

Board Governance eLearning Outline

Introduction

- Purpose of module
 - Welcome to the “Good Governance” module of the Secretary of State’s Nonprofit Board Education eLearning course.
 - The purpose of this course is to cover some basic governance principles that you, as a current or future board member, can use to improve your organization’s efficacy and efficiency. Good governance is not solely a set of specific practices, but more importantly the concept reflects an attitude of responsibility and accountability by nonprofit boards.
- Overview
 - The content in this course is divided into six topics, each of which will cover an important aspect of nonprofit governance
 - This course is meant only as an introductory look at governance issues, and one of our hopes is that taking the course will inspire you to examine more in-depth resources available to nonprofit boards. Colorado nonprofits are fortunate to have several resources available on the subject of good governance practices, including notably the Colorado Nonprofit Association’s “[Principles and Practices for Nonprofit Excellence](#)” and the “[Guide for Colorado Nonprofit Organizations](#),” published by CLE in Colorado, Inc., and affiliate of the [Colorado Bar Association](#).
 - Keep in mind that each nonprofit is different, and that there is no such thing as “one size fits all” advice. For example, Colorado nonprofit corporations can have, but are not required to have, members, and members can have voting rights or no-voting rights. It’s important to know the difference, because different governance responsibilities attached depending on that.

1. Legal Compliance and Public Disclosure

- Ensuring that your nonprofit complies with all applicable federal and state laws and regulations is one of the board’s most fundamental obligations and is often referred to as a director’s duty of obedience. Nonprofits should foster a culture of transparency and be prepared to regularly and openly provide information about mission, activities, accomplishments, and decision-making processes. (For more information on the fiduciary duties of directors, please see the eLearning topic on Fiduciary Duties of Nonprofit Directors.)
- Be active in requesting updates on legal issues facing the organization, and regularly seek out educational opportunities to stay current on legal compliance matters.
- Laws and Regulations - the board needs to be familiar with the legal and regulatory framework that applies to nonprofits. The following examples are common legal and regulatory requirements that every board should be aware of, but they do not constitute a comprehensive list:
 - **Registration and Filings**
 - Most nonprofit tax-exempt organizations ¹must file a Form 990-N, 990-EZ, 990 or 990-PF with the IRS annually, though there are some exceptions for certain religious organizations, governmental organizations. This includes very small organizations with gross revenue under \$5,000 that are tax-exempt under IRC §501(c)(3), even though they are not required to file a Form 1023 to apply for tax-exempt status. If a nonprofit is required to file a Form 990 series annual return but fails to do so for three consecutive years, its tax exemption will be revoked automatically. This in turn will require the organization to re-apply for tax-exempt status (entailing significant labor, application fees, and lengthy delays), or may even result in the organization being taxed as a for-profit corporation.
 - Please be aware that in addition to the requirement to file one of the Form 990 series annual information returns, there is an entire body of federal law applicable to tax-exempt nonprofits, which you can review at <http://www.irs.gov/Charities-&-Non-Profits/Life-Cycle-of-an-Exempt-Organization>
 - All nonprofits that are organized as nonprofit corporations must file a periodic report with the Business Organizations Program.
 - Charitable organizations soliciting contributions in Colorado need to file a registration renewal with the Charities Program. Note that the Colorado Charitable Solicitations Act is fairly broad in defining “charitable organization,” so even non-501(c)(3) organizations that are making charitable appeals can be subject to its requirements.
 - Charitable organizations soliciting contributions on a regional or national basis may need to register in multiple states. Thirty-seven states plus the District of Columbia have a charity registration law.
 - Although most private foundations are exempt from the state registration requirement due to their lack of solicitation of contributions from the general public, U.S. Treasury regulations require

¹ Note that nonprofit status and tax-exempt status are not one and the same; a nonprofit corporation must generally apply to the Internal Revenue Status) for recognition of tax-exempt status.

