

Testimony of H. Art Taylor, President & CEO
BBB Wise Giving Alliance, 4200 Wilson Boulevard, Arlington, VA 22203
before the
COMMITTEE ON FINANCE, UNITED STATES SENATE
on
Charity Oversight and Reform:
Keeping Bad Things from Happening to Good Charities
June 22, 2004

Mr. Chairman and Members of the Committee, I am Art Taylor, President and CEO of the BBB Wise Giving Alliance. I appreciate the opportunity to appear before this Committee to share with you our perspective on charity accountability.

At the outset, I want to stress that our aims, as a nonprofit organization, both resemble and differ from those of government. An objective we share is the fostering of ethical conduct. Both of us work toward that end through activities designed to educate charities about good governance and fund raising practices. While government seeks to identify and prosecute fraud, abuse of tax-exempt status, and financial improprieties in the charitable sector, the BBB Wise Giving Alliance works to help donors make informed judgments, based on ethical and other considerations, about the charities that seek their support. I believe the distinct characteristics of a charity monitoring program will become more evident as I describe our work—and the imminent expansions of our capacity.

The BBB Wise Giving Alliance (the Alliance) is a monitoring organization that sets voluntary accountability standards for charities. We are a charitable affiliate of the Council of Better Business Bureaus (CBBB), formed three years ago through a merger of the National Charities Information Bureau and the CBBB Foundation's Philanthropic Advisory Service. Our mission is to help donors make informed giving decisions. Between the two merger partners, we have more experience—over 100 years—in reviewing and reporting on charities than any other charity monitoring service in the nation.

Our national scope, the breadth of our standards, the public availability of our evaluations, and our practice of identifying organizations that do not meet our standards, as well as those that do, have together given the Alliance a distinctive reputation. Our association with the Better Business Bureau, a name familiar to virtually the entire public, lends it high credibility. We have extensive contact with the public through our website, www.give.org. Over 2 million people visited our website in 2003 to access our charity reports. The Alliance also reaches out to the public and charity community through its everyday work with media and through participation in major national charity conferences.

Assessing and Serving Donor Needs

The donor is our primary constituent. The generosity of American donors is well known. How seriously they take giving, and the problems they have in making choices are perhaps less familiar. In 2001, the Alliance commissioned Princeton Survey Research Associates International to conduct a major donor expectations survey, the results of which are available on the www.give.org website. Among the key findings:

- 70% of respondents say it is difficult to know whether a charity is legitimate;
- 44% say it is difficult to find the information they want in making a giving decision;
- 50% say they would be “very likely” to get information they wanted from the charity itself, although only 50% think that the charities provide enough information about their activities to help them decide about giving;

Clearly, donors are not sure what information they need or where they should get it, or in some cases, how to assess the information they have. They are looking for help in finding accountable charities. The Alliance dedicates itself to providing that help, primarily through evaluations of individual national charities based on our recently revised voluntary *Standards for Charity Accountability*. Developed over three years in an open process involving leaders from national and local charities, the accounting profession, grant-making foundations, research organizations and the Better Business Bureau system, with input from the public as well, the present *Standards* encompass not only how a charity spends its money, but its governance, fund raising practices, and solicitations and informational materials.

- The Alliance produces reports on national charities that specify whether or not an organization meets or does not meet the *Standards for Charity Accountability*.
- Our reports do not rank or grade charities but rather seek to assist donors in making informed judgments about charities soliciting their support.
- In addition, the Alliance goes beyond standards to issue special alerts and advisories for individuals on topics related to giving. These include tips on donating cars, as well as tips on charity telemarketing, police and firefighter appeals, and charitable responses to disasters.

Standards for Charity Accountability

The *Standards for Charity Accountability* (see attachment for full text) address four major areas:

Governance and Oversight: This section seeks to ensure that the volunteer board is active, independent and free of self-dealing.

Measuring Effectiveness: This section seeks to ensure that the organization has defined, measurable goals and objectives in place and a defined process in place to evaluate the success and impact of its program(s).

Finances: This section seeks to ensure that the charity spends its funds honestly, prudently and in accordance with statements made in fund raising appeals.

Fund Raising and Informational Materials: This section seeks to ensure that a charity's representations to the public are accurate, complete and respectful.

The Alliance's Charity Reporting Process

To illustrate the nature of our charity evaluations, I think it helpful to describe briefly the contents of the Alliance's reports and key points in the reporting process.

