

WISE GIVING™

GUIDE

A PUBLICATION OF THE BBB WISE GIVING ALLIANCE : SUMMER 2009

Charity by the Truckload:

GIFTS in KIND





A Publication of the
BBB Wise Giving Alliance

The *Wise Giving Guide* is published quarterly to help donors make more informed giving decisions. This guide includes a compilation of the latest evaluation conclusions completed by the BBB Wise Giving Alliance.

If you would like to see a particular topic discussed in this guide, please email suggestions to give@council.bbb.org or write to us at the address below.

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BBB Wise Giving Alliance
4200 Wilson Blvd.
Suite 800
Arlington, VA 22203
(703) 276-0100
www.bbb.org/charity

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president's MESSAGE

Gifts-in-kind occasionally get bad publicity. *The Arizona Republic* recently published several articles reporting what it called “controversial transactions with supplies” involving numerous charities, many of them in Arizona. According to the articles, donated medicines and other gifts-in-kind were transferred from one charity to another, on and on, with each claiming the goods’ values in their financial reports.

What the outcome of the paper’s reporting will be, I don’t know. I do know that actions like those described are by no means typical of charities that handle the tons of goods that corporations donate each year. These goods, distributed with skill and caring, ultimately benefit millions of people throughout the world.

But there are potential problems in gifts-in-kind operations that you should be aware of. Our article highlights several of them, and if accounting concepts aren’t your passion, I hope you’ll pardon us if we get a little wonky as we try to outline them. The point is that much professional guidance regarding gifts-in-kind is available to charities.

I suspect, though, that your deepest concern about donated goods is how they’re used—and with good reason. Piles of donated supplies sat rotting on the beaches of Indonesia after the 2004 tsunami, some sent by charities that had no organizational structure there to put them to use. Clearly, without good management, good intentions go to waste.

Our article can only suggest some aspects of gifts-in-kind programs. I hope it will encourage you to look beyond tonnage and dollar value and learn more about how charities maximize the humanitarian benefit of donated goods. With knowledge and understanding, you’ll find you can give with confidence.



H. Art Taylor, *President*





Charity by the Truckload: Gifts-in-Kind

In charity, Americans like bulk and heft. Truckloads, shiploads, carloads and crates filled with donated goods on their way to the needy impress us, even if we see them only looming large in photos or translated into big dollars in a charity's financial reports.

Gifts-in-kind, often referred to as GIK, are a vital part of charitable work. They can provide benefits that there would be never enough cash to cover. They are plentiful even in tough times. Firm figures are hard to come by, but people in the field estimate the dollar value of donated goods handled by American charities from about \$8 billion to over \$20 billion annually. Between a third and a half of all corporate giving, studies indicate, is in goods, rather than cash.

Though goods in quantity come from corporations (and government and sometimes other charities), it's cash contributions from individuals that give essential support to the hundreds of charities that use them. Without cash gifts, these pharmaceuticals, foods, clothing, building materials, computer hardware and equipment of innumerable types wouldn't leave the warehouse. That fact gives you, the giver of cash, a strong reason for understanding how gifts-in-kind are obtained and handled.

There's another reason for paying attention. Getting the goods from here to there requires charities to make their way through sometimes foggy territory, and some groups inevitably take advantage of the haze to misbehave. Even with the soundest intentions, charities deeply involved in GIK face challenging questions:

- What's the dollar value of donated goods?
- In what circumstances should charities take credit for getting and using GIK?
- What products are appropriate, what practices sound?

Since there seems to be an American charity ready to accept and use virtually any donated "thing," from human hair to office chairs, surveying them across the board would require far more than these few pages. Here we look mainly at national charities whose programs of relief and development rely substantially on noncash goods from non-governmental sources but also depend on contributions from individuals. If you're among those individuals, there are some issues that you'll want to be aware of.

Gifts-not-so-kind

There's perhaps no more vivid way to illustrate those issues than through a situation where gifts-in-kind go wrong.

In 1992 the states of Connecticut and Pennsylvania brought suits against several national charities. (The suits were eventually settled, with the charities' agreement to a number of payments and changes.) Gifts-in-kind—cookies, baby food, books, and flower and vegetable seeds among them—were at the core of the charges. According to the August 3, 1992 press release issued by the Pennsylvania attorney general's office, the suits alleged, among other things, that four charities “were part of a ‘pass-along’ network of charities through which donated or purchased commodities of little value were passed from one charity to another, with each organization drastically overstating the value of the goods and counting them as ‘program services’ on tax forms, financial reports and fund-raising material.”

