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Nonprofit Insights

A Newsletter for Nonprofit Decision Makers Summer 2015

Executive Sessions

What They Are and Why You Should Have Them

A private conversation among board members seems to fly in the face of the openness and transparency expected of today's nonprofits. Managed appropriately, however, executive sessions are a vital part of the board process.

An executive session is essentially a meeting-within-a-meeting — a special closed session of the board in which more candid, confidential conversations can take place. It may take place before, in the middle or at the end of a regular board meeting.

Boardsource (formerly the National Center for Nonprofit Boards) notes that, by definition, an executive session is exclusive to board members. Others, such as the chief executive and/or select senior staff members, may be invited to join for part or all of the session. Outside advisors (e.g., lawyers, auditors, consultants) may also be invited to issue findings or provide professional guidance.

It's important to note that an executive session is different from a meeting of an "executive committee." Usually composed of the chief executive, officers and committee chairs, an executive committee typically meets only in emergencies, although some meet more regularly and are charged with handling business between regular board meetings. When an executive committee meets, it is not called an executive session.

Strengthening Governance and Leadership

Properly called and conducted, executive sessions serve three core functions:

1. They assure confidentiality. Some organizational matters legitimately require confidentiality. For example, certain discussions with legal counsel are subject to attorney-client privilege. Likewise, the board and executive director may wish to hold a discussion of strategic business decisions privately — before sharing details with the organization's various stakeholders.

2. They foster board independence and oversight. Executive sessions encourage nonprofit boards to "think for themselves" in such critical areas as determining executive compensation, evaluating senior staff performance and accepting the organization's fiscal audit.

3. They enhance relationships among board members and with the chief executive. Executive sessions provide an opportunity for peer-to-peer discussion of issues and concerns between the executive and board without staff present. This helps foster a more constructive partnership between the board and chief executive.

Playing by the Rules

If not handled properly, an executive session can create the notion that "something is wrong" or that the board is somehow going behind the back of the chief executive. The key is to establish formal procedures for calling an

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Funding Matters

The Importance of Revenue Diversification

Nonprofits learned a critical lesson about the importance of revenue diversification during the global recession. Organizations that were dependent on just one or two funding sources found themselves fighting for their very survival. The lesson is age-old: Don't put all of your funding eggs in one basket.

Ultimately, a diversified revenue stream mitigates the risk of losing any single source of money. When government funding dries up, for instance, you can turn to foundation grants. Or when corporate donations dwindle, you can replace them with individual donations. Healthy nonprofits diversify revenue by tapping a variety of resource streams, including:

- Government agencies,
- Large national foundations,
- Family foundations,
- Corporations,
- Individual donors, and
- Earned income.

That said, over-diversifying revenue sources can create its own set of problems. Seeking out, acquiring and managing multiple diverse revenue streams requires specific skills, staff and management capacity.

Finding the Right Balance

When it comes to funding sources, there really is no golden egg. Each revenue stream comes with its own idiosyncrasies. Yet, even if your organization does rely on a single source for the bulk of its funding, it's important to not rely on a single payer.

So, for example, if you receive 90 percent of your funding from state government contracts, you can minimize that risk by tapping a number of government departments in a number of states.

Your goal should be to establish a base of funding that's reliable, flexible and varied. Consider these best practices that can help your organization diversify its funding:

Conduct a funding review. Start by establishing a baseline with a review of your organization's funding sources. Such a review should include:

- Your current funding mix,
- Restrictions or conditions placed on each funding source,
- Longevity and predictability of each funding source,
- Current funding gaps, and
- Potential future gaps.

Establish benchmarks. Likewise, a benchmarking study can show how your revenue mix stacks up against various peer groups — and identify any dangers. Note that as part of your organization's audit process, your CPA will evaluate your revenue sources and identify any areas where you may be too dependent on a single source.

