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Trends In Self-Regulation And Transparency Of Nonprofits In The U.S.

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Summary

After the United Way of America/Bill Aramony scandal in 1992, and several other surrounding scandals of high media visibility, many charitable leaders in the U.S. became concerned that the public, especially donors, would lose their confidence in the good of charitable organizations. The charitable community, thus, began thinking more about what should be done in terms of self-regulation and transparency that could both prevent similar scandals and prevent unwanted and possibly over-reaching new legislation. What has happened in self-regulation and transparency since? Is there more or less now? What forms do self-regulation and transparency take? What is effective and what not? Has existing self-regulation and transparency forestalled consideration of any new regulatory legislation?

Methodology: The author conducted a telephone survey of 41 charity leaders and state regulators to seek answers to these questions. Mostly national leaders were consulted, in the fields of health, education, welfare, the arts, advocacy and services. After interviewees identified significant attempts at self-regulation and transparency, relevant documents and other research were reviewed.

Findings: Improvement of board governance has been one form of self-regulation that has expanded. Codes of conduct emerged (*Ethics and the Nation's Voluntary and Philanthropic Community: Obedience to the Unenforceable*, the "Donor Bill of Rights" and "The Accountable Not for Profit Organization"). Some organizations with nonprofit members developed and implemented accreditation or "Good Housekeeping Seal of Approval" plans, usually with training and education of their members in good accountability practices as an essential component. One new independent national watchdog organization emerged, while the three established national watchdogs are all undergoing review and rethinking of how they do business. Cause related marketing linking business corporations and charities has expanded to $5 billion a year, attracting state Attorneys General interest and new self-regulation by charities. Disclosure or transparency has become the most popular means of self-regulation, especially through the Internet, though mostly it has been inspired by new federal government legislation that requires much easier public access to IRS forms 990 (for public charities) and 990PF (for private foundations), and allows Internet posting as an alternative to making paper copies of 990s available. Effectiveness, corruption, and use of 501c3 soft money for political campaigns were only considered as relevant issues by a very few respondents.

Conclusions.

Media attention to nonprofit sector scandals in the 1990s has increased the sector's discussion about regulation, self-regulation and transparency. Because once a scandal makes a splash in the national media, nonprofit leaders expect it to hit their charities, wherever located, however situated. But the media spend precious little time keeping track of nonprofits, and can only be counted on to publicize the really bad.

Governmental regulation wasn't effective in preventing these high profile scandals, nor is it seen to be effective generally in ridding the sector of bad apples. Resources are a key problem.

Thus, more attention in the nonprofit sector has turned to self-regulation. Both to avoid future major scandals and to avoid onerous legislation. Self-regulation through improving board governance is on the rise. Yet it is a sysipyan task with many difficulties. Sector-wide codes of conduct, codes of ethics, standards, principles of good practice all have garnered attention in the 1990s. Some have drawn media attention, but they have no persistence. Accreditation plans with enforcement or tangible rewards appear to be on the increase, particularly within nonprofit subsectors or membership organizations whose members undertake similar types of activity. Independent watchdog organizations are few and far between, with a limited growth potential, but have far-reaching influence. Cause related marketing is on both Attorneys-General and watchdog organizations' lists of serious problems, but involved nonprofits' self-regulation is tentative. Transparency, though mostly legislatively stimulated, and increasingly Internet stimulated, is on many charity leaders' minds as a better way to self-regulation.

TRENDS IN SELF-REGULATION AND TRANSPARENCY OF NONPROFIT ORGANIZATIONS

<u>Introduction.</u>

The 1990s have been a great trial for U.S. charities: the conviction of Jim and Tammy Faye Bakker for illegal activities connected with their televangelism; the forced resignation of the founder of Covenant House for improper advances to boys; the conviction of Bill Aramony, CEO of the United Way of America, for misuse of funds; the conviction of the founder/CEO of the Foundation for New Era Philanthropy for a pyramid scam; the forced resignation of the President of Adelphi University for lavish spending; the forced resignation of the trustees of the Hawaiian Bishop Estate for paying themselves $1 million each in trustee fees and other improper financial behavior; the forced resignation of the President of Feed the Children in Oklahoma for misuse of funds; the expose of fraudulent advertising by child sponsorship charities; the frequent reports of expired, inappropriate and sometimes perverse donated corporate products -- the list goes on and on when recounting the charity scandals exposed by the media in the past decade. Add in the *Philadelphia Inquirer's* book, *Free Ride: The Tax-Exempt Economy*.

Participants at the 1994 annual meeting of the Independent Sector were reported by *The Chronicle of Philanthropy*

> "...still not recovered from recent high-profile scandals involving misuse of funds by officials of well known charities....non-profit officials had been forced to look at themselves more critically and to come to terms with increased scrutiny from regulators, the press, and donors...The discussions covered a spectrum of topics that included establishing ethics codes, avoiding conflicts of interest, and creating new ways of penalizing charities that violate the law. A number of participants said they worried that unless non-profit groups cleaned up their own house and turned out cheats and frauds, regulators and lawmakers would step in and punish all charities collectively for the transgressions of the few."[1]

A year and a half later a *Chronicle of Philanthropy* poll of "292 people who gave at least $10,000 to charity in the past year found that almost 99 per cent said that the scandals had made them 'highly skeptical of claims made by fund raisers and non-profit executives.'"[2]

Also in 1996, the *Harvard Business Review* weighed in, saying, "Unless we are provided with credible, systematic information, fresh scandals will fill our daily newspapers and public trust in these critically important institutions will erode."[3]

In 1999, Joel L. Fleishman, Duke University Professor of Law and Public Policy, wrote, "...almost invariably, the press presents a picture badly out of focus, one that is unnecessarily alarming to the public, and even worse, that frequently undermines the public's confidence in the possibility of effective action. The result...is to create an atmosphere of hysteria which can sometimes lead to throwing out the baby with the bath. That is the single greatest threat to the (nonprofit) sector today."[4]

Also in 1999, Lester M. Salamon of Johns Hopkins University sounded cause for alarm, writing, "...important questions have been raised about the effectiveness and accountability of nonprofit organizations...this (and more have) undermined public confidence in the sector and prompted questions about the basic legitimacy of the special tax and legal benefits it enjoys."[5]

<u>Government Regulation.</u>

With so many bad apples in the barrel, greater government regulation of charities surely must be necessary.

