



Venable Model Nonprofit Governance Policies

Fall 2008 – Updated to Reflect the New Form 990

After months of deliberation and public comment, guided by the principles of “transparency, compliance, and burden minimization,” the Internal Revenue Service (“IRS”) has released a dramatically redesigned Form 990. Although the 2008 Form 990 allows tax-exempt organizations to better describe their activities and contributions to the community, it also requires significantly more disclosure than it ever has before.

In many respects, the most far-reaching changes to the Form 990 appear in Part VI of the Core Form, *Governance, Management, and Disclosure*. Section A of Part VI requires an organization to describe aspects of its internal governance: the composition of its board, the delegation of certain management responsibilities, and the rights of its members. Section B of Part VI asks, in almost checklist fashion, whether or not an organization has certain written policies in place. Specifically, the IRS is inquiring whether a tax-exempt entity has a conflict of interest policy, a whistleblower protection policy, a document retention and destruction policy, a policy for setting the compensation of key employees, and a policy to govern joint ventures with taxable entities. Part VI also asks whether or not the board of directors has reviewed the Form 990 before it is filed.

It should be noted that, while applicable nonprofit corporation laws in various states are continually being revised, often with the imposition of new obligations and restrictions, we are not aware of any state or federal statute that broadly requires nonprofit corporations to implement all of the above policies or actions. Nonetheless, it has become increasingly clear that adopting and implementing these policies is an accepted “best practice” within the nonprofit community. As such, even without affirmative statutory requirements, having such policies in place may soon be part of the prevailing common law standard of care for nonprofit organization governance. Further, given the close attention paid to organizations’ Forms 990 by the IRS, watchdog groups, and others, an indication that such governance policies have not been implemented may increase the risk of public complaints and/or IRS examination.

We have drafted this set of model policies with a few basic objectives in mind. First and foremost, we want your organization to be prepared when it files its next Form 990. These forms are designed to help you gather the information you need to describe your organization with accuracy and confidence. By adopting the policies by the end of your taxable year—as early as December 31 for many organizations—you will be positioned to answer “yes” to several key questions in Part VI.

Second, we recognize that there is no one best approach to any of these policies. Rather than adopting these model documents word for word, treat them as blueprints and craft a set of policies that fits the size and scope of your particular organization. We often provide you with more than one version of the same policy to help you with this task. Note particularly that, given the vast differences among statutes and regulations in the states, it is impossible for us to provide an effective “model” document retention policy. As such, we provide only a very brief statement regarding records retention responsibilities that will suffice for an organization to check “yes” in response to the applicable Form 990 question. We do not provide a model schedule or detailed policy in this regard. Note also that some of the attached policies may refer to an executive committee or an audit committee. We recognize that many nonprofit organizations may not have such committees, and the policies provided would need to be revised accordingly in such situations.

Finally, we hope that these documents lay the groundwork for year-round practices that strengthen and protect your organization well beyond the scope of annual reporting requirements. Simply adopting these policies as you find them may satisfy the narrow goal of being able to check the “yes” box on the IRS Form 990, but that alone affords little security in the long run. In fact, failure to enforce a written policy may cause your organization to be worse off than had it never adopted the policy at all. Use this period of adjustment to the new Form 990 to your



advantage. Implement new policies to encourage candor and transparency, and revisit old policies that may prevent your organization from putting its best face forward. Good governance need not be overly burdensome or complicated, but it does take some thought.

As always, please let us at Venable know how we may be of assistance.

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Conflict of Interest Policy

Conflicts of interest are a central focus of Part VI of the new Form 990. Line 1b of Part VI asks for the number of “independent voting members” of an organization’s governing board, and requires that an organization make a “reasonable” effort to determine any financial material benefit that might flow to board members and their families. Line 2 requires disclosure of any business or family relationships between officers, directors, trustees, or key employees. Line 12a asks whether or not an organization has formally adopted a conflict of interest policy. Line 12b asks whether or not an organization requires its leaders to make annual disclosure of potential conflicts. Line 12c asks whether or not an organization “regularly and consistently” monitors and enforces its conflict of interest policy.

