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Not For Profit Board of Directors and Governance

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Abstract

Anon-profit (NFP entity's Board of Directors) bears ultimate responsibility for its governance. It ensures the non-profit functions in accordance with all applicable laws, regulations, and the entity's internal guidelines and mission statement. We examine these Boards' role in overseeing the functioning of non-profit entities and their management. We begin by reviewing the purpose of a Board of Directors and a commonly adopted structure for them including who may serve on such Boards; and how these Boards differ from those in the for-profit world. We then review the formal responsibilities that NFP Boards have for the entities they govern as well as some unspoken requirements for Board members. We examine specific activities in which these Boards typically engage and some activities which violate good governance practices. We provide examples of both well-functioning boards and some which serve as cautionary tales for entities. We discuss how a Board can deal with Board members who violate an entity's rules and/or laws and how such members might be removed from their respective office as well as other regulatory and legal issues related to the conduct of Board members. We discuss the government entities both state and federal which regulate the function of non-profit Boards.

Keywords

non-profit entity, Board of Directors, governance, fiduciary duties

1. Introduction: The Purpose of a Board of Directors

The Board of Directors of a non-profit organization is responsible for the proper functioning of the entity. It has final authority over the actions undertaken by the entity. The Board delegates authority for the non-profit's day-to-day operations while retaining its power to approve management's actions.

Consider for example, the theoretical case of a New York City-based non-profit the purpose of which is to address and treat particular issues that prevent children in certain New York City public schools from achieving their full academic potential. In order to address this goal, this non-profit has created a treatment model. This model consists of two parts: Academic coaching performed by tutors and life skills taught by social workers. The hiring, supervision and termination of these employees is the purview of management and does not require any action by the Board. What would happen, however, if management determined that the treatment model required a change such as substituting psychological treatment by clinical psychologists for the life skills coaching by social workers? This change would require the approval of the Board of Directors because it is a fundamental change in the functioning of the non-profit not merely an administrative action.

2. Commonly Adopted Structures

There are few external requirements for the structure of a Board of Directors. The number of Directors, and any adopted hierarchy is specific to the particular non-profit. The members of the Board decide via vote on the size and structure of the Board and memorialize this decision in the governing documents of the non-profit such as its charter. The number of Board members can be changed at a future date by another vote of the Board at that time. Research indicates that the proper functioning of a non-profit Board is not correlated with its size as one might be tempted to think. For example, Stephes et al. found in 2004 that there is no relation between the number of directors on a non-profit Board and the Board's self-reported performance nor the level of commitment (also self-reported) of its Directors.

What then are the factors that influence the structure of a particular Board of Directors? They are the explicit duties of the Board as determined by its Directors. These functions will be discussed, in detail later; however, it should be noted that if a Board takes on roles that can be assigned to management such as fund-raising, the Directors would be more likely to have particular roles assigned to its members such as a Fundraising Committee. Such a decision could lead the members of the committee to open committee membership to non-Directors while reserving the leadership positions such as Committee Chair for members of the Board.

Despite this freedom of organizational from, many nonprofits in disparate industries have adopted a similar structure. This involves the election of officers who have responsibility for assuring that the Board functions in an orderly and efficient manner.

The four most common officers for non-profit Boards are: President, Vice-President, Treasurer and Secretary. In terms of nomenclature, the President and Vice-President are sometimes called Chairman and Vice-Chairman. The President is the presiding officer of the Board and serves to focus the activities of the non-profit during his/her tenure. Often, Presidents who have limited terms in office will have a "theme" for their term or terms. The Vice-President in many cases serves as a President-in-training and becomes President at the end of the current President's tenure. This office also becomes the presiding officer in the absence of the President and assumes all the duties and powers inherent in that office until the return of the President. The Secretary is responsible for writing the Minutes of all Board meetings. These Minutes are the official record of the discussions and decisions of the Board. The Treasurer is responsible for overseeing the finances of the non-profit without actually managing the day-to-day monetary dealings of the organization; this latter duty is the responsibility of management. In addition to these most common offices, individual non-profit Directors often choose to have an additional hierarchical structure that is relevant to the organization's purpose, design and activities.

