)(3)'s to register
 - Missouri requires little compared to others
- Just because you've satisfied Missouri, does **NOT** mean you're registered elsewhere.
- Consequences may be severe.
 - On September 2, 2008 Pennsylvania obtained a judgment of over \$1,290,000 for failure to register



If my nonprofit solicits online, where do we need to register?

- States created the Charleston Principles
 - Written in 2001, i.e. well before Mark Zuckerberg got shot down on a date, went back to his dorm, and created Facebook while drinking away his sorrows
 - Thus, language only addresses static websites
- Principles are still good, need to register if:
 1. In state where your nonprofit is *domiciled* (HQ, etc.)
 2. In other states if:
 - A. **Specifically target** persons physically located in the state for solicitation, or
 - B. Receives contributions from the state on a repeated and ongoing basis or a substantial basis



The Charleston Principles in 2013

- What is “specifically target”?
 - Posts on Twitter, Facebook, etc.
 - Software platform, i.e. First Giving, Crowdrise, changingthepresent.org
 - Platform (aka conduit)
 - Those who use platform

Note: examples are good sites (if they were in trouble, they would NOT be listed).



Have an account? [Sign in](#)



American Red Cross

American Red Cross

@RedCross

Official twitter stream for the American Red Cross. Follow us for disaster and preparedness updates.

Washington, DC · <http://www.redcross.org>

Follow

2,370 TWEETS

35,648 FOLLOWING

757,289 FOLLOWERS

Down the street. Across the country. Around the world.™

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American Red Cross @RedCross

3h

If you need to evacuate, use official travel routes&bring emerg. kit. More tips in [#Hurricane](#) app 3cu.be/hc2 [#Isaac](#)

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American Red Cross @RedCross

9h

Last night, more than 4,700 people were in [@RedCross](#)-run or supported shelters across 7 states. [#Isaac](#)

[Expand](#)



American Red Cross @RedCross

29 Aug

We need your help. [#Isaac](#) is a large relief effort. Donate: rdcrss.org/PSpvi2 or text REDCROSS to 90999. TY

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American Red Cross @RedCross

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MT [@DudeLikeTotally](#) According to [@RedCross](#) ur not supposed to use candles if power goes out during a hurricane



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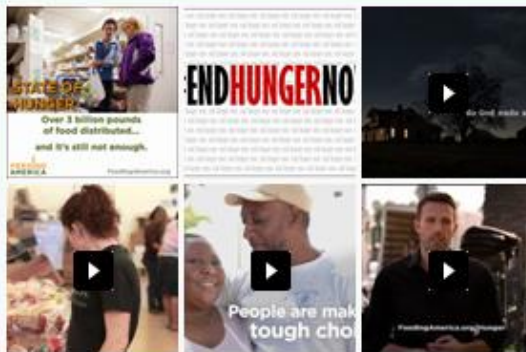
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STL Area Foodbank @STLFoodbank

55 mins

A new film, "A Place at the Table" opens today at the Tivoli. Very moving, inspiring film on hunger in America. ow.ly/ibdSI

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Feeding America @FeedingAmerica

3 hrs

RT @HuffPostImpact: What is the #sequester anyway? And how does it affect those most in need? huff.to/149KOut

Retweeted by STL Area Foodbank

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2 hrs

MO Foundation for Health #MFH awards \$1 million to

@STL Foodbank! ksdk.com/news/water.cnn via @ksdknews



SPECIAL OLYMPICS DELAWARE

2013 Pooch Plunge 2/2/2013 Rehoboth Beach, Delaware

- Email
- Share
- Tweet
- Post
- Like
- 0

Donate

\$500 goal | **\$775** raised so far

155 % to goal



Polar Bear Pam Notarange

\$20,495 raised for 1

nonprofit

Fundraising

2013 Lewes Polar Bear Plunge for Special Olympics

2/3/2013 | Delaware

2013 Pooch Plunge

2/2/2013 | Delaware

PAST 2012 Lewes Polar Bear Plunge for Special Olympics

2/5/2012 | Delaware

see all pages

Activity



Polar Bear Pam joined FirstGiving 6 years and 1 month ago (January 2007)

see all activity

- Story
- Nonprofit
- Event

Jamie Girl Polar Dog

03FEB2013 UPDATE:

I DID it. Piece o' cake, even though the temp was 23F. My Mommies say they were very proud of me! Well... I'm very proud of your generosity!!!!

THANK YOU VERY VERY MUCH for supporting my Mom & me!

JamieGirl

Polar Dog



JamieGirl Warfield-Notarange

Thank you for visiting my fundraising page!

My Mom has participated in the Polar Bear Plunge for many years. I'm happy to say that now I TOO am joining the efforts to support





#8 Violate fundraising laws

Part 2: Misrepresentations in solicitations

- Obviously, misrepresentations in soliciting donations are forbidden
- But can be easy to do, especially with untrained solicitors or over-eager volunteers.
 - % to charity, purpose of donation, how donation will be used, etc.
 - Incorrect response may be a misrepresentation.
- Penalties can be severe
 - Criminal sanctions are possible, ex: *State v. Richard Divers*



Who is responsible when deceptive acts happen in online solicitations?

- Your nonprofit could have an online volunteer go rogue, or stretch the truth on your behalf.
- Or if you are a pro fundraiser, a rogue could misuse your online services.
- When are you responsible?
 - Actual knowledge of fraudulent misuse = in trouble
 - FTC v. Neovi, 604 F. 3d 1150, Defendant engaged in an unfair practice thru its online services when it "engaged in a practice that facilitated and provided substantial assistance to a multitude of deceptive schemes."
 - Means you must take some action to prevent being used as a facilitator for deceptive schemes.



