

ETHICAL STANDARDS FOR CHARITIES

Developed by the Mayor's Task Force on Ethical Standards for Charity

October 31, 1990

(Currently being updated 2006)

III. Board Responsibility

STANDARD #1

The Board of Directors develops and approves a clearly defined mission statement; develops and approves policies; and, after consultation with the chief staff person, approves goals and objectives.

Comment:

The Board of Directors meets its fiduciary responsibilities through compliance with this standard and by ensuring that the organization is provided with the financial resources needed to accomplish its mission.

All policies, goals, and objectives must be consistent with the mission.

STANDARD #2

The Board selects, trains, removes, and evaluates its members.

Comment:

The selection and training of Board members fosters independent judgment, which is defined as the Board's ability to make decisions, without undue influence and based solely on commonly known facts, that serve the best interest of the charity.

A charity needs to develop and implement a plan for the orientation of new Board members. The Board member must know who is doing what and why, and how the Board member contributes to the overall success of the organization. A formal orientation training program, including written materials, is suggested. The training should include the duties, responsibilities, and expectations associated with Board membership, a history of the organization, and a statement on the legal obligations of Board membership.

STANDARD #3

The Board meets regularly to carry out its duties and responsibilities as stated in these standards. The Board establishes the time, place, and dates for its meetings.

Comment:

Board members should be selected in part on the basis of their willingness to serve and their ability to give the time necessary to participate in scheduled Board meetings and complete committee assignments.

STANDARD #4

The Board reviews and approves the budget and various financial statements and audits.

Comment:

Verifiable program statements (or a description of services provided) should be included with the budget. Thus the budget points toward material proof that demonstrates the existence, nature, and quality of charitable service programs.

STANDARD #5

The Board supervises, evaluates, and sets the compensation for the chief staff person.

Comment:

The Board is the immediate supervisor of the chief staff person. Such supervision can be achieved by delegation of this responsibility to the volunteer chair or president of the Board.

The Board achieves mission, policy, and program objectives through the chief staff person and does not interfere with the chief staff person's supervision and management of subordinate staff. The Board controls the operations largely through direction given to, and evaluation of, the chief staff person. A good relationship between the Board and the chief staff person is a partnership, where collaboration, consultation, and open communications are evident.

The chief staff person is responsible for implementing Board policies and managing the day-to-day operations of the organization. Thus the Board evaluates and sets the compensation for the chief staff person. Although the

Board does not evaluate subordinate employees, the salary account is subject to Board review and approval as part of the annual budget process.

STANDARD #6

The Board reviews and approves all fund-raising practices in general.

Comment:

The Board should establish written policies for all fund-raising activities. These policies serve the best interests of the organization by identifying acceptable and unacceptable fund-raising practices.

The Board should have a specific written policy on the acceptance of gifts from those whose business or reputation is inconsistent with the charity's mission (e.g., tobacco industry support for a lung association). To be ethical, a Board needs to discuss and adopt a policy on this issue before the development staff is confronted with a potentially controversial donation.

STANDARD #7

The Board reviews and approves all groups who wish to raise money for the organization.

Comment:

Whether the group be an internal support group (e.g., "friends of") or an outside firm (e.g., the local chamber of commerce), the Board should review and approve the group before allowing it to raise money in the name of the charity.

IV. Accountability and Public Disclosure

STANDARD #8

The Board reviews and approves an annual report.

Comment:

The annual report includes:

1. a roster of the Board;
2. a clear statement of organizational mission;
3. a delineation of program offerings consistent with the stated mission;

4. a statement of program accomplishments; and
5. financial information.

Financial information found in the annual report need not include the financial statements such as those prepared for an audit but shall be derived from the annual audit or other financial records, all of which shall accurately and completely reflect the financial condition and operations of the organization.

The preparation and availability of the annual report shall be consistent from year to year. Should the annual report serve a “fund-raising” and “donor bill of rights” are applicable to the annual report.

Final copies of the annual report and financial statements should be distributed to all members of the Board of Directors.

STANDARD #9

All financial records are kept and financial statements prepared in accordance with Generally Accepted Accounting Principles (GAAP) for nonprofit organizations.

