

The logo for SC&H Group is centered in the upper half of the slide. It consists of a dark blue square containing the letters 'SC&H' in a white, serif font. Below this square is a lighter blue horizontal bar containing the word 'GROUP' in a white, sans-serif font. The background of the slide is a black and white photograph of a modern building's interior, showing concrete beams and a staircase.

SC&H

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EXPERTISE THAT WORKS

# Sound Governance Practices

Presented by: Joe Freiburger, Director, SC&H Group

The bottom portion of the slide features a black and white photograph of a modern building's interior. Two people are visible in the foreground, their figures blurred as if they are moving. The background shows a complex structure of concrete beams and glass panels, suggesting a large, open-plan space like a lobby or atrium.

## AGENDA

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- Basic definitions, roles and responsibilities of the Board
- Standard governance documents and operating structure
- What to watch out for
- COSO Framework Update and Tips

## DEFINITION

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- Practices used by the board and executive management with the goal of providing:
  - Strategic direction
  - Ensuring that objectives are achieved
  - Ascertaining that risks are managed properly
  - Verifying that the organization's resources are used responsibly

## PURPOSE OF THE BOARD

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- Assume responsibility for the organization's compliance with laws & regulations
- Set strategic objectives
- Create policies designed to guide the organization toward meeting objectives
- Serve as content experts
- Hire CEO and monitor progress
- Set its own governance process and assess performance

## PRINCIPLES FOR GOOD GOVERNANCE

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- 33 Principles for Sound Practice Organized Under Four Main Categories:
  - Legal Compliance and Public Disclosure (7)
  - Effective Governance (13)
  - Strong Financial Oversight (6)
  - Responsible Fundraising (7)

*Principles For Good Governance And Ethical Practice: A Guide For Charities And Foundations*, Published in 2007, panel on the nonprofit sector

## PRINCIPLES FOR GOOD GOVERNANCE

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- Must have a governing body that is responsible for reviewing and approving the organization's mission, strategic direction, annual budget & key financial transactions, compensation practices and policies, and fiscal and governance policies
- Should meet regularly
- Should establish its own size and structure and review it periodically. Generally the Board should have at least 5 members
- Should include members with a diverse background (ethnic, racial, gender) experience, organizational and business skills
- Should have a substantial majority (two-thirds) independent members
- Should hire, oversee and evaluate the CEO

## PRINCIPLES FOR GOOD GOVERNANCE

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- Should ensure that the positions of chief staff officer, board chair and board treasurer are held by separate individuals
- Should establish an effective, systematic process for educating board members to ensure they are aware of their legal and ethical responsibilities, are knowledgeable about the programs and activities of the organization and can carry out their oversight functions effectively
- Should evaluate the performance of the board members individually and as a group no less than every 3 years and there should be clear procedures for removing board members who are unable to fulfill their duties
- Should establish clear policies relative to the length of terms and consecutive terms a member may serve

## PRINCIPLES FOR GOOD GOVERNANCE

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- Should review and evaluate organizational and governing documents no less than every 5 years
- Should establish the mission and goals and review them no less than once every 5 years
- Should expect members to serve without compensation, other than reimbursement for expenses incurred as a part of their service



## 10 BASIC BOARD RESPONSIBILITIES

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1. Determining the organization's mission and purpose
2. Selecting the chief executive
3. Providing proper financial oversight
4. Ensuring adequate resources
5. Ensuring legal and ethical integrity and maintaining accountability
6. Ensuring effective organizational planning
7. Recruiting and orienting new board members and assessing the board's own performance
8. Enhancing the board's public standing
9. Determining, monitoring and strengthening the organization's programs and services
10. Supporting the chief executive and assessing his/her performance

## LEGAL OBLIGATIONS

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- **Duty of Care:** Requires directors to exercise the care, diligence and skill that an ordinary, prudent person would exhibit under similar circumstances, including:
  - Understanding substantive matters brought before the board
  - Attending meetings
  - Asking questions
  - Challenging assumptions
  - Following up on unresolved issues
  - Consulting with experts, if needed
  - Reading and understanding materials and reports given to the board

## LEGAL OBLIGATIONS (CONTINUED)

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- **Duty of Loyalty:** Requires the pursuit of the organization's best interest, and the avoidance of self dealing and conflicts of interest
  - Boards should have a formal conflict of interest policy
  - Duty of Loyalty also includes:
    - **Duty of Confidentiality:** Duty not speak about board matters to non-board members unless authorized
    - **Duty of Obedience:** Requires directors to act in accordance with the organization's charter, bylaws, and its mission

## GOVERNANCE DOCUMENTS

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- Charter: Typically filed with the secretary of state, may also be called “certificate of incorporation” or “articles of organization,” depending on your state’s nomenclature
- Bylaws: Outline the basic operating rules for the organization, including how the board is structured and governed
- Code of Conduct: Define what the organization expects of board members and the board as a whole, and what the board expects of the management team
- Mission Statement: Defines the organization’s purpose and directs its future
  - May be the most important of a nonprofit’s governing documents
- Corporate Governance Guidelines: Written guidelines for governance in one document, sets forth clear “rules of the road”

## BOARD STRUCTURE AND OPERATIONS

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- Typical standing committees of most Boards:
  - Executive Committee
  - Finance Committee
  - Nominating/Governance Committee
  - Development Committee
- Larger Boards and organizations may have additional committees, such as:
  - Audit Committee
  - Personnel Committee
  - Compensation Committee
  - Investment Committee

## PERSONAL COMMITMENT

Actions and Practices that are generally considered to represent excellence in board service:

