A close-up photograph of a person's hand, palm facing up, with a thick red rope draped across it. The rope is looped and crossed, creating a grid-like pattern. The hand is wearing a light blue, long-sleeved shirt cuff. The background is plain white.

■ Leadership

Called to serve

By Keith Cerny and Vernon Ellis

As the nonprofit sector grows and organizations become increasingly complex, more and more executives are being invited to lend their skills as board members. Here are eight principles for effective governance that can help a broad range of nonprofit groups be more successful.



Quietly, with little fanfare, the nonprofit sector has ballooned into a major force. Indeed, if nonprofits—a broad category that includes a range of civic, social, cultural, health and other groups outside of government and business—were combined into a separate economy, they would be the world's eighth largest, slightly smaller than the United Kingdom's and Italy's but larger than Brazil's and Russia's.

The expenditures of nonprofits in 22 nations totaled \$1.1 trillion in 1995, the most recent year for which complete statistics are available. Nonprofits employed 19 million people in those 22 nations, more than were employed in the utilities industry and almost as many as worked in transportation. An average of 28 percent of the population in those countries volunteer some of their time and effort to nonprofits.

As the nonprofit phenomenon has grown, the larger groups have become increasingly complex to govern. Some of the biggest in the United States—such as the National Council of YMCAs of the USA, with 2000 income of nearly \$4 billion, and The Salvation Army, with \$2.8 billion in 2000 income—would rank somewhere in the middle of the Fortune 1000 if they were for-profit corporations. Their boards of directors can be huge compared with those of for-profits, sometimes numbering 100 members or more. Many, if not most, of the board members are wealthy and influential and have strong, sometimes divergent points of view.

At the same time, operating standards for nonprofits have become more demanding. As nonprofits compete to attract funds, their

techniques in reaching out to donors have become increasingly professional. They need to assure potential donors that their gifts will be used effectively.

Today a new type of giving, called venture philanthropy, is putting pressure on nonprofits to deliver results. Traditional donors contribute money to, say, an after-school literacy program for disadvantaged children, and might settle for a plaque on the wall in return. Venture philanthropists, however, expect results. For example, if students' test scores rise by 5 percent following a donation to a particular school, next year's gift might be increased by 5 percent. Conversely, if test scores don't improve, the school should not expect the venture philanthropist to contribute again. These kinds of demands, in turn, require new thinking about how to measure performance.

Multiple goals

Among the consequences of this upsurge in nonprofit activity and the increasing challenge of running these organizations is that more and more business executives are being invited to lend their skills and become members of nonprofit boards.

Perhaps you have been asked to serve—or are already serving—on the board of a large sports organization in France, a theater company in the United Kingdom or an organization to promote literacy in the United States. You understand that your position may involve making a substantial financial contribution to the organization and will require some of your time. But what else should you know about your responsibilities? What constitutes a well-run nonprofit board?

For a start, put aside many of the preconceptions you bring from

your experience serving on or working with the boards of for-profit public corporations, where there are clear financial objectives. The boards of nonprofits have to serve multiple constituencies and pursue multiple goals.

What follows are eight principles for nonprofit board management that apply to a broad range of organizations, from a renowned opera company to a local hospital, from an animal welfare center to the regional chapter of the American Red Cross. Not all eight rules apply with equal weight to all nonprofit boards. Organizations that depend heavily on public funding, for example, tend to have fewer board members because there is no need to reserve seats for a multitude of generous donors. However, those that receive public money clearly have to be more attuned to public—and political—opinion.

Define the organization's strategy and the board's role

For-profit corporations have a limited number of goals, and success in reaching them can generally be measured by such numbers as earnings growth and return on investment. The for-profit board's role is fairly clear-cut. It appoints the CEO, defines incentives and compensation, monitors the company's performance—intervening where appropriate—and approves major initiatives, such as acquisitions and large capital projects. Beyond that, its role diminishes.

