Statement of Geoffrey W. Peters
House Committee on Oversight and Government Reform
Hearings to Assess Veterans' Charities – January 17, 2008

Good Morning and thank you for your invitation to provide testimony concerning direct response fundraising and charities in general, and veterans charities in particular.

When Mr. Williams contacted me on Monday to invite me to testify today and then when we spoke on Tuesday, I asked what information I could provide that would be of use to the committee. Mr. Williams indicated that information on the costs of fundraising would be helpful and so I will address that complex issue briefly in these opening remarks.

Introduction

The so called "cost of fundraising ratio" is commonly a calculation of the percentage of funds spent by a charity on fundraising as a proportion of either income or total expenditures. This ratio is often used, or I should say misused, to evaluate the charity in some manner. Most frequently it is said that "good charities" have a high percentage of funds spent on programs as opposed to fundraising and administration and "bad charities" have low percentages spent on programs. Some refer to this as a measure of the "efficiency" of a charity. In the testimony of Mr. Borochoff before this committee he places great emphasis on this ratio and gives a failing grade to charities that do not meet his standards in this regard. Thus his reports are often not only wrong they are frequently misleading.

The focus on this measure is misplaced and more frequently than not leads to erroneous conclusions. This is not just my opinion, it is the opinion of nearly every major organization representing nonprofits in the charitable sector and is the opinion of nearly every serious scholar who has done research into the topic. It also happens to be the opinion of the Supreme Court of the United States.

Let me be clear. If a donor asks for information regarding a charity's expenditures and what the money they spend is used for – the donor should always be given a clear, accurate and transparent answer. If a charity or its staff are engaged in improper or illegal activity – they should be held legally accountable for that activity. It benefits no legitimate charity to have real fraud occur within our community as it damages the reputations of all charities and the public confidence in our sector when real fraud occurs. As Ms. Johns can testify, I have taught sessions on how to detect charitable fraud for the National Association of State Charity Officials and I support any efforts that this Committee can make to provide the necessary finances to assist state and federal officials to detect and prosecute fraud.

However, let me also be clear that fundraising cost ratios are neither a useful measure of charity efficiency nor do "poor" ratios signify fraud.

In theory the fundraising ratio is an attractive device for evaluating charitable operations and fundraising. It is deceptively simple and convenient to those who have a "one size fits all" view of how one might evaluate the work of nonprofits and charitable fundraising. However, in practice it is not a reliable assessment of a nonprofit's effectiveness or integrity. Rather, it is an invitation, at a minimum, to confusion and error and, at worst, to manipulate data for illegitimate ends all disguised as an invitingly simple percentage figure.

Reports of charitable fraud incite tremendous public outrage. In response government regulators and prosecutors as well as private sector "watchdog" organizations seek to separate the "good" nonprofits from mismanaged nonprofits and outright scams. Both often fail to understand the complexities and unreliability of fundraising ratios.

In addition to the problems with defining a measure that might be consistent, nearly every study done of this by charity experts, economists, legal scholars, and fundraising experts has concluded that such a measure is useless at best and misleading at worst. I won't bore you with a long list of citations to the research but I enclose my sources in my written statement for your review.[1]

For decades those of us who work in the charitable sector have seen the fundraising ratio mislead the public, become misused for political and public relations purposes,[2] and have generally found it to be a vexatious concept. This is primarily because there is no demonstrably rational, objective basis upon which to calculate the fundraising ratio so that it lives up to its promise of being a unitary measure of fraud or efficiency for most nonprofits under most circumstances.[3]

Economist Richard Steinberg who has extensively studied costs of fundraising notes:

> The costs of efficient fundraising are highly idiosyncratic, varying with organizational age, mission, press coverage, competition from other fundseekers, scale, experience, perceived levels of need, the economic well-being of potential donors and a variety of other factors. Charities situated in favorable fundraising environments may be highly inefficient and still secure low fundraising shares, whereas charities advocating unpopular causes or prospecting for new donors will have high fundraising shares (perhaps exceeding 100%) even if they operate at the limits of efficiency.[4]

And the Supreme Court, in a decision that has been reaffirmed on multiple occasions over the past two decades, has indicated that the fundraising ratio has little value as an indicator of fraud.[5]

The "cost of fundraising" or fundraising ratio purports to be the percentage or ratio of every charitable donation raised that was spent on fundraising expenses. In other words, it seeks to reduce a nonprofit's "efficiency" to a simple percentage. Thus, fundraising ratios are attractive to the government regulators and watchdogs that calculate them according to their own rules and use them to rate nonprofits, with little or no explanation, understanding, or context.

