MaRS Guide

Establishing Governance

A start-up guide for new businesses and non-profit organizations

MaRS

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I: Good Governance – Getting Started

A bright idea takes shape in the mind of an entrepreneur. Some specific need or want will be satisfied when this idea gets to market. It may be the sale of a product or the offering of a service. The end customer may be another business (B2B) or an individual consumer (B2C). The enterprise will be for-profit or not-for-profit. To supply this need or want, a venture is created. As a non-profit organization (NPO), it will probably be funded by its founders' own resources at the start, or from grants and donations. As a for-profit venture, it usually begins with the founder's own funds, then friends and families invest, debt is provided, and at the right time, venture capital is acquired.

Step, by step, a board evolves

As each organization grows, an operating team is hired with the skills and knowledge to carry out the plan as directed. Whether they are volunteers or paid staff, they need to "buy in" to the elements and aspirations of the organization and assist in every way they can, within the limits of their capacity. The organization's leader will want to be sure that what he or she is doing is worthwhile, that their management style is fair, and that the organization is valuable and within the limits of the applicable laws. So the leader will need guidance and support, just like the team does. When the time is right, even before incorporation, the organization will need some form of a board of governors, directors, or advisors to provide this oversight and advice.

II: Canada's Governance Structures

The "business" of the country is carried out by three sectors: the state, for-profit organizations and not-for-profit organizations. Each sector has its members—those to whom the organization reports and to whom it is responsible for achieving its goals.

- The stakeholders of government-controlled crown corporations are its population.
- The stakeholders of share capital corporations number more than their shareholders. They also include its employees, suppliers, regulatory authorities, customers, financial supporters, and their communities.
- The stakeholders of NPOs include those who are served and their community; the work of the NPO may cover such varying facets of our society as health, welfare, poverty, new Canadians, and personal assistance.

Different organizations need different boards

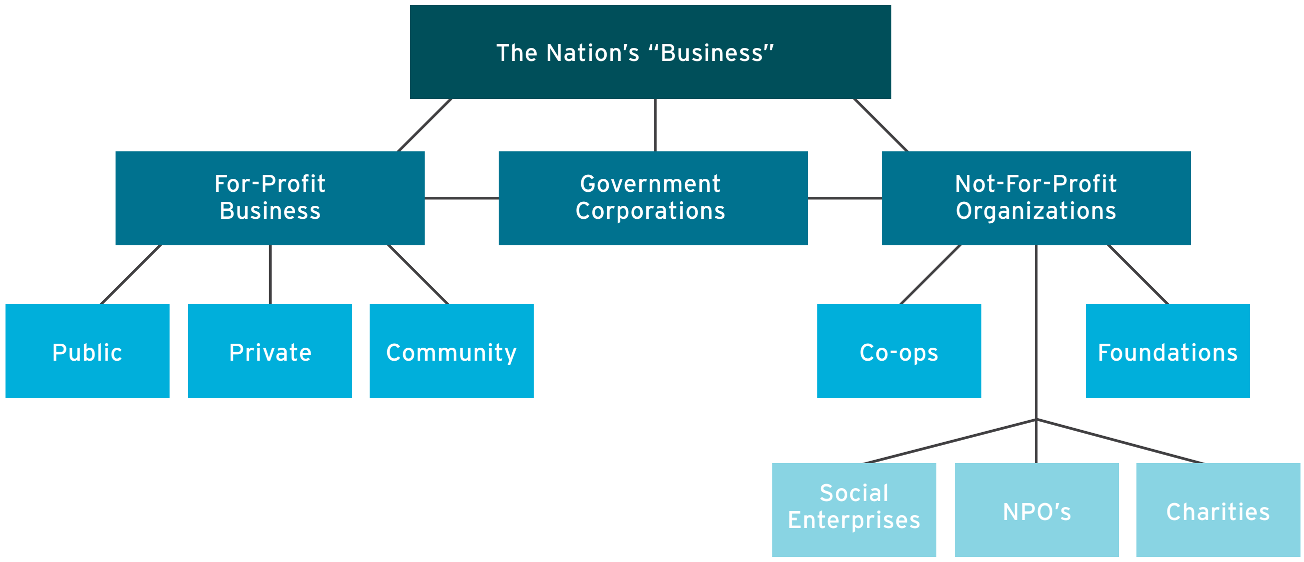
Figure 1 breaks down the nation's business organizations into three sets of corporate structures and eight types of ownership (or membership). The three sectors of business may be referred to as the Public, the Private, and the Community. The two non-government sectors are separated to distinguish their profit distribution differences.

Excluding the Crown corporations, the key difference between the other two sectors is that businesses intend to create wealth and redistribute it in part or in whole to their owners and/or shareholders, while non-profit organizations seek to assist people, their communities and their philanthropic activities. In doing so, they may operate a business to create surpluses (not profits) to augment their delivery of services (i.e., social enterprises).

