

# PRINCIPLES

## FOR GOOD GOVERNANCE AND ETHICAL PRACTICE



Independent Sector's *Principles for Good Governance and Ethical Practice* is the foremost guide for sound and successful practice by charities and foundations in the U.S., providing clarity about legal compliance and public disclosure, effective governance, strong financial oversight, and responsible fundraising. The 2015 edition provides considerable new value, reflecting changes in law as well as new circumstances in which the charitable sector functions, and new relationships within and between sectors. The following 33 Principles reflect the scope of the guide, while rationales and actionable steps for implementation can be found in the full guide, available at [PrinciplesForGood.com](http://PrinciplesForGood.com).

### LEGAL COMPLIANCE AND PUBLIC DISCLOSURE

1. A charitable organization must comply with all applicable federal laws and regulations, as well as applicable laws and regulations of the states and the local jurisdictions in which it is formed or operates. If the organization conducts programs outside the United States, it must also abide by applicable international laws, regulations and conventions.
2. A charitable organization should formally adopt a written code of ethics with which all of its directors or trustees, staff, and volunteers are familiar and to which they adhere.
3. A charitable organization should adopt and implement policies and procedures to ensure that all conflicts of interest (real and potential), or the appearance thereof, within the organization and the governing board are appropriately managed through disclosure, recusal, or other means.
4. A charitable organization should establish and implement policies and procedures that enable individuals to come forward with information on illegal practices or violations of organizational policies. This "whistleblower" policy should specify that the organization will not retaliate against, and will seek to protect the confidentiality of, individuals who make good-faith reports.
5. A charitable organization should establish and implement policies and procedures to protect and preserve the organization's important data, documents, and business records.
6. A charitable organization's board should ensure that the organization has adequate plans to protect its assets — its property, documents and data, financial and human resources, programmatic content and material, and its integrity and reputation — against damage or loss. The board should review regularly the organization's need for general liability and directors' and officers' liability insurance, as well as take other actions necessary to mitigate risks.
7. A charitable organization should make information about its operations, including its governance, finances, programs, and activities, widely available to the public. Charitable organizations also should consider making information available on the methods they use to evaluate the outcomes of their work and sharing the results of those evaluations.

### EFFECTIVE GOVERNANCE

8. A charitable organization must have a governing body that is responsible for reviewing and approving the organization's mission and strategic direction, annual budget and key financial transactions, compensation practices and policies, and fiscal and governance policies.
9. The board of a charitable organization should meet regularly enough to conduct its business and fulfill its duties.
10. The board of a charitable organization should establish its own size and structure and review these periodically. The board should have enough members to allow for full deliberation and diversity of thinking on governance and other organizational matters. Except for very small organizations, this generally means that the board should have at least five members.
11. The board of a charitable organization should include members with the diverse background (including, but not limited to, ethnicity, race, and gender perspectives), experience, and organizational and financial skills necessary to advance the organization's mission.
12. A substantial majority of the board of a public charity, usually meaning at least two-thirds of its members, should be independent. Independent members should not: (1) be compensated by the organization as employees or independent contractors; (2) have their compensation determined by individuals who are compensated by the organization; (3) receive, directly or indirectly, material financial benefits from the organization except as a member of the charitable class served by the organization; or (4) be related to anyone described above (as a spouse, sibling, parent or child), or reside with any person so described.
13. The board should hire, oversee, and annually evaluate the performance of the chief executive officer of the organization. It should conduct such an evaluation prior to any change in that officer's compensation, unless there is a multi-year contract in force or the change consists solely of routine adjustments for inflation or cost of living.
14. The board of a charitable organization that has paid staff should ensure that the positions of chief staff officer, board chair, and board treasurer are held by separate individuals. Organizations without paid staff should ensure that the positions of board chair and treasurer are held by separate individuals.

15. The board should establish an effective, systematic process for educating and communicating with 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.

16. Board members should evaluate their performance as a group and as individuals no less frequently than every three years, and should have clear procedures for removing board members who are unable to fulfill their responsibilities.

17. Governing boards should establish clear policies and procedures setting the length of terms and the number of consecutive terms a board member may serve.

18. The board should review organizational and governing instruments no less frequently than every five years.

19. The board should establish and review regularly the organization's mission and goals and should evaluate, no less frequently than every five years, the organization's programs, goals and activities to be sure they advance its mission and make prudent use of its resources.

