

# Reviewing charities: What counts

It seems that slimming down has become the national obsession—and please note, we’re not talking politics. Whole segments of the U.S. population are urged to lose weight. Personal opinions are transmitted in tweets. Web-only news accounts replace newspapers. Complex presentations of complex matters meet impatience: “What’s the takeaway?”

No surprise, then, that newer organizations aiming to aid donors have been choosing narrow criteria for their charity evaluations. This is a distinct change. For decades it was assumed—are you surprised?—that thoughtful contributors would want assurance that a charity seeking their support had an active and independent board of directors, reasonable expenses, truthful solicitations and a demonstrable commitment to accountability. Outside evaluators like the BBB Wise Giving Alliance and its predecessors have long built their charity evaluations around such interrelated points.

**Emphasis on finances assumes there’s a completely level playing field in charity. But that doesn’t exist.**

To date, the less comprehensive evaluations tend to focus on how a charity spends its money, as expressed in several financial ratios (for example, 75% of annual expenses going for program services).

You’ve probably come across web sites that feature these approaches. Typically the result of each evaluation can be summed up in eye-catching symbols like stars or letter grades that will satisfy the donor in a hurry.

Approaches like these raise a number of questions. What criteria are being used to measure the charity in question? Who set the criteria? Are they adequate?

We encourage you to get acquainted with the range of evaluation that’s out there. Personal points of view or judgments based on narrow criteria add to our thinking. But they have a serious failing: they short-change charities and donors alike.

## A view too narrow?

In personal life, ridding oneself of excess pounds has innumerable benefits. But in charity evaluation, less is rarely more. “Which charity should I support?” is, when you think about it, a hard question.

An easy but not necessarily sufficient answer is often to “look at the money.” Money is naturally a key interest for donors—in making a contribution, after all, they’ve entrusted their money to someone else, and the transaction isn’t going to bring them a TV or a plumber whose quality they can judge first-hand.

Information about a charity’s use of money is conveniently accessible in the report that most charities file annually with the Internal Revenue Service. Since the financial figures are presented in a common format in the IRS form, anyone can calculate, for example, the percentage of its total expenses that a charity spends on its program services each year.

For many donors, that’s enough. But should it be? They may be fully satisfied with even less—not the percentage itself but only the third party rater’s claim that a particular percentage spent for program services or fund raising merits a certain letter grade or number of stars.

## Ratios can’t stand alone

Financial ratios *are* important but have limitations. The Alliance uses them, as you’ll see in standards 8, 9 and 10 in the Alliance’s *Standards for Charity Accountability* on pages 48-49.

But a charity appraisal based on financial ratios alone has serious weaknesses:

- Such a narrow focus can produce a false positive. A charity with an admirable level of expenses for program services could be sending out appeals that give donors a misleading notion of what those services are. Or there might be significant problems in its governance.
- Emphasis on finances assumes there’s a completely level playing field in charity. But that doesn’t exist. The type of program and the funding sources that an

requests or on its own initiative. The **information is evaluated**, first by the computerized system and then by an Alliance analyst. A **draft report**, listing any standards not met and the reasons why, **is sent to the charity** with a request for a response, generally within three weeks.

At this point the back-and-forth between the charity and the Alliance is apt to be busy. Few charities meet every standard on the first round, but additional communication and information can sometimes make a big difference in the report's conclusion.

**The final report**, incorporating any appropriate changes made following the charity's response, is posted to the give.org Web site and the results are summarized in the next *Wise Giving Guide*.

No one has to file information with the Alliance—it's voluntary. And there's no charge to a charity for an Alliance evaluation. (Donors tell us, though, that some non-responding charities falsely claim that they don't file because they don't want to pay for an evaluation.)

Note that *all* charities that meet all Alliance standards (shown in this *Guide* with checkmarks) are designated as "accredited." Once a charity has been found to meet all standards, however, it can, if it wishes, obtain the right to use the national charity seal (which bears the word "accredited") in its materials by signing a license agreement and paying a sliding scale fee. Seal holders' compliance with standards is monitored, and national charities that no longer qualify for participation must discontinue use of the seal. See more about the seal program at give.org or on page 47 of this *Guide*.

## Charities review their review

In outline, the review process sounds dry. In practice, it's not. Recently we asked several charities to tell us about their experience in the review:

"We saw filing with the Alliance as a challenge we wanted to meet," said Meredith Wellington, recording secretary of the **Aschiana Foundation**. The Foundation assists Aschiana, an Afghan NGO, in a range of programs that aid and educate children.

Considering the number of fully resourced charities who say they haven't the time or staff to answer our requests, this was a surprising answer: Aschiana, the U.S. organization, is operated entirely by volunteers. Despite that handicap, it was pleased that it eventually met all standards. Wellington reports one particularly satisfying outcome: the Alliance's standard 11 spurred the organization to obtain audited financial statements,

Few charities meet every standard on the first round, but additional communication and information can sometimes make a big difference in the report's conclusion.

