Disclosure for Charitable Solicitors

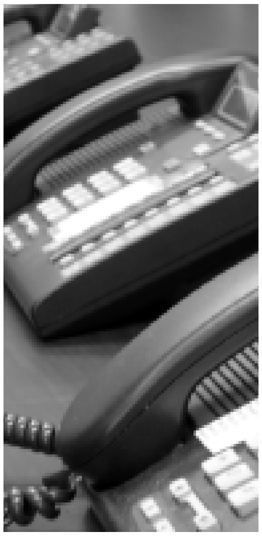
The FTC and state attorneys general pursue fundraising miscreants, but the sector hasn't stepped up to the task of honesty and accountability

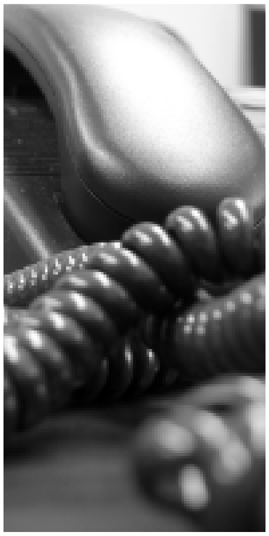
By Naomi T. Tacuyan

If you found out that only $15 out of the $100 you donated to a charity would ultimately make it to the charity, would you still donate? More importantly, wouldn't you want to know before making the decision to donate? How do you really know if your donation is being used the way telemarketers said it would be used? Charitable telemarketing has been an issue over the past several years. Not only are these cases of charity-hired solicitors deliberately misleading donors, but the media and state governments have raised concerns about scandalously low return rates for the charities themselves. A case that exemplified many charitable soliciting scenarios and that is a benchmark for this debate is *Madigan v. Telemarketing Associates*.

Madigan v. Telemarketing Associates: Free Speech or Fraud?

First Amendment rights versus fraud. That was the battle fought in the U.S. Supreme Court almost two years ago in the case *Madigan v. Telemarketing Associates*. The Illinois attorney general filed a case against a telemarketing company that would remove the company from the blanket of the First Amendment and make it liable for fraud, if it was found that the company deliberately misled or deceived donors. In May 2003, the Supreme Court ruled in favor of the Illinois attorney general—that the First Amendment did not protect telemarketers or fundraisers from being pursued for potentially fraudulent activities.





Telemarketing Associates in its fundraising for the nonprofit group VietNow, an organization servicing Vietnam veterans, had failed to tell telephone donors that more than 85 percent of their donations were pocketed by the telemarketers themselves.

The Supreme Court subsequently ruled that Telemarketing Associates deliberately deceived potential donors. According to the American Institute of Philanthropy (AIP), a nonprofit's fundraising expense should not exceed $35 for every $100 raised. AIP records indicate that VietNow spent $91 to raise $100.[1] Only 3 percent of the revenue that VietNow did keep was spent on the organization's program activities.[2] BBB Wise Giving Alliance's review of VietNow activities in 2000 revealed that only 2 percent of VietNow's income went to program services, the other 98 percent going to overhead and fundraising costs.[3]

The primary basis for the case wasn't necessarily the low return rates for the donor but rather, as described by the Supreme Court, "when nondisclosure is accompanied by intentionally misleading statements designed to deceive the listener." Nevertheless, the low return rates and the low percentage spent on actual programs—and the fact that they do not pass charity fundraising standards such as AIP's, BBB Wise Giving Alliance's, or Charity Navigator's— yield suspicion and the potential for charitable fraud, is a grave cause for transparency and accountability concerns.

Transparency and the Treasury

But beyond the individual donor, there is also the larger issue of overinflated tax write-offs and its effect on the Treasury. If the donor writes a $100 check, and deducts it from his taxes, and the charity only receives only $15 with which to run their programs, there are millions of dollars deducted for charitable purposes that ultimately aren't used for charity and that the Treasury never collects. These dollars, tax-exempt because of a donors' tax deductions, become revenue for for-profit organizations like telemarketers. In this case, charitable tax deductions, meant to funnel dollars to the charitable sector and its services, don't wind up in either the Treasury or with a charity. Telemarketers are the ones profiting from donor tax write-offs—under the guise of charity and philanthropy.

