

Best Practices for Municipal-Affiliated Nonprofits

It is not unusual to see community-oriented nonprofit organizations formed to support the activities of a municipality or a specific municipal department like parks and recreation or elder services. These organizations, which the OIG calls “affiliated nonprofits,” are created to support the community by coordinating and funding supplemental programming or activities that may not otherwise occur. For example, local residents may establish an affiliated nonprofit, the “Friends of the Town,” to fundraise and buy additional materials for town community events.

Affiliated nonprofit organizations can offer valuable benefits to municipalities. By supplementing appropriated funds, affiliated nonprofit resources can increase the quality and quantity of municipal events. Affiliated nonprofits also provide a structure through which members of the public can easily and directly support activities organized by a municipality.

Although affiliated nonprofit organizations are not under municipal control, you can and should adopt and follow best practices to mitigate risks that can arise from the interaction of the nonprofit with your government entity. This edition of *OIG In Your Inbox* highlights two areas for your attention: nonprofit governance and fiscal controls.

Nonprofit Governance

Affiliated nonprofits should develop governance documents that clearly identify the organization’s purpose and appropriate use of the organization’s funds. These governance documents should provide clear roles and responsibilities for organizational leadership, including rules regarding board membership, meetings, and fiduciary obligations for affiliated nonprofits subject to board oversight. In addition, affiliated nonprofits should adopt policies and procedures to ensure compliance with applicable law, including policies that address potential conflicts of interest and ethics.

Municipalities should be particularly mindful of the boundary between the activities of an affiliated nonprofit and the public function of the municipality. Municipalities need to exercise caution when municipal officials – or former officials – serve in leadership roles with an affiliated nonprofit. This scenario may create an actual or apparent conflict of interest, suggesting to outsiders that the affiliated nonprofit is not independent. Municipalities should enact and strictly enforce policies and procedures to ensure that these public-private boundaries are clearly delineated.

Fiscal Controls

All organizations need to implement fiscal controls to mitigate risk and prevent fraud, waste, and abuse of organizational resources. Such controls require organizations to develop written policies and procedures to govern financial transactions, including multiple levels of transactional review and approval, recordkeeping requirements, segregation of duties, reconciliation procedures, and regular training.

Affiliated nonprofits, and nonprofit organizations in general, may have inadequate fiscal controls in place. For example, the OIG received a complaint from a person in one Massachusetts town alleging that an affiliated nonprofit used funds for inappropriate purposes, rather than supporting town-organized activities as intended. While investigating the complaint, the OIG found that the affiliated nonprofit failed to preserve invoices or bank statements and tolerated poor fiscal recordkeeping. This environment made it difficult to verify that withdrawals from the affiliated nonprofit's bank account were made for appropriate purposes.

What Can Municipal Leaders Do?

- Maintain a list of all affiliated nonprofits and their officers;
- Prohibit municipal employees from serving as fiscal officers for nonprofits affiliated with their department or agency;
- Require municipal departments to keep detailed records of all financial transactions, including transactions with affiliated nonprofits, by retaining invoices, receipts, and other financial records; and
- Only affiliate with nonprofits that are willing to openly share their governance practices with the municipality. Determine whether the nonprofit complies with best practices, such as:
 - Obtaining and maintaining IRS 501(c)(3) status;
 - Registering with the Massachusetts Attorney General's Non-Profit Organizations/Public Charities Division and submitting annual filings as required by law;
 - Including a clear statement of purpose and specified uses of resources in governance documents;
 - Developing and implementing policies and procedures to ensure compliance with applicable law, particularly policies regarding conflicts of interest and ethics;
 - Engaging in sound bookkeeping practices and maintaining detailed records of financial transactions, including invoices and receipts;
 - Requiring multiple levels of review and approval for financial transactions and segregation of duties; and
 - Disclosing officers and board members to the municipality.

Conclusion

Affiliated nonprofits can serve a valuable role in the ecosystem of our communities, but they operate at their best when led with clear governance documents and good financial practices. Municipalities have an obligation to maintain public trust and protect public resources by enforcing a strict boundary with private resources. Keeping these objectives in mind when structuring interactions between municipalities and affiliated nonprofits is in the public interest and will serve as effective tools to prevent fraud, waste, and abuse.

*The OIG periodically issues **OIG In Your Inbox: Insights, Advisories and Alerts** as a way to succinctly share timely topics with key stakeholders, most notably the leaders within the Commonwealth's 351 local communities. The OIG hopes that **OIG In Your Inbox: Insights, Advisories and Alerts** will prompt dialogue and needed action on matters important to public entities.*

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