GOOD GOVERNANCE: ESTABLISHING THE RIGHT FOUNDATION

SYDNEY HILZENRATH, CEP, CECP

WHY GOVERNANCE IS TOP-OF-MIND FOR NOT-FOR-PROFIT ORGANIZATIONS

It is not simply that not-for-profit organizations must *be* well governed. Optics are crucial: not-for-profit organizations must also ***be seen*** to be well governed. This perception of good governance is of critical importance if the organization is to successfully meet the challenges created by:

- The need to manage more complex and sophisticated entities;
- Heightened accountability and expectations on the part of an expanding number of stakeholders;
- Rapid dissemination of information through social media, which can quickly affect the way an organization is perceived; and
- Difficulty in recruiting quality board members as the complexity of not-for-profit organizations grow, and along with it the time and dedication required of board members.

There have been several high-profile reports in the media of not-for-profit organizations that have suffered from poor management, ineffective boards, poor decision making and activities that call ethics and process into question. However, the objective of good governance is not just to avoid embarrassing headlines. Lack of governance can damage an organization's reputation, detract from its fundraising ability, hamper its ability to meet its objectives, and could ultimately lead to the loss of tax-exempt status.

Understanding what good governance really means is elusive – you know it when it's happening: information is disseminated amongst board members in a timely fashion, meetings flow smoothly, challenges are met, and decisions are made based on strong data and thoughtful discussion. So how does a board arrive at this enlightened state? By ensuring basic governance practices are in place.

THE BASICS OF GOOD GOVERNANCE

Although the IRS doesn't require not-for-profit organizations to have specific governance and management policies, it does encourage certain board activities. In addition, the IRS reviews an organization's exemption applications and Form 990 returns to determine whether the organization has policies in place relating to:

Executive Compensation: The Internal Revenue Code does not define any specific process to determine compensation. However, the compensation of officers, key employees, directors and trustees (and others in a position to exercise substantial influence over the organization's business affairs) should be determined by knowledgeable and independent persons. Ensuring that your organization has reviewed appropriate comparability data and documented any discussion and decision making is vital to the reliance on the IRS' rebuttable presumption. (See https://healthcareappraisers.com/what-tax-exempt-organizations-need-to-know-about-executive-compensation/)

Conflicts of Interest: Directors must act in the interest of the organization (not for personal interest) and must avoid conflicts of interest that are detrimental to the organization. Generally, organizations have written policies that address potential conflicts of interest for directors, trustees, officers and other employees. Adhering to a conflict of interest policy and reviewing the terms of that policy with all directors on a recurring basis is essential to strong governance practice.

Investments: Depending on state law or the organizational documents, the governing body (or a group with authority to act on behalf of that body) may be required to oversee or approve major investments made by the organization. For organizations that make such investments (including acquisitions of other entities), the IRS encourages the adoption of written policies and procedures to cover investment participation and ensure the organization's assets and exempt status are protected from any investment arrangement.

Fundraising: The organization should have policies in place to ensure that fundraising meets federal and state law requirements and materials are accurate. The IRS encourages this type of policy, and that the governing body monitor the policy while keeping fundraising costs reasonable.

Maintenance of corporate minutes and records: If your organization files a Form 990, it indicates whether or not the organization contemporaneously documents meetings or written actions taken during the year by its governing body (and committees with authority to act on behalf of the governing body). While not a requirement, the IRS strongly encourages organizations to contemporaneously document meeting minutes and actions taken.

Document retention and destruction policy: In a similar vein to the maintenance of minutes and records, the IRS urges organizations to adopt a policy that establishes standards for document integrity, retention and destruction. This policy would apply to, amongst other items, the books and records that are relevant to an organization's tax-exempt status and filings with the IRS.

Whistleblower protection policy: The IRS encourages organization's boards to adopt a policy to effectively handle employee complaints, along with procedures for employees to report suspected financial impropriety or misuse of resources in confidence. Form 990 asks whether an organization became aware of material diversion of its assets during the year and whether the organization has a whistleblower policy.

HOW ORGANIZATIONS SHOULD THINK ABOUT GOVERNANCE

Governing bodies are responsible for leading an organization by partnering with the CEO (or Executive Director) and are charged to address the following inquiries:

1. How is the organization performing in the context of its mission, finances and administration?
2. Where is the organization now and where is it expected to be in the immediate future?
3. What does the future of the organization look like?

Each of these items should be considered within the framework of the governance basics described above. By establishing a strong foundation built on these basics, the governing body will achieve a standard of good governance that will protect and support the organization.