But beyond the individual donor, there is the macro issue of revenue loss from tax write-offs. The donor writes a $100 check, and deducts it from his or her taxes. In the end, if the charity only receives $9 of the $100, considering the millions of dollars raised this way, there are millions of tax-exempt dollars from which telemarketers are profiting—a great loss for the Treasury's now-bleeding coffers—under the guise of charity and philanthropy.

It is vital that the nonprofit sector be honest with its donors. However, that has not always been the case for some nonprofits.

For national nonprofit organizations purportedly concerned about charity accountability and transparency, hiding behind the First Amendment in *Madigan* just sidestepped the larger issue of transparency and regulating fraud. However, nonprofits lined up behind Telemarketing Associates with the battle cry of protecting "charities' rights and responsibilities to educate the public on important issues." Attorneys for the Independent Sector (which took the lead), Public Citizen, Disabled American Veterans, Association of Fundraising Professionals, and others subsequently filed amici briefs in support of Telemarketing Associates. Their argument was that having to reveal cost and revenue proportions would be "forced speech" and "would be an obstacle to educating the public about nonprofit issues and causes." IS asserted that it was incorrect "to assume that there is a nexus between high solicitation costs and fraud."[4]

While IS did express concern about telemarketing fraud, these charities' support of Telemarketing Associates, aimed to shield telemarketing from oversight and review, defended inefficient telemarketing as just as good as the efficient and ethical telemarketing of others. To shield fundraising practices such as Telemarketing Associates' behind the First Amendment does nothing to uphold or strengthen the public's trust in charities. Sector leadership seemed more concerned with being able to fundraise and educate in any way possible, rather than being able to fundraise in an ethical, transparent manner that would win and sustain the trust of individual donors.

Charitable Solicitation as Telemarketing: The Federal Trade Commission

The Federal Trade Commission introduced a national "Do-Not-Call Registry" in 2003, intended to cut down on commercial telemarketing (under the rule, telemarketers are prohibited from calling registered numbers). The FTC amended the definition of telemarketing to include interstate calls that solicited charitable contributions. However, charitable telemarketers did not have to comply with the registry rule, though telemarketers have to comply if donors specifically ask the telemarketer not to call again.[5] Telemarketers soliciting charitable contributions must also state the name of the organization as well as the purpose of the call immediately, as required by the USA Patriot Act.

The same year, along with 38 states, the FTC, along with 34 state attorney general offices, launched "Operation Phoney Philanthropy," a law enforcement and education campaign designed to crack down on fraudulent charitable fundraising. The FTC pursued five national high-profile cases, while 34 states launched individual campaigns. Sixteen states announced they were pursuing legal action against charities and telemarketers, and two states announced new legislation.

State Legislation & Enforcement

While nonprofits have been touting the free speech argument, state lawmakers and enforcers have been the vanguard for regulating actual charitable fraud. Forty-eight states[6] have rules that govern and regulate charitable solicitation. The laws vary slightly, but generally have the same premise. Charities are required to register with the state attorney general's office and report their finances and fundraising activities. Even before *Madigan* and "Operation Phoney Philanthropy," state attorneys general, backed by state legislation governing charitable organizations and solicitations, have been actively pursuing fundraising miscreants through public reporting and legal action.

New York Attorney General Eliot Spitzer has been issuing his "Pennies for Charity" report since he took office in 1999. The reports reveal that charities on average have received only 30 percent of revenues raised by telemarketing campaigns, and that only one-fourth of fundraising campaigns gave 50 percent or more of revenues to charity. With the first few "Pennies for Charity" reports came a four-part initiative:

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> the ability to issue subpoenas to nonprofits and commercial telemarketers, which could lead to legal action—including lawsuits for fraud;
> preparing new regulations requiring charities to get majority-board approval before signing a telemarketing contract in which they will get only a small percentage of donations, and to do "comparison shopping" before agreeing to contracts;
> proposing state legislation that requires telemarketers to disclose to donors the percentage of funds the nonprofit has received in previous telemarketing campaigns
> proposing federal legislation that requires that if the charity receives less than half of fundraising dollars, only the remitted amount will be tax deductible.