Many potential donors do not understand the lack of scientific or economic basis inherent in fundraising ratios and thus reports of such by government agencies[6] and watchdogs may be influential. And a fundraising ratio can grievously damage a nonprofit's reputation when it is calculated without regard to the proper context.

No one, not fundraising experts, government regulators, tax authorities, consumer advocates, nor Attorneys General, has defined the fundraising ratio in a uniform fashion or in such a way as to make it a useful or reliable indicia of fraud or philanthropic efficiency. The problems associated with calculating a fundraising ratio are legion:[7]

- What is the proper time period over which data is gathered? One month? One quarter? One year? Several years? The length of a particular campaign?

- Should the numerator include or exclude "joint expenses" involving fundraising but which also advance the mission of the organization?
- Is the denominator the total of the nonprofit's expenses (as is done in Illinois) or the total revenue?
- How does one account for the residual value of byproducts of the solicitation? For example, what is the value of a deferred gift? What is the value of having identified a significant donor who will give over a period of many years? What is the value of recruiting an unskilled but loyal volunteer? What is the value of recruiting petition signers who choose not to donate?
- How does the nonprofit's commitment to building financial reserves factor into the fundraising ratio?
- How does one properly account for investments made in building a list of future donors – are these expenses or capital investment activities?
- Should the denominator be focused upon expenses or funds raised by any method or only by that particular campaign?
- Should the results of different methods of fundraising (e.g. telemarketing, direct mail, direct response TV, direct response radio, telethons, radio-thons, special events, corporate giving, foundation giving, government grants, major donor giving, lapsed donor renewal, membership recruitment and renewal, new donor acquisition, e-mail solicitation, etc.) each be measured independently for its own fundraising ratio or should the nonprofit be measured on its combined overall efforts?

A. What is the proper time period over which data are gathered and reported?

Consider a hypothetical nonprofit that begins a program of soliciting contributions through direct mail. Generally it must begin with a "prospect mailing" in which the nonprofit sends letters out to people who have not previously supported the nonprofit. Viewed alone, these campaigns have a very high cost. Often, they lose money.[8] The purpose of the prospect mailing is to identify donors willing to contribute <u>in the future</u> to the nonprofit's cause.

Once these new donors are identified, the nonprofit continues to solicit additional donations from these newly found supporters over a period of years, thereby recouping the initial cost and producing a net gain.

At some point in time, some of those donors will stop giving, and these "lapsed donors" must be replaced by prospecting for new donors, which begins the cycle again.[9]

How would the fundraising ratio be properly calculated?[10] Would one look at simply the first prospect mailing? If so, it is quite likely that the fundraising ratio will be "too high." This would stop the campaign before it starts.[11] Moreover, this would be misleading.

The whole point of the prospect mailing was to identify long term donors. Wouldn't it be less misleading if some of the long term value these donors will provide to the nonprofit could be included in the fundraising ratio calculation?

This then leads to the question – over what time period should this cost (investment) vs. revenue (return on investment) be calculated? – one quarter? – one year? – the estimated period during which the donor will continue to donate?

What about an analysis of a whole campaign? There are two immediate problems with this approach. First, it is unlikely that regulators would consider a fundraising ratio reported at the end of a multi-year campaign to be timely and useful information. Second, there is no accepted industry definition of "campaign." When does one campaign begin and another end?

Choosing any period can skew the results depending upon the fundraising activities in which the charity may be engaged, which is why this measure is simply not useful. If, for example the charity is just commencing a major fundraising drive, then the fundraising ratio for that year may be significantly higher than for the subsequent years when that first year's investment produces a return. Yet U.S. accounting rules prohibit nonprofits from amortizing the investment in creating a mailing list so as to properly match expense (investment) and revenue (return on investment).[12]

Thus, a start-up charity may not amortize or allocate the fundraising expense to the same periods in which the income is realized, but rather must suffer from a very high initial cost of fundraising as the charity makes significant investments in its future.

