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Barrett, Audrey; Deitrick, Laura; Donmoyer, Robert; and Libby, Pat, "2006 INTRODUCTION- Beyond Regulation: Creating Tools for Promoting an Ethical Culture in Nonprofit Organizations" (2006). *Nonprofit Leadership and Capacity Building*. 10.
<https://digital.sandiego.edu/np-npleadership/10>

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**BEYOND REGULATION:
CREATING TOOLS FOR PROMOTING AN
ETHICAL CULTURE IN NONPROFIT ORGANIZATIONS***

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**Presented at the Annual Meeting of the
Association for Research on Nonprofit Organizations and Voluntary Action (ARNOVA)
Chicago, Illinois, November 15-18, 2006**

BEYOND REGULATION: CREATING TOOLS FOR PROMOTING AN ETHICAL CULTURE IN NONPROFIT ORGANIZATIONS

Most people want to do the right thing; they also want to associate with organizations that operate in ethical ways. Ethics are especially important in nonprofit organizations because their mission, more often than not, is to serve others and to help right society's wrongs.

In recent years, however, decisions and behavior that are either clearly unethical or perceived by large segments of the general public to be unethical have tarnished the image of a number of nonprofit organizations and, in the process, the nonprofit sector as a whole. Paul Light, a New York University professor who conducts an annual survey to measure public confidence in the sector, traces the roots of the public's disenchantment with nonprofits to American's perceptions of how the Red Cross handled the contributions it received in the wake of the terrorist attack on 9/11. According to Light, prior to the terrorists attacks, 90 percent of Americans expressed a "great deal or a fair amount of confidence" in charitable organizations. This figure plummeted to 60 percent one year after 9/11 and was found to be only slightly improved, at 69 percent, in 2006. Light further reports that one-half of Americans say charity executives are overpaid and seventy-one percent believe that nonprofits "waste a great deal of time and money."¹

The sort of skepticism alluded to in the previous paragraph has been translated into efforts to increase government regulation and oversight of nonprofit corporations at both the federal and state levels. A bill signed by President Bush on August 17, 2006, for instance, included not only seven incentives to spur charitable giving but also 17 provisions designed to crack down on fiscal abuses.²

Ethical issues extend well beyond the fiscal domain, however, and, often, ethical questions are multi-dimensional and situation-specific. Consequently, most ethical issues cannot be adequately addressed by adopting general rules and regulations that are designed to apply to a wide range of organizational contexts with a wide range of missions. Ethical issues, in short, must be discussed and re-discussed periodically as situations change and organizations adapt to these changes.

This paper describes an effort to move the nonprofit field beyond regulation the regulation approach. The paper describes the process that was employed, the rationale behind the process, the results of the process, and the tools that were created from the results.

The Process

Between December 2005 and May 2006, the University of San Diego's (USD) Center for Applied Nonprofit Research scheduled six breakfast conversations about ethics in the nonprofit sector and invited those who worked in or helped govern nonprofit organizations in the San

¹These results were reported in an article in the August 31, 2006 issue of *The Chronicle of Philanthropy*.

² A summary of the law prepared by the House Ways and Means Committee can be found at www.waysandmeans.house.gov/media/pdf/taxdocs/072806pensionssummary.pdf.

Diego area to participate. One hundred sixty eight individuals attended one or more of these sessions. The group included staff and board members from a range of nonprofit organizations as well as corporate and private philanthropists. The number of participants at individual sessions ranged from a low of 29 to a high of 81. The average number of participants was 49.

Prior to the start of the series of breakfast conversations, USD's Center for Applied Nonprofit Research set the stage for the conversations that would follow by organizing a special event focused on the current regulation-oriented context in which nonprofit organizations must operate. Speakers for this event included: Diana Aviv, President and CEO of Independent Sector; Peter Berns, Executive Director, Standards of Excellence Institute; and Flo Green, Executive Director of the California Association of Nonprofits.

