Boardroom INSIDER

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The online newsletter for better boards and better directors *Ralph Ward, Publisher/Editor*

ARE NONPROFIT BOARDS ACTUALLY BETTER BOARDS?

The nonprofit world encompasses a large swath of businesses and organizations. Education, charities, trusts, governmental and parastatals, clubs, associations, co-ops, unions, and an endless variety of hybrids. To maintain their tax exempt or governmental status, nonprofits typically require governance and accounting controls. The "control" of interest to us for this issue is the nonprofit board of directors.

For business leaders, service on a nonprofit board is often treated as an afterthought. Many execs are strongly committed to the vision of the nonprofits whose boards they serve, and make major personal (and financial) investments in their goals. But even these board members tend to view sitting on a nonprofit board as an avocation compared to their "day jobs," or even to corporate board service. Short of a crisis, nonprofits tend to demand less time and bandwidth of their directors, and are noted for being largely safe when it comes to personal liability dangers.

This all tends to shape the impression that board and governance standards in the nonprofit world are lax compared to corporates. However, in some crucial ways, they may deliver even *better* board oversight. For starters, the past decade has seen corporate boards face far tighter compliance demands. Board time and effort must be diverted to reviewing disclosures and financials, leaving less time for strategy, advice, and mentoring management. The boards at most nonprofits face less of this compliance drudgework, giving them freedom to innovate, ask smart questions, and press for fresh results.

Many nonprofits also have more committed directors. Charities, schools, and associations tend to draw "cause" directors. You're a member because you have a passion for goals this entity works to achieve, and you're willing to govern without pay, and often contributing out of your own pocket. You believe, and this motivates you to lobby, volunteer and network for the organization with a zest even venture capital directors may lack.

Finally, any internet search for board advisors or consultants always delivers more who specialize in the nonprofit sector. Does this mean that nonprofit board members know less? I suspect it actually means they're just more willing to learn.

-- ***RDW***

STRATEGIC PLANNING FOR YOUR NONPROFIT

Strategic planning and the nonprofit board? Sometimes, that may seem like a contradiction in terms. Your board may be so tied up fretting over the next grant cycle, or federal/state budget, that "strategy" means wondering who to lay off if funding shrinks.

Yet there are approaches that nonprofits can take to map out a strategic road beyond the next quarter. Gary Patterson, who consults on governance issues and hosts the *Fiscaldoctor.com* website, shared a few tips with us:

- Ask yourselves where the organization will be in 10 years. Yes, this seems like a stretch -- "many nonprofits are so concerned with where they're going to get grants that they can't even imagine 5 years," says Patterson. Your board may need to jumpstart the conversation by investing in some outside consulting help. Even a one-day strategic retreat with a consultant can be the spark that turns long-term strategizing into a reality.
- Another problem facing the nonprofit world is weak understanding of the true costs of your resources. You have proper accounting, yes, but so much of what a nonprofit does is tough to quantify. How many hours do your volunteers invest annually? How is this allotted? Does this make the most sense (or are hot projects "overmanned," while less popular ones struggle for people to show up)? You know what you pay your CEO/executive director… but how many hours a week does she invest in the job, both in and out of the office? Again, what is the allotment of this time? Does she have to spend too many hours on nonprofitable "scut work?"
- How much time, effort and funding do you invest in new (under 3 years old) initiatives? How much of your resources go into older projects, maybe some reaching back to the launch of your nonprofit? Have you mapped out the benefits (financial, mission-oriented, supporting your stakeholders, etc.) of *all* your nonprofit's activities? Do a "bang for the buck" audit by each of these sectors, and you'll often find efforts that suck up resources, but no longer deliver value, or even well support your mission. "Every nonprofit has things it has been doing forever, but recipients don't value anymore," notes Patterson. Strategic planning frees you to shake up your menu of services, and make fresh decisions on how to allot limited resources.
- Is your nonprofit benchmarking against similar organizations? This is tricky, since "nonprofit" covers a huge range or organizations, with different funding, missions, legal structures, etc. But yours should belong to some associations in your sector that can offer valuable yardsticks. How do your funding/staffing levels compare? What are your income sources, and does a pie chart of yours look similar to peers? A good strategic dive into your organization's structure demands insight on how others are doing it.