These suits brought attention to the points we explore below.

“What's it worth?”

Deciding what an object is worth, dollar-wise, has a certain fascination, or “Antiques Roadshow” would not be in its twelfth year. If you're a fan of the show, you've probably noticed that those antiques experts, taking into consideration things like age, uniqueness, and condition, estimate values in ranges, from \$1,000 to \$3,000 for Grandma's art deco vase.

A charity that receives a donation of food, medicines, clothes or whatever else has to give these goods a dollar value in its financial statements. The total value will appear as part of both its income and program expenses. While dollar ranges may satisfy a “Roadshow” hopeful, they won't do for charities assessing donated goods.

Establishing a specific dollar figure can be hard. Accounting guidance calls for measuring at “fair value” gifts-in-kind that are to be used or sold. In determining fair value, such things as quantity, condition and age of the goods at the date of donation come into play. Spoilage dates for food and expiration dates for items like vegetable seeds and pharmaceuticals enter into the calculation. The conclusion may not be obvious: seeds past the date on which they can be sold in the States may still have a germination rate that gives them value. In general, donated goods are acquired in bulk, so

Establishing a specific dollar figure can be hard. Accounting guidance calls for measuring at “fair value” gifts-in-kind that are to be used or sold.

alarm bells should go off if you see an audit note stating that those goods are valued at retail.

What do charities tell us about their valuation methods?

Feeding America, which reports distributing 378 million pounds of donated food and grocery products in 2008, uses the approximate average wholesale value of one pound of donated product at the national level, or \$1.49 in that year, based on a Feeding America study. The study is re-done each year to keep values current.

Food for the Poor reports that it bases its valuations on those given by the donor but checks them against other sources, often on the Internet. For example, says Angel Aloma, the organization's executive director, if Food for the Poor gets an offer of 500 hospital beds, it goes online to check the value of comparable items, both new and used. Other charities also report using the Internet for such checks.

Charities that deal extensively with pharmaceuticals say their usual resource is the annually revised *Red Book: Pharmacy's Fundamental Reference*. There's also an international reference on generics. Some suggest that the existence of such guides (for those who use them) may make charities' valuations of donated pharmaceuticals more consistent than the valuation of clothes and other consumer products.

Still, proper valuation remains troublesome, even when done in good faith. “GIK valuation for accounting purposes often requires administrative effort (such as for gifts of clothing, food and pharmaceuticals). For that reason, some organizations are challenged to allocate sufficient staff time to properly care for the valuation process,” says Dan Busby, president of the **Evangelical Council for Financial Accountability** (ECFA). (ECFA is an accrediting agency for Christian charities which, like the Alliance, uses comprehensive accountability standards in its evaluations.) *continued*

Much guidance is available. Responding in 1992 to the “pass-along” stories we mentioned, the **Association of Evangelical Relief and Development Organizations (AERDO)** developed *AERDO International GIK Standards*, commonly referred to as the AERDO standards. A revised version was issued in 1999. Building on accounting principles, the AERDO standards note where abuse can occur and present detailed guidelines for sound practice. Their influence extends far beyond AERDO’s own membership. They are incorporated into the standards of **InterAction**, the largest U.S. coalition of international relief organizations.

A charity’s auditor, equipped with a general knowledge of how things are valued, also has a role. The auditor needs to know the valuation method the charity is using and see back-up documentation. He or she must be assured of the reasonableness of the method. It would clearly not be reasonable, for example, for an American charity that received goods valued by the Canadian donor at \$50,000 in Canadian dollars to value the goods at \$50,000 American at a time when the Canadian dollar was worth, say, 85 cents American. But reasonableness is not always so easily judged.