Note that simply answering “yes” or “no” to these questions often will not suffice. Your organization is encouraged—and, in some cases, required—to further explain its particular procedure for handling conflicts of interest on Schedule O, *Supplemental Information*. Further, there are additional, more detailed inquiries about transactions with, for example, organization directors, in other sections of the Form 990. The IRS has indicated as part of its Form 990 redesign process that having a robust conflict of interest disclosure and enforcement process is encouraged, as doing so helps to protect against abuse of a tax-exempt organization by directors, officers, or other private interests. An effective conflicts policy allows an organization to collect the necessary information to identify related-party issues before an organization’s board of directors takes a particular action.

Moreover, a well-drafted conflict of interest policy is likely broader in scope than the fiscal focus of the Form 990 instructions would suggest. Instructions to Line 12 state that a conflict of interest arises “when a person in a position of authority over an organization ... may benefit financially from a decision he or she could make in such capacity,” but not in other circumstances “involving a person’s competing or respective duties to the organization to another organization, such as by serving on the boards of both organizations, that do not involve a material financial interest of, or benefit to, such person.” Your organization ought to think beyond the specific needs of Part VI and develop a policy that provides protection from all potential conflicts, not simply those that involve potential material gain.

There are many different ways to address conflicts of interest. Some policies are sparse, deferring in large part to the judgment of the board of directors; others spell out detailed procedures. Some organizations adopt separate policies for directors and employees; others implement one overarching policy for the entire organization and its affiliates. To satisfy the Form 990, however, your conflict of interest policy must have a few core elements. As such, each of three model documents that follow define the term “conflict of interest,” identify the individuals who must adhere to the policy, require an annual disclosure of potential conflicts, and describe a means to resolve such conflicts as they occur.

Note that while conflict of interest policies and disclosure forms traditionally have applied only to organization directors and members of organization committees, the Form 990 asks specifically whether an organization’s officers, directors or trustees, and key employees are required to disclose annually interests that could give rise to conflicts. As such, the sample policies and disclosure forms are designed to apply not only to directors, but also to committee and task force volunteers, officers and key employees. Many organizations may take issue with this sort of approach, and in particular may prefer to keep the requirements for disclosure of potential conflicts of interest for employees separate from disclosure for directors. For instance, many organizations may already require employees to disclose annually potential conflicts of interest as part of their employee handbooks. For the purpose of being able to check “yes” on line 12b of the Form 990, having separate conflict disclosure regimes for volunteer leaders and employees will not present a problem.

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ABC NONPROFIT & ABC FOUNDATION Conflict of Interest Policy

In their capacity as directors, officers, and key employees, the individual leaders of the ABC Nonprofit (“ABC”) and the ABC Foundation (“Foundation”) must act at all times in the best interests of the organizations they represent.

1. What Is a Conflict of Interest?

A conflict of interest may arise in any circumstance that may compromise the ability of a director, officer, or key employee to make unbiased and impartial decisions on behalf of ABC or the Foundation. Such circumstances may involve family relationships, business transactions, professional activities, or personal affiliations.

The Board of Directors of ABC the Board of Directors of the Foundation require all directors, officers, and key employees to complete and submit an annual Statement of Disclosure detailing any facts or circumstances that might constitute a conflict of interest. The Board of Directors further requires directors, officers, and key employees to submit an amended Statement of Disclosure to reflect any material changes or additions to the submitted information that may arise during the course of the year. Officers, directors, and key employees are encouraged to err on the side of disclosure and to report any set of circumstances that may appear to pose a conflict of interest, even if there is uncertainty as to whether such circumstances should be disclosed.

2. How Are Conflicts of Interest Identified?

Each Audit Committee of ABC and the Foundation (“Audit Committee”) will review each Statement of Disclosure for any set of facts or circumstances that may reflect an actual, potential, or apparent conflict of interest. The applicable Audit Committee may request the assistance of legal counsel to identify potential conflicts. When evaluating a particular set of facts or circumstances, the Audit Committee shall consider the following non-exhaustive list of factors that may indicate a conflict of interest:

- Solicitation or acceptance of gifts or other items of value that may create an appearance or expectation of special treatment in ABC or Foundation matters;
- Any incident of abuse or misuse of a leadership position for personal or third-party gain or benefit;
- Situations in which a director, officer, or key employee may be divided between personal interests or the interests of another organization and the best interests of ABC or the Foundation;
- Business, professional, or other activities that would materially and adversely affect ABC or the Foundation, either directly or indirectly; and,
- Any arrangement in which a director, officer, or key employee provides goods or services to ABC or the Foundation as a paid vendor.