- them to file copies of their Form 990-PF with the Colorado Attorney General.
- Charitable Gaming. If you wish to conduct bingo games or hold raffles in Colorado, you must have been in existence for at least five years, have a dues-paying membership and be licensed by the [Colorado Secretary of State](#).
 - **Corporate Records.** Colorado nonprofit corporations are required to keep certain corporate records and allow voting members (if any) to inspect these records.ⁱ These records include:
 - Articles of incorporation - a legal document filed with the Secretary of State. Provisions in the articles of incorporation control over any provisions in the bylaws.
 - Bylaws - this is a legal document describing elements of the structure and process of the board of directors and membership (if any) that are not covered in the articles of incorporation. Organizations are not required to file their bylaws with the Secretary of State, but they may attach them to the articles of incorporation if they choose to.
 - Appropriate accounting records, including financial statements prepared for periods ending during the last three years, showing in reasonable detail its assets and liabilities and results of its operations.
 - Minutes of all meetings of the board of directors.
 - A record of all actions taken by the board of directors without a meeting.
 - A record of all actions taken by a board committee in place of the board of directors on behalf of the nonprofit corporation.
 - A record of all waivers of notices of meetings of members(if any) and of the board of directors or any committee of the board of directors.
 - A list of the name and address of all members (if any) in alphabetical order, by class, showing the number of votes to which each member is entitled
 - Copies of resolutions adopted by its board of directors relating to the qualifications and rights of its members or any category of members (if any).
 - Minutes of all meetings, of members (if any) and records of all action taken by members without a meeting, for the past three years
 - Copies of all written communications within the past three years to members generally as members (if any).
 - A list of the names and business or home addresses of its current directors and officers.
 - A copy of its most recent periodic report filed with Colorado Secretary of State.
 - **Required Public Disclosures.** The Internal Revenue Code also requires nonprofit tax-exempt organizations to make their tax-exemption determination letter, their application for tax-exempt status (IRS Form 1023 or 1024,) and their 990 returns (including 990-T) for the most recent three years available to the public for inspection upon request. Note that the application for tax-exempt status includes not only the Form 1023 or Form 1024 itself, but any subsequent correspondence to/from the IRS during the application process, as well as any amendments to the application.

- Taxes

- **Employee Withholding Taxes.** As an employer, the organization is responsible for withholding certain taxes from employees' pay checks. Employment taxes include the following: Federal income tax withholding (FITW), Social Security and Medicare taxes (FICA), Federal unemployment taxes (FUTA). More information on this topic is available on the IRS website at <http://www.irs.gov/Charities-&-Non-Profits/Employment-Taxes-for-Exempt-Organizations>. See in particular IRS Publication 15 (2013), (Circular E), "Employer's Tax Guide," and IRS Publication 15A, "Employer's Supplemental Tax Guide." In addition, the organization should consult the Colorado Department of Revenue's website for information about Colorado wage withholding tax requirements.
- **Federal Income Taxes.** Organizations that are exempt from federal income tax under 501(c) nonetheless must pay federal income tax on unrelated business taxable income ("UBTI"), and file Form 990-T to do so. Organizations with UBTI should not forget about their obligation to make estimated tax payments.
- **State Income Taxes.** Colorado tax-exempt status piggy-backs on federal tax-exempt status, so a nonprofit organization that is tax-exempt under section 501(c) is not required to file a Colorado corporation income tax return, unless it has UBTI. If a nonprofit corporation does have UBTI during the tax year, it needs to file Form 112, "Corporation Income Tax Return" with the Colorado Department of Revenue and pay tax. Nonprofits with UBTI are also required to file Form 990-T with the IRS state income.
- **State Sales Tax Exemption and State Sales Tax ID Number.** Colorado provides an exemption for 501(c)(3) charitable organizations from state-collected sales and use tax for purchases made while conducting regular charitable functions and activities. This exemption does not apply to locally collected sales and use tax levied by home rule cities. Home rule jurisdictions make their own tax regulations, so you need to contact them directly for information. File an application for a Colorado Sales Tax Withholding Account (Form CR0100) with the Colorado Department of Revenue. Note: while 501(c)(3) organizations may be exempt from paying sales tax, they may still be required to collect sales tax from their customers.
- **State Sales Tax License.** Nonprofits that sell goods and services are generally required to obtain a sales tax license from state and/or local taxing jurisdictions and collect any applicable sales taxes. The state and some local taxing jurisdictions exempt "occasional sales" with specific limits on revenue generated and the number of days per year that sales can occur. Contact the Department of Revenue and local taxing jurisdictions for more information.
- **Property Tax Exemption.** Certain properties that are owned and used for religious, charitable, and private school purposes are exempt from property taxations. Property owners can apply for a property tax

exemption with the Colorado Department of Local Affairs - Division of Property Taxation - Exemptions Section. Currently, exempt property owners are required to pay a filing fee and file annual reports online with the Division of Property Taxation to maintain this property tax exemption.

- **Insurance**

- **Unemployment Insurance.** Nonprofit and charitable organizations are covered by the Colorado Employment Security Act (ESA) if they have four or more employees for some portion of a day in each of 20 different weeks within the current or preceding calendar year. This program is administered by the Division of Employment and Training of the Colorado Department of Labor and Employment. Nonprofit organizations are not required to carry unemployment insurance, but they can (and can instead reimburse the state for any payments made) they must register if they have four or more employees. Alternatively, elect to apply for an unemployment insurance account with the Colorado Department of Labor and Employment by filing Form UITL-100. The Unemployment Compensation Program is administered by the Division of Employment and Training of the Colorado Department of Labor and Employment.
- **Workers Compensation Insurance.** All public and private employers in Colorado, with limited exceptions, must provide workers' compensation coverage for their employees if one or more full or part-time persons are employed. This includes nonprofit organizations. The state workers' compensation system is administered by the Colorado Department of Labor and Employment - Division of Workers' Compensation. The division publishes several guides to the workers' compensation system; visit their website for more information at <http://www.colorado.gov/cs/Satellite/CDLE-WorkComp/CDLE/1240336932511>.