Comment:

Standards #9, #10, and #11 are to be taken literally by an established charity with a substantial budget. Smaller or newer charities should view these standards as an ideal toward which the Board and chief staff person move the organization as it grows.

STANDARD #10

Financial statements are audited annually by an independent accountant or auditor.

STANDARD #11

Annual financial audits are conducted in conformity with Generally Accepted Auditing Standards (GAAS).

Comment:

The Board determines the scope and cost of the annual audit. A Board with a substantial budget is expected to retain an outside professional accountant to perform an annual certified audit.

The purpose of this audit is independent verification of the financial data from which financial statements are derived. Those data are kept according to GAAP;

the audit is conducted according to GAAS; and the resulting independent audit produces a qualified or unqualified audit report.

To achieve these technical accounting and auditing ends, a charity should possess, understand, and use standard reference work, including but not limited to:

American Institute of Certified Public Accountants.
Audits of Voluntary Health and Welfare Organizations. 2nd ed.
New York: AICPA, 1988.

National Health Council, Inc., National Assembly of National Voluntary Health and Social Welfare Organizations, Inc. and United Way of America. Standards of Accounting and Financial Reporting for Voluntary Health and Welfare Organizations. 3rd ed. Revised. New York: National Health Council, 1988.

United Way Institute, United Way of America.
Accounting and Financial Reporting: A Guide for United Ways and Not-for-Profit Human Service Organizations, 2nd ed. revised.
Alexandria, Virginia: United Way of America, 1989.

Other sources that should be consulted are:

the AICPA Statements of Position (SOP), including SOP 87-2, “Accounting for Joint Costs of Informational Materials and Activities for Not-for-Profit Organizations that Include a Fund-Raising Appeal.”

the Financial Accounting Standards Board (FASB) Statements of Financial Accounting Standards, notably number 32, 13, 43, 74, and 87.

the FASB Concepts Statements, notably number 6, “Elements of Financial Statement.”

Discussion here has focused on the financial audit, which typically yields statements involving a balance sheet, changes in fund balance, public support and revenue, line-item and functional expense, and explanatory notes (such notes should describe conflicts or self-dealing in objective terms). This audit, however important it may be, is not the only “audit” in which the Board of Directors has an interest. That is, the Board may wish to conduct other kinds of “audits,” including, for example:

A “compliance audit” that determines the extent to which the charity is adhering to external and internal laws, regulations, policies, and procedures;

A “cost effectiveness audit” that determines if the acquisition and use of personnel, materials, and facilities were accomplished in an economic and efficient manner; and

A “program effectiveness audit” that, based upon qualitative and quantitative performance measurements, determines if the charity has made progress toward or accomplished stated objectives.

STANDARD #12

The chief staff person obtains and maintains all appropriate or applicable exemptions, certifications, licenses, and permits.

V. Conflicts of Interest and Self-Dealing

STANDARD #13

The Board develops, adopts, and implements a written policy and procedure governing conflicts of interest and self-dealing transactions between the charity and associated persons. The policy and procedure are communicated to all associated persons.

Comment on Conflict of Interest:

The policy and procedure must provide for full disclosure of all potential or actual conflicts of interest or self-dealing transactions. The procedure must permit the Board to validate or invalidate transactions between the charity and associated persons.

Associated persons include members of the Board of Directors, employees, and other volunteers who act in a policy-setting capacity or have material decision-making authority. Persons or firms related to associated persons should be considered as associated also.

A conflict of interest occurs when an inappropriate benefit accrues to an associated person and there is a corresponding adverse impact on the charity. A variation occurs when the transaction or relationship has the appearance of a conflict when in fact there is no adverse impact on the charity.

A conflict of interest also occurs with non-monetary transactions. This is, an associated person should not use or consume for private gain or advantage a charity’s facilities, equipment, mailing list, computer data, employee time, or any other resource or asset.

Comment on Self-Dealing:

Persons are asked to become associated with the organization because of special skills, attributes, contacts, or affiliations. With this in view, complete avoidance of self-dealing situations is unrealistic. Thus the Board has policies and procedures to regulate such situations.