Once new donors are identified, their names and addresses often go onto a general mailing list that is used for other fundraising purposes including appeals for special projects, capital campaigns for new buildings, seeking gifts through wills and bequests, quarterly newsletters that may include an incidental opportunity to donate, and any number of other communications.

Even if the fundraising ratio of a campaign is calculated by the charity, it is often based only on the immediate results and not the value of having identified donors who may, for example, leave bequests. There is no logical time period during which such a calculation can be made.

Sometimes charities have multiple distinct charitable missions or programs, each of which has "earmarked" fundraising. Should each one have a different calculated fundraising ratio? If not, doesn't that mean that the "campaign" is effectively indefinite since the other missions will continue even if one is completed?

There is no agreed upon definition of the fundraising ratio in part because there is no agreement on any particular time period over which the calculation should be made.

B. What expenses and income are properly allocated to the fundraising ratio's numerator and denominator?

Assuming that the measuring period problem could be solved, there's still a problem of classifying what goes into the numerator and what goes into the denominator in order to calculate the fundraising ratio.

Each state tends to formulate its own methodology, some of which are vague. West Virginia requires nonprofits to calculate their "fund-raising percentage" by dividing "fund-raising expenses" by "income derived from fundraising."[13] Missouri requires nonprofits to report the "percentage of funds directly spent on fund-raising or directly allocated for fund-raising activities"[14] And Utah requires nonprofits to report "fundraising costs as a percentage of contributions" using data from the nonprofit's most recent Form 990.[15]

1. The Numerator: Solicitation expenses

Presumably the numerator is the amount of money spent soliciting donations or "fundraising." Money spent advancing the charitable mission should not be included.[16] Of course, this seems a simple distinction in theory; but in reality it is quite nettlesome. In many instances, the act of solicitation advances the charitable mission.[17]

Consider a nonprofit dedicated to women's health. A particular mass mailing might remind women to conduct a periodic breast self-examination. In part to defray the costs of the mailing and also to advance other aspects of the organization's mission, the letters might also include a solicitation for donations. The act of solicitation is inextricably bound up with the nonprofit's mission.[18]

Should the cost of these "educational" mailings be included in the fundraising ratio numerator or not? Apparently Illinois thinks they should not because their calculation of fundraising costs do not account for these activities.[19]

If the calculation of the numerator in the fundraising ratio is based on mission related expenses then the calculation depends upon a precise definition of the charity's mission. Is it the mission as set forth in the organization's articles of incorporation? Is it the mission as enunciated in its application for tax exemption and upon which exemption was granted? Is it the mission as stated in its informational tax return on IRS Form 990? Is it the nonprofit's current mission statement? Or is it the content and tenor of a specific appeal?

2. The Denominator: The amount raised

Calculating the denominator in the fundraising ratio, the amount of money raised, presents difficulties as well. Of course, determining the value of cash, checks, securities and even donated property such as works of art is straightforward. But the eleemosynary act takes many forms. How are donated services valued? The tax rules place a particular value on them only if they are derived from special skills while unskilled labor is assigned no value at all. Will state attorneys general and local regulators and charity watchdogs follow this rule?

There are, of course the same definitional problems as previously discussed. What is to be included in the denominator? Are funds raised only from a particular medium (e.g. telemarketing or a special event) to be included in both the numerator and denominator? Or, should one include all funds raised from all types of public solicitations in the denominator? Or, instead, should one include all revenue regardless of source (including government grants, service income, bequests, etc.) thereby lowering the fundraising ratio as a result of, for example, revenue from patients or government grants?

What about the value of future donations from new donors identified in prospecting campaigns? What about pledges and other promises to give (e.g. "I've left some money for your organization in my will")? They are not normally considered current income under U.S. accounting rules. Should charities avoid soliciting such gifts because the costs of solicitation will be recorded immediately while the substantial benefits may not occur until a later time period, thereby subjecting the charity to allegations of fraud? What if the nonprofit knows from years of experience that it can expect a certain percentage of pledges to be honored? What happens if pledges are honored or dishonored at an unusual rate in a particular year and the fundraising ratio reported earlier turns out to be in error?