Okay, okay, but I give cash

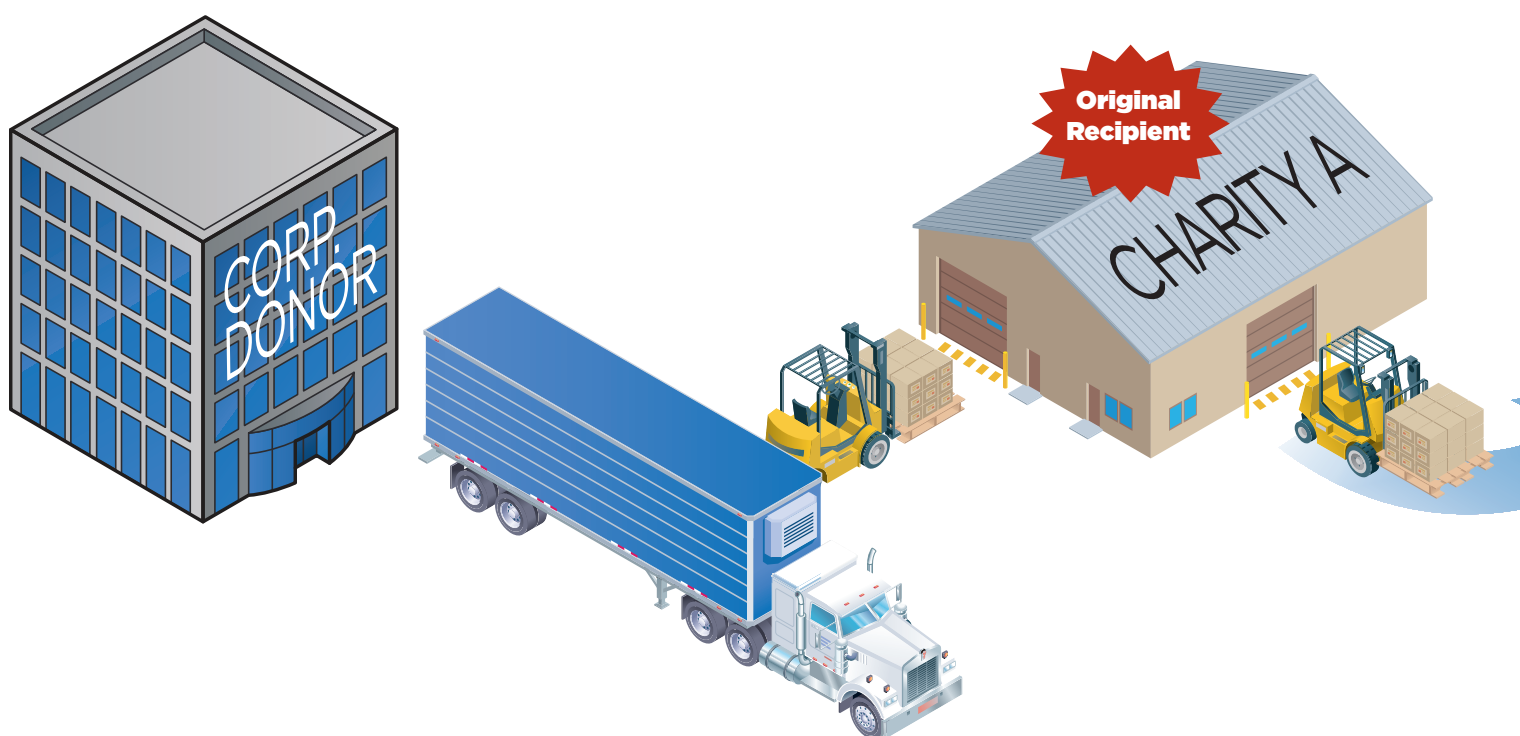
You may wonder what this accounting fuss has to do with you, whose contributions are made by check or credit card, not carload. Well, for one thing it’s a

reminder that there’s inevitably leeway in accounting for gifts-in-kind that doesn’t exist for accounting for cash gifts. That means that if you’re given to comparing organizations’ financial ratios, the playing field for organizations that deal significantly in gifts-in-kind and those that don’t can never be entirely even.

But because inflating the value of GIK can make a charity’s financial reports look great, boosting program services expenses (where the GIK always appears) and dwarfing expenses for the management and fund raising, there will always be charities that do it and auditors who go along.

As a donor, you’re not going to know how much credence to give to the figures you’re shown. If you’re bent on knowing more, the notes to a charity’s audited financial statements may tell you something about its valuation methods. The financial statements should be available to you on request and are often included on charities’ Web sites.

But it can also help to check out whether a charity is accountable in other respects—in being forthcoming with information and honest in its solicitations, for example, as the Alliance standards require. Charities often don’t tell as much as they could about their gifts-in-kind activities. Feel free to ask questions.



GIK moving on...and on?

