CHAPTER 3

Nonprofit Governing Boards

The governing board of a nonprofit organization holds ultimate responsibility for ensuring that the organization serves its mission and for the overall welfare of the organization itself. And, as we discussed in Chapter 2, the board plays a critical boundary-spanning role in the open system of a nonprofit organization, connecting the nonprofit to its community and constituencies, often including important sources of financial support. Understanding the board's responsibilities and role and knowing how to work with the board is an essential skill of effective nonprofit managers, especially chief executive officers (CEOs). This chapter will discuss the nature and responsibilities of governing boards, some characteristics of boards that are effective, and some challenges faced by nonprofit boards today. It also will consider the important question of the relationship between the board and the organization's CEO. But before we get started, it is important to clarify some terminology.

The boards we are concerned with here are those that have a legal responsibility for governing their organizations—they are *governing boards.* Nonprofit organizations may have various groups that are called "boards" but that do not have such responsibilities—for example, advisory groups that may contribute their expertise to the organization and help raise funds but that do not hold any legal authority for its governance. Such boards often play an important role in the organization, but they are not governing boards and will not be the focus of this chapter.[1]

Nonprofit organizations may use different terms to identify their governing boards. Most nonprofits are chartered as corporations, and members of the governing board are directors of the corporation under the law. Thus, many organizations use the term *board of directors* to identify them. Educational, cultural, and medical institutions often use the term *board of trustees.* Other organizations may use the term *board of governors, governing council*, or something else to describe their governing boards. This book generally uses the generic term, *governing board*, except when discussing the board of a specific organization, in which case it maintains the name that organization uses.

In many cases, the person who heads the board is called the "president" of the organization, and the paid staff person who manages the organization is called the "director" or "executive director." Some nonprofits—for example, universities, hospitals, and major arts and cultural institutions—have adopted corporate terminology, calling the head of the board the "chair" and the paid executive the "president." Others have adopted another corporate term, *chief executive officer*, or just "CEO," to identify the top paid staff person. This chapter refers to the top board officer as the "chair" and the paid executive of the organization as the "CEO."

One more point before we begin our discussion. The previous two chapters have drawn primarily from the academic literature, but this chapter relies much more on the practitioner literature. A substantial literature on boards has been developed by practicing nonprofit managers and consultants who work with boards and CEOs. Most of it *describes* what boards do or *prescribes* practices that boards should follow. Although the body of academic research on nonprofit boards is growing, it is still "limited, exploratory, and diffuse" (Callen, Klein, & Tinkelman, 2003, p. 496). This chapter draws on some of that research where it is especially relevant, but the practitioner literature is the more extensive, and it is the largest source of citations in this discussion.

TYPES OF GOVERNING BOARDS

Nonprofit governing boards are not all the same. For one thing, they differ in the way their members are selected. This may have important implications for how they operate and what agendas, priorities, and pressures members may bring to their work on the board. Different types of boards also may interact differently with the organization's CEO. For anyone working in a nonprofit organization, especially as a CEO or other senior executive, understanding how individuals come to be sitting at the governing board table is essential to understanding and working successfully with the board. Working successfully with the board is critical not only to the executive's effectiveness. Since in most cases the CEO is appointed by and reports to the board, it is also essential to his or her professional survival.

Elected Boards

Some boards are *elected* by the membership of the organization. This is common in member-serving and social welfare organizations. The methods used to elect the governing board vary; for example, some elections are conducted by mail, and others are conducted at an annual meeting. Depending on the political and cultural environment within the organization, elections may be contested, and some individuals may, in effect, campaign for seats on the board. In other cases, a nominating committee of the existing board presents recommended candidates, who are often approved in a proforma vote by the membership. Some procedures are multistaged and complex. Consider, for example, the process followed by the American Psychological Association:

> As in all democratic systems, the ultimate power is in the hands of the voters, in this case, the members of APA. The members of APA exercise their power through direct vote and through the election of members to serve on the Council of Representatives. The primary constituencies from which the representatives are elected are the divisions, which are an integral part of the Association, and the state and provincial psychological associations, which are affiliates. The number of representatives to which each is entitled is determined by an

> apportionment ballot in which members allocate votes among the constituencies according to their own priorities.
>
> The Council of Representatives has broad authority to develop the internal and external policies of the Association, within the framework of the charter and the bylaws. It has full authority over the affairs and funds of the Association. The Council elects almost all elected positions: the Board of Directors, the treasurer, the recording secretary and the chief staff officer. But the president, who is directly elected by the entire membership, chairs both the Council and the Board of Directors. (American Psychological Association, 2005)

Having an elected board may result in uncertainty about who will govern the organization from one year to the next—the outcome of elections is not always assured, and this may present a challenge to the CEO. What the board expects of the CEO may change; alliances and factions on the board may develop and shift; and the board's values and priorities may be dynamic, as political and philosophical cross-currents among the membership find their way into the boardroom. The controversy that surrounded the election of the Sierra Club's board in 2004 provides an interesting illustration.

In 2004, anyone could join the Sierra Club with a $25 dues payment, and all members were eligible to vote in the election of the board. (That was an unusually low threshold for voting eligibility. Many organizations limit those eligible to vote to members who have been active for a period of time or use an intermediate body like the APA's Council of Representatives.) The Sierra Club's board included 15 members, and five seats were open for election in 2004. Individuals who were strong advocates for more restrictive U.S. immigration began to organize and encourage people sympathetic to their views to join the Sierra Club. Their goal was to have their sympathizers elect new board members who would change the Club's position on the immigration issue. Within three months, 30,000 people became new members of the Sierra Club, compared with only 22,000 the previous year. Some of these new members had been organized by the anti-immigration candidates who were, in effect, running for the board. The election became contentious. Some described the outsiders' efforts as a "hostile takeover" and accused them of pursuing "the greening of hate." Others portrayed their efforts as addressing needed reform in the Club's operation and claimed that their election would increase the Club's effectiveness (Greene, 2004).

The insurgents did not prevail, but the Sierra Club case illustrates the potentially tumultuous environment that may be created when governing boards are elected by an organization's membership. To be the CEO of such an organization requires a high tolerance for discussion, debate, and uncertainty. In addition, the membership terms of an elected board tend to be relatively brief, and turnover on the board may make it difficult for it to sustain its focus on long-range goals and plans. Doing so requires considerable repetition of presentations and discussions, to maintain consensus among the changing membership of the board. It may be difficult to motivate members of an elected board to make gifts or engage in fundraising, since the ability and inclination to do so have not been the criteria in their selection. The skills of board members may be uneven, since their personal popularity or their positions on certain issues may have been the considerations in their election. However, elections do help ensure that the board will be representative of the constituency the organization serves and that the organization and its executive will be responsive to members' views and priorities. Elected boards are less likely than the next type, self-perpetuating boards, to become stale, uninvolved, or homogeneous in their membership.

Self-Perpetuating Boards

Most charitable nonprofits have *self-perpetuating boards.* New members of a self-perpetuating board are selected by the existing members of the board, who identify and enlist individuals according to criteria established by the board itself. When a new nonprofit organization receives a charter, it must identify the original, founding members of the governing board. Those individuals then have the authority to develop bylaws, which specify the total number of members of the board. The original board members then may select others to join them, up to the maximum permitted under the bylaws (which, of course, the board retains the authority to change). As individuals leave the board or complete their terms of service, the remaining trustees select others to take their seats, and this cycle continues as long as the organization exists.

In contrast to a board elected by the membership, a self-perpetuating board creates a relatively stable situation for the organization and its CEO. Although the bylaws of many boards do limit the number of terms that members may serve, self-perpetuating boards tend to have longer terms than elected boards, and the board's membership changes more slowly. Thus, the board's policies and culture may reflect continuity, reinforced by the tendency of its members to select successors who generally share their values and views. Indeed, in some cases, strong or long-serving CEOs may gain significant influence in the selection of board members, in effect choosing their own bosses.