C. Characterization of reserves

Assuming that one could resolve the measuring period problems and the numerator/denominator problems, there's still the difficulty of how to account for nonprofits that build reserves. Many nonprofits make it a priority to save a certain percentage of their income to build an endowment, to create a "rainy day" fund, to build new facilities, or to advance some other legitimate purpose. Most applaud this approach and view it as responsible management. Where would our major universities in the United States be if they were not permitted to collect and maintain endowments?

Others find the practice irresponsible and claim the nonprofit is not advancing its mission as aggressively as possible and is essentially "making a profit" from its charitable solicitations.[20] Will the federal authorities, fifty state regulators and hundreds if not thousands of local regulators view the practice in a consistent way?

Worth magazine listed one charity as one of the best nonprofits in the US. The authors went out of their way to explain that "'the conservation groups' ratios are skewed because they are forced to report land acquisitions as a capital cost rather than a program expense."[21] Retained earnings from other nonprofits would not necessarily be handled this way. Should such variations in accounting and reporting rules, which have a powerful effect on a nonprofit's fundraising ratio, become the basis for decisions about whether that charity is worthwhile or not?

Conclusion

Many years ago when I first started working in this field I attended a conference of charities that do international relief work. A panel consisting of the representative of a watchdog organization and the editor of Money magazine presented their findings which had been published and widely circulated about the "most efficient charity in the United States." Clearly the goal was to get the public to donate to the most "efficient" organizations rather than others. They then announced that one organization had a 99+% efficiency and named the group because 99% of all donated funds were used for programs.

I was surrounded by experts in international relief work and they all started to laugh. I inquired why. They told me that the charity in question was known for taking millions of dollars of gifts in kind ranging from Pop-tarts to outdated books on accounting written in English and shipping them to port cities in Africa where the materials would be unloaded and distributed to whoever was present and wished to avail themselves of these materials. The books were not used in education, they were burned to provide heat and the Pop-tarts and other excess inventory junk food was consumed by whoever stopped by to get them.

The charity achieved its efficiency by delivering millions of dollars of donated goods that were of marginal utility and spending next to nothing on staff and infrastructure.

The experts I was sitting with told me that real efforts to solve the problems of poverty and hunger in Africa were not focused on port cities but inland and involved having charity staff who could work on problems of sustainable agriculture, irrigation, construction of homes and schools and the like. Thus, those organizations had staff and trucks and equipment and expenses that required a certain amount of administrative overhead and as a result they were viewed on this measure as less efficient.

Just this month a wonderful and widely acclaimed new book was published called "Forces for Good: The Six Practices of High-Impact Nonprofits."[22] The authors extensively studied nonprofits that are making real differences in the world by accomplishing their mission. They describe in detail why program service and fundraising cost ratios are simply not useful.

> The problem with using these metrics is that they fall into the trap of measuring financial inputs or ratios as a proxy for success, rather than measuring impact, or the amount of change accomplished with that investment. Worse yet, they assume that nonprofits can implement programs without any infrastructure or support. They may encourage donors to support groups that spend too little on people, IT systems, or management, which can lead to weak organizations at best, or accounting trickery at worst.
>
> The nonprofits we identified [as high impact nonprofits], however, don't spend too much time worrying about these metrics. They spend what they need to sustain their impact.
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> . . .
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> In the business world, it is widely recognized that having a superior company enables success. It takes money to make money. But in the social sector, the idea still remains difficult for donors to grasp.[23]

The authors go on to list six myths about nonprofits that need to be dispelled.

> Myth 5: High ratings on conventional metrics. When we looked at traditional measures of nonprofit efficiency, such as ratings on Charity Navigator, many of these [high-impact] groups didn't score so well. A few garnered only one or two stars out of a total of five. These ratings Web sites can tell you which groups have the lowest overhead ratios, but they can't tell you which have had the most impact.

