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# Patchwork Oversight Allows Dubious Charities to Operate

By **BARRY MEIER** and **REBECCA R. RUIZ** MAY 21, 2015

James T. Reynolds Sr. first ran afoul of state regulators for the way he operated his cancer charity in the 1980s. But he kept going, hopscotching from state to state and helping to create new charities that received federal tax exemptions.

Sham charities have long been used to fleece well-meaning donors. But over the last decade, efforts to tighten the way charities are regulated or coordinate action between the Internal Revenue Service and state officials have largely failed either because of regulatory indifference, political lobbying or lack of political will.

Those holes were highlighted this week when the Federal Trade Commission, all 50 states and the District of Columbia accused Mr. Reynolds and four charities that he helped run of cheating donors of more than \$187 million, bringing the charges decades after he first hit regulators' radar.

"Fraud involving charities is viewed as a junior-league crime," said Dean A. Zerbe, a former staff member for Senator Charles E. Grassley, Republican of Iowa, who worked on legislation related to charities.

In announcing their action against the charities, F.T.C. officials said three defendants, including Mr. Reynolds's son, James T. Reynolds II, had settled the civil complaint and agreed to lifetime bans from the charity industry. F.T.C. officials said they were unaware of any criminal actions brought against their principals.

Much of the oversight responsibility for charities rests with the I.R.S., which awards tax exemptions to charities and monitors them for compliance. Few come under close scrutiny, however.

“There’s no central, powerful oversight of nonprofits in America,” said Sandra Miniutti, vice president of Charity Navigator, which evaluates charities in the United States. “There are more than a million charities, and the I.R.S. will say they don’t have enough resources to monitor them.”

A few years ago, the division of the I.R.S. that oversees tax-exempt organizations came under fire in Congress after disclosures that it was singling out the Tea Party and similar political groups for scrutiny. Morale and staffing at the unit has fallen over the years, said Steven Miller, a former acting I.R.S. commissioner.

But even before the political controversy, the tax agency’s oversight of charities was dropping. A report in December by the Government Accountability Office found that examinations of charities and tax-exempt groups had steadily declined over the years and that review rates were lower than for other filers. In 2013, the I.R.S. examined 0.71 percent of all charitable organizations’ filings, compared with 1 percent for individuals and 1.4 percent for corporations, the G.A.O. found.

In addition, the G.A.O. reported that the I.R.S. did not have “quantitative measures of compliance” or “particular aspects of noncompliance” to guide its reviews of charities.

“They’re focused on people who don’t pay their taxes, areas where they can make money,” said Ms. Miniutti of Charity Navigator. “Going after bad charities isn’t a way for them to increase revenue.”

A spokesman for the I.R.S. did not make agency officials available for comment. “Federal law prohibits us from commenting on any specific tax matters involving taxpayers or organizations,” the agency said in a statement.

The relative lack of oversight by the I.R.S. has put the onus on other agencies and the states to monitor potential fraud at charities. The F.T.C., for example, has previously brought actions against groups claiming to be charities.

The I.R.S. has been little help in those efforts.

“In the charities world, the I.R.S. is the elephant in the room in a lot of conversations,” said Sean Courtney, an assistant state attorney general in New York. “But it’s a silent elephant because it doesn’t really participate. It’s there, but it’s not really a partner.”

Nearly a decade ago, Congress, at the urging of a former New York State charities regulator, William Josephson, allowed the I.R.S. to share data on tax-exempt groups with states that were investigating them.

The idea was to allow states and the I.R.S. to bring joint actions against the worst offenders so they could be quickly stripped of their tax-exempt status rather than retain that benefit for years, as the cancer charities did, said Mr. Josephson, who is a retired partner at the law firm Fried, Frank.

After the law's change, California, Hawaii and New York State entered into information-sharing agreements with the I.R.S. But state officials said the terms of the agreement, laid down to protect taxpayer privacy, were too onerous and undermined the partnership.

"If we left information from the I.R.S. on our desks with our doors unlocked, we were subject to criminal penalties," said Yael Fuchs, an assistant attorney general in New York State's charities bureau. She said that the bureau underwent numerous audits to make sure it was following the rules.

Even at that cost, the information the states obtained from the I.R.S. could rarely be acted on, officials said. "There was very little we could put to use," said Hugh R. Jones, the supervising deputy attorney general for Hawaii. "It was frustrating to have some documents and not be able to do anything with them, or to let charities know what we knew. It was like we painted ourselves into a corner."

Mr. Jones said Hawaii and other states unsuccessfully tried to clarify the terms of the agreement, but the controversy that erupted in 2013 over the tax agency's audit of the Tea Party group made it unfeasible.

"That unit of the I.R.S. was mired in inquiries and hearings," he said. "It was put in defensive mode."

Mr. Josephson, who had pushed the plan to share information about charities, said he believed the arrangement could have succeeded if state regulators had worked together as a group to promote it.

But he and other experts said regulation of charities at the state level was a hodgepodge. Some states oversee them through the offices of their attorneys general, others through tax authorities.

Some people, however, including Mr. Zerbe, the former Senate staff member, said that many other states largely ignore problems with charities.

"Twenty of the states on any given day are O.K., and 30 are nowhere to be found," said Mr. Zerbe, who now is a lawyer at Alliantgroup, a tax consulting firm in Washington.

Mr. Jones, the deputy attorney general in Hawaii, said that his state had sued one of Mr. Reynolds's charities, the Cancer Fund of America, in 1989 for deceptive trade practices. The charity paid a \$250,000 settlement, he said.

"It's not like states didn't do anything," Mr. Jones said. "It really took a coordinated effort to bring these four charities to their knees."

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