- **Do-not-call List.** Although there is an exemption in the Colorado No-Call Law and the federal "Do-Not-Call" Provisions of the Telemarketing Sales Rule for charitable organizations, remember that the Federal Trade Commission's Telemarketing Sales Rule (TSR) requires all organizations to place individuals on an internal Do Not Call list upon request.
- **Lobbying and Campaign Activity.** Make sure you understand what federal, state, and local rules apply when your organization engages in lobbying or other forms of advocacy. Under federal law, lobbying activity cannot be more than an insubstantial part of a nonprofit's overall activities and campaign activities are prohibited for partisan all 501(c)(3) organizations. If your organization pays you to lobby, you need to register as a lobbyist with the Colorado Secretary of State's Office. Volunteer lobbyists who receive no more than reimbursement of expenses must register with the clerks of the Colorado House of Representatives and Senate.
- **Paid Solicitors.** If a charity engages a paid solicitor, it should actively oversee and monitor those activities. This includes at a minimum gaining reasonable assurances that its paid solicitor is in full compliance with the Colorado Charitable Solicitations Act (CCSA).

- **Private Foundations and Excise Taxes.** Under both federal and Colorado law, a private foundation (which is a specific type of 501(c)(3) organization) cannot engage in any act of self-dealing, retain any excess business holding, make any jeopardizing investments, nor make any taxable expenditures as defined in section 4945(d) of the Internal Revenue Code. In addition, a private foundation must meet the distribution requirement described in section 4942 of the Internal Revenue Code.ⁱⁱ
- **Colorado Uniform Prudent Management of Institutional Funds Act (UPMIFA).** UPMIFA governs management and investment decisions by charities and provides guidance for those who manage and invest the funds. UPMIFA sets the prudence standards for investment decision making and spells out more of the factors a charity should consider in making management and investment decisions. It requires a charity and those who manage and invest its funds to:
 1. Give primary consideration to donor intent as expressed in a gift instrument,
 2. Act in good faith, with the care an ordinarily prudent person would exercise,
 3. Incur only reasonable costs in investing and managing charitable funds,
 4. Make a reasonable effort to verify relevant facts,
 5. Make decisions about each asset in the context of the portfolio of investments, as part of an overall investment strategy,
 6. Diversify investments unless due to special circumstances, the purposes of the fund are better served without diversification,
 7. Dispose of unsuitable assets, and
 8. In general, develop an investment strategy appropriate for the fund and the charity.

In addition, UPMIFA provides guidelines for endowment spending, allows institutions to address fluctuations in the value of the endowment, and governs the release and modification of donor restrictions.

- **Managing Conflicts of Interest.** A conflict of interest represents a violation of the old adage about serving two masters and implicates a director's or officer's fiduciary duty of loyalty.ⁱⁱⁱ Every organization should have a written conflict of interest policy, so that even the appearance of a conflict of interest within the organization and the board of directors is appropriately managed through disclosure, recusal, or other means. Keep in mind that under Colorado law, it is illegal for the organization to make a loan to its directors or officers. See the module on Fiduciary Duties of Nonprofit Directors for more information on conflicts of interest.
- **Whistleblower Policy.** An organization should have a written whistleblower policy. There should be a system in place to allow individuals to come forward and report financial or other misconduct, including illegal practices or violations of organizational policies. The policy should clearly state that the organization will not retaliate against whistleblowers and will do its best to protect their confidentiality, as long as the report is made in good faith.

- Document Retention and Destruction. The Colorado Revised Nonprofit Corporation Act requires organizations to keep certain types of corporate records, (some permanently) and the Colorado Charitable Solicitations Act requires their paid solicitors to keep records of solicitation campaigns. In addition, organizations should be mindful of other laws and the statutes of limitations in various areas (including federal and state tax law, employment law and tort law, for example) that can create a responsibility (if not a hard-and-fast legal obligation) to keep certain documents for a certain amount of time (or even permanently). A charitable organization should establish policies and procedures to create and preserve the organization's important documents and business records, and specify when to destroy specific types of documents. Be aware that federal and some state laws prohibit the destruction, alteration, mutilation, or concealment of records related to an official legal proceeding, and an organization should provide in its policy that standard destruction practices will be suspended for documents that may be relevant to an actual or potential audit, investigation or lawsuit.
- Protection of Assets. An organization should have a solid plan in place to protect its property, financial and human resources, and program content and materials, as well as its integrity, good will, and reputation against damage or loss.
 - To guard against fraud and embezzlement, an organization should have strong internal accounting controls in place. For example, an organization ought to:
 1. Segregate or separate duties, especially the recording of revenue, receipt of funds, maintenance of accounts receivable records, maintenance of accounts payable records and bank reconciliation;
 2. Train volunteers and staff regarding fraud and the consequences of fraud;
 3. Obtain employee theft insurance;
 4. Have staff or board members other than the treasurer review the monthly financial statements;
 5. Specifically direct the audit committee to detect fraud; and
 6. Require background checks on all employees and volunteers that handle cash and/or accounts payable.
 - The board should ensure that the organization has sufficient general liability, property (if it holds property) and directors' and officers' liability insurance.

