

Statement of Daniel Borochoff, President, American Institute of Philanthropy, Chicago, Illinois
Testimony before the House Committee on Oversight
and Government Reform
Hearing on Veterans Charities
December 13, 2007

Our Nation's Veterans Deserve Better from America's Charities

The American Institute of Philanthropy (AIP) and Charitywatch.org is a nonprofit charity watchdog and information resource dedicated to helping its members and the general public make wise giving decisions. Since 1993 we have been America's toughest and most independent watchdog of the accountability, finances, governance and promotional practices of charities. Rather than merely repeating a charity's self-reported finances, AIP conducts an in-depth analysis of a charity's income, expenditures and financial position. Our letter grade (A+ to F) ratings of nonprofit organizations' financial performance as published in the *Charity Rating Guide & Watchdog Report* are utilized by thousands of conscientious donors across the nation to make better informed giving decisions. Nearly every major US media outlet has covered AIP's advice, analyses and concerns.

Americans, whether or not they favor our military's involvement in Iraq, Afghanistan or other conflicts, care deeply about the plight of our nation's wounded veterans. Compassionate Americans are distraught with grief that soldiers have sacrificed their lives and good health to protect us and/or our interests. We want to do something to help our brave wounded warriors. So when a veterans charity calls or writes for a donation, we feel compelled to open our wallets wide without thinking fully about whether the charity is deserving of our support. We are giving with our hearts and not our minds. Unfortunately, too many charities are taking advantage of this and getting away with wasting millions of dollars of contributions that were intended to help veterans.

AIP rates the financial performance and accountability of over 500 charities in 36 categories including International Relief, Health, Environment, Child Protection, Human Rights, and others. AIP believes that a charity should spend at least 60 percent of its cash budget on bona-fide charitable programs (35 percent or less receives an F and 75 percent or more receive an A), should spend less than \$35 to raise \$100 (\$60 or more receives an F and \$15 or less receives an A) and should not maintain over three years of available assets in reserves (over five years receives an F). The two worst performing categories are Veterans & Military and Crime & Fire Prevention. While most categories have a preponderance of charities with A and B grades, 75 percent of the groups in these two categories earn D's and F's. This is a very disappointing performance for these two categories since 78 percent of the charities that AIP rates receive a C or higher grade. It is ironic that two of the very most popular causes are the least efficient with America's donated dollars. It is a national disgrace that hundreds of millions of dollars raised in the name of injured veterans, police and firefighters are being squandered. (Please see the attachment to this testimony for ratings of veterans charities as reported in the December 2007 issue of AIP's *Charity Rating Guide & Watchdog Report*.)

Many veterans and military charities do a lot of good. They help veterans obtain benefits from the government, fund medical research and rehabilitative services, provide vocational and financial counseling and offer many other valuable programs for veterans and their families. Unfortunately, too many veterans charities choose to spend most of their donated dollars on direct mail and telemarketing solicitations, executive salaries, and other overhead expenses that do not directly benefit veterans.

Low Fundraising Efficiency

Many veterans charities, much like police or firefighter groups, are not very discriminating about whom they solicit because they know that their cause is so widely popular. Many groups conduct massive “cold call” solicitation campaigns to millions of people in the general public, rather than to smaller, targeted groups of people who are more likely to make a donation. This is an extremely inefficient solicitation practice that results in large fundraising expenses eating up nearly all of the contributions. Many veterans groups include address stickers, greeting cards or other trinkets with their solicitations. The problem with this fundraising method is not necessarily the cost of the gifts but rather the size of the individual contributions that are given in response to these items. Many people, especially senior citizens who receive the trinkets, do not want to make a donation but feel morally obligated to send the charity a few dollars to pay for these items. (Note: Under U.S. law recipients are under no obligation to pay for any gift that they did not order.) So the charity may be getting new people for its mailing list but not people strongly interested in its cause. Fundraising efficiency is usually a function of the average size of the contributions a charity receives. In other words, charities that receive mostly very small contributions tend to have high fundraising costs.

The wool is being pulled over the eyes of the donating public by some F-rated charities. Professional for-profit fundraising companies like to work with veterans and police/firefighter charities because they know that people are more likely to respond to solicitations from these charities than just about any other type of group. Veterans and other charities often enter into contracts with professional fundraising businesses that may keep (for their profits and expenses) 80 percent or more of the contributions raised. **National Veterans Services Fund (NVSF)** filed a 2004 contract with Bee LC that guarantees at least 15 percent of the gross revenues “for calling of individuals who have previously donated by telephone via this contract to NVSF.” It is unfortunate that NVSC did not insist on a higher guaranteed minimum of gross proceeds from current donors to benefit veterans.

