Chapter III: Ethics
An exemplary grantmaking institution operates as an ethical steward of the partly public dollars with which it is entrusted. Unfortunately, too many individuals continue to abuse philanthropy for personal gain. As the institution’s ultimate decision-making authority, trustees have a legal and moral obligation to ensure that their organizations are functioning in ways that ensure ethical stewardship.

Board composition is critically important to ethical operations. Research indicates that diverse groups make better decisions, and that a minimum of five people is needed to achieve a plurality of perspectives. Many family foundations and other grantmakers have seen tangible value from including the grantee perspective on their boards.

As a rule, trustees should serve without compensation. Research does not support the contention that compensated boards serve their institutions better. Moreover, every dollar spent on trustee compensation is one that could have gone toward achieving the mission of the foundation. The only exceptions should be if the CEO also is a trustee or if the foundation compensates lower-income board members who otherwise could not afford to serve.

One of the most important things a grantmaking institution can do to build public trust in its operations is to maintain appropriate policies and practices that make the possibility of abuse less likely and demonstrate substantive accountability. These policies include, but are not limited to: a) maintaining appropriate conflict of interest and whistleblower protection policies; b) establishing reasonable, not excessive, executive compensation; and c) subscribing to any of a number of available codes for ethical conduct and good governance.

Transparency also is integral to preventing abuses and enhancing meaningful accountability. A grantmaker practicing Philanthropy at Its Best should share freely extensive information regarding its grants, governance, management, investments and operations.

Because data on the issues covered by the ethics criterion are neither centralized nor easily available, we cannot say what proportion of the nation’s grantmakers meet or exceed these benchmarks. But many exemplary grantmakers operate in ways that meet or exceed the measures for this criterion.

Criterion III: Ethics — At A Glance

A grantmaker practicing Philanthropy at Its Best serves the public good by demonstrating accountability and transparency to the public, its grantees and constituents.

a) Maintains an engaged board of at least five people who include among them a diversity of perspectives—including of the communities it serves—and who serve without compensation

b) Maintains policies and practices that support ethical behavior

c) Discloses information freely

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Chapter III: Ethics

Foundation board positions are no longer ceremonial. Board members must be fully engaged in the oversight of their foundations’ operations and must actively seek to improve their skills. It is essential that foundations do everything they can to guard against both real and perceived abuses.

—Emmett D. Carson, President and CEO
Silicon Valley Community Foundation

Private foundations and other institutional grantmakers play a vital role in sustaining the U.S. civil society sector, and exemplary foundations operate ethically and with great integrity. Unfortunately, too many grantmakers do not take the necessary steps to demonstrate that they are using their tax subsidies to further their charitable purpose. It is incumbent on a foundation to demonstrate accountability and transparency in its operations so that regulators and the public know that all grantmaking institutions are acting as ethical stewards of the tax-subsidized dollars with which they are entrusted. As the Internal Revenue Service’s Governance and Related Topics guidelines for nonprofit organizations state: “The public expects a charity to abide by ethical standards that promote the public good. The organization’s governing body bears the ultimate responsibility for setting ethical standards and ensuring they permeate the organization and inform its practices.” As the ultimate decision-making body of a grantmaking institution, it is incumbent on a foundation board in particular to ensure that the institution it oversees complies with regulatory and legal requirements, public policy and generally-accepted ethical practices.

In 1975, the total number of foundations in the United States was 21,877. The most recent data available show a dramatic increase since then, with a significant surge in the type, number and assets of foundations. Currently, there are 72,477 grantmaking institutions, including independent, community, corporate and operating foundations. According to the Foundation Center, in 2007 the total assets of these foundations grew to $670 billion, the highest level yet recorded. Although the current financial crisis has reduced that figure significantly, foundations continue to control vast wealth. Because institutional grantmakers largely are exempt from taxation, the government foregoes substantial revenue that could be used to expand social safety net programs or provide for the common good in other ways. Steven T. Miller, commissioner of the Tax Exempt and Government Entities division of the Internal Revenue Service (IRS), underscored the purpose of the tax subsidy afforded to charitable organizations when he asserted that “every charity should make responsible and appropriate use of its resources to achieve its charitable purposes. That is what the tax-subsidy is for.”

Moreover, researchers estimate that “at least 45 per-
of disclosure about foundation operations. This also is in keeping with the IRS’s statement that charitable organizations must be “organized and operated exclusively for one or more exempt purposes.” Organizations must ensure that any earnings do not benefit any private individual or shareholder, and do not operate for the benefit of any private interests, including those of the founder, her or his family, its shareholders or any individuals controlled by these interests.

Viewed from a strictly legal perspective, some contend that foundation dollars are private dollars and ought not to be subject to public scrutiny. Yet, seen through a public policy lens, foundations, their grantees and the public are partners in pursuit of the common good. Coupled with the exempt organization’s legal obligation to demonstrate that it serves the public good and not private interests, as stated above, this is a compelling and justifiable rationale to expect institutional grantmakers to behave as ethical stewards of the partly public monies with which they are entrusted. Accountability and transparency have become meaningless buzz words despite some foundations taking steps toward enhancing public trust in philanthropy by voluntarily disclosing relevant information that demonstrates they are meeting their charitable purpose and furthering their missions.

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Institutional philanthropy historically has shown a preference for self-regulation over government regulation, with foundation trade associations and affinity groups frequently voicing collective opposition to any increase in governmental scrutiny. Even something seemingly as innocuous as mandated information disclosure is viewed with alarm, invoking unsubstantiated rhetoric about the “slippery slope” that leads to increased regulation. But disclosure regulation would not infringe on a foundation’s independence or decision-making; it simply would provide grantmakers, policymakers and the public with more robust information about the sector. Given that government regulation of philanthropy currently is so minimal, rigorous self-regulation is all the more important; but without substantive self-regulation further governmental regulation of foundations is likely. Sharing relevant information provides the public with important information from which it is free to draw its own conclusions; vigorous self-regulation is possible only with the right tools.

Independent research and congressional testimony by IRS officials demonstrate that the IRS’s tax exempt organizations division is extremely shorthanded and underfunded. State attorneys general lack the capacity to analyze voluminous foundation reports submitted to them each year with limited financial and human resources. Fully 36 states had one or fewer full-time equivalent attorneys dedicated to nonprofit oversight, with 17 states lacking any such legal capacity whatsoever. In other words, oversight capacity has not kept pace with the explosive growth among foundations. The quasi-public nature of foundation assets makes it incumbent on foundations to act ethically and prevent philanthropic abuses.

The information that private foundations must disclose publicly to maintain their tax-exempt status is limited to what is available on the IRS’s tax forms for these organizations, the 990 PF form, and annual reports provided on a voluntary and variable basis. Further, media reports indicate that many individuals continue to abuse philanthropy for personal gain. Examples range from political cronyism to extravag-
gant compensation and retirement packages for founda-
tion trustees and executives. Coupled with the lim-
ited publicly available data on foundation operations,
the public trust in institutional grantmakers has dimin-
ished and must be rebuilt. These are compelling rea-
sons for foundations to take robust voluntary steps
that demonstrate high levels of transparency and
accountability.

There are three things that a foundation can do to
make ethical operation more likely:

1. Maintain an engaged board with a minimum of
five trustees that brings a plurality of perspectives
to its decision-making;
2. Maintain policies and practices in support of ethi-
cal behavior; and,
3. Disclose significant amounts of information to the
public.

As more foundations take meaningful steps in this
direction, the public trust will be rebuilt and grant-
makers will maximize the social benefit of their con-
tributions to the American civil society sector.

