

A Tax Benefit for Big Donors Often Bypasses Idea of Charity

By Stephanie Strom, The New York Times
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George B. Kaiser, a publicity-shy oilman who built a fortune estimated at \$4 billion by snapping up busted petroleum businesses in Oklahoma, set aside roughly \$1 billion for charitable endeavors from 2000 to the end of last year.

In exchange, he can now deflect taxes on much of his own income over the next several years.

But it turns out that only \$3.4 million of the money he set aside has gone to charities. The rest is sitting in an obscure philanthropic entity called a supporting organization, so named because it is created to support a specific charity or charities.

Supporting organizations are attractive to donors because they offer the generous tax benefits associated with donating directly to charities and operate much like private foundations, but without a foundation's more onerous requirements.

Donors get those perks because they agree to relinquish control over the money. But since they appoint the organization's board, they can retain a great deal of influence over it.

Regulators and lawmakers suspect that many wealthy people have used these organizations more for tax planning than for any charitable aim and are pushing for tighter rules as part of a broader crackdown on charitable tax exemptions.

"I'm deeply disturbed that with a good number of supporting organizations, people are taking multimillion-dollar tax deductions for what they claim are contributions to charity, yet too often the result is a thimbleful of benefit to charity," said Senator Charles E. Grassley, the Iowa Republican who is chairman of the Senate Finance Committee.

The committee is examining several supporting organizations, including Mr. Kaiser's. An assistant to Mr. Kaiser referred calls about his supporting organization to Frederic Dorwart, his lawyer and a trustee of the organization. Mr. Dorwart said the organization had not been contacted by regulators and was operating within the law.

Regulators are going after some supporting organizations and donors that they say have violated even the current lax rules.

The Internal Revenue Service has revoked the tax exemption of one supporting organization, which is challenging the decision, and has brought two cases against people who claimed deductions for their gifts to such organizations. It is considering penalties on 15 promoters of these vehicles, examining three cases for possible criminal investigation, and is auditing about 100 supporting organizations and donors.

"We are treating it very seriously because we've seen so many abuses," said Mark W. Everson, commissioner of the I.R.S.

Among the concerns Mr. Everson has cited are donations to supporting organizations of assets held in offshore tax havens that find their way back into donors' pockets, and the challenge of determining whether the values donors are placing on unconventional gifts for tax purposes are valid.

The philanthropists behind supporting organizations and their legal advisers say that their actions are legal, a point that critics acknowledge.

"It is legal, but it shouldn't be," said Jeff Krehely, deputy director of the National Committee for Responsive Philanthropy, a nonprofit research group. "You're supposed to get the tax breaks because you're providing some public benefits."

Supporting organizations have swelled to 34,000 from 24,000 in 1995. In 2001, the 400 largest controlled \$76.7 billion in assets, according to the National Center for Charitable Statistics at the Urban Institute, a research group.

The center found that one-quarter of those 400 organizations made no grants at all in 2001, and an additional 22 percent spent less than 3 percent of their assets on charity. Foundations, by contrast, are required to pay out, on average, 5 percent of assets a year; supporting organizations have no such requirement.

Carl C. Icahn, the billionaire investor, has a supporting organization with \$118 million in assets; it has spent \$2.9 million since its creation in 1997 to underwrite a scholarship program at a private school and, more recently, the development of charter schools. It would have been required to pay out almost twice that much in a single year as a private foundation.

Mr. Icahn, meanwhile, was able to claim a tax deduction of \$115 million. That is the value he placed on the shares of a privately held company, American Railcar Industries, that he donated to the supporting organization.

The supporting organization has little cash at its disposal. Because Mr. Icahn owns the rest of American Railcar, there is no public market for the stock, which produces no income. The supporting organization has few other assets and cannot readily sell the shares unless Mr. Icahn wants to buy them.

Mr. Icahn could not donate American Railcar shares to his foundations without incurring taxes and penalties because foundations are prohibited from holding stakes in businesses that, combined with the holdings of their donors, donors' families and some others, exceed 20 percent.