The timing of this presentation came on the heels of a report to Congress prepared at the request of Senator Charles Grassley by the "Panel on the Nonprofit Sector" which had been convened by Diana Aviv in her role as President and CEO of Independent Sector. Consequently, as expected, Ms. Aviv endorsed some degree of federal regulation of the nonprofit sector.

The second panelist, Peter Berns, leads an organization that has dedicated significant time and other resources to developing what is arguably the most comprehensive set of certification standards for nonprofit organizations that currently exist. Not surprisingly, Bern spoke in favor of professional self-regulation through certification process such as the one his organization had in place.

The third panelist, Flo Green, heads up a state-wide nonprofit trade association. Her remarks centered on the obligation of individual nonprofits to regulate themselves and uphold high standards of accountability that exceed what is required by the law. The framework presented in this document most closely aligns with that philosophy as it puts the onus on each individual organization to police itself. It also provides a set of standard operating procedures for accomplishing self-regulation at the individual organization. Specific procedures that could be used to insure that self regulation occurs within an individual nonprofit organizations were not discussed by Ms. Green in her presentations.

Each of the subsequent breakfast conversation sessions focused on a pre-announced ethics-related topic and key questions associated with that topic. The list of topics and related questions can be found in Appendix A. Each session was ninety minutes long; most of that time was devoted to small group discussion. Time also was set aside for representatives from each of the small groups to report on some key ideas from their discussions to the group as a whole. A small amount of time also we spent framing the topic of the day at the start of each session.

The majority of small group discussions and all small group reports to the group as a whole were either video or audio taped. In addition, each small group designated someone to serve as a recorder; the recorder kept notes on the key ideas that emerged during the small group discussion. The notes and tapes from all sessions were analyzed and organized into a list of key ideas and strategies that nonprofit organizations could employ to increase the likelihood that their organizations would operate in an ethical fashion. This list was eventually

reorganized around more general categories and themes that emerged during the analysis process.

The results of the analysis were presented to those who participated in the sessions during an additional meeting in June 2006. This meeting served what researchers refer to as a *member checking* function. That is, the 18 people who attended this meeting indicated what they agreed and disagreed with and also made suggestions about any ideas that needed to be added to the list. Modifications were made in the initial summary of ideas in response to this feedback.

Because the University of San Diego's Center for Applied Nonprofit Research is at least as interested in producing work that is useful to practitioners as it is in writing academic papers like this one, the plan had always been to translate coded and categorized data into a practitioner-friendly product. The initial plan had been for that product to be some sort of ethical framework that nonprofit organizations could either adopt or tailor to their particular organizational needs.

Upon reflection, however, using the data for this purpose did not seem intellectually defensible for a number of reasons: the selection of participants had not been, in any way, systematic; the participants came from only one area within the United States, i.e., San Diego and the surrounding area; and, though the member checking process revealed considerable agreement about the ideas that had surfaced, there was also disagreement about some of the items.

Despite these limitations, however, the group that had generated the data for the analysis had been surprisingly diverse; it had representatives from foundations and charities as well as a wide array of substantive areas (e.g., arts, health, and social service agencies) that make up the nonprofit area; and a wide range of organizational roles (e.g., executives, lower-level employees, board members, etc.) found in third sector organizations also were represented at the breakfast meetings. Even more important was the fact that the ideas generated during the breakfast discussions were thoughtful, surprisingly comprehensive, and, at times, provocative.

In short, even though the ideas generated during the session should not be taken as definitive, they clearly had considerable heuristic value. To state this point another way: The ideas could help sensitize leaders in nonprofit organizations to things that they should think about when considering how to promote ethical behavior in their organizations; they also could help nonprofit decision makers at the organizational level both frame problems and frame discussions geared to solving problems. Interestingly, those who have systematically studied how decision makers use knowledge—for example, Harvard sociologist, Carol Weiss—suggest that this is the way practitioners and policymakers use the results of even the most methodologically sophisticated social science research.