Public vs. private boards

It is easy to recognize the three forms of corporations shown in the chart above: those that trade their shares publicly, those that do not trade their shares publicly, and

Figure 1 The Nation's Business



those whose shares are controlled by the governing family. Depending on their philosophy or size, family companies may trade their shares publicly as do many of the Canada's dominant corporations.

NPOs may incorporate and act like a private corporation but their mission is not to earn profit. Non-profit corporations include those with a community-based purpose such as science, patriotism, philanthropy, art, culture, social, and sports. Examples include hospitals, trade associations, non-government regulatory bodies, symphonies and universities.

Social enterprises stand out in the way they conduct a business to create surpluses and then distribute them in an altruistic way. One well-known example is Goodwill Industries (www.goodwill.org). It is organized regionally and operates a chain of stores selling donated goods while applying its profits to train underprivileged youth for employment. Like many similar social enterprises, it competes for its sales with for-profit businesses.

Charities are formed to support a whole community and help the needy; they have specific purposes such as the relief of poverty or disease, the advancement of education or religion, or the improvement of the lot of minorities and the disadvantaged.

Note: This guide does not cover the governance of co-operatives or foundations, nor does it deal with crown corporations.

The chart on the follow page lays out a number of governance elements and describes the key differences between shareholder businesses and NPOs.

Key Issues	Businesses	Non-Profit Organizations (NPOs)
Reason for being	their shareholders	their community or clients
Responsbility to	their shareholders and stakeholders	their members and the public
Goals	corporate wealth and growth of share value	community welfare and social purpose
Director's Income?	yes	no
Other Compensation	stock options, expense reimbursement	pre-approved expenses, but not always
Background	business and professional, related to the business / executive experience	business, professional, NPO experience / fund-raising talent
Involvement	usually not involved below the CEO	often involved with daily issues, depending on the management structure

III: Useful Definitions

The "business" of the country is carried out by three sectors: the state, for-profit organizations and not-for-profit organizations. Each sector has its members—those to whom the organization reports and to whom it is responsible for achieving its goals.

Many of the names, titles, and phrases normally associated with boards deserve explanation:

1. Governance

- The means by which the leading authority (the board of directors) guides and monitors the values and goals of its organization through policy and procedures.
- The process of overseeing a work activity at a level higher than direct managerial control.

2. Management

- Management in business is simply the act of getting people together to accomplish desired goals.
- Those in charge of running a business.

3. Chairperson

- A person who presides over a meeting or any body of people; the head of a corporation or a board of directors, a committee, or other formal entity.

4. CEO

- The chief executive officer, executive director, or president; the top executive responsible for the daily operations of a non-governmental organization; he or she reports to a board of directors.

5. Shareholders (or stockholders)

- Shareholders are the owners of a corporation based on their holdings. They own an interest in the corporation (at least one share) rather than specific corporate property.
- A shareholder may be a person, company, or institution.

6. Stakeholders

- Stakeholders are groups and individuals surrounding the venture who have an interest or "stake" in a corporation's activities. These include regulators, shareholders, customers, suppliers, employees and associated families.

7. Members

- Those who have been designated to vote at annual meetings and special occasions such as shareholders or donors who meet the definition of "member" as embedded in the articles of incorporation.

8. Directors

- Individuals elected by the shareholders to manage or direct the affairs of an organization, either for profit or not for profit. Director responsibilities involve establishing company policies, including selection and remuneration of the operating officers and the payment of dividends, if applicable.

9. Officers

- An executive of a company who shares legal liability for his or her company's actions.
- One who holds an office of authority or trust in an organization such as a corporation, or in government.

10. Trustees

- Individual(s) or an organization that either holds or manages and invests assets for the benefit of others.
- Members of a board elected or appointed to direct the funds and set the policy of an institution.

11. Advisory Board

- A group of individuals who have been selected to help advise a business owner regarding any number of business issues, including marketing, sales, financing, and expansion.
- A body that advises the board of directors and management of a corporation but does not have authority to vote on corporate matters.

12. Council

- An assembly of persons called together for consultation, deliberation, or discussion.
- A group of people chosen as an administrative or advisory group to oversee a family business or an NPO organization. Their authority and responsibility is less than that of a formal board.

13. Non-profit organization (NPO)

- An incorporated organization which exists to serve a worthy cause, and from which its shareholders or trustees do not benefit financially.
- NPOs are usually established with the objective to address a social need, rather than simply to provide a service to generate revenue.

14. Corporation

- A legal entity that exists independently of the person or persons who have been granted the charter to create it; it is invested with many of the rights given to individuals.
- A private corporation is a corporation whose shares are not publicly traded and are usually held by a small number of shareholders.

