

TWELVE “BEST PRACTICES” FOR A PROPERLY FUNCTIONING BOARD*

Board Composition:

1 Identify the various skills needed for effective Board oversight; assess whether Board composition is appropriate and adjust board composition as needed.

- Appoint members with a range of experience, diversity, knowledge and judgment (financial literacy is important). Add new members every so often.
- The Board should proactively and continuously monitor whether it has the necessary tools it needs to perform its function effectively. Develop a process for evaluating what’s missing. Don’t just add a board member because of her willingness to serve; add her for what she will bring to the Board.
- Board members should not be compensated for Board-related services other than reasonable reimbursement for expenses directly related to Board service.
- No member should serve as the Chair and the Treasurer simultaneously.
- No elected member of the Board shall serve for more than 5 years without standing for re-election.

Define Responsibilities:

2 Clearly define and communicate the respective roles of the Board, committees and senior management.

- Educate the Board as to its individual members’ duties, specifically the duty of care, duty of loyalty, duty of obedience to the law and duty to meet the general business standard.
- The Board’s function is to govern, not to manage. The Board is responsible for:
 - Establishing and implementing the organization’s overall direction, goals and mission.
 - Ensuring sufficient funds to accomplish the organization’s mission.
 - Establishing internal controls.
 - Hiring and firing the Executive Director (“ED”).
 - Reviewing the ED’s performance.
 - Setting the ED’s salary.
- Only Board members may vote on Board decisions.
- Discussions regarding all of the above must occur in person. The Board should not act based on email or telephone conversations.
- The Board should not decide on management issues of the organization. If a staff member or volunteer presents a management-related question to the Board or a Board Member, she should be directed to the ED.
- Fully inform any new members of their responsibilities as a Board member, and provide them with information necessary to actively participate in upcoming Board decisions.
- Establishing committees can improve the Board’s effectiveness, particularly if the Board is large. Committees are subject at all times to the direction and control of the Board. The Board must clearly define the scope of responsibility of the committees (specifically, whether the Board has delegated authority to make a decision, or whether the Board has only asked the committee for a recommendation).
- Although individual members will have varying opinions about issues, the Board must “speak with one voice” once a full discussion has taken place and a decision has been made. Minutes should generally reflect discussion, but not name names unless a person votes “no”. An abstention is the same as a “yes” vote in Minnesota (If a member truly wishes to abstain from a decision, she must recuse herself and leave the meeting to not be a part of the vote).

3

Internal Controls:

Establish a system of internal controls that require senior management to inform the Board of significant transactions.

- Adopt a policy outlining the types of transactions that need Board (or a Board Committee) approval.
- Adopt a policy to ensure that no person bears the sole responsibility for receiving, depositing and spending the organization's funds.
- The Board should consider requiring that the Chair or the Treasurer certify (or at least review) the financial statements of the organization and the Form 990 (the IRS Information Return).

4

Engaged Board:

Empower the Board to ask the "hard questions" by educating the Board members about their fiduciary duty to be fully informed and to make necessary inquiry.

- Meet regularly. Hold at least 4 meetings per year.
- The Board should receive reports from committees and senior management sufficiently in advance of meetings for the Board to review and consider.
- The Board should allow those with opinions or information regarding the organization to attend Board meetings and share ideas for guidance (however, only Board members may vote on Board decisions).
- While the Board is permitted to rely on information, opinions and reports prepared by others, Board members cannot avoid their responsibility to inquire. Board members must actively question management and outside advisors when they see a "red flag".
- Educate Board members that they are not only encouraged, but are required, to ask the hard questions. Board must be careful to retain the necessary oversight over committees and not rubber stamp committee or senior management's recommendations.

5

Self Evaluation:

Establish and implement an effective annual self-evaluation mechanism (including the opportunity for anonymous input) for the Board to review its performance and the performance of its committees.

- Revisit the vision statement and make sure the action in the past year has moved the organization closer to its goals.
- Revisit the bylaws and make adjustments as necessary to ensure the Board is functioning as stated.
- Consider developing a form that the Executive Director can use in evaluating his or her own performance in the previous year. The Board can compare its own analysis with the self-review to evaluate the Executive Director's performance and decide whether changes are necessary.

