

# **Creating a Board that Delivers**

***Virginia Department for  
Aging and Rehabilitative  
Services***

***11/27/12***

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Presenter***

## Topics to be Covered

- What is a good board?
- What duties are imposed on board members?
- What role does the chair play in making the board outstanding?
- What tools can be used to make the board more effective and focused?
- What policies should every organization have?

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## The Nonprofit Sector Is Huge

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## The Nonprofit Sector

- The economic impact of the nonprofit sector can not be overlooked
  - 2 million organizations
  - 6 trillion in assets
  - 3.5 trillion in income
- The amount of assets exceeds the combined assets of the retail trade sector, transportation sector, and non tax exempt part of the healthcare sector

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## Virginia Nonprofit Sector

- 52,856 exempt organizations
- 139 trillion in assets
- 75 trillion in income

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## These are Public Dollars

- The magnitude and the amount of money in assets and income raises concerns with Congress, IRS and the public.
- Form 990 is being used to more carefully audit and monitor nonprofits by the IRS.
- What would everyone be looking at:
  - Proper fiscal and financial management
  - No private benefit or inurement
  - No diversion of assets or income away from charitable purpose
  - No political activities

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## What is a Good Board?

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### What a CEO Wants From a Board

- Better understanding of organization's work and clarity on organization's philosophy
- More engagement, sense of urgency
- More strategic focus
- Fundraising, bigger contributions, energy about fundraising
- Making better use of skilled, committed members
- More influence and affluence
- Board chair should lead rather than direct
- Constructive partnership

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### Building the Board

- Have the responsibilities and duties of members and officers described in writing
- Provide orientation prior to appointment
- Have the right number of directors for the times
- Boards evolve and morph based on
  - Strategic/Business Plan
  - Organizational Needs
  - Personality Types
  - Diversity
  - Community Anchors
  - Passion for Mission

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**An Ideal Board Member Is One Who,  
When Asked to Serve, Says ...**

***I don't think you want me on your board. I am contentious. I ask a lot of questions, and if I don't get the answers, I won't sit down.***

*Bernie Marcus, Home Depot Chairman*

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**What Duties are Required  
of Board Members?**

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**Federal Law  
501(c)(3)**

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**Public Support**

- A 501(c)(3) organization must be publicly supported
  - Receive at least one third of income from government or the general public
  - Or be organized and operated to receive such support from the general public.
- Fees for services are not considered support from the general public.
- Support from just a few individuals could jeopardize this requirement.

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**Private Benefit/Private Inurement**

- No part of the net earnings may inure to the benefit of any
  - private shareholder or
  - individual.

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**Political/Legislative Activity**

- A 501(c)(3) organization can not participate in or intervene in (including the publishing or distributing of statements), any political campaign on behalf of any candidate for public office.
- Lobbying is not a charitable purpose and therefore any legislative or lobbying activity can not be substantial.
- No substantial part of the activities of an organization can be carrying on propaganda, or otherwise attempting to influence legislation.

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**State Law**

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## Duty of Care – Common Law

- Requires officers and directors to
  - Exercise ordinary and reasonable care in the performance of their duties, exhibiting honesty and good faith.
  - Act
    - In a manner which they believe to be in the best interests of the nonprofit,
    - With such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances, and
    - In good faith.
- When the duty of care is properly exercised, there is no personal liability.

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## Meeting the Duty of Care

- Active participation in meetings – prepare and ask Qs.
- Exercise independent judgment/ do not rely on representations that “all is well.”
- Obtain adequate information on financials, expenditures, compensation, etc.
- Request assistance when needed – from accountants, legal counsel, organizational reports.
- Investigate when you suspect need for further inquiry.
- Follow the money.
- Define the duties delegated; oversee and monitor such duties.

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## Duty of Loyalty – Common Law

- This duty relates to the director’s motivation in making decisions. It encompasses a duty
  - To avoid conflicts of interest, and
  - To provide undivided allegiance to the nonprofit’s mission.
- A director shall not use a corporate position for personal advantage.
- A director should not compete with the nonprofit itself.
- All opportunities presented to the director which may be of interest to the organization should be brought to the organization for its consideration.

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## Meeting the Duty of Loyalty

- Only engage in the same "line of business" or areas of endeavor as the nonprofit, if doing so is in good faith and without injury to the nonprofit.
- Do not consider outside interests, including any organization that you are representing, when making decisions for the nonprofit.
- If a "corporate opportunity" is offered to you that is related to the activities or programs of the nonprofit or would be in the best interests of the nonprofit to accept or pursue:
  - First offer it to the nonprofit,
  - Only pursue the opportunity after it has been rejected by the organization, and
  - Have the offer and rejection recorded in the minutes.

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## Duty of Obedience

- **Duty of obedience**
  - To further the organization's exempt purpose
  - To dedicate resources to the organization's mission
  - To adhere to the governing documents
  - To comply with all applicable laws

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## Importance of Reviewing By-laws

- Must follow by-laws.
- Amend, not ignore, if they do not work.
- Make sure by-laws are authorized by and consistent with the Articles of Incorporation.