IV: Keys to Good Governance

For-profit corporations and NPOs are composed of members or shareholders. They elect directors who appoint officers. The members also appoint the auditors. The directors govern the organization. Directors owe a fiduciary duty to their venture. They must act honestly, in good faith and in the best interests of the venture. Good governance is much more than just governance, however. Often-stated references to good governance include the following:

- Vision–envisioning the future and developing a corporate mission
- Direction–setting goals and policies for the venture
- Transparency–maintaining open processes, shared information, effective communication standards, and regular and meaningful reports
- Guidance–providing advice and direction
- Due diligence–getting inside the metrics and judging the risks involved
- Commitment–being engaged emotionally and intellectually to the venture's course of action

Much has been written on the subject of good governance. Essentially, it is the ability and willingness to ask the right questions at the right time and to provide good advice while demonstrating confidence in the venture.

The "double-duty" of the non-profit organization

A cynic may define for-profit organizations as self-centred and non-profit organizations as other-centred. It isn't this simple. Non-profit governance is more complex given its need to assist the organization to better use its resources in managing its focus. In his book, Managing the Non-Profit Organization, Peter Drucker suggests that the "bottom line" of an NPO is the community and that the board's job is to define this bottom line. Others have suggested that NPOs have a "double bottom line." Drucker states that while NPOs are not businesses, they must act "business-like." As well as financial self-sufficiency, they must work toward outcomes such as "the betterment of…", "the enhancement of…" and the "growth and achievement of…".

What is due diligence?

One of the keys to good governance is the exercise of due diligence. Directors must be familiar with and understand the governing documents as well as the organization's current and expected financial situation. They must know the guiding legislation and appropriate regulations surrounding the activity of the enterprise. Due diligence also involves risk assessment and risk management. The organization's actions and decisions need to be judged with regards to the possible risks involved. As part of their planning role, directors have the responsibility to "raise a red flag" if in their judgment the organization is taking action that might lead to trouble—or worse, financial or legal problems.

It's lonely at the top!

Good governance begins with good management. Entrepreneurs who have a dream or a bright idea create their venture with the confidence that their goals are realizable. They gather around them a team to assist them in building their organization to serve the market they have chosen and to provide the goods and services they intend to offer. This management group becomes a team of peers; they share their expertise, their relevant background of experience, and their insights, support, criticism and energy. Their business leader, in contrast, stands alone. He or she has no peers. So the smart entrepreneurs, as soon as it is feasible, create some sort of advisory group or board of directors to provide guidance and knowledge to oversee growth of the new venture and to judge its performance against its plan and goals. As long as boards stay out of the day-to-day running of the venture, they can see the bigger picture and better sort out priorities. This oversight provides a confidential forum for dealing with key issues of leadership and the management of the business. It offers the venture's leader the opportunity to go to a supportive group for confidential advice and consultation.

So, why bother with a board? Because "it's lonely at the top!"

V: The Role of a Successful Board

It's quite simple: boards govern while management manages. Board members are stewards. Good boards work on the premise that while accountability can be delegated, responsibility cannot. Boards are responsible to their members for the success and failure of the organization. They oversee the conduct of the business or the NPO, always through its leader, not around him or her. For this process to work, the business leader must report to the board, not be a member of it.

The overriding role of the board is threefold:

1. **Financial:** This applies to both profit and NPO ventures. It involves overseeing the financial results, judging the forecasts, ensuring that lines of funding are available, seeing to the fair allocation of earnings, and guiding the leader to always focus on the right path to growth, financial security and success. This sounds like a business but it equally applies to NPOs. Not only does it take money to make money, it takes money to serve a community with a worthwhile mission.
2. **Visionary:** This means "doing the right things" as opposed to "doing things right." While the strategic plan should come from the management, the board can provide insight, vision and focus on the rightness of strategic objectives and the way in which they can be achieved. Given their wider scope and experience, board members can bring ideas from their own backgrounds to assist with strategy and implementation.
3. **Reinforcement:** This includes the strengthening of the skills of the board itself as well as the staff. It involves being transparent, adding wisdom to the day-to-day workings of the organization and ensuring that the many choices facing the organization are prioritized, while watching over the balance of compensation, authority and responsibility. This reinforcement bears upon all members of the organization—from the key executive through to the staff.

The importance of reinforcement

The first two roles above are easily organized into reports and periodic agenda items. Too often, especially when times are tough and the competition is making gains or the community is not responding, boards spend too much time on the money issues, not enough time on the review of the current strategy, and little time on the soft stuff of reinforcement. The third role requires the board to step back now and then to reflect on the greater good of the venture. A balanced board led by a balanced chairperson is sensitive to this three-sided leadership triangle.

