

to back up his story of the truth of which I was convinced, that he had destroyed all such evidence. I do not criticize him for withholding the information from me, considering the circumstances under which he lived then. But when Mr. Kohlberg informed me of his interview with Mr. Dulles about the Hiss appointment to the Carnegie Endowment post, I told him that there was no material evidence to support the Chambers charges, and that it would all come down to one man's word against another's, that of Mr. Chambers against Mr. Hiss.

3. My alleged description of Mr. Chambers "in unflattering terms" related only to his unprepossessing physical appearance. I said, if memory serves me right, that an admitted ex-Communist and ex-Soviet agent would not make as good an impression as the debonair Mr. Hiss who then enjoyed the confidence of many ranking State Department officials.

ISAAC DON LEVINE.

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DIGEST OF STATE REGULATIONS

(The following is a digest of a manuscript written by Eleanor K. Taylor, associate professor in the School of Social Work, State University of Iowa. Miss Taylor began preparation of this material as a doctoral dissertation. In the course of the research the manuscript came to the attention of the Russell Sage Foundation. The foundation employed Miss Taylor to revise her study into one primarily designed to serve the interests and needs of Government officials, foundation officers and trustees, lawyers, and legislators interested in discovering the present facts as to the accountability of foundations and charitable trusts and working out a better future solution. For special assistance on legal aspects of this study the foundation retained Ray Garrett, chairman of the committee on corporate laws of the American Bar Association.)

REGULATION OF CHARITABLE CORPORATIONS

While the trust is created by will or trust instrument, the incorporated foundation is created by legislative grant in the form of a corporate charter. Charters may be granted by special acts of the legislature or by administrative officials under the provisions of general corporation statutes.

American philanthropy has characteristically taken the form of endowments held by corporate directors granted power through a charter. The statutes governing the issuance of a charter vary from jurisdiction to jurisdiction. The person usually responsible for issuing a charter is the secretary of state. Sometimes the application is little more than the filing of appropriate papers with this official. Sometimes provision is made for a public notice, such as the appearance of the name of the organization and its incorporators in some official list, the lapse of a stipulated number of days before the application may be approved, or other routine measures. Sometimes officials other than the one responsible for issuing the charter are supposed to carry on an investigation of the proposed organization to assure that its purposes are those purported in the application and that the individuals seeking the incorporation are responsible persons.

CHARTER ISSUANCE IN NEW YORK AND PENNSYLVANIA

The New York and Pennsylvania legislation are somewhat different. In New York the secretary of state is the official responsible for issuing the charter. However, a justice of the supreme court must approve the application prior to the issuance of a charter. This provision would appear to be a kind of licensing. Yet a search of citation sources indicates that charters are rarely contested. Only two of the six charters recently withheld were incorporated foundations. The others were those of associations claiming to be social or recreational groups having benevolent purposes. In three instances, however, suspicions aroused because of the name of the proposed organization seemed to have caused a review of the circumstances.

Pennsylvania has somewhat comparable provisions for investigation of the proposed organization prior to the granting of a charter. These are, however,

permissive and investigating is not intended in all cases as is the presumption of the New York statute. Inasmuch as Pennsylvania is one of the few States which publishes county and district reports, the limited number of hearings recorded is evidence of the infrequency of such actions.

Some of the Pennsylvania charter hearings exemplify the problems of attempting to judge in advance the nature of activities which may be carried on as a result of the grants of corporate power, particularly in the case of foundations which themselves only furnish the funds for other organizations.

It would be difficult to draw conclusions as to whether this intended safeguard in the chartering process operates as an additional check in the issuance of a charter. Investigation usually pivots about the motives and character of the incorporators. Some of the recent decisions suggest that suspicion of tax evasion led to careful review of the circumstances.

In view of the circumstances under which these Pennsylvania decisions were reached, it is apparent that the kind of routine chartering followed in most other States is hardly likely to bring to light the basic facts which should be known before a charter is granted. Nor does the chartering process provide protection beyond the initial step in the establishing of an organization.

REPORTING EXACTIONS

Almost every not-for-profit corporation law has some reporting exactions. Those found in sections 98 and 99 of the Illinois law are unusually stringent in granting interrogatory powers. Reporting failure is thus classified as a matter as serious as having obtained a franchise by fraud or abuse of corporate powers.

