

# PREPARED STATEMENT OF THE FEDERAL TRADE COMMISSION ON CHARITABLE SOLICITATION FRAUD

Before the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce United States House of Representatives Washington, D.C.

November 6, 2001

Mr. Chairman and members of the Committee, I am J. Howard Beales, III, the Director of the Bureau of Consumer Protection of the Federal Trade Commission. I appreciate this opportunity to appear before you today to testify on behalf of the Federal Trade Commission regarding fraudulent solicitations of charitable contributions, especially solicitations relating to the recent September 11th tragedies.<sup>(1)</sup>

## I. Introduction and Background

The Commission recognizes the important role that charitable organizations play in providing valuable services, a role that has become even more critical in the wake of the September 11th attacks. Solicitations for charitable organizations, and corresponding donations, have increased noticeably in recent weeks. So, too, have concerns about possibly fraudulent solicitation schemes seeking to exploit the overwhelming urge of the American public to aid victims of September's tragedies. The Commission has examined every complaint, inquiry, and press report raising any suggestion of such fraud. In addition, the Commission has surfed the Internet, reached out to other law enforcement agencies and watch-dog groups, and actively sought out potential fraudulent solicitors. To date, the findings of fraud are few and far between, and the Commission continues to monitor this situation as aggressively as any the Commission has ever pursued. Furthermore, the Commission has stepped-up efforts to educate consumers and businesses about how to spot potentially fraudulent solicitations.

Unfortunately, but not surprisingly, the potential for fraudulent fundraising may escalate in the aftermath of national tragedies, natural disasters, local calamities, and the like. Fraudulent solicitors, who prey upon a donor's charitable instinct, may deceive a donor about who they are and what they do with the funds they raise. The scam artists ultimately derail donors' charitable intentions, undermine the public's confidence in legitimate charitable fundraising, and, in turn, injure those legitimate nonprofit organizations that compete for a depleted pool of charity dollars. The Commission, which is the federal government's principal consumer protection agency, shares the Committee's deep concern over possible deceptive or fraudulent charitable solicitations.

Charitable organizations are closely regulated by the states. Most state governments implement detailed registration and reporting requirements that are crucial to the effective oversight of charities.

In addition to the statutory limitations on Commission jurisdiction over some charities, there are also constitutional limitations. The Supreme Court has held that fundraising for charities is fully protected speech under the First Amendment and that state statutes may not require a charity to prove the reasonableness of using more than 35 percent of its collected donations for fundraising expenses.<sup>(9)</sup> Nor can state statutes require fundraisers to disclose the percentage of donations the fundraisers keep.<sup>(10)</sup>

Against this background to the regulation of charities, the Commission now addresses your particular concern about fraudulent charitable solicitations, especially those relating to the tragedies of September 11th. The need - and challenge - for law enforcement here is three-fold: (1) to monitor developments closely and systematically so as to swiftly identify possible law violators, sharing that intelligence with other law enforcers; (2) to act quickly and effectively if someone violates the law; and (3) to educate consumers and businesses about how to spot potentially fraudulent solicitations, hopefully minimizing the extent to which deception of contributors will occur. As set forth

below, on the heels of September 11th, the Commission set up a disaster scam project to accomplish these important tasks.

## **II. The Commission's Efforts to Identify Fraudulent Charitable Solicitations and Other Disaster-Related Scams**

Immediately after September 11th, the Commission stepped-up its monitoring, on a systematic basis, of consumer complaints, tips from other law enforcers and watch-dog groups, and media reports about possible charity fraud and related scams. The Commission reviewed each one and continues to do so today. In addition, the Commission has surfed the Internet, reached out to other law enforcement agencies and watch-dog groups, and actively sought out potential fraudulent solicitors. There has been some media coverage warning that scam artists may try to take advantage of consumers' desire to help victims of the attacks. The Commission has not discovered any widespread problem but continues actively to monitor this area.

### **A. Consumer Sentinel**

A central part of the Commission's monitoring effort is Consumer Sentinel, a web-based consumer complaint database and law enforcement investigative tool that the Commission uses to identify targets for investigation.<sup>(11)</sup> Consumer Sentinel receives complaints and inquiries about all sorts of transactions, including charitable solicitations. The complaints come into Consumer Sentinel from a variety of sources, including from the FTC's Consumer Response Center ("CRC"), which processes both telephone and mail inquiries and complaints.<sup>(12)</sup> For those consumers who prefer the online environment, an electronic complaint form at [www.ftc.gov](http://www.ftc.gov), available since May 1998, permits consumers to channel information about potential scams directly to the CRC and the fraud database.