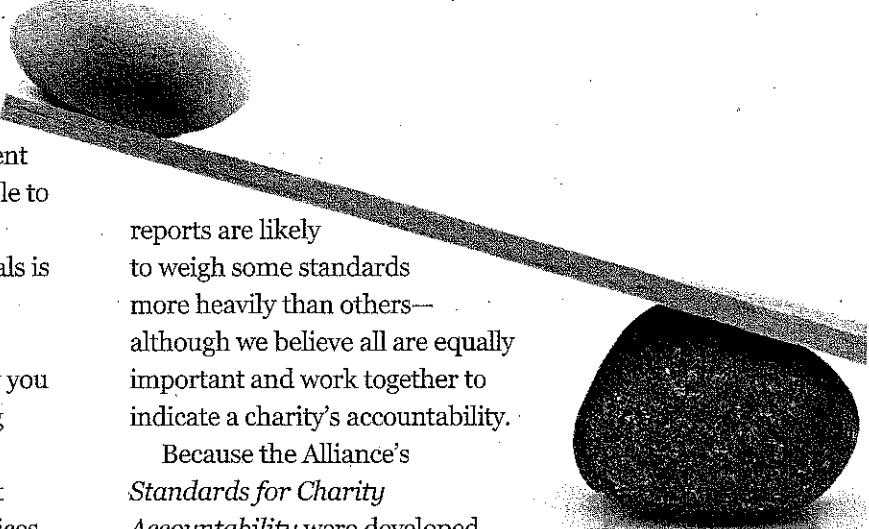
a move they were glad to have behind them when they came to apply for government grants and found that those statements were required.

Gary Barnhard, executive director of the **National Space Society**, which works to expand space exploration and settlement beyond Earth, acknowledged that the Alliance's first request for information came at a bad time. The Society was in the midst of preparing its audit and IRS Form 990, and several of the standards required board actions that took time to schedule. Understanding just what the Alliance expected was occasionally a problem, too, said Barnhard. Because of long delays, the Society was in the "did not disclose" category for a time. The Society's intention all along was to "do the right thing," however, said Barnhard, and ultimately it obtained a "meets all standards" report.

**A Wider Circle**, which conducts a range of programs "to help families and individuals lift themselves out of poverty," came to the Alliance on its own initiative, says Mark Bergel, its executive director. Several potential donors had urged the filing, and Bergel saw the evaluation process as "a chance to audit ourselves."

Bergel recalls in particular one step his organization took to meet standards, putting its finances on its Web site, as called for by Alliance standard 17. He said he thinks it strengthened the site, especially when he put a link to it on A Wider Circle's home page and included prior year figures in addition, so that viewers could see the organization's financial progress.

**Bat Conservation International** was another organization that did not immediately meet all standards, but Linda Moore, its director of administration and finance, saw value in persevering. She recalls especially that explanation and encouragement from the Alliance staff working on the group's report helped her provide documentation of her organization's procedures related to standard 7 (the



organization has may greatly affect its finances. An organization substantially funded by government grants and fees for service, for example, may be able to spend much of these funds on program, while an organization dependent on support from individuals is likely to put substantially more of its money into finding and retaining these donors.

- The diversity of funding sources is one reason why you can't assume that a charity that shows fund raising costs as 15% of related contributions is necessarily "better" than one with a 25% ratio, or that one that spends 85% of its funds annually on program services is "better" than one that spends 70%.
- Nonprofit accounting—including how expenses are categorized as "program," "fund raising," and "administrative"—is not an exact science that guarantees consistent financial reporting across the board. Consequently, a donor might inadvertently contribute to one charity rather than another only because the chosen organization has a more aggressive approach to categorizing expenses as "program," for example.
- Inaccurate financial reporting can distort ratios. Example: an organization reports receiving substantial contributions or grants, but shows no fund raising expenses. A miracle indeed!
- When a charity is at the center of a media firestorm, more than fund raising ratios is often at issue. Inadequate communication about how it would use contributed funds, questionable financial transactions with board members or deficient oversight by the board of directors are likely to be involved.

## Ratings and standards

Charitable organizations are diverse and complex. They're made up of individuals of varying degrees of competence, dedication and commitment to accountability. Their funding opportunities and resources are all over the map.

As we've explained, using mathematical calculations to evaluate charities across the board risks rigidity and irrelevance. Comments focused only on a charity's program expenses have value but don't touch other important parts of the organization.

Given charities' diversity, measuring them against standards rather than against one another makes sense. Standards are stated explicitly—no mystery here about the evaluative criteria being used. Of course, there's bound to be disagreement about the relative value of individual standards, and donors who use Alliance

reports are likely to weigh some standards more heavily than others—although we believe all are equally important and work together to indicate a charity's accountability.