In California the attorney general is charged with special inspection duties with regard to charitable foundations and corporations so as to give additional force to the existing reporting machinery, but this more exacting statute is unenforceable without administrative provisions. Here also, interrogatory powers do not add materially to the effectiveness of reporting measures. The same problem exists with regard to reporting as in relation to chartering. The laxness of reporting measures raises question as to whether the actual writing into the statutes of specific prohibitions can be counted upon to deter wrongful acts. For example, the Illinois act prohibits the corporation from issuing shares or from distributing dividends or any part of the income to members, directors, or officers (excepting reasonable compensation for services and distributions upon liquidation). The act further prohibits the making of loans to officers and directors. These are important statutory safeguards and would certainly make more difficult deliberate misappropriations of funds or use as risk capital, such as the pyramiding pointed up in the Rhode Island investigation into the regulation of charitable trusts conducted by a special committee in 1950. However, the penalty provided is that directors who assent to the making of such loans shall be jointly and severally liable until its repayment. This statute certainly is a corrective to the vague permissiveness of many other nonprofit corporation laws. Indeed, the new Internal Revenue Code relies on such legislation as a basis for tax exemption. Yet knowledge of the details of the activities of these organizations is dependent upon the regularity and completeness of reporting.

DISSOLUTION OF CHARITABLE CORPORATIONS

Charitable corporations live and die almost anonymously. Certainly the statutes which provide some ritual observance of the events of corporate life fail to assure that the facts of their continuing existence are known. New York recently passed legislation requiring all corporations organized prior to January 1, 1948, to file a certificate of existence by June 15, 1952. Corporations failing to file by the stipulated date would then be dissolved through proclamation by the secretary of state. This action suggests the difficulties of carrying out the existing provisions for dissolution.

The present law provides that any membership corporation may be dissolved by filing in the office of the secretary of state a certificate of dissolution signed and acknowledged by all of the voting members, together with an affidavit of certain officers of the corporation and the approval of a Justice of the Supreme Court, and, where appropriate, the approval of the welfare agency whose approval of its creation would be required by the law.

SUPERVISION BY COURT LIMITED

Some of the States under consideration provide for court supervision of dissolution proceedings. In Illinois, for example, involuntary dissolution requires

a decree of court. The court is given authority to liquidate the assets and affairs of corporations in actions brought by members, directors, or creditors under certain conditions, or by the corporations themselves or in dissolution proceedings instituted by the attorney general; and in every such case the court may dissolve the corporation by decree.

In South Carolina a corporation may voluntarily dissolve upon a vote of two-thirds of its members and the filing of an appropriate certificate with the secretary of state. In Wisconsin voluntary dissolution requires the affirmative vote of a two-thirds of the voting stock in stock corporations or a majority of the members in other corporations, followed by the filing of a certificate with the secretary of state. In Pennsylvania voluntary dissolution requires a decree of the court of common pleas upon application by the corporation authorized by the requisite vote of the members, notice and hearing.

New Hampshire has a more stringent requirement consistent with the existence in that State of a registry of charitable trusts. Corporations wishing to dissolve must petition the superior court. The resulting record is filed with the secretary of state and open to the public.

The provisions governing corporate dissolution have varying degrees of effectiveness in the different States. However, they all depend on adequate administrative arrangements, for the most part lacking.

SUPERVISORY USE OF STATE BOARDS OF WELFARE

Charter issuance sometimes has the additional safeguard of coming under the authority of a State board charged with certain welfare functions. The Massachusetts and South Carolina statutes both require that the board investigate all applications and make recommendations to the secretary of state. The New York membership corporation law divides responsibility for approval of proposed charters among a number of State boards in accordance with their supervisory tasks relative to certain groups.

The State board of welfare is, however, the typical agency looked to for investigation and the full force of any not-for-profit corporation law must be evaluated in conjunction with the welfare law of a given jurisdiction. The Illinois law is illustrative, for the general not-for-profit corporation does not itself call for investigation. But the welfare law specifies in chapter 23, section 208, that any proposed corporation which includes in its charter purposes the care of children must have its charter approved by the department of public welfare before it is filed with the secretary of state. However, the welfare law makes plain both the delegation of the investigative function and the extent of the powers accorded to the department.