### General:

- Understanding the mission
- Being familiar with basic governance documents
- Staying current on governance trends
- Staying current on business and societal issues
- Knowing key staff and their roles
- Meeting with executive director periodically
- Getting to know other board members
- **Attending board and committee meetings regularly**

### Board Meeting:

- **Reading materials in advance of meetings**
- Actively contributing
- Asking questions
- Offering suggestions
- Avoiding nit-picking or micro-managing
- **Being respectful of the management team and other directors**
- Being collegial and refraining from dominating
- Supporting the chair to keep meetings moving
- Keeping questions and comments relevant

### Supporting the Non Profit:

- Supporting the organization financially
- Attending functions of the organization
- Helping raise funds from others for the organization
- **Being an advocate for the organization**
- Engaging others in the work of the organization
- Keep alert for warning signs of potential trouble
- Raising concerns to the appropriate level
- **Knowing when to rotate off the board**

## WHAT TO WATCH OUT FOR

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- The board does not have or abide by a regular meeting schedule
- Nothing much happens at board meetings, and many board members don't attend
- Directors don't understand the mission or business of the organization and are not passionate about it either
- Directors don't understand the financial issues of the organization
- Directors attempt to micromanage
- Few directors dominate meetings
- Lack of trust and confidence between the board and management
- Directors or management speak disrespectfully of others on the board or management team
- Directors or management speak publicly, without authorization, about confidential board members
- Directors don't understand basic governance principles
- The organization is floundering

Committee of Sponsoring Organizations of the Treadway Commission

Internal Control – Integrated Framework

May 2013



## HISTORY

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- Formed in 1985, a voluntary organization dedicated to improving the quality of financial reporting through business ethics, effective internal controls and governance
- Started in response to unethical business practices in the 70's and 80's
- Framework developed in 1992
- Most prevalent framework used by organizations to evaluate their internal control structure

## WHY THE CHANGE?

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- Changes in the business and operating environment over the past several decades led to a change because of:
  - Expectations of governance oversight
  - Globalization of operations
  - Greater complexity in business
  - Demands and complexity in laws
  - Expectations in competencies and accountability
  - Use and reliance upon technology
  - Expectation related to preventing and detecting fraud

## THE FIVE COMPONENTS

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1. Control Environment
2. Risk Assessment
3. Control Activities
4. Information & Communication
5. Monitoring Activities

## CONTROL ENVIRONMENT

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- Demonstrates commitment to integrity and ethical values
- Exercises oversight responsibility
- Establishes structure, authority, and responsibility
- Demonstrates commitment to competence
- Enforces accountability

## WHAT CHANGED

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- Codifies the 17 principles that support the 5 components
- Clarifies the role of objective setting as a precursor to internal control
- Reflects increased relevance of technology
- Includes an enhanced discussion of governance concepts (role of Board and committees)
- Expands the objectives to include non-financial as well as financial controls
- Enhances the consideration of anti-fraud expectations
- Increases the focus on non-financial reporting objectives
- Additional examples for operations and compliance

## WHY THE NEW COSO FRAMEWORK MATTERS TO NONPROFITS

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1. OMB Circular A-133, which applies to many nonprofits receiving Federal grants, requires the use of the framework to evaluate internal controls
2. Core concepts remain unchanged
3. Codification of underlying Principles
4. Increased role of reporting objectives - non-financial reporting and both internal and external reporting are included
5. More relevant context to today's environment
6. Original framework terminates at the end of 2014

# INTERNAL CONTROLS FOR NONPROFITS

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Why are they important?

1. Internal Controls reduce fraud risk
2. Internal Controls protect funding and nonprofit status
3. Internal Controls can streamline your audit process
4. Internal Controls instill confidence and sets the right tone

# INTERNAL CONTROLS FOR NONPROFITS

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## TOP FIVE AREAS OF RISK

1. No clearly defined policies especially accounting policies
2. Non compliance with SOX requirements
  - Whistleblower
  - Document destruction and retention
3. Weak organization controls
  - Conflicts of Interest and Code of Conduct
  - Delegation of Authority



# INTERNAL CONTROLS FOR NONPROFITS

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## TOP FIVE AREAS OF RISK

### 4. Insufficient Information Technology controls

- Access controls
- System and data security
- Use of spreadsheets

### 5. Weak accounting controls

- Segregation of duties
- Cash management
- Payroll

## WHAT DOES THIS MEAN FOR MANAGEMENT & THE BOARD?

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- A means to apply internal control within any type of entity regardless of the industry
- A principles-based approach that provides flexibility in designing and implementing internal controls
- Requirements for an effective system of control and consideration of how all components operate together
- A means to identify and analyze risk, allowing for a means to respond to risk

## WHAT DOES THIS MEAN FOR OUTSIDE STAKEHOLDERS?

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- Greater confidence in the Board of Directors oversight
- Greater confidence in the organization's ability to achieve its objectives
- Greater confidence in the organization's ability to identify, analyze and respond to risk
- Greater understanding of the requirements for an effective control system
- Greater understanding that management will be able to eliminate ineffective, redundant or inefficient controls

## REFERENCES

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- [www.independentsector.org](http://www.independentsector.org)
- [www.boardsource.org](http://www.boardsource.org)
- [www.COSO.org](http://www.COSO.org)
- *The Best Of Boards: Sound Governance And Leadership For Nonprofit Organizations*, By Marci Thomas and Kim Strom-Gottfried, AICPA

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# Questions?



## CONTACT INFORMATION

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Thank you for the opportunity to introduce SC&H Group.  
Please feel free to contact us with any questions.

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