From a national charity being evaluated, the Alliance requests, among other things:

- annual financial statements
- annual report
- articles of incorporation
- board roster
- budget
- bylaws
- cause-related marketing promotions
- conflict of interest policy
- fund raising contracts
- IRS Form 990 (if applicable)
- scripts of telephone appeals
- solicitation materials
- tax-exempt status determination letter

Providing this information to the Alliance is voluntary on the part of charities, but 80% of the organizations that we ask for information provide it.

Alliance staff review this material in relation to the Alliance's charity standards to determine whether the organization meets or does not meet each standard. In some cases, the Alliance finds that the charity either did not provide all the requested information or that the information provided was not sufficient to reach a conclusion on the cited standard.

Results of National Charity Evaluations

Keeping in mind that approximately 68% of the organizations we report on meet all our standards, let me highlight some of the problem areas we see.

Of all instances of charity noncompliance summarized in the current edition of our *Better Business Bureau Wise Giving Guide* magazine:

53% relate to financial matters, including ways in which charities report or present their finances. The prevalence of problems in this area correlates with donors' focus on financial matters as their primary concern.

29% relate to the public's access to basic facts about the charity's programs, finances and/or fund raising.

18% relate to some area of governance, such as the oversight responsibilities of the charity's governing board.

The Alliance's reports not only state whether or not the subject charity meets the *Standards*, but also include information on program service activities, fund raising practices, governance, executive compensation, sources of funds, and how the organization spends its money. Organizations under review are sent the preliminary report and have an opportunity to respond to the Alliance's draft conclusions.

The Alliance reports whether a charity meets or does not meet the referenced standards. It does not comment on a charity's worthiness or approve or disapprove of any cause. Our aim is not to direct or inhibit donor choice but to provide facts, measured against widely accepted standards, that can inform that choice. Our evaluation results are available directly through all 120 local Better Business Bureaus in the United States and on our website, www.give.org. As a service to individual donors across the country, we also issue a quarterly magazine, the *Better Business Bureau Wise Giving Guide* that summarizes our evaluation findings and reports on other topics of interest to charity contributors.

The Alliance Introduces a New Charity Reporting and Evaluation System

The Alliance will shortly announce an important innovation in its reporting program, an *online* charity reporting and evaluation system.

This innovation is the Alliance's response to a rapidly changing charitable environment. Over 900,000 organizations have received charitable tax-exempt status; about 250,000 of them file either the IRS Form 990 or 990-EZ. Donors and potential donors want ready access to information that will help them learn which of the vast number of charities that solicit them are responsible, accountable, and well-governed. The Alliance's new reporting and evaluation system will produce that information on a greatly expanded scale. Currently we report on hundreds of national charities; our goal is report on thousands.

The new system will enable participating charities to submit information directly online. A computer program will, based on criteria of the BBB Wise Giving Alliance,

automatically evaluate the information, making an initial assessment as to whether the subject charity meets or does not meet the *20 Standards for Charity Accountability*.

This new reporting system also will alert us to problem areas that require individual scrutiny and possibly further clarification from the reporting charity. Staff will also review portions of information reported online against basic documents such as financial statements, the IRS Form 990, and annual report. We expect that the efficiencies created by the system will vastly expand our coverage of national charities and facilitate both the filing and the analysis of information so that we can provide information about more charities to donors more quickly.

To launch this online reporting and evaluation system, the Alliance will hold an event on July 13, 2004 at the National Press Club in Washington, DC. Media representatives, including those well acquainted with charity issues, will be able to see a demonstration of the system. Shortly afterwards, national charities will also be able to review the system through a web cast. We want to reach national charities across the country and acquaint them with this new evaluation tool.

In addition, this system will be shared with local Better Business Bureaus nationwide to assist them in reporting on local and regional charitable organizations. Through this expanded effort, we intend that national and local BBB charity reporting will become the primary accountability resource for the donating public.

BBB Wise Giving Alliance National Charity Seal

To call additional public attention to charities that meet the Alliance standards, we have also recently developed a national charity seal. National charities that meet the *Standards for Charity Accountability* may now apply to display this BBB Wise Giving Alliance seal. By signing a licensing agreement and paying an annual fee to help support this program, they are authorized to show the seal in their solicitation materials, on their website and in other authorized venues. A number of local Better Business Bureaus are beginning to offer participation in the seal program to local charities that have met the same standards.

The seal informs the public instantly that the charity using it meets the Alliance's standards, but it has other important functions, too. It gives participating charities a means to increase donor confidence and strengthen public trust; it extends public awareness of the Alliance's work in charity accountability, and it helps draw attention to the fact that charities are actively addressing issues, income some *beyond what government regulations require*—and this is what our standards are about.

