

For Goodness Sake: Legal Regulation and Best Practices in the Field of Cause-Related Marketing

By Edward B. Chansky

The marketing department sends you the following ad copy to review: “Buy our product and a portion of the proceeds will go to charity.” What do you do?

You have just entered the world of “cause-related marketing,” the technique of linking marketing with a social cause. This article provides an overview of cause-related marketing, the regulatory framework for this fast-growing field, and practical suggestions for compliance and best practices (including how and why you should change the ad copy proposed above).

Background

Modern cause-related marketing started in 1983 when American Express offered to support the Statue of Liberty Restoration project with one cent for every card transaction and \$1.00 for every new card issued. The program was a huge success. Over a period of 4 months, the company donated almost \$2 million, consumer card usage grew by 27%, and new applications increased 45%.¹

Since 1983, cause-related marketing has grown into a popular strategic marketing and public relations tool for corporations and charities alike. A leading nonprofit example is Susan G. Komen for the Cure, the breast cancer awareness organization whose pink-themed messages accompany products nationwide. Among businesses, notable examples abound: Paul Newman built his “Newman’s Own” food company around the idea of donating profits to charity; “Project Red” has become a global brand licensed by major companies such as Apple, Giorgio Armani, the Gap, and many others to help fight AIDS in Africa; and Coke and Pepsi both launched major cause-related initiatives to coincide with the 2010 Super Bowl.²

Today, economic and social realities demand that companies and brands act as good corporate citizens. Cause-related marketing supports that goal. It’s also good business. Studies show that sizable numbers of consumers may change purchasing behavior to select products and services associated with causes they care about.³

Contemporary cause-related marketing takes many forms, such as requesting customer donations at checkout, auctioning special items online, walkathons, inviting consumers to “vote” for charities to receive grants, and more. The primary technique, however, remains selling a product or service with a promise to make a donation. This technique is the focus of the discussion below.

Regulatory Framework

Cause-related marketing triggers issues under state commercial co-venturer (“CCV”) laws, federal tax laws, Better Business Bureau (“BBB”) Standards, and federal and state laws governing false or misleading advertising.

Commercial Co-venturer Laws. Approximately 20 states have CCV laws. New York’s statute is fairly representative of the majority definition of a CCV:

Any person who for profit is regularly and primarily engaged in trade or commerce other than in connection with the raising of funds or any other thing of value for a charitable organization and who advertises that the purchase or use of goods, services, entertainment, or any other thing of value will benefit a charitable organization.⁴

The two key elements are: (a) the offer for sale of a product or service, (b) based on a representation that the purchase will benefit a charity. Some states’ laws can apply where the advertiser promises to support a cause (*e.g.*, “cancer research”) without naming a specific charitable organization.⁵ At least one state does not even expressly require sale of a product or service in its definition, but rather only that a company use the name of the charity in connection with advertising a product or service.⁶ Regardless of specific wording, CCV laws generally share a common purpose to protect consumers and charities against fraudulent or misleading advertising, and to help assure that promised donations get delivered to the proper place.

Requirements for Commercial Co-venturers. The CCV laws are triggered by representation made to the public—*i.e.*, advertising that a purchase will benefit a charitable organization or purpose. As with most regulation of advertising, local laws apply in each state where the offer is made to the public. Nationwide cause-related marketing campaigns therefore must comply with the laws in all 50 states.⁷

The basic requirements are as follows:

- *Written contract with the charitable organization.* Approximately 20 states require a contract. Some specify certain provisions for the contract. A partial list of such provisions includes: accurate description of the offer to be made to the public, the charity’s right to an accounting of the program results, termination rights for the charity, citation to the state’s laws, an

estimate of the total donation, and signature by two officers of the charity.⁸

- **Per-Unit Disclosure of Donation Amount.** Approximately 11 states require ads to disclose the amount of the donation, on a per-unit basis, typically either “as a dollar amount or as a percentage of the value of the goods or services purchased or used.”⁹
- **Disclosure of Beneficiary.** If applicable, the name of any benefiting charity, contact information for that organization, and the purpose for which the donated funds will be used are required disclosures.¹⁰
- **Registration and Bonding.** A CCV has a duty to register, post a bond, and file an annual report in Maine, Massachusetts and Alabama; Illinois requires registration and annual reporting as a “charitable trust”; South Carolina and Hawaii require a simple notice of the promotion.¹¹ The charity has a separate duty to file a copy of the contract in a few states, and also to be registered for general fundraising purposes in all states with general charitable solicitation registration laws (there are approximately 40).¹²

While the requirements may sound daunting, compliance is not difficult. A contract would be desirable even without the CCV laws. Clear disclosure of the actual amount going to the charity is desirable as a matter of truthful advertising. And state CCV registrations, while awkward, can often be handled by knowledgeable counsel for a cost of about \$5,000 for a national program.