For example, a non-profit professional membership organization might also have chapters in different locations. Each chapter may have a designated voting seat on the Board. In addition to such a structure, or as an alternative to it, Boards may have committees which serve to break up the work of the Board among smaller groups. For example, the Treasurer might char a Finance Committee which will review the major financial issues of the non-profit and advise the Treasurer on such issues.

3. Who May Serve on Such Boards

Each individual non-profit entity has a particular purpose and specific manner of achieving its specific goals. The criteria for membership onto a particular non-profit's Board are established by each respective Board. These requirements reflect each entity's specific needs at a particular time. For example, if the entity is experiencing a shortfall in fundraising targets, the Board will seek to obtain new Directors who have a trach record of generating large levels of donations. In fact, for entities such as Lincoln Center for the Performing Arts in New York City, it is rumored that Board membership is offered to donors who have made a six-figure donation over a number of years. As the population of non-profit entities is diverse and each member has its own distinct needs, there are few strict rules for Board membership; although some do exist.

Despite the disparate nature and goals of individual non-profits, as with all areas of non-profit governance, although freedom of choice allows the organization much latitude in its decision-making, there are some common requirements to Board membership among non-profits.

Non-profit Directors are expected to enhance the reputation of the organization's which they govern. As such, one of the key qualities that a Board member should have is good standing in the community. This means that the prospective Director should not have a criminal record in terms of felonies. They should have a reputation free of controversy. This requirement exists for as long as the Director serves on the Board. Any violation of the requirement can be cause for the Director's tenure to end. Take the case of William Cosby, Jr.: When allegations regarding his potentially criminal conduct with women, he was asked to resign from the Board of his alma mater, Morehouse College prior to his being found guilty of any crime.

Board members are typically interviewed for a seat on the Board by current or former Directors. This is done so that the prospective members' commitment to the non-profit's goals can be gauged by those who have demonstrated strong commitment in the past. After the interview process, prospective Board members are typically voted onto the Board either by a vote of either current Board members or in the case of membership organizations, the entire membership; and they serve for designated terms.

It should be noted that research indicates that many NFP Board members believe the criteria to serve on such Boards are too stringent.

4. How These Boards Differ from Those in the for-Profit World

There are strong similarities between a non-profit of Directors and a for-profit Board. Both have overall responsibility for the governance of their respective entities. Both groups must also keep a positive public image; fulfill their oversight responsibilities; and participate in the decision-making process of their respective Boards. Despite these similarities, there are some significant differences between the two types of Boards.

Unlike their for-profit counterparts, non-profit Board members do not receive payment for their work on NFP boards. In fact, some jurisdictions such as New York State legally forbit non-profit Board members from receiving any income stemming from their membership on such boards (These Directors, are, however, allowed to receive reimbursement for legitimate expenses such as travel to Board meetings). This is a main reason why the interview process for membership to these Boards is of great importance. In the absence of a monetary motive, the Board members must be certain that prospective members are truly committed to the goals of the organization and be willing to devote time and energy to achieving those goals.

Another key difference is that the Chairman of the Board of a non-profit does not serve in the dual role of the organization's Executive Director or Chief Executive Officer. Many for-profit boards do not have such a separation. Jamie Dimon, Chief Executive of JP Morgan Chaise has publicly stated in the past that he would not consider continuing as that corporation's CEO unless he also retains his role as the Chairman of Chase's Board of Directors.

It should be noted that from a compliance perspective, the separation of the roles of Chairman of the Board and Executive Director is recommended. The compliance principle segregation of duties requires that any role that has the ability to override compliance safeguards for another role must be performed by a different person. For example, the Chairman of a non-profit Board is responsible for overseeing the compliance of the Executive Director with all appropriate governance principles. If one person were to be in both roles, then who could stop a corrupt Executive Director from stealing from the organization?

5. Responsibilities of NFP Boards

Non-profit organizations engage in a wide variety of activities in diverse areas of specialization. As a result, there are no uniform set of regulations among different jurisdictions which govern their work. A particular non-profit's programs and practices are regulated by its Board through its mission statement and internal policies. Despite this diversity, there are some overarching responsibilities in which the majority if not all non-profit Boards engage. These duties can be divided into two groups: Those that are formal and based on actions the Board undertakes; and those which are principle-based and govern the character of the actions undertaken by the Board members.