The Voluntary Approach to Accountability

This description of the work of the Alliance suggests some valuable assets of voluntary organizations that focus on strengthening the charitable sector. One is flexibility, the ability to re-visit standards, to establish new criteria or re-define former ones as

circumstances change. Voluntary standards also offer elasticity, being broad enough to take into account the multiple creative and productive ways in which charities operate.

Sometimes voluntary standards do what the law explicitly cannot do. Notably, a voluntary monitoring organization can have a standard that calls for fund raising expenses not to exceed a certain threshold. By contrast, several U.S. Supreme Court decisions do not allow the states to set across-the-board fund raising cost restrictions for charities.

On the whole, the high level of compliance we find in the charities we evaluate suggests that disregard of accountability is by no means rampant. We are well aware, however, that there are problems within the sector. And we expect that scandals are going to gain increased attention as the number of charities continues to grow and government action is limited by inadequate resources.

We are proud of our work but also know that we alone cannot deal with persistent problems in the charitable sector. Other organizations have also recognized the needs for betterment. Charities have become increasingly sensitive about responsiveness to their donors. We have seen the growth of nonprofit organizations formed to make information available to donors. Philanthropic Research, Inc. (commonly known as Guidestar), for example, provides the IRS Form 990 and other information at its website, enabling donors and others to access important charity facts. And we have seen organizations develop programs to help charities demonstrate their accountability and commitment to ethical behavior. Both the Evangelical Council for Financial Accountability (ECFA) and the Maryland Association of Nonprofit Organizations offer their own charity seals based on comprehensive standards. The National Committee for Responsive Philanthropy encourages greater philanthropic openness and engages in other activities important to the infrastructure of the nonprofit sector.

Government and Charity Monitoring

There is no question that governmental agencies have vital roles in assuring that charities merit the special advantages given them by law. In particular, that role is to fight fraud and abuse of tax-exempt status. The IRS Form 990 and the requirement that organizations make it available are extremely important in that effort. IRS has begun implementing regulations addressing excessive compensation and private inurement.

Only on rare occasions does the Alliance involve itself in governmental action: we presented an *amicus* brief in the recent case of *Madigan v. Telemarketing Associates* before the U.S. Supreme Court because we believed the voice of donors needed to be considered. The case involved a subject very close to donors—what telemarketers say and sometimes don't say when they solicit contributions. The U.S. Supreme Court, reversing an earlier decision of the Illinois Supreme Court, held that States have the right to bring fraud actions “when fundraisers make false or misleading representations designed to deceive donors about how their donations will be used.”

The Alliance is supportive of several possible government actions that have been suggested:

- Efforts to increase accuracy and completeness of the IRS Form 990;
- Additional funds for the Tax-Exempt and Government Entities Division of the IRS and the state regulatory offices, to increase their ability to address concerns about charities;
- Federal government fees received with applications for tax-exempt status as well as excise taxes paid by private foundations could serve as sources of funds for both government and private efforts to strengthen the charitable sector;
- Government encouragement of private foundation funding of efforts to strengthen the overall infrastructure of the charitable sector. This could include efforts designed to address, among other things, nonprofit management, accountability, governance, and effectiveness.
- Government encouragement of charities to participate in various available accountability programs.

In our view, the latitude of operation granted to charity in America is fundamental to its strength. I am convinced that the giving public prizes the voluntary nature of charity and the variety and creativity that voluntarism fosters. I believe that what donors want to see is that charities are ready, voluntarily, to show their commitment to openness and ethical conduct and to demonstrate that their efforts are sharply focused on their missions.

Donors should be wary about giving their support to a charity that simply attests that it obeys the law.

Inevitably, donors' choices will sometimes benefit less effective and/or poorly managed charities. Charities must be helped to understand and observe standards of accountability so that they can earn the support of donors—individual and institutional—who are also acquainted with those standards and insist upon adherence to them.

We realize that there is an interest in strengthening both federal and state oversight of charitable activities. We agree that there are concerns that government needs to address. We also believe that there is an essential and complementary role for voluntary charity monitoring, a role in promoting good practices that go beyond what government should seek to regulate.

We can say with assurance that whatever steps government decides to take, the Alliance will continue and expand its work at the front line of accountability, promoting openness and ethical conduct throughout the charitable sector and providing a way for charities to demonstrate their adherence to accountability standards that go beyond the law.

BBB WISE GIVING ALLIANCE STANDARDS FOR CHARITY ACCOUNTABILITY

PREFACE

The BBB Wise Giving Alliance *Standards for Charity Accountability* were developed to assist donors in making sound giving decisions and to foster public confidence in charitable organizations. The standards seek to encourage fair and honest solicitation practices, to promote ethical conduct by charitable organizations and to advance support of philanthropy.