The second accounting issue: In what circumstances should charities take credit for getting and using GIK?

It's not uncommon for charities to give money or things to one another. A community fund solicits monetary contributions for the support of other charities, for example. Similarly, a charity may focus on obtaining goods donations from manufacturers and providing them to other charities. This can make sense. The supplying organization seeks out and maintains contacts with corporate donors. It develops familiarity with the needs of charities it donates to. It offers expertise in handling GIK, leaving the recipient organizations to focus on distribution.

Arrangements among nonprofit organizations for acquiring, transporting and using GIK are of many kinds. In some situations, more than one organization may appropriately "recognize" the value of those goods, each showing a value for the same items in its income and expenses.

Unfortunately, accounting guidance doesn't offer a quick rule of thumb for determining when this reporting is appropriate. Numerous factors have to be weighed, just as in valuation. Basically these factors relate to the degree of special involvement that each charity has with the donated GIK—does one

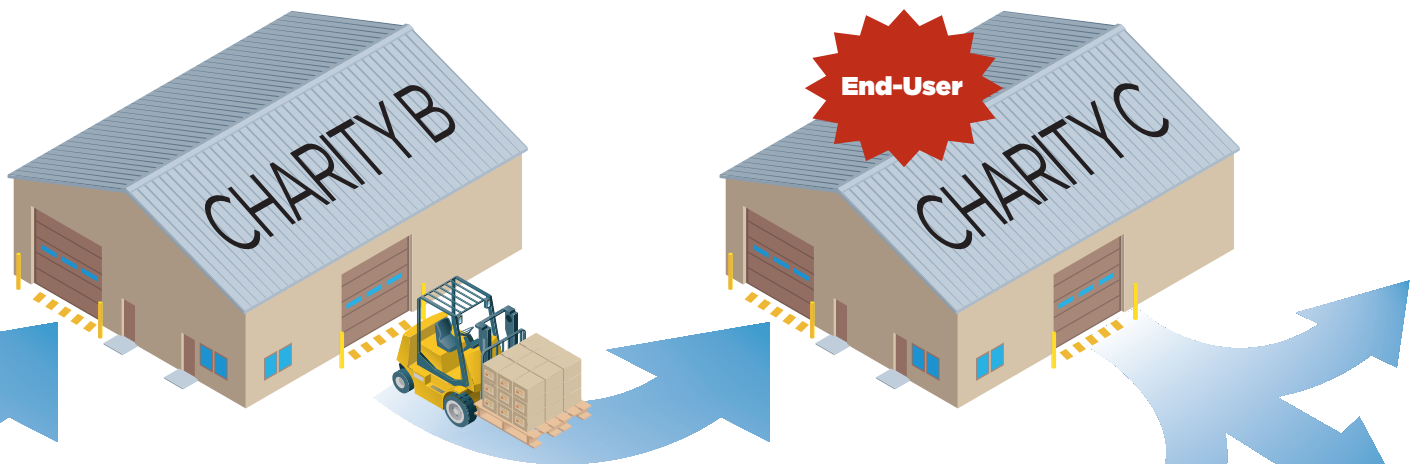
organization add value to the products in some way before passing them on, for example?

The AERDO standards (based on accounting literature) conclude that in general, "only the organizations that take possession of a GIK donation from the original donor or which take possession as the end-use agency may record the valuation of the GIK donation as revenue." That means only two organizations can count the goods. Our diagram shows this situation in very simplified form.

As a donor, you're not likely to know how closely one charity or several in a chain are following accounting guidance or their own ethical sense. Keep in mind, though, that as with valuation, abuse has a payoff: when the same goods go from charity to charity and each one along the way can show grand amounts spent for "program services," some donors will be wowed.

Thanks but no thanks?

Charities cannot accept any and every noncash gift they're offered. GIK donations must be consistent with the charity's mission. That, in brief, is the first of AERDO's seven GIK standards. "Donations offered which are inconsistent with the non-profit's mission and tax-exempt purpose should not be accepted," AERDO stresses. It's a legal matter, too. A charity that accepts such gifts jeopardizes its tax-exempt status.



A corporation donates \$200,000 of canned soup to Charity A in Boston. Charity A decides to donate the soup to Charity B in New York. Charity B then donates it to Charity C in Atlanta, which distributes it to the poor in Georgia. In this scenario, accounting rules permit only two charities—Charity A, the original recipient, and Charity C, the end-user—to include the value of the canned soup as part of revenue and expense in their respective financial statements.