So, we abandoned our initial plan to translate the ideas that emerged during the breakfast conversations into an ethical framework that would prescribe what organizations interested in promoting ethical action should do. Instead, we began to think of tools that would have a heuristic function within the organization. The findings and tools will be discussed in the next sections.

Results

For the most part, the ideas that emerged from the breakfast session—and that were vetted during the additional member checking meeting described above—fell into six broad categories³: education and training, governance, promoting transparency, establishing checks and balances, utilizing data-driven decision-making, and creating an ethics-oriented organizational culture.⁴ Each of these categories will be discussed briefly below.

Education and Training

Participants identified numerous stakeholders that they believed would benefit from further education and training. The list included: the general public, funders, board members, and staff. Not surprisingly, the list of issues people believed needed to be communicated during education/training sessions included such things as how to read a budget and board members' fiduciary responsibilities. Many participants were especially concerned that procedures be put in place to bring new board members "up to speed" on the fiscal aspects of their organizations.

Participants, however, also raised less obvious content that they believed education and training sessions should focus on. A number of participants articulated the belief that well-established beliefs and customary practices within the sector needed to be reconsidered and reframed and they saw education and training as the vehicles for doing this. Specifically, some participants endorsed making the following ideas a part of the education and training process:

- Nonprofits have a means and the rights (within established legal boundaries) to advocate on behalf of the populations they serve and on behalf of the nonprofit sector.
- Leveraging administration costs to the bare minimum is not ethical.
- Adequate training and compensation of nonprofit employees is essential to providing quality services.
- There are costs associated with using a volunteer workforce.
- Disparity in pay between the highest and lowest positions in the organization should not be the same as in the for profit sector.

³ Interestingly, many of our categories corresponded with those used by the Standards of Excellent Institute for their certification process.

⁴ There also was a seventh category that might be labeled *employment*, but many of the ideas that fit into this category were not endorsed by the group as a whole. Indeed, some ideas in this category even conflict with each other. The list of ideas includes the following: (a) Nonprofits should have salary ranges available as public information. (Options for disclosure include clustering, ranges, departmental type, position type, blended rates.) (b) Nonprofits should utilize benchmark standards such as California or national surveys to set rates of pay. (c) Disclosure of staff salaries is positive, makes people more honest, and may heighten awareness of any disparity between nonprofit and for-profit employees. (d) Mandated salary disclosure may place an undue burden on smaller nonprofits. (e) Minimize disparity between pay rates for executive director and staff positions. (f) Reveal and practice transparency regarding benefits, especially any "hidden" benefits i.e. housing, travel, and other perks. (g) Health insurance should be a part of nonprofit employee benefits. (h) Create a culture within the sector that does not tolerate under-employment of its members.

Governance

Not surprisingly, a nonprofit's system of governance was touted as a method for promoting ethical behavior within the organization. Many of the specific ideas that fell under this category were predictable; others, however, were somewhat novel. Some of the novel suggestions, we suspect, might even be judged unworkable and/or undesirable in certain settings. (Note: Our subsequent field testing of the tools we developed to guide ethics discussions within organizations have confirmed that this suspicion was correct, and that, consequently, the decision to use the information being reported here heuristically rather than prescriptively was, indeed, a wise one.) The vetted list of governance-related ideas included the following:

- Identify who on the board is responsible for ethics. (Appoint an ethics point person, in other words.)
- Have detailed and accurate board job descriptions.
- Provide board members with vital meeting information in advance of meetings. Include a complete set of financials each month accompanied by the information from the same month during the previous year, and budgeted numbers.
- Utilize the Board retreat and/or annual planning sessions as a time to discuss ethics and provide refresher training.
- Conduct Board evaluations.
- Have your financial auditor present all findings directly to Board.
- Board members should sign a commitment agreement prior to joining the Board which states responsibility to resign if not meeting Board duties, donations, etc. This provides a graceful exit when needed and/or reaffirms Board member's commitment to the organization. This may be reviewed annually.
- Develop policy that establishes the circumstances in which—and guides the process by which—a Board member can become a paid employee