Supporting organizations have no such limits. But in return for that freedom, the organization is supposed to be outside Mr. Icahn's control. He says his supporting organization is independent. The seven members of the board are Mr. Icahn, his wife, his uncle and four others who lead

nonprofit organizations that receive money from Mr. Icahn.

Mr. Icahn said that he had expected the value of the American Railcar shares to increase over time and that he now planned to sell them to a third party or buy them back himself.

"It was not the intent not to give the money out," Mr. Icahn said. "We'd like to do more and are working on giving out another \$10 million for four more charter schools."

Mr. Kaiser, known around Tulsa for driving used cars and living in a modest house, has protected his wealth by being savvy about taxes - when he pays them at all. During a stretch of the late 1980's and early 1990's, he paid just \$2,688 in federal income taxes, claiming negative income in six out of seven years.

When the I.R.S. sought \$49 million in back taxes and penalties, he fought and wound up paying only \$11,000 more.

In the same period, he assembled a fortune by snapping up failed petroleum businesses in Oklahoma and one of their biggest lenders, the Bank of Oklahoma. He then used those businesses' operating losses and a keen understanding of tax law to keep virtually all the profits.

His tight-fisted approach to taxes did not extend to charity. For years, the Betty and George Kaiser Foundation, a private foundation established by Mr. Kaiser and his late wife, made the required payout to dozens of charities, including the Tulsa Area United Way and Harvard University, his alma mater.

In 1999, he created a supporting organization and stopped giving to the foundation. Shuttling his money to the supporting organization gave him a bigger tax break and reduced the amount of excise taxes the foundation would have had to pay on the additional investment income.

His foundation continued to make its required payout, mostly by making grants to his supporting organization, a practice known among tax experts as "round-tripping."

In 2003, 95 percent of his foundation's donations went to the supporting organization. Of the \$16.6 million that the Betty and George Kaiser Foundation gave away that year, charities received \$915,000, down from \$2.8 million in the year the supporting organization was formed.

The supporting organization, which had about \$1 billion in assets at the end of last year, now dwarfs the foundation. Were it a foundation, nonprofit accounting experts and officials from other foundations estimated, it would have had to pay out \$20 million to \$35 million more than the \$3.4 million it had given away by the end of last year.

Mr. Dorwart said Mr. Kaiser had big plans for his organization, noting that it had committed an additional \$28 million to various community programs, though the money had not yet been disbursed. "Just the fact that money gets given out doesn't mean that's the wise or prudent thing to do," Mr. Dorwart said.

Mr. Kaiser has promised the bulk of his fortune to charity, Mr. Dorwart said; his primary objectives are to help pay for a safety net for the needy in northeast Oklahoma, a beautification program for Tulsa and an early education program for disadvantaged children.

Mr. Kaiser set up his supporting organization to benefit the Tulsa Community Foundation, which he helped found the same year and which has received \$876,000 in grants from the organization. When asked why the Betty and George Kaiser Foundation could not make grants directly to the Tulsa foundation, Mr. Dorwart said Mr. Kaiser wanted to encourage others to create supporting organizations for the Tulsa community.

"There's also the value of creating the community foundation and an organization to support it," Mr. Dorwart said, "which I would see as an offset to whether a lot of money gets handed out."

By law, the Tulsa foundation controls Mr. Kaiser's supporting organization, which is supposed to be independent of him and his family.

Some experts, though, questioned that independence. Two of the supporting organization's trustees, Mr. Dorwart and Phil Frohlich, sit on the board of the Tulsa foundation, and the third, Phil Lakin, is its executive director. Mr. Dorwart is Mr. Kaiser's longtime legal adviser, and Mr. Kaiser is the chairman of the Tulsa foundation's board, which is populated by many of his friends and business associates.

"There is arguably a semblance of control by the supported organization, but in fact, it's not operationally independent of the donor," said William Josephson, a former assistant attorney general in New York in charge of charities.

Mr. Dorwart said he was confident of his own independence. "If you knew me, you'd understand why I say that," he said. "And to suggest that Mr. Kaiser controls the board of the Tulsa Community Foundation is kind of wide of the mark."