

The Regulation Of Non-Profit Organizations

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ABSTRACT

The absence of governmental oversight and regulation of Not-For-Profit corporations has resulted in these entities performing their stated purposes inadequately and inefficiently and has enabled financial indiscretions which have tarnished their reputations. Enhanced oversight and regulation is needed to prevent recurrences of these failures.

Keywords: Non-Profit/Not-For-Profit Regulation; Non-Profit/Not-For-Profit Accountability

THE NATURE OF NOT-FOR-PROFIT ORGANIZATIONS

Although definitions vary slightly from case to case, not-for-profit organizations (NPO's) are generally defined as "associations, charities, and other voluntary organizations formed to further cultural, educational, religious, or public service objectives."¹ According to analysis done by graduate student Kate Luckert, approximately ten percent of income received by NPO's comes from donations, with over 70% of households making contributions to various charities.² One common misconception regarding NPO's is that they do not seek to make a profit. While this is true in the sense that they do not intend on making a profit to be distributed to shareholders as for-profit corporations do, NPO's do hope to make a profit in order to improve programs and secure future standing. Profit generation is allowed and encouraged because increased profits means less reliance on outside funding. The Internal Revenue Code which is one of the governmental regulatory schemes regulating NPO's requires that all profits "go back into the operation of the organization."³ The reasoning behind this requirement is evident when one considers the principal purpose of NPO's which is to aid society. Nearly every NPO has some share of volunteers giving up their time graciously and free of charge. Volunteers range from young to old; one might be an adolescent sentenced to community service or a retired elderly person looking to pass some time. Whatever the case may be, NPO's depend on volunteers to get their mission accomplished because oftentimes the company would not have enough funds to pay a full-time staff.

Also, NPO's are generally funded by donations, endowments, and government funding with most donors focusing on specific projects rather than on the organization as a whole.⁴ This can become problematic if the organization is not currently working on a specific project which has caught the attention of the public. On the other hand a single project may bring in millions of dollars, which demonstrates the volatility of NPO's. Larger, well-known NPO's receive a great deal of donations continuously, while smaller ones can struggle to raise enough money for one small, local project. Either way though, donors, corporations or governments that help fund NPO's do not expect repayment, dividends or equal value returned to them.

NPO's also contain the unique attribute of lack of ownership. These companies do not issue stock to the public and therefore ownership cannot be traded, bought or sold. The "absence of defined ownership interests" again reinforces the fact that money donated does not lead to a particular investor or investors gaining control of the nonprofit.⁵ There is thus no advantage for people who donate more money than others. The lack of ownership leads to an intricate situation when an NPO goes out of business because the assets are not distributed to shareholders as

¹ "Non-profit Organization." Business Dictionary

² Kate Luckert, *Nonprofit Organizations (Definition and Examples)*.

³ Kate Luckert, *Nonprofit Organizations (Definition and Examples)*.

⁴ Paul DiMaggio and Helmut Anheier. "The Sociology of Non-Profit Organizations and Sectors."

⁵ Earl Wilson, Jacqueline Reck, and Susan Kattelus. *Accounting for Governmental & Nonprofit Entities*.

with for-profit corporations. Instead, assets must be directed to another NPO having a similar tax exempt purpose.⁶ For example, if a local New York City branch of the YMCA finds itself unable to continue its operations, it must distribute its assets to nonprofit organizations serving the same purpose. In this particular case, an obvious recipient of the assets would be another branch of the YMCA, or at the very least another NPO that serves the youth of the community. In this way, people who have donated funds to a particular NPO can be assured that their money is generally serving the same purpose for which they originally donated.

Whether an NPO is large or small does not matter when it comes to the one major advantage they have in common – income tax benefits. Overall, nonprofits are income tax exempt (except for their unrelated business activities), a characteristic that clearly distinguishes NPO's from for-profit corporations ("FP's").⁷ This is the most significant advantage of NPO's because without it a tax on income would severely curtail their ability to use profits to help fund operations. For-profit companies are taxed on all types of profits, from business income to investment income. For any such corporation, income taxes can consume a substantial percentage of profits earned. NPO's contrastingly receive significant tax breaks of different types from the different segments of government that they deal with. They are normally exempt from sales, property, and certain employment taxes that state and local governments levy.⁸ The greatest advantage however comes from the federal government, which offers nonprofit's exemption from income taxes. Without such a significant tax liability, such organizations are able to reinvest income towards fulfilling their missions.