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## Reasonable Reliance

(Va. Code §13.1-870)

- A director must use good faith business judgment of the best interests of the corporation.
- A director may rely, unless such reliance is unwarranted, on information, opinions, reports or statements of
  - Officers or employees of the corporation whom the director believes, in good faith, to be reliable and competent in the matters presented;
  - Legal counsel, public accountants, or other persons as to matters the director believes, in good faith, are within the person's professional or expert competence; and
  - A committee of the board if the director believes, in good faith, that the committee merits the director's confidence.

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## Breach of Duties

- If the duties are breached
  - The director or officer could be personally liable.
  - The organization can lose its exempt status.
  - IRS may impose monetary sanctions.
- Directors cannot remain willfully ignorant of the affairs of the nonprofit.

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## Breach of Duties

- Examples
  - Selection of pension plan administrator based on personal friendship or favor without investigating the firm's competency or expertise
  - Engaging in self-dealing
  - Failing to safeguard confidential information
  - Seizing a corporate opportunity

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## Preventing a Breach

- Be informed and participate in the decisions of the organization.
- Oversee and monitor.
- Adopt policies for the conduct of business.
  - Conflict of Interest
  - Whistleblower
  - Procurement
  - Document Retention/Destruction
  - Investment
  - Financial Controls and Accountability

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## What Role Does the Chair Play in Making the Board Outstanding?

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## Effective Organizations Call for Effective Chairs

- A board must have a strong chairman whose primary purpose is to
  - create and maintain a spirit of unity among diverse people on the board.
  - ensure that the Board works appropriately with the executive staff in exercising its responsibilities effectively and ethically.
  - lead and to restrain, to blend in proper proportion the more capable and vocal members with the less experienced and silent ones.

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**What Tools Can Be Used to Make the Board More Effective and Focused?**

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**Tools to Control Board Meeting Effectiveness**

- Agenda
- Rules – procedural, time limits, order of participation, etc.
- Electing an effective chair/vice chair
- Have a parliamentarian
- Information provided to board in a timely manner
- Effective committee chairs

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**Concise but Thorough Meetings**

- Consent agenda
- Place information items at the end of the agenda.
- Allow members to take items off consent agenda, or move items to another point in the agenda.
- Provide written executive summaries for each action item.

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## Executive Summaries

- Describe the past, present, and future, obstacles, and opportunities
- Describe how the action item fits into strategic plan
- Refer to fiscal impact
- Indicate key staff
- Suggest the action desired of the board

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## What Policies Should Every Organization Have?

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## Conflict of Interest Policy

- A conflict of interest is a transaction (or contract) where the director has an interest that precludes the director from being disinterested.
- It can exist when an officer or director participates in the deliberation and resolution of an issue in which the director or a family member has a "material financial interest," i.e., payment of salary, contract fees, commissions, etc.
- If a conflict arises, full disclosure should be made to the organization, and the director or officer should refrain from participation in the organization's deliberation and resolution of the issue (i.e., recusal).
- It is important to be sensitive to and avoid apparent conflicts of interest as well as actual ones.

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## **Conflict of Interest State Law**

- A conflict of interest is a transaction in which the director has a direct or indirect personal financial interest, Va. Code §13.1-871.
- A transaction in which there is a conflict of interest can be voided unless
  - The material facts were known to all who participated,
  - The transaction was authorized, approved or ratified by a majority of disinterested directors or parties,
  - The transaction was fair.

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## **Financial Controls**

- Procedures for the timely and secure handling, depositing, and protecting assets and receivables should be developed.
- CEO/CFO should certify that the financial statements fairly present the financial condition of the organization.
- No single individual should be permitted to request, authorize, verify, and record expenditures.
- Checks and balances/ segregation of duties should always be in place.

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## **Management of Funds**

- Designate one person to oversee and monitor each grant and how the funds are spent.
- Make sure that funds are disbursed consistent with the donor's restrictions.
- Have a cash management policy – explore ways for cash to generate income.
- Establish good risk management policies that balance three sometimes competing goals:
  - Minimize risk
  - Easy access to funds when need arises
  - Earning a reasonable rate of return

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## Investment Policy

- **Components of an investment policy**
  - Establish objectives and capabilities.
  - One officer should be made accountable for overseeing the investment manager and any other consultants.
  - Develop an investment policy/ strategy.
  - Develop criteria for and select an investment manager.
  - Determine a suitable asset allocation.
  - Prohibit inappropriate investments.
  - Segregate duties/ second set of eyes to review transactions.
  - Have regular portfolio reviews.

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## Compensation Policy

- **Establish a policy on compensation and benefits that determines:**
  - Comparable benchmarks
  - Where salaries should be set in relation to these benchmarks – 80%, 120% and why
  - When exceptions can be made
  - Who has final decision on the salary offer
  - When raises will be given
  - What additional compensation should (or can) be offered

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## Compensation Plan

- Establish position descriptions for each position.
- Revise position descriptions when changes in duties occur.
- Re-evaluate compensation after a change in duties.
- Conduct periodic prevailing wage studies.
- Re-evaluate compensation as market conditions change.