Recent regulatory and policy history of philanthropic
accountability and sector reform
Issues of foundation accountability and regulation
date back to concerns that the early philanthropists
such as Andrew Carnegie and John D. Rockefeller
were using the charitable tax subsidy to exert undue
influence on many dimensions of the public sphere
through their giving.227 Government regulation
decreased in the early 1980s, following an IRS “exam-
ination study,” which concluded that private founda-
tions were complying with the dictates of their tax
exemption status. Faced with financial and human
resource deficiencies, the total number of audits on
private foundations decreased dramatically through-
out the 1990s, leaving the sector with markedly less
oversight and making it increasingly reliant on self-
regulation.228

The bull market period of the 1990s saw a tremen-
dous surge in the number of foundations and their
total assets. As The Robert Wood Johnson Foundation
states, “although this boom ... suggests that founda-
tions are thriving as never before, it is precisely this
rise in numbers, influence and complexity, coupled
with reductions in government spending for social
services that leaves them vulnerable to claims that
they are ‘unaccountable.’”229

In 2001, rampant scandals reported among corpo-
ations, government agencies and churches led to
increased public scrutiny and demands for more
investigations into foundations and other charitable
organizations. The public trust in institutional philan-
thropy diminished significantly following a series of
investigative media reports by the Washington Post
and Boston Globe in 2003. The newspapers ran in-
depth articles, demonstrating high levels of financial
abuses, particularly among foundation trustees and
executives. Financial scandals at Enron, Tyco
International, Adelphia and other corporations led to
the bipartisan Sarbanes-Oxley Act of 2002. The act
established uniform standards for all U.S. public com-
pany boards and management because of the impact
of the drop in private sector shares on publicly traded
securities. In light of the philanthropic abuses docu-
mented by the media, policymakers and regulators
began to consider the applicability of similar provi-
sions to nonprofit organizations to ensure compliance
with the law and justify the lost tax revenue from the
charitable exemption.

State attorneys general and members of Congress
with oversight of federal tax laws raised concerns
about their capacity to ensure that charitable organi-
zations were complying with the law, leading to
diminished oversight. In 2004, the Senate Finance
Committee chaired by Sen. Charles Grassley (R-Iowa)
began a series of hearings to determine the extent of
the problem. Among the myriad testimonies present-
ed to the committee, IRS authorities admitted that the
nonprofit sector long had been treated as a “compli-
ant area” by tax regulators. Because of limited finan-
cial and human resources, the agency audited less
than half a percent of the roughly one million charita-
ble organizations it is supposed to oversee. This was
in keeping with prior testimony from Marcus Owens,
former director of the IRS’s Exempt Organization
Division during the Clinton Administration, who stat-
ed that the IRS could access only 20 percent of the
information found on 990 PF forms, and with a budg-
et of $59 million in 1999, the exempt division was
incapable of conducting more than 115 audits of the
more than 60,000 foundations under its oversight in
the same fiscal year.230 Much of this depletion of staff
and resources at the IRS came in the wake of Sen.
William Roth’s (R-Del.) testimony on IRS abuses in
1997, which led to a massive reorganization of the
agency and Congress maintaining tight control over
the IRS budget.
Representatives of the National Association of State Charity Officials (NASCO) also underscored the paucity of funds available to support charitable enforcement cases. Mark Pacella, then president of NASCO, testified that financial resources were severely overextended and NASCO offices had insufficient personnel to conduct investigations of charitable organizations. Pacella noted that 990 PF forms frequently were submitted by organizations with inaccuracies and “filed one or more years after the fiscal period for which they relate has passed, making it doubly difficult for regulators to … pursue enforcement actions in a timely manner.” William Josephson, assistant attorney general for New York State, offered similar testimony, stating that although fully one-tenth of all 990 PF forms that his office reviewed raised red flags, resource deficiency and a void of legal expertise resulted in these cases often not being investigated. NASCO and several state attorneys general emphasized the need to reform the 990 PF tax form, promote greater communication between IRS and state enforcement agents, and create electronic filing systems that were available readily to both tax authorities and state jurisdictions. Watchdog groups such as NCRP also testified on the need to improve philanthropic accountability. In his June 2004 testimony during the Senate Finance Committee’s hearings on reforming charitable sector reform and oversight, Rick Cohen, then executive director of NCRP, noted three guiding principles that informed NCRP’s agenda for recommendations to reform accountability:

1. The laws and regulations for addressing the accountability of foundations and correcting the excesses reported in the press need to be strengthened.
2. Notwithstanding improved statutory and regulatory standards, the philanthropic sector itself has to get serious about dealing with the malefactors who sully the good work of organized philanthropy.
3. There should be an increase in the resources devoted to governmental oversight of philanthropy at the federal and state levels—and NCRP several months ago [in 2004] issued a specific proposal for the reuse of the foundation excise tax just for this purpose.232

Following the 2004 hearings, the Senate Finance Committee recommended the formation of an independent panel to analyze the state of governance and make recommendations to strengthen accountability and transparency in the nonprofit sector. In response, the Independent Sector convened a coalition of nonprofit experts and the Panel on the Nonprofit Sector was created to address concerns articulated by Congress, nonprofits, the public, and federal and state oversight agencies about the illegal and unethical practices of some charitable organizations. The panel produced final and supplemental reports, including recommendations for sector-wide reform, in 2005 and 2006.

The Senate Finance Committee eventually merged these recommendations into legislation passed as the Pension Protection Act of 2006. Provisions of the 2006 act subjected charitable organizations to more rigorous reporting requirements, authorized the IRS to revoke the tax-exempt status of any nonprofit or foundation that failed to file returns within three years, and established harsher penalties to inhibit inappropriate compensation and payout practices at charitable organizations, including foundations. The IRS also developed an electronic 990 form to improve the accuracy of nonprofit data collection and make information more accessible between state and federal enforcement personnel. In October 2007, the Independent Sector and the panel published the Principles for Good Governance and Ethical Practice: A Guide for Charities and Foundations, a list of 33 separate principles to strengthen ethical standards through self-regulation within the philanthropic community. Unfortunately, despite these various regulatory reforms and tools for self-regulation, abuses of philanthropy that diminish the public trust continue until today. For example, Bloomberg News reported suspicious insider dealing at the Robin Hood Foundation in 2007. An investigation revealed that the foundation maintained an emergency fund that grew from $20 million to $144.5 million in less than a decade and was invested in 19 hedge funds, of which seven were operated by Robin Hood donors and trustees. These board members were paid 2 percent of assets and 20 percent of profit for managing the donations; the charity paid $14 million in fees for hedge-fund management in 2005.233 These actions demonstrate a direct violation of the IRS’s guidelines for maintaining the charitable exemption. As the application guidelines for exempt status state, all 501 (c) (3) organizations “must not operate for the benefit of private interests such as those of … its shareholders or persons controlled by such interests.”234 After congressional scrutiny, Sen. Grassley voiced disapproval of the foundation’s trustee fee policies and the Robin Hood Foundation changed its practices. In a letter to foundation support-
ers, then–Executive Director David Saltzman defended the foundation’s policies, noting that none of the seven trustees served on the board’s investment committee. Still, because of the media and regulatory concerns, Saltzman’s letter announced a change in operations: “Although we are totally comfortable with these procedures, as part of our board’s ongoing governance review over the past year, and to avoid even the appearance of any conflict, we have decided that none of Robin Hood’s leadership will manage these funds going forward.”235 Such reports underscore the need for substantive reform of the way accountability and transparency are demonstrated in the philanthropic sector. This also ensures legal compliance barring insider dealing.

As NCRP co-founder and long-time commentator on the charitable sector Pablo Eisenberg stated before the Senate Finance Committee in 2004, “Public confidence in our charitable organizations has decreased. … There is a growing perception that the nonprofit sector lacks accountability. We cannot maintain strong and vibrant foundations and nonprofits without public trust. Restoring that trust must be the objective of any attempts to reform what is wrong with the system and to strengthen those practices that have been effective.”236 The partially public nature of foundation dollars, coupled with the significant increase in foundation assets, makes restoring the public trust in institutional philanthropy a practical and a moral imperative.

BOARD COMPOSITION

Board composition is critically important for any grantmaking institution. Boards need to be large and diverse enough to protect the public trust and to reflect authentically the priorities of communities served by the foundation.