20. Board members are generally expected to serve without compensation, other than reimbursement for expenses incurred to fulfill their board-related duties. A charitable organization that provides compensation to its board members should use appropriate comparability data to determine the amount to be paid, document the decision, and provide full disclosure to anyone, upon request, of the amount and rationale for the compensation.

## STRONG FINANCIAL OVERSIGHT

21. A charitable organization must keep complete, current, and accurate financial records and ensure strong financial controls are in place. Its board should receive and review timely reports of the organization's financial activities and should have a qualified, independent financial expert audit or review these statements annually in a manner appropriate to the organization's size and scale of operations.

22. The board of a charitable organization must institute policies and procedures to ensure that the organization (and, if applicable, its subsidiaries) manages and invests its funds responsibly, in accordance with all legal requirements. The full board should review and approve the organization's annual budget and should monitor actual performance against the budget.

23. A charitable organization should not provide loans (or the equivalent, such as loan guarantees, purchasing or transferring ownership of a residence or office, or relieving a debt or lease obligation) to directors, officers, or trustees.

24. A charitable organization should spend a significant amount of its annual budget on programs that pursue its mission while ensuring that the organization has sufficient administrative and fundraising capacity to deliver those programs responsibly and effectively.

25. A charitable organization should establish clear, written policies for paying or reimbursing expenses incurred by anyone conducting business or traveling on behalf of the organization, including the types of expenses that can be paid for or reimbursed and the documentation required. Such policies should require that travel on behalf of the organization is to be undertaken cost-effectively.

26. A charitable organization should neither pay for nor reimburse travel expenditures for spouses, dependents or others who are accompanying someone conducting business for the organization unless they, too, are conducting such business.

## RESPONSIBLE FUNDRAISING

27. Solicitation materials and other communications addressed to donors and the public must clearly identify the organization and be accurate and truthful.

28. Contributions must be used for purposes consistent with the donor's intent, whether as described in the relevant solicitation materials or as specifically directed by the donor.

29. A charitable organization must provide donors with specific acknowledgments of charitable contributions, in accordance with IRS requirements, as well as information to facilitate the donors' compliance with tax law requirements.

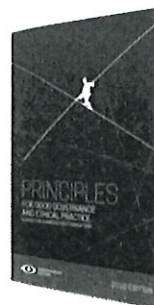
30. A charitable organization should adopt clear policies, based on its specific exempt purpose, to determine whether accepting a gift would compromise its ethics, financial circumstances, program focus, or other interests.

31. A charitable organization should provide appropriate training and supervision of the people soliciting funds on its behalf to ensure that they understand their responsibilities and applicable federal, state, and local laws, and do not employ techniques that are coercive, intimidating, or intended to harass potential donors.

32. A charitable organization should not compensate internal or external fundraisers based on a commission or a percentage of the amount raised.

33. A charitable organization should respect the privacy of individual donors and, except where disclosure is required by law, should not sell or otherwise make available the names and contact information of its donors without providing them an opportunity at least once a year to opt out of the use of their names.

## FULL ACCESS TO THE PRINCIPLES



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- The Complete 2015 *Principles for Good Governance and Ethical Practice*
- *Principles* Legal Reference Edition
- Organizational Assessment Tool
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# Principles of Governance: Key Responsibilities

## Mission

- Ensure that your organization has a clear, succinct written mission statement that expresses its core values and reason for being.
- Tie the organization to the spirit of the sector and to the major issues facing the organization's field and community.
- Revisit the mission statement annually in light of internal and external change, and revise it if necessary.
- Ask other organizations and similar organizations for copies of their mission statements and compare how they describe their vision and values.
- Seek internal and external feedback - from staff and from members or constituents -- about the organization's mission.
- Make the organization's mission widely known by promoting it in the community.

## Oversight

- Engage in regular strategic planning as an integral part of effective leadership and management.
- Commission a periodic organizational assessment that examines, in detail, the organization's programs and services, as well as its management, structure, and capacity.
- Adopt and regularly review a code of ethics and conflict of interest policy for board and staff.
- Understand and respect the relationship between board and staff.
- Select the chief executive carefully, and provide a clear description of duties and relationships.
- Support and strengthen the chief executive and the board - CPO relationship through a regular performance evaluation.
- Ensure high quality executive leadership.
- Make board self-assessment a routine part of the board's work.