2. Governing Body and Management

- The Board and Management and their responsibilities
 - According to Colorado law, all nonprofits corporation must have a board of directors, and must have management consisting of a president (or other senior executive officer), a secretary, and a treasurer.² Colorado law requires only that nonprofits have at least one director, and the same individual may hold more than one office. However, Principles & Practices for Nonprofit Excellence in Colorado recommends at least five board members to ensure proper oversight and ensure that each director can have meaningful participation.
 - The rest of this course will provide plenty of detail on board member responsibilities, but on a very basic level, directors and officers should be concerned with meeting the **duty of loyalty** and **duty of care**. (in addition to the **duty of obedience** mentioned above)
- Availability and review of governing documents
 - As a director, your most important guides are your organization’s articles of incorporation and bylaws, but you should also review any other corporate policies, such as its conflict of interest or whistleblower policies. In addition, be sure to review the organization’s application for tax-exempt status, if any, and its most recent Form 990 returns and financial statements.
 - At the very least, you should be provided with these documents when you become a member of the board.
 - As your organization changes and grows, it is important that directors take the time to re-examine your foundational documents. and other policies The appropriate timeline for review will vary with the nonprofit, but it’s a good idea to do it once a year, if possible, but every two or three years at the very least.³
- Meeting frequency and attendance
 - Ideal meeting frequency will vary depending many factors, such as where your organization is in its lifecycle., whether the board is a working board or fundraising board, whether you have an active committee structure Most nonprofits determine the minimum number of Board meetings in their bylaws or other corporate policy, one reason it is important to review your founding documents and policies often.
 - While there isn’t a “magic number,” the Colorado Nonprofit Association recommends meeting at least every quarter, a common practice in the for-profit sector.⁴
 - So what are the benefits of holding more meetings? A study by the Urban Institute found that the number of meetings per year was positively correlated with higher levels of Board involvement in fundraising and community involvement.⁵
- Board orientation and ongoing training
 - As with any job, effective onboarding and continuous development are key to maintaining a successful board.

² CRS § 7-128-101 and CRS § 7-128-301

³ Principles and Practices, Page 6, Column 1

⁴ Principles and Practices, page 7, column 2

⁵ Urban Institute, Nonprofit Governance in the United States, 2007.

- Many effective boards maintain an updated board manual, which includes governing and planning documents, policies, and an overview of board member responsibilities.⁶
- Succession Planning/Staff transitions - the board should have a process in place to ensure smooth transitions between outgoing and incoming leadership and to train new directors, staff, and volunteers. All too frequently, organizations fail to meet an important obligation because they lacked a comprehensive plan for bringing new officers and key employees on board and equipping them with the knowledge they need to ensure the organization continues to operate effectively and efficiently.
- Colorado has a number of organizations that offer general and customized board training courses, including:
 1. Metro Volunteers (www.metrovolunteers.org)
 2. Community Resource Center (www.crcamerica.org)
 3. Center for Nonprofit Excellence (www.cnecoloradosprings.org)

⁶ Principles and Practices, page 7, column 1

3. Compensation

- **Executive compensation**

- As a nonprofit board member, one of your most important responsibilities is to help recruit and select the organization’s executive leadership—those individuals who manage the nonprofit’s day-to-day operations. Most often, the board will be responsible for selecting the and evaluating the performance of chief executive, but you may also be involved in selecting and evaluating the performance of other executive staff It’s always a good idea to have direct reporting relationship between the board and the senior financial officer of the organization.
- When hiring executive staff, you and your colleagues will need to settle on a compensation package. While Colorado and federal law prohibit nonprofits from providing excessive compensation⁷, neither offers absolute black-and-white rules on what constitutes “reasonable compensation.”
- However, the IRS does provide a process that boards should follow for crafting a compensation package⁸, which allows a 501(c)(3) public charity or 501(c)(4) social welfare organization to establish a rebuttable presumption that compensation is reasonable Though it technically does not apply to other types of tax-exempt organization, it’s a good process for them to follow regardless. :This process requires the following steps
 1. The compensation package should be approved in advance by an independent governing body, which is usually the board or the board’s compensation committee. Importantly, members of this body should recuse themselves if they have a material or perceived conflict of interest (we’ll learn more about conflicts of interest soon).
 2. The independent body should obtain data on compensation for comparable duties or positions, and should rely on this information in making its determination.
 - CAUTION: some boards fall into the trap of using “questionable comparables” to determine executive compensation. This can occur if the board looks for comparable positions at larger entities, organizations in vastly different geographic areas or organizations working in different fields or market segments⁹. To avoid this pitfall, use care in selecting your comparables.
 3. The independent body should adequately document the basis for determination, including the comparables data and analysis, concurrently with making the determination.
- So, you’ve hired your executive team and followed the three-step compensation guidelines. You’re all done, right? Wrong.
- The board of directors should consistently review compensation packages for and evaluating the performance of the chief executive and, where appropriate, other key staff. The Colorado Nonprofit Association recommends that the board conduct an annual performance and compensation review for the chief