Board size
Recent research indicates that diverse groups are better at problem-solving. Because a small board restricts the number of perspectives of a foundation’s decision-making body, increasing board size is an important corollary to diversifying board composition. In contrast to the final panel recommendations made to the Senate Finance Committee that boards ought to include a minimum of three people, the tenth principle from the Panel and the Independent Sector’s Principles to improve governance and ethical behavior suggests that boards should comprise a minimum of five individuals. Similarly, in his 2004 statement to the Senate Finance Committee, Eisenberg noted that neither regulation nor legislation should mandate the maximum size of a board. Highlighting that many grantee organizations have between 20 and 30 board members, he emphasized the benefits of larger boards: “Often, their size is an important asset, enabling them to achieve regional, ethnic, professional and community diversity and capacity.”238 Eisenberg added that while committee staffers recommended a minimum of three board members, maintaining a minimum of five trustees “provides a better guarantee that the organization can have a broad perspective and better understanding of the organization’s purpose and programs.”239 The potential negative consequences of a three-person board become clearer when one looks, for example, at the Bill and Melinda Gates Foundation, discussed in the case study of this chapter. Taken together, these perspectives suggest that ensuring at least a five-person board at a foundation increases the likelihood that collective preferences will inform and lead to better decision-making. Improved decision-making is not a panacea for eliminating abuses of philanthropy for personal gain. But, at a minimum, it offers the potential for better judgment to curb the level of abuse and restore the public trust in institutional philanthropy.

The board [of a charitable organization] should have enough members to allow for full deliberation and diversity of thinking on governance and other organizational matters. Except for very small organizations, this generally means that the board should have at least five members … The board of a charitable organization should include members with the diverse background (including but not limited to, ethnic, racial and gender perspectives), experience and organizational and financial skills necessary to advance the organization’s mission.

—Panel on the Nonprofit Sector, Principles 10 and 11237
Diversifying board composition
Recent studies indicate that foundation staffs, particularly program officers, are becoming more diverse, but the same cannot be said of boards. This means that decision-making remains concentrated in the hands of a homogeneous group at most foundations. Moreover, while staffs are becoming more diverse, progress appears to have slowed in recent years and the majority of staff diversity is attributable to the increase in the number of female program officers. A recent study commissioned by the Rockefeller Philanthropy Advisors on the diversity of foundation staff and boards over the last 25 years found that while there has been much progress, it has been inconsistent. The biggest gains were seen in the first half of the time period, but stagnation set in during the second half. For example, board diversity increased by 127.9 percent from 1982 through 1994; from 1994 to 2006, the gains were only 32.7 percent.

Currently, 87 percent of foundation board members are white, and demographic data on socio-economic status of trustees do not exist. Coupled with the small size of many boards, this means that decision-making remains significantly concentrated in the hands of homogeneous groups. These are disturbing trends among foundation decision-makers, especially considering the tremendous increase in foundation assets, which remain largely exempt from taxation, controlled by these groups.

Similarly, CEO diversity increased by 156.3 percent from 1982 to 1994 and then by only 41.5 percent from 1994 to 2006. Foundation CEOs were even less diverse than the boards analyzed; total CEO diversity increased by a mere 5.8 percent in 2006. Regarding program officer diversity, the majority of increases in the proportion of diversity were between 1982 and 1994. Notably, the period from 2002 to 2006 saw a decline in program officer diversity. Neither the report nor this writing seeks to identify causal relationships between the factors related to increases in staff and board diversity and the trends identified. But even for those in the group that has seen the biggest gains in diversity, the statistics are telling: although the percentage of women in philanthropy increased, particularly as a proportion of program officers, these gains were made largely by

The board of the Bill and Melinda Gates Foundation comprises three people: Warren Buffett, Bill Gates and Melinda Gates. Can such a small group of decision-makers bring a plurality of perspectives to the board, especially in the absence of critical feedback? This is a vitally important question considering the mammoth size of the Gates Foundation.

Pablo Eisenberg, Joel Fleishman and Dr. Arata Kochi, the former leader of malaria programs for the World Health Organization (WHO), are among the few voices that have raised concerns about the lack of controls or honest feedback from grantees to ensure that the Gates Foundation is achieving its mission. In fact, Dr. Kochi no longer is with the WHO, although the organization states that he is on leave and that his departure is unrelated to his criticism of the Gates Foundation as a “cartel” that imposed its agenda on the WHO and was unresponsive to critical feedback. Even the former director of the Gates Foundation, Patty Stonesifer, cautioned about the dangers the foundation faces because of its lack of receptivity to critical feedback, stating in the 2007 annual report that “the danger isn’t in what people do tell you – it’s in what they don’t.”

While the mission and vision of the Gates Foundation are almost universally accepted as laudable, some like Dr. Kochi raise important issues, for example about the reliance on technological solutions such as the malaria vaccine versus addressing immediate problems such as dire poverty in less developed countries. Indeed, many developing countries that welcome the infusion of monies to improve health find themselves in the awkward position of lacking the needed infrastructure to put those resources to use. Health systems
white women. Moreover, even white women remain underrepresented on foundation boards, comprising 31 percent of all board members in 2006.243

Diversity is a nuanced, complex and dynamic concept; true and inclusive diversity cannot be reduced to numbers and measures alone.244 Thus, demographic diversity is not the only important factor in determining how diverse or inclusive a foundation or its board is. As Mary Ellen Capek and Molly Mead note in defining “deep diversity,” “Diversity also works to democratize boards and staffs of organizations. More diverse boards and staffs have a better shot at being effective. Understanding gender in the context of other diversities like race, class and culture—which also means understanding the insidious, often subtle and unacknowledged preference for ‘normal’—is essential for building healthier institutions. Philanthropic and nonprofit leaders interviewed for our book emphasized the need for new language to capture this understanding, so throughout our book, we use the term ‘deep’ diversity to describe an institutionalized understanding of diversity that goes wide as well as deep.”245

University of Michigan professor Scott E. Page’s seminal book The Difference: How the Power of Diversity Creates Better Groups, Firms, Schools and Societies246 presents compelling evidence that diversity leads to enhanced effectiveness and gains in efficiency. Drawing on various statistical models, Page contends that diversity should be valued for its positive contributions within a market framework and especially for decision-making and addressing problems. His findings indicate that diverse groups outperform homogeneous groups, even when ability is controlled for. Page argues that diverse backgrounds, perspectives and opinions lead to more accurate collective predictions and better decisions. The link between “diversity” and effectiveness is one that resonates with many funders, particularly given the connections between philanthropy and the private sector. Importantly, Page’s work must be contextualized so that “diversity” does not get reduced to simple metrics. Social inclusion and authentic ways to diversify foundation boards suggest including the grantee and community perspectives as two important means to achieve meaningful “deep diversity.” As Dr. Robert K.
Ross, president and CEO of the California Endowment states, “Diversity is best understood, prioritized and integrated into the operations of a foundation as a tool for effectiveness in, and responsiveness to, the communities being served.”

There is general consensus that the diversity and heterogeneity of the foundation universe results in variable perceptions of effectiveness. Yet, there is less discussion or agreement on the issue of what comprises an authentically diverse board. To address this gap, the Center for Effective Philanthropy (CEP) conducted a rigorous statistical analysis as part of its Foundation Governance Project. In its second report of the Project, CEP found that “once minority membership reaches higher absolute numbers—three or more—ratings of opportunity for influence do not vary between minority and non-minority [board] members.”

Importantly, as CEP acknowledges in this report, the lack of a single or uniform measure of foundation effectiveness makes any analysis of this important component of foundation governance challenging. Thus, CEP relied on self-reporting from foundation trustees regarding their perceptions of what comprises effectiveness as a proxy measure in this analysis. The findings on board diversity merit a specific caution: while the correlation between the absolute number of minority persons on a board and the minimum number of those members needed to ensure that they feel empowered in board discussions is sound, it has the potential to perpetuate reductionist viewpoints on what diversity comprises. Put differently, just as Page’s work on board diversity and effectiveness must be framed in the larger context of social inclusion, so must the CEP findings. It would be counterproductive for boards to assume that once they reach the nominal figure of three “minority” members that there is, in fact, authentic diversity reflected in the board’s composition. But the CEP findings underscore that a board must have a minimum of five people; because a minimum of three non-majority members is needed for them to express their opinions, increasing board size to a minimum of five is a reasonable and achievable benchmark for any grantmaking institution to meet.

Including the grantees in decision-making
Grantees are more attuned to the needs of their constituents, understand the local context in which they work and bring other valuable intellectual and human capital to the relationship that funders do not have. This expertise should inform philanthropic decision-making by including these representatives on boards. It is knowledge that increases sector-wide impact and helps foundations better understand on-the-ground realities of the environment in which both parties are working. Some exemplary grantmakers already include grantees or constituent representatives on their boards.