When questioned about their lopsided agreements with for-profit solicitors, charities often rationalize them by saying: “We don’t have the staffing to fundraise,” “It’s very expensive to raise money” or “It’s money we wouldn’t have otherwise.” AIP doesn’t buy these arguments. By far most charities are able to receive C or higher grades for getting 60 percent or more of their cash budgets to bona-fide program services. It is my position that unless a charity can operate efficiently it should either merge with another group that can do so or close its doors. There is an opportunity cost to funding highly inefficient charities. Total U.S. giving (now at about \$300 billion a year) is a fixed pie. It has been 2 percent of GDP (Gross Domestic Product) for over four decades. Therefore, contributions wasted by a poorly performing charity is money that is

not available to a charity that could use most of it to help a wounded veteran or other worthy recipient.

A number of AIP F rated veterans charities return most of the money raised to their professional fundraisers. It's a shame that groups such as **American Veterans Relief Foundation, American Ex-Prisoners of War Service Foundation, National Veterans Services Fund** and **Vietnow National Headquarters** dishonor America's brave veterans by using over 80% of the money raised on their behalf to pay fundraising expenses. More charities need to adopt a policy to not enter into costly arrangements with for-profit operations.

AIP strongly believes that most charities raising money for a highly popular cause such as injured veterans, firefighters, police, disaster relief, hungry or ill children, cancer, etc... should maintain reasonable annual fundraising costs of 35% or less. Exceptions would be made for groups that have been in existence for less than 3 years or with gross revenues of \$500,000 or less. Controversial or unpopular causes, e.g. legalization of marijuana, gun rights, abortion, and gay rights should be allowed to have fundraising costs exceeding 35% per year due to the smaller number of people willing to support these causes. Past attempts to regulate fundraising costs have failed in the courts due to free speech concerns. The First Amendment should continue to guarantee that we have the right to raise money for unpopular causes even if it is very expensive to do so. Opportunistic fundraisers, who purposely pick causes that the public is most likely to support, should not be allowed to hide behind the First Amendment.

Low Accountability

Most of the veterans charities that AIP rates do not pass our basic accountability test. Of the 27 major Veterans & Military groups rated in the December 2007 issue of AIP's *Charity Rating Guide & Watchdog Report*, 16 groups or 59% receive a "closed book" for not making their most recent audited financial statements, IRS form 990 and annual report available to AIP. Since so many veterans charities do not make their audited financial information readily available, AIP must turn to public sources such as state offices of charity registration, which are severely understaffed and do not exist in some states. Due to charities' late filing of information and processing time at state agencies, information that is two years old or more may be all that is available. Guidestar.org and some other sources post charity tax forms from the IRS but rarely provide audits, which AIP considers to be a much more solid document. For example, NVSF reports in its fiscal 2006 IRS form 990 that it does not allocate the costs of its solicitations to program services yet in its audit of the same year it reports allocating \$971,927 of these costs to program services. The donating public would not know on the basis of a tax form alone that 59 percent of NVSF's reported program service expense is the educational component of a direct mail or telemarketing solicitation.

What sets AIP apart from other sources of charity information is our thorough analysis of every group that we rate. Other watchdogs do not use the same standards when evaluating charities. For example, one ratings group simply runs the self-reported, unaudited numbers from a charity's tax form through a formula, which does not take into account the many complexities and inconsistent nature of charity financial reporting. Another watchdog has an opt-out policy

which allows charities to decide when and if they want to be rated. At AIP, we carefully review a charity's audited financial statements, IRS form 990, including all schedules & attachments, and annual reports in order to determine how a given charity is actually raising and spending the public's donated dollars. Our rating criteria are available in each edition of the *Charity Rating Guide & Watchdog Report*, as well as on our web site at www.charitywatch.org.

The public is being bombarded with an ever-increasing amount of phone and mail solicitations from all types of charities, including veterans groups. As a nationally prominent charity watchdog organization, we are flooded with questions from both the public and the media, who want to understand how charities are using donors' hard-earned dollars. Many people are outraged to learn that under an accounting rule called AICPA SOP 98-2, charities are allowed to report large portions of solicitation costs as program service expenses.