Currently, Oregon profiles the 20 charities that receive the most inquiries and complaints, showing their financial statements and reporting on whether they meet BBB Wise Giving Alliance standards. In the 2003 Oregon report, only two out of 20 charities met these standards.[7]

The California attorney general issues a similar yearly report on charitable solicitation by commercial fundraisers, but specifically lists those charities, and their fundraisers, that make 15 percent or less in their campaigns, 15 percent being significantly below the $35/$100 AIP standard.

Connecticut's 2003 report revealed in-state campaigns having a 35.5 percent return for nonprofits, but multi-state campaigns show only a 9.5 percent return to the charities.[8]

Colorado's 2004 report fared better than others, showing that of the $96 million Colorado charitable fundraising yielded, $53 million or 55 percent was returned to the charities. Their 2003 report had yielded an even better return, at 41 percent.

Noteworthy Telemarketer Miscreants

Low returns are particularly common among veterans, police, and emergency personnel groups' fundraising. For example, two firefighters' organizations in Connecticut's 2003 report, the Association for Disabled Firefighters (ADF) and the Association for Firefighters and Paramedics, had 9.55 and 10 percent return rates, respectively. ADF, based in Santa Ana, CA, has been sued by three states so far, North Dakota in 2002, Oregon in 2003, and Ohio in 2004, for deliberately misleading donors as to the use of their donations.

Massachusetts Police and Fire Groups and All Pro Telemarketing Associates

According to a *Boston Globe* article, All Pro Telemarketing Associates of Fairfield, NJ, "reported raising a total of $3.0 million last year from donors in Massachusetts and around the nation." Only 14 percent went to its ten charities. The clients? Among them were Police Protective Fund of Austin, Texas, and the Firefighters Charitable Foundation of Westerly, R.I. According to Charity Navigator, the Police Protective Fund spent 90.3 percent of its income in fundraising, and only 7.4 percent on actual programs. The Firefighters Charitable Foundation of Westerly, R.I. spent 86.3 percent on fundraising, and twelve percent on programs. Charity Navigator gave both charities zero stars out of four for their (lack of) efficiency.

The Cancer Fund of America and the Civic Development Group

The Cancer Fund of America (CFA) would catch the eye of any casual observer in California's 2002 report on charitable solicitations by commercial fundraisers. CFA's mission is to provide support and services to cancer and hospice patients. They boast about their 26,000 sq. ft. storage space for products for distribution, but have no clear listing of how often, where, and to whom exactly these products are distributed.

Out of two telemarketing campaigns CFA ran, 90 percent of revenues went to its for-profit fundraiser, the Civic Development Group (CDG), with CFA pocketing only $28,671 of $262,642 that CDG raised. Furthermore, only $4.5 million of CFA's $19 million in expenses were spent on actual program services. New York's 2000 report shows CFA hired three different telemarketers that raised a total of $3,806,761, of which the telemarketers received $3,339,889 (88 percent) and CFA received just $466,872 (the remaining 12 percent). The CFA shows up again in Connecticut's 2003 report—this time using a group called Barry E. Schmoyer and Associates. Their return rate with that particular fundraiser was 15 percent.

The Civic Development Group is even more suspect. A consumer-run Web site (www.ripoffreport.com) blasts CDG for unethical telemarketing practices, such as impersonating firefighters and police officers. CDG will soon also be fundraising for the New York State Fraternal Order of Police, opening up a 200-person call center in New Jersey in April. According to Spitzer's 2004 report, CDG raised $3.7 million for the Order but gave only $464,000 to the charity (12.5 percent). An article in the *Albany Times Union* further states that the highest percentage of funds that charities gained from seven CDG campaigns in 2002 was 17.9. CDG has been in hot water with the Federal Trade Commission for misrepresentation in 1998, and with the state of Vermont in 2001 for raising money purportedly for medical equipment for disabled children. Not surprisingly, no money went to any Vermont children. CDG will be opening call centers in states such as Kentucky, Illinois, and Virginia. Strangely, Charles Caputo, executive vice president of the Order says, "In New York, we had no problems with them."