What is "accountability"

Behind all of the nice words applied to the ideal attributes of any board, the strongest is "accountability." Accountability requires good governance from the voluntary sector as much or more than it does from the for-profit sector. It is the obligation to demonstrate and take responsibility for performance in light of agreed expectations. Accountability involves due diligence. There is a difference between responsibility and accountability: responsibility is the obligation to act; accountability is the obligation to answer for an action.

VI: Creating the Initial Board of Directors

Much has been written about the job of a board member. The following are a number of issues that need to be addressed as the board is formed. They form a checklist for the board as it starts the routine of meeting regularly. Entrepreneurs face many challenges as they create their organization. Many of these hurdles involve the regulations, restrictions and controls that govern the activity of an organization as it brings its products and services to market.

A good starting list will include:

- incorporation
- bylaws
- banking
- patents, intellectual property
- FDA approval
- accreditation
- product testing and approval
- market research
- taxation
- shareholders' agreements
- importing/exporting
- health and safety requirements
- packaging
- technology
- licensing

It is not possible to include here the many rules and regulations regarding these varied issues. Each of these business elements requires investigation to determine if they apply to your new venture. The key to early success is to address these issues from the start by connecting with experts who can guide your venture through its necessary compliance requirements.

Bringing expert help on board

Entrepreneurs, both corporate and non-profit, create their enterprise to fulfill a dream. As they formalize their mission, they seek advice from family, friends, business associates, fellow church members, the Internet, text resources and special organizations such as MaRS. As their dream takes shape, they add the few people who will share their goals and provide their time, talent and treasure.

As an organization emerges, functions such as marketing, finance and operations are created by new team members—some who want to become part-owners in the enterprise, and some who wish to remain employees. The owner/founder needs independent help, advice and guidance from beyond this group. Now is the time to create the first board.

In the early stages, the directors meet informally. Over time, directors ask for scheduled meetings, newsletters between meetings, and agendas in advance. As the board grow more formal, some of the early directors will step up to their responsibilities while others, for varying reasons, will drop out or remain in an advisory capacity.

Historically, there has been little attention paid to small businesses and their boards. One reason behind this lack of interest is that their boards were assumed to be "paper boards"—i.e., that their members were relatives or close friends of the owner/founder, not objective and not trained or qualified to carry out the obligations of a properly constituted and functioning board. Today, given the recent history of governance failures, there is increased political and regulatory pressure to set up active boards that contribute to oversight, risk-assessment and value creation. In summary, good boards give their businesses and organizations "the lead they need."

When is the right time to create a board?

When is the right time to create a board? There is a simple answer to this key question: "as soon as possible." A better answer is: "before the end of the start-up phase." To explain: all ventures tend to go through at least four phases as they mature and survive. The first phase is "start-up," the second is "emergence," the third is "expansion" and the fourth is "sustainability." As this guide focuses on creating governance, the start-up phase needs a brief explanation. "Start-up" begins when the entrepreneur embarks on pulling together the needed resources and commits to spending money in order to achieve the goals of the business plan. The start-up phase ends and the next unfolds when revenue from the sales and service provided begins to flow on a steady basis, or when individuals or groups of designated people begin to receive the guidance or service offered by an NPO. In the case of a for-profit business, this process could take years (consider the creation of an electric car) or in the case of a charity, it may take only a few weeks (consider a local church deciding to run a shelter service for the homeless in their community).

Taking into account all that you need to create a venture, good advice offers the greatest value. Even before you launch your enterprise, talk to peers and experts and seek guidance from sector associations or organizations like MaRS. This will help you reduce the unknowns and avoid pitfalls.

VII: Different Board Models for Different Ventures

Establish a formal board of directors, as soon as possible. See the details in the corporation's bylaws regarding numbers, officers, positioning of the business leader and board leader, frequency of meetings, and other numerous requirements. It is wise to check these bylaws regularly to ensure that compliance is in place. Related board forms include:

- **For-profit boards:** The press covers the corporate sector from every viewpoint. For-profit boards are structured around proven forms of governance and regulations. Their members are a combination of friends of the CEO, experts from similar businesses and specialists in matters such as human resources, marketing, audits, lending, and growth techniques.
- **NPO boards:** These boards may be responsible for the governance of a share-capital corporation and be guided by its Articles of Incorporation, or, more commonly, they may govern non-share organizations and be guided by its Letters of Patent. NPOs may be provincial or national. Their boards are made up of individuals with a variety of backgrounds but with a strong common desire to serve their community in a responsible way that is compatible with the organization's goals and mission. They also have a responsibility to ensure that funds are provided to meet the NPO's needs on an ongoing basis. Board members are often chosen for this key reason only. They meet the criteria known as: "give, get, or get off!"
- **Social enterprise boards:** Such boards have the dual responsibility of ensuring that the venture is properly funded until the profits from its business venture are available for its charitable mission. Even then, they watch over the balance between the source of funds from operations and the need for funding from donors, businesses, foundations or governments.