Under current rules, a charity that includes an "action step" in their phone or mail solicitations such as "buckle your seat belt," "fly your U.S.A. flag," "hire a veteran" or "don't park in spaces for the handicapped unless you are handicapped," can claim that they are "educating" the public, and can therefore report much of the expense of these appeals as a program. Such "action steps," often relayed to potential donors through professional fundraisers, are typically messages of information that is common knowledge. Professional telemarketers, on average, keep two-thirds of the money they raise before the charity receives anything. What this means is that someone donating \$50 to charity through a professional fundraiser may have just paid \$30 to be solicited and "learn" that they should buckle their seatbelt. This is not what most donors would consider to be a charitable program.

Charities may claim that such activities are educating the public. You would not know this based on the complaints we frequently receive from donors who are fed up with the constant barrage of phone calls and mail they receive from charities requesting contributions. Based on AIP's more than fifteen years of experience reviewing such mail and phone appeals, we think it would be obvious to almost anyone that the primary purpose of solicitations is to raise funds, with the educational component being largely incidental in most cases.

The reporting requirements for joint costs, which are the program, fundraising, and management and general expenses related to solicitation campaigns that include an educational message, should be expanded so donors know what they are really paying for. The public accounting profession in its nonprofit audits and the IRS in its nonprofit disclosure report called the Form 990 should add an additional requirement in which charities would disclose their five most expensive solicitation campaigns, including a breakout of each campaign's program, management and general and fundraising expenses, and the method used for allocation. The nonprofit should also provide a fair description of the program being conducted in conjunction with each solicitation that cites specifically what is being accomplished and why the recipient of the solicitation has a use or need for the information.

Another technique that charities use to inflate the amount they report spending on program services is to include large amounts of donated goods and services in their financial statements. Lumping donated goods and cash into the same pool can produce very misleading results when

attempting to discern how efficiently charities will use cash contributions in forwarding the causes donors are intending to support. AIP makes a distinction between cash and donated goods when determining how efficiently a charity is operating and offers an “apples to apples” comparison with charities that do not obtain in-kind donations. When charities report a high percentage of their expenses going to program services, it may be far less when in-kind items are excluded.

A good example of questionable in-kind items flowing through the financial statements of veterans charities is the \$18,750,000 of “phone cards” that **Help Hospitalized Veterans (HHV)** in fiscal 2006 received and passed through to its related entity, **Coalition to Support America’s Heroes (CSAH)**. These “phone cards,” which were distributed to overseas military personnel by CSAH, were not for soldiers to call home to their family but rather to make free calls for sports scores with ads provided by a company called EZ Scores. HHV and CSAH, who share the same president and founder, each counted \$18,750,000 of the sports score cards as a contribution and program expense in their respective fiscal 2006 financial statements. These sports score cards and \$2 million in donated public service airtime accounted for 85 percent of CSAH’s total program expenses reported in its 2006 financial statements.

In-kind items are difficult to value and distort the calculation of how efficiently a charity is spending your dollars. Charity financial statements often disclose the amount of donated items that are collected and distributed. However, they do not always tell you how useful these items are to the final recipient, or if they will even result in additional problems such as disposal fees for unusable items. (See *Appetite Stimulants for the Starving* at www.charitywatch.org). Sometimes groups accept in-kind goods of questionable value that they cannot use, simply to puff up their program expense. In other cases, groups may be told by a company looking for a tax deduction that they either must accept all the goods the company wants to give, or get nothing. The ability of the charity to use or distribute said goods is not always given primary consideration. More importantly, a charity’s ability to obtain and distribute donated goods has little relevance as to whether a charity efficiently spends its cash donations. For these reasons, donated items are generally excluded from AIP’s calculations of program and fundraising ratios. AIP gives favorable ratings to many groups that receive and distribute large amounts of in-kind items and are still able to use their cash efficiently.

AIP strongly believes that charities should report their finances in a way that gives the public a better understanding of how their contributions are being used. Charities should also be required to make available to the public their audits and tax forms within one year of the end of their fiscal years. The failure to do so should incur the risk of losing their ability to offer tax deductions on contributions during the time that the reports are over one year late. Donors need better and more timely financials in order to evaluate a charity’s current level of efficiency.