CONCLUSIONS

Analysis of the regulatory machinery applicable to charitable trusts made it plain that the protection of equity over trusts is more potential than real. Not only is equity machinery inadequate to supply basic information as to the existence of a trust, but in those instances in which the trust is known the peculiarities of the trust instrument with its emphasis upon trustee accountability to the donor means that it is possible for the trustee to be relieved of reporting responsibility. On the other hand, where the trustee is expected to make reports to the court the administrative and clerical staff necessary to this service are often not available. Furthermore, routine accounting might still fail to bring to light the need for redirection of the trust to other uses.

Similar enforcement difficulties have been pointed out with regard to the transfer of private wealth to public purposes through the medium of the charitable corporation. Chartering is routine and casual, and even in requirements such as those in New York for certification by a justice or provision in Pennsylvania for hearing by masters in chancery there is evidence that these are not the most effective safeguards for continuing supervision. Existing reporting measures are as ineffectual in the case of charitable corporations as they are in the instance of the trust.

The actual extent to which charitable trusts and foundations are abusing their privileges is still an open question. The important fact is that the prevailing statutes do not prevent abuse.

AMERICAN REGULATORY PROPOSALS

Since the hearings of the Commission on Industrial Relations in 1915 a number of investigative groups have grappled with the problem of charitable regulation.

Groups have argued before a subcommittee of the Senate investigating the Textron trusts and the Rhode Island committee that the multiplying of vast charitable endowments constituted a social danger. They urged the establishment of a special supervisory board and legislation which would limit the life of foundations to 25 years, restrict their investments, and force annual distribution of most of their income. Other witnesses have advocated strengthening the existing State regulation through implementing court and legislative machinery.

RECOMMENDATIONS OF THE INDUSTRIAL COMMISSION

The recommendations of the Industrial Commission are still important today because the general problems of economic control were first defined in these hearings and some of the measures advocated by the Commission have been repeated recently. Though the Commission divided, members were united in the view that Government should have a supervisory role over private endowments. The ultimate objective was the socialization of philanthropy. Minority members were more outspoken on this point than the majority. Their advocacy of a graduated inheritance tax was to bring about forced displacement and a gradual expansion of the public-welfare program. Majority members urged the expansion of governmental activities along lines similar to those of the private foundations. Stepped-up Federal appropriations for education and the social services would counteract the influence of the private endowments by competition. The Commission did not deny the value of philanthropy. Minority members acknowledged that services now carried by Government were developed first through private initiative. However, this historical fact was used as argument that the State could provide better and more universal charity. The majority recommended a Federal statute governing the chartering of all incorporated nonprofit organizations empowered to perform more than a single function and holding funds in excess of a million. Stipulations for such Federal charter were sixfold: (1) A limitation on the total funds to be held by the proposed organization, (2) specification of the powers and functions which were to be undertaken with provision for penalties if the corporation exceeded them, (3) prohibitions against accumulation of unexpended income and against the expenditure in any one year of more than 10 percent of the principal, (4) accounting of both investment and expenditure, (5) publicizing through open reports to a Government official, (6) banning of any alteration of charter purpose unless empowered by Congress at the end of a 6-months' waiting period.

THE RHODE ISLAND REPORT

The Rhode Island investigation came after a period of unprecedented foundation growth. The rise of a powerful labor movement refuted the prophecy that the foundation could be a strategic weapon in industrial warfare and foundations had become increasingly evaluated in terms of their programs and disassociated from judgments about their donors. Only with the sudden emergence of a new type of foundation was suspicion redirected to private philanthropy. The multiplication of small trusts, the increase of "family foundations," the use of lease-back arrangements raised question as to the legitimacy of many charitable organizations with no social-welfare program.

EMPHASIS ON PROTECTING LEGITIMATE FOUNDATIONS

Like the earlier commission, the Rhode Island committee directed its attention to the possible abuses of charitable foundations, but unlike the congressional commission the State investigation was concerned with protecting the legitimate foundation. The emphasis was upon providing adequate supervision to assure that funds set aside for charitable beneficiaries realized their purpose.

The explorations of the group involved them in consideration of the statutes governing labor relations, business tax laws, the organization of the attorney general's office, the powers of the secretary of state, the regulations of insurance companies, and a multitude of other questions. However, the committee brought the essential problem into sharp focus: the inadequacy of prevailing statutory machinery to provide for the simplest duties of supervision.