Yet at a Philanthropy Roundtable conference in 1995, the lawyer for the Heritage Foundation made a presentation about the IRS' diminishing capacity to monitor and regulate private foundations, using statistics of the declining number of IRS audits of foundations in recent years to prove his point.

And at a National Center for Philanthropy and Law conference in 1997, the lawyer who runs the Nonprofit Coordinating Committee of New York presented statistical evidence that neither IRS nor state governments had the personnel capacity effectively to monitor and regulate nonprofits. Neither the IRS nor the representative of state government at the conference contradicted the speaker.

And last year the IS Government Relations Committee launched a lobbying campaign to persuade Congress to commit more tax revenues to beef up the Exempt Organizations Division of the IRS so it could more properly fulfill its responsibilities of monitoring and regulating the nonprofit community. It was unsuccessful.

Greater regulation to curtail and eliminate the bad apples in the charitable barrel is not at all likely. As Harvey Dale, Director of the New York University's National Center on Philanthropy and the Law, said in 1993, state charity bureaus are "inactive, ineffective, and overwhelmed."[6] Or as *The Chronicle of Philanthropy* reports in 1997, James J. McGovern, former IRS Assistant Commissioner for...Exempt Organizations, said that "Without significant changes in the way the federal government oversees nonprofit groups, 'I believe that a credible compliance program is in jeopardy.'"[7] And in 1999, according to Fleishman, "The present accountability-enforcing arrangements of the state and federal governments are entirely inadequate, as they currently function, to detect, deter, and punish illegal actions by a tiny number of organizations..."[8]

And private colleges and universities don't have to worry about any federal or state regulations (except for Massachusetts), according to *CASE Currents*, the publication of the Council for the Advancement and Support of Education.[9]

Thus, without effective regulation to provide solace, charity leaders throughout the U.S. have wrung their hands and felt tortured in their souls publicly and privately about the perverted state of charitable affairs the media has reported to the public.

So more and more charity leaders talk about the need for greater *self-regulation*. Also, they talk about *disclosure* and *transparency* as a means to promote better public accountability and self-regulation.

With this in mind, the author conducted a telephone survey of 41 charity leaders and state regulators to identify what currently exists as effective self-regulation and transparency and what trends were emerging.

Mostly national charity leaders were consulted, in the fields of health, education, social services, religion, arts and culture, and advocacy, also from charitable trade associations and watchdog groups. A complete list of interviewees is appended. After interviewees identified significant attempts at self-regulation and transparency, relevant documents were solicited and reviewed.

The Media as Regulator.

Interestingly, only two (5%) of the 41 surveyed mentioned the media when asked about trends..... (Borochoff and Ward). They mentioned the Feed the Children expose by *The Oklahoman*, *New York Times* reporting on inappropriate or unusable corporate donated goods to Bosnia, a recent article by the *Wall St. Journal* on corporations sending unwanted products to charities along with items in high demand, and the *Chicago Tribune's* critical coverage of child sponsorship groups.

Back in 1992, right after the huge Bill Aramony/United Way of America scandal, noted philanthropist turned critic Waldemar Nielsen reviewed all the possibilities of how to "make sure that the nation's charitable resources are not being misspent" and concluded that only the news media were truly available "as a protection for the public interest."[10]

Nevertheless, writing in *The Washington Post* two months ago, Geneva Overholser of the *Post's* editorial page reports that "Surveys over recent years show public confidence in, and approval of, American media (generally) decreasing steadily and substantially." She quotes Paul McMasters, the Freedom Forum's First Amendment Ombudsman, as saying, that studies discover that Americans view "the press (as) part of the problem, rather than part of the solution."[11] While these comments followed the media's feeding frenzy over the Clinton-Lewinsky affair, nevertheless, they reflect the cumulative change in American public opinion about media reporting about all matters over many years.

Fleishman, focusing exclusively on media attention to the media's reporting on charities, adds that "the press almost always neglects its...vital duty to put the 'bad' news it reports into the context of the 'good' news that forms the backdrop. It is almost always the case, too, that there is far more 'good' news to report than 'bad,' and that it takes much more effort to gather it than does the 'bad' news that comes in over the transom..."[12]

Self-Regulation through Improvement of Board Governance.

Analysis of the Jim and Tammy Faye Bakker, Covenant House, Aramony/United Way of America, Adelphi University, the Bishop Estate and Feed the Children scandals reveal that staff controls on heads of organizations were ineffective (because of inadequate procedures, insecurity, fear) and/or boards of directors either failed to detect the wrongdoings, or denied they existed (because the organizations seemed to be very effective in their missions).

A nonprofit board of directors is a "beauty" and a "beast." It is a beauty because any few people can form a nonprofit for almost any purpose imaginable. It is a beast because it can act "improperly."