Excessive Available Asset Reserves

Another practice that is keeping veterans from being helped is the policy of some charities to hoard money that is desperately needed now by veterans, particularly the estimated 200,000 homeless veterans, which account for one-third of the adult homeless population. As reported in

AIP's August 2006 *Charity Rating Guide & Watchdog Report*, the official armed forces charities for the U.S. Army, Air Force, Navy and Marines are holding massive asset reserves. These three charities, which provide financial, educational and other assistance to current and past members of the armed services and their families, have combined fund balances of \$638 million yet spent only \$59 million, according to their 2005 financial reports. **Army Emergency Relief (AER)** tops AIP's list of charities with large asset reserves in relation to expenses with 17.6 years of available asset reserves and a fund balance of \$307 million as of 2005. This means that AER could continue to operate at current spending levels without raising another dime until the year 2023. **Air Force Aid Society (AFAS)** has 10.1 years of available asset reserves and as of 2005 holds fund balances of \$172 million. **Navy-Marine Corps Relief Society (NCRS)** has fund balances of \$158 million as of 2005. Its years of available assets is lower at 4.8, just low enough to keep them from earning an automatic F grade for charities having over 5 years worth of available reserves. AIP believes that charities that hold more than 5 years of available assets in reserve have a poor basis for which to ask for additional funds.

Why are these large stockpiles of reserves not going to aid the vast numbers of homeless veterans? The answer is that most of the homeless vets do not meet the armed forces charities' eligibility requirements. For instance, AER states that it only helps active duty soldiers and reservists and their dependants, or soldiers retired from active duty due to reaching age 60 or to "longevity," usually defined as 20 or more years of service, or physical disability. AER also helps surviving spouses and children of soldiers who died while on active duty or after retirement from the military. Since poverty is the major cause of homelessness, the veterans eligible for AER assistance due to having obtained Army retirement status and the accompanying Army benefits are not likely to become homeless. It's a shame that AER's eligibility requirements keep aid from reaching those veterans that arguably need it most.

While these armed forces charities do accept contributions from the general public, most of their contributions come from armed services personnel through payroll deduction plans. Little to no funds come from the U.S. Government. They are very efficient fundraisers; each has a cost to raise \$100 of only \$2 to \$3 in 2005. Also, each of these charities spends a very high percentage (93% to 94%) of its budget on charitable programs.

The armed forces charities operate more like private foundations than emergency relief charities. Private foundations typically spend only a small portion of asset reserves, usually 5% of their investment portfolio, whereas emergency relief charities generally spend most of their donations in the year received. For example, AFAS reports on its web site, www.afas.org, that throughout its 64 years of operations some donations were put into an investment fund for contingencies and future programs. AFAS' 2005 audit says its current policy is to spend annually about 6% of its investments.

I asked Col. George Mason, Treasurer of AER, why it was not spending more of its available asset reserves to assist needy veterans. He said, "the key reason and probably the only reason" is "the unknown contingencies faced on a daily basis." He said that the largest outflow of funds from AER was 15% during a 1.5-year period in the early 90's as a result of Operation Desert Storm and Desert Shield. I replied that based on AER's reasoning for holding its high level of

asset reserves, the American Red Cross could claim that it needed to hold a few billion dollars in reserve in the event of another Katrina scale hurricane. Many other charities could also claim that they need to hold large reserves for unknown contingencies. The problem with this reasoning is that there are not enough charitable dollars to go around for groups to stockpile massive reserves for events that may never happen. Groups that hold over five times their budget in reserve are limiting the supply of money for other charities that need it to meet their annual budgets so that they don't have to turn away those in immediate need. Certainly, it is reasonable for some charities to maintain reserves worth a year or two, but to hold available reserves for over five years worth their budget is, in AIP's opinion, excessive.

I asked why AER wouldn't undertake a special public fundraising campaign in the event of a large, protracted war, rather than holding 17.6 years of asset reserves that could be used to assist veterans now. He said that traditionally AER has refrained from actively soliciting the public. AER's audit reports that 35% of its total contributions were "unsolicited." Its web site, www.aerhq.org welcomes contributions from "Army or civilian individuals or organizations."

I also asked Col. Mason if AER was doing enough to inform soldiers and veterans of the availability of charitable aid. He said that \$100,000 had been spent to publicize AER over the last 6 months and cited some new outreach efforts, including 45-minute classes for brigade commanders and spouses, and briefings to Army Reserve and National Guard. He said that traditionally 8% of the Army utilizes AER and that they would like to increase that to 10%-12%.

Misuse of Congressional Charter Status

Veterans charities that prominently state or display their congressionally chartered status are confusing the American public. Many of the major veterans groups are chartered by acts of the U.S. Congress, including **American Ex-Prisoners of War, AMVETS, Disabled American Veterans, Jewish War Veterans of the USA, Paralyzed Veterans of America and Veterans of Foreign Wars of the U.S.** According to a 2004 report by the Congressional Research Service, Congressional charter status does not mean that the U.S. government approves these groups' activities and provides oversight. That report also stated that Congress has never pulled a charity's charter status. Congressman Barney Frank was cited in a 1992 Washington Post article as calling charters "a 'nuisance,' a meaningless act. Granting charters implied that Congress was exercising some sort of supervision over the groups and it wasn't." In order to reduce public confusion, AIP believes charities that wish to promote their Congressional charter status should be required to state that this status does not imply endorsement, approval or recommendation by Congress.