- Formal responsibilities

A Board's formal responsibilities are those that are most often visible to the public and are most commonly associated with service on a non-profit Board. According to the National

Center for Nonprofit Boards, among the many responsibilities that non-profit Boards might assume there are ten major functions that an overwhelming majority of such Boards perform. As many organizations rely to some degree on grants and/or donations, these responsibilities serve as a measure of the Board's accountability to both their patrons and the public. These ten responsibilities are as follows:

- To determine the organization's mission and purpose,
    - This is arguably the most important function of the Board of Directors. An entity's mission statement and purpose are public declarations of the organization's reason for existence, its means, goals, and primary constituents served. These two documents together serve as a primary fundraising tool for the entity during its initial years of existence by presenting a valid reason for foundations, corporations, government agencies, and individuals to financially support it.
    - The entity's purpose and mission statement frequently appear together in a written document on an entity's website.
    - Mission statements should be periodically reviewed to determine its ongoing relevance, adequacy, and accuracy. It should also highlight the entity's uniqueness and viability. If it is found to be lacking in any of these areas, the Board should update the mission statement accordingly by a vote.
- To select the Executive Director,
    - Most nonprofit Boards are comprised of volunteers. Some jsurisdictions such as New York State do not allow such Directors to receive compensaion for the work they do on behalf of their organizations. As a result, Board members often have obligations which prevent them from doing the work of the entity on a daily basis. In addition the Board's responsibiltiy is to govern and not manage the non-profit. As a reuult of these factors, Boards must delegate the entity's daily managerial functions to the salaried staff of the non-profit. Chief among these employees is the Exectvie Director.
    - The selelction of the Exectuve Directror, who fucnions as the Chiuef Exectuve Officer (CEO) of the non-profit, is second in importance only to the formulation of the entity's mission statemetnt and purpose.
    - The CEO of a non-profit is often called the Executive Director. The exact duties and auhority given to Execuive Directors of non-profit organizations by their respective Boards var and are usually stated in a contract between the ED and the Board. In some casees, the reporting structure is such that the Executive Director is the Board's only employee and every other staff

member of the non-profit is the ED's staff member. In many organizatoins, the ED has a level of authority that might seem to rival thatof the Board, but Boards cannot delegate their fundamental responsibilities to another.

- To support the executive and review his/her performance,
  - The effective evaluation of the entity's ED can ensure that the Boards plans are implemented and its goals attained. Hyman (2011) indicates, however, that this is a responsibility is often neglected by Boards. He notes the most common reasons for this are:
    - fear of conflict,
    - lacking adequate resources,
    - a lapse in judgement (Hymen, 2011).

  Hyman notes that, in order to be most effective, these performance reviews should evaluate accomplishments rather than be based on the personality of the ED (Hymen, 2011). This analysis can be carried out effectively by establishing a formal policy for the chief executive's annual performance review. Hyman suggests that this evaluation be one component of an overall annual performance evaluation of the organization as a whole. Many Boards do make the executive evaluation part of an annual cycle of broader organizational evaluation because the executive's performance is so closely associated with the performance of the organization. This gives the Board verifiable performance measures of the ED's effectiveness. Information on the ED's accomplishments is very helpful, as the information on organizational performance yields comprehensive measures of executive performance. Furthermore, such measures lead to the establishment of the following year's entity-wide goals. These goals form the basis for the Executive Director's performance review for the upcoming year.
- To ensure effective organizational planning,
  - Good governance dictates that non-profit Boards consider factors that will affect the Board in future years and take actions that willl reasonably assure that the organization will remain not only viable but successful during that time.
  - An often overlooked part of planning for an organization's future is risk analysis. This is a thorough evaluation of the factors that might jeopardize the orgnaization's financial well-being and continued survival. Some issues that a Board might underdake in this evaluation are its insurance policies and the existence of organizations with which the entiy is competing for donar funds. This is a key reason why the mission statemnt of an entity should be evaluated

regularly; there is a need for non-profits to express an identity distict and separate from other entities so that donors will not view them as interchangeabe and by extension will not think that donating to one has the same effect as donating to the other.