The Audit Committee may request additional information from any director, officer, or key employee at any time; however, no individual whose relationships or activities are under review may participate in deliberations, debate, or any vote of the Audit Committee while such review is pending.

3. How Are Conflicts of Interest Resolved?

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If the applicable Audit Committee, the Board of Directors of ABC, or the Board of Directors of the Foundation identifies an actual, potential, or apparent conflict of interest, it may take one of the following actions to resolve such conflict:

- **Waive** the conflict of interest as unlikely to affect the director's, officer's, or key employee's ability to act in the best interests of the organization;
- Determine that the individual director or officer should be **recused** from all deliberation and decision-making related to the particular transaction or relationship that gives rise to the conflict of interest. This course of action should apply particularly when the transaction or relationship is one which presents a conflict only with respect to one or two discrete programs or activities; or
- Determine that the individual director or officer must **resign** from his or her service to ABC or the Foundation. This course of action should apply when the conflict of interest is so pervasive that the director or officer would likely seldom, if ever, be able to act solely in the best interests of the organization.

The Board of Directors of ABC reserves final authority over the resolution of all conflicts of interest involving a director or officer of ABC. Likewise, the Board of Directors of the Foundation reserves final authority over the resolution of all conflicts of interest involving a director or officer of the Foundation. The appropriate Board of Directors may overrule any decision of the Audit Committee with regards to any actual, potential, or apparent conflict of interest, and the Audit Committee may refer any such matter to the Board of Directors at any time.

4. May Directors and Officers Do Business with ABC?

A conflict of interest exists any time a director, officer, or key employee seeks to enter into a business relationship with ABC or the Foundation. Similar conflicts may arise through family members or through organizations in which directors, officers, or key employees serve in a leadership, employment, or ownership capacity.

Such conflicts do not, however, necessarily preclude business relationships with ABC and the Foundation. The following procedure is designed to resolve conflicts of interest whenever a director, officer, key employee, or a related party, seeks to provide goods or services to ABC or the Foundation as a paid vendor, or applies to receive a significant grant or contract from either organization:

- The director, officer, or key employee must promptly disclose the intent to enter into a business relationship with ABC or the Foundation, either to the appropriate Audit Committee, the appropriate Board of Directors, or both.
- The director, officer, or key employee must recuse himself or herself from all deliberation, debate, and voting related to the contemplated business relationship.
- If the value of the transaction exceeds \$5,000, ABC or the Foundation must solicit proposals or applications from a broad range of other qualified candidates for the agreement, contract, or grant under consideration.
- The appropriate Board of Directors must determine, without the presence or participation of the director, officer, or key employee under review, that the transaction is fair and in the best interest of ABC or the Foundation.
- If the appropriate Board of Directors approves the business relationship under consideration, the director, officer, or key employee may not participate in any process by which his or her performance as a vendor, grantee, or recipient is evaluated, or in any such evaluation of a related party.

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The attached Statement of Disclosure shall be completed, signed and submitted annual basis.

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ABC NONPROFIT & ABC FOUNDATION Statement of Disclosure

As a director, officer, or key employee of ABC or the Foundation, I understand that I am obligated to disclose the existence of any facts or circumstances that may constitute a conflict of interest, as the term is defined in the Conflict of Interest Policy above.

- I have the following interests in third parties providing goods and services to ABC or the Foundation:

- I serve in a leadership capacity, have a significant investment, or own at least a one percent interest in the following entities or organizations that may have conflicting interests with those of ABC or the Foundation, or take public positions contrary to those of ABC or the Foundation:

- I expect to receive compensation from ABC or the Foundation in the following amount, not including reimbursement of reasonable expenses:

- The following members of my family expect to receive some form of compensation or material financial benefit from either ABC or the Foundation:

- Outside of my capacity as a director, officer, or key employee of ABC or the Foundation, I have a family relationship or business relationship with the following directors, officers, or key employees of either organization:

- I wish to disclose the following additional facts or circumstances:

I have read the ABC Conflict of Interest Policy in full, and understand that I am required to notify the appropriate Audit Committee, the Board of Directors of ABC, or the Board of Directors of the Foundation in the event of any material change to the answers I have provided in this statement.

Date: _____

Signed: _____

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