Take the case of United Way of America in 1992 at the time of the big scandal with Bill Aramony, UWA's CEO:

> The organization was highly visible through nationwide TV ads every week.
>
> The organization was well established, over 100 years old.
>
> The mission and goals were clear.

> The board was a “blue ribbon” board including 2/3 corporate CEOs and 1/3 leaders from the professions and civic organizations.
>
> The administrative and fund raising expenses were quite low.

So what happened?

Well, the board looked at the huge size of the organization (raising $3 billion a year with its affiliates) and its substantial growth over the years, credited Aramony for this, slapped him on the back and said, “Good job, ole buddy. How can we help you today?”

The board, however, was acting like a beast! Among other things, the board obviously had failed to evaluate properly the organizations Aramony had proposed spinning off as independent subsidiaries, to inquire into the nepotism involved in staffing these spin-off organizations, and to assess the arrangements for continuing UWA oversight of the spin-off organizations. The board also had failed to provide routine oversight of the CEO’s expenditures. And the board had lost touch with charitable reality when setting Aramony’s salary and benefits package.

The real issue here is that all this could happen anytime, anywhere, to any size charity – especially when an organization appears to be doing very well. And it happens a lot more than the media reports.

Keeping the beast, however, is the price we pay for keeping the beauty. There is no silver bullet to slay the beast in the board. There are no ways to guarantee selection of good, conscientious people as board members, nor to keep them focused on proper board oversight matters. The beauty of the current legal framework for nonprofits – that a few people anytime, anywhere, can organize a nonprofit for almost any purpose imaginable – outweighs the horror of the beast.[13]

Nevertheless, improvement of board governance as a means to keep charities on track and scandals at bay was mentioned by eight (20%) of the 41 surveyed.

Bennet Weiner of the Philanthropic Advisory Service of the Council of Better Business Bureaus says improvement of board governance is currently a “big trend.” He cited the growth of the National Center for Nonprofit Boards (NCNB) as an example.

Judy O’Conner, President of the NCNB, verified Weiner’s insight, citing statistics of the monthly “hits” on her website growing from 15,000 in 1997 to 60,000 this year. O’Conner also reports growing interest of nonprofit academic centers and business schools in board improvement issues, especially how boards can play a bigger role in both governance and accountability, citing a newly initiated joint program with Harvard University as one example.

Nancy Axelrod, founding head of NCNB, now consulting, notes that she and others working closely with a wide variety of boards are observing four trends: (1) A greater incidence of self-assessments by boards. A number of umbrella organizations have developed or are currently developing customized self-assessment tools for their members to use (e.g. National School Boards Association, Association of Governing Boards of Universities and Colleges, American Symphony Orchestra League, and Council on Foundations). (2) A greater demand for developing procedures for boards to evaluate constructively the performance of the chief executive officer (and to review compensation). (3) An increase in establishment of "Governance" or "Board Development" committees dedicated to the orientation, continuing education, and assessment of the board, as well as identification and recruitment of new board members. (4) More scheduling of special sessions or board retreats to focus on strategic planning, governance reform or evaluation of programs and services.

According to Eric Wentworth, formerly with the Council for Advancement and Support of Education (CASE), the Association of Governing Boards has been working to improve selection and competence of college and university boards, but mostly this has involved large public institutions with lots of political appointees.

The National Council of Nonprofit Agencies reports board training by some NCNA state level member associations and hearing of same by some state Attorney General offices.

But David Ormstedt, State of Connecticut Attorney General's office, and former Chair of the National Association of State Charity Officials, said he has heard no such thing. He reports that Massachusetts and Minnesota have done some occasional board training seminars, but nothing regular. (Earlier in the decade Massachusetts and Nevada prepared and distributed handbooks for board members.[14])

However, Ormstedt talks about how board training and regular self-audits by boards can help make nonprofits much more accountable and have better practices, particularly if combined with a community network that encourages nonprofits to share information with each other. He's part of just such an effort in Connecticut now, which involves training of board trainers.

A proposal for a national commission to focus on improving standards of board governance has been advanced by Ulanov Partners, who are a U.K.-based management consulting firm started from McKenzie and Co. They have worked in 15 different countries, mostly in Europe, with both for-profit and non-profit organizations. Whether organizations wanted to grow or had other problems, board governance became central in most cases. There was not much understood about what governance was, or what the standards were (legal and otherwise). They worked with the (Sir Adrian) Capri Commission in the UK, a corporate sector initiative at the highest levels, to develop standards for corporate board governance. According to Nelson Gonzalez of the Ulanov Partners, the Commission had lots of impact. This led them to start thinking about doing something in the US, which led them to the proposal for a national commission.

Self-Regulation through Codes of Conduct, Codes of Ethics, Standards of Accountability, and Principles of Good Practice.

Many survey respondents mentioned codes, standards and principles as tools for encouragement of self-regulation and public accountability.

A key issue is whether the codes, etc. are designed to apply *within* an organization, with *affiliated* or *member* organizations, or with totally *independent* organizations. The *intra*-organizational use of codes is *not* part of this inquiry, so the focus below will be on the latter two situations.

On contract for the Independent Sector, the Maryland Association of Nonprofit Organizations studied 70+ nonprofit organizations' accountability efforts, and found "a 'continuum' of accountability services and programs...(ranging) from the most basic code of ethics or organizational values statement to the most comprehensive and sophisticated credentialing program involving multiple layers of evaluation, monitoring, and improvement...

"Such statements may cover employees, board members, volunteers, and their affiliated organizations...

"Some of these codes are aspirational in nature or values based in nature...Others more specifically address conduct. Codes which focus on conduct tend to set forth specific performance standards by which the actual behavior of the organization (or individuals within the organization) may be judged."