One advantage is that a self-perpetuating board can craft its own membership, selecting individuals specifically to bring needed skills or augment its strength in areas important to its work. Many boards maintain an inventory of the expertise and connections represented among their members and make a systematic effort to identify and recruit new members to fill any identifiable gaps. For example, if someone with financial expertise is needed, the board can seek out such an individual and recruit him or her to join the board in order to add those skills. A social service organization may try to find someone with professional social work experience, who can help the board evaluate program recommendations from its staff. If the organization desires to increase the amount of support it receives from corporations, the board can identify and recruit corporate executives who may be helpful in that regard.

But these advantages of the self-perpetuating board are accompanied by some potential weaknesses as well. One is that the board may come to be unrepresentative of the constituency or community the organization serves. If the existing members of the board do not recognize the importance of diversity, they may continue to select new members who are just like them, drawing on their own business and social circles to fill board openings. Over time, the organization could become out of touch and be unable to adapt sufficiently to changes in its environment. Another risk is that a self-perpetuating board may become too stable in its membership and too complacent. There have been cases in which self-perpetuating boards, without the scrutiny that comes from the broader constituency of the organization, have been too lax in their oversight of their CEOs or even the behavior of their fellow board members, with disastrous results for the organization.

Appointed and Hybrid Boards

A third way in which board members may be selected is through appointment by some authority outside the organization. This is the typical model for public organizations; for example, the boards of state universities are usually appointed by the governor of the state. Few nonprofits have totally appointed boards, but some do have some appointed members. This is sometimes the case in nonprofit organizations that are affiliated with a religious congregation, which may have board members appointed by a church authority. Colleges and universities may have board members appointed by an alumni association. Organizations that work closely with government may have some board seats held by individuals who are appointed by a governmental authority. Boards also may have some seats that are held ex-officio—that is, designated to be held by the individual who holds a certain office or position. For example, the head of the board of trustees of the Catholic University of America is the Archbishop of Baltimore, who serves ex-officio. The organization's CEO often holds a seat on the board in an ex-officio capacity, which may come with or without a vote.

Some boards are hybrids, with some members being elected, some appointed, some self-perpetuating, and some serving ex-officio. Until recent reforms, the Board of Governors of the American Red Cross was an especially complex hybrid including 50 members. Eight were appointed by the President of the United States (an appointed component); 12 were at-large members elected by the governors themselves (a self-perpetuating component); and 30 were elected by delegates representing Red Cross chapters and Blood Services regions across the country (an elected component). The President of the United States served as the honorary chair of the Board of Governors in an ex-officio capacity (www.redcross.org).

Hybrid boards may represent the best of both worlds, encompassing an elected component that helps keep the organization responsive to its constituencies; a self-perpetuating component that provides stability, continuity, and perhaps financial support; and an appointed component that ensures the organization's accountability to a parent organization or government. However, hybrid boards also can present challenges. For example, if elected, appointed, and self-perpetuating members hold different views or agendas, stalemate may result. Ex-officio members may not always feel a real commitment to the organization and its mission, having just landed on the board by virtue of some other position they hold. If this is the case, they may not fully participate in the work of the board or develop a full understanding of the organization and its work. Indeed, following criticisms of the American Red Cross's response to Hurricane Katrina in 2005 and the resignation of its then president Marsha Evans, some cited the structure of the board as an area of needed reform. After a long study, the Red Cross announced in October, 2006, that it was undertaking major changes to its board to strengthen the organization's governance. The planned

TABLE 3.1 Types of Governing Boards

Type of Board	*Advantages*	*Disadvantages*
Elected	Helps ensure that the organization and the CEO will be responsive to members' needs and priorities	Political division among the membership may create disagreement on the board Turnover on the board may make it difficult to sustain the board's focus on long-term goals and plans Skills of board members may be uneven, since personal popularity or positions on issues may influence election
Self-perpetuating	Can maintain continuity of culture, priorities, goals Can craft the board membership to gain needed skills Can select members who are helpful in fundraising	May become unrepresentative of the community or constituency May become too stable to respond to changes in the environment May become too passive and yield too much authority to the CEO
Hybrid (including appointed, self-perpetuating, ex-officio)	May combine the responsiveness of elected boards, the stability of self-perpetuating boards, and accountability to an appointing authority—for example, a sponsoring church	Different interests and loyalties of board members may lead to a stalemate Ex-officio members may not be fully committed to the organization

reforms would include reducing the membership from 50 to 20 and increasing the number of self-perpetuating members. Under the new structure, individuals appointed by the president would serve on an advisory committee rather than as regular members of the governing board (Schwinn, 2006b).

THE BOARD'S RESPONSIBILITIES

Now that we understand different types of boards and how their members come to sit at the table, exactly what are their responsibilities? And to whom are they accountable for meeting those responsibilities? The answers are not always simple.

As Bruce Hopkins (2003) describes it, nonprofit governing board members are "fiduciaries of the organization's resources and guardians of its mission" (p. 1). The board is accountable, that is, answerable, "for everything the organization does and how those things are accomplished" (Howe, 2002, p. 30). In the corporate world, it is clear to whom the directors are accountable and for what they are accountable. Members of the corporate board of directors are the agents of the owners (the principals), and their responsibility is to direct and monitor the activities of management in the interests of the owners. Those interests also are quite clear—the maximization of economic value, consistent with sustainability of the business and the values of the owners. There are, of course, boards in the public sector as well. Most of them also have an identifiable constituency whose interest they serve; for example, a city council is accountable to the citizens of the city, who elected them. But in the nonprofit sector, it is not always so clear to which owners the governing board is accountable.

Perhaps the owners of a member-serving organization are the members—it is primarily their interests that the organization exists to serve. But suppose the organization is a professional association that also sets standards for practice and certifies members of the profession. It may be primarily a member-serving organization, but doesn't the public—especially individuals served by members of the profession—also have some interest at stake? Who owns a charitable nonprofit, chartered to pursue a mission in the public interest? Are the owners the donors who support the organization through their philanthropy, the clients served by the organization, or perhaps the general public? If it is the general public, how can the board serve its interests when there may not be consensus about what the public interest means? Without the simple measure of results that the bottom line provides to business, by what standards should a nonprofit's effectiveness be evaluated, and who should determine those standards? Without clarity or agreement about who owns the organization, it is difficult to answer those questions. This creates an environment in which the board's responsibilities and role may be the subject of discussion and debate.

The Board's Legal Responsibilities

Some governing board responsibilities are unambiguous. They are defined by law. Most law affecting nonprofit boards is state law, enforced by state attorneys general and state courts. However, the federal government, and specifically the Internal Revenue Service (IRS), has gained increasing power in recent years, and current debate surrounds proposals to increase the federal role.

A landmark case in 1974 is often cited as providing the most definitive statement of nonprofit board responsibility. In that case, *Stern v. Lucy Webb Hayes National Training School for Deaconesses and Missionaries* (usually known as just "The Sibley Hospital Case"), parents of children who had been patients at the hospital alleged that members of the board had mismanaged the hospital's assets and had placed hospital funds in accounts at banks in which they had personal financial interests. The parents claimed that hospital charges were unnecessarily high because of actions by the board. Judge Gerhard Gessell found that the Sibley board members had not really benefited financially and that the hospital had not been disadvantaged by the board's practices—in other words, the parents lost, but in the process of stating his decision, Judge Gessell clarified the standards of legal responsibilities of nonprofit boards that are still applied. Those responsibilities are summarized as the concepts of *care, loyalty*, and *obedience.*

Care, Loyalty, Obedience

"Care" in this context means paying attention and exercising due diligence in monitoring the organization's finances and supervising the actions of its management. Board members who do not attend meetings, who sleep through meetings, who do not read board materials, or who vote without understanding the issues are guilty of a lack of care. Included within the concept of care is the requirement that members of the board act in a prudent manner in managing the organization's finances—for example, by ensuring that any endowment assets are invested in a diversified portfolio to minimize risks. This does not mean that the board will necessarily have violated its responsibilities should it make the wrong investment decisions and the organization's assets decline but merely that it should exercise common sense and not lose money as a result of recklessness, indifference, or failure to seek appropriate advice.

