

Weasels on the March: The Struggle for Charitable Accountability in an Indifferent Sector

by Dean Zerbe

OVER THE PAST SEVERAL YEARS, THE charitable sector's credibility has eroded under the weight of scandal and a corresponding failure to fully acknowledge and address its problems. With massive theft exposed and organizations' leaders ousted on a regular basis, charities have yet to own this systemic dysfunction and define methods of self-regulation. This article argues that charities' credibility problem is unsustainable, and the time is now for charities to stop relying on external entities to take action.

Studies from the Association of Certified Fraud Examiners report consistent and costly fraud in the nonprofit sector. Such claims should shake the nonprofit sector and cause outrage: torches lit, pitchforks grabbed. But unfortunately, the lifecycle of scandal in charities is all too familiar: the media (or Senator Chuck Grassley) discovers scandal; the public is shocked; sheepish charity sector "leaders" are unavailable for comment; Congress demands that the IRS or a state charity organ-

ization "does something" to address the scandal; charities say dealing with scandal is an enforcement issue; Congress learns that the scandal is legal under current law; Congress proposes changes to the law; charities counter that "scandal" shouldn't be justification for legislation, parroting the three phrases they know: (1) the scandal reflects only a few bad apples, (2) we shouldn't throw out the baby with bathwater; and (3) the sector isn't suited to one-size-fits-all legislation; Congress decides to (1) study, (2) shelve, or (3) water down the proposed reforms and only partially addresses the problem; charities decry the watered-down legislation as burdensome, especially for small charities; the media (or Senator Grassley) discovers yet another scandal. . . .

Let me make clear that "scandal" here extends beyond the unfortunate but typical fare of embezzlement and fraud highlighted by the Association of Certified Fraud Examiners' report. I also haven't focused on the champagne lifestyles of charity executives. So many of our nation's largest charitable institutions are built like Muhammad Ali but punch like Pee Wee Herman: that is, the vast resources of these charities aren't commensurate with the level of support they provide to those in need. I believe that Senator Grassley will rightly focus his energies on this area: major charities that punch like

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Pee Wee (while receiving tens of billions of dollars in taxpayer-subsidized support).

Because charities accomplish great things for those in need and our communities, and could accomplish so much more, we must take off the rose-colored glasses and get clear-eyed about the problems in the sector. Strengthening the integrity and vitality of charities and ensuring that charitable dollars are used effectively and responsibly has never been more important now that our economy is in bad shape and those in need are most desperate.

Let's revisit the lifecycle of the weasel above and see where we can prevent these abuses and fulfill the desires and hopes of the public—a public that supports charities with its donations but even more so with massive tax subsidies at the federal, state, and local level.

The Board

The charitable sector's trouble begins with the board. Too often charity boards don't show up (or never meet), are from the CEO's inner circle, never ask for—much less read—the audit letter, and the list goes on and on. A board that is independent, engaged, informed, and knowledgeable can detect and prevent scandal and be the cornerstone for a successful charity. It would be especially nice if boards engaged in their central function: reviewing and evaluating the work of the CEO and, when necessary, removing the CEO. How fresh the air would be if a board publicly announced its goals for its president and publicly stated at year's end whether those goals had been met.

Lawyers

The road to hell must be paved with bricks that say "It's legal." Some lawyers for charities have abdicated their responsibility to counsel their clients on best practices and instead act as enablers, informing a charity that whatever flim-flam action it wants to take is legal.

Imagine instead a world where lawyers truly

advise these organizations and tell charity boards and executives something like this: "You cannot let the fact that something is legal be your guide. While it is legal, it is inappropriate and at odds with your public trust and the intent of your donors. It will cause harm to the charitable goals of this institution."

The Charitable Sector: The Good, the Bad, and the Ugly

The good. The work of Independent Sector's nonprofit panel and the diligent efforts of the organization's leadership, Diana Aviv and Pat Read, has been the rare shining light. While the nonprofit panel's recommendations are fair guidance, it is frustrating that policies have been watered down by exceptions and caveats. The real question is whether Independent Sector will press on, educate, and encourage charities to adopt its principles. I should also note the work of the number of grading or ranking agencies. I would encourage the establishment of common measurements in the field.

The bad. Too often when it comes to influencing charities' behavior, the purse is left at home. But what if private and community foundations that pour money into nonprofit hospitals that overcharge the poor and engage in grinding collection efforts against the most vulnerable were instead to say "No more"? If institutional donors focused more on the power of the purse to do good, those in need would benefit.