Consumer Sentinel also benefits from the contributions of many public and private partners. It receives data from other public and private consumer organizations, including 64 local offices of the Better Business Bureaus across the nation, offices of numerous state Attorney's General, the National Consumers League's National Fraud Information Center, and Project Phonebusters in Canada.

The Commission provides secure access to this data over the Internet, free of charge, to over 300 U.S., Canadian, and Australian law enforcement organizations - including the Department of Justice, U.S. Attorneys' offices, the Federal Bureau of Investigation, the Securities and Exchange Commission, the Secret Service, the U.S. Postal Inspection Service, the Internal Revenue Service, the offices of all 50 state Attorneys General, local sheriffs and prosecutors, the Royal Canadian Mounted Police, and the Australian Competition and Consumer Commission.

Consumer Sentinel first went online in late 1997. Since then, the Commission has upgraded the capacity of the Consumer Sentinel database and enhanced the agency's complaint-handling systems by creating and staffing a new toll-free consumer helpline at 1-877-FTC-HELP, and adding several new functions to Consumer Sentinel. In 2000, Consumer Sentinel received over 100,000 consumer complaints. Currently the database holds over 300,000 consumer complaints.

Significantly, the Consumer Sentinel database is fully searchable. This search feature enables users to search the entire database, using certain key words, to identify specific types of complaints or complaints against specific entities. For example, an investigator can search for the term "disaster" or "September 11th" and cull specific disaster-related complaints. The database also features a specific identification code that enables users to sort complaints specifically involving charitable solicitations.

Since the September 11th events, the Commission has closely and systematically monitored disaster-related and charitable solicitation complaints in the Consumer Sentinel database and followed up on any potential leads. Between September 12, 2001, and October 25, 2001, Consumer Sentinel received 193 disaster-related complaints, 24 percent of which related to charitable solicitations. The vast majority of complaints has been from consumers alerting the Commission to potential scams, not complaining about being defrauded. The Commission has followed up on likely

scams and has worked with agents and investigators from a number of other agencies and organizations, including the Secret Service, FEMA, and the Red Cross, in investigating those cases that look genuinely problematic.(13)

In addition to monitoring Consumer Sentinel for complaints about fraudulent fundraising, the Commission has also monitored the database and actively surfed the Internet for other related consumer frauds. For example, the FTC has seen an increase in the number of entities marketing bioterrorism-related products. These include everything from dietary supplements sold as effective treatments against anthrax or small pox, and home testing kits for anthrax, to gas masks and water filters. The FTC, along with the FDA, EPA, and over thirty states, is making a concerted effort to search the Internet for deceptive claims about these products. Based on the results of this effort, the FTC will take follow-up law enforcement action as appropriate.

## **B. Information Exchanges with Watch-Dog Groups and Other Law Enforcers**

The Commission's efforts to track and analyze consumer complaints through Consumer Sentinel are complemented by a proactive program to uncover fraud and deception by partnering with other law enforcers as well as public- and private-sector charity watch-dog groups. For example, the Commission regularly participates in an e-mail discussion list that has over 100 subscribers from 40 states, consisting of government regulators and law enforcement officials involved in regulating charities and charitable fundraisers. Subscribers exchange daily messages about a variety of topics, including possible scams, registration requirements, and recent legal actions. The Commission also monitors other public Internet sources, including on-line discussions of charity issues.

In addition, since September 11th, the Commission, spearheaded by its Northeast Regional Office, has reached out aggressively to others in the New York-area law enforcement community. Further, as discussed below, the Commission's Northeast Regional Office has launched a full-scale consumer education campaign. Staff in the Northeast Regional Office has communicated regularly with a New York based consumer protection group that provides a venue for exchanging information about possible charity or other disaster-related scams. The ad hoc group also includes the New York City Department of Consumer Affairs, the Attorney General's Office in New York, and the New York State Consumer Protection Board. The Commission has also partnered with the Secret Service, FEMA, and the Red Cross to pursue possible fraudulent fundraisers.

State charity officers are another invaluable source of information. After the September 11th attacks, Commission staff attended the annual Charitable Trusts Solicitations Seminar, sponsored by the National Association of Attorneys General and the National Association of State Charity Officials. The staff met with state officials, representatives of the Internal Revenue Service, charity and foundation officers, fundraising counsel, professional solicitors and private attorneys. Both in closed-door sessions with other law enforcement officers and in open sessions with representatives from the private nonprofit sector, Commission staff participated in informative discussions about possible fraudulent charitable fundraising, as well as recent law enforcement actions.