The duty of loyalty means that members of the board put the interests of the organization above their own personal financial interests or that of another organization with which they may also have a formal relationship. Individuals cannot use their position on a nonprofit board to enhance their own businesses or financial position. Closely related to the concept of loyalty is that of *conflict of interest*. A conflict of interest may arise, for example, when the board has to vote on whether to give a business contract to a company that may be owned in whole or in part by a member of the board itself or that perhaps may employ a board member's relative. Or a conflict could exist if the board is voting to enter some kind of partnership with another nonprofit and one of the members voting serves on both boards. Conflicts of interest are not unusual, especially in smaller communities, where there may not be much choice about which suppliers or contractors the nonprofit can use and where prominent business leaders who own those businesses may serve on multiple nonprofit boards. Conflicts of interest are not per se illegal, but it is important how the board deals with them. Well-managed boards have formal conflict of interest policies that describe the procedures to be followed. Such policies usually require that potential conflicts be disclosed and that the board independently determine that any business transaction that gives rise to the conflict is not disadvantageous to the organization.

A legal concept related to conflict of interest is that of *private inurement*. Anyone who is an insider, generally any board member or officer of the organization, cannot unreasonably benefit from the organization's funds. This is related to the nondistribution constraint that was previously discussed. Nonprofits cannot use their profits to benefit owners, nor can they pay unreasonable amounts to board members or executives, which might have the same effect as sharing the profits with them—that is, giving them financial benefits as if they were owners. For example, a board can pay its CEO a salary and other compensation that is reasonable in exchange for his or her services, but anything exceeding a reasonable amount may be illegal private inurement. And an organization can do business with a company owned by a board member, but only if the payment is appropriate for the goods and services received.

The duty of obedience requires that the board makes sure that the organization is complying with the law and, in addition, that any decisions or actions taken are consistent with the organization's mission and governing documents, including its charter. Following the law may seem a simple charge, but ensuring that the organization does not drift from its mission may require greater vigilance, especially if that drift may bring with it some unanticipated risks.

Intermediate Sanctions

In general, if a board member carries out his or her duties faithfully and prudently, he or she is unlikely to be found personally liable for any losses that the organization may incur. Just making a mistake, or even a bad decision, is not in itself a violation of the board's responsibilities, provided that one has met the standards of care, loyalty, and obedience in making it. However, the risks to individual board members are somewhat higher today than they were prior to 1996, when federal legislation was passed providing IRS with the authority to impose *intermediate sanctions*—that is, financial penalties to punish individuals who engage in or permit improper transactions.

Prior to the passage of intermediate sanctions, virtually the only weapon available to the IRS in dealing with a nonprofit board that violated its fiduciary responsibilities was to drop the atom bomb by revoking the organization's tax-exempt status. Facing an all-or-nothing situation and reluctant to take a drastic step that might essentially impose a death sentence on the organization, the IRS had few options. Intermediate sanctions provided a fly swatter alternative to the atom bomb by permitting the IRS to impose penalties on *individual* board members or officers who engage in an *excess benefit transaction,* meaning one in which "a person's level or type of compensation is deemed to be in excess of the value of the person's services" (Hopkins, 2005, p. 219). The intermediate sanctions legislation and the regulations that the IRS has issued pursuant to it are complex and beyond the scope of our discussion here, but the penalties can involve return of the excess benefit received as well as additional penalties. Because it made the possibility of IRS action more than a remote threat, the passage of intermediate sanctions was a wake-up call to nonprofit boards. Faced with a more realistic possibility of IRS action, which could involve financial costs to individual board members, many boards quickly adopted new or more stringent conflict-of-interest and disclosure policies and standards for reasonable compensation.

Sarbanes-Oxley Act

In the wake of corporate governance scandals in the early 2000s, including the demise of Enron and WorldCom, Congress passed the Sarbanes-Oxley Act in 2002. Sarbanes-Oxley placed new requirements on the governance of publicly traded for-profit corporations. Only *two* provisions of Sarbanes-Oxley apply as well to nonprofit organizations, those regarding the destruction of documents and protection for whistle-blowers. However, Sarbanes-Oxley served as another wake-up call for nonprofit boards, and larger nonprofits in particular have voluntarily adopted some or all of its provisions (Williams, 2006, p. 59). Independent Sector and BoardSource have recommended that nonprofits voluntarily adopt some provisions of Sarbanes-Oxley, including those prohibiting loans to board members or executives, requiring the CEO's approval of the organization's Form 990, and requiring the creation of separate audit committees of the board for those organizations having outside auditors. In addition, some state laws—for example, the California Nonprofit Integrity Act of 2004—have incorporated Sarbanes-Oxley-type requirements. Sarbanes-Oxley will be discussed again, in more detail, in a later chapter of this book.

The Board's Functional Responsibilities

The law primarily dictates the things nonprofit boards *cannot* do—fail to exercise care, place its own members' individual interests above those of the organization, or lead the organization in directions inconsistent with its mission and the law. But what is it exactly that boards should *do*?

A number of authors have offered lists of a board's functional responsibilities—that is, job descriptions that list the duties that boards should perform (see, e.g., Axelrod, 1994; Ingram, 2003; Nason, 1993). Most lists are similar on the principal activities in which the board should be engaged, although there are often differences among the experts with regard to the division of specific tasks between the board and the organization's CEO. The following responsibilities are common to most board job descriptions, although, as we will see later, some authors express contrary views.

Appoint, Support, and Evaluate the CEO

Although the CEO may serve as an ex-officio member of the board, he or she is generally appointed by the board and serves at the pleasure of the board, subject, of course, to any contractual terms that may be negotiated at the time of appointment. However, having appointed the CEO, the board also has a responsibility to support that individual. That includes acting as a sounding board for the CEO to discuss ideas and problems and also coming to his or her defense when pressures may arise from within or outside the organization. If the board's response to every criticism of the CEO's actions is to challenge him or her or take the side of the critic, the board will quickly undermine the CEO's ability to be effective and it is unlikely to attract or retain a strong executive. But the board also is responsible for setting expectations for the CEO, monitoring his or her performance against those expectations, and providing the executive with performance evaluations. Of course, if expectations are regularly not met, the board also has the responsibility of dismissing the CEO and beginning a search for his or her successor.

The relationship between the governing board and the CEO is complex, and it is a topic that generates its own considerable literature. The subject is of such importance that we will return to a more thorough discussion of it shortly.

Establish a Clear Institutional Mission and Purpose

Establishing the organization's mission is the responsibility of its board. Although the organization's charter states its purposes in broad terms, the board can and should periodically review its mission; indeed, doing so is often the first step in the process of strategic planning.

Approve the Organization's Programs

Although experts advise boards to avoid becoming involved in the details of management, most think that the board should approve the programs undertaken by the organization, to meet its responsibility for ensuring adherence to the mission and protecting the organization's financial viability. For example, the board of a liberal arts college would need to consider whether establishing a business school would be consistent with its mission, the implications for the college's financial resources, and the ability of the college to maintain its academic standards and reputation in light of such an expansion of its programs. The board of an organization serving dinner to the homeless would need to consider any extension of its activities to provide medical services or transitional housing. Because such decisions relate directly to the mission, which is the responsibility of the board, they cannot be delegated to the CEO or the staff.

Ensure Sound Financial Management and the Organization's Financial Stability

Protecting the organization's assets is, of course, central to the board's legal responsibility as fiduciary. Most boards approve annual budgets and receive regular reports of the organization's financial status. Many boards, especially since the passage of Sarbanes-Oxley, also have separate audit committees that meet with outside auditors of the organization's finances (Williams, 2006, p. 59).

Some authors claim that board members' responsibility to ensure the organization's fiscal soundness implies an obligation to provide their own gifts and actively engage in fundraising. Indeed, except perhaps for the debate about the appropriate relationship between the board and the CEO, no subject commands more ink, or more lung power, than the role of the board in giving and raising philanthropic funds. Of course, not all boards are expected to provide their personal financial support to the organizations they serve. Boards of member-serving organizations often have no significant responsibility for fundraising, since the largest portion of revenue may come from dues, subscriptions, or meeting fees. Organizations that are primarily or entirely dependent on revenue from government contracts and grants also may not place emphasis on the board's fundraising role. But in most charitable nonprofits, the board is expected to play a significant role in providing and soliciting philanthropic funds.