The other major tax related advantage of NPO's actually benefits donors more so than the NPO's. Those who donate money to qualified NPO's receive a charitable contribution deduction on their income tax returns.⁹ Thus, a donation that is tax deductible will lower one's taxable income and in turn lower the tax payable. This characteristic greatly benefits NPO's because it provides a further incentive to some donors over and above the gratification of making the donation. NPO's are significantly benefitted in that they receive more donations from people who are looking to gain from the deduction. Some donors might not donate as much if the incentive of a tax deduction was no longer present.

NPO INDISCRETIONS AND RAMIFICATIONS

All of these different rules, exemptions and characteristics make NPO's very unique entities. Since they are formed with the intention of selflessness and are granted many tax benefits to help them carry on their mission they are held to a higher standard than for-profit companies by outside entities including the general public, the media and the government. Those people who donate, and even those who do not, presume that NPO's will be trustworthy in handling the funds they receive and in the use of those funds. Unfortunately such is not always the case and in where questions arise the NPO's find their relationships with society damaged.

Two recent incidents involving the American Red Cross and the United Way illustrate the effect of NPO's losing the faith and trust of the general public and have left them still currently struggling to have their donations reach the levels they once were prior to these occurrences. In recent years they have both come under criticism for a number of reasons including excessive CEO pay, mishandled or lost funds and inefficient disaster relief. A majority of the scandals could have been avoided however if proper, effective regulation was put in place to monitor the activities of the organizations. The preventative regulations would not only have helped avoid the criticism and scrutiny, but would also have saved the time, money and effort that have expended in trying to recover from the negative attention.

The American Red Cross is a "humanitarian organization [that] will provide relief to victims of disaster and help people prevent, prepare for, and respond to emergencies".¹⁰ It is funded by donations, volunteer assistance and government funding. It's total income for 2008 exceeded \$3.2 trillion, of which \$788 million were donations by

⁶ Sandy Deja. "What happens when nonprofits go out of business?"

⁷ Robert Yetman, "Tax-Motivated Expense Allocations by Nonprofit Organizations."

⁸ Earl Wilson, Jacqueline Reck, and Susan Kattelus. *Accounting for Governmental & Nonprofit Entities*.

⁹ Ibid.

¹⁰ "About the Red Cross." *American Red Cross*

private individuals, corporations and foundations.¹¹ Around the world, the American Red Cross supplies lifesaving blood, military support, and disaster relief. The organization and its workers have had a tremendous influence on the world and those in need; they have saved countless lives and improved the standard of living for a large number of communities everywhere. In general, this charity can be considered highly socially responsible because of the number of good things it does for regions throughout the globe.

Despite the overwhelming good the American Red Cross has done, it found itself engulfed in scandal during the aftermath of Hurricane Katrina. The charity found itself under attack by the government, the victims of the hurricane, volunteers and donors. Following the treacherous hurricane, the organization raised over \$1 billion which it claimed would be spent for food, shelter and mental health services. Many people speculated however that more money was raised than was necessary and that the money was not spent properly. According to a *New York Times* article written a few weeks after Hurricane Katrina, victims “complained that the Red Cross [was] reluctant to dispense cash”.¹² In addition, the author referenced the fact that the company only works during the relief stage; not during any time of recovery or rebuilding. The Red Cross senior vice president for preparedness and response, Joe Becker, stated that it would not “give money to other groups that might pick up the recovery effort after the relief stage”.¹³ Donors, victims and the government felt as though the funds were not being properly allocated or reported. Consequentially, members of society became reluctant to donate funds because although the organization claimed that any left over money would be put towards the costs of more low-key disaster relief projects, donors increasingly wanted the money they donated to be traced to a specific effort.