In 2003, NCRP convened representatives from 50 local, national and regional nonprofits including affinity groups, civil rights organizations and community-based organizations. Among the issues raised by participants in their discussion of improving philanthropic practice was diversifying board composition. As the report on the convening states, “Meeting participants particularly cited the need for putting [grantees] on the boards of foundations and for expanding the representation of people of color on foundation boards as high priority tasks …”

A 2008 survey by Grantmakers for Effective Organizations (GEO) found that only 14 percent of grantmaker respondents indicated that they had delegated power about decisions regarding funding to grantees or representatives of recipient communities. Foundation asset size is associated with the likelihood of engaging grantees or communities served: the larger the foundation, the more likely it is to do so. Even so, GEO’s analysis found that only 21 percent of the largest foundations with assets in excess of $400 million reported delegating decision-making.

GEO’s survey also found that foundation boards that include members with nonprofit experience are more likely to engage in grantmaking practices that are associated with grantee success. In their sample, respondents with one or more nonprofit representatives on the board were twice as likely to report soliciting anonymous or non-anonymous feedback from grantees. GEO notes that while there is an association between the presence of such board members and these “grantee-friendly” practices, causality is hard to determine. As the report states, it is possible that grantmakers already engaged in such practices are more likely to maintain nonprofit representation on their decision-making bodies if the presence of these members is associated with better decision-making practice.
TRUSTEE COMPENSATION
Trustee compensation persists as the subject of significant debate and research in philanthropy. The IRS does not provide definitive guidance on how to determine appropriate levels of trustee compensation, noting that “the compensation of officers, directors, trustees, key employees, and others in a position to exercise substantial influence over the affairs of the charity should be determined by persons who are knowledgeable in compensation matters and who have no financial interest in the determination.” Media reports continue to demonstrate abuses of trustee fees for personal enrichment and recent research demonstrates high variability across foundations regarding trustee compensation policies and practices. There are two compelling reasons for a grantmaking institution to maintain an uncompensated board: the data do not support proponents of compensation who contend that such policy results in better service; and more importantly, every dollar that goes to excessive trustee compensation is a publicly subsidized dollar that should be used to further the grantmaker’s mission. Thus, as a rule, trustees should serve without compensation; this is expected of and true for the vast majority of grantee organizations. The only exceptions should be if the CEO also is a trustee or if the foundation compensates lower-income board members who otherwise would be unable to serve because they cannot afford the time lost from work. As Virginia Esposito of the National Center for Family Philanthropy states, “Foundations are generally averse to supporting that sort of behavior on the nonprofit side, so why do they do it themselves? I would be appalled if a nonprofit that I was thinking to fund paid their trustees, so we should not either.”

The 2007 Principles for Good Governance and Ethical Practice, issued by the Panel on the Nonprofit Sector convened by the Independent Sector did not rule out compensating board members. The 20th senior fellow at the Hudson Institute, synthesized many of the arguments stated by grantee and foundation executives for and against compensation of trustees. As Schambra notes in discussing the Roundtable’s response, trustee compensation is a legal practice provided that payments are not excessive and can be considered “reasonable and necessary to carry out the exempt purposes of the foundation.” In contrast, Pablo Eisenberg et al.’s 2003 research notes the potential for self-dealing and abuse that results from variable interpretations of the IRS guidelines that bar trustees from engaging in such practice. As the report states, “According to the IRS, trustees, even family members, can be paid for services to a foundation that are reasonable, necessary and not excessive. There are, however, no firm criteria for evaluating what is reasonable, necessary and not excessive. Such vagueness leaves the door open to potential ethical problems and blatant abuse by trustees.” Some grantmaking institutions such as the Charles Stewart Mott Foundation never have compensated board members. As the foundation’s presi-

Philanthropy has an honest reputation that’s being tarnished by the actions of a few greedy trustees and staff members who pay themselves far too handsomely …. Foundations have tax-exempt status because they contribute to the greater good. To survive and prosper, they need the public’s trust. Excessive compensation drains money away from charity and creates an intolerable stain for the many selfless trustees who work for little or no money.

dent and CEO William White states, “We have never had to pay our board members. There are many, many excellent potential candidates who would love an opportunity to serve on a foundation board free of charge.”

Media reports indicate that foundation trustees continue to receive excessive compensation and abuse their positions in other ways. The 2003 *Boston Globe* series concluded that there were many foun-

dations “whose tax returns show that officers and directors are themselves the principal beneficiaries of foundation assets.” For example, the *Globe* found that Paul C. Cabot Jr., principal trustee of the Paul and Virginia Cabot Charitable Trust, paid himself an annual salary of more than $1 million from 1998 to 2001, with an increase in 2001 to finance his daugh-
ter’s $200,000 wedding. During the same five years, the foundation’s assets declined significantly from $14 million to roughly $5 million under Cabot’s stewardship while paying out an average of $400,000 a year to grantees. Cabot admitted to the *Globe* that a large proportion of foundation assets was used to maintain his affluent lifestyle. This example demonstrates not only a violation of the public trust but a clear breach of federal laws regarding charitable organizations that apply to private foundations, i.e., that such entities “must ensure that its earnings do not inure to the benefit of any private shareholder or individual” and “must not operate for the benefit of private interests such as those of its founder [or] the founder’s family.”

More recently, the *Buffalo News* reviewed the tax returns of 80 foundations of variable size and type in a series of articles analyzing foundation grantmaking and expenses in Western New York. The analysis found that 30 (37.5 percent) of these foundations compensated their trustees. The foundations that provided the highest levels of trustee compensa-
tion include the Margaret L. Wendt Foundation and the Oishei Foundation. The article notes that the $124 million Wendt Foundation pays three trustees $156,000 a year while the Oishei Foundation pays its nine trustees a total of more than $300,000 annually. Oishei holds $305 million in assets. Such behavior is an abuse of the public trust and negatively impacts the proportion of foundation assets that are much needed by grantees. In the aggregate, the 80 foundations analyzed spent approximately 25 cents on operating and administration expenses for every dollar awarded in grants. The article highlights the variability in foundation expenses associated with asset size and con-
cludes, “Whether for costly investment advice or trustee costs, [some, mostly smaller, foundations’] operating and adminis-
trative expenses, as a percent of their grants, [are] twice the average for foundations between 2002 and 2007.”

Local context may be an influencing factor in the cost ratios of smaller foundations noted here. In contrast to the *Buffalo News* analysis, the Association of Small Foundations found that most surveyed members usually spend 8 cents for each dollar they pay out in grants. Smaller samples drawn from the membership of the Council on Foundations indicate that in 2004, 58 percent of independent foundations provided compen-
sation to all or some of their board members, a figure that went up substantially to 83 percent for foundations with assets greater than $500 million. A recent comprehensive analysis by the Urban Institute, the Foundation Center and GuideStar found that roughly 25 percent of all the foundations studied indicated board compensation on their tax filings for at least one of the three years studied. Although some of these foundations did not compensate trustees in each of the three years analyzed, approximately 18 percent did. The report authored by Elizabeth Boris et al. is one of the first thorough analyses of the various factors that influence foundation expense and compensation patterns across different types of foundations with variable asset sizes. The study analyzed
influencing factors at 10,000 foundations from 2001 through 2003. Data analyzed included compensation records for more than 50,000 individual staff members, managers, trustees and executives as reported on the 990 and 990 PF forms. The foundations studied represent 16 percent of all independent, corporate and community foundations, and account for 78 percent of all foundation giving and 77 percent of all grantmaking assets. The report thus presents the most accurate available picture of the influential factors for foundation expenses sector-wide.

The analysis shows that compensated board members at independent foundations earned a median salary of $8,000 in the course of the three years studied. But the same research indicates that the median, usually less subject to influential outliers than the mean, still obscures highly compensated board members, whose excessive compensation increased the overall average compensation among independent foundation board members to roughly $15,700 in the three-year study.270 Trustee compensation among community foundations was rare, but the average among those that did compensate directors was between $5,000 and $7,000. Corporate foundations compensated trustees at rates much lower than either community or independent foundations, but these costs do not include other forms of compensation such as direct payment from the parent corporate company or other monetary recompense for tasks performed for the corporation. Compensation was greater for board members of large foundations with higher annual giving trends.