⁷ CRS § 7-133-102; IRC §§ 501(c)(3) & 4958

⁸CFR § 53.4958. <http://www.gpo.gov/fdsys/pkg/CFR-2012-title26-vol17/pdf/CFR-2012-title26-vol17-sec53-4958-6.pdf>

⁹ Cotter, Timothy J. “Advising the Executive Compensation Committee: Practical Suggestions for the General Counsel.” 2011.

executive, including an assessment of industry standards. By doing so, you will help ensure that you are offering reasonable, competitive compensation for critical staff over time, and will also protect your organization from liabilities associated with excess compensation.

- **Board compensation**

- In general, nonprofit board members do not receive compensation for their service, although Colorado law does allow for “reasonable” compensation for directors.¹⁰ The federal tax laws also allow for it, though the IRS often frowns on this practice. Principles for Good Governance and Ethical Practice issued by the Panel on the Nonprofit Sector and the Principles and Practices for Nonprofit Excellence in Colorado issued by the Colorado Nonprofit Association both discourage compensation for board members. The Better Business Bureau’s Standards for Charity Accountability recommend that not more than one or 10% (whichever is greater) directly or indirectly compensated person(s) serve as voting member(s) of the board, and that no compensated member serves as the board’s chair or treasurer.
- There are some cases where it may make sense to provide compensation for board members. For Some organizations pay directors a fairly modest stipend, for example, in recognition of the time that directors put in to the organization and to emphasize that they provide much value. Organizations should be mindful, however, when they embark upon this practice that there can be some backlash by funders or watchdog groups.
- Reimbursing directors for board-related expenses is more common, such as expenses related to board meetings and retreats. Ideally, these types of reimbursements are made in accordance with established corporate policy, to ensure they are appropriate and reasonable.

In any case, it is important to remember that compensating board members can mean that the protection of volunteer immunity laws is lost (though this won’t always be the case with respect to expense reimbursement). For more information about the volunteer immunity laws, see the topic on the Fiduciary Duties of Nonprofit Directors.

¹⁰ CRS § 7-133-102(b)

4. Organizational Control

- A board’s ability to guide the organization effectively is dependent, in part, on the policies and structure that the board puts in place to manage and protect itself, often referred to as organizational control measures. This section will cover some of the central tenets of effective organizational control.
- **Board Size.** Colorado law allows an organization to have a minimum of one director, but the *Principles & Practices for Nonprofit Excellence in Colorado* recommend at least five. In addition, for 501(c)(3) organizations other than private foundations, the IRS likes to see a larger board that represents a cross-section of the community (though this is not a hard-and-fast legal requirement). There is no magic number of directors for every organization, but the organization should weigh whether the board is too small to provide proper oversight, or too large for each director to have meaningful participation.
- **Independence of board members**
 - The concept of independence is central to establishing and maintaining an effective and dispassionate board that is connected to the community that the nonprofit serves, encourages diversity of discussion, and fosters public confidence.
 - The IRS has issued guidelines in their [Form 990 instructions](#) for determining whether a board member may be considered “independent.” In order to meet this definition, the board member may not:
 1. Receive compensation as an officer, employee, or independent contractor of the organization.
 2. Have their compensation determined by individuals who are compensated by the organization.
 3. Receive direct or indirect material financial benefits from the organization. This does not include any benefits received as a result of the individual’s status as a member of the organization.
 4. Have a family or outside business relationship with any person or entity that .”falls into any of the above categories
 - The IRS requires organizations to indicate how many independent directors are on their board using Form 990, but does not provide guidance on the number or portion of directors that should be independent.
 - The Colorado Nonprofit Association does offer such guidance, suggesting that at least two-thirds of a public charity’s board members be independent.¹¹
- **Prohibition against private benefit/inurement**
 - In addition to maintaining an independent board, you should keep an eye out for two potential sources of trouble: private benefit and inurement. Private benefit and inurement are two related but distinct ideas, and occur when a nonprofit’s resources are used inappropriately to benefit specific parties.
 - In its “life cycle” analysis of nonprofit organizations, the IRS cautions against allowing any portion of an organization’s net earnings to “inure” to the benefit of any private shareholder or individual. It’s important to note that private shareholders and individuals are defined as any person who has a personal and private interest in the activities of the organization.¹² Thus, it may be useful to

¹¹ Principles and Practices, p. 6.

