

Boston Business Journal

EXCLUSIVE REPORTS

From the February 27, 2004 print edition

AG mulling Sarbanes-like rules for state nonprofits

Tom Witkowski and Jill Lerner
Journal Staff

Nonprofit organizations may soon face the same scrutiny felt by public companies and their boards in the wake of Sarbanes-Oxley regulations: The Massachusetts attorney general's office is floating ideas for additional rules for the governance of the state's nonprofits.

No specific legislation has been offered, but a summary of the draft being circulated, if voted into law, would mandate changes akin to those permeating the for-profit world today. The attorney general's office is now seeking input from the charitable sector on its proposals.

Observers, while supporting the AG's goal of executive and fiscal responsibility, worry that, at best, more stringent demands are unnecessary for the majority of nonprofits and, at worst, will be fiscally burdensome to small organizations when many are struggling to stay afloat.

"What we're trying to do is help charities strengthen their policies and practices with regard to financial matters, with regard to reporting to the public and to the regulatory agencies," said Jamie Katz, assistant attorney general.

Charity officers would have to certify financial statements, according to the draft of the act to promote financial integrity of public charities. Charities would also need internal financial controls and procedures, as well as independent audit committees and whistleblower policies.

"The concern you would have is, you create a much more extensive and overbearing reporting mechanism for the majority of nonprofits, who do business correctly," said Ron Ancrum, president of Boston-based Associated Grant Makers, a trade group for nonprofits.

"Many nonprofits are already stretched thin. They don't have the benefit of the resources of for-profit firms to take on the additional accounting work or to pay for additional staff labor to fill out reports," he said.

The attorney general's proposal does take into account the costs of the regulations. The minimum annual revenue threshold for filing audited financials would be raised from \$250,000 under current rules to \$750,000. Only those groups above the \$750,000

threshold would have to put internal financial controls in place, have audit committees made up of independent directors and have a whistleblower policy, for example.

"We want charities to have a strong system in place so they operate better, so they bring strong confidence to the sector. We believe, on balance, this will help more charities than it's going to hurt," said Katz.

Although the nonprofit world has not seen nearly the scope of criminal activity and corporate fraud appearing in daily headlines about the for-profit sector, local problems have been found. The attorney general's office shut down one Chelsea-based nonprofit last year because of excessive compensation of officers and other abuses, said Katz. Increased regulation of nonprofits and their boards is long overdue, said Hal Shear, president of Boston-based Board Assets Inc., a corporate-governance advisory service for boards of directors. Shear is also a senior adviser to the National Association of Corporate Directors.

"Many (nonprofits) run like a company, but they have boards that are not value-added boards," Shear said.

Charities face the same financial issues with which corporations are now dealing, though under a much brighter spotlight, he said.

"The ones that see the need for this have been aggressive from the beginning, doing board evaluations, job descriptions for directors, thinking about strategy, looking at independence of audit committees, worrying about financial controls," Shear said.

Similar regulations are being proposed by state attorneys general outside of Massachusetts as well, said Allen Grossman, a professor of nonprofit management at the Harvard Business School. If the attorney general's office includes nonprofit leaders and law enforcement officials in the drafting of the legislation, the result could help the sector, he said.

Having board members and executives verify financials, a key to the Sarbanes-Oxley Act, could work with nonprofits too, he said. "Some form of that -- you bet I'm in favor of that," said Grossman.

Whistleblowers at the United Way of Massachusetts Bay can now bring an alleged wrongdoing to an ethics officer, a position added in December. The group, with \$55 million in annual revenue, also added steps to its audit process, including having its auditor meet independently with all 15 members of the leadership team. Still, for some of the smaller organizations under the United Way's umbrella, added regulations could be expensive, said chief operating officer Mary Kay Leonard.

"We know it would be a lot harder for a (smaller) organization to comply with some of this," she said.

One critic believes a new law will accomplish little else than burdening charities to pay more accountants and lawyers. "All the abuses and self-dealings and excessive compensation and perks and so on are already covered by existing law," said Roy Hammer, an attorney and partner with Boston-based Hemenway & Barnes.

Hammer is active in charitable organizations and has been a trustee of Jane's Trust and the Jessie B. Cox Charitable Trust. "The problem is not a lack of laws to deal with these offenses, but a lack of ... funding and staffing to enforce existing laws."