In 2003, the Center for Public and Nonprofit Leadership at Georgetown University published a study analyzing information on trustee compensation for 176 of the largest private foundations in the United States determined by assets and for 62 smaller U.S. foundations. Pablo Eisenberg et al. analyzed tax returns from 1998 for each foundation and conducted telephone interviews with private foundation representatives to verify the accuracy of the data reported on the 990 PF forms. The results demonstrated that:

1. In the 238 surveyed foundations, a total of $44,891,982 was paid in trustee fees; close to $25 million went to trustees at the large foundations.
2. Fourteen of the large foundations studied paid their trustees more than $100,000 each. Five of the 62 smaller foundations paid their trustees more than $100,000 each in fees, while nearly half paid $25,000 or more.
3. A subsample of 113 of the large foundations paid trustee fees, and compensation at 18 of these totaled 10 percent or more of administrative costs, while the fees of seven were one-third or more. Further, 22 small foundations provided fees comprising 25 percent or more of administrative costs.271

The study concluded that trustee fees should be capped at $8,000 annually per director, emphasizing that this would translate to the equivalent of an annual salary of $96,000. The researchers recommended excluding trustee fees as an allowable expense for foundations to count toward meeting their yearly payout requirements. As Pablo Eisenberg, one of the analysts, stated recently to the *Buffalo News*, “It comes down to a class issue that has not been addressed by the foundation world. It’s just an outrageous thing that these wealthy folks should get paid for doing their civic duty.”272 He also noted that trustee fees account for some $300 million annually and that most foundation boards are homogeneous and do not include the types of variable perspectives that many nonprofit boards do.

Some grantmakers contend that paying trustees is necessary because of heightened competition for qualified board members from the private sector, where they receive such fees. For example, John Healy, former president of the Atlantic Philanthropies, stated that the foundation paid its board members “quite handsomely” because “we’re asking busy people who have other careers, sometimes in very specialized fields, to give us a lot of time.” Similarly, Joel Fleishman, former president of the Atlantic Philanthropic Services Co. Inc., the U.S. program staff of Atlantic Philanthropies, cites this competition for trustees from the private sector and their limited time as the rationale for foundations compensating trustees.273

In contrast, foundations such as Charles Stewart Mott, William and Flora Hewlett, David and Lucile Packard, William Penn, Surdna, Rosenberg, George Gund, and the Rockefeller Brothers Fund do not compensate their trustees. Colburn Wilbur, former president of Packard, explained the foundation’s policy by stating, “Universities, hospitals and even the largest nonprofits seldom pay trustees; why should the Packard Foundation?” Kirke Wilson, former executive director and president of the Rosenberg Foundation for some three decades, noted that “there is no
research supporting the notion that trustee compensation results in higher levels of engagement, better grantmaking or better work.” Some smaller foundations including the Baptist Community Ministries, the S. H. Cowell Foundation and the New World Foundation also do not provide trustee fees. This allows them to invest more foundation money towards charitable causes.

In assessing whether compensated trustees provide better service than uncompensated boards, the Center for Effective Philanthropy (CEP) studied the effectiveness of both types of boards. CEP found that paid trustees often were more active outside of the board room than voluntary trustees but concluded that the data could not determine whether there is a causal relationship between more trustee engagement and compensation. The report also concludes that “even if pay were shown to cause the different behaviors described here, it would remain an open question whether this would justify the practice—or whether there are other, equally effective ways to motivate such behavior.”

In lieu of direct monetary compensation, some grantmaking institutions allow trustees to make discretionary grants with foundation dollars. But this is, in fact, an alternate form of compensation and is not exemplary practice. While this practice at least ensures the dollars still are going to a charitable cause of some kind, there often is little relation between the mission of the foundation and the recipient organization. Some trustees use these discretionary grants to advance their own social standing or to replace monies they would have given from their personal funds.

The IRS guidelines on board compensation are vague, subject to variable interpretations of what is “reasonable,” and lead to a lack of consensus across the sector about what this means, even within similar grantmaking institutions. Because of this lack of agreement and the continued abuses documented by the media, as a rule, trustees should serve without compensation with the two exceptions of the CEO or lower-income board members who would be unable to serve otherwise. Especially because most foundation trustees come from affluent backgrounds, there is no defensible rationale for compensation that drains the U.S. civil society sector of needed grant dollars to maximize the social benefit of institutional philanthropy’s contributions to its nonprofit partners.

POLICIES AND PRACTICES THAT SUPPORT ETHICAL BEHAVIOR

In 2008, the IRS revised the 990 form for charitable organizations, including some grantmaking institutions such as community foundations, to include governance information. However, similar changes were not made to the 990 PF form filed by private foundations. Ensuring ethical operations is integral to demonstrating that a grantmaker is using the tax subsidy appropriately, not violating the law, and giving the public a maximum return on its charitable investments. One of the most important things a grantmaking institution can do to build public and regulatory trust in its operations is to maintain appropriate policies and practices that make the prospect of abuse less likely and demonstrate substantive accountability. These policies include but are not limited to: a) maintaining appropriate conflict of interest and whistleblower protection policies; b) establishing reasonable, not excessive, executive compensation; and c) subscribing to and abiding by any of a number of available codes for ethical conduct and good governance.
Maintaining appropriate conflict of interest and whistleblower protection policies

Several of the Panel on the Nonprofit Sector’s principles for good governance align with recommendations made in this chapter. Principle 3 is applicable directly to ensuring that a foundation is carrying out its work ethically and that conflict of interest policies are in place. It states, “A charitable organization should adopt and implement policies and procedures to ensure that all conflicts of interest, or the appearance thereof, within the organization and the board are appropriately managed through disclosure, recusal, or other means.”

The most recent IRS guidelines for nonprofit organizational governance state that “the directors of a charity owe it a duty of loyalty [that] requires a director to act in the interest of the charity rather than in the personal interest of the director … In particular, the duty of loyalty requires a director to avoid conflicts of interest that are detrimental to the charity.” The same duty of loyalty should apply to conflicts of interest at grantmaking institutions. Ensuring that a conflict of interest policy is in place provides a foundation a range of benefits. It can ensure that there is no self-dealing, a loophole left open by the mid-2000s’ regulatory focus on abuses in the charitable sector. By addressing self-dealing, a conflict of interest policy has the potential to curb or prevent abuses from occurring. For example, in 2004, the New York Times reported that executives from the J. Paul Getty Trust were being paid retirement packages many times their base salary. Further allegations led the Council on Foundations to investigate whether there was “inappropriate compensation for the foundation’s CEO and potential self-dealing” because of a land procurement deal between the Getty Trust and Eli Broad, a billionaire financier and close personal friend of the trust’s CEO.

By ensuring compliance with its conflict of interest policy, it is possible that the trust would have avoided public embarrassment and censure by the Council on Foundations. This example also demonstrates the trust’s failure to adhere to its role as an ethical steward of its assets as required by the IRS guidelines for ethical operations, specifically that tax exemption is contingent on the organization neither operating for private interests nor engaging in business transactions that do not relate to its tax exempt purpose.

Putting a whistleblower protection policy in place is an important step to ensure that if and when abuses of philanthropy for personal gain are suspected, the employee or trustee knows that she or he can report their superiors without fear of retribution. Similar to adhering to a conflict of interest policy, protecting whistleblowers demonstrates that a grantmaker takes seriously the generous tax subsidies it receives and is committed to eliminating abuses. The media reports discussed earlier demonstrate continued violations of the public trust. These investigative articles would not have been possible had the journalists not granted anonymity to their tipsters. This is one area in which grantmakers could draw lessons from the fourth estate in exercising due diligence that ensures ethical operations. The IRS governance and related topics guidelines for nonprofits “encourages the board of directors to adopt an effective policy for handling employee complaints and to establish procedures for employees to report in confidence any suspected financial impropriety or misuse of the charity’s resources.”

NCRP advocates such policies to ensure that abuses are reported without fear of retribution at grantmaking and grantee organizations alike.

Establishing reasonable, not excessive, executive compensation

Executive staff are compensated under the IRS stipulation that such compensation is “not excessive and can be considered reasonable and necessary to carry out the exempt purposes” of the foundation. As with the variable interpretation of the terms “reasonable and necessary” in trustee compensation, determining what constitutes “reasonable” compensation for executives of grantmaking institutions remains an area of considerable debate and disagreement.