Situations like these have provided the fodder for attorneys general in their capacity as regulators of charitable organizations. For example, the same month that the *Madigan* case was decided, Oregon Attorney General Hardy Myers filed a complaint against the Association of Disabled Firefighters as part of "Phoney Philanthropy." The basis of his complaint was that ADF deliberately concealed the fact that out of the $4.4 million they had raised nationwide, less than 1 percent of funds was used to actually provide assistance to firefighters.

In January of this year, Massachusetts Attorney General Tom Reilly won $75,000 from the Cancer Society of America,[9] which violated the state's charitable solicitation laws by misrepresenting their charitable activities.[10] The settlement requires the society to pay $75,000 to the Cancer Center at the University of Massachusetts Memorial Center and Why Me Inc., nonprofits that provide cancer patients with financial assistance. Of the case, AG Reilly said, "Charities and their fundraisers have an obligation to be forthright to prospective donors about the mission of their organization."

In March of this year, New York Attorney General Eliot Spitzer went after the Saratoga County Deputy Sheriffs' Benevolent Association for misrepresentation.[11] The association purports to represent deputy sheriffs and solicits accordingly, when in fact it represents only support staff of sheriffs' offices. On top of that, the Attorney General's office has determined that only 10 percent of its revenues go to charitable purposes.

Not all states have been as active in pursuing charitable fraud as New York, Massachusetts, or Oregon has. It may be a question of funding, staffing, or legal priorities. Nonetheless, state attorneys general like Spitzer and Myers are developing a standard for effective, ethical, and legal state-level charitable fraud regulation, which will need more funding and staffing if states are expected to continue uncovering fraudulent schemes.

Disclosure and Fraud Prevention: Whose Responsibility?

The potential for fundraising fraud means more instability for an already shaky public trust of the charitable sector, and a significant loss in tax revenue for the government. It is obvious that attorneys general, even with their limited resources, are continuing to find cases of fundraising fraud. Government enforcement and education certainly does not exempt the nonprofit sector from doing its part to curb misleading, fraudulent, or inefficient charitable fundraising practices. For the nonprofit sector and the people it represents and serves, the mentality of fundraising at any cost with hardly a concern concern for basic ethical behavior will do more harm than good if this type of behavior dissuades increasingly large numbers of donors from giving money to nonprofit organizations. If sector leaders are truly concerned about fraud, they need to step up and advocate for further regulation at the state and federal levels of charitable fundraising practices, including mandatory disclosure of the return rates to actual charities. They need to hold charities accountable for inefficient fundraising and high overhead costs. Perhaps then, charities and telemarketers to think twice when planning their fundraising-- or for charities specifically, when choosing a fundraising company.

Notes

[1] "Telemarketers can be liable for fraud, high court rules," CNN, May 5, 2003.

[2] *Chicago Tribune*, November 5, 2002.

[3] Rick Cohen, "Fundraising or Fraud?," *Responsive Philanthropy* (Spring 2003).

[4] http://www.independentsector.org/programs/gr/ryan-faq.html

[5] http://www.ftc.gov/opa/2002/12/donotcall.htm

[6] www.nasconet.org/

[7] http://www.doj.state.or.us/ChariGroup/CAS06158.pdf

[8] http://www.ct.gov/dcp/cwp/view.asp?a=1629&Q=285442&PM=1

[9] Despite the striking similarity in names, this organization is not the same as the Cancer Fund of America discussed earlier in the article. There was no website on this organization, and there have been accusations that this organization used to its advantage the fact that its name is similar to the American Cancer Society (www.cancer.org).

[10] http://www.ago.state.ma.us/sp.cfm?pageid=986&id=1365

[11] http://www.oag.state.ny.us/press/2005/mar/mar22a_05.html

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