The ugly. The charitable sector is wholly incapable of calling out the weasels in its own community. Time and again, the response to the latest scandal is to fight ostriches for holes. The rare counterexample is the leadership of the Make-a-Wish Foundation, which loudly decried the sound-alike charity that bilked donors and did nothing for children. Make-a-Wish's public comments made a difference and bolstered the oversight of Senator Grassley and the first-rate enforcement efforts by the Pennsylvania Department of State's Bureau of Charitable Organizations.

For those in need, what a better day it would be if there were a scandal and the leaders in charity joined in outcry, denounced the actions, marched for reform by the board and leadership, pulled funding, and, where appropriate, demanded enforcement.

The University Philanthropy Department

It's all too common for philanthropy departments to confuse their work with the cheerleading program that is housed next door on campus.

Imagine a different world. A seminar that is open to the public and inviting fresh thinkers, for example, sets a goal to provide 12 practical proposals: targeting enforcement, legislative, regulatory, and self-reform measures to address the problem of scandalous veterans' charities, which is something that the public actually cares about.

Federal and State Enforcement

We need to have more substance in the law for the IRS to enforce; otherwise it's a labor-intensive effort with few results. There is a yawning gap between what the public thinks is wrong in the charity sector and what is actually illegal. The failure to bring to book those who gained notoriety through the *Boston Globe* spotlight team investigations, for example, indicates that this isn't an issue of failure to enforce: federal and state laws and regulations are inadequate and need to be strengthened.

An additional problem is that too often the IRS's central penalty—revoking tax-exempt status—is meaningless. Those involved will just go set up another charity tomorrow. We need to expand efforts that bring meaningful penalties to bear. We also have to bring in other federal enforcement arms; the Federal Trade Commission, for example, should be front and center in dealing with fraudulent solicitation.

The IRS's Exempt Organizations division has taken steps to modify Form 990 and the attached schedules. But the next question is whether the IRS

and Treasury will finally stop showing leg on the issue of the commensurate test—which measures whether a charity's activities are commensurate with its financial benefits—and actually put it into practice. And while the Exempt Organizations division has done good work, the Department of Treasury and IRS counsel's office haven't done enough to address abuses in charitable activity.

My recent meeting with the National Association of State Charitable Officials gives me some confidence that at the state level, things have improved (although some states, such as Florida, are exceptions). Particularly during these hard economic times, state charity officers need to protect the public fisc, or treasury (given that charities are recipients of massive subsidies provided by taxpayers), and ensure that those in need get the benefits that donors intend.

Congress and State Legislatures

Congress will continue its oversight. Senator Grassley is never one to rest on his laurels. I expect Chairman Henry Waxman to continue his oversight as well (although if he becomes chairman of Energy and Commerce, it's more unclear), particularly in the area of veterans' charities. Congressman Peter Welch has been a leader on the college endowment issue, and Congressman Xavier Becerra and Congressman Robin Hayes have been thoughtful about the charitable sector (with Hayes's defeat in November 2008, however, Congress has lost a member with significant firsthand knowledge of charities). In addition, Congressman John Lewis has held hearings on certain aspects of charities and Chairman Max Baucus has presided over the bully pulpit of rural philanthropy. The question is how these efforts will translate into change, whether within charities or in the law.

When it comes to the charitable sector, my confidence in self-reform and self-regulation is limited. Universities' response to the endowment issue, for example, constituted fig-leaf reform. Senator Grassley is always optimistic and can certainly point to

success in his work with Sister Carol Keehan at Catholic Health Association to bring real change at nonprofit hospitals.

At the state level, state legislatures must stop relying on the feds to fix the problems in charities. State and local officials can show leadership that will have an impact across the country, including among the feds.

The Media

The media has only a handful of reporters that have a charity beat, with Stephanie Strom of the *New York Times* nonpareil. But while the press does a great job of exposing scandal, it does only a fair job of following up and holding other players—such as enforcement agencies, legislatures, and charity leaders—accountable. I should also note that *NPQ*'s own Rick Cohen does a tremendous job in his reporting, and of course life wouldn't be complete without Pablo Eisenberg's wonderful commentary.

Imagine how we could bolster press oversight of charities if private foundations supported investigative journalism positions through awards and grants. I would particularly encourage funding for the creation of an entity to be a resource center for investigative journalists to assist them in navigating the minefields.

The current infrastructure for ensuring charitable sector accountability can't support a sand castle. A better world is possible, but it will take leadership from charities themselves to make it happen. If the payoff is a more vibrant and successful charitable sector—with the weasels kept in their holes—it's certainly worth the effort.

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