A nonprofit has more complex goals and often many more stakeholders to please. A theater company, for example, wants to mount productions that draw large audiences, but also ones that please critics, donors and the current (as well as the next) generation of talent in the company. More-

over, it may be eager to promote new works, enhance its standing in the local artistic community relative to the symphony and the museum, and reach out to schoolchildren. Finally, it may have to keep the peace with several trade unions.


With so many stakeholders and competing goals, the nonprofit's mission is often very fuzzy. Clarifying the basic purpose of the organization is one of the board's major tasks. While the institution can and should continue to serve its many constituencies, their often different needs should be identified and prioritized by the board. In addition to setting the purpose and direction, the board must determine the supporting values for the organization.

The members of a nonprofit board often get more deeply and personally involved in the organization's finances. When the board of a for-profit corporation reviews management's projections of revenues for the next three to five years, it basically kicks the tires to see if the assumptions are sound. But when the management of a nonprofit gives its board a revenue projection of, say, \$10 million, it may well be telling the board to go out and raise \$5 million.

Except for those that receive public funds, many nonprofits rely on private donations for around half of their revenues, and they expect their board members to be large donors as well as fundraisers. This is one reason that some nonprofit boards are enormous. A medium-sized American opera company can have 40 or more board members, for example, compared with an average of 14 for the top 100 companies on the Fortune 500 list.

Reliance on private donations used to be restricted to US nonprofits, but

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increasingly, their European counterparts are seeking private money as well. For example, historically the Orchestre de Paris has depended heavily on the national and municipal governments to supplement the revenues it gets from ticket sales. But these public sources, like governments everywhere, are being squeezed by growing demands and shrinking income.

Now the orchestra's board is reaching out to private donors, primarily companies. A few years ago private donors contributed only about 1 percent of the orchestra's budget. This year the board expects to raise 4 percent or 5 percent of the orchestra's \$13.5 million budget from private donors, and it hopes to double that percentage within a few years. Even in Germany, where there is a strong tradition of state support for the performing arts, it is likely that nonprofits will have to seek private funding. In the United Kingdom that movement is already well under way (see box, page 90).

Establish a rigorous financial plan and operational model

The world of the nonprofit has become more complex over time. Many nonprofits are now bigger and have various funding sources—public grants, regular fund-raising, capital drives, subscriptions, project and other event-related incomes, ticket sales—that can fluctuate significantly from year to year. They also have a complicated cost structure of fixed, semi-fixed and variable costs, as well as capital costs.

Yet the standard form of charity accounting has not changed. Nonprofit board members, especially those with for-profit experience, often find it difficult to understand the nature of the balancing act and

the vulnerabilities that nonprofits have to cope with. Finance personnel at nonprofits can simplify matters for the board by preparing statements showing these financial issues explicitly.

It is also important that the board understands the business and financial model of the organization. It needs to ensure that there is a rigorous financial plan in place that covers the medium term—perhaps three to five years—as well as an annual plan. Whatever vulnerabilities the organization faces should be clearly understood. And the board needs to carefully oversee how the organization is faring against its plan.

In addition, some nonprofit boards may find it necessary to adopt a tougher, more commercial attitude toward their institutions. A nonprofit children's theater should tolerate one or two box office failures in a season, perhaps, but not a dozen.

Give every board member a meaningful role

This may not be as easy as it sounds. Board membership per se does not necessarily guarantee an active role. Take opera boards, for example. Only about 25 percent of board members are directly involved with their organizations on a weekly or more frequent basis. Monthly involvement is more common; it's the norm at 40 percent of boards, according to a survey done last year by OPERA America, the service organization for professional opera in the United States and beyond. Board members will likely want to speak their minds from time to time, however, especially if they have contributed chunks of their personal fortunes to the enterprise.

People join boards of public companies to network with their peers,

Balanced scorecard for a typical arts organization

While each institution will need to create its own set of metrics, this scorecard for a performing arts company can provide a useful starting point. The artistic and audience metrics are probably the ones that require the most tailoring.