- Risk Analysis can hightlight factors thatr need to be considered in the non-proffit's annual budge process wihich as mentioned above is an area in which Board influence is critical. Evaluating and accepting the annual budget is another key area of organizational planning.
- Some other areas include:
- Enusring that key employee positions are filled on a timely basis;
- Assuring that phsyical accomodations and the related leasees are adequate;
- Evaluating and Joint programs wih other organizations to ascertain that the non-profit will be well-served by the ventures.

- To ensure adequate resources,
    - This responsibility is the main reason that non-profit Boards approve an organization's annual budget. Depeonding on the size and structure of the Board and the non-profit's staff, Board mamebers might work closely with the staff in formulating the budget. Or the budget might be prepared entierly by staff and presented to the Board for its approval.
    - In addition to approving the annual budget, im some non-profit organizations Board members have mandatory giving levels which they have to meet in order to remain on the Boad. For example, New York Walks to End Domesic Violence, an organization which could not maintani funding after the September 11th terrorist attacks reqired Board members to contirbute $1,000 annually to the organization as part of their Drectoror responsibilities.
- To effectively manage resources,
    - Onece the Baord has ensured that the non-profit has adequate resources, it must ascertain that the managemennt team is using and managing the resources in such a way as to ensure that th entity can meet its financail obliagations. The most comon ways that non-profit Boards perform this function is through review of the entity's financial statemetns and by managin the annual financial statemetn audit process.
    - Any finaincial statements generated by manangement should be presented to the Board or a committee of the Board such as the Executive Committee or Fiancne Committee. The former is usually compriesed of the executive officers of the Board such as the President, Vice-President,

Treasurer and Secretary as well as other members chosed by the President. The latter is most often chaired by the Treasurer and is comprised of Board members who have a background in accounting or finance. These committess should review the fianncial stattements for accuracy; have any related questions anwered by management; and bring to the full Board any matters that the Committee members deem important. The frequency of financial statements (monthly, quarterly, annually) depends on the organization. As a general rule, good governance practices recommend that financial statements be generated at least quarterly. Regardles of this, the annual financial statements are deemed to be most important as these are usually subject to an annual independent audit. Such statements should be carefully reviewed and possibly even presented to the whold Board by management for approval prior to the start of the independent audit.

- Independent auditors should be interviewed by, hired by, and report directly to the Board of an entity, not its management team. It is the auditors' responsibility to opine on whether the management-generated financial statemetns represent in all matthers the financial status of the non-profit for the period just eneded. The audit firm should meet with the Board (or a subset of the Board most commonly the Audit, Finance or Executive Committee) to prseent its audit findings which include its opinion on the mangement team's effectiveness. The audit report must be accepted by a vote of all the Directors. Each Board committee to which the report is presented prior to the whole Board should vote to accept the report and have it presented to the next group that will review it.

- To determine and monitor the organization's program and services,
  - Closely related to the idea of resouce funding for the non-profit is the idea of allocating the resoucse adequately to the non-profits's programs and services. Just as a for-profit corporation is evaluated on whether it increases shareholder value; a non-protit entity is evaluated on whehter it effectivley provides progams and allocations in line with its mission statement and purpose. During the initial years of an enttiy, programs and services are closely scrutinized by the Board with Directors playing an active role in proposing and scrutinizing them. Once an initial slate of programs and services are set, management has disreion to update them basedon changing condisions so long a the Board is notified and the chagnes do not profoundly alther the programs and servies.

- A non-profit's major new programs need Board approval to verify that these are in keepong with the organization's mission statement. The Board can ask management to justify the reasons for proposting new programs and servies and should obtain inforamation to confirm that the new activties will be appropriate ones in which the enttity should engage. If the Board does approve any new programs, this approbal should be memorialized by a Board vote. Once approved, the Directors should ask the entity's execitove staff to report on the effectiveness of all major programs.