Because the Alliance's *Standards for Charity Accountability* were developed with input from many sources, including the charitable sector and the public, they've had broad acceptance. Charities in general back the standards, not only because they had a role in their formulation but because they recognize various aspects of charities' operations, not just finances, for instance.

(You'll find, though, that charities can be ambivalent about financial ratios as indicators of worth. Charities may regard the focus on finances as off-base, but because they also fear that it's the only measure that some donors care about, they sometimes highlight ratios in their appeals.)

In sum, the Alliance standards rest on the belief that charities are too multi-faceted to be summarized and judged on a narrow aspect of their operations, and that savvy donors don't rely on overly simple evaluations.

No surprise, then, that the Alliance evaluates charities not against one or two *Standards for Charity Accountability*, but 20. But we don't argue that "20" is magic; the number and nature of criteria used by the Alliance and its predecessors have varied over the years and assuredly will in the future.

Nor do we tout the Alliance's approach as the be-all and end-all of evaluation. But we can show you how radically—and importantly—the Alliance differs from evaluators who get their information from public sources, process it mechanically and, often, present the results as ratings. We can show you too how the Alliance standards "work" for charities generally, despite their diversity.

## Charity evaluation, person-to-person

Follow us through a charity evaluation. You may be surprised at how interactive and hands-on it is, and at how much can happen in the process.

In outline, evaluation proceeds from a charity's **filing certain information**, either following written Alliance

board's approval of the organization's self-assessment report) that led to meeting the standard's requirements.

Of course, all is not forever sweetness and light between the Alliance and the charities it asks to participate in review. Our request for information adds to the tasks of busy staff members. Some charities press on through problems of compliance less out of commitment to meeting all standards than to avoid whatever they see as the consequences of not meeting them.

Many charities find it off-putting to be told that failure to provide information will mean they'll be publicly listed as "did not disclose." We can understand their reaction. But when we've taken actions on behalf of inquiring donors, we think we have a responsibility to let them know the outcome.

Yet over and over again, charities have told us that filing information with the Alliance, even when there are strains, is worth the effort. Linda Moore of Bat Conservation International called the Alliance's review process labor-intensive and time-consuming, but she found its thoroughness re-assuring. "I was glad to find that 'meets standards' conclusions aren't just handed out," she said: "Our experience heightened my confidence in the Alliance's evaluations of other charities."

## Beyond computation

Alliance standards aren't applied mechanically. Although a sophisticated computer program helps with the work, each charity evaluation requires the personal attention of Alliance staff. This is particularly the case in the Alliance's analysis of charity financial statements.

For that analysis, staff must often ask charities for additional information on issues ranging from the reported value of in-kind donations to the allocation of certain expenses. If the response to the questions raised is not sufficient, the report explains that the Alliance is unable to determine whether the charity meets the applicable financial standards.

In instances where the Alliance can confirm its initial doubts about the accuracy of certain expense allocations (showing fund raising costs lower than they actually are, for example), the Alliance report explains that the charity does not meet standard 13, which calls for charities to accurately report expenses in their financial statements.

## Down the road

Expect to see more and more new ways of evaluating charities. For one thing, the IRS Form 990, which most charities file and which is publicly available, has recently

been expanded to include not only additional financial information but also more about the practices and policies of governing boards. You can be sure that all this newly available data will be sliced and diced to create new and novel devices for charity evaluation. No doubt another aspiring watchdog is at this moment seeking an algorithm that will convert a range of charity data into a single score.

The need for sound approaches to helping strengthen both charity operation and donor understanding is constant. New developments that affect charities must be acknowledged. Over the years the standards used by the Alliance have changed—the latest ones, for example, incorporate modern issues like donor privacy and Web content—and some will no doubt change again.

Right now there's much attention on charity "effectiveness." Since 2003 the Alliance has had two standards (6,7) relating to that subject. In essence, charities are required to assess their own performance and effectiveness at least very two years. The results of their self-examination are to be summarized in a written report submitted to the board for its approval.

The BBB Wise Giving Alliance is currently involved in a project about charity effectiveness with two other organizations: Independent Sector (a coalition of charities, foundations and corporate giving programs) and Guidestar USA (an organization that provides online access to the IRS Form 990 and other charity information). The project, titled Charting Impact, is developing a common framework that will help charities publicly share information about their effectiveness. We expect to tell you more about this project in a future *Guide*.

## Donors' views?

Nate Adelman of Beverly Hills, California, is a long-time user of the *Guide*. He says he knows the Alliance does an extensive job, so he checks Alliance reports before he contributes. As to charities that don't provide information the Alliance asks for, he says, "the heck with them." Another Alliance supporter, Marge Roy of Topeka, Kansas, says, "The *Guide* is my Bible, and you can quote me on that."

Based on the calls and letters from donors we receive every day, we're pretty sure they agree on this: in charity review, what counts isn't simple. ■