dynamic solution associates

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Board Governance FAQs

This FAQ document was designed by DSA to provide general guidance with respect to best practices for nonprofit board governance. These materials were prepared with reference to the Principles Workbook for Good Governance and Ethical Practice issued by the Panel on the Nonprofit Sector and published by the Independent Sector and Board Source in 2009 (Principles Workbook). The answers to these questions have been framed so as to discuss the principle(s), core concepts as well as the corresponding best response. It should be noted that these core concepts are often interrelated and therefore, should not be regarded as independent concepts. References to principles below are to those cited in the Principles Workbook.

Board Composition and Roles

1. Should the Executive Director be on the board or take the role as board chair?

Principle and Core Concepts

It is best practice to separate the Executive Director, board chair and board treasurer roles in a nonprofit that has paid staff. Organizations without paid staff should ensure that the positions of board chair and treasurer are held by separate individuals. The segregation of duties is a key element to making sure that sufficient internal controls are in place so that an organization's best interest take precedence. The Executive Director is responsible for managing daily operations, the chair for leading the board on governance issues and the treasurer for the organization's management of financial records. *Principle 14: Separation of CEO, Board Chair and Board Treasurer roles.*

So long as there are adequate segregation of duties on the board, there is no bar to an Executive Director being on the board.

2. Should staff members be on the board?

Principle and Core Concepts

A substantial majority of the board should be independent. Independent members should not: (1) be compensated by the organization as employees or independent contractors; (2) have their compensation determined by individuals who are compensated by the organization; (3) receive, directly or indirectly, material financial benefits from the organization except as a member of the charitable class served by the organization; or (4) be related to anyone described above (as a spouse, sibling, parent or child) or reside with any person so described. *Principle 12: Board Independence.*

Staff members should therefore be discouraged from being on the board to ensure its independence.

3. Is it permissible for an organization to hire a board member as a consultant?

Principle and Core Concepts

The "duty of loyalty" requires board members to put the interests of the organization above personal and professional interests. A nonprofit should adopt and implement policies and procedures to ensure that all conflicts of interest, or the appearance thereof, within the organization and the board are appropriately managed through disclosure, recusal, or other means. *Principle 3: Conflicts of Interest.*

Hiring a board member as a consultant is automatically perceived as a potential conflict of interest. The board should establish if hiring this board member as a consultant is in the best interests of the organization. Only independent board members should decide on this issue given the facts and circumstances. Making this determination may involve obtaining an independent evaluation of the services proposed such as obtaining third-party quotes. This would allow independent board members to more fully assess if it would be in the best interest of the organization to hire a board member as a consultant.

Financial Transactions and Financial Oversight

1. Should an organization loan money to a board member?

Principle and Core Concepts

The funds of the organization should be used to advance the mission of the organization. A nonprofit should not provide loans (or the equivalent, such as loan guarantees, purchasing or transferring ownership of a residence or office, or relieving a debt or lease obligation) to directors, officers or trustees. *Principle 23: Loans to Directors, Officers or Trustees.*

Providing loans to executives and board members creates real and perceived problems. Loans should not be made to board members under any circumstances.

2. Should an organization borrow money from a board member?

Principle and Core Concepts

Board members should put the interests of the organization above professional and personal interests. *Principle 12: Board Independence.*

Independent members of the board should decide on whether it would be in the best interests of the organization to borrow money from a board member. Considerations should include reviewing the terms and conditions of the proposed loan as well as how this loan may impact the board member's ability to provide impartial input on future activities of the organization.

3. What should a budgeting process be?

<u>Principle and Core Concepts</u>

As bearers of fiduciary responsibility for the organization, the full board should approve the budget and receive regular financial statements to monitor the implementation of the budget. *Principle 22 Annual Budget, Financial Performance and Investments.*

All board members should understand their roles and responsibilities in overseeing the financial health of the organization. This includes ensuring that a process is in place to develop a well-considered and realistic budget. This budget should be reviewed and approved by the board before the fiscal year begins. The board (and staff) should regularly compare financial results to the budget.