They cover "topic areas relating to governance and management practices, such as: mission and program, governing board, human resources, volunteers, financial accountability, legal compliance, public policy, communications, public relations, fund raising, conflicts of interest, disclosure and information technology."

According to the Maryland Association study, some organizations require those covered by the codes to sign statements of their commitments to act according to the codes, while other organizations leave compliance as an entirely voluntary matter.[15]

From survey interviews it is clear that most respondents believe codes of ethics, codes of conduct, accountability standards and principles of good practice are ineffective without enforcement, whether commitment statements are signed or not. Three lawyers in particular expressed this view. While other respondents, asked to recall some major efforts to establish new codes in the 1990s, either could not recall them, or, when prompted, commented that such codes had disappeared from sight.

The Independent Sector's *Ethics and the Nation's Voluntary and Philanthropic Community: Obedience to the Unenforceable* is one such effort. Published in 1991 after a huge membership involvement in defining it, this code of ethics was completely absent from the minds of all 41 survey respondents. Nor was the follow-up publication recalled by anyone (*Everyday Ethics: Key Ethical Questions for Grantmakers and Grantseekers,* 1993).

The "Donor Bill of Rights" in 1993 is another such effort. This outlines the guarantees and information that the public in entitled to receive from charities. Developed by the National Society of Fund Raising Executive, Council for Advancement and Support of Education (CASE), Association for Healthcare Philanthropy and the American Association of Fund-Raising Counsel, it had been in the works for several years, but the United Way of America scandal moved it fast forward. Five other major national charities joined in to endorse it: Independent Sector, National Catholic Development Conference, National Committee on Planned Giving, National Council for Resource Development and the United Way of America. All nine organizations were to take it to their members and affiliates for endorsement and to publicize it widely.[16] With the exception of one survey respondent who had a key hand in drafting the document, not a single other respondent mentioned the Donor Bill of Rights as on his/her radar screen. Although it did help stimulate another code.

"The Accountable Not-for-Profit Organization" was developed in 1995 by a group of charity leaders brought together by the Mandel Center for Nonprofit Organizations at Case Western Reserve University, the National Health Council and the National Assembly of Voluntary Health and Social Welfare Organizations, supported by the Lilly Foundation. Despite its auspicious parentage, again only one of the 41 survey respondents recalled this code effort, and she was one of those who had drafted it. It was invisible to all other respondents as a means to encourage self-regulation.

Herein lies the heart of the matter about codes, standards and principles. Does purely voluntary compliance provide effective self-regulation for the nonprofit sector? Or does compliance with rewards or non-compliance with penalties increase the possibilities for effective self-regulation?

The Maryland Association study addressed this somewhat obliquely, saying, "Rarely does the Code stand alone as an organization's exclusive effort in the area of ethics and accountability. The Code is not, after all, self-executing. It must be embraced by organizational leadership, become part of the corporate culture, and be implemented and followed by individuals that make up the organization. Educational activities play a major part in the success of any ethics program."[17]

The foregoing three attempts at sector-wide codes of conduct appear to have failed miserably. Commitment of organizational leadership beyond the drafters of the codes did not develop. There was no educational program implemented beyond the initial take-back to members and affiliates. There were no teeth to bite those in non-compliance, nor were there tangible rewards for compliance with the codes. Today no one knows the codes exist.

According to Diana Aviv, UJA Federations of North America, accountability has to be enforced by a larger community. She says that the Jewish community collective conscience is utilized to keep Jewish community agencies in line. When there is a problem with a local affiliate, key lay individuals are called upon to investigate and implement solutions. Aviv believes that lay leaders must be heavily involved in organizations and their processes for organizations to be publicly accountable. When professionals run the show, public accountability is more difficult to achieve, because it is easier to cover up misdeeds or wrongdoing.

According to Ngoan Lee, a community activist and state department of human services employee in Chicago, a similar collective conscience operates in Southeast Asian immigrant communities.

Membership organizations have a penchant for codes, standards and principles.

The Council for Advancement and Support of Education in 1994 issued standards for its nearly 3000 member educational institutions regarding uniform public reporting of campaign contributions. To encourage members to follow the uniform reporting requirements, CASE issues an annual report to donors and the public on members' campaign progress, only listing information for those in compliance.[18]

On a more comprehensive basis, since at least the early 1980s, the Council on Foundations -- with 1874 members -- has had "Principles for Effective Grantmakers." A foundation not willing to agree to the principles will either be denied membership or have its membership terminated. Since 1994, Independent Sector -- with 736 national organizations as members -- has had by-laws requiring members to "be committed to the corporation's values of openness, accountability and ethical behavior," otherwise membership, like in the Council on Foundations, could be denied or terminated.[19] While clearly these codes have acted as deterrents for applicant agencies not wanting to comply (in fact, a whole new council of foundations, the Philanthropy Roundtable, was created by right-wing foundations which did not want to commit to the Principles and Practices), nevertheless, there has been no public record of ever activating these codes to kick out existing members.

Nevertheless, both the Council on Foundations and Independent Sector are making new attempts at defining accountability and planning new educational programs for their members. In the Council's plan for the year 2000 and beyond, "accountability" has been recommended to the board for action in December as one of five "strategic priorities."[20] And the Independent Sector has just completed action on another Task Force on Accountability report (there had been one in 1994).[21]

According to the National Council of Nonprofit Associations (NCNA), at least two of its state association members have developed comprehensive codes, and a third is flirting with the idea. One of the leading and most outspoken associations, the Minnesota Council of Nonprofits, worked long and hard from 1993-1998 on developing a "Principles & Practices for Nonprofit Excellence," although the Council made compliance purely voluntary: "Because of the diversity of the sector by size, region, and activity area, each organization must make a determination of whether or not an individual practice is appropriate for the organization in its current situation."[22]

Meanwhile, another active state association, the Maryland Association of Nonprofit Organizations, has developed a "Standards for Excellence" program which has drawn very positive reviews from several of the survey respondents. The code has a strong educational component for member organizations to learn what is expected of them. However, the program also involves accreditation.