Need to do something, but what?

- The specific actions depend on what you do, but would suggest these four guideposts
- You need a system that:
 1. Stops basic misuse automatically
 - Ex: (c)(3) verification, if a pro fundraiser
 2. Detects more sophisticated attempts at fraud or misuse
 3. Requires some active effort by you
 - no head in the sand
 4. Fixes flaws as they become known
- Please cooperate with law enforcement



#8 Violate fundraising laws

C. Violation of Do-Not Call rules

- § 501(c)(3)'s are exempt from many Do Not Call laws.
- **BUT** everyone is subject to federal Telephone Consumer Protection Act, which forbids:
 - Calling a person when:
 - They have advised caller of desire not to be called
 - They have advised caller of non-interest in making donation
- State of Missouri can enforce
 - \$5,000 penalty per violation
 - Recent settlement of \$100,000, have gone up to \$500,000
- All rules now apply to cell phones too



#9 Misusing your endowment

(assuming your nonprofit still has one)

- Must follow restrictions on donations
 - Attorney General can enforce
 - Donors can choose to not give
- Must prudently invest
 - Duty to diversify assets
 - Don't put your eggs in one basket (or auction rate securities)
 - Example: Mortgage backed securities were once viewed as very safe
 - Duty to prudently invest
 - Invest assets with all reasonable skill, care and caution
 - Review ALL investments, especially in a turbulent market
 - Duty to minimize costs
 - Duty to supervise investments and investors
 - Why? One word: Madoff

[←](#) [→](#) [http://www.joplinglobe.com/local/x803553103/Attorney-general-to-review-use-of-fund-money-for-concert-loan](#)

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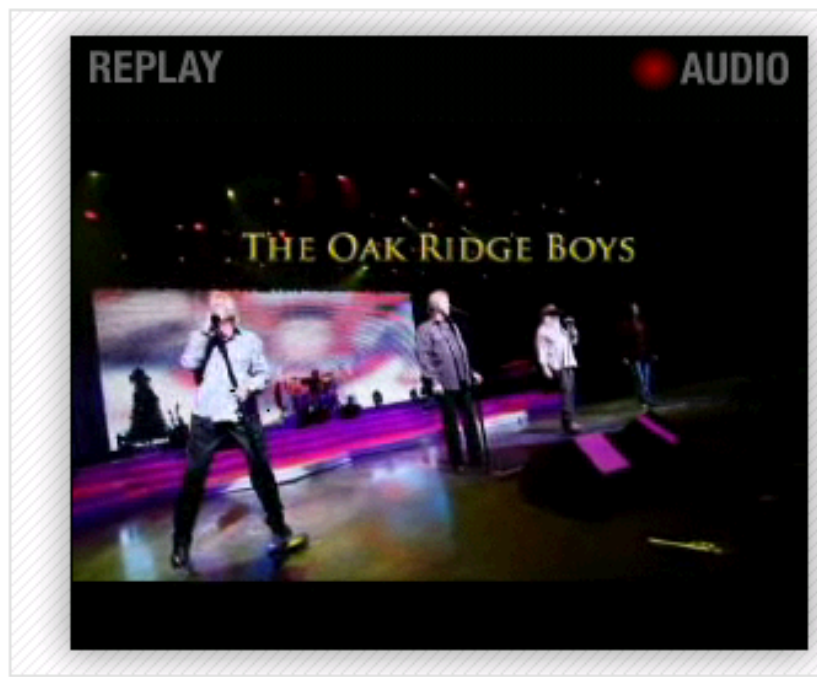
September 12, 2011

Attorney general to review use of fund money for concert loan

By Debby Woodin
 news@joplinglobe.com

JOPLIN, Mo. — Complaints by Joplin residents about the city borrowing from a Joplin tornado recovery fund to seed a 9/11 concert has prompted the Missouri attorney general's office to review the arrangement.

"We did receive some calls about the concert, so we are reviewing the situation," said



Discussion



Active and engaged boards are the only way to assure rational and informed decision-making.

But a law could read like this:

- Section 1. Board members cannot suggest that the institution invest in funds or assets that they learned about in the locker room or on TV.
- Section 2. Boards should not sit in dark rooms watching PowerPoint presentations by consultants while eating morning buns and sipping coffee.
- Section 3. Board members should not be permitted to brag about how their institution placed money with a hot money manager.
- Section 4. Membership on an institution's investment committee doesn't give the member the right to experiment with or test a new investment theory that the member wants to apply to his personal investments.
- Section 5. Just because an institution has high-paid in-house investment managers does not mean those investment managers should be setting the risk parameters.
- Section 6. Maximizing return cannot be an end in itself. Return should be maximized in light of pre-defined risk tolerances.

From: Jack Siegel, March 12, 2009, www.charitygovernance.com



#10 Convert from Nonprofit to For-Profit

- Assets committed to nonprofit causes must remain so.
 - Generally, can't convert from nonprofit to for-profit.
- Must notify the Attorney General of fundamental changes 20 days in advance
 1. Dissolution
 - When dissolving all assets must go to other nonprofits
 2. Merger
 3. Sale or transfer of “substantially all” assets (+ 51%)



#10 Convert from Nonprofit to For-Profit Asset Sales or Transfers

- Take duty quite seriously
 - Rather intense review for larger transfers
 - Health assets even more so
 - Have reviewed 10,000 pages and had public hearings for medium-sized transactions
 - Larger transactions will take more time
- Reviews are unique but look at 3 core issues
 1. Price – is the sales fair?
 2. Process – was process used legally sufficient?
 3. Proceeds – what will the proceeds be used for?



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