Informal boards

In the rush to get the venture up and running, setting up a proper board seems like a heavy task, one that might get in the way of building the venture. Two alternate forms of governance are outlined below; they provide the owner/operator with a team of people who are available to help grow the venture without the formal structure of a board of directors. Often, after a proper board has been established, one of these advisory forms of governance may be kept in place because of the unique nature of the venture.

- **Family council:** Often, family members act as the early advisors and form a family council. This council often includes the accountant of the firm, the lawyer, interested family members, and the founder. It is wise to keep the group small, with three to five members. This council is not used with NPOs because they rarely are family ventures. Usually, compensation is not paid to family council members. By avoiding the formality of a board of directors, the need for directors' liability is avoided (for more details, see section XIV of this guide). The council needs to be made aware of this. Later on, when a formal board of directors is set up, this council can become the board or remain as a family support group. Regardless of this extended role, it is essential that the individuals chosen support the mission and values with experience and objectivity.
- **Advisory council:** Similar to family councils, this form of governance is often voluntary. NPOs often create advisory boards to obtain the help of key individuals in the community who are proven specialists in the venture's field of endeavour, such as medical doctors who support an NPO health charity. Similar to family councils, advisors are available for advice and consultation on an informal basis and they may be called to meet on an as-required or regular schedule. Do not expect councils to provide capital or to raise funds; their role is background support.

Expanding the shape of the board

As boards increase in size and diversity, their work may need to be divided into committees. These committees usually meet between board meetings. They provide reports to the board at the appropriate time. The most common committees and usually the first to be set up due to their importance are finance (or audit), and human resources (or compensation). Depending on the mission of the venture, other committees may be formed. NPOs frequently establish a fundraising committee at the outset as well.

By the time these committees are required, the board should have grown in enough size and strength that each committee can consist of experts in their appropriate field. Avoid overloading board members with too many committee appointments. Keep in mind that board committees can be enhanced by including staff members and external specialists.

VIII: Board Size, Duties and Responsibilities

How big should a board be?

Typically, the first board of directors consists of a minimum of three people. This usually includes the owner/founder or the first president. Check the appropriate governing legislation or accreditation guidelines to determine any regulations related to board size.

As the venture grows and becomes more complex, additional board members are brought in. Each will bring to the board a special background that adds value to the total board. Key elements of the operation may require board members to have familiarity or expertise in areas such as research, marketing, fundraising, law, and finance, as well as knowledge of the relevant industry. A pattern of backgrounds needs to be developed to ensure that the board is balanced and valuable.

The bylaws of the venture should set a maximum number of directors and the board must endeavour to maintain this level. Try to ensure that the number of board positions is an uneven number, to avoid the problems that might arise from a tie vote.

When boards get too big, members find it easier to miss meetings. They also find it difficult to hold a reasonable discussion wherein everyone interacts. This can lead to the formation of sub-committees of the board where certain directors have greater expertise on a certain issue. This is the usual reason for establishing an executive committee that includes a few key board members. It is easier to get this group together more often. Nevertheless, subcommittees have the potential of lessening the effectiveness of the board. So the general rule is to create few subcommittees, but to have them for at least audit and compensation, and to utilize there the independent (i.e., non-management) directors.

Board Duties

The duties of boards, either for-profit or non-profit, include: establishing policies and objectives for the organization

- selecting, supporting and conducting performance reviews on the chief executive
- ensuring that there is adequate financing from

- lenders, share offerings or donors
- approving the annual operating plans and the strategic direction
- answering to the stakeholders, specifically the shareholders and/or members
- insisting upon regulatory audits and compliance with the appropriate authorities
- appointing auditors and approving the audited statements

Beyond this list, there are other more lofty responsibilities such as:

- ensuring that short- and long-range plans are generated, maintained and achieved
- enhancing the organization's public image
- setting a high-quality example of how governance functions and adds quality to the venture

IX: Board Recruitment and Tenure

Successful recruitment is the key to a successful board of directors. The expression "time, talent, and treasure" applies. Good recruitment finds and secures individuals with all three attributes:

- **Time**—to attend meetings regularly; to read over necessary materials between meetings; to see the organization in action, visit its facilities and get to know its operations.
- **Talent**—past experience in a similar field of activity; previous governance experience; a proven record of success in business, government or the community; or, the ability to provide a unique insight.
- **Treasure**—for the NPO, personal giving and/or the willingness to ask people and their organizations for money is a great gift. Beyond money, an individual's qualities and willingness to give of one's experience are a treasure welcomed by any board.

The following guidelines can help improve a board's ability to recruit the right people:

- Treat recruitment as a marketing program. Use the process to spread the word about the enterprise. Describe its history. Show confidence about its mission, vision and values.
- Put the subject of board recruitment on the agenda regularly.
- Always include a comment about the board when explain your mission.
- Develop job descriptions for board members.
- Insist that every board member remain vigilant for possible new members.