## Resources

- Formulate a fund-raising strategy, including a case statement that expresses the rationale for financial support.
- Expect each board member to make an annual contribution to the organization according to his or her means, and take an active role in raising money.
- Cultivate board members with expertise in finance.
- Approve and monitor the annual operating budget.
- Review regular financial reports from staff. Require an annual audit by an independent accountant.

## Outreach

- Listen to the needs and interests of current and potential stakeholders.
- Be active community ambassadors, promoting the organization's mission, service, and achievements as well as bringing community perspectives to the attention of the board and staff.
- Ensure that the organization has a marketing and public relations strategy to support outreach.
- Seek out key leaders in business, government, education, and the media to inform them about the organization.
- Develop policies that support and encourage outreach activities.

Adapted from *Meeting the Challenge: An Orientation to Nonprofit Board Service* (video) BoardSource, 1998

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# Common Board Shortcomings

What are the main weaknesses, omissions, mistakes, flaws, bad judgments, and sins that a board or an individual board member can commit? This paper lists several ways that a governing board can lose its way, along with some basic principles by which to operate.

## 1. Veering off the mission

Example: A youth education organization accepts a generous grant to build a sports facility for young people.

The most important decision-making guideline for a board is the mission statement. If the mission is not a central theme at every board meeting, it can be easy for a board to lose focus of the organization's true purpose.

## 2. Complacency

Example: A board member does not know how to analyze financial statements. Instead of asking questions, he votes with the majority.

A core obligation of every board member is active participation. Some symptoms of complacency might include board members who put off their assignments, disregard the core responsibilities that come with being a board member, fail to ask questions, or miss meetings.

## 3. Misguided motivations

Example: A board member recruits an out-of-work relative to run the organization.

Board members must always think of the organization first. Allowing personal preferences to affect decision making places the organization in a secondary role in a board member's mind. Misguided and unethical motivations, undeclared conflicts of interest, and the pursuit of personal benefit can endanger the organization's tax-exempt status.

## 4. Multiple voices

Example: A board member is interviewed by the press and advocates for her own solution to a crisis situation - one not adopted by the board.

A board only has authority as a group. Boards speak with one voice, which is formulated through deliberation. Individual board members are bound by the collective decision. Differing opinions need to be resolved in the boardroom, not declared outside to constituents, the media, or customers.

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## **5. Micromanaging**

Example: The board insists on being involved in choosing a new computer system for the organization.

One of the key duties of a board is to hire a competent chief executive to run daily operations. Part of this duty assumes that there is a valid job description and a performance evaluation process in place. A board's role is to oversee that the organization is well run; not to interfere in the domain of the chief executive.

## **6. Limitless terms**

Example: Fearful of losing control, the founding board of an organization has been governing for 15 years.

Every board must accept and even thrive on change. New perspectives and different ideas keep a board and organization moving forward. Term limits can help boards avoid stagnation.

## **7. Lawless governance**

Example: To get through a temporary financial crunch, the chief executive decides not to pay payroll taxes for several months. The board is unaware that this is happening.

Nonprofit tax-exempt organizations must heed federal, state, and local regulations, as well as their own bylaws. It is the board's role to make sure that all laws are respected. The board needs to assure that the organization files its Form 990 correctly and on time; that employment taxes are withheld regularly; and that official documents are saved appropriately. If a board fails to adopt appropriate policies or to effectively oversee financial regulations, it may become liable for wrong doings.

## **8. No self-assessment**

Example: Board members' morale is low, attendance is sporadic, and the chair has no clue about how to energize the board.

By studying its own behavior, sharing impressions, and analyzing the results, a board is able to lay the groundwork for self-improvement. Failing to assess its own performance, a board is unable to define its strengths and weaknesses. As a by-product, it can also enhance its team spirit, its accountability, and its credibility with funders and other constituents.

## **9. Lack of self-improvement**

Example: Board members have never seen individual board member job descriptions and are not familiar with their legal obligations.

Self-improvement is one of the innate consequences of self-assessment. Regular self-assessment is a futile process if it does not address apparent weaknesses in a board and result in structured

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self-betterment. Boards that do not provide learning possibilities for their members miss opportunities and inefficiently utilize their members' abilities.