Finance and operations	People	Audience and other stakeholders	Artistic
Operating expense relative to budget	Employee satisfaction (<i>salaried, hourly</i>)	Audience satisfaction (<i>e.g., measured through periodic surveys</i>)	Favorable press coverage (<i>local, national, international</i>)
Deficit as a percentage of revenue	Number of union issues identified and resolved	Status of education/ outreach projects (<i>red/yellow/green</i>)	Status of long-range artistic bookings (<i>red/yellow/green</i>)
Marketing relative to budget (<i>with breakouts—e.g., subscriptions, single tickets</i>)	Attrition rate	Status of key community projects (<i>e.g., improving diversity of attendance</i>)	Status of key artistic initiatives (<i>commissions, key hires, new technology deployment, new facilities</i>)
Development relative to budget (<i>with breakouts—e.g., individuals vs. corporate vs. foundations</i>)			
Status of special projects (<i>red/yellow/green</i>)			

to enhance their reputations and even, at times, for the income. They join nonprofit boards for a much greater variety of reasons. The founder of a software company may join the board of a museum because as a college student she was an aspiring sculptor. A retired banker joins the local board of the American Cancer Society because a loved one died of breast cancer.

The wise board leader has a clear understanding of why each member joined and finds a way to keep each engaged constructively, making the most effective use of their experience within the confines of their time constraints. At the same time, it's also important to prevent board

members with more time on their hands from roaming the institution, poking into operations at random.

That generally means assigning each to a committee with clearly defined and limited roles. General Motors has only six committees on its board, IBM just four. To make full use of its board members' talents, the board of a well-run nonprofit may have more than a dozen committees, ranging from those a corporate executive would recognize, such as nominating, compensation, audit and finance, to names that may be less familiar to the corporate ear, such as planned giving, special events, facilities and education.

Match the board to the mission

For-profit boards tend to be responsive to the changing world, more alert to what the market and shareholders expect and to what the competition is doing. They keep those considerations in mind when nominating new board members. Nonprofit boards tend to perpetuate themselves. Despite profound changes in the world a nonprofit serves, its board may look a lot like it did 10 years ago because these groups tend to add new board members according to how much they resemble current ones. The board leader should resist the inclination to "clone" the current board and should encourage nominations that represent new or potential stakeholders, including

The English National Opera redefines private giving

The English National Opera, founded in 1931 as the Vic-Wells Opera, produces an average of 18 operas a year. All of them are performed in English, regardless of their original language, a strategy designed to bring in a wide audience. So is the practice of keeping ticket prices low, many in the range of £5 to £15 (\$7 to \$21); 60 percent of the tickets cost less than £40.

But despite this pricing policy and the ENO's great popularity, box office receipts don't come close to supporting the company of 500 people. Moreover, the opera's board of directors faces a future of increasing financial challenges—as do the boards of many cultural institutions and other nonprofits around the world (see story). *Outlook* talked recently with ENO Chairman Martin Smith, who is the former chairman of Donaldson, Lufkin & Jenrette's European investment banking group.

***Outlook:* Americans take it for granted that if they are asked to serve on a nonprofit board, they will be asked for money.**

Smith: That's not the tradition in Europe, including the UK. People who join boards here are the great and the good, but even when they happen to be the wealthy as well, it has not been assumed that they would make a financial contribution. But many of us running nonprofit boards are now interested in emulating the US.

What has changed to make the American model attractive?

Look at our situation at the ENO, for example. We have revenues of £25 million a year. We get £15 million of government subsidy from The Arts Council of England. Another £8 million comes from ticket sales and other commercial activities. The final £2 million comes from private sponsorship. But we'll have to increase the private subsidy considerably, because the government subsidy for the arts is going to be crowded out by other demands. The UK has a transportation system that is creaking, an education system in trouble and a health system that seems to need reinvention.

How have your board members reacted to the request for money?

When I first brought up the idea on a different arts-related board seven years ago, I worried that some people on the board were going to have coronaries. Even some well-heeled



Smith: Adopting an American model

people say that as a matter of principle they don't think they should make a financial contribution. But I'm happy to say that now all 15 of our board members are giving.

Did you threaten to horsewhip them in Trafalgar Square?