A growing need for diversity

Whenever possible, add to the diversity of the board. Those who buy shares or fund the venture want to be assured that it represents the best array of talent, not just friends or relatives of the founder.

Good boards always contain a diversity of talent and background. Individuals with backgrounds related to the focus of the enterprise are always welcome. Those with experience as members of other boards of directors offer value. Strategic thinkers always raise the level of board discussions. CEOs of non-competing organizations add strength and usually sound advice for the firm's leader. Gender diversity also provides value, as does ethnic diversity, especially if the venture focuses on Canada's metropolitan centres where ethnic diversity is highest.

How long is "too long" as a board member?

One faces pros and cons with board-member turnover. There is much to be said in favour of allowing members to serve as long as they feel that their contribution is worthwhile. Seasoned board members are quick to indicate that it takes time to fully grasp their role and learn how their venture functions. Corporate boards, where fees are paid (and more importantly, where stock plans and options are available), often leave the subject of tenure open. While this develops experience, it also has the possibility of generating complacency or "group think."

Busy members may resign if the workload grows too onerous, forcing the board to recruit new talent. On the other hand, a fixed board term such as three to five years, with the option to stay a second term, provides for a graceful exit while opening the door for new talent to come aboard. Some boards with this policy allow their retired directors to be re-elected after an absence of one or two years. A reasonable tenure is at least three years. By this time, a member can rise to the role of Vice Chair, then a year later, to the role of Chair. A retiring chairperson is usually asked to stay on one more year as "Past Chair." These matters need to be spelled out in the organization's bylaws and they deserve to be highlighted when new directors consider a board role.

The matter of board tenure can be solved by creating a rotating board. At the start, elect one-third of the board for one year, one third for two years, and one third for three years. Each year thereafter, replace the retiring members with three-year members. Members may be granted the right to be re-elected for one more term before retiring.

X: Separating Governance from Management

If the governance group governs and management manages, the CEO or executive director should not be a voting board member, nor should anyone reporting to this individual have voting privileges as a board member. The CEO, president, executive director, or general manager should report to the board as an ex-officio member. Family-controlled organizations may not choose to follow this advice because of their outright control of ownership. As reported in The Globe and Mail (July 29, 2009), when Ted Rogers was chairman of Rogers Communications Inc., his board voted 15 to 1 against getting into the wireless business. The opposing vote was Ted's. The rest is history!

While not a practice found with NPO boards, many businesses create their first boards with members of the management team, supported by independent or "outsider" members. While this is practical (and low-cost), these insiders need to be cautioned to step outside of their day-to-day responsibilities and rise to their role of governance. If the board is mixed in this way, it requires the appointment of at least an audit committee and a personnel committee made up from the independent directors. Where management sits on the board, it might be wise to appoint a "lead director," an independent, to act as chairperson. This helps greatly with establishing the board as not a super-management committee but an oversight committee, as it should be.

Many firms, especially family firms, create their first board of directors and combine the positions of CEO or president with the position of chairman of the board. This is often a result of the founder not wanting to relinquish total authority and control. The trend at the governance level among public corporations is to separate these two positions. The reasons go back to the major theme of this guide: "governance governs; management manages."

Carver's Policy Governance® Model

The Carver Policy Governance® Model is the best-known model of governance worldwide. It applies to all types of boards. Unlike the usual governance/management relationship of typical boards, policy governance demands that board's primary relationships be outside the organization—that is, with the owners. The board speaks with one voice or not at all. The chair and the CEO or executive director positions keep separate. The top venture leader attends board meetings but is not a member. The model provides another key mandate: boards must set a single point of delegation and hold this position accountable for meeting all of the board's expectations for performance.

The key to policy governance is the insistence that a CEO, president, general manager or executive director be appointed and held responsible for all management activities. The model holds that if there are committees, their deliberations and reports are delivered to the board, not to management. Frequently, NPO boards include management members at the board level and board members acting like managers as they assist the enterprise with its day-to-day goals. For these reasons, many organizations will not adhere to the Carver model nor consider its benefits. Policy governance requires the discipline of separating governance from management.

XI: Ensuring that Boards are Successful

More checklists!

Worthwhile board meetings rely on an effective chairperson. Too often, meetings can become overly formal and lose momentum via limited discussion, fixed timelines, too many internal reports, a lack of advance reports, and having just a few members dominate the discussion. The meetings themselves deserve to be monitored. Consider:

- Are we progressing toward our goals?
- Does our mission fit the times?
- Are we growing in purpose and value?
- Can we objectively measure the business and forecast wisely?
- Are we equipped "to see an accident on its way to happen"?