#### **10. Knotted purse strings**

Example: A board is not able to reach consensus on its personal contribution policy. It becomes divided due to feelings of unfairness and lack of commitment.

Asking for and giving money are natural aspects of being a board member in most 501(c)(3) charities. Boards that are responsible for fundraising, yet don't have a 100 percent personal contribution rate, have failed the ultimate commitment test. If the board is not supporting the organization whole-heartedly, how can it convince others to do so?

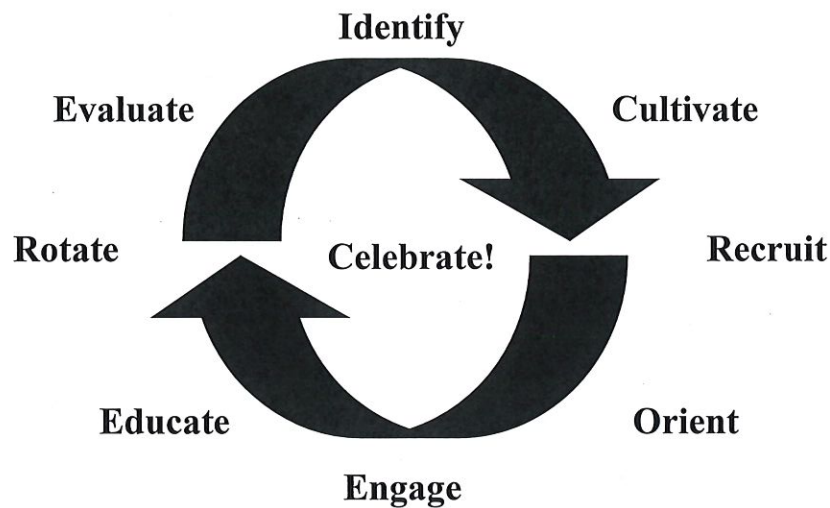
#### **References**

Richard T. Ingram, *Basic Responsibilities of Nonprofit Boards* (BoardSource Revised 2003).  
Berit M. Lakey, *Nonprofit Governance: Steering Your Organization with Authority and Accountability* (BoardSource 2000).

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# The Board Building Cycle



**Step 1: Identify** board needs (Skills, knowledge, perspective, connections, etc., needed to implement the strategic plan). What do we have? What is missing? Identify sources of board members with the needed characteristics.

**Step 2: Cultivate** potential board members. Get them interested in your organization and keep them informed of your progress.

**Step 3: Recruit** prospects. Describe why a prospective member is wanted and needed. Describe expectations and responsibilities of board members, and don't minimize requirements. Invite questions, and elicit their interest and preparedness to serve.

**Step 4: Orient** new board members to the organization - program, history, bylaws, pressing issues, finances, facilities, organization chart - and to the board - recent minutes, committees, board member responsibilities, lists of board members and key staff members.

**Step 5: Engage** all board members. Discover their interests and availability. Involve them in committees or task forces. Assign them a board "buddy." Solicit feedback. Hold everyone accountable. Express appreciation for work well done.

**Step 6: Educate** the board. Provide information concerning your mission area. Promote exploration of issues facing the organization. Don't hide difficulties. Celebrate accomplishments.

**Step 7: Rotate** board members. Establish and use term limits. Do not automatically re-elect for an additional term; consider the board's needs and the board member's performance. Explore advisability of resigning with members who are not active. Develop new leadership.

**Step 8: Evaluate** the board and individual board members. Engage the board in assessing its own performance. Identify ways in which to improve. Encourage individual self-assessment.

**Step 9: Celebrate!** Recognize victories and progress, even small ones. Appreciate individual contributions to the board, the organization, and the community. Make room for humor and a good laugh. (Adapted from *The Board Building Cycle* by Hughes, Lakey & Bobowick, 2003)

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# Governance Committee Job Description

The governance committee is responsible for ongoing review and recommendations to enhance the quality and future viability of the board of directors. The work of the committee revolves around the following five major areas:

## 1. Board Role and Responsibilities

- Leads the board in regularly reviewing and updating the board's statement of its roles and areas of responsibility, and what is expected of individual board members.
- Assists the board in periodically updating and clarifying the primary areas of focus for the board, and helps shape the board's agenda for the next year or two, based on the strategic plan.