But you can imagine situations in which a charity is ready to accept a substantial gift-in-kind which has little connection to its mission but can be delivered somewhere and will definitely enhance its financial report. “For free, take” isn’t an adequate guideline.

Eyes on the goods

Donated pharmaceuticals and medical supplies get lots of public attention. We give them special attention here because their care and handling suggests the kind of work that underlies many GIK programs.

In all the gifts-in-kind that charities use in their relief and development, food may take up more space or weigh more, but pharmaceuticals have the greatest monetary value, estimated at about \$5 billion annually. In a survey of giving by 197 major corporations and corporate foundations in 2007, the Conference Board found that pharmaceutical companies were the largest non-cash givers.

Why do companies give away so much? Recipient charities say the companies have a strong sense of social responsibility. They want to see a healthy world. And certainly products are available, for various reasons. Sales predictions may be overly optimistic, a newer version of a drug may make the older one obsolete, or a generic may be coming onto the market and replacing the version still in stock. “Companies take a loss on the products they don’t or can’t sell,” says Luke Hingson of **Brother’s Brother Foundation**, speaking of gifts-in-kind generally. “It’s just probably often less of a loss if they donate them.”

Charity programs built around donated pharmaceuticals have a special responsibility to ensure the security and usability of the products. Professional expertise and complex data management systems are among the resources needed to make these programs work.

Corporate gifts-in-kind, primarily pharmaceuticals and medical supplies, made up 69 percent of **Project Hope’s** 2008 income. Pat Bacuros, director of in-kind giving, oversees the gifts-in-kind program that requires daily interaction with both donor companies and HOPE staff in 33 countries. When a Ministry of Health official or a hospital representative submits a request for

Charity programs built around donated pharmaceuticals have a special responsibility to ensure the security and usability of the products.

medicines or medical supplies to HOPE, Bacuros begins gathering information such as who will be the beneficiaries of the medicines or medical supplies, how they will be distributed and who will monitor the distribution process to ensure the gifts-in-kind get to the intended audience.

After Bacuros reviews the information, she contacts a pharmaceutical or medical supply company which, in turn, checks product availability and determines if the request is in line with the company’s giving criteria. If the request is approved, the donor company sends the gift-in-kind to the Project HOPE warehouse. There, products are entered into a comprehensive inventory system that logs and tracks every product. When the gift-in-kind is shipped and reaches its destination, in-country staff manage the customs process and deliver the product to the requester.

“**AmericCares** operates somewhat differently from other organizations using the gift-in-kind model because a major part of its work is providing immediate response to emergency medical needs in both the U.S. and abroad. That requires proactively acquiring and warehousing a vast inventory of goods that will be available when a disaster strikes,” says Elizabeth Furst



Frank, senior vice president of global program operations. AmeriCares corporate donors, primarily pharmaceutical companies, provided in-kind gifts valued at close to \$1 billion in 2008. In addition to emergency response, AmeriCares also supports ongoing humanitarian assistance programs, including sending needed medical supplies to about 1,000 volunteer doctors who are traveling and working overseas.

“An information explosion in this field has brought great advances but also put new pressures on charities that provide pharmaceuticals,” says Frank. “Because we now know more about the safety of medications than ever before, there is more data to scrutinize, and as medical sophistication grows throughout the world, recipient countries ask for additional information, such as quality certification, about the products sent to them. That has given us the opportunity to enhance the impact of the donations, enabling us to deliver the right medicines to the right people at the right time.”

Given the magnitude of charity-directed pharmaceutical distribution, it’s not surprising that “healthcare logistics” is a growing profession. You may not be ready for a job change, but a little video called “Mission Possible” made by the **Partnership for Quality Medical Donations (PQMD)**, at www.PQMD.org/cms/agentrx, offers a primer, with a light touch, on the correct steps for delivering an order of medications abroad. These include ordering, preparing customs clearance documents, distribution, storage, security and the all-important record keeping. (“Paperwork is not fun, but neither is dying,” says the narrator.)

A note about outdated pharmaceuticals: it’s not enough that donated medications leave the U.S. before their expiration dates. Standards in the field require that the expiration date be far enough off to cover the time needed to transport them and give them a reasonable shelf life (at least one year, in the InterAction standards) once they reach their destination. Otherwise, sending them off is waste. “Expired product is a tragedy for everyone,” notes that video.