Only the Board may authorize or validate a self-dealing business transaction between an associated person and the organization. The associated person shall not vote or use personal influence on the matter and cannot be counted in a quorum in any meeting where the matter is under discussion. Further, the following criteria apply to the transaction:

1. the services of goods are provided at a fair price;
2. the terms of the contract are reasonable to the charity;
3. the contract is for the charity's, not the associated person's benefit; and
4. the charity could not have obtained a more advantageous arrangement with reasonable effort.

A self-dealing transaction includes, but is not limited to:

1. sales or exchanges of property;
2. leases;
3. loans;
4. the provision of goods, services, or facilities, and
5. any use of the organization's income or assets that constitutes a material financial interest of an associated person.

In addition to a written policy and procedure governing conflicts and self-dealing, a Board should ask a simple question when confronted with these situations: Would a reasonable, objective, and fair-minded individual find the conduct or transaction improper?

Comment on Disclosure:

The best protection against conflicts or abusive self-dealing is complete and accurate disclosure. Accordingly, any potential conflict should be disclosed to the Board and made a matter of record in the minutes of the Board through an annual procedure. When a potential conflict arises between annual notification dates, the situation should be reported to the Board and recorded in the minutes of the

Board. Where appropriate, disclosure should be made to donors and prospective donors of any relationship that poses, or appears to pose, a possible conflict of interest.

Where a conflict of interest or self-dealing transaction has occurred, full disclosure is mandatory. Disclosure to the Board should include the nature of the relationship involved, a description of the transaction (including non-monetary transactions), and the dollar amount of the transaction. The Board is required to take whatever action is necessary to protect the charity and its assets.

VI. Effectiveness Through Diversity

STANDARD #14

A charity has a policy and procedure to cause the nomination and appointment to the Board of persons who reflect the diversity of the client population served.

Comment:

Factual data on the ethnic and cultural diversity of the client population should be developed and presented to the Board. When these data are compared with the existing Board, a need for diversification will become evident.

The Board itself should be large enough to accommodate diversity. A change in the by-laws may be required to achieve this objective.

STANDARD #15

A charity has a policy and procedure to cause the employment of a staff that reflects the diversity of the client population served.

Comment:

When a factual data on the diversity of the client population is compared with the existing staff, a need for diversification will become evident.

Both standards #14 and #15 describe a process for diversification as opposed to diversification itself. While diversification is the goal, measurable progress is the more immediate objective.

STANDARD #16

A charity has an outreach program through which unserved or underserved segments of the population are contacted.

Comment:

Oftentimes ethnic or cultural groups within a charity's geographic service area do not participate in the charity's service programs. Where this exists, a charity needs an outreach program. One suggested device is the establishment of a network of agencies, among which are included other agencies that have penetrated the unserved or underserved population. These agencies can provide access for the charity to the target population. As one example, a network that includes ethnic media representatives can be developed. Staff jobs and services provided can be promulgated with the aid of these ethnic media representatives.

STANDARD #17

A charity provides training to its Board, staff, and volunteers on the social, psychological, and cultural implications of diversity in three areas: (a) serving a client population; (b) serving as volunteers on boards and committees; and (c) working together as staff.

Comment:

Various cultural and ethnic groups have differing values and styles of behavior as they relate to working together and seeking charitable services. Board members, volunteers, and staff should have a working knowledge of these value and behavioral differences in order to be most effective.

VII. Fund-Raising

STANDARD #18

The raising of funds by a charity is the responsibility of its Board and is accomplished by its members with the support of development staff.

Comment:

Paid development staff or fund-raising counsel supplement and never supplant volunteer fund-raising. When paid fund-raisers are used, bonuses, commissions, or percentages are to be avoided.

STANDARD #18a

The raising of funds by a charity is the responsibility of its Board and is accomplished by its members with the support of the development staff.

Comment: Paid development staff or fund-raising counsel supplement and never supplant volunteer fund-raising.

STANDARD #18B

The Board should retain fund-raisers for a salary or fee.

COMMENT: Percentage-based compensation or a commission may serve the financial self-interest of the fund-raiser at the expense of the charity.

STANDARD #19

All fund-raising statements, both written and oral, are direct, concise, complete, and true.

Comment:

“True” also means that the statements are not unrealistic, deceptive, misleading, or sensational.

