COMMENTS ON THE ROLE OF THE MODERN CHARITABLE HEALTH CARE PROVIDERS: PITT HEALTH LAW CERTIFICATE PROGRAM 10TH ANNIVERSARY SYMPOSIUM FEBRUARY 5, 2007

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As was indicated earlier, my name is Karl Emerson and I am the Director of the Pennsylvania Bureau of Charitable Organizations. The Bureau is the state agency responsible for administering Pennsylvania's Solicitation of Funds for Charitable Purposes Act.[1] This is the statute that governs organizations soliciting charitable contributions from Pennsylvania residents, businesses, and/or private foundations. Pennsylvania's solicitation statute is similar to the solicitation statutes of 38 other states and requires organizations soliciting charitable contributions in Pennsylvania to typically register with the Bureau prior to soliciting.[2] Registration usually involves the organization submitting a registration statement; a copy of its IRS 990 Return; a copy of its audited or reviewed financial statements; and copies of its Articles of Incorporation, By-Laws, and IRS Determination Letter.[3] The Bureau then makes this information available to the public through our toll-free number, our website, and otherwise.

However, there are lots of types of organizations that are either specifically excluded from the Act's coverage all together or are simply exempt from the Act's annual registration requirements.[4] One of the many types of organizations that are exempt from having to register with the Bureau each year is hospitals and their foundations.[5]

However, just because hospitals and their foundations are exempt from the Act's registration requirements, does NOT mean the Bureau or other state

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1. 10 PA. CONS. STAT. § 162.1 *et seq.* (2006).
2. § 162.5.
3. *Id.*
4. § 162.3; § 162.6.
5. *Id.*

enforcement agencies cannot investigate these types of organizations for allegedly violating one or more of the Act's provisions. Hospitals and their foundations are still required to comply with the rest of the Act's requirements. For example, the Bureau, local District Attorneys Offices, and/or the Pennsylvania Attorney General's Office can all investigate allegations that a particular hospital or its foundation has not kept true and accurate fiscal records, has misspent charitable contributions, has engaged in deceptive solicitation practices, or has engaged in any of the many other types of conduct specifically prohibited by the Act.[6] All three of these offices have concurrent jurisdiction to enforce Pennsylvania's solicitation statute.[7]

However, local District Attorneys and the Pennsylvania Attorney General's Office actually have much broader jurisdiction than the Bureau because they can also file criminal charges for conduct that violates the Pennsylvania Crimes Code. We have recently been working closely with a number of District Attorneys Offices to get particularly egregious violators prosecuted criminally and, in several cases, sent to prison for as long as six years.[8] The Pennsylvania Attorney General's Office actually has the broadest jurisdiction of these three state offices because it can also investigate allegations that one or more hospital executives are excessively compensated, have improperly spent restricted funds, have not applied charitable contributions in accordance with the representations they have made to donors, or otherwise breached their fiduciary duties.

Hospitals and their foundations, just like other types of charitable organizations, are increasingly having their operations scrutinized much more closely by not just state enforcement authorities—but also by the IRS, the media, and the public at large. As a result, they need to know what the applicable state and federal statutes require and, equally important, the types of conduct these statutes prohibit. In this age of significantly heightened governmental and media scrutiny, hospitals and their foundations, like all other charitable organizations, need to ensure they are operating in conformity with all applicable state and federal laws. If they do not, they can be held accountable by the federal government through the IRS which has recently begun to significantly ramp up its enforcement efforts; by the various states through their attorneys general, district attorneys, and/or secretaries of state; by private watchdog organizations such as the Better Business Bureau's Wise

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6. § 162.15-16.

7. § 162.16.

8. Kathleen Brady Shea, *Chesco Ministry Founder Sentenced to Jail for Fraud*, THE PHILADELPHIA INQUIRER, Apr. 2, 2005, at B5.

Giving Alliance; by an ever-vigilant media always eager to expose irregularities and fraud in the sector; and lastly, but in many cases most importantly, by the donating public that can, and does, stop its support of organizations that violate its trust.