Find funding sources aligned with your mission. Funders' interests often fall into distinct categories. The key is to find these natural matches between your organization and particular funding sources. For example, corporations tend to support hunger and health issues while individuals tend to give to issues that cross socio-economic boundaries, like environmental advocacy. Ultimately, they all give to organizations that have clear, compelling and simple messages.

Develop alternative funding sources. Consider developing revenue streams that are not dependent

on the vagaries of state and federal funding or the whims of donors. For example, income from food and beverage sales, program ads and gift shop sales can add to your organization's bottom line. Just note that this "earned income," if not properly managed, can trigger tax and compliance issues.

The problem occurs when the earned income comes from a source that is not substantially related to your organization's tax-exempt purpose. The IRS calls this Unrelated Business Taxable Income (UBTI). To be clear, there is nothing wrong with a tax-exempt organization earning UBTI. Just be aware that gross proceeds of greater than $1,000 will require filing Form 990-T.

However, depending on the consistent and proper allocation of expenses, your organization may or may not owe income taxes. Note also that federal law generally limits UBTI to 30 percent of total organizational income in order to maintain tax-exempt status.

Get Your Board Onboard

Revenue diversification requires a long-term strategy that includes planning, ongoing cultivation and plenty of patience. Make sure your board and leadership understand the importance of revenue diversification – and embrace the need to seek out new sources and combinations of funding.

Executive Sessions

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executive session, clearly communicate the intent of such a session, and then appropriately document it.

Following these simple steps can help diffuse the perception that executive sessions are convened only in times of crisis or to deal with matters involving the chief executive:

Establish policy. Typically, the board chair has the authority to call an executive session — either on an ad hoc basis or planned by the chair and chief executive in advance and listed on the agenda. Some boards require that a majority or super majority confirm the decision if an executive session is requested by a board member other than the chair.

Consider establishing a board policy that articulates the process for calling and conducting an executive session. This includes identifying issues that are acceptable for closed meetings, such as:

- On the advice of counsel.
- To discuss current pending legal matters.
- To consult with the auditors and compensation consultants.
- To acquire or dispose of property.
- To discuss or act on personnel issues.
- To address such other matters as the board deems appropriate.

Utilize appropriately. The majority of board business should be conducted in a traditional board meeting. Executive sessions should be reserved for cases where frank, open discussion is needed. Wherever appropriate, the board should officially return to an open meeting for a formal vote — especially for critical decisions such as determining executive compensation or settling contract disputes.

Document accordingly. The fact that an executive session was held should be clearly documented in the regular board meeting minutes — including when the board went into executive session, the primary purpose of the session and any formal decisions that were made.

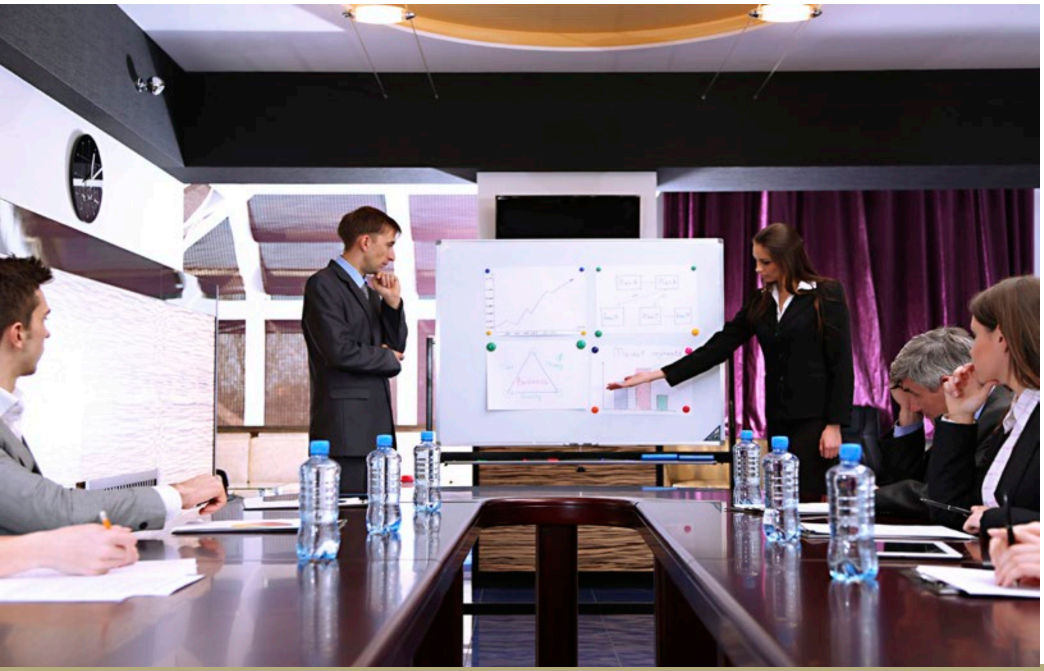
Detailed minutes may not be necessary if the executive session resulted in only an informal discussion, but the general substance of the executive session should be noted in the board minutes. If the session contributed to a formal board decision, it may be necessary to provide further documentation in the minutes. If the chief executive was not present, the board chair should promptly summarize the gist of the session for the executive.