The following procedures will help maximize the effectiveness of meetings:

- Distribute sufficient information (e.g., financial and operating reports) to board members on a regular basis so they remain aware of the venture's progress (or lack of it).
- Issue a complete agenda in advance of board meetings so that members can review the material and arrive prepared. As well as the usual financial and operating agenda items, highlight in advance any key decision that the board is expected to make.
- Provide background materials as they are generated, not just in time for the meetings.
- Encourage members to communicate among themselves between meetings to better understand unfamiliar issues and results.
- Circulate minutes of each meeting as soon as possible afterwards, not at the next meeting.

Avoiding board meritocracy

Unlike the operations of an enterprise that may function five to seven days a week, boards tend to meet only periodically. The most common frequency is four times per year but among NPOs, it is often monthly. There is general agreement that a positive relationship exists between the length of board meetings and the involvement of the members. With longer meetings, they get to know the organization and each other better.

Over time, boards tend to become fixed in their habits: seating does not vary, the agenda appears the same, reports sound like reiterations of previous reports, and the focus centres on finance or trouble-shooting. Meetings become retrospective instead of proactive. Fresh concepts, self-examination, and impromptu strategic discussions do not surface. The meetings always end on time as everyone heads out to their next engagement. To counter this entrenchment, the board, and especially the chair, has to ensure that meetings are refreshing and worthy of the members' attendance.

XII: Board Renumeration

Pay or no pay?

The business thrust for profit ventures and NPOs varies greatly. One actively pursues strategies to enhance shareholder value while the other owes its reason-for-being to its members and the community. While many of the guidelines for establishing governance apply alike to both profit and non-profit ventures, the subject of compensation differs between those who seek to create profit and wealth and those who seek to assist or improve some element of society.

NPO boards are "special"

NPOs have one thing in common: their members and directors cannot make a financial gain from their investment of time and money. This includes social enterprises that are basically NPOs that generate surpluses for their good works, not profits. The Globe and Mail's "Report on Business" (August 12, 2009) commented that Canada has 84,771 registered charities that together reported donations of $10 billion for the previous twelve-month period for which statistics were available. Furthermore, they reported that "charities are more market-driven than they appear. They got more of their revenue from the sale of things ($11.5 billion), for example, than they did from straightforward donations."

One might think there is much to be said regarding the advantages of paying compensation at the board level of a venture. It could make it easier to attract the most qualified individuals whose time has value. It should make it easier to hold board members accountable for their actions. But does it? Plenty of evidence across our society demonstrates that busy people with huge job loads or responsibilities find time to serve voluntarily when they buy into the vision, mission and values of an NPO.

The bottom line, simply stated, is: it is illegal to pay compensation to NPO directors in Canada. A 2006 study of the voluntary sector of Canada includes statistics showing that when asked about revenue allocated to governance expenditures, 90% of respondents reported an allocation of between 0% and 2% of revenue. Less engaged boards had an even higher percentage who reported no allocation for governance expenditures for fees or expenses.

Compensating board members

Regarding for-profit businesses, consider the following guidelines when setting up your first board:

- Use the structure of a voluntary advisory committee as the first form of governance.
- Ensure you include qualified, independent people along with the key executive.
- As the business expands and requires a better form of oversight, shift to a formal board.
- Begin with a minimum of three, but preferably five, directors.
- If management or other insiders are included, balance their presence with the right mix of independents.
- Meet monthly to establish the rhythm of governance, shifting to quarterly meetings when the board and management are comfortable with their working relationships. Move family members to a family council that also meets regularly, reporting to the board.
- For board members who are non-management, set up a compensation policy along the lines of "equal pay for equal work." For example, if at the start, the president earns $80,000 per year, his or her daily pay over a 250-day year works out to $320.00. Assume that board members meet four times per year and are expected to spend one day getting prepared for each meeting, and one day off and on between meetings dealing with company business. These 12 days at $320.00/day works out to $3,840.00 or an annual stipend of $4,000.00.
- If the president earns a raise or a bonus, consider increasing the board members' compensation by the same relative amount.
- Consider granting stock to directors if the existing stock plan allows for it. Bear in mind that family companies may have a problem with this as it breaks down the family unit as a single owner. But if the right friends are willing to help the owner-operator, you may wish to include them in the proceeds of growth and financial success.

The matter of board compensation grows more complex as management becomes stockholders and grants or options are created. Regardless of the nature of the venture, boards should have a compensation committee made up of independent directors to review these matters and to make recommendations to the board.

XIII: Getting External Assistance with Board Issues

Many resources and countless articles deal with the topic of governance. We've listed several here. A few key NPOs in Canada are included, and it is recommended that owner-operators, key executives and board members research them and decide the merit in joining them or attending their periodic conferences or educational courses.