Accreditation.

Accreditation is a significant move beyond simple codes, standards or principles. The Maryland Association has a voluntary certification program which has recently certified its first three organizations as demonstrating their compliance. They are now eligible to utilize the program's logo ("A Symbol of Trust") on their fund raising appeals and other literature.[23]

According to the Maryland Association study, "Credentialing programs are important accountability mechanisms among nonprofit organizations today, particularly in the association community. Certification, Standards, and Licensing programs have all increased in prevalence in recent years[24]...Self assessment, peer review, site visits, and extensive review of organizational documents are common place....Ultimately, one of the critical considerations in structuring any credentialing program is enforcement."[25]

National accreditation programs have long existed for trade associations, colleges, universities, hospitals and even the fairly new health maintenance organizations, often involving both private and public entities. But national accreditation programs for other private nonprofit organizations are not so ubiquitous.

Part of the problem in creating sector-wide codes or accreditation programs is the diversity of organizations by type of activity, certainly at the national level, but, also at the state level, as illustrated by the fact that only two of the NCNA's 40 members have actually adopted codes, and only one a serious accreditation program.

Organizations whose members share types of activity, such as the National Health Council and the Evangelical Council for Financial Accountability (ECFA), seem to develop codes and accreditation programs more easily.

In place since 1997, the National Health Council's "Good Operating Practices Criteria" embrace 35 mandatory standards of public accountability and 13 non-mandatory standards (any eight of which members must meet). All 46 voluntary health agency members of the Council must meet these standards to be able to publicize that they are members in good standing with the Council. Vice President for Operations and Membership, Bob Goldberg, characterized the program as a "Good Housekeeping Seal of Approval." When the criteria were implemented, Goldberg reports that some then-current members were initially judged as only "conditionally" meeting the standards, but that all have subsequently come into line and now are in full compliance. No member has fallen from full compliance once achieved. Compliance is determined annually based on a lengthy questionnaire each organization submits to the Council, although if an organization meets all 48 standards (35+13), it only has to submit to review every three years.

The Evangelical Council for Financial Accountability (ECFA) was seen by several survey respondents as the epitome of an umbrella organization with a code and accreditation program that was effective. Scandals certainly were the instigation for ECFA, though not the 1990s scandals, but ones many years earlier. Threatened with legislation, the evangelicals banded together 20 years ago, developed effective peer regulation, and today have 925 organizations as members of ECFA. As Paul Nelson, the President, says, "It's the church caring for its own." ECFA has a standards committee separate from its board of directors which acts as the investigative arm of the board. It includes various types of experts, some from members, others not, all, however, part of the religious culture. The committee has not power in itself, but must make recommendations to the board. The committee reviews extensive questionnaires filled out by the members, but also makes 50-60 random site visits a year, during which members must pass the "red face and smell test." Nelson believes the peer regulation works because any bad member organization "threatens the good image of all the others." ECFA also separately investigates when complaints are made about a member's possible non-compliance. Nelson reports that while they add one new member organization every week, they also expel one member every two weeks.[26] The ECFA seal of approval thus provides donors with assurances of members' legitimacy. This is a code with the teeth of a serious accreditation program.

<u>Independent Watchdog Organizations.</u>

Independent watchdog organizations evaluate nonprofits against standards they conceive, then publish the results for public scrutiny. There are four national, sector-wide watchdog groups, only one of which is new in the 1990s.

- National Charities Information Bureau (NCIB), New York City (1918)

- Philanthropic Advisory Service of the Council of Better Business Bureaus (PAS-CBBB), Arlington, VA (circa 1974)

- National Committee for Responsive Philanthropy (NCRP), Washington, DC (1976)

· American Institute of Philanthropy (AIP), Bethesda, MD (1992)

Three of the four watchdogs evaluate public charities governance and financial situations, while the fourth (NCRP) evaluates institutional philanthropies for their responsiveness to disenfranchised populations.

Three of the four are undergoing major changes, as new chief operating executives have taken over in two (NCIB and NCRP) and the third (PAS-CBBB) has created a new Standards Review Panel to rethink its criteria for evaluation of nonprofits. The reasons for the new PAS-CBBB Panel are:

1. Increased public interest in charity accountability

2. Changes in nonprofit accounting guidelines

3. New forms of fund-raising, such as Internet-based appeals

4. Growth of cause related marketing

5. Rise of local charities in importance

6. Rise of international charities in importance.[27]

NCIB will also be undertaking a review sometime soon. Bill Massey has just been on the job as President for under a year. He plans to rethink NCIB's standards because:

1. Accounting standards have changed.

2. Technology has entered the picture.

3. The public wants easy answers (which might not be possible or useful).

4. The older generation is more trusting (thinking charity is an act of kindness, with nothing expected in return), while the contemporary generation seeks more to be philanthropic entrepreneurs (seeing philanthropy as an investment, wanting to see clear return).

5. But younger donors are tending to give more locally, because they can more clearly see the results, and because they want their own parks, neighborhoods, schools, etc. to be better (though this is not entirely selfish).

6. What is accountability? Is it visibility? More people believe in a charity nowadays if they hear about it on National Public Radio, annual reports are not read.

