

*"Effective governance by a board of trustees is a relatively rare and unnatural act... trustees are little more than high-powered, well-intentioned people engaged in low-level activities."*  
Chait, Holland, and Taylor

*"There is one thing all boards have in common... they do not function."*  
Peter Drucker

I'm willing to say that most if not all persons who serve in the role of senior pastor will at some time or many times in the course of her or his career be asked to serve on the governing board for a nonprofit organization, or NPO. In fact, the local congregation is a *nonprofit* organization (insert snicker here), as are our regional and national ABC-related bodies. But as we serve the church, the community, and our denomination, we are often invited to also serve on the governing boards of colleges and universities, hospitals, foundations, relief societies, and a smattering of other community and national organizations formed for the public good.

Beginning then with a sense that most of you serve in such ways, I wonder if perhaps you have had an experience similar to mine. I once attended an NPO board meeting where financials were reported and I did not understand some of the information on the financial documents I was given. But not wishing to protract the meeting (or to confess how under-prepared I was), I remained silent.

After the meeting I asked another director, and then another, and then another, "What did 'such and such' mean on the report?" Each director responded in turn with some version of, "Truthfully? I didn't understand that either." I began to wonder how often we as directors just "let things go," trusting that others are being vigilant so we do not need to be. Then I wondered why we need so many directors on a board if only a few, at best, are actually carrying out their fiduciary responsibilities.

How seriously do we pastors who are also directors of NPOs carry out our responsibilities? How well prepared are we for this non-pastoral work, and how well does the organization orient us to the task and provide the necessary information and training to leverage the strengths we bring? Questions like these are not just mine. They have been actively discussed in NPO circles in recent years, particularly since the Sarbanes-Oxley Act of 2002 (SOX).

Sarbanes-Oxley does not focus primarily on NPOs, and most provisions do not apply to NPOs,<sup>1</sup> yet the law has had significant impact on NPO governance, in part because some NPO

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<sup>1</sup> Two provisions of SOX do apply to NPOs: a provision to protect whistleblowers and a provision for the retention of documents. In addition, some states have proposed or passed regulations that extend certain SOX provisions to NPOs. The same environment of heightened concern about NPOs led the IRS to revamp their Form 990 to require NPOs to report on whether they have a conflict of interest policy. Congregations are exempt.

directors also serve on boards of publicly traded companies. The public outcry following the Enron scandal and a host of questionable activities within corporate America and the nonprofit sector, have also contributed to greater scrutiny of NPOs and greater attention to governance by management and boards alike.

This presentation is a review of the nature of NPO governance, a quick look at the attention given governance in recent years, and call to take nonprofit governance seriously. The role of a trustee or director may vary significantly from one organization to another. My own experience has included several churches, a hospital, a college, a foundation, a mental health services organization, and various American Baptists entities.

Nathan Garber suggests there are five different approaches to governance: 1) Advisory Board, 2) Patron Model, 3) Co-operative Model, 4) Management Team Model, and 5) Policy Board Model.<sup>2</sup> My own experience as a director has been with the policy board model as encouraged by John Carver in his 1990 publication, *Boards that Make a Difference*.<sup>3</sup>

What is the role and function of a nonprofit governing board? Richard T. Ingram summed up the generally accepted responsibilities of governing boards in his booklet *Ten Basic Responsibilities of Nonprofit Boards*.<sup>4</sup> Let's begin with his list.

1. Determine the organization's mission and purpose.
2. Select the chief executive
3. Provide proper financial oversight
4. Ensure adequate resources
5. Ensure legal and ethical integrity and maintain accountability
6. Ensure effective organizational planning
7. Recruit and orient new board members and assess the board's performance
8. Enhance the organization's public standing
9. Determine, monitor, and strengthen the organization's programs and services
10. Support the chief executive and assess his or her performance

These responsibilities are carried out by members of the board and the board's committees, in meetings of the whole and in committee and individual work. While these are board functions, failing to fulfill the responsibilities of the board may subject the individual directors to liability. Volunteer directors can be sued.

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<sup>2</sup> *Governance Models: What's Right for Your Board?*, Nathan Garber (London, Ontario: Nathan Garber & Associates, 1997 )

<sup>3</sup> *Boards that Make a Difference: A New design for Leadership in Public and Nonprofit Organizations*, John Carver (San Francisco: Jossey-Bass, 2006)

<sup>4</sup> *Ten Basic Responsibilities of Nonprofit Boards*, Richard T. Ingram (Washington, DC: BoardSource, revised 2003)

Accepting that Ingram has adequately described board responsibilities, what are the corresponding responsibilities of individual directors? The legal obligations of directors has been described using three rubrics: duty of care, **duty of loyalty** and **duty of obedience**.