Canada Business
www.canadabusiness.ca

Canada Business acts as a single source of information for Canada's businesses and start-up entrepreneurs, including non-profits. This one-stop shop provides access to both federal and provincial resources on topics ranging from writing a business plan to finding new markets. In addition to the information it supplies via the Web, Canada Business services are available at service centres across Canada. In Ontario, the Ministry of Small Business and Consumer Services operates Small Business Enterprise Centres that offer consultant services and business-related seminars.

Charity Village
www.charityvillage.com

Charity Village is Canada's leading source of online information dedicated to the charitable and non-profit sector. News, jobs, how-to articles, volunteer and event listings, educational opportunities and more comprise more than 35,000 pages of content on their website. The site maintains up-to-date "quick guides" on topics such as donors and grantmakers, starting a non-profit, and charity fundraising. Free newsletters provide updates on the latest news and developments in the sector.

enp (enterprising non-profits)
www.enterprisingnonprofits.ca

enp is a partnership between foundations and other funders to develop social enterprises and help them gain visibility in the market. enp works to shape public policy and increase the availability of capital for social enterprises. In addition, the enp program provides assistance with business development, information resources and education to non-profit organizations. The Toronto enp grant program provides matching grants of up to $10,000 to social enterprises.

Imagine Canada
www.imaginecanada.ca
www.nonprofitscan.imaginecanada.ca

Imagine Canada provides tools, resources and networking opportunities to charities and non-profits with the overall goal of building an effective and sustainable non-profit sector. The organization produces research reports on trends, issues and opportunities relevant to Canada's non-profits. Imagine Canada also maintains the Canadian Nonprofit Library Network (CNLN), Canada's largest collection of charitable and non-profit sector resources. They offer 80% of their holdings freely online.

Institute of Corporate Directors
www.icd.ca

The Institute of Corporate Directors (ICD) is a non-profit professional association for Canadian directors and boards in both the private and public sectors. ICD provides professional development opportunities and continuing education events for directors including the Governance Essentials Program for Directors of Not-for-Profit Organizations. ICD offers board placement services and networking opportunities as well as information resources on governance.

Volunteer Lawyers Service
www.volunteerlawyers.org

Volunteer Lawyers Services (VLS) is a project of Pro Bono Law Ontario that offers free legal services to Ontario charities and non-profit organizations. VLS matches organizations with volunteer lawyers to help with legal business processes such as incorporation, board governance, and contracts. Additionally, VLS provides educational seminars and information online on topics relevant to non-profit organizations. Legal questions may be answered via their Online Hotline.

XIV: Good News! Bad News!

First—the bad news!

Directors' liability
Directors are fully responsible for the venture they direct; thus, they are liable for its actions, good and bad. The liabilities of directors are covered in the Canada Corporations Act and in the Ontario Corporations Act. (Outside Ontario, other provinces have similar laws.) Director liabilities are also dealt with in the Income Tax Act, the Employment Insurance Act, pension legislation, occupational health and safety regulations, and environmental protection legislation. It should be accepted that directors of non-profit organizations are as liable as directors of for-profit organizations. Directors must satisfy themselves that they are properly protected.

Directors' liability is a complex subject, beyond the scope of this guide for start-up governance. To repeat the fundamental law of governance: while authority may be delegated, responsibility may not. For-profit and NPO boards are responsible for the conduct of the organization they govern. Thus there is a need for directors and officers to have contractual indemnification agreements with their organizations and the appropriate insurance coverage in place.

Scalability
While this guide appears to be a step-by-step road to size and success, history shows that very few entrepreneurs adapt their start-up skills to their growing business needs. Their business remains small, known in economics as a "SME"—a small-to-medium enterprise. In the Harvard Business Review, the article "Why Entrepreneurs Don't Scale" suggests there are four reasons:

1. Entrepreneurs remain loyal to the small band of colleagues that helped them get started, unable to raise their sights or reach higher goals.
2. They stay tied to their start-up tasks, failing to delegate authority and grow the team.
3. They are stuck with tunnel vision (remaining task-oriented instead of goal-oriented), failing to see the big picture.
4. They fail to listen to others who can bring their experience and talent. Fundamentally, they fail to create a governance structure that opens their minds and extends their horizons.

Now—the good news!

Governing is both a privilege and a responsibility. The commitment is not to be taken lightly. Its priorities can be demanding. Yet, individuals can join together to help entrepreneurs to get started easier, grow faster and create more wealth or community benefit than what could be possible if any of them acted on their own. Here are ten stepping stones to greatness:

1. Get started.
2. Incorporate—become aware of compliance regulations and other industry requirements.
3. Attract the right advisors.
4. Create a management team.
5. Form a board of directors of three to five members.
6. Create the business plan and set out the goals
7. Embed the directors' duties and responsibilities in the bylaws.
8. As the organization grows in complexity, add specialists to the board.
9. Use your board for strategizing, scaling, prospecting and prospering.
10. Enjoy the growth and success. Good luck!

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