¹² <http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Inurement-Private-Benefit-Charitable-Organizations>

think of inurement as related to “insiders.” Private inurement restrictions apply to 501(c)(3) organizations, but also to other nonprofit exempt organizations like trade associations and social welfare organizations.

- A related trouble spot is private benefit, in which an organization operates for the benefit of private interests, which can include individuals such as the creator or the creator's family, shareholders of the organization, other designated individuals, or persons controlled directly or indirectly by such private interests.¹³ Unlike inurement, the private benefit rule is not aimed solely at the organization's insiders. This is a much broader doctrine that requires an organization to be mindful of benefit flowing to any private individuals or entities vs. to the public or a charitable class, and whether it is appropriate. However, it is limited to 501(c)(3) organizations.
- So what does this mean for you as a board member? As a director, you should be actively involved in reviewing and approving financial transactions. While playing this role, you may see transactions that, in your opinion, qualify as inurement or private benefit. It is your responsibility to identify these issues and highlight them to your directors and the organization's management team.
- Written conflict of interest policy and disclosure forms
 - The IRS defines a conflict of interest as a situation that arises when a person in a position of authority (such as a board member) in an organization can benefit from a decision that he or she has the power to make.
 - Though they have a bad rap, conflicts of interest are likely to occur in almost any organization. As a nonprofit board member, the question you should be asking yourself is not, “Does our board have conflicts of interest,” but instead, “How do we manage conflicts of interest in a responsible manner?” Creating a written conflict of interest policy will help your organization answer the second question in the case that the answer to the first question is “yes”.
 - It is important to remember that conflicts of interest may be material or simply perceived. In both cases, a conflict of interest policy is a valuable tool for identifying and dealing with the conflict. Two questions that you may ask yourself when beginning to prepare a policy are:
 1. What types of conflicts of interest might affect our organization?
 2. What conflicts have we dealt with in the past, and what did we learn from those experiences?
 - With those questions in mind, here are a few components to consider including in your conflict of interest policy:
 1. Require directors and staff to act solely in the interests of the organization without regard to personal interests. In other words, these parties should meet their duty of loyalty.
 2. Require directors, officers, and key employees to annually disclose, on a standard form, any interests that may result in conflicts.
 3. Require each of these parties to disclose potential or material conflicts as soon as they arise.
 4. Require board members with a material conflict of interest to recuse themselves from board discussions and votes. This means physically

¹³ <http://www.irs.gov/Charities-&-Non-Profits/Charitable-Organizations/Inurement-Private-Benefit-Charitable-Organizations>.

- excuse themselves from the meeting, and not exercise any influence on the decision outside the meeting.
5. Provide clear guidance on who administers the policy and who each party should submit conflict disclosures.
- The Independent Sector has made its [conflict of interest policy](#) available to the public, and it may serve as a good resource for getting started on your own internal policy.
 - Document retention policy - CCSA, IRS, CRNCA
 - The final topic we'll cover under "Organizational Control" seems straightforward: how to store and (eventually) dispose of documents. A thoughtful document retention policy is key to ensuring consistency and efficiency within your organization, and may even help if your organization finds itself in a legal bind.
 - As with conflicts of interest, there is no one-size-fits-all document retention policy. Nevertheless, there are a few guidelines that you should think about including¹⁴:
 1. A retention and destruction schedule, organized by document type (corporate, organizing documents, general records, electronic files, voicemails, etc.).
 2. Clear delineation of responsibility for administering and implementing the policy.
 3. Backup and archival procedures.
 4. Periodic audit and checkup guidelines.
 - When creating your document retention policy, keep in mind that, according to Colorado law¹⁵, a nonprofit organization must keep certain corporate record at its principal office. (and must keep some documents permanently)
 - Federal law also has some bearing on how you store and dispose of documents. Most importantly, provisions in Sarbanes-Oxley prohibit the destruction of documents pertaining to current or pending official investigation, audit or litigation. These restrictions do apply to nonprofits, so your document retention policy should include provisions for suspending document destruction in case of an investigation. In addition, a growing number of laws address how certain types of data must be destroyed, so your document retention policies should address this as well.
 - Again, the Independent Sector has made its own [document retention policy](#) available to the public.