PROBLEM OF SPORADIC SUPERVISION

Admitting that the duty of the attorney general as a supervisory officer was unquestioned, the committee agreed that supervision was sporadic at best, and concluded that any accounting by trustees was a matter of "private discretion

rather than public obligation." They unanimously advocated a trust registry in the office of the attorney general.

The Rhode Island statute followed rather closely the committee recommendations. In this regard its omissions are as significant as its inclusions. The committee heard witnesses who advocated the establishment of a separate administrative board, some who urged that legislation require distribution of no less than 85 percent of annual income, and others who proposed limiting the life of charitable trusts to 25 years or restricting their size. There were also reformers who saw the solution of charitable supervision as primarily a problem in corporate regulation and advocated chartering controls.

IDEA OF SEPARATE BOARD REJECTED

The committee chose to meet the problem in terms of extending the already existing machinery. In so doing they both followed and deviated from the British pattern. They recognized the need for additional administrative powers and the staff to carry them out. However, they rejected the idea of a separate board and made the registry the function of the attorney general.

In regarding a trust registry supervised by the attorney general as the most practical solution to the problem of public accountability, the Rhode Island committee also focused on continuity in supervision as the essential issue. The possible use of the office of secretary of state, particularly as a basis for regulating corporate trusts, was disregarded. Chartering controls were thus considered secondary to the kind of regulation based on detailed knowledge of the activities of an organization.

The recommendations of the Rhode Island group, in following so closely the pattern of trust regulation in New Hampshire, commits a second State to a new supervisory pattern.

THE ENGLISH CHARITABLE TRUSTS ACTS

In England a special board is responsible for regulating charitable endowments. Trust abuses had been the subject of legislative reform from Tudor times, and the Elizabethan statute was the direct outgrowth of legislative concern with the problem of charitable supervision. The present legislation climaxed the investigations of the Brougham Commission. This inquiry continued for 19 years and its final report filled 37 volumes. The commission recommended two remedies: An accounting which would insure safe custody of funds, and modification of court machinery so that trust administration would be less involved and costly, particularly when it was necessary to redirect a charity to a new purpose.

POWERS OF THE COMMISSIONERS

The Charitable Trusts Act, finally passed August 20, 1853, was a compromise bill, but it did sanction the setting up of a separate administrative group for the supervision of charities. The Board of Charity Commissioners had power to exact accounts, including access to records, the right to demand written replies, and question trustees under oath. These reporting measures provided the basis for a national registry of trusts. The chief limitation was that the large ecclesiastical and educational charities, and all charities wholly or partially maintained by voluntary subscriptions, were exempted.

The commissioners were also given semijudicial powers. Their administrative hearings could be substituted for the more involved legal process of bringing "an information" and through the authorization to make "schemes" for the reorganization of a charity they could exercise a type of *cy pres* power. However, these powers were limited, because the commissioners could not make schemes for the reorganization of any charity having an annual income in excess of £50 except upon application of the majority of the trustees. Such schemes also had to be approved by Parliament.

DIFFICULTIES OF ENFORCEMENT

Soon after the passage of the legislation, critics began to attack the legislation and select committee hearings were held in 1881, 1884, and 1894. The commissioner's annual reports also point up administrative difficulties. Recent reports of the commissioners echo complaints made in 1883 and 1893, when the chief commissioner told investigative groups that the board had some check-back on charities created by will through duplicate returns from the inland revenue office, but that there was no basis for identifying endowments created by deed except

through the filing of reports by trustees or some accident bringing a charity to the attention of the board. The 1951 report admits that reports coming in represent only a small proportion of those expected.

CURRENT REVIEW IN ENGLAND

In 1950 a select committee headed by Lord Nathan began reviewing the question of trust supervision. Their report has not yet been made public; but preliminary discussion indicates that the Charitable Trusts Act have not succeeded in solving the very problem it was designed to meet, for this group is especially concerned with the continuing problem of obsolescent charities.

On the positive side the act has tended to minimize litigation. Statistics show an increase in the number of schemes and a decrease in the number of disputed cases carried to courts; but it would appear that the inherent weaknesses in the original act have never been overcome.

POSSIBLE STATUTORY MODIFICATION IN UNITED STATES

In considering modification of existing statutes, two possibilities exist—further extension on a national level or modification of regulatory machinery on the State level. Extension on the national level would necessitate the creation of a board having many of the powers now exercised through the various State attorneys general. The creation of a group comparable to the British Board of Charity Commissioners would be a fantastic break with American tradition. Resulting administrative problems might well cancel out the presumed gains of national uniformity. Supervision of charities has been defined as a State responsibility. Administrative adjustments accordingly must be on the State level.