The United Way also felt the effects of public criticism in the decade spanning the early 1990’s to the early 2000’s for various reasons. These involved allegations of excessive CEO pay, questionable spending and outright theft. The organization, which prides itself on coordinating various efforts to achieve the highest level of possible success, was the center of a pay scandal in 1992 when many of its upper level executives were accused of receiving excessive pay and lavish benefits. For example the president of the United Way at the time, William Aramony was accused of receiving over \$463,000 in salary and benefits. Ralph Dickerson, Jr., executive director of the United Way of New York City, resided in a rented apartment costing \$4,700/month paid by his employer.¹⁴ In 2002, the CEO of the United Way National Capital Area, Oral Suer was forced to resign amid allegations that he stole “as much as \$1.5 million from the organization”.¹⁵

During this period the United Way felt the financial effects of these scandals. Donations that had once been at levels nearing \$93 million fell to \$35 million amidst the allegations of financial misconduct.¹⁶ Donors no longer viewed the United Way as trustworthy and therefore held back donations or put them towards other, more stable charities. One of the most significant effects of these scandals was the loss of United Way’s contract to manage the Combined Federal Campaign, which raises money from governmental employees and distributes that money to nonprofit organizations.¹⁷ With the loss of that contract, amounting to nearly \$60 million in revenue, the United Way suffered a severe blow to both its finances and its reputation.¹⁸

Over the past eight years the organization has been working its way back and attempting to regain the trust of the public. Reports and statistics show that donations have recently been on the rise as the United Way has worked to become more transparent with its accounting practices. For example, the United Way located in Washington, D.C. was close to reaching its goal of raising \$40 million in 2007 after an “error-free audit” by an independent accounting firm.¹⁹ According to sources at that location, they have “tightened their finances” and therefore donations have increased because they have successfully responded to stakeholder demands. Had the firm implemented stricter regulations to begin with, then perhaps the scandals that they have spent years trying to recover

¹¹ "BBB Wisegiving Report for American Red Cross." *Better Business Bureau*

¹² Stephanie Strom, and Campbell Robertson. "As Its Coffers Swell, Red Cross Is Criticized on Gulf Coast Response"

¹³ Ibid.

¹⁴ Ibid.

¹⁵ Philip Rucker. "United Way Fundraising Rises After Scandal-Induced Plunge."

¹⁶ Kerry Hall. "United Way of Central Minnesota is Shifting its focus in the Face of the Recession."

¹⁷ "Combined Federal Campaign." *US Office of Personnel Management*

¹⁸ Kerry Hall. "United Way of Central Minnesota is Shifting its focus in the Face of the Recession."

¹⁹ Ibid.

from would not have occurred. During the years following the damage to its reputation, the United Way missed out on millions of dollars in donations that could have made their operations run more efficiently and effectively and in turn millions of dollars that could have been spent to help society and those in need.

CURRENT REGULATIONS

It is critical to look at the current regulations that the government has implemented as a result of these scandals and questionable practices. Such regulations play a large part in how companies maintain and record their finances. Currently, NPO's that meet certain very stringent criteria are classified as 501(c)(3) corporations under the Internal Revenue Code of 1986 ("IRC") so that donations made to them are deductible under IRC section 170.²⁰ These types of organizations receive tax exemptions and donors obtain a tax deduction for contributions to them only if they operate for charitable purposes. If a company is granted tax exempt status from the IRS, it can only consider income directly linked to its tax-exempt purpose as tax free.

NPO's are required to treat income unrelated to their tax exempt purpose much differently. In fact, they must report those earnings as unrelated business income which is taxable. Unrelated business activities result in income "from a trade or business, regularly carried on, that is not substantially related to the charitable, educational, or other purpose that is the basis of the organization's exemption."²¹ Those companies that earn more than \$1000 from such activities are required to file a 990-T form. Some analysts have witnessed a problem with this system however as it appears that corporations may manipulate their finances to garner undeserved tax benefits. For example, Robert J. Yetman explained that NPO's may manipulate their expenses to report heavy losses in their taxable income while showing high profits in tax exempt areas. In this way, income and expenses that cannot be directly classified as either direct or unrelated business income can be put into whichever category yields the best results for the nonprofit.²²

In terms of financial accounting, NPO's are subject to much different regulation than publicly traded companies. For-profits must follow strict guidelines set forth by many different agencies, including the Financial Accounting Standards Board (FASB), whereas only a handful of their guidelines might apply to nonprofits. For example, FASB has published over 150 statements related to accounting procedures and of those, only two apply specifically to NPO organizations.²³ The two that are applicable to NPO's are Nos. 116 and 117 - "Accounting for Contributions Received and Contributions Made," and "Financial Statements of Not-for-Profit Organizations." The first requires that tax exempt organizations record contributions as revenues or gains, not as deferred revenue, which had been a common practice. The rule clearly outlines how to categorize contributions, but it still provides NPO's with a number of choices in terms of stating those contributions. For example, they are allowed to decide how to record past contributions, either retroactively or prospectively. The second, FASB 117, dealt with the financial statements that nonprofit organizations had to prepare. While it clearly outlined which ones must be completed, along with certain totals that had to be reported, it did not specify a format.²⁴ Even with the two FASB statements, NPO's still face significantly less regulation than FP's. The minimal standards and the vague nature of those standards give nonprofits much more flexibility when it comes to financial reporting.