There are divergent views on whether board members should be required to give or raise a specific minimum amount, and the question raises some complicated issues. Some boards require a minimum personal gift from each board member. But if this requirement is substantial, it may make it more difficult to achieve appropriate diversity among the board membership without making exceptions to the policy for those who may bring important skills and qualities but do not possess financial capacity. But making such exceptions may introduce the perception that there are two classes of board members—those who give and those who don't. If that perception exists, those who cannot provide financial support may too readily defer to those who are known to be important sources of support to the organization. On the other hand, if the minimum is set so low that all board members can meet it, it can have the effect of converting an intended floor into a ceiling. In other words, some board members who have the financial ability to give more than the minimum may come to see the minimum as all that is expected of them, foreclosing the possibility of larger gifts. Such a situation leaves potential "money on the table" (Rosso, 1991, p. 139; Worth, 2005, p. 73).

Some boards do not set a minimum for personal giving by board members but adopt what is often called a *give-or-get policy*, requiring that each board member either give personally or solicit gifts from others to total the minimum amount. But this may also be a standard that some board members may find difficult to meet, especially if they are not involved in business or professional circles that provide access to wealth. And it raises the risk that board members may solicit gifts without coordination by the organization's staff, creating a potentially chaotic situation that could alienate donors. An alternative to setting minimums for board giving and getting is to simply establish the expectation that each board member will give and participate in fundraising proportionate to his or her capacity to do so. If that standard is firmly embedded in the culture of the board, then conscience and the judgment of peers may motivate the board to its peak fundraising performance without the risks inherent in defining specific minimum amounts. Whatever approach is taken by individual boards, the subject of the board's responsibility for giving and fundraising is on the agenda for discussion at many nonprofit organizations today (Worth, 2005).

Establish Standards for Organizational Performance and Hold the Organization Accountable

The board should define the standards by which an organization's effectiveness in achieving its mission is to be evaluated. Establishing standards to judge whether the organization is effectively employing the resources entrusted to it in pursuit of its mission is a fundamental aspect of the board's responsibility to those who provide financial support, to the society that grants the organization exemption from taxation, and to those whose needs its programs serve.

Some authors see the role of nonprofit boards as especially important because many nonprofits do not face the same market discipline that business firms do. As John Carver (1997) explains, "Without a market to summarize consumer judgment, [a nonprofit] organization literally does not know what its product is worth . . . In the absence of a market test, *the board must perform that function*" (p. 7). Christine Letts and colleagues (1999a) elaborate on this point:

> Compared to their for-profit counterparts, nonprofit boards carry a much bigger burden in demanding and supporting performance . . . [In the for-profit world] both boards and management can use market feedback to assess how well they are performing: customers, investors, and creditors all make evaluations that eventually show up in the bottom line. . . . In contrast, the nonprofit board must often substitute for many of the feedback systems available in the marketplace. Nonprofit clients very often do not have a choice of providers, and are therefore unlikely to signal dissatisfaction by "voting with their feet." [Funders of nonprofits] may signal dissatisfaction by withdrawing their support,

> but are much less likely to play the affirmative role of a shareholder activist or institutional investor. (p. 133)

For these reasons, Letts et al. (1999a) argue that "nonprofit boards are more vital [than for-profit boards] in ensuring performance and accountability."

THE BOARD AND THE CEO

The relationship between the governing board and the organization's CEO is the subject of an extensive literature, reflecting divergent views. The questions addressed in this literature go well beyond who does what. Rather, they include fundamental assumptions about the nature of nonprofit governance and leadership.

At the heart of the matter is the question of who leads the nonprofit organization. In some organizations, the CEO may be dominant, with the board playing a passive role. The CEO proposes and the board disposes, often with little discussion or debate. As noted before, the CEO may even come to influence the selection of board members, in effect choosing his or her own bosses. This situation could arise in any organization, but it is especially common in organizations led by their founders, a special case we will discuss further in Chapter 4.

The realities of many organizations may enable CEOs to gain the upper hand. Boards are composed of "part-time amateurs," while the organization's staff, including the CEO, are "full-time professionals" (Chait, Holland, & Taylor, 1999). In other words, the CEO may know more about the organization and its programs than do the lay trustees, especially if its programs involve highly technical services, and board members may be reluctant to show their ignorance by questioning. Large boards pose a special challenge in this regard. Individual board members may be unwilling to risk embarrassment by challenging a CEO's proposals in front of a large number of other board members or may assume that others on the board are well-informed and just go along with what appears to be a consensus. The CEO may control access to information about the organization, and indeed, the CEO may be the only one who knows what information actually exists. He or she may determine what information reaches the board and develop the agenda of matters that the board will even get to consider. In sum, it may be possible for a CEO to manipulate the board, orchestrate board meetings, and relegate the board to the role of a rubber stamp for his or her initiatives.

The danger in such a scenario is that the CEO could lead the board and the organization in directions that are inappropriate or risky and that the board may not be able to meet its responsibilities for ensuring adherence to mission, fiscal soundness, and optimum performance. But an alternative scenario in which the board micromanages the organization and usurps the authority of the CEO is no better. Such a board is likely to find it difficult to attract or retain a strong chief executive and may find itself making decisions about details outside its expertise. What most experts recommend is neither of these extreme scenarios but rather a partnership between the board and the CEO in the leadership of the organization.

There are, however, different views on exactly how this partnership should be constructed and operate.

Various authors have addressed the subject of the board-CEO relationship, and a comprehensive review would be beyond the scope of this chapter. But let's compare the thinking of three sets of authors who are widely cited and whose different approaches highlight the major issues. First, we will look at John Carver's (1990) "policy governance model," described in his book *Boards That Make a Difference* and in subsequent editions published in 1997 and 2006 (Carver, 2006). Carver draws a clear line between the board's responsibility for *policymaking* and the executive's responsibility for *implementation* and provides what he calls an "operating system" to ensure that the distinction is maintained. Next, we will review the concept of "governance as leadership," described by Richard Chait, William Ryan, and Barbara Taylor (2005) in their book of that title, which was sponsored by BoardSource and which BoardSource uses as the foundation for its advisory work with nonprofit boards. Chait et al. target Carver (2006), writing that "governing is too complicated to reduce to simple aphorisms, however seductive, like 'boards set policies which administrators implement'" (p. 5). Instead, they advocate a leadership role for the board that blurs the distinction between policy and implementation and focuses the attention of both boards and CEOs on "what matters most." And, finally, we will consider the research of Robert Herman and Dick Heimovics (2005), who argue that the most effective CEOs are those who accept the reality of their "psychological centrality" in the organization and provide "board-centered leadership," working to "develop, promote, and enable their boards' effective functioning" (p. 157).

Carver's Policy Governance Model

According to John Carver (2006), boards should be the leaders of the organization, "not by invading territory best left to management but by controlling the big picture, the long term, and the value laden" (p. 6). But his diagnosis of the prevailing reality is bleak. He observes boards mired in the trivial, largely reactive to staff initiatives, and absorbed in reviewing and rehashing actions the staff has already undertaken (pp. 19–20). Carver argues that board committees are often organized in a way that leads to this condition. Committee responsibilities often coincide with those of senior managers; for example, there may be committees on finance, fundraising, program evaluation, and other areas of the organization's operation overseen by professional staff. In many cases, the staff prepares materials for meetings of the relevant committee and influences what items the committee considers. This structure pulls the board's attention into the details of each of the management silos. Board members thus become either supermanagers or just advisors to the professional staff. This prevents them from staying focused on big-picture matters such as mission and goals. As Carver writes, "Our tradition of board work encourages boards to derive their agendas from staff-based divisions of work. This common board practice is tantamount to classifying a manager's functions on the basis of his or her secretary's job areas" (p. 46).

Carver (2006) calls for a clear distinction between the work of the board and that of the management staff and argues that the board should lead the organization, by focusing its attention on establishing *policies*. But this does not mean the kinds of policies that boards often discuss, such as personnel policies, which really reflect the work of management and are related to implementation rather than leadership of the organization. The board should make policies that reflect the board's values and the interests of the "moral owners" of the organization.