## 2. Board Composition

- Leads in assessing current and anticipated needs related to board composition, determining the knowledge, attributes, skills, abilities, influence, and access to resources the board will need to consider in order to accomplish future work of the board.
- Develops a profile of the board as it should evolve over time.
- Identifies potential board member candidates and explores their interest and availability for board service.
- Nominates individuals to be elected as members of the board.
- In cooperation with the board chair, contacts each board member to assess his or her continuing interest in board membership and term of service and

works with each board member to identify the appropriate role he or she might assume on behalf of the organization.

## 3. Board Knowledge

- Designs and oversees a process of board orientation, including gathering information prior to election as board member and information needed during the early stage of board service.
- Designs and implements an ongoing program of board information and education.

## 4. Board Effectiveness

- Initiates periodic assessment of the board's performance. Proposes, as appropriate, changes in board structure and operations.
- Provides ongoing counsel to the board chair and other board leaders on steps they might take to enhance board effectiveness.
- Regularly reviews the board's practices regarding member participation, conflict of interest, confidentiality, etc., and suggests improvements as needed.
- Periodically reviews and updates the board's policy guidelines and practices.

## 5. Board Leadership

- Takes the lead in succession planning, taking steps to recruit and prepare for future board leadership.
- Nominates board members for election as board officers.

The Governance Committee Job Description is adapted from the work of Fred Miller, Chatham Group, Inc. and *The Board Building Cycle* by Hughes, Lakey & Bobowick, 2003



# Board Orientation Chart

**The following is an overview of the information that needs to be conveyed to new board members at their orientation. The materials can be presented in person and in writing at an orientation meeting.**

Information	Issues	Presentation Options
<b>About the Organization</b>		
<b>Program</b>	Offer new board members a feel for the work of the organization – what it does, whom it serves, what difference it makes – to get them emotionally and intellectually connected and motivated.	<ul style="list-style-type: none"> <li>• Tour of facilities</li> <li>• Observation of/participation in program activities</li> <li>• Presentation by client, member, or program participant</li> <li>• Video, slides, film presentation</li> <li>• Verbal presentations</li> <li>• Written materials</li> </ul>
<b>Finances</b>	Help new board members become informed about where money comes from, how it is spent, and the state of the organization’s financial health, including their role in fundraising.	<ul style="list-style-type: none"> <li>• Presentation by chief executive, chief financial officer, or treasurer</li> <li>• Background materials (most recent audit, budget, financials), graphically presented, if possible</li> <li>• Presentation of the fundraising strategy</li> </ul>
<b>History</b>	Provide sufficient knowledge about the past so that the present makes sense. Also, help new board members see their own participation as part of the organization’s ongoing story.	<ul style="list-style-type: none"> <li>• Stories told by “old timers”</li> <li>• Pictures</li> <li>• Written materials</li> </ul>
<b>Strategic Direction</b>	Present a framework for new members to participate effectively. Clarify the mission, vision, organizational values, and goals that inform organizational actions.	<ul style="list-style-type: none"> <li>• Presentation/discussion by the chief executive or board chair</li> <li>• Copy of strategic plan (or other documents, especially mission statement, if no plan is available)</li> </ul>
<b>Organizational Structure</b>	Help new board members understand who does what and lines of accountability.	<ul style="list-style-type: none"> <li>• Copy of the bylaws, IRS determination letter</li> <li>• Organizational chart</li> <li>• Introductions to key staff members</li> </ul>
<b>Board Roles</b>	Ensure that new board members understand the roles of the board.	<ul style="list-style-type: none"> <li>• Presentation/discussion, preferably with the whole board involved</li> <li>• Written materials</li> </ul>
<b>Board Member Responsibilities</b>	Ensure that new board members understand their own responsibilities as board members.	<ul style="list-style-type: none"> <li>• Presentation/discussion</li> <li>• Signed agreement (job description), including conflict of interest and ethics statements</li> </ul>
<b>Board Operations</b>	Help new board members understand how the board operates so that they may participate effectively.	<ul style="list-style-type: none"> <li>• Board manual</li> <li>• Board mentors</li> <li>• Committee charges and member lists</li> <li>• Meeting schedule</li> </ul>
<b>Board Members</b>	Facilitate new board member integration with other members.	<ul style="list-style-type: none"> <li>• List of board members and biographical data</li> <li>• Time set aside for social interaction</li> </ul>
<b>Skills</b>	Instruct new members on how to read a financial statement.	<ul style="list-style-type: none"> <li>• Written materials</li> <li>• Presentation by the treasurer or finance committee</li> </ul>

Adapted from *The Board Building Cycle* by Hughes, Lakey & Bobowick, 2003

# Individual Board Member Self-Evaluation

Use the following questions for individual board member evaluation. For board members answering yes to these questions, they are likely to be fulfilling their responsibilities as board members.

