Ethical Leadership
By Jane A. Van Buren, Noonmark Nonprofit Services

This brief paper explores the meaning of ethical leadership on a practical level in nonprofit organizations. We will also discuss the interaction between organization culture and ethical practice.

What is ethical leadership? Let's start with some definitions. Ethics are the principles, values and beliefs that define what is right and wrong behavior. Leadership is the process of influencing others to achieve goals. Thus, we can define ethical leadership as the process of influencing people through principles, values and beliefs that embrace what we have defined as right behavior.

Here is an example: Susan is the director of an organization that provides services to people who are homeless. One day several boxes of stylish new sweaters are donated to the organization from a popular clothing store. The staff is very excited and starts sorting through the clothes and trying on different sweaters. An unethical leader will allow herself and the staff to select what they want from the boxes before making them available to clients. An ethical leader reminds everyone, including herself, that the donations were intended for clients and makes the sweaters immediately available to the people they serve.

Why should we be concerned with ethical leadership in the nonprofit sector? A 2008 Brookings Institution survey found that about one third of Americans reported having "not too much" or no confidence in charitable organizations, and 70 percent felt that charitable organizations waste "a great deal" or a "fair amount" of money. Only 10 percent thought charitable organizations did a "very good job" spending money wisely;

only 17 percent thought that charities did a “very good job” of being fair in decisions; and only one quarter thought charities did a “very good job” of helping people. Similarly, a 2006 Harris Poll found that only one in 10 Americans strongly believed that charities are honest and ethical in their use of donated funds. Nearly one in three believed that nonprofits have “pretty seriously gotten off in the wrong direction.” These public perceptions are particularly troubling for nonprofit organizations that depend on continuing financial contributions. It is important to remember the following:

- Nonprofits operate with public support and they need to grow and maintain the public’s trust.
- Nonprofits do not pay income tax on revenues, thus they are indirectly supported by all taxpayers.
- Nonprofits seek financial support from the government and private foundations in the form of grants and they ask community members and corporations for donations.
- Nonprofits must maintain high standards of transparency and integrity if they hope to maintain the support of the community.

The Stanford Social Innovation Review (2009) has described areas where ethical issues arise in the nonprofit sector. The first is **compensation**. Nonprofit organizations sometimes find themselves walking a thin line when it comes to compensating their employees. The sector may be nonprofit, but it's by no means noncompetitive. Organizations looking to hire the best and the brightest in their fields must offer attractive salary and benefits plans (Guidestar 2003) If, however, a salary package is deemed in excess of reasonable compensation, the IRS may impose intermediate sanctions on both the individual receiving that salary and the organizational managers who approved it. Salaries that are modest by business standards can cause outrage in the nonprofit sector.

The second area is **conflict of interest**, which arises frequently in the nonprofit sector because of the very nature of the sector’s composition. Nonprofit boards are generally made up of community members, many of whom are private business people. This leads to the potential of a number of ethical questions. Should board members obtain contracts for their company? Is the board member's disclosure and abstention from a vote enough? Should a major donor receive special privileges? Detailed, clear conflict of interest policies can answer these questions, and help the organization maintain public trust.

The third area identified by the Stanford Social Innovation Review is **publications and solicitation**. Nonprofits must be clear and transparent in all publications and in all solicitation for funds about the percentage of funds spent on administrative costs. If an organization maintains that every dollar donated will go directly to the people served they must be able to demonstrate the truth of that statement. Most organizations cover administrative costs with some unrestricted donor dollars and will need to educate donors about that reality. Transparency is crucial. Organizations cannot afford to raise funds on the basis of misguided assumptions, or to violate public expectations in the use of resources.

The fourth area is **financial integrity**. Nonprofit organizations also face ethical dilemmas in deciding whether to accept donations that have any questionable associations or conditions. Should an organization that works with people affected by cancer take money from a tobacco company? Should a women's study program take money from Playboy? Each organization must reach their own decisions on how to address these questions, however, appearances matter, and it sometimes makes sense to avoid affiliations where questions may arise or when the intentions of the donor are less than philanthropic.

The final area is **investment policies**. Advocates of socially responsible investing argue that nonprofit organizations should ensure that their financial portfolio is consistent with their values. This ranges from investing in ventures that further an organization's mission to divestment from companies whose activities undermine that mission. Of course many organizations are not in the position of having an investment portfolio! Regardless, the point is that all decision made by a nonprofit organization should be tested against the mission and the organization's set of values.

It should be clear by now that leaders set the moral tone for an organization. Leaders are the ones who uphold the shared values of the organization and set the cultural tone. Of course, people vary in their capacity for moral judgment—in their ability to recognize and analyze moral issues, in their capacity for moral behavior and in the priority that they place on moral values. Organizations make their ethical priorities evident in multiple ways, including through policy; the criteria for hiring, promotion, and compensation; and the fairness and respect with which they treat their employees. People care deeply about "organizational justice" and perform better when they believe that their workplace is treating them with dignity and is rewarding ethical conduct.

What can leaders do to create an ethical culture? A strong organizational culture that supports high ethical standards will have tremendous influence both in the community and on employee behavior. Although there are no guarantees, leaders can take several steps to create a strong ethical organizational culture.

1. Be a visible role model. Employees take their cues about appropriate behavior from those at the top.
2. Communicate ethical expectations. Organizations can create a "code of ethics." It should state the organizations primary values and the ethical rules that employees are expected to follow. If widely accepted and enforced, codes can also reinforce core values, deter misconduct, promote trust, and reduce the organization's risks of conflicting interests and legal liability.
3. Promote effective financial management. Use resources in a socially responsible way and strive to be cost-effective without sacrificing long-term institutional capacity. Ensure that the organization is using generally accepted accounting practices, and is transparent with donors and grantors.
4. Provide ethical trainings to employees; use these training sessions to reinforce the organization's standards of conduct, to clarify what practices are and are not permissible, and to address possible ethical dilemmas.
5. Institutionalize an ethical culture by measuring employee performance and organizational performance against your code of ethics. Make sure the

organization pays as much attention to what you are doing, as it is to where you end up.

6. Provide protective mechanisms. The organization needs to provide formal mechanisms so that employees can discuss ethical dilemmas and report unethical behavior without fear of reprimand. This might include creation of ethical officers, counselors or ombudsmen.

In conclusion, remember that any leader can behave ethically and create an ethical organization. It takes time, staff involvement and a commitment to put in place policies and procedures that institutionalize ethical expectations and practice.