The expenses, costs and expenditures of a nonprofit organization also pose another issue when it comes to accounting procedures. Costs are generally broken down into "allowable" or "unallowable" when an NPO receives a grant or funding from the government. A grant given by the government usually is meant for a specific purpose or research project. For example, a university may be the recipient of a grant that is to be used for stem cell research. The university takes on the responsibility of monitoring costs incurred while conducting the research. To prevent abuse of the fund the government might define which costs are allowable or unallowable, meaning which particular expenses of the university can be covered using the fund. Some of the guidelines are clear-cut and easy to follow, while others of them are vague and imprecise.

²⁰ DiMaggio and Anheier, 140.

²¹ Ibid.

²² Yetman, 299.

²³ Federal Accounting Standards Board, www.fasb.org

²⁴ Martha Benson and Alan Glazer. "Implementing FASB 116 & 117."

The National Endowment for the Arts, which delegates grants to organizations and projects involving the arts, is responsible for keeping track of money provided by the government. In the “Financial Management Guide” given to the agency, Congress outlines which costs are unallowable or may be unallowable. Some of the strictly unallowable expenses include those associated with lobbying and fundraising, fines, and bad debts. These costs are not eligible for reimbursement against the funds available. The government outlines that costs related to entertainment, such as food and lodging, and interest are usually unallowable.²⁵ This terminology reflects the failure of the government to properly regulate NPO’s by making guidelines ambiguous. By leaving important aspects of accounting for such costs unclear the government leaves it up to NPO’s to decide how to account for their own finances. An ambiguous explanation leaves the interpretation up to the nonprofit, therefore leaving room for errors which might be innocent, but which can still lead to significant mistakes or even intentional misstatements.

In these tough economic times, some analysts blame the lax financial regulations for the strain that NPO’s are facing. Donations are nowhere near the forefront of people’s minds. People who have lost a great deal of money in investments, mortgages and retirement funds are looking simply to stay afloat and cannot afford discretionary expenditures such as charitable donations. As a result, nonprofit organizations that rely so heavily on cash flow from donations are getting hit hard as donations are decreasing. As stated in an article in *The New York Times*, roughly one third of 900 nonprofit groups indicated “they did not have enough cash on hand to cover more than one month’s expenses.”²⁶ Americans in financial binds are keeping a stronger hold on their money and if they make a donation, they want to know exactly where it is going. The current financial regulations of NPO’s do not provide donors with clear cut, unified reports, which may deter people from donating. If a company cannot show its donors exactly where their money is being spent, donors will be more likely to hold back on that donation. On the other hand, if an NPO can provide a detailed path of money that is donated, people may be more inspired and encouraged to donate. For example, if a person can trace his donation to a house that was built for a family facing difficult times, he would most likely continue donating because he has concrete evidence that his money was put to good use.

In addition to the lack of regulations having an effect on the external funding of NPO’s, it has prevented strong internal control of finances. Many NPO’s face difficulty in knowing how much money they have on hand and how to manage that money for long term investment. Ms. Clara Miller of the Nonprofit Finance Fund explained that “we (nonprofit groups) don’t tell our financial story well,” meaning that the financial statements put forth fail to communicate the true financial standing of an NPO to either outside donors or internal controllers.²⁷ A major problem that arises for a nonprofit from inaccurate financial understanding is the inability to create a sound financial base for itself. If a company puts all of the donations it receives towards individual projects and fails to establish a sufficient reserve aimed towards securing its future then its existence will be at stake in times such as these when donations are lagging. A key strategy in running a business is to make sure there is extra money or inventory to spare, or a safety stock to protect against stock outs.²⁸ The current regulations on NPO’s do not require sound financial data and therefore makes it difficult for nonprofits to know if they have a “safety stock” or not. These uncertainties have led some people within those organizations to “argue for new operating principles and practices that would enable [nonprofits] to secure a better financial footing,” or in other words, new regulations that would more clearly depict the true financial standing of NPO’s.²⁹ New regulations could lead to more efficient financial choices and thus a more solid, long term existence for NPO’s.