➢ To enhance the organization's public Image,

- Non-profit Board members have a tacit responsibility to behave in a way tha creates a positive opinion of them in the public's mind. By extension, this positve image extends to any non-profit on which the Director serves. As noted earlier, Board members who become embroiled in negative legal issues can be asked to resing from a non-profit Board or can be removed by a vote of other Board members.
- A major way that non-profit Board members can ehnance the image of the non-profit organizations they serve is by donating sizable sums to the entity. This serves as an indication to the public that the Board members believe in the non-profit's mission and purpose. It also shows the public that Board membrs have faith in the entity's continued viability because they would lose such donations if the non-proft ceased to exist.
- Another key way in which Board members can enhance the public image of thnon-profit is to avoid discussing private entity matters in publie and to judiciously highligh the entity's accomplishments. To this end, most non-profits have their Directors sign confidentialtiy agreements so that Board members know exactly what they are allowed to discuss with non-Board members.

➢ To serve as a court of appeal,

- A non-profti's management team is responsbile for oversseing all employee and vendro relationships for the entity. Ideally, the staff fucations as a team in implementing the Board's vision for the entity. However, this is not always the case. In most institutions, when an employee has a complaint against or a professional issue with his or her immediation supervisor that employee can duscuss the situatiuon with the immediate supervisor's manager. In a similar manner, if an employee or vendor needs to discuss a matter concerning a member of upper mangement, this person can approach the Board of Directors. As the Board of Dirrecotrs bears ultimate responsibility for the operations of the non-profit, it has the abiltiy to overtrn any decision made by the executive management team.

  - As a practical matter, most Boards rarely exercise this power and only do so judicsiosly and after great deliberation. This is so because the relationship between a non-profit Board and its senior management especially its Exectuve Director is one based on mutual trust. If the Board overrules manageent's decisions, it exhibits a lack of trust in mangement's ability to govern the entity. Relationships such as these can rarely survive wihtout a chagne in either the composision of management or the Board.

- To assess its own performance.
  - The diverse nature of governing activities in which non-profit Boards engage leads to a variety of criteria on which they can be measureed. For example, if a Board were to undertake a fundraising campaign, they would vewi their progress and ultimate success on the amount of money raised and the timeframe in which the funds were received. If the Board had a major goal of establishing a new database system, then the evaluation criteria would be different.
  - In this latter case, the Board might evaluate itself on whetther it chose a database system within the budget it had aproved; whether the dateabase probided functionality to all the departments that needed it; whether the software was compatible with the entity's existing software; whether the process of chooosing the dateabase was completed wihtin the timeframe determied by the Board.

6. Unspoken Requirements for Board Members

Non-profit Board members are in most instances' volunteers (Some jurisdictions such as New York State forbid such Directors from receiving compensation). However, although thee Directors do not receive a salary for the work they do on behalf of the entity, they still have certain legal duties to the non-profit. This is due to their being recognized as fiduciaries of the entity by the non-profit corporation laws under which the non-profit was incorporated. These laws create legally binding duties for the Board members. These obligations are "unspoken" in that they are inherent due to the fiduciary role Board members play rather than being formally enumerated as are the mission statement and purpose of the entity. These are also duties that each individual Board member rather than the Board as a whole has to the organization. They are also overarching and many of the responsibilities that are enumerated above fall under them.

As these fiduciary duties arise from the incorporation of the non-profit under its respective state law, a Board member can face prosecution if the Director is found to have violated any of them (National Council of Nonprofits, 2017). In 2015, New York State Attorney General's Charities Bureau issued guidance for non-profit Board members regarding their fiduciary duties entitled "Right from the Start: Responsibilities of Directors of Not-For-Profit Corporations". These guidelines identified three main statutory duties: the duty of care; the duty of loyalty; and the duty of obedience (Charities Bureau, 2015).