In Carver's (1997) model, boards lead by developing and maintaining policies in four areas:

1. *Ends to be achieved:* Ends policy statements describe what the organization is to achieve and "could be called results, impacts, goals, or outcomes as well as ends, each title having its own connotations" (p. 31). The broadest ends statement would be the organization's mission. More specific ends policies might address more detailed goals—for example, those related to products, consumers, and costs.
2. *Means to the ends:* In Carver's model, means statements are expressed in terms of "executive limitations"—that is, boundaries that the CEO may not cross in pursuing the ends established by the board. For example, the broadest statement of policy in this area might be that the CEO not violate the law. More detailed limitations might address more specific constraints, perhaps levels of cost and debt that may not be exceeded. Carver argues that by stating executive limitations in negative terms—that is, by prescribing what executives may *not* do, the board preserves maximum flexibility for the CEO. Subject to the constraints that the board has explicitly stipulated, the CEO is free to determine the best methods for achieving the ends that the board has established, without the board's inappropriate involvement in operations.
3. *Board-staff relationship:* Policy statements in this area clearly delineate the responsibilities of the board and the CEO, defining what decisions are delegated to the CEO and which ones are retained by the board. This category of statement also includes specific criteria for monitoring and evaluating the CEOs' performance. Carter argues that one benefit of such clarity is that it addresses the common concern about board members communicating directly with other staff within the organization or with other volunteers. "When the roles are clear, it is possible for anyone to talk with or elicit wisdom from anyone with no harmful effects on the 'chain of command'" (p. 118).
4. *Process of governance:* This fourth category of policy addresses the board's own role and operation, clarifying which owners it represents and defining its own "job process and products"—for example, the procedure through which new board members are elected (p. 33).

Meetings of a board practicing Carver's (1997) model would be driven by the need to develop and maintain its policy manual. When issues arise, the first question to be addressed would be to which category of policy the issue belongs, whose issue it is, and whether it is addressed by an existing policy. If not, a new policy needs to be adopted, eliciting discussion and debate. Carver argues that this approach steers boards away from the mundane, from show-and-tell presentations by staff, and from merely rubber-stamping the staff's recommendations. According to Carver, following the policy governance approach leads the board toward discussions focused on the long term and rooted in the board's values and perspectives (p. 181).

Chait, Ryan, and Taylor: Governance as Leadership

Now let's examine a different approach, the governance-as-leadership model proposed by Chait et al. (2005). The authors agree with many of Carver's criticisms of the way boards operate today. Boards are not leading their organizations. They are reactive to staff initiatives. They structure their work in a way that draws them into managerial details and routine technical work. Indeed, these authors argue, things are turned upside down. Boards are so mired in operational details that they are, in effect, *managing* their organizations. Meanwhile, CEOs are articulating missions, beliefs, values, and cultures—in essence *leading* their organizations and engaging in activities that "closely resemble conventional notions of *governing*" (p. 3, italics added). As the authors explain,

> In theory, if not in practice, boards of trustees are supposed to be the ultimate guardians of institutional ethos and organizational values. Boards are charged with setting the organization's agenda and priorities. . . . Boards are empowered to specify the most important problems and opportunities that management should pursue. If this logic holds, as we contend, then many nonprofit executives are not only leading their organizations, but . . . they are actually governing them as well. (p. 3)
>
> With sophisticated leaders at the helm of nonprofits, a substantial portion of the governance portfolio has moved to the executive suite. The residue remains in the boardroom. This surprise twist in the story line suggests that the real threat to nonprofit governance today may not be a board that micro*manages* but a board that micro*governs*, while blind to governance as leadership. (pp. 4–5)

But while their diagnosis of board problems is similar to Carver's (1997), Chait and his colleagues (2005) offer a quite different prescription. Instead of drawing sharp lines between policy and implementation, clearly dividing the role of the board and the CEO, they call for breaking down the barriers and focusing the attention of both the board and the CEO on the critical issues facing the organization. In other words, the question should not be "Is this an issue of policy or implementation?" Rather, the question should be "Is the issue at hand important or unimportant, central or peripheral?" (Taylor, Chait, & Holland, 1999, p. 62).

In their book, Chait et al. (2005) define a new model, which they call "governance as leadership," based on three "modes" of governance in which a board may be operating at any given time:

1. *The fiduciary mode:* When the board is operating in this mode, it is concerned with the "bedrock of governance," that is, with matters such as stewardship of tangible assets, faithfulness to mission, performance accountability, and obedience to law—in other words, generally addressing its legal responsibilities.

2. *The strategic mode:* When operating in the strategic mode, boards go beyond their basic fiduciary responsibilities and "create a strategic partnership with management," addressing matters such as the organization's long-term directions and goals.
3. *The generative mode:* A board in generative mode is engaged in generative thinking—that is, the creative, out-of-the-box thinking in which visionary leaders often engage. It relates to values and judgments, encompasses "sense making" (essentially, coming to understand things in new ways), and may result in insights that lead to paradigm shifts. The authors say that generative thinking is a necessary foundation for setting direction and goals and thus an essential activity of leadership.

Chait et al. (2005) observe that most boards work only in the fiduciary and strategic modes and therefore are not participating in leadership of the organization. But "when trustees work well in *all three* of these modes, the board achieves governance as leadership" (p. 7, italics added). Thus, rather than maintaining a clear distinction between what is the board's territory and what is the CEOs' territory, Chait et al. propose that boards and CEOs focus together on what matters most, moving together among the three modes as appropriate to address the issues at hand. Setting goals, and thus generative thinking, cannot be a task for the CEO or the board alone but rather must be a *shared* activity:

> Because we resolutely regard this [generative thinking] as shared work, we cannot offer what the board-improvement field so often promises trustees and executives: a set of bright lights that neatly divide the board's work (policy, strategy, and governance) from the staff's (administration, implementation, and management). It simply makes no sense to reserve generative work for boards when leaders are vital to the process, or to reserve for leaders work that belongs at the heart of governance. Generative work demands a fusion of thinking, not a division of labor. (p. 95)

Simply stated, Carver (1997) envisions the board and the CEO on opposite sides of the table, one clearly labeled "policy" and the other "implementation." Chait and his coauthors (2005) envision a three-sided table, with the board and the CEO sitting together on one side but moving around the table to the other sides, depending on the nature of the business to be considered at the time.

Which model is "right?" Does adoption of Carver's (1997) policy governance model improve board performance? Does Chait et al.'s (2005) governance-as-leadership approach? One 2003 study, by Patricia Nobbie and Jeffrey Brudney, compared organizations using the Carver (1997) model with others that had received training from BoardSource, and suggested mixed results. There were few differences, and those were generally not significant. The job satisfaction of CEOs working under the Carver model measured somewhat higher than that of the others, but the researchers found the difference to be statistically nonsignificant. One important conclusion of the study was that boards that had received training tended to perform better than those that had not been trained, regardless of which model had been used. Carver, with characteristic confidence, responds to the Nobbie and Brudney

(2003) study in the 2006 edition of his book, arguing that his model is superior and that the latter authors' choice of variables reflects an inaccurate understanding of its purpose.

Herman and Heimovics: Psychological Centrality and Board-Centered Leadership

In Carver's (1997) approach, boards lead their organizations. Chait et al. (2005) describe a model for leadership shared by the board and the chief executive. Robert Herman and Dick Heimovics (2005) provide a third perspective. Based on their research concerning effective nonprofit CEOs, they offer a pragmatic approach, concluding that CEOs should lead but that their leadership needs to be *board centered* and designed to support the board in meeting its governing responsibilities.

