



OUR STAFF EXPERTS CONDUCT “SPECIAL INVESTIGATIONS” INTO YOUR QUESTIONS.

Dear 501(c)3I,

My organization is very concerned about being ethical and avoiding conflicts of interest. In the next six months to a year, we plan to apply to earn the Seal of Excellence through Maryland Nonprofits Standards for Excellence® program.

Our organization is small (only about 12 staff) and we are considering filling an open staff position with a person who is a relative of one of our board members. The board member is the committee chair that oversees the work under which this employee will be working. Is this okay? I heard that there might be some sort of definition of “key employee” according to the IRS. Can we proceed with hiring this relative?

There are so many different types of potential conflicts of interest in nonprofits. Unfortunately, this is not a question with a simple answer.

Regarding your question of what constitutes a key employee, I would have to defer to the instructions on the form 990. The 990 instructions state that a *Key employee* is “any person having responsibilities, powers, or influence similar to those of officers, directors, or trustees. The term includes the chief management and administrative officials of an organization (such as an executive director or chancellor). A chief financial officer and the officer in charge of the administration or program operations are both key employees if they have the authority to control the organization’s activities, its finances, or both.”

Sometimes the conflicts of interest are not clear cut. In this particular situation, I think you are correct to look at whether the family member is a person who would be serving in a “key employee” role. If the staff member is a director or manager, clearly the conflict will be more pronounced, particularly if the staffer regularly reports to the Board. The fact that his/her family member serves as the chair with responsibility over this person’s work area certainly raises a red flag.

In addition, it would also be worthwhile to look at whether the board member is likely to move up to a higher officer position on the board in the future. The potential conflict as it exists now could be even more pronounced if the person now serving as a committee chair, next year found him/herself in the board president’s position.

You’ll also want to consider the size of the board of directors. Where a situation like this might be seen as appropriate on a board with thirty members, a board with 5 members would be a totally different circumstance due to the fact that quorum may only be 3 people on a 5 person board.

It is not illegal to have a family member of a staff member on the Board of Directors, but is it wise? In many cases, it is not. That answer depends on whether the organization prohibits board service by someone related to a paid staff member and whether the organization’s policies provide that board members recuse themselves from every vote or discussion where a potential issue involving staff (benefits, layoffs, terminations, evaluations, etc.) which could create a conflict of interest for the Board member, arises. On a practical note, if such topics arise frequently, it may be

very difficult to be constantly recusing such a Board member.

Bringing this issue back to the Maryland Nonprofits Standards for Excellence: An Ethics and Accountability Code for the Nonprofit Sector®, it appears that if this organization hires the family member of a board member, it may not be viewed as illegal, but it will likely be exposed or reported publicly on the form 990. This transparency might not stand up to public scrutiny.

The organization would also need to be very clear on whether it follows the related portions of the Standards for Excellence® (having a conflict of interest policy which includes (1) coverage by board, staff, and volunteers with significant decision making authority, (2) identifies type of conduct that might constitute a conflict, (3) set forth procedures for disclosure and (4) provides for review by uninvolved members of the board, having an annual conflict of interest disclosure statement, having at least 5-7 unrelated board members. If the organization were applying to earn the Seal of Excellence, it might also be asked additional questions to show that it meets the spirit of the Standards for Excellence® and the process that was undertaken to decide to hire the family member of a board member.

So, to summarize, I do not think it is always a violation of the Standards for Excellence® to have a staff member who is a relative of a board member. But, all of the facts and circumstances should be taken into consideration. The strength of the organization’s conflicts policy, the size of the board, whether or not the employee is a key employee or not – are all factors that would need to be taken into consideration.

If you would like more information on how to handle conflicts of interest in your organization, you may find the Maryland Nonprofits Standards for Excellence® Educational Resource Packet on Conflicts of Interest helpful. To download this packet, please visit the Member’s Only section of the Maryland Nonprofits website, or visit the Maryland Nonprofits Libraries in the Baltimore and Silver Spring offices, or call 800-273-6367 ext. 13.

This and all Standards for Excellence® Educational Resource Packets are a free member benefit for all Maryland Nonprofits members.

Thanks for asking,

Amy Coates Madsen, *Program Director, Standards for Excellence®*