Promoting Transparency

Although some early comments by participants suggested that transparency should be viewed as an unqualified good, over the course of the breakfast meetings, conversations about transparency became more nuanced, and costs as well as benefits were discussed. In the end, most participants appeared to agree that *transparency* does not mean a free-for-all sharing of every aspect of organizational life. Rather, it refers to a thoughtful disclosure of as much information as possible without putting the organization at a competitive disadvantage in such matters as retaining staff or in competitions with other organization for limited resources within a region. Specific vetted ideas that surfaced about promoting transparency included the following:

- Internet/Websites can be used effectively to enhance an organization's transparency. It is easy to post your 990's to your organization website, just post a link to the state AG's charity or to GuideStar. Donors can quickly see your tax returns.
- Websites should provide clear contact information for staff.
- Program evaluations, Board meeting minutes, and annual reports should be available to the public. (Organizations should consider posting these on the organization's website.)

Establishing Checks and Balances

The ideas that fit comfortably under the establishing-checks-and-balances category seemed relatively congruent with a regulation-oriented approach to promoting ethical behavior in nonprofit organizations. This is hardly surprising since many of the ideas related to the fiscal management of an organization, and fiscal management virtually requires a bit of a regulatory mindset. The ideas in this category that survived the member checking process included the following:

- Do not allow one person to become the sole keeper of the organization's fiscal knowledge.
- Maintain at least one financial expert on the board.
- Understand and follow the law.
- Develop and implement conflict of interest policies with clearly defined steps to resolve potential conflicts.
- Implement detailed and understandable nepotism policies.

Utilize Data-Driven Decision-Making

Some participants argued that the concept of ethical action encompassed the notion that an organization needed to utilize its resources wisely by adopting established best practices and constantly monitoring the impact of the practices it had adopted in the past. This logic, in turn, led to the argument that decisions needed to be based on research and the results of evaluation. Some participants, for instance, lamented the fact that evaluations conducted within nonprofit organizations are little more than procedural displays conducted to comply with a funders' requirements. Some participants argued that truly ethical organizations take research and evaluation results seriously, and other members of the group eventually endorsed this line of thinking.

The ideas below are specific ideas that fit under the utilizing-data-driven-decision-making category:

- Utilize best practice research when designing programs and policies.

- Duplicating services wastes important resources. Complete thorough needs assessments in areas where programming or funding is being considered. (i.e. gap analysis of programs and services).
- Feedback/constructive criticism from funders regarding denial of a grant application is important to organizations. A way for nonprofits to receive this information needs to be devised. And those who receive this information must signal to the funders that provide this information that they are not defensive and want to learn from their failures.

Creating an Ethics-Oriented Organizational Culture

The final category to be discussed here involves the building of organizational culture. The culture-building label may seem a bit odd to those accustomed to thinking of culture exclusively in ethnic (e.g., Mexican American, African American) and/or nationalistic (e.g., French culture, American culture, etc.) terms. Those who study organizations, however, have demonstrated that all formal and informal groups have cultural elements. These elements include shared beliefs, informal (and, at times, even unconscious) organizational norms, and established standard operating procedures. *The way we do things around here* is one scholar's commonsensical definition of organizational culture.

Given the framing of the questions being discussed during the breakfast conversation and the announced intention of the breakfast conversation sessions to move the discussion of ethics in the nonprofit sector "beyond regulation," it should come as no surprise that we consider this sixth and final category to be exceedingly important. Indeed, we concluded that it represents an alternative to the regulation-based bureaucratic approach to promoting ethical action in nonprofit organizations.

There are, in fact, two strategies that organizations can use to influence their members. The bureaucratic strategy relies on rules and regulations, along with rewards and sanctions doled out on the basis of whether or not established rules and regulations have been adhered to. Obviously, this approach requires careful monitoring of employees to determine who has and who has not complied with stated expectation.