GIK on the agenda

- The Financial Accounting Standards Board recently issued new guidance on measuring fair value, further evidence that the whole area of noncash transactions is not an accounting cinch (that area includes securities and real estate, among many other things). The new guidance, which calls for more disclosures about fair value measurement, takes effect for fiscal years

The change in the IRS Form 990 (the report that many charities must file annually) requires more detailed information about non-cash contributions than it did formerly...

beginning after November 15, 2007, so few financial statements that reflect it are yet available.

- In an April 6, 2009 speech on “Maintaining Public Trust in Charities During the Economic Downturn,” Lois Lerner, the Director of Exempt Organizations of the IRS, said that the IRS “will be on the lookout for aggressive fundraising tactics and the valuation manipulation that often accompanies them....” Further, she said, “we believe the information about non-cash contributions required on the redesigned Form 990 [coupled with other new IRS rules] leave[s] little room for organizations to hide and will help us detect and combat this type of abuse.”

The change in the IRS Form 990 (the report that many charities must file annually) requires more detailed information about non-cash contributions than it did formerly, including information about the method used by a charity to determine the value of non-cash contributions.

- Charities, too, continue to wrestle with GIK issues. Just this past April, **World Vision** and **Mercy Corps** co-hosted a three-day conference titled “Exploring Gifts-in-Kind” to which it invited all those “with an interest in promoting GIK best practices.”

There have been periodic conferences about AERDO issues, but this was the first that included organizations outside the “faith community” (you’ll recall that the “E” in AERDO stands for Evangelical), and it was attended by a hundred people from 62 organizations, reports World Vision spokesperson Anne Duffy. Among the agenda items were the very subjects addressed here, valuation and recognizing GIK revenue.

continued



New routes, new destinations

But another subject on that agenda surely touches donors more directly: what is the impact of gifts-in-kind on the communities they reach?

Matthew Schwartzberg, senior material officer at Mercy Corps, thinks we've been paying too much attention to numbers (how many truckloads, how many dollars' worth) when we think about gifts-in-kind, and not enough attention to how donated materials will influence the communities and individuals that receive them. He includes charities and donors, corporate as well as individuals, in that collective "we."

"These programs are too often supply-driven, and fundamentally based on finding homes for donated goods," Schwartzberg says. "Both donors and charities need to balance this perspective with a deeper understanding of how donated materials can help poor communities grow and prosper."

Schwartzberg and his colleague Colleen Regalbuto think that the GIK community has lagged behind other parts of the humanitarian aid sector in assessing the impact of donated goods. But now, they say they see a growing concern and awareness among charities about the impacts of GIK work and a desire to view GIK as a tool for change rather than a gift.

Controversy about donated goods programs is not new. Gifts can cause jealousies, splitting communities or making recipients targets for crime.

Impact isn't always positive, as Schwartzberg and Regalbuto note. Besides maximizing benefits, charities must minimize potential negative effects, they say, referring to reports of how donated American clothes have undermined the textile industries of developing countries in Africa.

Controversy about donated goods programs is not new. Gifts can cause jealousies, splitting communities or making recipients targets for crime. Controversies swirl around food aid, especially in relation to large government food aid programs: Is food aid only palliative, without long-term benefit? Can food aid be even harmful over time to a country's economy? Should food be shipped in or purchased locally? Is food or cash more efficient? Such questions often apply as well to other kinds of GIK.

Getting value from gifts-in-kind

Clearly charity gifts-in-kind programs are less simple and straightforward than we sometimes think. There's much for thoughtful givers to consider:

- Are the goods that are sent the goods that are most needed—or just what a charity has on hand to give?
- Are the goods appropriate—not just food, for example, but food that is culturally acceptable?
- Are there adequate means of distribution?
- Is there monitoring and reporting back?
- What's the effect, long- or short-term, on the communities they reach?

To seek the right goods, to transport and warehouse them, to provide for and monitor their proper distribution and use and at the same time to be aware of how they can be tools for change, negative and positive—all this requires strong and accountable charities. Who will provide the money to make sure goods do good?

The tons of donated goods that can be so helpful to so many don't move without the cash contributions and often the volunteer time of individuals. For those who want to give their support to this work, there is a lot to weigh. When it's a question of goods, quantities and dollars can tell something, but it's important to know when they don't tell enough. ■