STANDARD #20

The Board and chief staff person monitor and minimize fund-raising costs.

Comment on General Appeals:

General appeals have a proper place in a total development program. Direct mail or telephone solicitation can be expensive, however, leaving a small percentage for the charitable cause promoted in the solicitation.

Thus a general appeal should be considered as but one part of the development program and should be viewed as a multi-year donor development project.

Where a general appeal serves a legitimate public educational purpose, the functionalization of costs must be controlled carefully by the Board and chief staff person. (See AICPA Statement of Position 87-2, cited in the comments under Standard #11 above.)

Comment on Special Events:

Special event fund-raising frequently serves multiple purposes, including recognition of volunteers and donors, promulgation of information, entertainment, tradition, etc. Unless carefully planned, implemented, and evaluated, these events can become quite costly.

Comment on Planned Giving:

Where a charity conducts a planned giving program, donor privacy and confidentiality of records involve separate but interrelated ethical requirements; i.e., to respect donor privacy and to keep donor file information confidential. The

“golden rule” is a serviceable standard that a Board can employ in the review and approval of a planned giving procedure. The question for each Board member then becomes: “Would I object if I were subjected to this planned giving program (a) as a prospective donor and (b) as a donor?”

As part of a planned giving program, the Board should have a procedure to receive, acknowledge, and respect a restricted gift.

A planned giving program should include a procedural mechanism that ensures that the prospective donor understands (1) how the gift will be used; (2) all fees and costs associated with the gift, including financial remuneration afforded to financial service professionals who may be involved in soliciting the gift; (3) all financial considerations involving the donor’s family and taxes; (4) valuation, if applicable; and (5) various ways of making the gift, if applicable.

The recent industry-wide controversy surrounding “finder’s fees” associated with large gifts can be resolved by a Board’s adoption of three simple propositions:

1. a fee charged should be reasonable;
2. a fee charged should be for actual services rendered; and
3. the person for whom the services are provided should pay the fee.

Comment on Specific Fund-Raising Costs:

The Charitable Services Section keeps data on thousands of fund-raising events and campaigns conducted each year. Fund-raising costs for these events and campaigns are summarized and available by contacting the Section at 200 North Spring Street, Room 1513, Los Angeles, CA 90012; (213) 978-1144.

STANDARD #21

No charity or fund-raising umbrella group shall engage in or permit others to engage in solicitation activities of a coercive nature. The Board has a written policy that prohibits such coercion.

Comment:

This standard is designed to avoid a problem associated with overzealous fund-raisers both within and outside the charity who have influence and power over subordinates. Unless prohibited from doing so, these fund-raisers may adopt coercive tactics that erode the spirit and intent of philanthropic giving. A coercive tactic is anything that conveys the sense that giving is a condition of employment relating to appointment, transfer, assignment, promotion, training, career advancement, or pay.

VIII. Donor Bill of Rights

STANDARD #22 (Organization and Management)

The donor has the right to expect that the agency for which monies are being solicited:

- 1. is properly organized as a charity;**
- 2. is exempt from taxation;**
- 3. is controlled by a Board of Directors that exercises independent judgment in overseeing its affairs;**
- 4. keeps accurate financial records and is audited annually; and**
- 5. has implemented the charitable service program to which donated funds will be applied.**

STANDARD #23 (Content of the Actual Solicitation)

The donor has the right to:

- 1. know that the material used or statements made in the solicitation are complete and true;**
- 2. know the relationships of the solicitor to the charity (e.g., paid outside solicitor, paid employee, volunteer, etc.);**
- 3. know the fair market value of anything given to the donor as an inducement to contribute or participate (i.e. any and all information needed to help the donor file correct tax returns);**
- 4. know exactly how a donation will be spent (including the amount of the donation that will be applied to a charitable service program);**
- 5. an immediate response from the charity's management to any question or inquiry regarding the charity, its solicitation, or the use of the donated monies;**
- 6. information that would allow a donor to verify solicitation claims (e.g., information on how to visit program sites and talk with program managers);**
- 7. information that would allow the donor to designate funds for a specific charitable service program; and**

- 8. full disclosure of the conditions that apply to a designated contribution, including all solicitations made by fund-raising umbrella groups that promote donor-designated giving.**