Numerous factors inform the process for determining an executive’s compensation level. Because of regional variations in the cost of employing and retaining high-quality staff, heightened competition for qualified staff who otherwise could work in the private sector, and the huge variations in the cost of conducting a foundation’s day-to-day operations, the current mandate that compensation be “reasonable” leaves grantmakers substantial flexibility. It is impossible to determine a single, uniform metric to determine an appropriate level of compensation for foundation executives. But the variable definitions of “reasonable” make it all the more important that grantmakers have clear and transparent processes in place to make compensation decisions. Excessive executive compensation damages the public trust in grantmaking institutions and is an affront to the spirit of philanthropy. For a foundation to increase reg-
ulatory and grantee trust in its operations, it should be transparent about the steps taken in determining what it perceives as reasonable and why. By clarifying and publicizing the process and policies used to determine executive compensation, a foundation executive’s compensation is contextualized better and abuses of philanthropy for personal gain can be curbed.

The Chronicle of Philanthropy notes that the median levels of executive compensation across the nonprofit sector grew at a rate faster than inflation: inflation was 4.1 percent in 2007, while grantee and foundation CEOs received a median compensation increase of 5 percent. As the Chronicle highlights, this is the largest increase in a one-year period since the paper’s 2002 survey that showed a 7.5 percent increase. Although this analysis emphasizes variability across types of foundations and notes the emerging trend of larger charities hiring leaders with private sector backgrounds as contributing factors, some foundations appear to provide unjustifiably large compensation to their CEOs. Another important finding in the analysis is that many foundation trustees now provide exorbitant bonuses and fringe benefits that supplement even seemingly reasonable executive compensation levels.

Negative publicity that often accompanies excessive compensation has significant consequences for a grant-making institution. For example, the infamous 1992 scandal about United Way President and CEO William Aramony’s theft from the organization continues to haunt United Way chapters nationwide because of the extensive media coverage the incident received. Aramony was convicted in 1995 on 25 counts, including conspiracy to defraud and filing false tax returns; he served seven years in prison. In 2002, upon Aramony’s release from jail, the Nonprofit Quarterly quoted Bob Beggan—the man in charge of United Way’s international work who had reported to Aramony for nineteen years—as stating that he had to travel with a document that explained what had happened because the Aramony scandal came up in other parts of the world.

The same article notes that many local chapters disaffiliated themselves from the national United Way office and filed for name changes, and that local chapters that did not even exist during the early to mid-1990s still must address this scandal in the “Frequently Asked Questions” sections of their websites. In 2006, Kevin McCarthy, CEO of the United Way of Inland Valley in California, said that he still heard regularly about the Aramony scandal. This egregious example demonstrates how executive largesse and abuse of the public trust hurts the charitable purpose of an organization. More recently, the public scandal surrounding former CEO Gloria Pace King’s $2.1 million pension led to outrage among individual donors who withdrew their support, resulting in the United Way of Central Carolinas closing its fundraising campaign in November 2008 some $20 million short of the amount raised in the previous year; the chapter was among the 20 leading fundraising chapters at that time. Excessive executive compensation that brings a grantmaker bad press is especially harmful for grantmaking public charities that rely on raising funds from the public.

Pablo Eisenberg has been a regular critic of the practice of augmenting executive compensation at the expense of talented program officers. He states, “Such compensation practices show how many foundations have begun to borrow the corporate cult of the chief executive, with its increasingly high pay, large benefits, special perks, and separation from the rest of the staff. In many cases, the second-highest ranking official in a foundation … receives half or less of the CEO’s salary, while excellent program officers may get one-third or less of the salary their CEO receives.” The 990 PF form requires data on the compensation provided to all officers, managers, trustees and directors to be listed. A foundation also must report compensation of the five highest paid employees not included in the section on board members and others noted. While these data provide meaningful insight into compensation, the variability in how the information is reported makes comparisons over time challenging. For example, although only 25 percent of foundations employ staff, the data on the PF form vary by year. An employee’s name may be reported one way in a given year and differently in another (e.g., John A. Smith can be reported as J. Smith). Uniformity in reporting these data would enhance transparency and allow for longitudinal comparisons, providing better sector-wide trends and benchmarks of accountability and transparency.

**Subscribing to codes of ethical conduct and good governance**

The Panel on the Nonprofit Sector’s second principle for good governance states: “A charitable organization should have a formally adopted written code of ethics with which all of its directors or trustees, staff and volunteers are familiar and to which they adhere.” The
Ford Foundation, for example, makes publicly available on its web site the code of ethical conduct it expects staff to follow. It also publicly discloses its governance practices. Additionally, Ford makes other documents on governance available in three broad areas: the foundation’s governing documents; its committee charters and memberships; and the policies and procedures it adheres to. The California Endowment publicly discloses similar information on its web site, including its code of ethics and conflict of interest policy. There likely are many more foundations that follow similar practice, but without centralized data it is not currently possible to determine the proportion of foundations that do so.

There are numerous codes for good governance, accountability, ethical behavior and transparency. The Independent Sector has compiled a list of nearly 100 such standards for nonprofits and foundations. Among those comprising the Independent Sector’s compendium are several resources for grantmaking institutions of variable types, including the Council on Foundations and the Minnesota Council on Foundations, Indiana Grantmakers Alliance, Washington Grantmakers and the New York Regional Association of Grantmakers. These publicly available codes of ethical conduct and good governance provide useful tools for grantmaking institutions, and exemplary grantmakers subscribe to and abide by one or more of these sets of principles.

TRANSPARENCY AND DISCLOSING INFORMATION FREELY

Transparency is integral to ensuring that a grantmaking institution is able to demonstrate that it is making appropriate use of the generous tax subsidies afforded it by the government. The public also has a right and a vested interest to expect a significant level of disclosure about foundation operations. Meaningful transparency can help policymakers and the public discern the extent to which the subsidies afforded foundations actually serve the public good and if a foundation is maximizing its own and the public’s return on its charitable contributions. As Supreme Court Justice Louis Brandeis often is quoted in discussions about transparency and accountability, “Sunlight is said to the best of disinfectants.”

NCRP believes that regulation of philanthropy is necessary and important, and that when done properly, it can help foundations achieve their missions and protect the public interest. Although regulation and mandates are among the ways that grantmaking institutions can demonstrate substantive transparency, voluntarily engaging in meaningful transparency by disclosing relevant information publicly is one way that an exemplary grantmaker demonstrates its stewardship of the partly public dollars with which it is entrusted. As Sean Stannard-Stockton, principal and director of Tactical Philanthropy states, “We need to reframe transparency away from some sort of thing that philanthropy is being forced to consider by outside forces and instead celebrate transparency as the mark of an organization that is truly committed to improving the field.”

NCRP long has advocated for voluntary information disclosure as one way to help ensure foundation accountability. At the 1980 Council on Foundations annual conference, NCRP presented its first report on foundation accountability, *Foundations and Public Information: Sunshine or Shadow*. The report brought media and foundation attention to sector-wide lax reporting. The increased publicity led to many foundations, including the Pew Memorial Trust and the Rockefeller Foundation, to publish annual reports. Today, most foundations routinely publish such reports and make them publicly available.

In 2008, the IRS revised the 990 form, the tax form all charitable organizations must file, to include information about governance. Steven Miller described the rationale behind the changes to the 990 form as follows: “Despite the absence of explicit federal statutory provisions setting forth clear governance standards, what I am calling jurisdictional gaps, we are not inter-
lopers trying to regulate an area that is beyond our sphere. Rather, the effects of good or bad nonprofit governance cut across virtually everything we see and do in our work. It impacts whether the organization is operated to further exempt purposes and public, rather than private, interests. It dictates whether the organization’s executives are compensated fairly or excessively. It influences whether the organization makes informed and fair decisions regarding its investments or its fundraising practices, or allows others to take unfair advantage. The question is no longer whether the IRS has a role to play in this area, but rather what that role will be.299 Grantmaking public charities now are required to disclose this governance information because they file a 990 form. For private foundations that file the 990 PF form, it is reasonable and fair to expect similar disclosures voluntarily.

Some people … have been raising the issues of philanthropic diversity and inclusiveness as if such calls were new. But these concerns, in fact, have been acknowledged in philanthropic circles for at least three decades.