The cultural strategy, on the other hand, relies on socialization into an organization's belief system and its standard operating procedures. Constant monitoring is not required because, once socialization has taken hold, employees will simply "do the right thing."

Many—though certainly not all—of the ideas that were placed under the five other categories evidence a cultural as opposed to a bureaucratic orientation, and we ended up using this category as an overarching category when translating the findings being discussed in this section into tools that organizations can use to promote ethical decision making and action. The comments that were originally placed under the discrete creating-culture category during data analysis include the following:

- Embrace (and do not fear) transparency.

- Be proactive about ethics.
- Make decisions that are guided by the organization's mission.
- Regard the letter of the law as a minimum operating standard. "*We should always strive to exceed the minimum requirements.*"
- Be a learning environment where mistakes are not covered up, but are used to build the organization's knowledge base.
- Recognize that all decisions may not lend themselves to complete transparency, but the process by which decisions are made should always be clear and transparent.
- Have clearly defined Board and staff procedures.
- Promote a high level of trust throughout the organization.
- Create an environment that encourages dialog and feedback.
- Be willing to turn down gifts or grants when the cost of accepting the gift or implementing the funding as a program outweighs the amount of the award.
- Reject money that is tainted or when the funding is off-mission.

Translating Results Into Tools for Analyzing and Enhancing the Ethical Dimensions of Organizational Culture

Three tools were created from the ideas generated during the breakfast conversations and the analysis of these ideas described in the previous section. As has already been suggested, the final category focused on culture became the organizing concept in each of the tools.

The first tool that was developed was a *discussion guide*. We assumed that the discussion guide could be used during board and/or senior staff meetings (a) to explore existing ethical practices within a nonprofit organization (b) reach a common understanding about the ethical culture that participants wish to see in action and (c) uncover any discrepancies that currently might exist between what is currently happening and what people engaged in the conversation believe ought to be happening.

After we had completed a draft of the discussion guide, we realized that, in larger organizations, many people would not be able to participate in the discussion. This realization led to the development of a second tool: a *cultural survey*. We assumed that this second tool would be used in conjunction with the discussion guide to gauge whether those at the top of the organizational hierarchy and those at other levels shared a common perception of ethical practices in the organization. We imagined, in other words, that the survey would be a source of data—a kind of reality check—in the discussions that board and/or senior staff members were engaged in.

Finally, we realized that both the discussion guide and the survey were probably not applicable to certain smaller organizations that had never discussed ethics. This sort of group probably needed a more basic tool: a template that would help Board and/or staff members develop an ethics policy for their organization. Thus, for this sort of group, the data were used to develop what we called an *Ethics Policy Template*, even though policy can be seen as a method for promoting regulation rather than a method for moving beyond the regulatory mentality.

The second and third tools are still in the development stage. The discussion guide currently is being field tested. A copy of this particular tool can be found in Appendix B. The two other tools, as well as updated versions of the discussion guide found in Appendix B, will be posted on the Center's website (www.sandiego.edu/nonprofit).

Conclusion

Both the bureaucratic and the cultural approaches have their advantages and disadvantages. Consequently, the cultural strategy is best viewed as a supplement to rather than substitute for the rules and regulations (and rewards and sanctions) that are the hallmark of the regulation-oriented bureaucratic approach. Indeed, despite the announced intent of the ethics conversation to move the discussion of ethics in the third sector "beyond regulation," and despite the use of discussion questions during the breakfast conversations that were intended to push conversations beyond a regulatory mindset, some of the ideas that were generated still endorsed a regulatory rather than a culture-building strategy. Even one of the tools that were developed from the ideas generated during the breakfast conversations might be viewed as embracing more of a regulatory rather than a culture-building stance. The other two tools, however, clearly are designed to facilitate the analysis and building of an organizational culture that is likely to encourage and promote ethical action by an organization's employees and board.