**Duty of care** means that a director must be prudent when making decisions for the organization. **Duty of loyalty** means that a director's actions must place higher value on benefit to the organization than on benefit to self. **Duty of obedience** refers to the director's faithfulness in carrying out the stated mission of the organization. Cf., Bruce R. Hopkins, *Legal Responsibilities of Nonprofit Boards* (BoardSource 2003).

So how well do directors of NPOs across the country fulfill their responsibilities? As you can guess several studies have been completed in search of an answer. I will share the results of two such studies, one by Johns Hopkins and one by The Urban Institute.

In 2005, The Urban Institute conducted what TUI described as "the first-ever national representative study of nonprofit governance."<sup>5</sup> The study included 5,100 NPOs from a stratified random sample across the nation. The respondents were CEOs or their designees. The findings were extensive; I will name a few. But first..., a little background.

In the wake of SOX, followed by a 2004 Senate Finance Committee's draft paper calling for stronger nonprofit governance,<sup>6</sup> an IRS draft paper on *Good Governance Practices for 501(c)(3) Organizations*,<sup>7</sup> and a public outcry over excessive executive compensation and other governance-related issues, many professional organizations began a renewed focus on better governance. They encouraged their members to work towards compliance with the provisions of SOX. Francis Ostrower, writing for The Urban Institute, helped by identifying six important practices for NPO boards.

1. An external audit
2. An independent audit committee
3. Rotating audit firms and/or lead partners every five years

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<sup>5</sup> *Nonprofit Governance in the United States: Findings on Performance and Accountability from the First National Representative Study*, Francis Ostrower (Washington D.C.: The Urban Institute, Center on Nonprofits and Philanthropy, 2007)

<sup>6</sup> The U.S. Senate Finance Committee's Staff Discussion Draft (2004) grew out of a concern that "many nonprofit organizations lack effective financial and programmatic accountability procedures and that nonprofits are not adequately performing their oversight responsibilities." Senator Charles Grassley, committee chairman, suggested that too often "problems at... charities can be traced back to poor governance." Cited in Lester M. Salaman and Stephanie L. Geller, *Communique No. 4, Nonprofit Governance and Accountability* (Johns Hopkins University, 2005)

<sup>7</sup> This document can be found at [http://www.irs.gov/pub/irs-tege/governance\\_practices.pdf](http://www.irs.gov/pub/irs-tege/governance_practices.pdf).

4. A written conflict of interest policy
5. Formal policies for employees to report complaints without retaliation
6. A document destruction and retention policy

NPOs increased their focus on governance policies and compliance. The result of that increased focus could be seen in the TUI study which revealed that 47% of the NPOs that had a conflict of interest policy created that policy after SOX was enacted. Fifty percent of the study participants indicated that they still did not have a conflict of interest policy by 2005. Conflicts of interest, of course, violate the duty of loyalty requirement if not the duty of care and duty of obedience.

There was equally bad news with regard to financial transactions with companies where board members had vested interests. Twenty-one percent of respondents in the TUI study had purchased goods or services from board members or affiliated companies during the previous two years, and that number doubled among NPOs with more than \$10 million in annual expenses. Only 29% of NPOs in the study required disclosure of financial interests.

The Urban Institute study included other functions traditionally considered basic to good NPO governance. Ostrower writes, "Only a minority of boards were *very* active when it came to most of the activities we asked about, including fundraising (29%), monitoring the organizations programs and services (32 percent), monitoring the board's own performance (17 percent), planning for the future (44 percent), community relations (27 percent), and educating the public about the organization and its mission (23 percent)."<sup>8</sup> A significant number of the boards were not even rated as "somewhat active" in several of these areas. Twenty-six percent of the boards did not annually or biennially assess whether or not the organization's mission was being accomplished.

Other board characteristics were studied, including racial, ethnic, and gender diversity, director compensation, recruitment criteria and activity, and board size. The study was particularly interested in the relationship between the public policy environment and board performance. Apparently even the threat of public policy change is enough to impact board behavior. But overall the TUI study indicated a sub-par level of best practices governance.