PROPOSALS FOR FUTURE REGULATIONS

As the current financial crisis lingers on, there have been calls for heavier regulations on both public corporations and NPO’s. The government has focused primarily on the public corporations however because they have been the center of the blame. Changes in tax policies and requirements relating to financial data have

²⁵ United States. National Endowment for the Arts. Office of Inspector General. *Financial Management Guide for Non-Profit Organizations*.

²⁶ Stephanie Strom. "Financial Safety Net of Nonprofit Organizations Is Fraying, Survey Finds."

²⁷ Ibid.

²⁸ James Olver, Theresa Lant, and Robert Plant. Cost Measurement and Analysis

²⁹ Stephanie Strom. "Financial Safety Net of Nonprofit Organizations Is Fraying, Survey Finds."

attempted to make such corporations more transparent. The spotlight may now be turning more towards NPO's; analysts have suggested a need for heavier regulation of such companies, considering they have access to millions of dollars as well.

In an article in the Financial Executive, the author mentioned that the Sarbanes-Oxley Act (SOX) which was passed in 2002 might one day be applied to NPO's. She wrote, "although Sarbanes-Oxley rules currently apply to only publicly held companies, (it) could be mandated for the nonprofit sector in the near future," which seems even more likely now with the economy being the number one issue facing the government.³⁰ The Sarbanes-Oxley Act was implemented during the aftermath of the Enron scandal when politicians and taxpayers saw the need for heavier oversight on such corporations. Scandals within the United Way and other nonprofits could possibly lead to the imposition of similar regulations. Questionable spending and excessive executive salaries are just a few reasons why nonprofits are gaining notice by legislators and regulators. As a result of nation-wide scandals and growing pressure, some nonprofit groups have voluntarily come into compliance with the Sarbanes-Oxley Act.

While some NPO's have willingly adopted SOX rules and guidelines, many others have not, which leads to the need for mandated government regulation. There have been many discussions and proposals from the government, the public and leaders of nonprofits themselves in terms of what should be required. The subject matter of the proposals range from salary caps of CEO's of nonprofit organizations to the number of board members to publicizing financial statements. Some of the areas of interest are more important than others in terms of their effectiveness in keeping tabs of the finances of NPO's. The debate is heated and has many angles; many people agree that some sort of reform is needed, but most cannot agree as to the degree of regulation needed. Leaders of certain charities fear that government regulation means harsh, costly, time-consuming new rules that punish nonprofits more than anything else. Despite the different sides, there are a few proposed changes that should be mandated for all nonprofit organizations because they would force such organizations to keep tighter accounting records and therefore prevent misuse of funds.

The first proposal deals with spending on behalf of charities. The spending relates to money spent on food, lodging and travel. Currently there is "no standard rate for meals, travel, and lodging...no specific limit of such spending by charities."³¹ This lack of oversight allows for charities to include expenses that perhaps should not be included in the budget of the organization. For example, if an employee of an NPO goes on a business trip for a fundraising campaign, he or she may stay at a hotel that charges a high rate per night and then put that expense to the charity under normal business expenses. That employee however may have had the opportunity to stay at a less expensive hotel, but chose to stay at the more expensive one only as a matter of personal convenience. In this case, he or she would be taking advantage of the lack of expense monitoring policy in charging more money to the charity for the expenses than was necessary.

During a senate panel it was suggested that to help account for charity spending and avoid misuse of donated monies there should be standards put in place that all nonprofits would have to abide by. The rule would state that "charities could pay no more than the federal government for meals, travel and accommodations. Board members, however, could authorize increased spending; the charity would have to disclose such expenses on its informational tax return."³² Such a rule would standardize the amount of money to be expended on business trips and the like. The fact that charities would have to inform the government of any expenses that exceeded the standard helps to keep track of whether the expenses were reasonable or not. In addition, it might discourage some executives or employees from trying to pass off lavish expenses on the NPO because those expenses would be reviewed by the IRS. The government should take steps to implement this type of regulation because it is not very costly yet can be very effective. With one set standard for expenses related to travel, the guesswork would be taken out of whether an expense is extravagant. Limiting the amount spent on such items would prevent employees from taking advantage of the finances of the charity; instead the charity can precisely judge how much a business trip might cost and account for it accurately. The expenses can then be followed up by the government since nonprofits would be required to report those expenses on their tax return.