The *purposive-rational model* of organizations, based on Weber's theory of the bureaucracy, conceives of the board as the top of a hierarchy and the CEO as merely its agent. Indeed, Herman and Heimovics's (2005) review of the normative literature on nonprofit boards finds that most research has been based on that model and thus "has advanced a heroic ideal for nonprofit boards" (p. 155). However, they apply the *social-constructionist* model and explain that "official or intended goals, structures, and procedures may exist only on paper. Actual goals, structures, and procedures emerge and change as participants interact and socially construct the meaning of ongoing events" (p. 156). Regardless of what the organizational chart or the conventional view of organizations may suggest, Herman and Heimovics find that the reality in most organizations is that of *executive psychological centrality*. In other words, it is the CEO who is actually *seen as* responsible for the organization's success or failure. They interviewed CEOs, board chairs, and other staff members and found that *all* of them saw the chief executive as "centrally responsible for what happens," including both successful and unsuccessful events (p. 156). This does not imply that the CEO holds more formal authority than the board or that the CEO *is* indeed the central figure in the life of the organization. "Psychological centrality" means than he or she is *perceived as* responsible, even by members of the board.

If this is the reality, then what do Herman and Heimovics (2005) recommend that CEOs should do? They do not recommend that CEOs become autocrats or demote their boards to rubber stamps but rather that they take a leadership role to ensure "that boards fulfill their legal, organizational, and public roles" (p. 156). In exercising board-centered leadership, CEOs take responsibility for "supporting and facilitating the board's work." In doing so, they engage in six behaviors that Herman and Heimovics observed among the effective, board-centered executives they studied (p. 158):

1. Facilitating interaction in board relationships
2. Showing consideration and respect toward board members
3. Envisioning change and innovation for the organization with the board
4. Providing useful and helpful information to the board

5. Initiating and maintaining structure for the board
6. Promoting board accomplishments and productivity

Herman and Heimovics (2005) conclude that not only are the CEOs who have developed these board-centered leadership skills effective as CEOs, they also have hardworking, effective boards. "The board-centered executive is likely to be effective because he or she has grasped that the work of the board is critical in adapting to and affecting the constraints and opportunities in the environment" (p. 159).

NONPROFIT BOARD EFFECTIVENESS

"And so," students may be wondering at this point in the chapter, "what's the bottom line?" Are most nonprofit boards effective or not? What are the characteristics of effective boards? What is the right way to define the relationship between the board and the nonprofit CEO? What is indeed the best model for governance?

Critics of Board Performance

In answer to the question of how nonprofit boards are doing, there is no shortage of negative commentary. For example, Chait et al. (1999) reported that "after 10 years of research and dozens of engagements as consultants to nonprofit boards, we have reached a rather stark conclusion: effective governance by a board of trustees is a relatively rare and unnatural act" (p. 1). Carver (1997) essentially agrees, writing that "the problem is not that a group or an individual *occasionally* slips into poor practice, but that intelligent, caring individuals regularly exhibit procedures of governance that are deeply flawed" (p. 9).

Writing in the *Stanford Social Innovation Review*, Michael Klausner and Jonathon Small (2005) note little improvement since Chait et al.'s (1999) and Carver's (1997) observations of several years before. They reference a 2004 newspaper story that revealed financial mismanagement at the Beard Foundation and write, "In recent years, news reports like this one increasingly suggest that too many directors of nonprofit organizations are failing to govern" (Klausner & Small, 2005, p. 42). They cite the opinions of (unnamed) "commentators [who] suggest that each and every director should work harder and more effectively at governance" and conclude, "In our view, the commentators are right on the money" (Klausner & Small, 2005, p. 43).

Such criticisms cannot be ignored, but it may be prudent to question the evidence behind such sweeping statements. Most are based on experience rather than research. Some are reported by consultants who are called on to work with troubled boards and whose samples therefore may be somewhat self-selecting. Others, like Klausner and Small (2005), generalize from single anecdotes. Surely, instances of board corruption or mismanagement are to be deplored. But it is reasonable to question whether individual cases illustrate the systematic failure of nonprofit governance or merely reveal the frailties of particular boards and individuals, which are unfortunately all too often visible in business and government as well. However, it is equally reasonable to believe that the performance of boards and their members can be improved and to continue the search for best practices in nonprofit governance.

The Search for Best Practices

Various researchers have attempted to identify behaviors that are associated with effective nonprofit governing boards—that is, to identify those practices that, if followed, will lead to effective governance. In 2005, BoardSource assembled a panel of experts to address the question. Their consensus produced the following "twelve principles that power exceptional boards":

1. *Constructive partnership:* Exceptional boards govern in constructive partnership with the chief executive, recognizing that the effectiveness of the board and chief executive are interdependent.

2. *Mission driven:* Exceptional boards shape and uphold the mission, articulate a compelling vision, and ensure the congruence between decisions and core values.

3. *Strategic thinking:* Exceptional boards allocate time to what matters most and continuously engage in strategic thinking to hone the organization's direction.

4. *Culture of inquiry:* Exceptional boards institutionalize a culture of inquiry, mutual respect, and constructive debate that leads to sound and shared decision making.

5. *Independent-mindedness:* Exceptional boards are independent-minded. When making decisions, board members put the interests of the organization above all else.

6. *Ethos of transparency:* Exceptional boards promote an ethos of transparency by ensuring that donors, stakeholders, and interested members of the public have access to appropriate and accurate information regarding finances, operations, and results.

7. *Compliance with integrity:* Exceptional boards promote strong ethical values and disciplined compliance by establishing appropriate mechanisms for active oversight.

8. *Sustaining resources:* Exceptional boards link bold visions and ambitious plans to financial support, expertise, and networks of influence.

9. *Results-oriented:* Exceptional boards are results-oriented. They measure the organization's advancement toward its mission and evaluate the performance of major programs and services.

10. *Intentional board practices:* Exceptional boards intentionally structure themselves to fulfill essential governance duties and to support organizational priorities.

> 11. *Continuous learning:* Exceptional boards embrace the qualities of a continuous learning organization, evaluating their own performance and assessing the value they add to the organization.
>
> 12. *Revitalization:* Exceptional boards energize themselves through planned turnover, thoughtful recruitment, and inclusiveness. (Excerpted from BoardSource, 2005)

BoardSource's 12 principles of governance offer an attractive description of an exceptional board and reflect the consensus of a distinguished panel of experts assembled to develop them. But it is nevertheless primarily a compilation of practitioner wisdom rather than science. There remains a relative paucity of research on the subject of nonprofit board performance, and there is no single definition of board effectiveness. This is so in part because there is no single standard for defining the effectiveness of nonprofit organizations. As John Carver (2006) notes, the variables chosen for measurement in some research studies seem to imply

> that effectiveness in governance is to be judged by whether board members are more fulfilled, challenged, or involved; the CEO is happier or the board is less meddlesome; the board raises more funds; grant revenues are increased; committees are more active; or the board chair perceives the CEO to be meeting his or her objectives. (p. 337)

But the link between such variables and the effectiveness of boards—or organizations—remains elusive.

In a 2002 review of the literature on nonprofit effectiveness, Robert Herman and David Renz conclude that "[board] effectiveness is whatever significant stakeholders think it is, and there is no single objective reality." Calling the concept of best practices "somewhat of a holy grail," they advise nonprofit boards and CEOs to take a skeptical view of "one right way" prescriptions:

> Many sources that claim to offer "best practices" for NPO boards or management provide little or no basis for their assertions. *The evidence from our . . . study does not support the claim that particular board and management practices are automatically best or even good (that is, that using them leads to effective boards and organizations.* We prefer to talk in terms of "promising practices" to describe those approaches that warrant consideration.
>
> Not only is there no "silver bullet" (i.e., one practice that ensures board effectiveness)—there is no "silver arsenal." In the context of other research, we support the assertion that boards (perhaps with facilitative leadership from their chief executives) need to identify those processes that are most useful to them. Boards should not use a practice just because other boards, experts, or consultants say it is useful. They should ask some key questions: Does the practice fit this board's circumstances? Does the practice actually help the board reach good decisions? Does the practice contribute to the organization's success? (pp. 6–7)

Herman and Renz's (2002) caution should not be interpreted as saying that the literature on nonprofit governing boards has nothing to offer and should be disregarded. Rather, their conclusions are consistent with the philosophy expressed in the Introduction of this text: There is often no right answer, and the best way is often pragmatic and eclectic. This includes viewing a problem from multiple perspectives and drawing from various approaches selectively as the situation may dictate.