5+ STEPS ON NONPROFIT CEO SUCCESSION

As I regularly scold our *BI* readers, CEO succession planning is a crucial board task that too many corporate boards still avoid. And the boards of nonprofits? They make for-profits seem dutiful. However, the broad nonprofit world faces some unique challenges in succession planning for executive leadership -- which require unique solutions:

- Board members of many nonprofits are focused on the mission of the nonprofit, the projects it takes on, and of course, endless money concerns. This means that long-term thought about executive leadership occupies a negligible slice of their governance mindshare. "Too often there isn't enough thinking ahead, so when the need arises, the board has to rush," notes Preeta Nayak, a partner in the San Francisco office of nonprofit resource Bridgespan. "This means less time to groom a successor, and often a poor fit." Long-tenured CEOs may be so identified with the nonprofit's mission that directors find it hard to visualize it without him or her at the helm. As noted in the article on strategic planning, it can help to bring in a consultant to help kick loose board thinking on an overall executive planning process.
- At parastatals, education, and other government-related entities, the board may play a limited role in selecting executive leadership. It may act in an advisory capacity, but some state ministry often drops in a chief executive based on civil service rules, politics, or some mysterious machinations that no one on the outside can decode. The board can still step up in these circumstances, however, by pushing for a sound succession *process*. Seek solid executive job descriptions, transparent, public vetting and selection, and true long-term planning, so successors work their way into the role.
- Traditional "nonprofits" in the charitable and civic sector place the board at the center of the executive succession process, but they still face hobbles. When it comes to internal succession, smaller nonprofits often have trouble properly paying a #1 executive, much less a #2. "Good succession planning should go at least 3 levels deep," says Gary Patterson (see above article). "But that doesn't happen at most nonprofits -- they just don't have a deep bench." Some smaller nonprofits make good use of interns and recent college grads to support their top executive. These are smart young folks who learn well -- and then leave for bigger opportunities. As one nonprofit director told me, "we do a great job of training executive directors… for someone else."
- A solution for this quandary is for the nonprofit board to do what no board really likes doing -- making some

bold, perhaps controversial, budget choices. "Paying for a successor is a problem," says Karen Eber Davis, who heads a nonprofit consulting ***firm*** and writes on nonprofit management issues. "But the board is in charge of making sure the nonprofit has the resources to be viable" -- and what resource is more vital that leadership? This can mean a fundraising push to pay for a proper successor-in-waiting, or juggling the budget to add administrative overhead. Although nonprofits are often judged by how tight this admin funding is, Eber Davis feels this is a false, and even destructive, measure. "Except in the most egregious cases, overhead is a very poor way to measure a nonprofit." Be willing to bite the bullet and divert funding to nurture future talent needs.

- Long-time executives (especially nonprofit founders), raise further succession issues. Most such nonprofits are small and focused enough that the entity's mission, structure, and organization may be shaped around this one person. This means a daunting pair of shoes for any new leader to step into. Long-term executives with a passion for your mission may well be paid under the market level needed to tempt new talent. "Often, the founder is paid peanuts, and you won't get the same level of talent for that when the founder leaves," observes Gayle Gifford, founder of Ceffect nonprofit board strategic consulting
- As noted, there are lots of good resources out there for nonprofits, including exec succession. The Annie E. Casey Foundation offers an excellent ***online guide***, and the Bridgespan Group consultants provide a good ***page*** of tips and links to resources.

BOARD SUCCESSION FOR THE NONPROFIT

Nonprofit planning on strategy and CEO succession is vital, but let's not forget those people you convene with once a month -- what about nonprofit board talent planning?

As with many other aspects, board succession for the nonprofit differs from that of for-profits. Not necessarily better or worse, just different. Here are a few things to remember:

- Give some study to your entity's bylaws on who becomes a director and why. Membership may elect representatives; directors may volunteer from the community; specific seats may be reserved… there is endless variety in nonprofit board makeup. Your board itself should weigh these rules, though, consider whether they still do the job, and have at least some say in qualifications.
- Roll out this study of board makeup into a consistent, objective board evaluation. How does the current board, its talents, representation, structures and commitment, match up with the goals you've set? (There are plenty of good nonprofit board ***evaluation*** tools out ***there***). What specific weaknesses in membership have you identified? Are there lacking areas of expertise your board will need going forward?
- Most nonprofits (except for high-status charities) don't have the problem of sorting through eager, qualified board applicants. Instead, they're endlessly trying to fill an empty board seat with someone who can do the entity the most good. Many nonprofits set goals for board members based on giving or bringing in funding -- why not add another target that each current director is expected to suggest at least one prospective new member per year?
- Long (often too-long) tenure is a problem found on the boards of many nonprofits. Perhaps your co-op or association has founding members who've been stalwarts from the very beginning. Or your local group board has a member who's long retired, but likes the company. Every director can recall at least one nonprofit board with an older member who tended to doze off at meetings.