The Duty of Care: The duty of care requires that Board members act in good faith in exercising their oversight of the non-profit which they serve. In plain language it means that the Board members will to the best of their individual abilities honor the commitment they voluntarily made to sit on the Board. The NYS Charities Bureau identifies several key areas on which a Board should focus and particular actions it can take to effectively exercise its duty of care and practice good governance (Charities Bureau, 2015). These are as follows:

- Practicing due diligence in assuring that the entity complies with all relevant laws and regulations;
- Establishing decision-making processes to facilitate major decisions;
- Undertaking continuous financial review;
- Performing risk assessment; and
- Reviewing CEO performance;
- The Charities Bureau's recommended compliance activities mirror provisions of the Sarbanes-Oxley Act of 2002 which apply to for-profit publicly traded companies. Keogh 3 The specific activities that he NYS Charities Bureau recommends Boards undertake to assure full compliance with laws and regulations are:
    - Create and execute a comprehensive compliance program,
    - Engage an independent external Certified Public Accountant (CPA) to perform an annual financial statement and compliance audit,
    - Develop a written plan to protect whistleblowers,
    - Implement internal controls over financial reporting and the safeguarding of assets and evaluate the operating effectiveness of these controls.
- Another Charities Bureau recommended activity is for the Board to create a comprehensive process to evaluation and decide upon major items that impact the non-profit's financial health. These include fundraising programs; external auditor fees; compensation agreements; and construction agreements. Research conducted by Ostrower and Stone (2010) supports having non-profits follow Sarbanes-like practices by expanding the knowledge base of Board members regarding these practices. They state, "Having board members who also sit on corporate boards, was positively and significantly associated with engagements in five of the six practices (have an external audit, have an independent audit committee, have a written conflict of interest policy, have a whistleblower policy, do not use same audit firm and/or lead partners for more than 5 years)".

Duty of Loyalty: This fiduciary obligation is defined by the Charities Bureau (2015) as the duty to act in the interest of the corporation in all matters. This means that the Board members will not engage in any activity whereby they might personally profit either in reality or appearance from any interaction involving the entity. A situation involving the entity in which the Board member might personally profit is called a conflict of interest. Most non-profits address these situations via a conflict of interest policy. These policies include definitions of situations that give rise to conflicts; require annual disclosure by each Board member as to whether such conflicts exist for him or her; and how the will be evaluated and addressed. These latter functions are usually performed by a Board committee.

Duty of Obedience: This fiduciary duty requires that Board members themselves and the non-profit they serve both comply with all applicable laws and regulations, the respective Keogh 4 mission statement, and internal governance protocols. In other words, the duty of obedience requires the Board to follow every aspect of the duty of care and obedience.

> It should be noted that that a Board is not guaranteed success in its endeavors even if it meets all of its obligations. Lincoln Center for the Performing Arts conducted a search for a new Executive Director that rivalled those of for-profit corporations which culminated in the appointment of Deborah Sklar, the then president of Barnard College. She resigned a year later.

7. Activities in Which These Boards Typically Engage

Many of the common activities in which Boards engage have already been discusses in the preceding sections. That is because the fulfilment of many of the duties and responsibilities outlined above are inexorably linked to activities. For example, selecting an Executive Director is a responsibility governed by the fiduciary duties of care, loyalty and obedience as the selection process should be carried out to the best of the Board members' abilities; be free of any conflicts of interest with Board members; and be in compliance with all requisite laws and regulations. The actual selection of the Executive Director requires the Board to engage in certain possible activities such the hiring of an executive search firm; interviewing the actual candidates and reviewing the candidates' references.

The volume and type of activities in which Boards engage beyond those that are necessary for them to meet all of their duties and responsibilities as well as the level of such involvement depends on the specific entity's structure and needs. Many functions such as fundraising can be almost entirely to qualified and experienced staff. Two activities, however, must remain the purview of the Board: The selection of the entity's Executive Director; and the selection of other Board members. As we have reviewed the former in some detail, we now turn to the latter function.

An entity's first Board of Directors is generally formed during its incorporation process. Those non-profits which seek to be granted tax-exempt status by the IRS are required to have Boards in place at the time of the request for this status. Typically, those who serve on an entity's first Board are selected by the founder who many times is then hired by that Board to be the entity's first Executive Director.