The Johns Hopkins University *Listening Post Project* conducted a "sounding" the same year as The Urban Institute study (2005). However, the John's Hopkins "sounding" was much smaller (207 organizations versus 5,100) and limited to key sectors of the nonprofit world: children and family services, community and economic development, elderly housing and services, museums, and theaters. The Hopkins survey focused on financial accountability, board

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<sup>8</sup> *ibid.*, p. 12.

responsibilities, ethical practices, best practice standards, changes in structure and mission, and board awareness.<sup>9</sup>

Perhaps largely because the sample was smaller and limited to five specific sectors, the Hopkins results were quite different from the Urban Institute study. Respondents to the Hopkins survey indicated a significantly higher overall level of board performance in governance. The report writers were led to conclude, *"What this evidence strongly suggests is that the presumed problems with the management and accountability of nonprofit organizations have been significantly exaggerated."* Their communiqué continues, *"... the dire assessments emanating from alarmist media accounts seem significantly overdrawn. The nonprofit sector is well along toward getting its organizational house in order and legislative fixes premised on worst-case scenarios should therefore be approached with considerable caution."*<sup>10</sup>

Well, the larger and broader Urban Institute study, together with the Hopkins communiqué (though the latter seems defensive and with political ends) suggests to this writer that many improvements were needed and have been made in nonprofit governance over the last decade, but much work remains to be done.

What guidance is available for directors to improve their governance performance? How can directors assess the quality and effectiveness of their board? The Society of Corporate Secretaries and Governance Professionals suggests directors ask the following questions, particularly in regard to measuring their boards against SOX standards.

- ~ Are the directors independent of the management?
- ~ Do the directors—or their family members—have a financial interest in the organization (such as [that which] vendors or professional consultants to the organization would have) that creates a conflict of interest? If there are any potentially conflicted directors, is a majority of the board free of conflicts and fully independent?
- ~ Does the board meet regularly, including in executive session without the presence of management?
- ~ Does the board have a finance committee and an audit committee or a full board process for reviewing the financial statements, evaluating internal controls, and interacting with the independent auditors?
- ~ Does the board have a compensation committee or a full board process for regularly evaluating the performance of senior staff and setting their compensation?

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<sup>9</sup> *ibid.*, p. 1

<sup>10</sup> *ibid.*, p. 15

~ Does the board have a nominating/governance committee or a full board process for identifying new directors?

~ Is there an ethics code or code of conduct for the directors and the employees? Do the directors have a way to evaluate compliance with that code? Is there an annual certificate of compliance required?

~ Is there an organizational policy to protect whistleblowers?

~ Is there a written document retention/destruction policy for the organization and how often is it reviewed?<sup>11</sup>

For motivated nonprofit directors and boards there is an abundance of resources available to help improve board governance. The available resources cover a wide range of issues. I list a few of them below.

- the selective and strategic recruitment of quality board members
- the orientation of board members, including clear role expectations and an understanding of the organization's mission
- the structure and performance practices of officers and committees
- the periodic formal self-assessment of boards and directors
- the board's willingness to hold itself and its directors accountable for high performance
- efficient and effective meetings, with more focus on the future and less on the past
- an independent audit committee, regular external audits, and rotation of external auditors
- clear and periodically-reviewed investment policies
- agreement on, and use of, best practices
- good working relationships between board and staff
- transparency and documentation

The ills, strengths, and challenges of nonprofit boards are nothing new. Board governance in America dates back at least to the Massachusetts Bay Colony. Since that time, boards have assumed many "looks" and have been variously empowered and restricted by public legislation, political will, economic forces, and public opinion.

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<sup>11</sup> *Governance for Nonprofits: From Little Leagues to Big Universities; A Summary of Organizational Governance Issues and Principles for Directors of Nonprofit Organizations (Society of Corporate Secretaries and Governance Professionals, Inc., 2008) p. 8.*

The New Era social philosophy of the twentieth century, for example, fostered efforts to educate board members and improve board performance. Peter Dobkin Hall writes for BoardSource, *"These efforts raised a host of concerns about directors' responsibilities to the public and to stockholders, focusing on such issues as accountability, conflict of interest, fiduciary prudence, and the duty of loyalty."*<sup>12</sup> Hall's words about the 1920s sound very much like our own time.