"A well-designed nonprofit board has some elegant ways to let these directors know their time is finished," says Karen Eber Davis. Term limits are a blunt (if useful) instrument, but a more effective one can be a formal membership/nominating committee (which many nonprofit boards lack). The chair of the committee can take Old Joe out for lunch, and "ask if serving on this board is really still fun for him" suggests Eber Davis. She finds that Old Joe often will honestly say no, it isn't. A general board reorganization to make the board smaller (many nonprofit boards are too large) is another way to nudge retirements.

DO YOU *REALLY* WANT TO JOIN THAT NONPROFIT BOARD?

Joining the board of a nonprofit often seems an obvious career plus, particularly for rising board wannabes -- visibility, practical boardroom experience, networking, and often a cause that moves you. But one rule applies for both nonprofit and corporate boards -- asking first if this is a club you really want to join. What questions should you ask (and answers you should receive) before accepting that nonprofit board seat:

- What are your motivators? If it's a charitable or cause-related nonprofit, is the mission one you believe in?

Probably yes, but also do some digging into the entity's approach, funding, strategy and leadership. You may like the cause, but discover this group's priorities and implementation just aren't your style. "Know what you want to accomplish as a board member with them," advises Gayle Gifford.

- After learning what to expect from this nonprofit, clarify what they expect of *you*. Charities, civic and cause groups often expect board members to deliver on fundraising, either personally or by lobbying others. Problems arise if you join the board without asking (and them not telling), and then discover yourself on the hook for more than anticipated. "The good nonprofits say upfront what their expectations [on financial support] are," says Karen Eber Davis. "But if that information is not given, be sure to ask."
- Of course, more than money is expected of the nonprofit board member. The days when directors showed up at corporate board meetings to doze through reports, have a nice lunch, and then leave are long past, and nonprofit boards are moving in the same active direction. While you'll want to know about board and committee time demands, dig even deeper into other commitments. Events, fundraising, member relations, and affiliated group meetings and conferences are a major element of nonprofit service (and, of course, your time is gratis). As with the above point, learn as much as you can on the way in.
- Those with corporate and venture board background may view the nonprofit world as a safe oasis from the liability concerns that dog private sector governance, particularly in public companies. But that "corporate veil" isn't absolute. Courts in the U.S. have proven willing to find nonprofit directors liable for egregious oversight gaps (such as the recent ***Lemington Homes*** case in Pennsylvania). Nonprofits that handle large endowments or government funds, or that fall behind in tax liabilities, have particularly vulnerable directors. Again, ask about exposures as part of your due diligence, and query whether D&O coverage is offered, or if it would seem a wise addition.
- Another area to check out -- the quality of governance the current board offers. Is it a large one (as nonprofits often are), which can mean clumsy oversight? What is the committee structure, and how often do they meet? Are some recent agendas and minutes available for you to review? Can you sit down over a cup of coffee with the board chair to discuss governance goals and needs?
- Finally (and here's the big pay off) don't be afraid to frankly weigh how serving on the board of this nonprofit benefits you and your career. "This is a perfectly legitimate reason to be there," says Eber Davis. Part of the board recruiting process should include "saying to potential board members 'how can we help you in meeting other people.' Let new directors know you're here to help them." Who are the other board members? How could you add them to your network? How can you do well by doing good?

BOARD RISK OVERSIGHT - A 3-POINT PLAN

Smart oversight of risk has become one of the world's biggest boardroom headaches in recent years. The need is doubtless urgent, but enterprise risk management (ERM) is also a complex, esoteric subject that most boards lack the time, resources and expertise to monitor well.