¹⁴ From P&P, p. 9 and Principles Workbook, p. 16

¹⁵ CRS § 7-136-101

5. Financial Oversight

- As a nonprofit director, another of your primary responsibilities is to see to the long-term financial health of the organization. This section will provide some guidance and tips for fulfilling this duty.
- Organizations must be able to file an accurate and complete Form 990-N, Form 990-EZ, or Form 990-PF (and, if applicable, Form 990-T) and should provide annual reports containing detailed financial information that includes at a minimum, its total income, expenses, and ending net assets.
- The board should be trained on how to read financial statements and the Form 990. It should review and discuss the financial statements at least quarterly and the applicable Form 990 annually before it is filed with the IRS or state charity offices. Among other things, directors should review these records to determine how the organization is performing with relation to industry-standard measures such as program expense ratios and fundraising efficiency. You can find more information on these analyses in the “Board Review of 990 Forms” module of this course offering.

Be very clear about who is responsible for filing the Form 990, because the organization’s tax-exempt status is automatically revoked if the it fails to file a required Form 990 for three consecutive years.

- **Financial controls.** Financial controls ensure the integrity of an organization’s financial records. and activities Effective financial controls help ensure timely and accurate financial reporting and the safeguarding of the organization’s assets.
 - Segregation (separation) of duties is a vital component of financial controls. The aim is to ensure that one person cannot commit and conceal a fraud. A revelation of fraud has been known to destroy donor confidence in an organization. Even small organizations should try to separate as many duties as it can, especially the recording of revenue, receipt of funds, maintenance of accounts receivable records., maintenance of accounts payable records and bank reconciliation
- **Financial audits, financial committee, and auditing committee.** A charitable organization should have a qualified, independent financial expert audit or review its financial statements annually.
 - Some states - although Colorado is not one of them - require an independent audit or review, so an organization should confirm the legal requirement in each state.
 - For smaller organizations, a financial review by an independent auditor can provide essential guidance.
 - An audit committee composed of independent board members with financial expertise can ensure that the audit is conducted appropriately. The audit committee serves to reduce possible conflicts of interest between outside auditors and the organization’s paid staff.

- **Loans.** Colorado law does not permit loans to directors, officers, or trustees. Any director who assents to making such a loan becomes personally liable for the obligation.

6. Responsible Fundraising

- One of the most important relationships that your organization will develop is with its community of donors and funders. The board plays an important role in maintaining these relationships, and it is critical that directors understand how to raise funds responsibly. This section provides responsible fundraising tips and guidelines, many of which originate from state and Federal laws.
- Accuracy and Truthfulness of Fundraising Materials.
 - Colorado law prohibits misrepresentations in fundraising. This means an organization must not tell donors their donations are tax-deductible unless they actually are, and they cannot misrepresent the purpose for which a donation will be used. Because tax-exempt status will be revoked if the applicable Form 990 tax returns are not filed for three consecutive years, it is possible that some organizations that were formally exempt no longer are, and boards should be wary of this when representing to donors that their donations are tax-deductible.
 - A paid solicitor cannot misrepresent the percentage of a donation that will go to the charity. In addition, it is illegal to misrepresent the extent to which a donation will have a local benefit.
 - Organizations should provide clear contact information on any fundraising materials, so donors can contact the organization if necessary and request information.

Remember that generally only 501(c)(3) organizations¹⁶ can accept tax-deductible contributions, so other types of nonprofits should be transparent about the fact that donations aren't deductible.

- Compliance with Donor's Intent.
 - The organization should use donations only for the purposes intended by the donor. If a donor restricts a donation to a specific program or charitable purpose, that restriction must be honored at all times.; there are some limitation mechanisms under the law to modify restricted gifts, but this is not something that a board can do unilaterally
 - So, the organization needs to be very clear and specific about how donations will be used, i.e. will they go the general programs and operations of the organization, or will they support specific programs or types of programs? If donors are asked to contribute to a fund, be very clear if the fund has more than one purpose.
 - Fundraising materials should also clearly state how quickly donations will be distributed - especially when raising money for disaster relief efforts.
- Acknowledgment of Tax-Deductible Contributions and Gift Acceptance Policies. Organizations should develop policies and procedures to acknowledge contributions quickly and accurately as a confidence-building measure for donors, and because the IRS might require it. The IRS provides the following guidance regarding how organizations and individuals can substantiate contributions:

¹⁶ Certain fraternal societies and veterans organizations can accept tax deductible contributions.