– Lori Villarosa, Director, Philanthropic Initiative for Racial Equity

There is a void of information that can help the public gauge whether or not taxpayer subsidized dollars are being used to further a foundation’s charitable purpose. This results in a lack of substantive transparency. Recent legislation in California highlighted the lack of available information about diversity in foundations. Although the bill, AB 624, eventually was withdrawn by its sponsor, the debate sparked important discussions about diversity in philanthropy and has led to some additional research and to new foundation investments in the capacity of minority-led nonprofits.300

Some foundations provide ready access to diversity data. The San Francisco Foundation, for example, sees contextualized diversity as a core value and demonstrates its values by making demographic data on its staff and board publicly available and ensuring that its grants go to truly diverse groups that reflect the communities being served. According to the foundation’s policy on diversity, it “actively seeks to promote access, equity, and diversity, and to end discrimination based on race, ethnicity, gender, sexual orientation, disability, or age.”301 Importantly, this foundation also seeks out grantees that reflect the same diversity values that it employs in its own staffing and board composition. The California Endowment discloses the ethnic and gender breakdown of its staff and trustees. This mirrors the foundation’s mission of improving the health of California’s multicultural communities.302 These foundations display a commitment to ensuring inclusive diversity, matching mission with grantmaking and disclosing publicly information that helps build the public trust in philanthropic institutions. Institutional grantmakers should take valuable lessons from such foundations’ work on diversity and their willingness to share information openly.

Notably, many grantmakers require their grantees to provide demographic data on staff, including executive leadership and sometimes boards and constituents. Just as the heterogeneity of the foundation world compels accountability to be repositioned without a “one-size fits all” approach, grantee and constituent diversity must be considered variable, subject to local context and non-uniform. Further, if a foundation believes that grantee diversity disclosure is relevant information to inform board decision-making, the same criterion should apply to foundation disclosure of diversity data. As Lori Villarosa, director of the Philanthropic Initiative for Racial Equity, stated in the wake of the debates surrounding AB 624, “Some people … have been raising issues of philanthropic diversity and inclusiveness as if such calls were new. But these concerns, in fact, have been acknowledged in philanthropic circles for at least three decades.”303 This is an important reminder that diversity is not a new concept for grantmakers; rather, it is a dynamic and salient issue that relates directly to a foundation’s own effectiveness. Moreover, it underscores that diversity should be valued and contextualized in the framework of authentic inclusion.

Some foundations have made notable voluntary efforts to share information publicly. Yet, too few
foundations engage in real transparency, leading to questions about whether the tax subsidy is being used appropriately. Rigorous self-regulation is valuable for strengthening the public trust in institutional philanthropy and ensuring that grantmakers can withstand any level of scrutiny from the IRS and the public. Sharing significant and relevant information freely is a necessary step. At a minimum, an exemplary grantmaking institution demonstrates transparency and accountability by sharing a range of information including but not limited to:

a. Information about the policies it maintains that promote ethical behavior;
b. Demographic data on its trustees, staff, grantees and the intended beneficiaries of its grants;
c. Information about whether or how it is using its assets in non-grantmaking ways that support its mission;
d. Information about the types of grants it provides; and,
e. Useful information for grant seekers about priorities and application procedures.

By voluntarily disclosing this information freely, an exemplary grantmaker demonstrates that it is an ethical steward of the partially public dollars with which it is entrusted.

Information that should be voluntarily disclosed
Grantmakers should make comprehensive information about their charitable contributions, governance and management policies publicly available. They also should disclose relevant information about aspects of their other operations to demonstrate substantive accountability. In keeping with the IRS’s guidelines for nonprofits, complete and accurate financial statements and accounting reports should be posted on a foundation’s web site and made publicly available upon request. Many foundations already do this, but gauging whether an individual foundation implements these policies is a daunting task in the absence of centralized data.

The issue of disclosing demographic data on trustees, staff and grantees is addressed earlier in this chapter under board composition. However, recently, the question of who benefits from philanthropy has received substantial attention. In response to the debate sparked by AB 624, the Foundation Center worked with three California regional associations of grantmakers to analyze how much of the state’s philanthropic giving benefits communities of color. The report analyzed domestic giving from 1996 to 2005 and found variable trends for giving to benefit the economically disadvantaged and racial or ethnic minorities. Giving that is intended to benefit marginalized groups, broadly defined, is discussed in-depth in Chapter I of this book. The salient point for disclosure however, is that studies like the one referenced above fill a void in sector-wide knowledge about who institutional philanthropy seeks to benefit.

In the absence of comprehensive disclosure, there is no way to assess whether a funder is making appropriate use of the generous tax subsidies afforded it or if it is advancing elite interests via patronage grants.

The 990 PF form requires disclosure of the top two program-related investments (PRI) that a foundation makes, and the balance of PRI monies are reported in the aggregate. These usually are below-market loans made to grantee organizations and count toward the qualifying distribution requirement. Beyond this, there are no publicly available data on if and how a foundation is leveraging its assets in ways that support its mission. An increasing number of funders engage in mission investing, a strategy discussed in Chapter IV that seeks both a financial and social return, but there is little publicly available data on this. NCRP encourages those grantmakers who do screen their investments, engage in shareholder activism or seek out proactive mission investments to make such information publicly accessible.

The Foundation Center tracks data on nearly all U.S. grantmakers; it also tracks and analyzes detailed information for more than 1,200 large foundations. A crucial component of the Foundation Center’s data collection is the information it gathers on the types of support a foundation provides. Data include information on the proportion of monies granted for direct services, general operating support, continuous funding, leadership development and capacity building, among others. These data allow for closer scrutiny of foundation financial priorities and are the only information available outside of the 990 PF forms that the public, grantees, watchdogs and the media can use to look at private foundations. They also provide grant seekers with valuable information on which grantmakers to approach when looking for particular types of support. There are many benefits to demonstrating transparency through increased disclosure of the types of grants a foundation provides. Some criticize
the inherent bias of self-reported data, but two important caveats about the Foundation Center apply: the data are verified against financial records for accuracy, and until such time as more disclosure is mandated, this is an interim step to rebuild the public trust in institutional philanthropy. Finally, foundations themselves can benefit by participating in such voluntary reporting, allowing institutions to assess their own behavior against similarly endowed counterparts to gauge their own effectiveness and policies.

Grant seekers currently can look to specific grantmakers, and to databases such as the ones maintained by the Foundation Center and GuideStar, to find information about what a particular foundation requires to consider a grant application. A recent report by a collaborative of foundations and nonprofits identified variable application procedures as a serious impediment to grantee and funder effectiveness and efficiency.306 While this may seem obvious, a foundation also should make its application procedures easily available to grant seekers and the public. This will result in efficiency gains for both parties and further demonstrate ethical stewardship. Grantees often are frustrated by how challenging it is to determine the priorities and procedures of various grantmakers.

Securing anonymous feedback

Third party or neutral external actors often can help foundations elicit the needed anonymous feedback on their performance. Independent consultants present funders with an opportunity to get authentic feedback that is not euphemized because of the threat of lost funding. An important issue that arises in working with independent consultants is where the costs to cover this expense should come from. Because this feedback offers significant improvements for decision-making, foundations should consider seriously whether anonymous feedback should be viewed as a fixed cost in institutional philanthropy.

Some institutional grantmakers already engage in this exemplary practice; for example, the David & Lucile Packard Foundation solicits confidential grantee feedback, which can be provided anonymously or non-anonymously.307 The foundation also makes its Grantee Perception Report, a grantee survey tool developed by the Center for Effective Philanthropy (CEP) to help foundations secure grantee feedback, publicly available on its web site. The James Irvine Foundation also makes the findings of its CEP assessment publicly available on its web site and has an online form for non-anonymous feedback.308 Many foundations that have commissioned CEP to conduct these assessments make their findings publicly available.309 This is a good grantmaker practice of demonstrating accountability and transparency publicly, especially when the results not always are positive.

The Kresge Foundation commissioned CEP to conduct their analysis for grantees and applicants. The findings indicated that Kresge was ranked by survey respondents at or below the 25th percentile on five of CEP's eleven main indicators, including community impact and grantee satisfaction. In response, Kresge president Rip Rapson issued an open letter to the community, noting that while he was disappointed with the report's findings, that he "wanted our partners to help us serve them better. This is the only way we will realize our desire to innovate and improve the bedrock conditions and long-term opportunities for individuals, families and communities in need."310 Not only does Kresge provide public access to its survey, the foundation developed a multi-year transition guided by nine core values in expanding its grantmaking. As the foundation states on its web site, “We believe we have a moral obligation to recalibrate our grantmaking by elevating the values that have quietly guided us for more than 80 years. In doing so, we hope to contribute more meaningfully to those organizations that most directly advance these values.”311 By incorporating critical feedback in its decision-making, this institutional grantmaker demonstrates responsiveness to external feedback and exemplary stewardship.