The most extensive database on nonprofits and their reported annual financial results in the United States has been compiled and published on the Internet as "Guidestar."[24] The chief executive of Guidestar's parent nonprofit organization has spent a great deal of time thinking about the various ratios that can be calculated to measure the performance of nonprofits. He says:

> In the final analysis the worthiness of a charity is a function of the unique value set of the individual donor. Some donors like large, endowed institutions that work on a long-term society need. Others like fast growing, cash-poor organizations that attend to acute needs. There are scores of potential models for assessing the value of a charity. In our opinion, "efficiency" per se, based upon certain financial ratios is probably not a good measure unless you are looking at a single organization's financial progress over time or at a group of very similar peer organizations. If you are looking at ratios as an indicator of worthiness, remember that the age, growth rate, dependence upon donations from the public (as opposed to foundation or government grants or earned revenue), and type of work (research, education, direct service, resource pass-through, etc.) will likely all have far more to do with the reported ratio than the fundamental operating efficiency of the organization.[25]

With all due respect, I would hope that this Committee will not add weight to the myths about the nonprofit sector which not only mislead the public but discourage them from participating by volunteering, donating and generally supporting worthwhile missions. We have too many headline seekers posing as leaders both within our own nonprofit community and in the political community as well.

As Einstein famously said: "Everything should be as simple as possible, but not simpler." Please do not allow yourselves or others to think that these simple metrics of cost of fundraising ratio or program services ratio are useful or valuable measures of anything. Look instead at the work that is really done by the organizations you are studying and let their work inform your judgment of their worth.

ENDNOTES

[1] The problems with using this crude measure are revealed in numerous scholarly studies of the matter. See, generally, Espinoza, Straining the Quality of Mercy: Abandoning the Quest for Informed Charitable Giving, 64 Southern California Law Review 633 (1991); Frumkin & Kim, Strategic Positioning and the Financing of Nonprofit Organizations: Is Efficiency Rewarded in the Contributions Marketplace?, 61 Public Administration Review 266-275 (2001); Greenlee & Gordon, The Impact of Professional Solicitors on Fund-Raising in Charitable Organizations, 27 Nonprofit and Voluntary Sector Quarterly 277-299 (1998); R. Rettig, Cancer Crusade: The Story of the National Cancer Act of 1971 (1977); Rose-Ackerman, Charitable Giving and "Excessive Fundraising", Quarterly Journal of Economics 97 (1982); Sargeant, Using Donor Lifetime Value to Inform Fundraising Strategy, 12 Nonprofit Management and Leadership (2001); Smallwood & Levis, The Realities of Fund-Raising Costs and Accountability, The Philanthropy Monthly (September 1977) (also found at http://www.nonprofits.org/misc/fps/realities.html); Steinberg, Should Donors Care About Fundraising? in S. Rose-Ackerman, ed., The Economics of Nonprofit Institutions 347-364 (1986); Steinberg, Economic Perspectives on Regulation of Charitable Solicitation, 39 Case Western Reserve Law Review 775 (1988); Steinberg, Profits and Incentive Compensation in Nonprofit Firms, 1 Nonprofit Management and Leadership 137-151 (Winter 1990); Steinberg, The Economics of Fundraising, in D. Burlingame & L. Hulse (Eds.), Taking Fund Raising Seriously, 239-256 (1991); Steinberg, On the Regulation of Fundraising, in D. Burlingame (Ed.), Critical Issues in Fundraising 234-246 (1997); Titus, Heinzelmann & Boyle, Victimization of Persons by Fraud, 41 Crime and Delinquency 54-72 (1995); Watkins, Discussion on the Cyber-Accountability List-Serv, archived at cyb-acc@CharityChannel.com., #2002-140 (Aug. 24, 2002), Are ratios useful? For donors? For the community? (found at http://www.nonprofit-info.org/npofaq/11/14.html)(1996).

[2] Former California Attorney General Lungren issued a Press Release prior to Christmas in 1994 (Attorney General of California, Press Release 94-120) and a report Attorney General's Report on Charitable Solicitation by Commercial Fundraisers (1994) in which at least one charity, Christian Appalachian Project, was castigated for an excessively high fundraising ratio. Unfortunately, the report did not differentiate between full fledged fundraising campaign and small feasibility test conducted to determine whether a campaign was viable. In this case the charity conducted a small feasibility test of telemarketing to lapsed direct mail donors. The costs were, as might be expected, high because it was a small test. However the charity's annual report filed with the California Attorney General in that year showed its *overall* cost of fundraising *for the year* was a mere 18% of income.
The Attorney General of New York issues a similar report each year. See, Spitzer, Pennies for Charity – Where Your Money Goes (December 2002).