I might have tried that if I thought it would work. But the matching-fund concept has been very effective. We need £41 million to restore our theater, the Coliseum. It's the largest in London and hasn't been touched since it was built in 1904. The National

Lottery will give us just over half, provided we can match that with private donations. About 40 percent of the private money will come from the board. We want to set an example, establish a precedent that will legitimize giving to nonprofits.

What other incentives are helpful?

People can't give money unless they have it. Until recently the UK tax system was much less favorable to charitable giving than that of the US. But now the system has been simplified. People can donate securities, avoid capital gains and deduct the contributions from their incomes.

Donors also get great satisfaction out of supporting the ENO because it is the largest employer of talent coming out of the nation's music schools and has a hugely successful education program, reaching some 12,000 young people every year.

Do you worry that donors will try to control the ENO's program?

No. Donor interference concerns me far less than that which comes with government subsidies. One of the great difficulties of government money is the combination of bureaucracy and social engineering, which tends to want a particular mix of people [to] come to the theater and perform in it.

For those who will be in London for the rest of 2002, which ENO productions are must-sees?

In the second half of 2002, whilst restoration work is being done at the Coliseum, the ENO will be performing three elements of Wagner's Ring cycle—*The Rhinegold*, *The Valkyrie* and *Siegfried*—at the Barbican Centre in London. Later in the year, the company will be putting on a new production of *Tosca*, under the celebrated director David McVicar.

those who can tap additional revenues and other resources.

Whenever it's possible and appropriate, the nonprofit board should enhance the organization's prestige by recruiting at the top. If it's important to have a fast-growing biotech company or an influential Hispanic media power represented on the board, make sure the CEO or COO fills the seat. A Los Angeles nonprofit could have a movie star on the board; a New York nonprofit could have a luminary from Wall Street.

A caveat: Celebrities must be willing to work as well as lend their names. Indeed, all new board members should have lengthy discussions with the chair and the president, in which the leaders lay out their expectations. The organization bylaws should stipulate that everyone, including the board's leaders, serve specified terms, which may or may not be renewed. That helps elderly or less committed board members retire gracefully without losing face.

Another type of board member who can be helpful is someone who is or has been a beneficiary of the services. At a university, this would mean an alum would serve; at a rehab center, a former patient could be invited to join the board.

Reach out to all of the stakeholders

Many boards focus their attention narrowly on the immediate beneficiaries of their services, whether they are symphony audiences or endangered animals. For a number of reasons, it's essential for the board to broaden its vision and cultivate relationships with all the groups likely to feel the organization's impact. One organization that does this well operates a yearly arts festival that brings thousands of visitors to a medium-sized city in the United

States. The influx clogs streets with traffic and otherwise burdens municipal services. True, the tourists spend money, but that mostly benefits white businessmen, not the African-Americans who are a substantial part of the local population. Moreover, the audiences at the festival are 98 percent white. So the board leaders stay in year-round contact with the African-American community and its leaders, trying to broaden community involvement in the festival while encouraging participation.

A local social agency that is raising money for the hungry and diseased in faraway lands should reach out to international organizations like Oxfam and Médecin sans Frontières to find out how the local program can complement what the major players are doing.

Forging relationships with other nonprofits, however, should be done carefully. A symphony orchestra might profitably exchange subscriber lists with the local museum; both might gain more attendees. But if the symphony were to swap lists with the opera, it might inadvertently encourage its fans to spend their music money elsewhere. That's not to say competing organizations should not try to work together. Some of the most successful groups will be those that find ways to collaborate. For instance, the symphony and opera could work together to try to increase interest in classical music in general.

Treat the CEO like a CEO

The nonprofit's CEO (or executive director, or whatever his or her title might be) generally has an ex-officio place on the board but is almost never the chair. But even if the nonprofit CEO did not graduate from the London School of Economics and Political Science, INSEAD or

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Harvard Business School, he or she should be treated with respect. Too often board members dismissively refer to the CEO and others in top management as “the staff.” Says the executive director of one artistic company, “Some of the board members look at me as though I ought to be coming in through the service entrance.”

Realize instead that the top managers are professionals, and treat them accordingly. The board appoints the CEO, approves a strategic direction, and works closely with top management on finance and overall operations. But in other matters, such as negotiating a union contract, the board should get out of the CEO’s way.