THE CHALLENGE OF NONPROFIT GOVERNANCE

Serving as a member of a nonprofit board today is an interesting and challenging assignment. Nonprofit boards are buffeted by strong cross-currents emanating from virtually all their constituencies. The forces of law, media scrutiny, and more demanding funders are pushing them to do a better job of governance. At the same time, the financial pressures facing many nonprofits in light of diminished government support, increased competition for philanthropy, and the rising needs and expectations of their clients are leading to greater emphasis on their responsibilities to serve as the organization's advocates, protectors, and fundraisers. As the brief review in this chapter reveals, the literature of nonprofit governance includes an abundance of advice, but some of it is inconsistent, even contradictory. Today's boards are being exhorted not only to raise money and promote the organization but also to be more aggressive in monitoring its performance. They are told to develop independent sources of information about the organization's operations but to stay focused on the big picture and not meddle in operations, to maintain a clear line between themselves and their CEO but not to forfeit their responsibility for leadership.

Nonprofit boards are expected to be Janus-like—that is, like the Roman god of doorways and arches, who was said to have two faces and be able to look outward and inward at the same time. Nonprofit organizations are open systems, with vaguely defined and often porous boundaries. The board is positioned on that boundary, between the organization and its external environment. From that position, the board is expected to look inward, fulfilling its fiduciary responsibilities on behalf of the membership or society. It is a kind of watchdog, responsible for ensuring that the organization is accountable for the resources entrusted to it, that those resources are used effectively in pursuit of its mission, and for representing the interests and viewpoints of the owners, whoever they may be.

But board members are also expected to be looking outward in order to meet their responsibilities to the organization itself and advance its interests. This is especially true for boards of charitable nonprofits, which may depend at least in part on philanthropic support. Because they are often leading citizens themselves, board members bring credibility to the organization in the broader community and authenticate its worthiness to receive support. They serve as its ambassadors and advocates, increasing its visibility and reputation within their own social and business circles. They protect the organization against inappropriate intrusions on its autonomy by government, donors, or other external forces. And they have a responsibility to ensure the organization's financial strength and sustainability, which many accomplish in part through giving or helping secure financial resources. These dual responsibilities—to society and to the organization itself, looking inward at the same time as looking outward—can sometimes be complex and competing. As Chait et al. (1999) explain,

> Boards constantly wrestle with when to be "product champions" and when to be studied neutrals—whether to stand and cheer like rabid partisans when the President of the United States delivers the State of the Union address or to remain seated and stone faced like the Supreme Court justices. (p. 3)

As Table 3.2 suggests, the complex responsibilities of boards may imply somewhat different ideal qualities in the individuals selected to serve, depending on which set of responsibilities are emphasized—a possible trade-off between what is often called "wisdom" (shorthand for the skills and judgment needed to govern well) and "wealth" (meaning the ability to give or obtain funds and other external resources). To fulfill their fiduciary responsibilities, boards must include individuals of integrity, and at least some will need to have specialized knowledge in finance and perhaps in professional fields related to the organization's programs and services. For example, a human services organization may need some board members with a background in social work, and it may be important that the boards of medical institutions include at least some members who understand medical terminology or the economics of health care. To properly represent the needs of the community and clients served by the organization, boards also need diverse memberships reflective of their constituencies, perhaps even including some who have been beneficiaries of the organization's programs—for example, former clients, patients, or students.

TABLE 3.2 The Board's Sometimes Competing Responsibilities

To society:	*To the organization:*
Accountability for resources and results	Advocacy and authenticity
Adherence to mission and law	Protection of autonomy
Representation of community needs	Fiscal stability and sustainability
Indicated board member qualities:	*Indicated board member qualities:*
Integrity	Stature
Expertise on programs and finances	Influence
Knowledge of community/clients	Wealth or access to wealth

But to advance its reputation, protect its interests, and secure funds, a nonprofit also needs board members who are individuals of stature in their communities, perhaps having influence with governmental officials or other regulators, and who have either the wealth to be significant donors or access to other individuals, foundations, or corporations that can provide financial support. John Pocock (1989) notes that "wealth and wisdom are not mutually exclusive [qualities of human beings]." He is, of course, correct that there may be *individual* candidates for governing board service who are possessed both of wisdom and of wealth—that is, who are equally well suited to meet their responsibilities for governing the organization and for serving as its external advocates and fundraisers. But not all individuals may be strong in all the requisite qualities. Boards attempting to craft their membership and faced with selecting a new member to fill an open seat may indeed face a dilemma regarding which qualities should be emphasized. Likewise, in deciding on which issues to focus its limited time and attention, a board may face either-or choices between the tasks associated with governing and those associated with advancing the organization, its interests, and its resources. Today's environment presents increasing pressures on boards to do all things better—to be better stewards and better fundraisers and to become more engaged with the organization's planning, programs, and effectiveness while also giving and raising more funds to support its work. The proper trade-offs between wealth and wisdom and how to balance the sometimes competing demands are questions causing discussion—and some anxiety—in many nonprofit boardrooms today.

CHAPTER SUMMARY

The governing board holds ultimate responsibility for the nonprofit organization. There are various types of boards, including those elected by the organization's membership; self-perpetuating boards; boards appointed by some outside authority; and hybrids, which may include elected, self-perpetuating, appointed, and ex-officio members. Each of these methods offers advantages but also introduces risks for the organization and the board.

The governing board's fiduciary responsibilities are defined in law and include the duty of care, the duty of loyalty, and the duty of obedience. Since the passage of intermediate sanctions in 1996 and the Sarbanes-Oxley Act in 2002, there has been increased scrutiny of nonprofit boards by the federal and state governments, the media, and other organizations. Under intermediate sanctions, nonprofit board members can face individual penalties for violating their fiduciary responsibilities, and many boards adopted new conflict-of-interest and disclosure policies in response to that legislation. Although Sarbanes-Oxley applies primarily to publicly traded corporations, many nonprofit organizations have voluntarily adopted some or all of its provisions, and some have been encompassed in legislation passed by states.

Functional responsibilities of boards have been defined in the literature and include appointing, supporting, and evaluating the CEO; establishing a clear institutional mission and purpose; approving the organization's programs to ensure consistency with its mission and financial prudence; ensuring sound management and financial stability; and establishing standards by which the organization's performance will be evaluated. Some view the board's responsibility to ensure the organization's financial stability and sustainability as implying an obligation on the part of board members to give from their personal resources and actively engage in fundraising. Some boards have policies requiring that members give or raise a minimum amount, but others rely on a culture that encourages members to participate as appropriate to their capacities.

The relationship between the governing board and the CEO is the subject of a substantial literature. In some organizations, especially those managed by a founder, the CEO may be a dominant figure, and the board may be largely reactive to the executive's initiatives. Most experts call for a partnership between the board and the CEO but differ on how that partnership should be designed. Three experts discussed in this chapter include John Carver (1997), whose policy governance model suggests a clear separation of roles, defined in policies established by the board related to ends, means, board-staff relationships, and governance process. Chait and colleagues (2005) propose a model they call governance-as-leadership, in which the lines between the responsibilities of the board and the CEO are broken down and both work together in focusing on the most critical issues and questions facing the organization. Leadership is shared, particularly when both engage in generative thinking. The research of Robert Herman and Dick Heimovics (2005) revealed that in reality both board members and the chief executive see the CEO as primarily responsible for the organization's success or failure, a condition they call "executive psychological centrality." They advise CEOs to accept that reality and practice board-centered leadership, not usurping the responsibilities of the board but rather supporting and facilitating its work.

In today's environment, there is considerable emphasis on the effectiveness of nonprofit governance. There are many criticisms, but there is a paucity of research to substantiate many of them. BoardSource and others have identified best practices of effective boards, but research by Herman and Renz (2002) suggests that there may be no one right way that works for every organization.

Nonprofit boards today face conflicting pressures. They are expected to do a more effective job of governing but also become more active in generating financial support for the organizations they serve. The appropriate trade-offs between the wealth and wisdom needed to meet these sometimes competing priorities are a matter of current discussion and debate in many nonprofit boardrooms.

NOTE

1. Some experts recommend that advisory groups not be called "boards" at all but rather "councils" or by some other term that does not imply legal responsibility for the organization.