The sad reality is that hardly a day goes by without charitable sector scandals and abuses being exposed in the media. The head of our investigative unit goes on the Internet each morning and typically finds at least five or six stories about charitable sector scandals and abuses practically every day. Unfortunately, when these scandals and abuses are reported in the media, it hurts every legitimate charity because each day an ever-growing segment of the public is becoming more and more skeptical and refusing to make donations it might otherwise have made. Numerous studies have documented this fact and the sector's declining credibility in recent years—especially since September 11th.[9]

And now that all charities' IRS 990 Returns, including those of tax-exempt non-profit hospitals and their foundations, are readily available from the *GuideStar* website, lots of donors and reporters regularly view and analyze these important tax documents.[10] There are now over 3.4 million IRS 990 Returns readily available through the *GuideStar* website.[11] In terms of nonprofit accountability, this new technological capability is a significant development. However, as important as it is, it is not the ultimate solution because state and federal investigators regularly document that many charities' 990s often contain material falsifications, misrepresentations, and omissions. Indeed, several years ago, *The Chronicle of Philanthropy* documented that as many as one out of every four charities reporting contributions of at least $500,000 on their 990s may have falsely reported no fundraising expenses—that was one-quarter of the largest charities in the

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9. *See* Jacqueline L. Salmon, *Nonprofits Show Losses in the Public's Trust*, WASH. POST, Sept. 10, 2002, at A2; Ben Gose, *42% of Americans Say Relief Effort Damaged Faith in Nonprofit Groups*, CHRON. OF PHILANTHROPY, Sept. 5, 2002, at 12; Paul C. Light, *Trust in Charitable Organizations*, BROOKINGS INST. (Dec. 2002); Brad Wolverton, *Public Confidence in Charitable Organizations Continues to Lag, Report Finds*, CHRON. OF PHILANTHROPY, Dec. 11, 2003, at 27; Brad Wolverton, *Many Americans Are Still Skeptical of Charities, a New Opinion Poll Finds*, CHRON. OF PHILANTHROPY, Sept. 16, 2004, at 3; *To Give or Not to Give: The Continued Crisis in Charitable Confidence*, BROOKINGS INST. (Dec. 2003), *available at* www.brookings.org; Harvy Lipman, *Survey Identifies Troubling Trends for Nonprofit Organizations*, CHRON. OF PHILANTHROPY, Nov. 14, 2002, at 13; Gina Russo & Colin Johnson, *Confidence in Charitable Organizations Reaches Lowest Level Since 9/11*, BROOKINGS INST. (Sept. 9, 2002), *available at* www.brookings.org.

10. http://www.guidestar.org/.

11. As of June 28, 2007, Guidestar had over 3.4 million IRS Forms 990s available on its website at http://www.guidestar.org.

country at the time![12] A more recent study documented that 37 percent of charities with contributions of $50,000 or more reported no fundraising costs on their 990s.[13] These two studies confirm what Pennsylvania and other states have been documenting for some time now—there are lots of material falsifications, misrepresentations, and omissions on charities' IRS 990s.

And even though lots of these falsifications, misrepresentations, and omissions may be unintentional, tax-exempt non-profit hospitals and other charitable organizations can still be prosecuted for submitting false 990s. For example, we recently collected a $41,000 fine from a national charity we prosecuted for making 41 intentional material false statements totaling 1.2 million dollars in a 990 it submitted to the Bureau.[14] In a more recent case, our prosecuting attorney has filed a 1,289 count Order To Show Cause against four related charities, their officers, and their CPA for submitting a series of 990s to the Bureau that we allege contain at least 1,289 material false statements.[15] The potential fines that could be assessed in this case exceed 1.3 million dollars. When charges like these get filed, the resultant damage to an organization's credibility and fundraising capabilities can be devastating—especially if there is lots of media coverage. So, hospitals and their foundations need to make sure they file accurate and complete 990s to avoid these types of prosecutions and the resultant negative publicity that inevitably accompanies such prosecutions.

