

# CA Issues Cease-and-Desist Orders to Out-of-State Charities

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On March 12, 2018, Javier Becerra, the Attorney General of California, announced cease-and-desist actions against four charities from other states that had fraudulently – according to the government – solicited funds from California residents.

The jurisdiction of this state's top law-enforcement officer extends not only to California charities but also to 501(c)(3)s *anywhere in the nation* who ask for contributions from Californians. There are registration and reporting requirements for these charities; an organization that fails to abide by these laws and rules or engages in false and misleading fundraising campaigns is subject to sanctions including cease-and-desist orders, injunctions, and significant penalties. (This type of extended jurisdiction is not unique to California, but is typical of the reach of attorneys general nationwide.)

The four cases are similar – though, otherwise, apparently unrelated, in that they involve a consistent fact pattern: Each is part of a chain of distribution of soon-to-be-expired pharmaceutical drugs, donated by the drugmakers, to the developing world. The gist of the AG's claims is that they (1) used an accounting ploy that is, itself, wrongful because it's misleading; and (2) touted these inflated figures to support fundraising appeals in California for additional (and, in at least one case, nonexistent) projects.

Under California law, any charity soliciting funds in the state must follow Generally Accepted Accounting Principles (GAAP). Under those rules, for gifts-in-kind (GIK), charities may claim only "fair market value" which – for GIKs – is defined as the "price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date." In each of these cases, the organizations used the FMV of the medications in the U.S. market

instead of the much lower prices for these drugs in the developing world.

### *Three Active Cease-and-Desist Orders*

Three of the four cases are active: There are April 11, 2018, deadlines either to appeal or to comply with the cease-and-desist order, have their charitable registrations revoked, and face fines over \$1.65 million. “Collectively, the three organizations reported revenues of almost \$2 billion, much of it in the form of noncash contributions – that is, the pharmaceutical drugs.

The active cases are:

- Food For the Poor (FFTP) (Coconut Creek, FL)
- MAP International (Brunswick, GA)
- Catholic Medical Mission Board (CMMB) (New York, NY)

The cease-and-desist orders are available on the Attorney General's “Charities” [homepage](#).

The AG may assess a penalty of up to \$1,000 for each act. He issued a total penalty of \$1.088 million to Food For the Poor, \$409,575 to CMMB, and \$158,725 to MAP International. Payment is due within 30 days of the March 12 filing unless the written appeal is timely filed.

Catholic Medical Mission Board plans to appeal and a spokesman asserts its “compliance with all laws; “(w)e’ve been following industry practice.” He describes this case as a “difference of opinion in how they value pharmaceuticals.” The executive director of Food For The Poor said: “We believe we have done nothing wrong and we are actively working to resolve the Attorney General’s concerns.”

### *Fourth Charity Agrees to Stipulated Judgment*

The fourth case is different. Just a day after the formal announcement of a cease-and-desist order, the National Cancer Coalition (NCC), a Delaware corporation, signed a Stipulated Judgment, which was approved by a Los Angeles judge, and agreed to dissolve. In that agreement, substantial fines were waived due to the apparent insolvency of the group and its leadership – subject to confirmation of this lack of ability to pay.

As usual, there is a link to the full Complaint filed by the California AG on that agency’s website. It’s a good read, in large part because it’s written in a refreshing plain-English style and includes a “Summary of the Case” – commonly seen in legal briefs, but not in charging complaints. The first two paragraphs of that summary showcase this laudable style.

“This case involves the false public reporting of donations of pharmaceuticals and the resulting large-scale deception of unsuspecting donors. Potential donors view costs spent on a charity’s programs, i.e., “program expenses” in furtherance of its mission, favorably, and those spent on fundraising and administration (“overhead”) unfavorably. As a result, charities try to keep their publicly reported program expenses high and their fundraising and administrative expenses low.”

“Over the past several years, media sources have reported that some charities report exceedingly high, unsubstantiated valuations for pharmaceutical donations in their public financial reporting in order to attract donors and get favorable ratings from charity rating organizations. These charities

report inflated values as revenue and program expense to make them appear larger and more efficient than they really are, and/or to hide high fundraising and administrative costs from potential donors. Charities accomplish this, in part, by using United States market prices to value pharmaceuticals intended for distribution outside the United States, even if the pharmaceutical company donors prohibit distribution and use in the United States. These same pharmaceuticals are shipped to developing countries where their applicable fair market values are a small fraction of the values in the high-priced United States markets.”

There you have it. Anyone wanting to get “into the weeds” of AG Becerra’s thoughts on these accounting practices can read the rest of the Complaint, but – for the rest of us – that opening gives us a fairly good idea of what this case is all about.

### *Expert Commentary*

According to Professor Brian Mittendorf of Ohio State University, an expert on nonprofit accounting: “It’s not across the board but lots of organizations are aggressive in how they report accounting numbers and how they convey those externally.” He says he “hasn’t yet seen state regulators aggressively clamp down when charities push those boundaries,” adding that “GIK [gifts in kind] is ‘definitively a grey area’ and organizations have pushed what’s acceptable and for the most part haven’t been challenged.” Mittendorf adds: “Certainly it’s more than these three organizations.”

Bob Mims, a nonprofit consultant and former chairman of the not-for-profit advisory committee of the Financial Accounting Standards Board (FASB), explains that “(t)he AG’s office appears to be taking a black-and-white view specific to pharmaceutical donations on GAAP,” adding that he’s not sure he’d agree “as valuations are subject to interpretation.”

### *Conclusion*

“Let this serve as a stern warning.” said Attorney General Becerra in announcing the current enforcement actions, that “charities that intentionally mislead the public at the expense of others will be held accountable.” His office is taking on not only charities in the State of California but also organizations from around the nation that are soliciting California residents for donations in improper and misleading ways.

— Linda J. Rosenthal, J.D., FPLG Information & Research Director