[3] [F]actors other than honesty and efficiency … drive the fundraising cost ratio. For example:

- It could be a start-up charity without a donor base
- It could be an organization with an unpopular mission, such as a home for unwed mothers, where many people must be contacted in order to find a few concerned donors who are not deterred by social stigma
- It might be a national charity that is supported by a small but loyal group of donors who are scattered across the country and make relatively small donations per capita.
- It could be an organization that is precluded from using a fund raising method that tends to deflate the fund raising cost ratio, such as the use of volunteers to solicit door-to-door or special events to raise funds locally. ...

Even if it were feasible for an organization to use a fund raising method that will deflate the fund raising cost ratio, it may still be a responsible decision to use a method that boosts the ratio. For example, a cause-oriented group may need to maximize the number of adherents in order to further its program mission. For that group, it may be worth it to use direct mail even at a loss in order to find more adherents."

Miller, Suggestions to Improve Private Standard Setting for Charities: The NCIB Proposals, Philanthropy Monthly 14 (Nov. 1987).

[4] Steinberg, On the Regulation of Fundraising, in D. Burlingame (ed.), Critical Issues in Fundraising, 234-246 (1997) (parenthetical in original).

[5] Riley v. National Federation of the Blind of North Carolina, Inc., 487 U.S. 781 (1988).

[6] Some state regulators publish fundraising ratio data on state managed websites. See, e.g., Kansas' "Charity Check" website http://www.kscharitycheck.org/search.asp where fundraising ratio is based upon the ratio of "fundraising expenses" to "gross receipts." See also, http://web.dos.state.pa.us/charities/dsf/explain.cgi which

explains the calculation done by Pennyslvania. Charity Navigator, one of several "watchdog" groups, measures amongst other things "fundraising efficiency" based on the percentage of total contributed revenue expended on fundraising. See, http://www.charitynavigator.org/index.cfm/bay/content.view/catid/2/cpid/35.htm.

[7] "[T]here is no uniform method for measuring fund-raising expenses. Indeed, there is disagreement within the nonprofit field over the definition of fund raising, including when and how to allocate costs between program and fund-raising activities." Hopkins, A Struggle for Balance, Advancing Philanthropy 26-31 (Fall 1995).

[8] "[A] solicitation may be designed to sacrifice short-term gains in order to achieve long-term, collateral, or non-cash benefits." Riley, 487 U.S. at 792. "Experienced fundraisers seem to agree that direct-mail prospecting is considered effective if it breaks even (e.g., Bergen, 1991; Bush, 1991; Warwick, 1994)." Greenlee & Gordon, The Impact of Professional Solicitors on Fund-Raising in Charitable Organizations, 27 Nonprofit and Voluntary Sector Quarterly 277, 284 (1998).

[9] "One third to one half of first-time donors will never make a second gift. The pool of previous donors (the 'house list') also suffers from attrition or what Rosso (1991) calls 'the transiency factor.' According to Royer (1989), 60% of gifts to many charities come from people aged 60-76. As these donors die, lose interest, and so forth, the charity must find replacement donors. Accordingly, prospecting tends to be an ongoing process, but, for established organizations, the high cost is masked by the efficiency of resolicitations of the house list." Greenlee & Gordon, The Impact of Professional Solicitors on Fund-Raising in Charitable Organizations, 27 Nonprofit and Voluntary Sector Quarterly 277, 284-85 (1998).

[10] Many contracts for fundraising services are based on flat fees for particular services rather than percentages. Therefore the fundraising ratio cannot be determined merely by reference to a commission set in the contract. Instead, revenues or expenses and costs of fundraising for like periods must be compared after the fact.

[11] The nonprofit, fearing a reputation-damaging fraud investigation, would likely be too afraid to even begin a direct mail campaign. Even if it did begin, the nonprofit might face a fraud investigation just after the prospect mailing which would prevent the nonprofit from ever recovering the investment it made in the prospecting.

[12] Instead of treating the ongoing operational investment in building a mailing list just as any other asset that might be purchased and then expensed over a number of years, U.S. accounting rules require treating such operational investments as expenses in the year made despite the fact that revenue associated with those expenses will occur later. See, American Institute of Certified Public Accountants, Audit and Accounting Guide for Nonprofit Organizations ¶ 13.06 (2002). By contrast, other countries such as Germany, the Netherlands, France, etc. allow nonprofits to amortize investments in mailing lists just as investment in any other asset may be amortized.