Tax-exempt hospitals in this age of heightened governmental and media scrutiny also need to be especially mindful that they follow appropriate procedures when determining the salaries they are going to pay their executives and key employees to avoid the imposition of intermediate sanctions by the IRS—as well as the negative media stories that can potentially be even more harmful to the organization than the sanctions themselves. Technology is increasingly making it much more likely that organizations that pay their executives excessive salaries or submit falsified

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12. Harvy Lipman, Holly Hall & Martha Voelz, *Charities' Zero-Sum Filing Game*, CHRON. OF PHILANTHROPY, May 18, 2000, at 1.

13. *Nonprofit Overhead Cost Project*, Ctr. on Nonprofits and Philanthropy at the Urban Inst. and Ctr. on Philanthropy at Indiana Univ., Brief No. 1, Feb. 2004, *available at* http://www.coststudy.org. *See also* Harvy Lipman, *Study Examines Causes Behind Reporting Errors on Federal Tax Returns*, CHRON. OF PHILANTHROPY, Jan. 20, 2005, at 19.

14. Commonwealth v. Children's Wish Foundation Int'l, Inc., Docket No. 0012-98-00, *available at* http://www.dos.state.pa.us/char/lib/char/consent_agreements/childrens_wish_foundation_international_inc._00-98-02634.pdf.

15. Commonwealth v. Nat'l Child Safety Council, Docket No. 0012-98-04, available from the Department of State's Prothonotary's Office by calling (717) 772-2686.

IRS 990s will eventually get caught. There is actually a company that both the IRS and several state enforcement authorities have contracted with that has developed an incredibly sophisticated software program and database that allows the IRS and these other enforcement agencies to immediately and easily identify potential excess compensation cases.[16] You simply ask the computer to plot out all the salaries for say hospitals with gross revenue of $500 million or more and in a matter of seconds you can easily see whether there are particular individuals whose salaries are way out of line with their peers in similar positions at similar organizations. I have seen this demonstrated and it is really quite amazing.

And, as I indicated earlier, it is not just the IRS and state regulators who are examining IRS 990s much more closely now—we regularly get individuals and reporters contacting us about potential irregularities on organizations' 990s. In fact, some of our best cases to date have been as a result of information initially brought to our attention by either reporters or the donating public.

Given the heightened scrutiny by Congress, tax-exempt hospitals also need to ensure that they are providing an appropriate level of community benefits to maintain their tax-exempt status. As Tom and others have indicated, this is a real hot-button issue with at least certain Senators and Congressmen right now. And even though Senator Grassley is no longer chairman of the Senate Finance Committee, it is fully anticipated that he and his staff will continue to highlight abuses in the sector and propose additional legislation to address these abuses.

So, here is the bottom line on this topic from a state regulator's perspective: even though hospitals and their foundations are exempt from having to register annually with the Bureau under Pennsylvania's solicitation statute, they are not exempt from having to comply with the statute's many other provisions. In addition, they are not exempt from being prosecuted criminally by either local District Attorneys, the Attorney General's Office, or the IRS. And then lastly, but perhaps most importantly, they are not exempt from the ever-increasing scrutiny of the Congress, the media, and the donating public which can, in many cases, be far more damaging to an organization than even a state or federal prosecution.

I could give you a list of names of individuals and organizations that truly fear much more getting a letter of inquiry from Senator Grassley at the Senate Finance Committee than a letter from Karl Emerson or a letter from the

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16. Economic Research Institute, http://www.erieri.com/index.cfm.

attorney general of Pennsylvania himself. We file this 1,289-count **O**rder **T**o **S**how **C**ause—it is this thick—without any attachments—against four national charities, their officers and their CPA, charging them with making 1,289 material false statements. They can be nailed for $1.3 million in fines but we do not get any coverage in the *Chronicle of Philanthropy* or other publications on that. However, Senator Grassley writes a letter—and every time he writes a letter—to any organization asking for anything, it is front page or there is a major story about it. So that is the point that I want to make sure that everybody understands, that the media and the public and the Senate Finance Committee they play a vital role here. As Tom said, there is this very heightened scrutiny and I would not count Senator Grassley out.