Professional Fundraiser Laws. In addition to CCV laws, many states also have statutes regulating “professional fundraisers.” Again, the New York statute is representative of the general definition:

Any person who directly or indirectly... for compensation or other consideration plans, manages, conducts, carries on, or assists in connection with a charitable solicitation or individually solicits or who employs or otherwise engages on any basis another person to solicit in this state for or on behalf of any charitable organization....¹³

The primary distinction from a CCV is that a professional fundraiser solicits contributions separate and apart from the regular retail price of a product or service, and does so for compensation.

Most cause-related marketing programs normally will not be deemed covered by the professional fundraiser statutes. If not designed carefully, however, a cause-related marketing program could invite such regulation. A theoretical example arises if a company invites consumers to make donations, but the company accepts those donations only with a required purchase. In such a case, a regulator could argue that the company is soliciting (asking for a donation separate from the regular price of the product)

for compensation (only accepting donations when making a sale).

In the common case of a retailer inviting consumers to make voluntary donations at checkout *without* any purchase required, the retailer typically will be viewed as a non-regulated volunteer, *provided* that (a) the retailer is not compensated in any way, and (b) 100% of the donated funds are given to the charity. If either of these two conditions is not satisfied, then the risk of being deemed a professional fundraiser increases. In addition, if the retailer handles the money (as distinguished from consumers depositing donations in locked boxes opened only by the charity), the states of Illinois and Massachusetts could apply their “charitable trust” or CCV laws even though no product is being sold.¹⁴

A company should avoid being deemed a professional fundraiser. The laws are much stricter than for CCVs, including much more extensive contracting, registration, bonding and disclosure requirements in several states.¹⁵

Better Business Bureau Standards. BBB Standard 19 establishes disclosure guidelines similar to those under the CCV laws, including disclosure of the per-unit amount of the donation as “the actual or anticipated portion of the purchase price that will benefit the charity (e.g., 5 cents will be contributed to abc charity for every xyz company product sold),” the time period during which the offer is valid, and whether any overall maximum or minimum applies to the contribution (e.g., up to a maximum of \$200,000).¹⁶

Proposed Multistate Consumer Law Guidance Principles. In 1999, the Attorneys General in 16 states plus the District of Columbia proposed guidelines for cause-related marketing. The proposals were made largely in response to perceived abuses of charity names in advertisements for commercial products, particularly where the charitable organization (often a health-related group) appeared to be endorsing or approving a commercial product when such endorsement or approval was not true. Key concepts under the guidelines include disclosing the financial relationship between the advertiser and the charity, avoiding misrepresentation of endorsement by the charity, and not misleading consumers as to the effect purchases will have on any donation.¹⁷

The proposed guidelines do not have the force of law. However, they provide insight into the types of practices likely to trigger concern under general laws governing false and deceptive advertising. The most important guideline for traditional cause-related marketing is to avoid misleading consumers as to the effect a purchase will have on any donation, which is discussed in the next section.

Common Problems in Cause-Related Marketing

The Flat Donation. The company agrees to give a fixed amount to the charity. The amount does not depend on the number of sales. Yet the advertising tells consum-

ers that each purchase results in a donation. This situation should be avoided. It misleads consumers as to the effect a purchase will have on the donation. A more appropriate form of advertising would be to simply say that the company is a proud sponsor of the charity and to disclose the gross amount of the donation. Consumers can then decide whether they think the fact of the donation is a reason to purchase the advertiser's product. A further advantage of this approach is that it generally avoids the need to comply with CCV laws.

Caps and Minimums. The accurate, per-unit donation amount is disclosed in the advertising, but the total donation is subject to either a cap (e.g., "up to \$200,000"), a guaranteed minimum, or both. Common sense and BBB Standard 19 both dictate disclosure of any applicable maximum or minimum. But is such disclosure enough? It depends. For a cap, if the offer continues to be communicated for a substantial time after the cap is reached, anyone purchasing later may be misled as to the effect his or her purchase may have on the donation. For a minimum, if the threshold is well above anticipated sales, consumer action may be irrelevant to the donation.