## **C. Other Investigative Tools**

In addition to Consumer Sentinel and exchanges with other law enforcers and watch dog groups, Commission staff is surveying media reports. The Commission has closely monitored reports about fraudulent solicitation, has followed up on possible scams, and has worked with other law enforcement agencies in investigating those that look genuinely problematic.

The Commission's assortment of investigational tools has enabled it to develop robust experience bringing law enforcement actions against fraudulent fundraisers and other disaster-related scam artists. These law enforcement efforts are discussed below.

## **III. The FTC's Law Enforcement Activities Against Fraudulent For-Profit Telefundors and Other Disaster-Related Scams**

Acting within the parameters of its authority, the Commission has asserted a strong enforcement presence in the fraudulent fundraising arena. In the past decade, the Commission has filed over 25 cases in federal district courts challenging deceptive fundraising practices by for-profit solicitors. Many of these cases involved "badge fraud," where a telemarketer poses as a law enforcement officer or an affiliate and typically claims that he is raising money to support law enforcement efforts in the donor's local area. In fact, the telemarketer is not a law enforcement officer or affiliate, and the money is not used to support local efforts, as promised.

The Commission ultimately obtained injunctions stopping the deceptive fundraising and, in many cases, recovered monetary redress for consumers. The Commission has also obtained injunctions against these for-profit solicitors, which, among other things, have prohibited deceptive fundraising and other remedies.

It is the Commission's experience that meaningful consumer protection also requires coordinated law enforcement with other state and federal agencies. The FTC has organized two "sweeps" of multi-state, multi-agency law enforcement actions targeting fraudulent charitable solicitation. In 1997, the FTC announced Operation False Alarm, which targeted badge-related solicitation fraud. Federal and state officials brought 57 law enforcement or regulatory actions as part of this initiative. In 1998, the Commission announced Operation Missed Giving, which also targeted deceptive fundraising. In that sweep, federal and state officials brought 39 law enforcement and regulatory actions.

In addition, the Commission has experience prosecuting other types of non-charity but nevertheless disaster-related scams. For example, the Commission is contacting marketers of home-testing kits for anthrax and demanding substantiation for their efficacy claims. Drawing on its past experience prosecuting marketers of ineffective at-home test kits for HIV, the Commission is able to identify possible law violators and quickly bring them into compliance with the law.

The Commission intends to remain active in these areas in the future. However, the Commission recognizes that vigilant investigation and law enforcement activities alone cannot wipe out fundraising fraud. As set forth below, meaningful consumer protection also depends on education.

#### **IV. The FTC's Consumer and Business Education Efforts**

The FTC's consumer and business education program communicates anti-fraud and educational messages to reach vast numbers of people in creative and novel ways quickly, simply and at low cost. In the wake of the September 11th terrorists attacks, the FTC has alerted consumers to potential charity frauds. As mentioned earlier, the Commission's Northeast Regional Office has been actively involved in the Commission's outreach to the New York area after September 11th. On September 20th, the Northeast Regional Office held a press conference in New York City with city, state and federal agencies and nonprofit organizations to announce a coalition to protect New York consumers and provide essential information during this time of crisis. The Northeast Region staff distributed a new Consumer Alert, "Helping Victims of the Terrorist Attacks: Your Guide to Giving Wisely," which was posted to the FTC website, [www.consumer.gov](http://www.consumer.gov).

In a little over a month, this single publication has been accessed more than 9,400 times. The Commission also developed a dedicated webpage, where consumers and businesses can obtain more information about donating wisely and filing a complaint, and a banner ad promoting the site.

The FTC also released other consumer and business information related to the attacks. They include:

- "Out of Work? How to Deal with Creditors,"(e-mailed to more than 1,500 daily and weekly newspaper editors).
- "Offers to Treat Biological Threats: What You Need to Know," produced in cooperation with the Centers for Disease Control and Prevention and the Food and Drug Administration. This Alert was e-mailed to consumer and health editors at more than 17,000 radio and TV stations and daily newspapers nationwide.

- "FTC Explains 'Made in USA' Standard To Confirm Consumer Confidence" (more than 3,900 web hits to-date).
- "Selling 'American-Made' Products? What Businesses Need to Know About Making Made in USA Claims" (more than 1,600 web hits to-date).

It is worth noting that while the FTC Headquarters building was without mail service for nine days, the Commission used electronic mail to continue the agency's mission of getting practical, plain language information out to the American public.