That's why some information I've received from top-flight law firm Latham & Watkins caught my eye. Three L&W attorneys, Scott Hodgkins, Steven Stokdyk and Joel Trotter, suggested a 3-part plan to help boards frame their approach to risk oversight. I liked their approach, and asked if we could share it with *BI* readers.

A solid board ERM plan should meet several goals laid out by the Committee of Sponsoring Organizations (COSO) of the Treadway Commission. The board should: Concur with management's view of acceptable "risk appetite;" understand management's steps toward effective ERM; review the company's risk portfolio against its risk appetite, and; know the most significant risks and how management is responding. The L&W board risk blueprint does this with 3 steps:

- *Determine the board's preferred oversight model*. Typically, boards either retain primary responsibility for risk oversight or delegate it to a committee, such as the audit committee or a risk committee. If the board retains primary responsibility, committees may provide input on specific types of risk, such as compensation, audit and finance, and regulatory and compliance risk.

  The board should assign directors with the expertise to oversee unique market, liquidity, regulatory, innovation, cybersecurity and other risks that may require special attention. Also consider whether adding duties to an existing committee (such as audit) may be too burdensome.
- *State a board approach to risk management*. As with other policy statements, a risk management statement creates a tone-at-the-top benchmark for assessing opportunities as they arise, and helps shape management's

operational decisions.

A risk management statement should identify: Acceptable strategic risks; undesirable risks; specific risk tolerances in stated categories (strategic, financial, operational, compliance, etc.). In shaping the company's approach, the board should consider: Investor expectations; competitors' apparent risk appetite; stress tests for risk scenarios; long-term strategy versus core competencies; potential long-term market developments; risk concentrations; effects of new business generation on the risk profile, and; strategic planning and operations compared to your risk appetite.

■ *Assess board risk capabilities and effectiveness*, paying particular attention to possible cognitive bias or "groupthink." The board should consider: Directors' skills and expertise compared to the company's current and future operations; director education plans, or adding directors with new skills; delegating risk oversight in highly technical areas, such as cybersecurity; outside assessment of risk management practices, and; clear allocation of responsibility among the board committees and membership.

Q&A: Setting Our CEO Expense Policy

Q: "I'm a board member with a major regional economic development group, and have a question. We've recently become more involved in international trade missions, with our CEO traveling globally to represent us. This means that his business expenses have increased substantially. Our present CEO expense policy is fairly loose, and it may be time to upgrade to a system with better accountability. How do we shape a new CEO expense policy that avoids trouble, while not being too burdensome?"

***A*:** Smart move. Though not common, boards in both the private and public sectors are hugely embarrassed when their CEOs are caught using company expense accounts as their personal platinum cards. The former CEO of U.S. tech leader Polycomm not only lost his job for such abuse, but now faces SEC charges of defrauding investors through his luxe expenses.

Boards can be intimidated by the idea of writing a solid expense policy for the CEO, but shouldn't be. "This isn't rocket science -- you just need a policy on what spending is allowed, and the ability to verify it," notes Jim Ratley, CEO of the Association of Certified Fraud Examiners. This means laying out a guideline of what the board considers legitimate, work-related spending -- which means anything outside the guideline is on the CEO's dime. Set quarterly or annual estimates of reasonable amounts for travel, lodging, dining, materials, and so on.

The basic elements of a workable CEO expense policy will be: Authorization (empowering the CEO to incur expenses for your group); Receipts (or other independent documentation backing up the spending); reimbursement (stating that the expenses will be reimbursed, subject to approval by the CFO, auditor, or other authority). There are good guides for CEO expense policy language, such as from ***Concur***, or from ***Jitasa*** for nonprofits.

One self-imposed stumbling block for the board is treating your CEO's expense policy differently from anyone else's. Yes, your CEO's international travel for promotion will involve more entertainment and incidental expenses. But why should he have any less need to back up expenses with receipts? "In my experience, most competent CEOs want to have this spending verified," says Ratley.

COMING IN BOARDROOM INSIDER --

- *THE BOARD ROLE IN STRATEGIC PLANNING*
- *WHEN YOUR CEO BECOMES EXECUTIVE CHAIR*

RALPH WARD'S BOARDROOM INSIDER is published monthly for directors, CEOs, those who work with corporate and nonprofit boards (corporate secretaries, corporate counsel, support staff, and consultants), and those who are board prospects.
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