Arthur Schmidt, founder of GuideStar, notes that CEP has made a significant contribution to the field by offering its Grantee Perception Report as a tool for institutional grantmakers to solicit anonymous grantee feedback. Yet, Schmidt highlights the tool’s limitations because foundations only participate voluntarily and there are significant costs associated with contracting out this work. Like NCRP, Schmidt believes that public disclosure of these reports has sector-wide benefits but that “until the candid views of grantees toward foundation grantmakers are gathered and revealed publicly, the model has limited utility.”312 In sum, exemplary philanthropy solicits authentic grantee feedback, uses that information to inform its decision-making, and is open and transparent about the findings.
Publicly disclosing “failures” is one final area that merits specific attention. As James E. Canales, CEO of the James Irvine Foundation, said, “Given the emphasis in foundations these days on communication, transparency and accountability, it just seems to me that you aren’t going to be credible if all you talk about is your successes.” The Hewlett and Irvine Foundations each made publicly available reports that documented problems encountered during program implementation. Moreover, both foundations shared this information with the New York Times, allowing broad public access to this information. These two foundations demonstrate exemplary voluntary disclosure of relevant information and the importance of substantive accountability and transparency.

CONCLUSION: SETTING THE BAR FOR PHILANTHROPY AT ITS BEST
As this chapter demonstrated, the partly public nature of foundation dollars makes it incumbent on institutional grantmakers to behave as ethical stewards of the monies with which they are entrusted. The board of a grantmaking institution ultimately is responsible for ensuring legal and regulatory compliance, transparency, accountability and maintenance of policies that promote ethical behavior. Because of the lack of centralized or comprehensive data cited throughout this chapter, it is not possible to determine the proportion of foundations that employ these practices. Yet, some exemplary foundations already do follow these policies and practices, as documented throughout. Based on the analysis presented in this chapter, NCRP advocates that all foundations adopt and implement the three fair and reasonable measures that increase the likelihood of a foundation acting as an ethical steward. As more grantmakers adopt the measures described in this chapter, the social benefit of philanthropy will be maximized and the public trust in institutional grantmaking will be rebuilt.
Criterion III: Ethics

A grantmaker practicing Philanthropy at Its Best serves the public good by demonstrating accountability and transparency to the public, its grantees and constituents.

a) Maintains an engaged board of at least five people who include among them a diversity of perspectives—including of the communities it serves—and who serve without compensation

b) Maintains policies and practices that support ethical behavior

c) Discloses information freely

DISCUSSION QUESTIONS

NCRP encourages staff and trustees of foundations and other grantmakers to engage in serious discussions about each criterion and the chapter that elaborates on the criterion. Sample discussion questions are provided here to help get you started.

> Which parts of the chapter did you like the most? Why?

> Which parts did you like the least? Why?

> Is it important to demonstrate accountability and transparency? Why or why not? How and when did we reach this decision? How often do we review our policies regarding these issues?

> Do we feel that the size and diversity of our board could improve? If so, in what ways? If not, what are the barriers to us doing so? Have we considered including the grantee perspective on our board? How do we define diversity?

> How did we establish the compensation policy we have in place for trustees? Why? If we don’t compensate trustees, are we ensuring that there’s no self-dealing or providing other non-monetary forms of compensation? If yes, how did we determine this is appropriate?

> What policies and practices do we have in place to support ethical behavior? How did we establish our conflict of interest policy? Our whistleblower policy? Who is ensuring compliance with these? How do we set executive compensation? Should we consider adopting new policies, following our current policies more closely or revising our policies to align more with funders with comparable assets and missions?

> What information do we disclose freely to the public? Is that enough? How did we determine that this level of disclosure is appropriate? Do we share demographic information about our board, staff and grantees? Do we have ways to ensure we get authentic feedback? Why or why not?

> What else from this chapter should inform our current grantmaking priorities?

> If we want to make any changes based on this discussion, what will need to happen in order to make those changes? What are the next steps?
NOTES FOR CHAPTER III: ETHICS

218. He was president of the Minneapolis Foundation when this was written. Quoted in: Emmett D. Carson “A Worst Case Scenario or the Perfect Storm? Current Challenges to Foundation Board Governance,” Responsive Philanthropy, (Summer 2003).


224. Ibid. Adapted from p. 3.


226. Only private foundations must file a 990 PF form while other grantmakers such as community foundations file the same 990 form as do grantees organizations, leading to variable disclosures among institutional grantmakers.


231. Mark Pacella, testimony before the United States Senate Committee on Finance Hearing on Charity Oversight and Reform: Keeping Bad Things from Happening to Good Charities, June 22, 2004.


239. Ibid.


241. Ibid., pp. 19–20

242. Ibid.; Women comprised a total of 75.8 percent of all foundation staff.; 74 percent of program officers and 51.5 percent of CEOs in 2006.

243. Ibid. p. 21


249. The National Committee for Responsive Philanthropy, The
Core of the Matter: NCRP's First Convening on the Need to
Increase Nonprofit Core Operating Support, June 4, 2003
(Washington, D.C.: National Committee for Responsive
Philanthropy, July 21 2003), 11.

250. Grantmakers for Effective Organizations. Grantmaking
Practices that Support Grantee Success: Survey Report
(Washington, D.C.: Grantmakers for Effective Organizations,
2008), 31–32.


252. Sandi Doughton. “Not many speak their mind to the Gates

253. Ibid.

254. Ibid. See also http://gateskeepers.civilblog.org/, a watchdog
group that monitors the Gates Foundation’s activities.


258. Quoted in William A. Schambra. “Board Compensation: To Pay
or Not to Pay?” Philanthropy Roundtable (January/February

259. Ibid.


262. Beth Healy et al. “Some officers of charities steer assets to

263. Ibid.

264. The Internal Revenue Service. Applying for 501 (c) (3) Tax-

265. Patrick Lakamp and Mary B. Pasciak. “Why does it go to
much to give Money away? A few foundations spend almost
as much on expenses as they do on grants,” The Buffalo News,
story/530961.html

266. Ibid.

Operations & Management Survey: The tool for small founda-
tion benchmarking (Washington, D.C.: The Association of
Small Foundations, 2007), p. 31. The report notes that these
cost ratios would earn most ASF members “a perfect ten rat-
ing” using Charity Navigator’s metrics. Survey respondents
included more than 950 of ASF’s 3,145 members.

268. See Schambra, Op Cit.

269. Elizabeth Boris et al. What Drives Foundation Expenses &
Compensation? Results of a Three-Year Study (Washington,
D.C.: The Urban Institute, 2008), 56.

270. Ibid, p. 55.


274. Schambra, Op. Cit., p. 3

275. Eisenberg et al., 2003 Op Cit. p: 21; See also Table 1 of this
publication for trustee fees in the sample. Because of the lack
of centralized data, there are likely many more foundations
that do not compensate trustees. The list of foundations cited
here is simply illustrative, demonstrating that regardless of
foundation size, some grantmakers already engage in this
exemplary practice.


277. Steven T. Miller, “Remarks before the Georgetown Law Center
Seminar on Issues in Nonprofit Governance,” speech,
Georgetown University Law Center, Washington, D.C., April


280. Randy Kennedy and Carol Vogel, “Executive Severance Is a

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in December 2005; membership was restored in mid-April
2006, contingent on the trust providing the council with infor-
mation regarding management and governance practices. The
trust’s web site states that it ‘strengthened’ its conflict of inter-
est policies as part of this process. J. Paul Getty Trust, “J. Paul
Getty Trust Membership Status in Council on Foundations
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ter/council_on_foundations_release041706.html.


283. Noelle Barton and Ben Gose. “Executive Pay Outpaces

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The Nonprofit Times, March 1, 2002.

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Nation: Agency’s probe of pension scandal spurs warning to
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292. Ibid.

293. See: The California Endowment. “About Us: Striving to Set the
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