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## Gift Acceptance Policy

- Identify what gifts will be accepted.
- Who has the authority to accept the gift?
- When legal review of terms of gift required and who will pay for that review?
- Who will assess value of gift?
- Who will acknowledge gift?
- What terms will be imposed on gifts that "continue to give" or are earmarked?

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## Document Retention and Destruction Policy

- Properly define "document" to include information of all types – electronic or paper, historical or transient business record.
- Designate who is responsible for each type of document and what authority that position has with respect to the documents.
- Establish the specific retention period for each type of document.
- Identify specific staff or functions that have appropriate read, write and edit access.

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## Document Retention and Destruction Policy

- If a file or folder contains multiple types of documents necessary for a coherent record, then the whole file or folder must be retained for the duration of the longest-held item.
- In digital documents, try to separate the documents in storage based on the duration period that they have to be retained.
- Establish the process for the removal of the documents from storage and the procedures for destruction.
- Remember that confidential information must be kept confidential even when in storage and when sent for destruction.

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## Whistleblower Policy

- **Persons Covered**
  - Directors/ trustees, officers and employees, volunteers, grantees, contractors and/or vendors who in good faith report suspected violations
- **Reporting Complaints**
  - Have a clear channel through which a person can report any suspected improper or illegal activity
  - Include examples
  - Indicate how and to whom the complaint can be made

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## Whistleblower Policy

- **Investigating and Resolving Complaints**
  - Identify the compliance officer or other person responsible for the investigation.
  - Have a back up person in case of a conflict.
  - State when and how suspected violations will be documented, investigated and resolved.
  - Specific procedures are recommended for investigating accounting and legal issues.
- **Key Concepts to Incorporate**
  - Anonymity and confidentiality
  - Be vigilant in reporting improprieties
  - Acting in good faith and consequences if complaints are made recklessly or maliciously
  - No retaliation against person bringing a complaint

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## Procurement Policy

- **A procurement policy should specify**
  - Who has authority to purchase
  - Scope of that authority
  - Requirements for procuring
  - Who has the authority to contract
  - Small purchases and credit card use
- **Competitive bids whenever possible**
- **Solicited bids or unsolicited bids**
- **Written bids v. oral bids**
- **Avoiding conflicts of interest**

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## Confidentiality Policy

- Define what is meant by confidentiality.
- Identify who is covered and what types of information and documents are confidential.
- Designate the person to respond to all requests for information.
- Have staff sign an acknowledgement of confidentiality, responsibilities and obligations.
- *"Everything within these four walls is confidential."*

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## FOIA Policy

- Freedom of Information Act applies to organizations, agencies, and corporations in the Commonwealth supported wholly or principally by public funds (Va. Code §2.2-3701)
- Records must be available to public within 5 work days of request.
- Notice of meetings must be provided to public at same time members receive a notice.
- Meetings open to public.
- Minutes of meetings must be kept.

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## Role of the Board

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## **Financial Oversight**

- **Board as a whole or committee**
  - Thorough review of financial statements
  - Build budget, monitor expenses
  - Approval of ED's expenditures
  - Monitoring credit card expenses
  - Establish segregation of duties for expenditures
  - Contract review and approval
  - Grant compliance
  - Insurance coverage

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## **Governance**

- **Adherence to by-laws**
- **Maintaining required number of members on board**
- **Filing reports with state and federal agencies**
  - IRS Form 990
  - Charitable Solicitation
  - State Corporation Commission annual reports
  - Registered Agent
  - Charitable Gaming Registrants

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## **Providing Policy and Direction**

- **Strategic Plan**
- **Financial Solvency**
- **Organizational restructuring such as mergers, partnerships, affiliates**
- **Ambassadors – but not spokespersons**

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## **Importance of the Clerk**

- **Maintain minutes**
- **Minutes need to capture**
  - **Substance of discussion**
  - **Votes, abstentions, removal from discussion**
  - **Approval of all contracts, loans, lines of credit**
- **Retaining/ preserving minutes**

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## **Role of the Executive**

- **Develop and execute business plan**
- **Hire and direct staff**
- **Maintain financial integrity**
- **Create and maintain significance of agency in community**
- **Forthright and accurate in projections**
- **Ability to turn on a dime**
- **Keep board informed**

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## **A good board is not a gift but a victory – what can you do to make your board great?**

- **Find the right people.**
- **Select persons to serve as chair who can listen/learn/lead.**
- **Have rules and performance expectations.**
- **Good practices and custodian policies.**
- **Monitor, question, evaluate and act always in the best interest of the organization.**

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***"Great boards do far more than just follow good governance rules.***

***Their members know how to ferret out the truth, challenge one another, and even have a good fight now and then."***

Jeffrey Sonnefeld, Harvard Business Review, September 2002, "What Makes Boards Great"

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## **Questions?**

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