³⁰ Ellen Heffes, "Will Non-Profits Be Next Focus of Sarbanes-Oxley?"

³¹ Brad Wolverton. "Rethinking Charity Rules."

³² Ibid.

The next proposal relates to charities with expansive budgets. Presently, charities are not characterized by how much money they deal in. Both small and large nonprofits face similar regulation and policies. This can be a problem however because those companies that have access to millions, if not billions, of dollars have the opportunity to involve themselves in scandals of enormous degree, as was seen in the case of the United Way. In addition, audits are not required of NPO's, meaning that they are not legally expected to have independent auditors come in and perform an audit of their accounts.³³ Again, without an audit requirement, nonprofits are given more room to falsify documents, expense reports, and budgets because they do not have the threat of an independent audit looming in the distance.

The senate panel suggested "that the Internal Revenue Service require that groups with budgets of \$250,000 or more supply such information to the IRS" and that such charities would have to have "independent audits of informational tax returns...every five years the charities would be required to switch auditors."³⁴ As a result of this regulation, the bigger nonprofit organizations that receive the most donations, grants and contributions will be forced to keep track of how much money comes in and how that money is expended. The government, via the IRS, will be able to ensure that that money is being sufficiently accounted for therefore leading to a decreased chance of scandal. This regulation should be put in place because it deals with the bigger nonprofits who can cause the biggest harm. By requiring that such companies undergo annual audits, the government, the general public and the nonprofit itself will be able to judge how honestly, efficiently and methodically transactions are recorded.

The third proposal, which is most important, involves the publication of financial information. For-profit corporations are required to publish their financial statements for the public to understand, decipher and utilize. These statements contain many details about the financial standing of the company such as its assets, liabilities, cash flows and financial disclosures. On the other hand however, nonprofit organizations do not face the same requirement, giving them the option to keep their financial statements private. Once again, without regulation of this area of their business NPO's have more room to make mistakes or intentionally misstate information. The general public does not have sufficient information when it comes to making donations if nonprofits do not voluntarily disclose their financial information. As a result, a citizen looking to make a donation might do so without full confidence in the charity they are donating to and perhaps might decide to hold back on that donation.

Upon their discussion about the financial statements of nonprofit organizations, the senate panel recommended that "charities would be required to make their financial statements available to the public."³⁵ Such a policy would have the greatest impact on regulation of nonprofit organizations. The benefits would flow to the nonprofit organization, the general population and the government. If the government mandated the publication of financial statements, statements that would be audited if the previous proposal was also enforced, then the general public would have more trust and confidence in nonprofits. First, donors would be certain that the facts and figures were accurate because they would be subject to independent audits. Second, donors would have easy access to those facts and figures because nonprofits would be obliged to publicize them therefore opening the lines of communication between those companies and their donors. Being able to analyze the financial condition of a particular nonprofit would give donors increased confidence that their money is being used properly thanks to the required audits and transparency that comes with public financial statements. With transparency being one of the biggest demands of stakeholders, these proposals would move NPO's toward that direction, resulting in more satisfied donors; more satisfied donors correlates with increased donations, more effective nonprofit organizations and finally an improved standard of living for people around the world.

As previously mentioned, some NPO's have already engaged in steps to regulate themselves. Whether it be through adoption of SOX policies or other forms of regulation, a number of NPO's have heard the outcries of stakeholders everywhere and have responded. One such case involves the American Red Cross, which had received a number of complaints and damage to its reputation. In 2008, the major philanthropic group decided to use a new, detailed accounting program to keep track of its finances. The programs, called ReconNet and AssureNet GL by Trinitech Group, are automated systems that will allow the Red Cross to have a tighter control of their accounts.

³³ Ibid.

³⁴ Ibid.

³⁵ Ibid.

Trintech is a “leading global provider of integrated financial governance, transaction risk management, and compliance” and has gained a strong reputation as a trustworthy, accurate producer of accounting systems. The Red Cross decided to implement ReconNet and AssureNet GL, which “automate the reconciliation of their disbursement accounts” and “control general ledger account reconciliation processes and closing tasks and activities,” respectively.³⁶ These two programs guarantee a more accurate collection of accounting receipts and records.