These standards replace the separate standards of the National Charities Information Bureau and the Council of Better Business Bureaus' Foundation and its Philanthropic Advisory Service that were in place at the time the organizations merged.

The *Standards for Charity Accountability* were developed with professional and technical assistance from representatives of small and large charitable organizations, the accounting profession, grant making foundations, corporate contributions officers, regulatory agencies, research organizations and the Better Business Bureau system. The BBB Wise Giving Alliance also commissioned significant independent research on donor expectations to ensure that the views of the general public were reflected in the standards.

The generous support of the Charles Stewart Mott Foundation, the Surdna Foundation and Sony Corporation of America helped underwrite the development of these standards and related research.

Organizations that comply with these accountability standards have provided documentation that they meet basic standards:

- ♦ In how they govern their organization,
- ♦ In the ways they spend their money,
- ♦ In the truthfulness of their representations, and
- ♦ In their willingness to disclose basic information to the public.

These standards apply to publicly soliciting organizations that are tax exempt under section 501(c)(3) of the Internal Revenue Code and to other organizations conducting charitable solicitations. The standards are not intended to apply to private foundations, as they do not solicit contributions from the public.

The overarching principle of the BBB Wise Giving Alliance *Standards for Charity Accountability* is full disclosure to donors and potential donors at the time of solicitation and thereafter. However, where indicated, the standards recommend ethical practices beyond the act of disclosure in order to ensure public confidence and encourage giving. As voluntary standards, they also go beyond the requirements of local, state and federal laws and regulations.

In addition to the specific areas addressed in the standards, the BBB Wise Giving Alliance encourages charitable organizations to adopt the following management practices to further the cause of charitable accountability.

- ♦ Initiate a policy promoting pluralism and diversity within the organization's board, staff and constituencies. While organizations vary widely in their ability to demonstrate pluralism and diversity, every organization should establish a policy, consistent with its mission statement, that fosters such inclusiveness.
- ♦ Ensure adherence to all applicable local, state and federal laws and regulations including submission of financial information.
- ♦ Maintain an organizational adherence to the specific standards cited below. The BBB Wise Giving Alliance also encourages charities to maintain an organizational commitment to accountability that transcends specific standards and places a priority on openness and ethical behavior in the charity's programs and activities.

GOVERNANCE AND OVERSIGHT

The governing board has the ultimate oversight authority for any charitable organization. This section of the standards seeks to ensure that the volunteer board is active, independent and free of self-dealing. To meet these standards, the organization shall have:

1. A board of directors that provides adequate oversight of the charity's operations and its staff. Indication of adequate oversight includes, but is not limited to, regularly scheduled appraisals of the CEO's performance, evidence of disbursement controls such as board approval of the budget and fund raising practices, establishment of a conflict of interest policy and establishment of accounting procedures sufficient to safeguard charity finances.

2. A board of directors with a minimum of five voting members.

3. A minimum of three evenly spaced meetings per year of the full governing body with a majority in attendance, with face-to-face participation. A conference call of the full board can substitute for one of the three meetings of the governing body. For all meetings, alternative modes of participation are acceptable for those with physical disabilities.

4. Not more than one or 10% (whichever is greater) directly or indirectly compensated person(s) serving as voting member(s) of the board. Compensated members shall not serve as the board's chair or treasurer.

5. No transaction(s) in which any board or staff members have material conflicting interests with the charity resulting from any relationship or business affiliation.

Factors that will be considered when concluding whether or not a related party transaction constitutes a conflict of interest and if such a conflict is material, include, but are not limited to: any arm's length procedures established by the charity; the size of the transaction relative to like expenses of the charity; whether the interested party participated in the board vote on the transaction; if competitive bids were sought and whether the transaction is one-time, recurring or ongoing.

MEASURING EFFECTIVENESS

An organization should regularly assess its effectiveness in achieving its mission. This section seeks to ensure that an organization has defined, measurable goals and objectives in place and a defined process in place to evaluate the success and impact of its program(s) in fulfilling the goals and objectives of the organization and that also identifies ways to address any deficiencies. To meet these standards, a charitable organization shall:

6. Have a board policy of assessing, no less than every two years, the organization's performance and effectiveness and of determining future actions required to achieve its mission.

7. Submit to the organization's governing body, for its approval, a written report that outlines the results of the aforementioned performance and effectiveness assessment and recommendations for future actions.

FINANCES

This section of the standards seeks to ensure that the charity spends its funds honestly, prudently and in accordance with statements made in fund raising appeals. To meet these standards, the charitable organization shall:

Please note that standards 8 and 9 have different denominators.