6

Feedback Mechanism:

Adopt a whistleblower policy and establish an appropriate anonymous means for employees (or volunteers) and others to report compliance concerns.

- The Board should ensure that there is an appropriate and effective means for employees (or volunteers) to report compliance concerns and make sure concerns are addressed. Having a feedback mechanism is specifically inquired upon in the Form 990.
- A hotline may not be appropriate for all organizations (it's expensive), but a suggestion box or other means for employees to report concerns may suffice.
- Templates outlining common feedback system can be found online.

7

Conflicts of Interest:

Adopt a substantive conflict of interest policy.

- If any transaction or action of the Board may present a Board member with a conflict of interest, he or she shall disclose the conflict in a timely manner.
- The member with the conflict of interest should abstain from voting on the action or transaction (if appropriate, leave the room so Board can discuss freely).
- If the Board decides to enter into a transaction with a party that has a conflict of interest, Board members should document that they have explored the same transaction with unrelated parties and established why this transaction with a related party furthers the organization’s charitable purposes.
- It is important to address the “appearance” of the conflict of interest. Make it visible so no questions are asked.

8

Establish an Audit Committee:

Establish a Board audit committee comprised of independent Board members to oversee financial reporting, risk assessment and management practices.

- The Audit Committee shall consist of Board members who are “independent,” which means not being on the management team, not receiving compensation, and not having a financial interest in, or any other conflict of interest with, any entity doing business with the organization.
- The Audit Committee shall engage auditors, review audit plans, and review financial statements, accounting policies, internal compliance programs as well as tax, legal and regulatory matters.
- Members of the audit committee should meet financial literacy standards (have accounting and financial management expertise).

9

Rebuttable Presumption of Reasonableness:

Establish a rebuttable presumption of reasonableness for all transactions with “disqualified persons.”

- Compensation is approved by the Board or a committee composed of individuals without a conflict of interest. The person being compensated should not participate in the approval.
- The Board must rely on appropriate data as to the compensation’s reasonableness to create the presumption. The Board must do its own research regarding compensation and discuss in person.
- The Board must adequately document the basis for its determination at the time the compensation is approved (not after the fact). Include in the meeting minutes what research had been done regarding the compensation, that a discussion took place, and which specific members approved the compensation. *Those who approve the compensation can be personally liable if it is too high and the rebuttable presumption of reasonableness has not been created.*
- The best source for determining proper compensation is a survey issued once every two years by the Minnesota Counsel of Nonprofits.

10

Oversee Finances:

Oversee finances; manage and spend the organization's funds appropriately.

- Use the organization's funds in a responsible, effective and efficient manner to further the organization's mission.
- The Board shall approve an operating budget prior to beginning of each fiscal year and receive financial reports at least quarterly.
- Regularly compare the organization's actual spending to the operating budget.

11

Be Transparent:

Be transparent to the public about programs, governance and finances.

- The purpose of having a system of self-review, conflict resolution, decision making, and other processes is to be as transparent as possible. This is important for purposes of maintaining the 501(c)(3) status, and for seeking donations. The Board should use the Form 990 as a tool to show both the government and the public that it is running a great nonprofit by illustrating exactly how it's being governed.
- Ensure that the organization's Form 990 accurately describes the organization's programs and finances.
- The organization's annual report shall include a description of the organization's purpose, activities, accomplishments, geographic area served, a summary of costs for each program, and a list of the Board members.
- Many donators check the Form 990 in deciding where to contribute, so put as much detail into the Form 990 as possible; use it as a marketing tool.

12

Follow Policies:

Follow your own policies, procedures and audit recommendations

- The Board should monitor management's compliance with the organization's policies, procedures and audit recommendations.
- Consider having an independent consultant/attorney perform an internal assessment of the organization's compliance with its own policies, procedures and recommendations on an annual or biannual basis.

**This information is a summary of the Hennepin County Bar Association's presentation, "Critical Issues for a Lawyer Serving on a Nonprofit Board," December 2, 2009, with speakers Ulrika Vettleson, Esq., Dorsey & Whitney, LLP, and Heidi Neff Christianson, Esq., Moore, Costello & Hart, PLLP, created by Anne K. Lindberg, Esq., Kretsch & Gust, PLLC.*