A TRUST REGISTRY

A statute setting up a registry would effect such a purpose. Registration should be required of all charitable endowments whether set aside by the donor during his lifetime or provided for by will. Some modification could be allowed in the case of gifts dependent upon future contingencies; but these would be registered at the time of vesting. The registry should extend to every type of charitable bequest whether made in the form of a trust, a quasi trust, or a gift outright to a charitable corporation set up to hold funds or endowments for charitable purposes. Only gifts made to charitable corporations or associations actually operating as functional social agencies would be exempt from enrollment.

The creation of such a registry would effect two remedies: (1) The *inter vivos* trust by which charitable gifts may be made without official knowledge would cease to be a private affair; (2) the quasi trusts or charitable corporations would be winnowed out from the amorphous group of benevolent associations and recreational and social organizations with which they are now classified only because they share a declared nonpecuniary purpose. The registry thus would identify those philanthropic endowments which have special fiduciary responsibilities and bring them together in one file.

NEED FOR CONTINUING SUPERVISION

The logical place for this registry would seem to be the office of the attorney general. It is this official who is charged with trust enforcement and the setting up of a file in his office would bring together information now scattered between the courts and the office of the official responsible for charter issuance. The registry must, of course, call for annual reporting. Initial registry is only the first step in identifying the funds over which continuous supervision is necessary.

The statute setting up the registry should be a broad enabling act insuring powers sufficient to effect its purpose. It should make explicit the authority of the attorney general over charitable trusts and foundations, including powers to audit accounts, interrogatory powers to question trustees. *Cy pres* should be specified with regard to both trusts and philanthropic corporations. A statute comparable to those of Illinois and Michigan covering the use of *cy pres* in the process of corporate dissolution might be necessary in some jurisdictions. Only by such statutory definition could the attorney general function to prevent misapplication of funds and nonapplication due to outmoded purposes.

ENFORCEMENT MACHINERY

Enforcement should be assured by providing adequate penalties. Failure to report for a 2-year period should be classed as an abuse of trust, and, in the instance of the charitable corporation, subject the organization to involuntary dissolution.

Care must be taken to provide the necessary administrative machinery for carrying out the tasks incidental to a registry. Adequate funds must be allocated for the attorney general to have sufficient clerical and accounting staff to audit accounts and conduct necessary investigations. The New Hampshire experiment has indicated that registry costs are higher during the first year of operation but may diminish thereafter.

The statutory modification which has been suggested does not, of course, solve all the problems of accountability. It does, however, solve the basic problem. It would assure that endowments are identified, that funds held for charitable purposes are safeguarded in the process of investment and disbursement. By focusing on the fund granting character of charitable trusts and foundations and providing appropriate registry and accounting methods, the legislative changes recommended do much to overcome the divorce between the initial step in giving from the final transfer of private wealth to public uses.

FREEDOM AND REGULATION

Furthermore, the proposed statute is limited in two ways: (1) It does not attempt to cover type of abuse such as tax avoidance, which though implying statutory change are special problems calling for other legislation; (2) it does not attempt to solve problems of accountability outside the legislative field. It is important in this regard to acknowledge that the crux of the problem is beyond the power of legislation to correct. As has been pointed out in the previous discussion, the American foundation has because of its flexibility freed the donor from narrow adherence to purely charitable objectives and opened the way for an ameliorative and preventive approach to social problems. Had the fears of early opponents, voiced at the time that the Rockefeller and Carnegie Foundations were under attack, been heeded, much that has been constructive in foundation giving would have been impossible. Hurried legislation enactment to cope with the presumed abuses of charitable foundations today might be just as disastrous.

To point out that the more subtle aspects of accountability elude legislation is not to ignore them; it is rather to emphasize the burden which foundations themselves carry for trusteeship. The foundation has enjoyed a freedom which has enabled it to be a flexible instrument for an imaginative and resourceful philanthropy. This freedom is fraught, however, with the dangers of a narrow individualism. Charitable trusts and foundations share the responsibility of all philanthropy for social gifts. Full accounting of their activities is a necessary earnest of the stewardship they have assumed for wise giving.

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