Conclusion

AIP strongly believes that our brave veterans, as well as the intentions of donors who sincerely want to help them, are being dishonored by poorly rated veterans charities. Too little of America's donated dollars given in the name of veterans are actually benefiting veterans. AIP encourages the public to support accountable veterans charities that raise money efficiently and spend a high percentage of their budget on bona-fide charitable programs that substantially assist veterans. We would also like to see Congress, the IRS and the states create and enforce rules that motivate veterans groups and other charities to better fulfill their important missions.



VETERANS & MILITARY



American Ex-Prisoners of War Service Foundation		423-453-2820	4	85	F	<50
American Veterans Relief Foundation		800-215-6782	1	84	F	<50
AMVETS National Service Foundation		800-810-7148	29-46	40-55	F	83-119
Armed Services YMCA of the USA		703-313-9600	84	18	A-	251
Blinded Veterans Association		202-371-8880	43-76	21-55	D	72-97
Disabled American Veterans		859-441-7300	50-68	30-49	D	198-277
Fisher House Foundation		888-294-8560	92	2	A+	100-352
Freedom Alliance		703-444-7940	23-56	24-43	F	51-131
Help Hospitalized Veterans						
/Coalition to Salute America's Heroes		909-926-4500	31-53	39-61	F	254-426
Intrepid Fallen Heroes Fund		800-340-4376	95-97	1-2	A+	106
Military Order of the Purple Heart Service Foundation		703-256-6139	28	62	F	121
National Military Family Association		703-823-6632	82	9	A	53-60
National Veterans Services Fund		203-656-0003	2	97	F	60
National Vietnam Veterans Committee		202-408-0944	48-54	46-54	D	116-222
NCOA National Defense Foundation		703-549-0311	27-73	25-78	F	<50
Paralyzed Veterans of America		800-424-8200	34-64	30-60	F	190-223
Soldiers Angels		615-676-0239	36	48	D	<50
USO (United Service Organizations)		800-876-7469	67	39	C+	202-492
Veterans of Foreign Wars of the US and Foundation		816-756-3390	56-70	32-52	C-	202-236
Veterans of the Vietnam War & The Veterans Coalition		800-843-8626	41-52	41-54	D	54
Vietnam Veterans Memorial Fund		202-393-0090	41-61	21-36	D	52-130
Vietnow National Headquarters		800-837-8669	11	90	F	N/A
World War II Veterans Committee, a program of American Studies Center		703-302-1012	48-54	46-54	D	116-222

Grades Reduced for Charities with Large Asset Reserves



Army Emergency Relief	93	3	17.6	307,288	A+	F
Air Force Aid Society	93	3	10.1	172,209	A+	F
Navy-Marine Corps Relief Society	94	2	4.8	158,722	A+	C

Key of Symbols in the Guide



in the Rating Guide indicates the percent spent on program services. AIP's Target is 60% or more.



in the Rating Guide indicates the cost to raise \$100. AIP's Target is \$35 or less.



in the Rating Guide indicates a charity's grade based on percent spent on program services and cost to raise \$100.



in the Rating Guide gives the telephone number of the charity.



in the Rating Guide indicates whether a group has an open book status or not.



in the Large Asset Reserve Chart indicates an organization's years of available assets. AIP's target is three years or less.



in the Large Asset Reserve Chart indicates an organization's recent fund balance.



indicates charities that have provided the following documents to AIP: annual report, complete audited financial statements and Internal Revenue Service Form 990, with Schedule A where applicable.



in the Rating Guide indicates a charity's top salaries.



in the Large Asset Reserve Chart indicates grades reduced due to high asset levels.

AIP strongly believes that your dollars are most urgently needed by charities that do not have large reserves of available assets. AIP therefore reduces the grade of any group that has available assets equal to three to five years of operating expenses, and assigns an F to groups with over five years of reserves. In AIP's view, a reserve of less than three years is reasonable and does not affect a group's grade.

These reductions in grades are based solely on the charities' asset reserves as compared to budget. If you agree with these charities that reserves greater than three years budget are necessary to enhance their long-term stability, you may wish to disregard the lower grades that AIP assigns on the basis of high assets. AIP's definition of "years of available assets" includes funds currently available for the charity's use, including investments that the charity has set aside as a reserve but could choose to spend if it wanted to do so.