So, as the Teacher wrote in Ecclesiastes 1:9,  
*What has been will be again,  
What has been done will be done again;  
There is nothing new under the sun.*

Even so, we should be vigilant as directors or trustees of nonprofit organizations. A casual approach to nonprofit governance is no longer an option. We have a legal, missional, and ethical obligation.

We serve because we believe in the organization's mission. We must serve well in order to advance the mission and because we represent others. Nonprofits belong to the community, the nation, the public. We hold a public trust. The Apostle Paul wrote, *"Now it is required that those who have been given a trust must prove faithful."* (1 Corinthians 4:2)

## DISCUSSION

- What types of NPOs are represented in our colloquium?
- Did you ever have an experience at an NPO board meeting similar to the experience I shared today?
- Do the NPO boards on which you serve:
  - Have a clear set of expectations for directors?
  - Have an annual self-assessment for directors? Periodic assessment for the board?
  - Have an audit committee separate from the finance committee?
  - Provide adequate orientation and training for directors to contribute at a high level?
  - Require each director to file a conflict of interest disclosure document?
  - Have a whistleblower policy known to all employees?
  - Have a document retention policy?
- What are some ways your contributions as a director or trustee can be improved?

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<sup>12</sup> *A History of Nonprofits in the United States*, Peter Dobkin Hall (BoardSource, 2003), p. 20.


*Non-Profit Boards: Taking Governance Seriously*  
MMBB Colloquium, February 1, 2012  
Ft. Lauderdale, FL  
Presenter: Reg Mills


### **Selected Quick-Reads and Sample Resources**

- 📄 2009 National Board Governance Survey for Not-for-Profit Organizations (Grant Thornton 2009)
- 📄 *Best Practices: Nonprofit Corporate Governance* (McDermott Will & Emery)
- 📄 Carver, John, *Boards that Make a Difference: A New design for Leadership in Public and Nonprofit Organizations* (San Francisco: Jossey-Bass, 2006)
- 📄 Garber, Nathan, *A Strategy for Building Governance Capacity* (London, Ontario: Nathan Garber & Associates)
- 📄 Garber, Nathan, *Governance Checkup* (London, Ontario: Nathan Garber & Associates, 2001)
- 📄 Garber, Nathan, *Governance Models: What's Right for Your Board?* (London, Ontario: Nathan Garber & Associates, 1997)
- 📄 *Governance for Nonprofits: From Little Leagues to Big Universities; A Summary of Organizational Governance Issues and Principles for Directors of Nonprofit Organizations* (Society of Corporate Secretaries and Governance Professionals, Inc., 2008)
- 📄 Grace, Kay Sprinkle, *The Nonprofit Board's Role in Setting and Advancing the Mission* (BoardSource 2002)
- 📄 Hall, Peter Dobkin, *A History of Nonprofits in the United States* (BoardSource, 2003)
- 📄 Ingram, Richard T., *Ten Basic Responsibilities of Nonprofit Boards* (Washington, DC: BoardSource, revised 2003)
- 📄 Masaoka, Jan, *All Hands on Board: The Board of Directors in an All-Volunteer Organization* (BoardSource 1999)
- 📄 Matan, Ron, and Peter Levy, *Nonprofit Board Governance: What Does it Mean?* (Sobel & Co., LLC, 2008)
- 📄 Ostrower, Francie, *Nonprofit Governance in the United States: Findings on Performance and Accountability from the First National Representative Study* (Washington D.C.: The Urban Institute, Center on Nonprofits and Philanthropy, 2007)
- 📄 *The Handbook of Nonprofit Governance* (BoardSource 2010)



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 *The Sarbanes-Oxley Act and Implications for Nonprofit Organizations* (BoardSource 2006)

 Salaman, Lester M. and Stephanie L. Geller, *Communique No. 4, Nonprofit Governance and Accountability* (Johns Hopkins University, 2005)

### Sample Resource Websites

[www.boardsource.org](http://www.boardsource.org)

[www.Garberconsulting.com](http://www.Garberconsulting.com)

[www.intrust.org](http://www.intrust.org)

[www.Carvergovernance.com](http://www.Carvergovernance.com)

[www.sobel-cpa.com/resources/white-papers](http://www.sobel-cpa.com/resources/white-papers)

[www.Governanceprofessionals.org](http://www.Governanceprofessionals.org)

[www.basingerconsulting.com](http://www.basingerconsulting.com)

[www.urban.org](http://www.urban.org)