KEY TERMS AND CONCEPTS FROM CHAPTER 3

board-centered leadership
board of directors
board of trustees
BoardSource
conflict of interest
duty of care
duty of loyalty
duty of obedience
excess benefit transaction
executive psychological centrality
ex-officio
fiduciary mode
generative mode
give-or-get policy
governance as leadership
governing boards
intermediate sanctions
policy governance model
private inurement
purposive-rational model
Sarbanes-Oxley Act
self-perpetuating
social-constructionist model
strategic mode

CASE 3.1

United Way of the National Capital Area

The United Way of the National Capital Area (UWNCA) is one of about 1,350 local United Way organizations, each of which is separately incorporated and governed by a board of volunteers from the community it serves. UWNCA serves the Washington, D.C., area, including the District of Columbia and its suburbs in Maryland and Virginia.

In 2002, the community was rocked by accusations that UWNCA's executive director, Oral Suer, had received as much as $1.6 million in improper payments, including nonreimbursed cash advances, encashment of vacation and sick leave that he had in fact taken, and reimbursement for travel and entertainment that were personal rather than related to United Way business. Those improper payments were alleged to have occurred over the period of 27 years that Mr. Suer was employed at the UWNCA (Wolverton, 2003b). *The Washington Post* also reported that UWNCA had withheld funds from charities, had excessive overhead costs, and had inflated its reported fundraising totals ("New Directors to Be Installed at United Way," 2002).

The UWNCA's board had 45 members, including prominent business leaders, attorneys, and accountants. One former employee of the organization told the *Chronicle of Philanthropy*, "This was definitely a 'clapper' board. They listened to staff members tell wonderful stories about how much money we were raising, and they applauded instead of asking tough questions" (Wolverton, 2003b). Others cited the organization's internal culture, which made it difficult for the board to meet its fiduciary responsibilities. One board member said that the board met only four times a year, a total of eight hours, and that the large board discouraged her from speaking. She said that she didn't have the phone numbers of the other board members, so she was unable to follow up with them after meetings. When she tried to obtain the numbers, a secretary at UWNCA told her that the numbers were confidential (Wolverton, 2003b).

Following the scandal at UWNCA, the national office of the United Way of America established new guidelines for the governance of local United Ways. UWNCA's board resigned, and a committee of community leaders was appointed to recruit a new board of 21 members. A new executive director was appointed to reform the organization and rebuild the community's trust.

Sources: "New Directors To Be Installed at United Way" (2002), Salmon (2002a, 2002b), Salmon and Whoriskey (2003), and Wolverton (2003b).

CASE 3.2

Robin Hood Foundation

The Robin Hood Foundation is a nonprofit that fights poverty in New York City. Its board includes prominent Wall Street hedge-fund managers as well as other well-known figures. An article by Donmoyer and Fitzgerald (2007) in the *Washington Post* raised questions about Robin Hood's "rainy-day fund," which had grown to $144.5 million from $20 million in a decade. The article noted that about half the fund was invested in hedge funds, managed by members of the Robin Hood board.

The article noted that there was nothing illegal about the arrangement. Robin Hood's executive director also pointed out that the managers are among the best and that the Foundation's investment returns had been excellent. The amount of management fees being paid were standard in the industry. He said that decisions on where to invest were made by a committee of Robin Hood's board and that the committee was not allowed to invest in funds managed by members of that committee. He also explained that the board members received fees for managing the Foundation's funds because their company policies did not allow them to charge different fees to different investors. The director of the Better Business Bureau's (BBB) New York Philanthropic Advisory Service said that Robin Hood met BBB's standards for charity accountability. (The BBB standards are discussed in Chapter 5 of this text.)

But some people raised questions about the role of Robin Hood board members in managing the organization's funds. Senator Charles Grassley, a member of the Senate Finance Committee, who is often critical of nonprofit organizations, said, "I don't remember Robin Hood keeping [management fees] as his cut." An official of the Kellogg Foundation described the situation as "flirting with self-dealing." The national president of the Better Business Bureau Wise Giving Alliance also raised questions: "You start to wonder what happens in the year that the hedge fund doesn't do well. Does the board have the power to fire the hedge-fund manager?"

Source: Based on Donmoyer and Fitzgerald (2007).

CASE 3.3

Bishop Estate

Hawaii's Bishop Estate is a charitable trust created through the will of Princess Bernice Pauahi Bishop, a descendant of King Kamehamena I, and has as its sole purpose supporting the Kamehamemaha Schools for children of native Hawaiian descent. It was reported in 1999 that the Estate was the largest landowner in Hawaii, and its assets were estimated at between $5 billion and $10 billion. According to the Princess's will, the trust was to be governed by five trustees, who would be appointed by the justices of Hawaii's Supreme Court (Greene, 1999).

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In the 1990s, the IRS began investigating the trust and expressed its concern about the activities of the trustees. First, the IRS said that the trustees were receiving excessive compensation for their services, reported to be more than $1 million annually each. In addition, the IRS said that the trustees were using the Estate's funds to pay for personal expenses, that they were focused more on the Estate's commercial activities than on running the schools, and that they had improperly lobbied against passage of the intermediate sanctions legislation in 1996. The trustees defended their actions, arguing among other things that they deserved the compensation for their work in managing the trust's assets as well as the schools. The trustees had indeed been involved in the day-to-day management of the schools, which some said had caused problems and tension between the schools and the trustees.

The IRS threatened to terminate the Estate's tax exemption, which would have required the Estate to pay millions of dollars each year in federal taxes as well as state and county taxes, thus diminishing the benefit of its assets to the schools and the children. The IRS demanded changes that would include removal of the existing trustees, a new method for selecting trustees, revisions in trustee compensation, stronger internal financial controls, and external audits.

Reacting to the IRS criticism, in 1999 Judge Kevin Chang of the Hawaii court removed four of the five trustees and accepted the resignation of the fifth, saying that their "inaction and indifference" was "a breach of duty." The IRS decided to pursue intermediate sanctions against the removed trustees, making it one of the first cases under the law passed in 1996. In 2001, the former trustees announced that they had settled with the IRS, which did not disclose the details. The media reported that the State of Hawaii also had brought a case against the trustees, which also was settled, but the court records were sealed, so the final result could not be known (Schwinn, 2002).

Some saw the IRS's action as an encouraging example, showing that it would act to curb abuses. Others saw it as alarming for the nonprofit sector that the IRS would use its power to pressure a state court to remove nonprofit trustees (Greene, 1999).

Source: Greene (1999) and Schwinn (2002).

QUESTIONS FOR DISCUSSION

1. Which of the legal responsibilities of boards may not have been met by the board of the United Way of the National Capital Area? How might this scandal have been prevented?
2. What does the United Way case suggest about the relationship between the CEO and the board?
3. What are the issues in the case of the Robin Hood Foundation? Although they are legal, are the relationships between the board and the managers of the organization's finances appropriate? Why or why not? What safeguards would you introduce to assure the organization's donors that the board is behaving properly?
4. How is the case of the Bishop Estate different from that of the Robin Hood Foundation and the United Way of the National Capital Area?

5. Do you see any ways in which the recommendations of Carver (1997), Chait et al. (2005), and Herman and Heimovics (2005) might be relevant to the cases discussed in this chapter?

SUGGESTIONS FOR FURTHER READING RELATED TO CHAPTER 3

Books

Carver, J. (2006). *Boards that make a difference: A new design for leadership in nonprofit and public organizations* (3rd ed.). San Francisco: Jossey-Bass.

Chait, R. P., Ryan, W. R., & Taylor, B. E. (2005). *Governance as leadership: Reframing the work of nonprofit boards*. Hoboken, NJ: Wiley.

Ingram, R. T. (2003). *Ten basic responsibilities of nonprofit boards*. Washington, DC: BoardSource.

Worth, M. J. (2005). *Securing the future: A fund-raising guide for boards of independent colleges and universities*. Washington, DC: Association of Governing Boards of Universities and Colleges.

Web Sites

Association of Governing Boards of Universities and Colleges, www.agb.org

BoardSource, www.boardsource.org