This is not to say caps and minimums are prohibited. Instead, the advertiser should seek to establish a reasonable fit between the scope of the offer and the disclosed maximum or minimum. For a maximum donation, the fit might involve controlling inventory to create only a limited number of qualifying, specially marked packages so that the maximum cannot be exceeded, or using historical sales information to make the offer valid only for a limited time period in which an appropriate sales level is likely to occur. For a minimum donation, the floor should not exceed anticipated sales. Such precautions—together with transparent disclosure to the consumer—can generally avoid problems with a maximum or minimum donation.

Vague Disclosure. A typical reason to promise a donation with purchase is to induce a purchase. As noted above, many consumer purchase decisions are likely to be influenced by such promises.¹⁸ Given these facts, a regulator can credibly argue that the public is entitled to know exactly how much money goes to the charity for each purchase. For example, a consumer likely cares if the donation is \$1.00 vs. one-ten-thousandth of a penny. Were it the latter amount (and if the consumer knew), the consumer might not make the purchase. For all these reasons, disclosure of the donation amount in terms the consumer can easily discern or calculate is the recommended way to comply with the CCV laws and BBB Standard 19.

Advertisers, however, sometimes want to use vague disclosures, such as "a portion of the purchase price," "a portion of proceeds," or a designated percentage of "profits" or "net profits." Occasionally a vague disclosure is proposed because the actual per-unit donation amount can't be calculated accurately in advance. Other times the actual amount is known, but the advertiser worries that the

amount sounds too low to induce purchases. Regardless of the motive, the fundamental problem with a vague disclosure is that it lacks transparency. "A portion of the proceeds" could mean anything between zero and the full purchase price of the product. Even more troubling is where the advertising trumpets a generous-sounding percentage of profits (e.g., "50 percent of net profits") when the actual donation is a relatively or extremely small percentage of the purchase price. While such disclosure may be literally true, it further increases the risk that consumers may be misled as to the actual amount donated.

Practical advice for a "percentage" disclosure is to base the percentage on the retail purchase price of the product rather than on "proceeds" or "profits." If a profits-based formula must be used, then an additional disclosure should be added to disclose a minimum, per-unit amount to be donated for each purchase. Such disclosure establishes a baseline for consumer expectations. If the actual per-unit donation exceeds the disclosed baseline, no harm occurs to either the consumer or the charity.

The Charity's Perspective

When considering cause-related marketing, a company should bear in mind certain tax-related issues that affect the charity. Without an awareness of these issues, the company might not understand why a charity typically cannot agree to actively promote the sale of the advertised product or service, or the company may unknowingly lead the charity to engage in activity that could jeopardize the charity's tax-exempt status.

Unrelated Business Taxable Income. The major issue for charities is unrelated business taxable income ("UBTI"). UBTI arises when a tax-exempt organization engages on a regular basis in business activity unrelated to its charitable purpose. Actively promoting the sale of a commercial sponsor's goods or services—even if such sales help generate donations to the charity—is not normally considered part of a tax-exempt organization's charitable purpose, but rather rendering of advertising services that can potentially become taxable at standard corporate tax rates.¹⁹ Too much UBTI can result in loss of tax-exempt status.²⁰

An exception to UBTI allows a charity to publicly "acknowledge" a sponsor's support. Acknowledgement is typically a thank-you message that also may include a general reference to the sponsor's business and products, as well as contact information for the sponsor.²¹ Unfortunately, the line between "acknowledgement" and "advertising" is not always clear. The major earmarks of advertising include qualitative or comparative statements about a product, price information, indications of savings or value, or "*an endorsement, or inducement to purchase, sell, or use any company, service, facility or product.*"²² A thank-you message mentioning that each purchase of the sponsor's product benefits the charity can be viewed as an inducement to purchase, and thus a form of advertising. For this reason, sophisticated

tax-exempt organizations often will not agree to actively promote an advertiser's product or service in a cause-related marketing program. A conscientious advertiser may wish to consider whether the charity is aware of this risk when negotiating the terms of a cause-related marketing agreement to help avoid later misunderstandings or bitterness if the charity is subsequently audited by the IRS.