Established non-profits have a formal protocol for new Directors to join the Board. Such a process will involve the formation of a Nominations Committee the purpose of which will be to accept applications for open Board positions. Members of this committee will receive and evaluate (including interview) the prospective candidates. Evaluation criteria include the number of Board seats that need to be filled as well as specific skillsets (such as accounting and finance) which are lacking among Board members. Once the committee has selected the slate of prospective candidates, this slate will be presented for voting. The particular group which will vote on the slate depends on the specific non-profit. Member-based organizations such as professional societies will present a ballot to each dues-paying member. Other non-profits' Boards will be determined by a vote of current Board members. Board members are elected for a set term and must run for re-election if they would like to serve for additional terms. Once elected, the Board members elect the officers (President, Vice-President, etc.) from their own ranks.

8. Good Governance Practices

Two effective methods of creating a climate of good governance are a Board of Directors Handbook and annual governance training for Board members.

A Board Handbook describes in detail the behavior expected from a Board member as well as those actions which are deemed inappropriate. Typical items found in these handbooks are:

- A Code of Conduct;
- A conflict of interest policy;
- Attendance policy, if any, for meetings of the Board;
- A description of the Board officer positions;
- A description of the Board committee structure, if any.
- Any additional information deemed necessary for the Board members to perform their duties, such as a description of the different departments within the entity.

The Code of Conduct usually contains a description of the duties and responsibilities of Board members noted in preceding sections. It typically also describes prohibited actions and transactions.

9. Violations of Good Governance Practices

Misconduct is the term used to describe behavior and actions conducted by Board members which violate good governance practices. The most common items which fall into this category (some of which have been described before) are:

- Disclosure by a Board member of the entity's confidential information to a third party.
- Using the entity's resources (both tangible and intangible) resources for the Board member's personal benefit.
- Assisting another entity which is competing with the Board member's non-profit.
- Continuous non-attendance at Board and/or Board committee meetings.
- Receiving kickbacks from vendors who do business with the non-profit in exchange for giving the vendor the entity's business.
- Failure to disclose or resolve a conflict of interest appropriately.

- Any other act or behavior contrary to applicable laws, regulations, policies or code of conduct/ethics whether internal or external.

10. An Example of a Well-Functioning NFP Board

For an example of a non-profit which practices good governance and, therefore, has a well-functioning Board of Directors, we turn to The Girls Scouts of America. The GSA is known as a premier non-profit in terms of its innovative programs and the leadership training it gives young girls. It has a reputation for having a dedicated, ethical Board of Directors which has remained free of misconduct. It follows many of the good governance practices we have detailed above. We highlight below one which we have not yet mentioned.

The Girl Scouts of America was founded in 1912 and is currently headquartered in New York City. The national board of directors consists of 30 diverse individuals from a variety personal and professional backgrounds. Non-homogeneity of backgrounds is a quality for which all Boards should strive. Successful Boards benefit from a variety of opinions that diverse members can present because of the innovative ideas that can arise from them. The Girl Scouts Board, for example, includes people with backgrounds in accounting, finance, retail, and telecommunications. As these are all areas which are germane to a national non-profit that is known for selling goods, the organization can benefit from the vast multi-subject knowledge of its Directors.

A major benefit of such knowledge is that it decreases the likelihood of the Board members being deceived by corrupt vendors and staff. This in turn reduces the opportunities for fraud to occur within and against the organization.

Girl Scouts Board members serve 3-year terms and can run for re-election at the end of any term. In order to create the greatest possible pool of Board candidates and thereby promote the highest level of diversity, nominations for the Girl Scouts Board are open to the public on the organization's website. This easily accessible method allows anyone to nominate him/herself or nominate another individual. Three-year Board terms are favored by non-profit organizations because they promote accountability of Board members for the organization's recent successes and/or failures. It is important to note that the three-year term for Board members is a matter of practice not a legal or regulatory mandate.