The board’s style of interacting with management can range from very formal—business is transacted in the boardroom only; all other meetings are social—to very informal, in which the organization’s affairs are settled over coffee in the cafeteria. But the board leader has to make it clear to all where and when serious business will be conducted. Otherwise, an individual board member might get the CEO off in a corner and, claiming to represent the entire board, try to cancel a scheduled event or add a new program. One board member had to be removed from the executive committee of a large nonprofit because he contacted the CEO on his own and berated him for his judgment over proposed spending in the five-year plan.

Perhaps the touchiest management issue that the board, and especially the leader, has to cope with is having, in effect, two CEOs. This is a more common occurrence at nonprofits, and especially at cultural institutions, than at for-profits. Both the artistic director and the business

manager may think of themselves as the final authority, unwilling to defer to the other on crucial questions. If the board leader doesn’t have the time to resolve every jurisdictional dispute, he or she will have to make it clear to both that one or the other is the first among equals.

Control contacts with the professionals
In general, no board member other than the chair and president should have a working relationship with anyone on the organization’s payroll other than the CEO, the CFO, and perhaps one or two others. The exception to this rule is when a board committee is specifically asked by the chair and the CEO to work with the professionals on undertakings like fund-raising or recruiting a star talent. Allowing board members free access to the professionals would dangerously disrupt the chain of command.

That same principle applies to public companies, of course. But board members of for-profits take that restriction for granted. Board members of nonprofits sometimes push the limit, presumably because they believe that since they gave or raised the money, they have the right to decide how it is spent.

A rogue board member rooting into the budget can be disastrous. The members of a nonprofit board may all be wealthy and generous, but otherwise their values and tastes are apt to be as varied as any other slice of the population.

Consider what might happen if a rogue member burrowed into the daily financial operations of a rehabilitation center for alcoholics. Maybe most of the board members believe that a balanced program of treatment and discipline is the right mix, but the rogue is convinced

that the only way to help the clients is through tough love and that medication and psychiatry are a waste. So he picks apart the medication budget and harasses the psychiatric staff. The result will be a demoralized and ultimately ineffective organization.

Bring in measurement systems

Increasingly, both public and private donors are demanding that nonprofits produce numbers to demonstrate their value to the community. In part, that's a side effect of the proliferation of nonprofits, which has given donors many more nonprofits to choose among. In the United States, donors and others can go to a website called GuideStar.com, which lists more than 850,000 nonprofits, details flows of funds and quantifies their performances by such measures as overhead as a percentage of disbursements.

Some nonprofits drag their heels on metrics, for understandable if not justifiable reasons. A public corporation can easily measure its progress with such figures as growth in earnings per share from year to year. But how does a nonprofit, which generally has much broader and less quantifiable goals, evaluate itself? What numbers does an opera company marshal to show that its artistic quality is on an upward curve? How does a drug rehabilitation center demonstrate that its clients are being successfully reintegrated into the community?

Those numbers are not easy to come by, but not impossible either. A rehab center can follow up on those it has discharged and count how many have jobs and a permanent place to live a year later. An opera company can keep track of its media coverage. (The measurements don't have to be strictly quantitative; qualitative measurements mat-

ter too.) It can also track things like sales of CDs by the company's repertory performers. A balanced scorecard approach (see page 89) would work for most organizations and would include four elements: mission-oriented metrics, financial and operational metrics, people metrics and stakeholder metrics.

So it's appropriate for the board to insist on performance metrics, including metrics that reveal whether the objectives of the other principles listed above are being met. If the goal of a museum in Germany is to reach out to a part of the community that has never seen a work of art up close, it can keep a tally of how many schools it has contacted and how many tours it has conducted for children. What do teachers have to say about the experience? Parents? How could the visit have been improved?

Happily, despite the current worldwide economic downturn, people have not turned inward. Volunteering is holding steady, perhaps even increasing. And nothing contributes to volunteerism's productivity, effectiveness and all-around usefulness like well-run nonprofit boards. ■

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