Self-Dealing. "Self-dealing" is an additional concern if the benefiting organization is the advertiser's own private charitable foundation. Stated simply, self-dealing occurs when a private foundation's assets are improperly used to benefit "disqualified persons," who include substantial contributors and their officers and directors, as well as officers and directors of the foundation. Ordinary cause-related marketing programs where the foundation merely allows the company to use the foundation's name on commercially reasonable terms, and the foundation receives donations passively without promoting or advertising the company's business, are unlikely to cause a problem. But the more active the foundation becomes in promoting the company's business, the greater the risk of a self-dealing problem. In addition, the terms of the relationship must be arm's-length, and preferably should be approved by independent board members of the foundation unrelated to the CCV. Penalties for self-dealing can include individual liability for the corporate officers involved in the transactions.²³ As a result, great care should be taken when implementing a cause-related marketing program between a company and its own charitable foundation.

What Should a Company Do?

To date, enforcement of the CCV laws has been lax. With the rapid growth of cause-related marketing, however, increased regulatory attention can be expected. The following are best practices to help minimize the legal risks in typical cause-related marketing programs:

- Sign a written contract with the charity, including any statutorily mandated provisions.
- Structure the promotion to avoid misleading consumers as to the effect purchases will have on any charitable donation.
- Review advertising carefully for transparent disclosure of the per-unit donation amount and compliance with applicable state disclosure laws and BBB Standard 19.
- Register and bond the program in any applicable jurisdictions.
- Confirm that the benefiting charity is registered for general fundraising purposes in all states where the offer will be made.
- Be sensitive to UBTI issues for the charity.
- Take care in structuring programs with your own corporate foundation to avoid return benefits that could be construed as "self-dealing" in the eyes of the IRS.

Cause-related marketing is here to stay. It is popular. It is growing. The legal regulation of this powerful advertising tool is not yet widely understood. With a little effort—and some help from experienced counsel—companies can safely engage in cause-related marketing for the mutual benefit of business and charity alike with minimal risk and cost. In short, you can do good while you do well.

Endnotes

1. See *Past. Present. Future. The 25th Anniversary of Cause Marketing*, Cone, Inc. <http://www.coneinc.com/research/index.php>.
2. See news report at <http://causeintegration.wordpress.com/2010/01/28/coke-launches-cause-marketing-campaign-to-rival-pepsi/>.
3. See *Past. Present. Future. The 25th Anniversary of Cause Marketing*, *supra*, note 1, and studies cited therein.
4. NY Executive Law § 171-a.
5. See, e.g., Conn. Gen. Stat. § 21a-190a (9) (defining "charitable sales promotion" as benefiting a "charitable organization or purpose").
6. See Mass. Gen. Laws, ch. 68, Section 18.
7. While international laws are beyond the scope of this article, it is worth noting that, apart from a few Canadian provinces, most foreign countries generally do not have specific "commercial coventurer laws" but instead regulate CCV-style offers primarily under laws governing false or misleading advertising.
8. See, e.g., NY Exec. Law § 174-a; Georgia Code § 43-17-6(a); Mass. Gen. Laws, ch. 68, Section 22.
9. See, e.g., Arkansas Code § 4-28-408(c)(2); Conn. Gen. Stat. § 21a-190g(c). NY Exec. Law § 174-c requires disclosure of "the anticipated portion of the sales price, anticipated percentage of the gross proceeds, anticipated dollar amount per purchase, or other consideration or benefit the charitable organization is to receive."
10. Mass. Gen. Laws, ch. 68, Section 23.
11. Alabama Code § 13A-9-71(h); Hawaii Stat. § 467B-5.5; 760 Illinois Compiled Stat. 55/6; 9 Maine Rev. Stat. § 5008; Mass. Gen. Laws, ch. 68, Section 24; S.C. Code § 33-56-70.
12. See list of states at <http://www.multistatefiling.org/index.html>.
13. NY Exec. Law § 171-a.
14. See 760 Illinois Stat. 55/3; Mass. Gen. Laws, ch. 68, Section 18.
15. See, e.g., NY Exec. Law § 173, *et seq.*
16. BBB Wise Giving Alliance for Charity Accountability, Standard 19.
17. "What's In A Nonprofit's Name?," Public Trust, Profit and the Potential for Public Deception, a Preliminary Multistate Report on Commercial/Nonprofit Product Marketing, April 1999.
18. See note 3, *supra*, and sources cited therein.
19. See 26 U.S.C. § 511 *et seq.*
20. See 26 CFR § 501(c)(3)-1(e)(1).
21. 26 CFR § 1.513-4(c)(iv).
22. 26 CFR § 1.513-4(c)(v) (emphasis added).
23. 26 U.S.C. § 4941.

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