FTC staff also has been active in the Washington, D.C. area. At a town hall meeting focusing on the local impact of the September 11th events and the anthrax investigations, the FTC distributed more than 1,000 related consumer publications to District residents. The meeting was hosted by Del. Eleanor Holmes Norton (D-D.C.) at the Washington Convention Center on October 29.

## **V. Conclusion**

Thus far, it appears that consumers have generally shown themselves to be both generous to legitimate charities and aware of the potential for con-artists posing as fundraisers. The press has been warning consumers to be wary of possible scam artists trying to take advantage of consumers' desire to help victims of the attacks. The Commission has found few such schemes. The Commission will continue to monitor developments closely, stands ready to take appropriate law enforcement action, and continues to educate consumers about how to avoid deceptive solicitations and to inform businesses how to comply with the laws.

I would be pleased to answer any questions.

### **Endnotes:**

1. The views expressed in the prepared statement represent the views of the Commission. My oral statement and responses to any questions you may have, however, are my own and do not necessarily reflect the views of the Commission or any individual Commissioner.
2. 15 U.S.C. § 45(a). The Commission also has responsibilities under more than 45 additional statutes, e.g., the Fair Credit Reporting Act, 15 U.S.C. §§ 1681 et seq., which governs the privacy, fairness, and accuracy of certain sensitive consumer information; the Truth in Lending Act, 15 U.S.C. §§ 1601 et seq., which mandates disclosures of credit terms; and the Fair Credit Billing Act, 15 U.S.C. §§ 1666 et seq., which provides for the correction of billing errors on credit accounts. The Commission also enforces over 35 rules governing specific industries and practices, e.g., the Used Car Rule, 16 C.F.R. Part 455, which requires used car dealers to disclose warranty terms via a window sticker; the Franchise Rule, 16 C.F.R. Part 436, which requires the provision of information to prospective franchisees; and the Telemarketing Sales Rule, 16 C.F.R. Part 310, which defines and prohibits deceptive telemarketing practices and other abusive telemarketing practices.
3. These include the authority to file civil actions in federal district court, as well as to bring administrative cease and desist actions, against those who engage in deceptive practices. The FTC Act also enables the Commission to obtain a full range of relief for injured consumers. Typically these civil actions seek preliminary and permanent injunctions to halt the targeted illegal activity, as well as redress for injured consumers.
4. Section 5(a)(2) of the FTC Act states:

The commission is hereby empowered and directed to prevent persons, partnerships, or corporations . . . from using unfair or deceptive acts or practices in or affecting commerce. 15 U.S.C. § 45 (a) (2).

Section 4 defines "Corporation" to include:

any company, trust, so-called Massachusetts trust, or association, incorporated or unincorporated, which is organized to carry on business for its own profit or that of its members . . . .15 U.S.C. § 44.

5. See *Community Blood Bank of Kansas City, Inc. v. FTC*, 405 F.2d 1011 (8th Cir. 1969).
6. *Community Blood Bank*, 405 F.2d at 1019; *Ohio Christian College*, 80 F.T.C. 815 (1972).
7. See *FTC v. Saja*, 1997-2 Trade Cas. (CCH) ¶ 71,952 (D. Ariz. 1997). Cf. *California Dental Ass'n v. FTC*, 526 U.S. 756 (1999).
8. USA PATRIOT Act, Pub. Law No. 107-56, §§ 6102(a)(2), (3)(D), 6106(4), \_\_\_ Stat. \_\_\_ (2001).
9. *Riley v. National Fed'n of the Blind of N. Carolina*, 487 U.S. 781 (1988).
10. *Riley*, 487 U.S. at 800.
11. See [www.consumer.gov/sentinel](http://www.consumer.gov/sentinel).
12. The CRC now receives over 12,000 inquiries and complaints per week. They cover a broad spectrum - everything from complaints about get-rich-quick telemarketing scams and online auction fraud, to questions about consumer rights under various credit statutes and requests for educational materials. Counselors record complaint data, provide information to assist consumers in resolving their complaints, and answer their inquiries.
13. The number of complaints the Commission has received is lower than might be expected. This might be in part due to the fact that victims of fraudulent solicitations often do not know that they have been scammed and therefore do not file complaints. It might also be in part due to the Direct Marketing Association's request that its members that engage in charitable fundraising, and that solicit people and businesses with whom they do not have a previously existing customer relationship, cease outbound telemarketing fundraising through the end of September. The announcement about this directive can be found at: <http://www.the-dma.org/cgi/dispanouncements?article=115>.