



July 23, 2007

Michael R. Phillips  
Deputy Inspector General for Audit  
Department of the Treasury  
Washington, D.C. 20220

Dear Mr. Phillips,

I am writing on behalf of the Treasury Guidelines Working Group of Charitable Sector Organizations and Advisors (the "Working Group"). The Working Group is a group broadly representative of U.S. charitable organizations that was originally convened to consider and comment on the "U.S. Department of the Treasury Anti-Terrorist Financing Guidelines: Voluntary Best Practices for U.S.-Based Charities" (the "Guidelines").

We, like you, remain steadfast in our opposition to the use of charitable vehicles for the support of terrorist activities at any time in any place. Our work is geared towards supporting appropriate safeguards against any use of the charitable sector for this purpose, while also seeking to assure the vast majority of law-abiding, well-intentioned, and desperately needed charitable activities are not hampered in this process. Since our first meeting, we have convened periodically to consider subsequent drafts of the Guidelines and other publications issued by Treasury regarding terrorist involvement in the U.S. charitable sector.

We would like to request a meeting with you to discuss certain concerns we have regarding your report of May 21, 2007, entitled "Screening Tax-Exempt Organizations' Filing Information Provides Minimal Assurance That Potential Terrorist Related Activities Are Identified" (the "Report"), which criticizes the Internal Revenue Service for not using the FBI's Terrorist Screening Center's (TSC) consolidated watch list to check nonprofit tax filings for possible matches to suspected terrorists and for failing to automate its list-checking process. As explained below, we believe that the Report's recommendations for improvements to IRS's list-checking procedures will do little to combat financing of terrorist activity by U.S. charities but will impose heavy burdens on the IRS that could affect the charitable sector.

The Report's recommendations appear to rest on two assumptions: first, that U.S. charities are a significant source of terrorist financing, and second, that more efficient and comprehensive list-checking procedures would increase the likelihood of uncovering such terrorist financing. We believe that there is little factual basis for either of these assumptions.

There is simply no evidence that the U.S. nonprofit sector is a significant source of terrorist financing. Out of thousands of charities and billions of dollars in grants, only six U.S. charities have had their tax-exempt status revoked under section 501(p), and only 44 charities have been sanctioned under Executive Order 13224 because of their support for terrorist

activities. In addition, only six of the 43 charities on OFAC's list are based in the United States.

Furthermore, we find it unlikely that the procedures recommended by TIGTA will provide useful leads to the IRS Criminal Investigation Division or FBI on terrorist financing by U.S. charities. Checking nonprofit tax filings against lists of known terrorists is likely to uncover only inadvertent financing of terrorist organizations by U.S. charities, since a charity that intentionally involves itself with a terrorist organization is unlikely to disclose that fact to the IRS. Given the practical limitations on the amount of information reported on tax forms imposed by the size of the forms themselves, even an inadvertent transfer of funds to terrorist organizations is unlikely to be reported. In fact, thus far, there has been no evidence that any inadvertent diversion of funds from a U.S. charity to a terrorist organization has occurred. For example, of the 44 charities that have been sanctioned by the United States Government since 9/11 for involvement in terrorist activities, all were knowingly and intentionally financing groups that supported terrorist activity.<sup>1</sup>

Not only do we question the effectiveness of the recommended procedures in combating terrorist financing, we are concerned that the procedures will prove to be unmanageable and will divert IRS resources from more pressing needs related to the charitable sector. The IRS currently checks Forms 1023 and 990 manually against OFAC's list of 1,600 individuals and entities officially designated as terrorists. However, so far the vast majority of potential terrorist-related cases identified by the IRS list-checking have been "false positives." In fact, there is no evidence that list-checking by the IRS has ever uncovered a single instance of charitable involvement in terrorist activities.<sup>2</sup> Use of the

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<sup>1</sup> *Violent Islamist Extremism; Government Efforts to Defeat It: Hearing Before the S. Homeland Security Comm., 110<sup>th</sup> Cong. (2007) (statement of Chip Poncy, Director of Strategic Policy at the Treasury Department's Office of Terrorist Financing and Financial Crimes).*

The following is excerpted from Chip Poncy's testimony in front of the Senate Homeland Security Committee on May 10, 2007:

SEN. LIEBERMAN: ...But the connection therefore between the local charities – American-based charities – and foreign terrorist groups is knowing. I mean, this is not – they're not being duped by, you know, Hamas or Hezbollah. They intend to support them, correct?

MR. PONCY: That is certainly our view of it.

<sup>2</sup> The Report states that between October 2005 and September 2006 the IRS only identified 93 potential connections to terrorist groups based on Form 1023. Of these, only three merited further review, and one was cleared and granted tax-exempt status. The other two were still under review as of December 2006. Likewise, list checking against Form 990 between April 2005 and October 2006 produced 201 potential connections, and further review revealed that none were positive matches.



TSC list, which includes 200,000 names, will most likely only increase the incidence of false positives, requiring the IRS to spend valuable time and resources tracking down these leads and leading to delay in the processing of applications for exemption. An audit report from the Department of Justice's Inspector General in 2005 criticized the TSC for using inaccurate and incomplete information.<sup>3</sup>

We would appreciate an opportunity for a small delegation from the Treasury Guidelines Working Group to meet with you at your earliest convenience to further discuss these concerns. Rob Buchanan, Managing Director of International Programs at the Council on Foundations, will coordinate the meeting on behalf of the Working Group. His email address is buchr@cof.org; telephone: (202) 467-0391.

Sincerely,

Steve Gunderson  
President and CEO

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<sup>3</sup> *Review of the Terrorist Screening Center*, U.S. Department of Justice, Office of the Inspector General Audit Division, Audit Report 05-77, June 2005.