[13] See http://www.wvsos.com/forms/charity/chr1.pdf at page 4.

[14] See http://www.ago.state.mo.us/charities/charityannualreport.pdf at page 1.

[15] See http://www.commerce.utah.gov/dcp/downloads/permitapps/charitableorganization.pdf at page 4.) Although, for Utah, a nonprofit can rely on the Form 990 instructions for a degree of certainty in calculating his fundraising ratio, Missouri and West Virginia give very little guidance on how they expect the fundraising ratio to be calculated.

[16] The American Institute of Certified Public Accountants, Accounting for Costs of Materials and Activities of Not-for-Profit Organizations and State and Local Government Entities that Include Fundraising, Statement of Position 98-2 ("SOP 98-2") regarding accounting for expenses that are allocable between fundraising and program services specifically provides the rules for this. In order for a charity to receive a "clean" audit opinion, they must follow these rules despite the fact that organizations such as the American Institute of Philanthropy disregards these official rules when doing its ratio calculations.

[17] "Campaigns may directly accomplish the charitable mission as a side effect of fund raising. For example, political fund raising may also raise the candidate's profile, and fund drives for Mothers Against Drunk Driving (MADD) may educate the public about the dangers of drunk driving while also raising money." Steinberg, The Economics of Fundraising, in D. Burlingame & L. Hulse (Eds.), Taking Fund Raising Seriously 239-256 (1991). See also, Secretary of State of Maryland v. Joseph H. Munson Co., Inc., 467 U.S. 947, 961 (1984) and Riley v. National Federation of the Blind of North Carolina, Inc., 487 U.S. 781, 798 (1988).

[18] Economist Richard Steinberg suggests:

> Even if public education is not one of the charity's goals, the public is educated about the charity through the solicitation process, and this information is not valueless. ... Solicitation expenditures may provide socially valuable information even when they result in a decrease in donations. The information contained in solicitation literature may convince a donor who was otherwise predisposed to contribute that his interests would be better served by spending his money elsewhere. Thus, the 'public education' defense extends far beyond those charities which explicitly count advocacy or education among their goals.

Steinberg, Regulation of Charity Fundraising: Unintended Consequences, Working Paper, Indianapolis: IUPUI Dept. of Economics (1991).

[19] The Supreme Court of Illinois has already discussed this very problem in Ryan v. Telemarketing Associates, Inc., 198 Ill. 2d 345, 359-60 (2002).

> [H]igh solicitation costs, and a solicitor's high rate of retaining receipts, can be attributable to a number of factors. Certain types of fund-raising campaigns, for example include a wide range of activities that must be paid for. The present case illustrates this point. … [The] contracts [attached to the Complaint] show that, in exchange for its fee, Telemarketing agreed to supply and pay the salaries of all marketing personnel, as well as pay all costs for an office and phones. In addition, Telemarketing agreed to be responsible for producing, publishing, editing and paying all costs for the annual publication of more than 2,000 copies of an advertising magazine that would "increase community awareness of [VietNow]." The contract required Telemarketing to conduct "an efficient and professional marketing program, promote goodwill on behalf of [VietNow], and enhance good public relations." … Defendants in this case were contracted to perform a wide range of activates on behalf of VietNow, all of which were to be paid for out of [Telemarketing's contractual portion of] the solicited funds."

[20] The American Institute of Philanthropy, which earlier testified before this committee, "*reduces* the grade of any group that has available assets equal to three to five years of operating expenses." See, http://www.charitywatch.org/criteria.html.

[21] Yaqub, America's Top 100 Charities, Worth, December 2002.

[22] L. Crutchfield & H. Grant, Forces for Good: The Six Practices of High-Impact Nonprofits, Jossey-Bass 2008.

[23] Id. at 200, 203.

[24] This can be found at http://www.guidestar.org and was compiled by Philanthropic Research, Inc. a nonprofit organization. A discussion of fundraising cost ratios and their calculation and usefulness can be found on the "Guidestar" website at http://www.guidestar.org/news/features/ratios.stm.

[25] Found at http://societytalk.guardian.co.uk/WebX?14@189.mim4cojfuLb.0@.ee902fb/3.