7. The public cannot count on the courts or governments to encourage or order charities to do the right things, or to monitor them.

8. There is a blurring of sector lines which is causing the public to lose public trust in charities as distinct entities from government and business.

9. Cause related marketing is growing, and the public has a right to know about the details of charities' involvement with corporations in these deals.

10. There are major Internet abuses about the percentage of purchases from for-profit firms that go to charity. Disclosure is key.

11. Confusing forms. The 990 is useless as a marketing or public relations piece. What does the

public know about reading a 990.

12. There is a need for education of young donors so they can learn to enjoy and celebrate giving.[28]

In 1998, the board of the National Committee for Responsive Philanthropy approved a strategic plan reaffirming NCRP's traditional role as a critic of foundations, corporate giving programs and United Ways, but also calling for increased collaboration with other organizations in carrying out its programs and greater attention to building a "grassroots" movement for change. NCRP then installed a new President earlier this year, but deepened its commitment to the new strategic directions in a June board retreat. What will this really mean, after nearly 23 years of leadership by the founding Executive Director/President? It is hard to tell yet, but change is in the air.

The American Institute of Philanthropy has made some big waves in its short tenure (seven years). Deciding to publicize the charities which had huge reserves yet continued soliciting for operating money, AIP gave Father Flanagan's Boys Home (Boys Town) a failing grade for having reserves that could fund operations for five years. The charity hauled AIP into court, saying donors would think Boys Town was corrupt. They settled out of court with neither party backing down, but deciding on a clarifying statement.[29]

AIP's founding President, Daniel Borochoff, is thinking of moving on. This "new kid on the block," smaller and with less history than the other watchdog organizations, may see a major transformation when Borochoff goes, whether he wants that to happen or not.

<u>Cause Related Marketing and Government-Encouraged Self-Regulation.</u>

Six (15%) of 41 surveyed mentioned charity-corporate relationships as a growing concern, including three major independent watchdog agencies and two state regulators. The newest standard for the National Health Council concerns members' corporate relationships. More and more of the Council's voluntary health agency members have gotten involved with corporate marketing efforts. The health agencies get money, rent their logo or name, the corporations market their products or services identified with the health agencies.

Sixteen Attorneys-General recently issued a report and held a public hearing in New York City about the issues surrounding the use of charities' good names in marketing corporate products and services. The report estimates this action at $5 billion/year (corporations only grant around $9 million a year). Health charities were a prime concern. The report concluded with a set of preliminary recommendations. None of these recommendations are for potential laws, but are to be considered as useful principles for charities to maintain their good names.[30] One might call this government encouraged self-regulation.

According to Goldberg at National Health Council, the health agencies and Attorneys-General are close to agreement on principles for charities' involvement in corporate advertising -- except that they differ about what should be told to the public about what they are *not* doing. For example, if the health agencies are not actually endorsing a product or service, the Attorneys-General want the ads to state that the charities are *not* making an endorsement, while the charities say the ad should say *nothing* if, indeed, they are making *no* endorsement.

According to Borochoff of the American Institute of Philanthropy the hearing demonstrated that charities are against further disclosure.

Disclosure/Transparency Is Another Means to Self-Regulation.

Disclosure/transparency is another means to self-regulation, because it gets people involved in evaluating nonprofits who are outside the staff and board power structures, such as those listed below:

Junior staff

Board members not in power loop

Clients

Members/constituency

Peer nonprofit organizations

Funders

Potential donors

Media

The public

Government

Disclosure has been a hallmark of leading charities and grant-making foundations for many years. They have *voluntarily* been publishing annual reports, grant guidelines, brochures and newsletters to inform the public, potential and actual donors and grant-seekers. Data usually include financial balance sheets and statements of income and expenses; lists of officers and key staff; mission statements, organizational and program goals; reviews of history and accomplishments; future plans; lists of donors; and more. Foundations usually also report lists of grants made, to whom, for how much, and for what purposes.

However, according to the National Committee for Responsive Philanthropy (NCRP) study in 1980, only 40% of 208 of the largest foundations rated “acceptable” based on the content of their voluntarily published annual or other reports, while nearly one-third voluntarily provided no information to the public about their activities.[31]

Moreover, according to the Foundation Center, only 41% of large foundations with assets of $25 million or more voluntarily publish annual reports, and only 25% of the 11,000 largest foundations (assets $1 million+ or grants $100,000+) publish anything at all. These figures are *lower* than they were 20 years ago.[32]

Statistics are not available on *charities’* publishing of annual reports, etc., but those that are proud of their work and plans, publish, while many do not.

Voluntary disclosure, however, has other inadequacies. Selected information might only be disclosed. Insufficient information might be disclosed. Inadvertently wrong information might be disclosed. Deliberately omitting damaging information is possible. Intentionally erroneous information might be disclosed. The first three of these five sins of disclosure are not evil, but rather sins of omission and honest error. Nevertheless, they cause problems for people intent on evaluating the reporting organizations. The fourth and fifth sins, though, are evil, designed to mislead, generally to shield principals who are self-dealing or seeking private benefit.

Legally required public reporting can help to minimize all these sins of disclosure, though it will not, by itself, eliminate any of them. Legally required disclosure means that certain items of information must be publicly reported whether an organization wants to or not. Therefore, this virtually eliminates the problem of "selected" and "insufficient" information reporting (assuming the reporting requirements are right). Legal requirements for public reporting do not eliminate "inadvertently wrong" reporting, nor, of course, the deliberate omissions and intentional errors. But the requirements do expose these sins to greater public scrutiny than the uneven, inconsistent content of voluntary reporting. People who care become used to seeing certain key items of information, will miss them when they are not there, or are insufficient, or may be egregiously wrong.