Compensation and Personnel

1. Should board members be paid?

<u>Principle and Core Concepts</u>

A substantial majority of the board should be independent. Independent members should not: (1) be compensated by the organization as employees or independent contractors; (2) have their compensation determined by individuals who are compensated by the organization; (3) receive, directly or indirectly, material financial benefits from the organization except as a member of the charitable class served by the organization; or (4) be related to anyone described above (as a spouse, sibling, parent or child) or reside with any person so described. *Principle 12: Board Independence.*

The "duty of loyalty" requires board members to put the interests of the organization above professional and personal interests. To ensure the independence of the board, best practice dictates that board members should not be paid for their services.

2. How should an executive director's salary be determined?

<u>Principle and Core Concepts</u>

The board should hire, oversee, and annually evaluate the performance of the chief executive officer of the organization, and should conduct an evaluation prior to any chance in that officer's compensation, unless there is a multi-year contract in force or the change consists solely of routine adjustments for inflation or cost of living. *Principle 13: CEO Evaluation and Compensation*.

One of the board's primary responsibilities is to select and supervise the CEO who in turn is responsible for the daily management of the organization. The supervision of the CEO also includes conducting annual performance evaluations for the CEO. These evaluations should be a formal, documented process that is based on a clear job description and mutually agreed-upon annual goals. Compensation adjustments should be based on performance and tied to predetermined performance goals. It should be noted that the payment of excessive compensation can jeopardize an organization's IRS tax exemption.

3. Who determines the salary of staff members?

Principle and Core Concepts

One of the board's primary responsibilities is to select and supervise the CEO who, in turn, is responsible for the daily management of the organization. *Principle 13: CEO Evaluation and Compensation*.

The CEO's responsibilities for the management of the organization includes the selection and supervision of staff in line with the strategic direction set by the board. These duties include determining the salary of staff members and conducting their annual performance evaluations. The board, as the supervisor of the CEO, will in turn, review the CEO's salary determinations for staff to ensure that these figures are reasonable but competitive enough to attract and retain qualified individuals.

4. How should an organization determine the best staffing pattern?

Principle and Core Concepts

Similarly, to question 3 above, the CEO is charged with the daily management of the organization within the guidelines of the strategic direction set by the board *(see Principle 13 above)*.

The CEO has the technical discretion to determine staffing patterns. However, these determinations will be subject to the supervision of the board and should be determined by the needs of the organization and in line with its best interests. These decisions should also follow the strategic direction of the organization as set by the board. As a nonprofit organization operating for public purposes with public support, it is important that the organization makes the most effective use of its resources. This includes making sure that the organization is appropriately and efficiently staffed. The employees' needs should be considered but should never be put above the best interests of the organization.

Fundraising Responsibilities

1. As a board member, what is my role in fundraising?

Principle and Core Concepts

A nonprofit should provide appropriate training and supervision of the people soliciting funds on its behalf to ensure that they understand their responsibilities and applicable federal, state and local laws. *See Principle 31: Oversight of Fundraisers*.

In addition to oversight responsibilities of fundraisers, board members are expected to make a personally significant financial contribution to the organization, be an active participant in its fundraising initiatives and help set the strategic direction of its fundraising strategy. The board is ultimately responsible for attracting funding resources to ensure the financial viability of the organization and its programs. Unlike the private sector, nonprofits are sustained by voluntary contributions, grants and government contracts. Its continued operation is dependent on those from whom it seeks contributions and grants. Therefore, raising money to support the organization is a key priority and an important component of a board member's job description. Board members are often selected for their fundraising skills and/or networks.

2. I hear this all the time, "we are a working board, we don't have rich people and we don't raise much money", what is the correct response to this?

As set out in the answer to question 1 above, it is important for board members to take an active role in fundraising for the organization. Given that a nonprofit's financial viability is dependent on outside funding sources, fundraising is a critical part of a board member's duties. It is also standard for funders to ask what percentage of the board gives money to the organization. As leaders of the organization, the amount contributed on an annual basis should be financially significant for that individual. The level of each board member's donations are expected to vary according to individual circumstances. There is no "minimum contribution" required and certainly, no maximum. Board members should be strong advocates for the organizations and use their personal and professional networks to advance the mission of the organization through recruiting volunteers as well as raising funds.