11. Cautionary Information for Entities

As noted above, one of the key responsibilities of non-profit Board members is to oversee the work of their organization's Executive Director. Many times, once this role is filled, Board members don not adequately review contracts presented by Executive Directors. This can lead to an abuse of power by the ED and represents misconduct on the part of the Board members. An example appears below:

- Jonathan Dunning the former CEO of the Birmingham Health Care & Tuskegee Clinic (BHCTC), hired as the entity's consultant, a for-profit company he owned, Synergy Medical Solutions. Over a four-year period, the company earned two million dollars from BHCTC. Conflicts of interest can exist between the entity and its executives in the same manner that they can exist between the organization and its Board. The Board members did not know of this conflict of interest and did not, therefore, take steps to prevent it nor rectify it. As a result, the BHCTC was in violation of federal regulations. The Internal Revenue Service (IRS) requires the disclosure of any transaction greater than $100,000 between a non-profit and any related party such as a Board or staff member. Therefore, this Board failed in both its duty of care and its duty of obedience. In 2008 Dunning committed additional fraud by creating a real estate company under his name and entering into several transactions with the entity. When was arrested by the federal agents on 112 count fraud charges and indicted for bank fraud, money laundering and conspiracy.

12. Sanctions for Board Members Who Violate Laws and/or an Entity's Rules

What remedies an organization has for the misconduct of its Board members depends on several factors. These include: Severity of the misconduct; whether the misconduct is intentional; and, if the misconduct violated laws and regulations or the entity's internal rules. The former will have specific punishments mandated while the latter might give the organization some leeway in determining the appropriate punishment.

13. Other Regulatory and Legal Issues Related to the Conduct of Board Members

As non-profit organizations are incorporated under state law, Board members must be aware of the specific laws and regulations of the state in which their Board is incorporated. One such area is state registration of non-profits raising money in a state other than their state of incorporation.

Many states require that a non-profit which reaches a certain threshold of donor funds received from residents within its state must register with that state. This is independent of and unrelated to the registration requirements for the non-profits within its state of incorporation. Board members have a duty to make certain that all such certifications for their respective non-profits are current.

Another key area that Boards need to review at least annually is whether the entity has current and sufficient insurance coverage. This is true for all the entity's activities as well as the Directors; and Officers' policy.

14. Government Entities Which Regulate the Function of Non-Profit Boards

- State

A corporation is granted non-profit status by a state government: and is, therefore, regulated by these governments. The level of oversight varies from state to state. Often, those who wish to from a non-profit will do so in a state that they perceive will not heavily regulate the entity's activities. Specific requirements for Board members also depend on specific state regulations.

It should also be noted that states can have different requirements for different types of non-profit entities. As noted previously, the New York State Attorney General's Office has a Charities Bureau which offers guidance to non-profits and oversees their operation. This Bureau, for example requires that non-profits which are granted tax-exempt status by the federal Internal Revenue Service (IRS) are under Internal Revenue Code (IRC) Section 501©3 and which generate a certain annual revenue level submit their yearly independent auditor's report with the New York State Attorney General's Charities Bureau.

In addition, New York State law requires every not-for-profit operating in New York to have a written conflicts-of-interest policy. This policy must adhere to the guidelines outlined previously (e.g., defining clearly the circumstances that trigger such a conflict, etc.)

- Federal

Organizations which achieve non-profit status under state law frequently register for tax-exempt status with the federal government. This designation releases the entity from an obligation to pay federal income taxes. Once this federal status is grant ds most states extend "tax freedom" from their respective state income taxes to the entity as well.

All organizations which register under IRC section 501© are tax-exempt at the federal level. Those which are registered under section 501©3 can over donors the benefit of having those donations be tax-deductible on the benefactor's federal tax return. In a manner similar to the case of the entity's state income tax return, these donations are deductible on the donor's state tax return as well. As this is an enormous benefit to donors, the regulations of 501©3 entities are much greater than those of other tax-exempt organizations.

For example, every 501©3 entity is required to have a board of directors. Federal regulations do not, however, require that the board undertake specific governance activities such as requiring an annual financial statement audit. As noted above, some states require certain non-profits to have and submit these audits to state agencies. These audits, however, do not require certifications by upper level management as to the nature of the internal control structure of the entity as is required for all publicly traded for-profit corporations registered with the Securities and Exchange Commission.

15. Conclusion

Non-profit Board of Directors although volunteers have many diverse responsibilities to the organizations which they serve. The level of involvement any particular Board member has with his/her entity is a matter of choice for the Director. However, there are minimum requirements to serve on these Boards and a lack of involvement in the organization's governance by Board members can lead to not only a poorly functioning organization but legal penalties for the Board members as well.

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