Local and state governments usually require registration for public solicitation, and some require filing of solicitation plans as public documents.

Federal and often state law require filing of 990s/990PFs as public documents. These documents contain all the basic information identified above that nonprofits and foundations usually voluntarily publish, but they also include expenses by program; lobbying expenses; complete lists of directors or trustees, with any compensation, expense accounts and/or allowances; identification of the five highest paid employees and five highest consultants; analysis of income producing activities (including program service revenue, government fees and contracts, member dues and assessments); and more.

New federal law requires greater public access to 990s/990PFs. Any citizen visiting a charity or foundation's office can request immediate access to the 990s/990PFs and the organization's original application for tax exempt status, and any citizen posting a written request can expect to receive these documents within 30 days for no more than nominal costs of duplicating and postage. Regulations are out and final on 990s, and are published as draft regs for 990PFs. (As of March 2000, the regs for 990PFs are final. The *Chronicle of Philanthropy* reports that some differences exist between the 990 and 990PF regs. Private foundations will have to make their contributor lists available, while nonprofits filing 990s do not have to. Also, while both private foundations and other charities must eventually make their last three years of 990s/990PFs available to the public, for now, private foundations need only make their 990PFs available if filed after March 13, 2000, whereas other charities must make their 990s available for the last three years regardless of when filed.)[33]

Publication on Internet is now a legal alternative to making paper copies freely available, under the regulations.

These new laws regarding 990/990PF disclosure and Internet posting are already making disclosure more popular, according to many of the survey respondents. Although Connecticut's Assistant Attorney-General David Ormstedt says it isn't so.

Mandatory electronic filing of 990s/990PFs will be here in a few years, leading to instant public Internet access. This required filing will lead to more voluntary Internet disclosure. The Securities and Exchange Commission (SEC) now requires all corporations selling to the public to file 10K forms electronically.

Rep. Paul Gillmor (R. OH) proposed legislation in the late 1990s which held promise for required public reporting of *all* corporate contributions on the Securities and Exchange Commission's 10K form. (Corporate foundations have to report *all* contributions on the 990PF, but other corporate giving programs are *not* currently required to make any public report.) However, the Independent Sector, Council on Foundations and many of their member corporations sacked it. What emerged is a weakened bill (H.R. 887) requiring corporations to report (1) their *total* gifts (whether cash, in-kind or whatever), rather than each and every charitable contribution, (2) individual contributions which exceed a threshold amount to be determined by the SEC, and (3) contributions involving conflicts of interest. Hearings were held by Rep. Gillmor Oct. 29.[34]

Guidestar (Philanthropic Research, Inc.) and the Evergreen Society have been putting up some charities' 990s plus selected other information from annual reports, brochures, etc. on the Internet to permit active donor research. Guidestar is expanding its service to reports on "over 100,000 charities" this fall.[35] (As of

March 2000, Guidestar's website <www.guidestar.org> claims to have reports on 620,000 charities.)

Scanned versions of *all* 990s received by the IRS are going up on the Internet in 2000 in a program worked out by Philanthropic Research, the Urban Institute's National Center for Charitable Statistics and the IRS. "Timely, in-depth disclosure of this public information will revolutionize our understanding of charitable organizations – their structure, missions, investments, administrative costs and interactions with the government and business sectors," says Elizabeth T. Boris, Director of the Center on Nonprofits at the Urban Institute.[36]

This Internet exposure might encourage charities to put up more information than the 990 requires, in order to explain or provide a context for salaries, board of directors' fees, consultant fees, unusual expenses and other data.

But more data/information is not a panacea for accountability, since potential donors do not have time to search through everything, nor necessarily the capacity to evaluate same, says Chuck Bell of Consumers Union.[37] And there is little in the way of analysis, criticism or comment, adds Dan Borochoff of the American Institute of Philanthropy.[38]

Quality reporting on 990s is an increasing issue: first, to improve the quality of the required data and information, eliminating blanks and improperly filled out forms; second, to improve the user-friendliness of the 990 document. Sponsors of the Quality 990 project are the Urban Institute's National Center for Charitable Statistics, National Council of Nonprofit Agencies, Independent Sector and National Society of Fund Raising Executives. See <www.qual990.org>

Some cities are passing more far reaching transparency ordinances, such as San Francisco, which requires open public meetings and publication of meeting minutes by nonprofits accepting substantial government dollars.

Some nonprofits are worried that all this increased transparency will provide easier access for troublemakers (Planned Parenthood of America, UJA Federations of North America, Alliance for Children and Family). And according to an email from Independent Sector, Marcus Owens, Director of Exempt Organizations at IRS is "expecting the number of complaints about tax-exempts to increase dramatically now that Form 990s are widely available on the web."[39]

But Peter Swords discovered that "large numbers of cases of abuse (of the charitable trust) that (IRS and state agencies) investigate and prosecute are originally brought to their attention from outside sources, particularly by stories appearing in the newspapers and other media."[40]

Disclosure, thus, helps society deal with several issues:

Provide information to potential clients, members, constituents

Provide information to potential donors and volunteers

Provide basic data to media

Provide basic data to researchers

Establish norms for peer organizations:

Salaries

Trustees' and directors' fees

Total revenues

Mix of revenues

Total expenses

Mix of expenses

Fund raising costs as % of revenues

Performance

Identify possible conflicts of interest

Identify possible corruption

Identify possible illegal activity.

What Has Not Been Discussed in This Paper.

Effectiveness: only two people surveyed mentioned this -- even though Independent Sector has a huge project designed to develop better measures of effectiveness, instigated because of perceived public concern.