The Red Cross adopted the system to improve its accounting practices and to increase accountability. As stated by Martha Zweier, Director of General Accounting at the company, “during a natural disaster, we have some very complex reconciliation needs. ReconNET is expected to eliminate losses due to error and tighten our financial controls. The tracking function within AssureNET GL should allow us to better enforce policies and procedures and ensure the absolute integrity of our data.”³⁷ The voluntary move by the Red Cross will benefit the organization extensively in many ways including more precise accounts that reflect the actual financial position of the company and inventories on hand. Increased precision lessens waste and increases productivity therefore allowing the company to have a greater impact on the world, including more lives improved and saved. In addition, the company put itself in a favorable position by willingly attempting to make its operations and finances more transparent and accountable. Donors will view this as the Red Cross trying to better itself. As its reputation improves, more and more people will be inclined to donate to the Red Cross. The benefits will outweigh the costs in the long run for the company, as it has set a standard that other nonprofit organizations should look to follow to better their own operations.

Nonprofits do not always voluntarily adopt new systems, policies or rules however to ensure the accuracy of their finances. Many of them are distinctly opposed to government regulation, arguing that the costs to comply with regulations would be unbearable and result in many NPO’s going out of business. The debate has carried on for many years with no resulting significant outcomes. Many parties however have seen a growing need for regulation of these companies, including the Financial Accounting Standards Board. To get moving on these important problems, the FASB has taken steps to get input and feedback from NPO’s and come to a compromise that everyone is satisfied with. For example, in 2009 the FASB announced that it would create the Not-For-Profit Advisory Committee (NAC). This committee would obtain “input from the not-for-profit sector on existing guidance, current and proposed technical agenda projects, and longer-term issues affecting those organizations.”³⁸ The hope is that open communication between the board and the nonprofits that would be affected by any policies implemented by the board will result in policies that are effective and accepted by both parties. A friendly approach such as this might lead to regulation that NPO’s find reasonable and simple to comply with. The committee will consist of “12-15 individuals from the nonprofit sector, will be formed in early 2010, [and] will meet two or three times per year,” therefore the nonprofit sector will have appropriate representation and sufficient time and opportunity to have its voice heard with regards to proposed regulations.³⁹ Steps such as these toward standardizing regulation are crucial because the more time that passes without regulation opens up the door for more scandals and abuse of funds.

Regulation of NPO’s has been a sensitive topic for decades. Some people think that those companies should be left to their own devices since their main objective is to help others, while other people think that those organizations hide under the cloak of innocence and take advantage of a trusting public. During difficult economic times such as the “Great Recession” though, every sector of business comes under fire, including nonprofits. Citizens that are trying to recover from large personal losses cannot begin to think of making donations to nonprofits and as a result put them on the back burner. Nonprofits however cannot exist without such donations and so they must take the initiative to better control their finances and their reputation. Better controlled finances in a tough economic climate would help prevent a nonprofit from going under because waste would be reduced and they would know exactly how much money they have on hand and how much they need to continue their operations. Furthermore, better controlled finances would boost their reputation which would make them noticed and trusted by the general public leading to more donations.

³⁶ "The American Red Cross Selects Hosted Versions of Trintech's Recon-NET to Automate Reconciliation and Account Balancing Processes and AssureNET GL to Improve Accounting Compliance."

³⁷ Ibid.

³⁸ FASB. *FASB Establishes Not-For-Profit Advisory Committee*

³⁹ Ibid.

Since most NPO's fail to efficiently regulate themselves the government and the FASB must establish compulsory procedures and policies for nonprofits. Despite the objection of some NPO's, the government cannot afford to waste any more time on the debate; if they do, they soon will suffer the consequences of nonprofits going under and hence people relying more heavily on the government for services the NPO's once provided. By creating the NAC, the FASB is attempting to include nonprofits in the discussion of their own regulation. Ideally both parties will compromise and establish regulations; if not, the government must go forward and mandate regulations covering issues such as public financial statements and reporting, limits on charity spending and audit requirements. During tough economic times, donors expect to know how their money is helping and need every incentive possible to make them reach into their pocket and give. Regulation, transparency and accurate accounting are some of the incentives that NPO's can provide their donors in attempts to receive more donations. When it comes down to it, the regulation of NPO's, or lack thereof, is a matter of life or death.

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