Hushed Money

It's time that philanthropic donors speak up for reforms

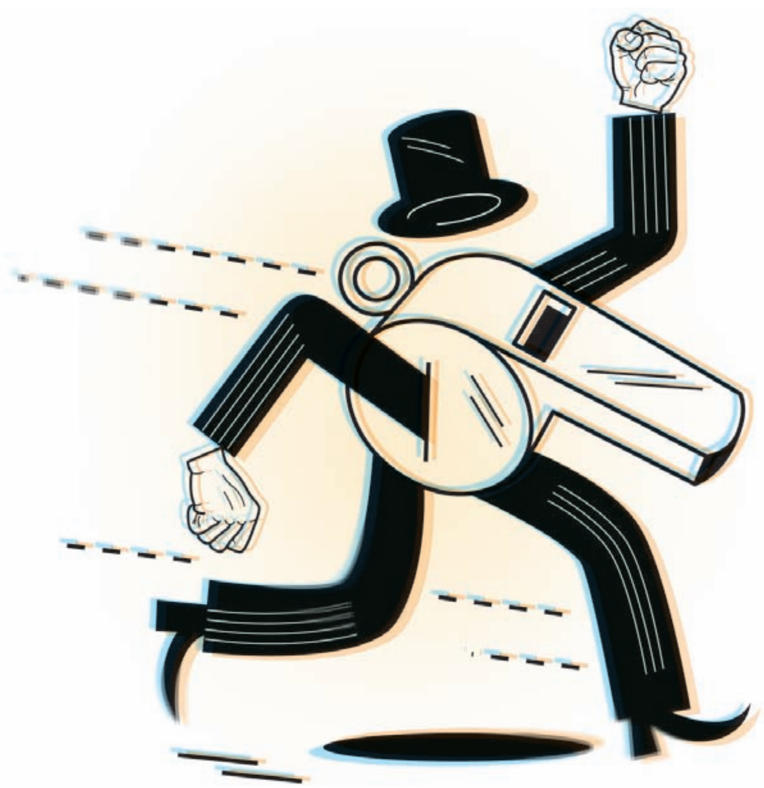

ILLUSTRATION: HARRY CAMPBELL; PHOTO: DAN DEMETRIAD

It's time to hear from the donors. While the Sarbanes-Oxley Act of 2002 required new levels of accountability and transparency from America's publicly-traded corporations, no such accountability is demanded of America's publicly-supported nonprofit institutions. Yet Americans' aggregated annual gifts to charity of $240 billion is higher than the revenues of many corporations. And many individual charities receive very large sums annually—more than $4 billion to the United Way and $1.5 billion to the Salvation Army in 2004 and $750 million to the American Red Cross in the weeks following Hurricane Katrina.

If the shareholders of America's publicly-traded corporations can now expect improved board governance and more responsible oversight of revenues and costs, surely America's donors deserve similar oversight in the organizations they support.

Perhaps it's time for those donors to demand such reforms.

Sarbanes-Oxley grew from revelations of fraud, corruption and board negligence at Enron, WorldCom, Tyco and other corporate giants. Corporate America was largely silent until the Senate began its hearings.

The nonprofit world is hardly immune from similarly appalling practices. Recent headlines have pointed to mismanagement or outright fraud at the American Red Cross, the James Beard Foundation, and the J. Paul Getty Trust, for example. Yet stakeholders in the nonprofit world have been silent.

Now, however, the Senate Finance Committee has begun to focus on the nonprofit sector. Committee Chairman Senator Charles Grassley (R-Iowa) has urged his committee to examine rules and regulations for nonprofit institutions similar to many incorporated in Sarbanes-Oxley. According to Senator Grassley, "Such laws will strengthen charitable governance…[and] help ensure continued public confidence and support for nonprofits." Senator Max Baucus of Montana, the ranking Democrat on the panel, joined his call for action by adding, "It is time for Congress to send a message."

Suggestions for more regulation and increased transparency are as controversial in the nonprofit world as the Sarbanes-Oxley act is in the corporate world. Some say that self-regulation alone can control problems in the nonprofit sector. Others argue that additional regulations will place undue financial burdens on these organizations and that additional requirements for board members—a central feature of the Sarbanes-Oxley Act—will discourage good people from serving on boards.

> "The recent history of corporate America shows self-regulation has not worked and there is little reason to believe it will work any better in the nonprofit sector."

Naomi Levine

> "Just as the corporate world stood largely silent in the Enron debacle, leaders of the nonprofit world have done little to further nonprofit reform."

But the recent history of corporate America demonstrates that self-regulation has not worked. There is little reason to believe it will work any better in the nonprofit sector.

Many of the provisions of Sarbanes-Oxley can be applied to nonprofits at minimal additional cost to them. For example:

1 Board membership should require financial literacy training.

2 Nonprofits with budgets of more than $500,000 should assess the benefits and costs of annual audits.

3 All nonprofits that conduct outside audits should have an Audit Committee separate from the Financial Committee. The Audit Committee should be directly responsible for hiring, setting compensation and overseeing the activities of the auditors, and for reporting on the audit to the full board.

4 All nonprofits should ensure that no member of the staff, including the chief executive officer, should serve on the Audit Committee, although it is reasonable to have the key financial officer provide staff support to the Audit Committee.

5 Auditors should be rotated every five years and no auditing firms should provide non-auditing services, such as bookkeeping, financial information systems, appraisal, management, human resources, investment or legal services.

6 The chief executive officer and the chief financial officer should certify the organization's financial report, with the board having ultimate financial responsibility. Audited financial statements must be available to the board.

7 Every nonprofit organization should have a Conflict of Interest statement and every board member should sign it.

8 No board member should ever receive loans from the nonprofit organization.

9 The IRS should be prepared to receive Forms 990 and 990-PF filed electronically.

Many of these suggestions for the nonprofits were recently incorporated into a report by the Panel on the Nonprofit Sector created on the recommendation of the Senate Finance Committee. The panel—with input from many of the most important leaders in the world of philanthropy— issued its report in June 2005, but there has been little public debate about the panel's findings in the nonprofit community.

Perhaps it's time to hear from the donors.

Just as the corporate world stood largely silent in the Enron debacle, leaders of the nonprofit world have done little to further nonprofit reform. In October 2005, Senator Grassley said:

"The charitable community should stop standing silently on the sidelines when the newspapers are filled with stories of flagrant waste and abuse at a charity. I'm troubled that there was little to no criticism from the charitable community about the serious problems at American University and the Getty Foundation. Charitable leaders must be strong-voiced in condemning inappropriate behavior in their sector."

So I end this column as I began: If the leadership of the nonprofit community fails to speak out on necessary reform in board governance and transparency, it is time—in fact, past time—to hear from the donors.

> "Every nonprofit should have a Conflict of Interest statement and every board member should sign it."

19%

The percentage of 1,820 Americans surveyed who said charities were doing a very good job running their programs and services.

Source: NYU's Robert F. Wagner Graduate School of Public Service

Naomi Levine is chair and executive director of New York University's George H. Heyman Jr. Center for Philanthropy and Fundraising and a regular columnist for this magazine. Her next column will appear in the May/June issue. Please send comments about this column to editors@contributemedia.com.