8. Spend at least 65% of its total expenses on program activities.

Formula for Standard 8:

$$\frac{\text{Total Program Service Expenses}}{\text{Total Expenses}} \text{ should be at least } 65\%$$

9. Spend no more than 35% of related contributions on fund raising. Related contributions include donations, legacies and other gifts received as a result of fund raising efforts.

Formula for Standard 9:

$$\frac{\text{Total Fund Raising Expenses}}{\text{Total Related Contributions}} \text{ should be no more than } 35\%$$

10. Avoid accumulating funds that could be used for current program activities. To meet this standard, the charity's unrestricted net assets available for use should not be more than three times the size of the past year's expenses or three times the size of the current year's budget, whichever is higher.

An organization that does not meet Standards 8, 9 and/or 10 may provide evidence to demonstrate that its use of funds is reasonable. The higher fund raising and administrative costs of a newly created organization, donor restrictions on the use of funds, exceptional bequests, a stigma associated with a cause and environmental or political events beyond an organization's control are among factors which may result in expenditures that are reasonable although they do not meet the financial measures cited in these standards.

11. Make available to all, on request, complete annual financial statements prepared in accordance with generally accepted accounting principles.

When total annual gross income exceeds \$250,000, these statements should be audited in accordance with generally accepted auditing standards. For charities whose annual gross income is less than \$250,000, a review by a certified public accountant is sufficient to meet this standard. For charities whose annual gross income is less than \$100,000, an internally produced, complete financial statement is sufficient to meet this standard.

12. Include in the financial statements a breakdown of expenses (e.g., salaries, travel, postage, etc.) that shows what portion of these expenses was allocated to program, fund raising and administrative activities.

If the charity has more than one major program category, the schedule should provide a breakdown for each category.

13. Accurately report the charity's expenses, including any joint cost allocations, in its financial statements.

For example, audited or unaudited statements which inaccurately claim zero fund raising expenses or otherwise understate the amount a charity spends on fund raising, and/or overstate the amount it spends on programs will not meet this standard.

14. Have a board-approved annual budget for its current fiscal year, outlining projected expenses for major program activities, fund raising and administration.

**FUND RAISING AND
INFORMATIONAL MATERIALS**

A fund raising appeal is often the only contact a donor has with a charity and may be the sole impetus for giving. This section of the standards seeks to ensure that a charity's representations to the public are accurate, complete and respectful. To meet these standards, the charitable organization shall:

15. Have solicitations and informational materials, distributed by any means, that are accurate, truthful and not misleading, both in whole and in part. Appeals that omit a clear description of program(s) for which contributions are sought will not meet this standard.

A charity should also be able to substantiate that the timing and nature of its expenditures are in accordance with what is stated, expressed or implied in the charity's solicitations.

16. Have an annual report available to all, on request, that includes:

- (a) the organization's mission statement,
- (b) a summary of the past year's program service accomplishments,
- (c) a roster of the officers and members of the board of directors,

(d) financial information that includes:

- (i) total income in the past fiscal year,
- (ii) expenses in the same program, fund raising and administrative categories as in the financial statements, and
- (iii) ending net assets.

17. Include on any charity websites that solicit contributions, the same information that is recommended for annual reports, as well as the mailing address of the charity and electronic access to its most recent IRS Form 990.

18. Address privacy concerns of donors by
(a) providing in written appeals, at least annually, a means (e.g., such as a check off box) for both new and continuing donors to inform the charity if they do not want their name and address shared outside the organization, and

(b) providing a clear, prominent and easily accessible privacy policy on any of its websites that tells visitors

- (i) what information, if any, is being collected about them by the charity and how this information will be used,
- (ii) how to contact the charity to review personal information collected and request corrections,
- (iii) how to inform the charity (e.g., a check off box) that the visitor does not wish his/her personal information to be shared outside the organization, and
- (iv) what security measures the charity has in place to protect personal information.

19. Clearly disclose how the charity benefits from the sale of products or services (i.e., cause-related marketing) that state or imply that a charity will benefit from a consumer sale or transaction. Such promotions should disclose, at the point of solicitation:

- (a) the actual or anticipated portion of the purchase price that will benefit the charity (e.g., 5 cents will be contributed to abc charity for every xyz company product sold),
- (b) the duration of the campaign (e.g., the month of October),
- (c) any maximum or guaranteed minimum contribution amount (e.g., up to a maximum of \$200,000).

20. Respond promptly to and act on complaints brought to its attention by the BBB Wise Giving Alliance and/or local Better Business Bureaus about fund raising practices, privacy policy violations and/or other issues.