Corruption: only one mention -- even though all the scandals noted by the media involved corruption in some form or another.

501c3 "Soft Money" for Campaign Finance: only one mention – even though the issue has been a paramount one in Congress ever since the 1996 election.

Of course, if a new survey were conducted with these three terms explicitly raised with each respondent, much might be said about them.

Conclusions.

Media attention to nonprofit sector scandals in the 1990s has increased the sector's discussion about regulation, self-regulation and transparency. Because once a scandal makes a splash in the national media, nonprofit leaders expect it to hit their charities, wherever located, however situated. But the media spend precious little time keeping track of nonprofits, and can only be counted on to publicize the really bad.

Governmental regulation wasn't effective in preventing these high profile scandals, nor is it seen to be effective generally in ridding the sector of bad apples. Resources are a key problem.

Thus, more attention in the nonprofit sector has turned to self-regulation. Both to avoid future major scandals and to avoid onerous legislation. Self-regulation through improving board governance is on the rise. Yet it is a sysiphyan task with many difficulties. Sector-wide codes of conduct, codes of ethics, standards, principles of good practice all have garnered attention in the 1990s. Some have drawn media attention, but they have no persistence. Accreditation plans with enforcement or tangible rewards appear to be on the increase, particularly within nonprofit subsectors or membership organizations whose members undertake similar types of activity. Independent watchdog organizations are few and far between, with a limited growth potential, but have far-reaching influence. Cause related marketing is on both Attorneys-General and watchdog organizations' lists of serious problems, but involved nonprofits' self-regulation is tentative. Transparency, though mostly legislatively stimulated, and increasingly Internet stimulated, is on many charity leaders' minds as a better way to self-regulation.

LIST OF THOSE INTERVIEWED

Ed Able, President and CEO, American Association of Museums, Washington, DC

Diana Aviv, Senior Associate Executive Vice Pres., Public Policy, UJA Federations of North America, Washington, DC

Nancy Axelrod, Founding President of National Center for Nonprofit Boards, now consulting, NonProfit Leadership Services, Washington, DC.

Chuck Bell, Director of Programs, Consumers Union, NY

Peter V. Berns, Executive Director, Maryland Association of Nonprofit Organizations, Baltimore MD

Dan Borochoff, President, American Institute of Philanthropy, Bethesda, MD

Diane Canova, Vice President of Advocacy, American Heart Association, Washington, DC

Harvey Dale, Founder and Director, NYU National Center on Philanthropy and the Law, NYC

John De Haan, Executive Director, Association of Evangelical Relief and Development Agencies, Washington, DC

Shelly Dreyling, Minnesota Council of Nonprofits, St. Paul

John Edie, Senior Vice President and General Counsel, Council on Foundations, Washington, DC

Rita Fuerst, Volunteer Project Manager, CIVICUS Code of Conduct Project; CPM Counsel, Boston

Janne Gallagher, Deputy General Counsel, Council on Foundations, Washington, DC

Bob Goldberg, Vice President for Operations and Membership, National Health Council, Washington, DC

Nelson Gonzalez, Ulanov Partnerships, Princeton NJ

Nathan Gray, Director of Office of CEO Operations, American Cancer Society, Atlanta, GA

Sandra Gray, Vice President, Independent Sector, Accountability Task Force, Washington, DC

Flo Green, Executive Director, California Association of Nonprofits, Los Angeles

Dierdra Halloran, General Counsel, U.S. Catholic Conference, Washington, DC

Michael Hone, Prof. of Law, Univ. of San Francisco, Reporter for *The Revised Model Nonprofit Corporation Act,* 1988, Prentice Hall Law and Business.

Linda Lampkin, Manager of National Center for Charitable Statistics, Urban Institute, Washington, DC.

Ngoan Lee, Department of Human Services, State of Illinois

Bill Levis, Senior Associate, Urban Institute, NYC

Pat Lewis, Professor, Nonprofit Management Studies, George Mason Univ.; former President/CEO, NSFRE

Bill Massey, President, National Charities Information Bureau (NCIB), NYC

Paul Nelson, President, Evangelical Council for Financial Accountability (ECFA), Washington, DC

Judy O'Conner, President, National Center for Nonprofit Boards, Washington, DC

David Ormstedt, Assistant Attorney General, State of Connecticut, Hartford

Joe Romer, Executive Vice President Public Affairs, National Easter Seal Society, Washington, DC

Cathy Shea, Consultant, International Center for Not-for-Profit Law, Washington, DC

Mark Silbergeld, Co-Director of the Washington, DC Office, Consumers Union

John Sparks, Director of Government Affairs, American Symphony Orchestra League, Washington, DC

Sheldon Steinbach, General Counsel, American Council on Education, Washington, DC

Peter Swords, President and Executive Director, Nonprofit Coordinating Committee of New York, NYC

Barbara Turkheimer, Assistant Attorney-General, State of Wisconsin, Madison

Carmen Delgado Votaw, Vice President for Public Policy, Alliance for Children and Family, Washington, DC

Jane Robinson Ward, Director of Public Policy, National Council of Nonprofit Associations, Washington, DC

Bennett Weiner, CEO, Philanthropic Advisory Service of the Council of Better Business Bureaus, Arlington, VA

Eric Wentworth, former Director, Government Relations, Council for Advancement and Support of Education (CASE), Washington, DC

Mildred Kiefer Wurf, Director of Public Policy, Girls Inc., Washington, DC

Adam Yarmolinsky, Regents Professor of Public Policy, University of Maryland; former Chair, Independent Sector Government Relations Committee, Washington, DC

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