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Ponzi schemes threaten charities with more than lost investments

Tom Gallagher | Jun. 30, 2009 NCR Today

This is an important article for any charity [1], large or small, Catholic or not. Here is an excerpt:

> "With last year's collapse of perhaps the largest Ponzi scheme in history, Bernard Madoff's, many people, including charities, became aware that trustees or receivers of failed companies can bring lawsuits to "claw back" distributions of fictitious profits to help offset losses by other investors.
>
> For this reason, some courts have considered whether there should be a defense available to nonprofits that have acted in good faith. But they have uniformly rejected such a defense, finding no basis in the law to support it. As Judge Richard Posner of the U.S. Court of Appeals for the Seventh Circuit explained, charities must return donations because the law "makes no distinction among different kinds of recipient of fraudulent conveyances. Every kind is potentially liable."
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> With courts unwilling to interpret the law as affording some defense for charities, there have been efforts to persuade legislators to amend existing laws to provide such a defense. But little has come of these efforts.
>
> In the Religious Liberty and Charitable Donations Act passed in 1998, Congress amended the definition of fraudulent transfer in the U.S. Bankruptcy Code to provide protection to charitable contributions made by people who later go bankrupt. But the reach of that provision is quite limited: it does not apply where the donor is engaged in a fraud.
>
> Moreover, many clawback cases are brought not under the federal bankruptcy law's fraudulent transfer provision, but under state laws, and state legislatures have not taken any action to protect nonprofits."

My 2 cents: Charities need to first manage risk, then manage donations. Managing risk first requires a charity to ask the question: "Do we know the donor?" If yes, then acceptance of the gift makes sense. Otherwise, there's the embarrassment of taking a donor's name off of a building or worse, explaining to a board of directors and a charity's constituency why you're giving the donation back. Of course, even with appropriate due diligence, complications can arise. The important thing is to exercise as much prudence on the front-end of a major gift.

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Links:
[1] http://www.huffingtonpost.com/david-donell/charities-face-greater-th_b_223088.html