1. 501(c)(3) charitable organizations must provide a written disclosure statement to donors of a quid pro quo contribution in excess of \$75. A *quid pro quo contribution* is a payment made to a charity by a donor partly as a contribution and partly for goods or services provided to the donor by the charity.
 2. A donor claiming a deduction of \$250 or more is also required to obtain and keep a contemporaneous written acknowledgment for a charitable contribution. Organizations should be prepared to provide such written acknowledgments routinely.
 3. For contributions over \$5,000, the nonprofit must generally obtain an appraisal prepared by a qualified appraiser
 - In addition, the CCSA requires paid solicitors who solicit by telephone to send a written confirmation of the expected pledge prior to collecting or attempting to collect any contribution.^{iv}
 - Organizations should have rules and procedures for evaluating whether it can accept a contribution and the circumstances under which their legal counsel or other experts will need to review the potential gift. Some contributions have the potential to create ethical problems for the organization, subject it to liability, result in unrelated business income, or even have adverse tax consequences, if, for example, a gift of property needs to be sold soon after it is received.
- **Oversight of Fundraisers.** A charity should be actively oversee contracts with any paid solicitor. This includes at a minimum gaining reasonable assurances that its paid solicitor is in full compliance with the Colorado Charitable Solicitations Act (CCSA). The charity should verify that the paid solicitor:
 - is registered and has filed a solicitation notice signed by the charity with the Colorado Secretary of State, and subsequently files a solicitation campaign financial report signed by the charity
 - has a written contract with the charity containing all of the elements required by the CCSA
 - adheres to scripts approved the charity
 - makes all of the written and oral disclosures required by the CCSA
 - complies with both the Colorado No-Call Law and the Federal Trade Commission's Telemarketing Sales Rule (TSR). The TSR requires paid solicitors to put individuals on the organization's internal do-not-call list when asked.
 - transfers the list of donors resulting from the solicitation campaign back to the charity on at least an annual basis
 - **Fundraiser Compensation.** When contracting with a fundraising professional, keep in mind that there are industry standards around how they should be compensated.
 - For example, the Association of Fundraising Professionals (AFP) Standard of Professional Practice No. 21 states that their members will not accept compensation or enter into a contract that is based on a percentage of contributions; nor will they accept finder's fees or contingent fees.
 - AFP provides three reasons for this standard:
 1. Support for a nonprofit organization in any form is a voluntary action for the public benefit.
 2. The seeking or acceptance of charity revenues should not result in

the personal benefit of any employees, contractor, or representatives of a charitable organization.

3. Donor attitudes can be unalterably damaged in reaction to undue pressure and the awareness that a commission will be paid to a fundraiser from his or her gift, thus compromising the trust on which charity relies.

- The concern is that a fundraiser being compensated on a percentage basis may not always have the charity's best interests in mind, and a certain amount of self-interest may come into play.
- **Donor Privacy.**
 - A charitable organization should respect the privacy of individual donors and should not make available the names and contact information of its donors without providing them an opportunity at least once a year to opt out of the use of their names. Respecting and maintaining the confidentiality of this information bolsters donor trust and support.
 - Organizations that collect personally identifiable information from donors and other visitors should have a privacy policy that spells out how the information will be used and how to inform the organization if the donor does not want personal information shared outside the organization.

Resources

“A Guide for Colorado Nonprofit Organizations,” First Ed. (Karen E. Leaffer ed., CLE in Colorado, Inc., Supp. 2013.

IRS Governance Check Sheet.

<http://www.bing.com/search?q=irs+exempt+organizations+governance+checklist&form=IE10TR&src=IE10TR&pc=MALNJS>

IRS Exempt Orgs Determinations CPE May 2009.

http://www.irs.gov/pub/irs-tege/eo_determs_governance.pdf

IRS Stay Exempt. <http://www.stayexempt.irs.gov/>

IRS ACT Report on Governance June 2008. http://www.irs.gov/pub/irs-tege/executive_summary_actgovernancerept.pdf

IRS Governance Topics - 501c3. http://www.irs.gov/pub/irs-tege/governance_practices.pdf

IRS Speeches

- [Sarah Hall Ingram, Nonprofit Governance-The View from the IRS, Georgetown Law Center, \(6/23/2009\)](#)
- [Steven T. Miller, Nonprofit Governance, Loyola University \(11/20/2008\)](#)
- [Steven T. Miller, Nonprofit Governance and Effectiveness and Efficiency of Operations \(4/24/2007\)](#)
- [Steven T. Miller, Issues on Nonprofit Governance, Georgetown Law School \(4/23/07\)](#)
- [Steven T. Miller, Issues on Nonprofit Governance, Georgetown Law School \(4/23/08\)](#)

Principles & Practices for Nonprofit Excellence in Colorado - Colorado Nonprofit Association.
<http://www.coloradononprofits.org/help-desk-resources/principles-practices/>

The Principles Workbook: Steering Your Board Towards Good Governance and Ethical Practice, 2009. Independent Sector.
http://www.independentsector.org/uploads/Accountability_Documents/Principles_Workbook.pdf

Urban Institute - Nonprofit Governance In The United States.

http://www.urban.org/UploadedPDF/411479_Nonprofit_Governance.pdf
