

Forward Thinking

Governance practices for not-for-profit board members and executives Issue no. 16

Conflicts of interest

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Through their personal affiliations and professional job responsibilities, board members often operate in the same sphere as the not-for-profit organizations they have been entrusted — and have committed — to serve. This arrangement, unsurprisingly, can lead to conflicts of interest. Conflicts of interest are usually viewed negatively but can sometimes be beneficial to an organization. Perhaps a conflict of interest can be better described as a conflict of roles or a potential conflict of fiduciary responsibilities. Conflicts of interest may occur in a variety of forms, including private inurement, nepotism or self-dealing for financial gain. Broadly speaking, conflicts of interest occur when the interests of one's employment responsibilities or personal affiliations directly or indirectly (e.g., through influencing decision-makers) contradict the interests of the organization to which he or she has a duty of loyalty



and stewardship. In general, when one's personal initiatives, desires and interests are elevated over those of the organization one has committed to serve, a conflict of interest arises.

In today's world, we are hearing more and more about conflicts of interest occurring — not only at an organization's board and senior management levels, but at all levels. While most attribute this to the turbulent economic times and financial difficulties experienced by so many, another answer may be a heightened awareness within organizations of the need to educate their employees about the existence of either perceived or real conflicts of interest. The increasing volume of conflicts of interest could be the direct result of the expanded disclosure requirements of the IRS's updated Form 990. Not-for-profit boards and management teams are becoming increasingly knowledgeable about the extent of their organizations' operations, significant vendor relationships, and related parties and other associations. Coupling this broader understanding of an organization's activities with a greater sensitivity to and knowledge of conflicts of interest has led to more robust policies, educational requirements and annual disclosure statements with personal certifications.

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Conflicts of interest (continued)

As stated earlier, while conflicts of interest usually connote something negative, they can sometimes be beneficial to an organization. For example, a board member's employer may be able to provide goods or services of a higher quality at a lower price than an unrelated party. But even in that instance, certain safeguards need to be in place. An adequate process must be used to evaluate whether a transaction or relationship that involves a member of the board or management is in the best interests of the organization. When a conflict of interest is reported or identified, it should be brought to the attention of the appropriate committee of the board for discussion and evaluation. In most cases, the audit committee is the appropriate body to receive the report. In addition, such matters should be brought periodically to the attention of the full board for their edification. Those individuals who are connected with the conflict of interest (conflict of roles) should recuse themselves — or abstain — from any discussion or vote on the perceived conflict of interest. The board or committee must assess the conflict of interest to see whether it is in the best interests of the organization, the alternatives that exist, and the ultimate resolution or decision. The organization's board or committee minutes should document the discussion and assessment of the conflict, the relevant personnel involved, and the decision(s) reached.

Conflicts of interest in their most extreme sense, when unreported, potentially expose an organization to several risks, the most significant of which is reputational. Further,

conflicts of interest resulting from private inurement could undermine an organization's strategic initiatives and its ability to deliver its services to the constituency its mission is designed to serve. Private inurement can result in significant regulatory issues with the IRS and state agencies.

Best-practice recommendations to ensure that your organization is properly safeguarded from the potentially negative implications of conflicts of interest include:

- establishing or re-examining your existing conflict-of-interest policy statements to ensure compliance with the most recent intermediate sanctions regulations;
- implementing an annual reporting and certification process for members of the board and senior management;
- developing a process to accumulate, track and report conflicts of interest;
- bolstering your code of ethics and conduct policies to reinforce the organization's views about perceived and real conflicts of interest, emphasizing that board members' principal fiduciary responsibility is to the organization;
- continuing to educate organizational personnel about how to identify conflicts of interest; and
- providing a mechanism for individuals to self-report conflicts of interest as well as to report potential or actual conflicts of interest by others within the organization. •



About the author

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