Ensure confidentiality. Participants in an executive session should be made aware of what parts of the discussion should remain confidential. Also, access to executive session materials or minutes should be limited to those persons who participated in the executive session, as permitted by law. Of course, if your nonprofit is subject to open meeting or sunshine laws, make sure that executive sessions are in full compliance.

Consider making them a regular agenda item. Some nonprofits make executive sessions a regular part of their board meetings. The board meets privately for a time with the chief executive and then conducts a debriefing without the executive. This helps bring conversations that would otherwise happen in the parking lot into a collective forum.

Executive sessions are a valuable tool that can create an environment for important conversations among board members — sometimes alone and sometimes with the chief executive.

Questions? Our accounting professionals have plenty of real-world experience with nonprofits just like yours.



Meeting With the Auditor

Nonprofit boards have a fiduciary responsibility for ensuring an audit of the organization's finances. Therefore, the board (typically through a specifically delegated audit committee) should select and engage the auditor. The auditor should then report directly to the board, which should review and accept the financial audit.

At some point in the board's review of the financial audit, the board should meet in an executive session with the auditors without any staff present. This allows the board to receive unfiltered feedback and provide unhindered financial oversight of the organization's financial health and practices.

How to Perform Cloud Computing Due Diligence

Cloud computing makes sense for nonprofits on a variety of levels. While some have dipped a toe in the cloud computing waters with non-critical applications such as online publishing or project management, many nonprofits have not tapped the cloud's full potential.

To be sure, migrating critical applications such as accounting and financial management to the cloud can feel like a technological leap of faith. But with the proper due diligence, there's no reason your organization can't benefit from the increased productivity, security and cost savings of remotely hosted data.

TechSoup, a 501(c)(3) nonprofit that helps other nonprofits make informed decisions about technology, offers some sound guidance for evaluating cloud providers, including these key steps:

Verify performance. A reliable provider will offer real-time information on its performance levels. Look for guaranteed performance of 99.8 percent or better. Ditto for rapid response to issues.

Verify backup. Best are continuous local backups plus streaming backups to a remote disaster recovery center.

Verify compliance. Review a cloud provider's audit or certification of security, backups and maintenance practices — commonly referred to as a SSAE 16 "SOC 1" Type II audit. If you need to be HIPAA or PCI DSS compliant (you handle credit card information for processing donations or payments), make sure that your service provider is properly certified.

Verify ownership. Make sure that you still own your information and can get your data back out of the cloud when you need it.

Transition incrementally. Focus on your processes and workflows, then try a cloud tool that can help address a currently ineffective or challenging process. Select the tools that will help you do your work better.

Plan for divorce. Pay close attention to the terms of your agreements with cloud providers. This is especially true when it comes to termination clauses and the process by which the data will be returned to or retrieved by your business upon termination of the contract.