	Yes	No	Not Sure
1. Do I understand and support the mission of the organization?			
2. Am I knowledgeable about the organization's programs and services?			
3. Do I follow trends and important developments related to this organization?			
4. Do I assist with fundraising and/or give a significant annual gift to the organization?			
5. Do I read and understand the organization's financial statements?			
6. Do I have a good working relationship with the chief executive?			
7. Do I recommend individuals for service to this board?			
8. Do I prepare for and participate in board meetings and committee meetings?			
9. Do I act as a good-will ambassador to the organization?			
10. Do I find serving on the board to be a satisfying and rewarding experience?			

Adapted from *The Board Building Cycle* by Hughes, Lakey & Bobowick, 2003

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## Board Governance Planning Form

We can start or complete the following projects in the next 90 days.

1)

2)

3)

4)

We can start or complete the following projects in the next 180 days.

1)

2)

3)

4)

We can start or complete the following projects before the end of this year.

1)

2)

3)

4)

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## Board Check List

*Answer each question with a yes, a no, or a kind of.*

1. Do you share the organization's strategic plan/vision with potential Board Members?
2. Can existing Board Members clearly express the organization's future vision? The mission?
3. Do you show prospective Board Members your Board Member Expectation Statement (job description) before electing them to the Board?
4. Do prospective Board Members see your governing documents, financial statements and budget before agreeing to join the Board?
5. Are new Board Members selected strategically to fulfill a need or weakness on the Board? (rather than selecting a PLU? . . . Person Like Us)
6. Do you have an effective new Board Member orientation or onboarding process in place?
7. Do prospective (and existing) Board Members understand the legal duties/responsibilities of a nonprofit Board?
8. Do new Board Members understand the difference between a 501c3 public charity and other nonprofit organizations they may have been associated with? (professional societies, trade associations, business development organizations)
9. Have you reviewed and updated your governing documents and policy statements in the past five years?
10. If your budget is over 2 million dollars have you established an Audit Task Force or Audit Committee that does not overlap with the Finance Committee?
11. Does your Board of Directors not your staff hire your auditor?
12. Does the auditor report directly to the Board of Directors (or Finance Committee or Audit Committee) and not to the staff?
13. Does your Board, your Audit Committee, or your Finance Committee review the 990 before it is filed?
14. Do you review the audit or management letter with the full Board of Directors?
15. Have you reviewed/updated/adopted your Conflict of Interest Policy in the past 5 years?

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16. Does each Board Member sign a conflict of interest disclosure statement each year?
  17. Does the Board receive timely financial statements?
  18. Are the financial statements formatted in a way that they are clearly understood by the Board?
  19. Does your entire Board vote on the CEO compensation package?
  20. Does your Finance Committee or Executive Committee review 501c3 salary surveys before recommending the CEO's (Executive Director's) salary package?
  21. Do you have a formalized CEO (Executive Director) review process in place that is followed annually regardless of who is the Board Chair?
  22. Does the full Board approve/modify the CEO annual goals and objectives at the start of each year?
  23. Does the full Board give feedback through written survey on the CEO performance at the end of the year?
  24. Do you have an emergency CEO succession plan in place should something unexpected happen to your chief staff professional?
  25. If you have an Executive Committee does it steer, guide, lead and monitor Board work, **not** do Board work? Are Executive Committee meetings and conference calls open to all Board Members?
  26. Is a Board Member's performance reviewed at the end of his/her term before they are re-elected to an additional term?
  27. Does the full Board complete a comprehensive anonymous governance assessment survey every three to four years to benchmark its governance journey?
  28. Do you have meaningful term limits and enforce them?
  29. Do you have a plan to keep good former Board Members engaged in committee work and task force work or otherwise involved?
  30. Are your Board Members knowledgeable enough about the organizations charitable work and programs that they can talk about them in the community?
  31. Do your Board Members regularly open doors and make connections for your development staff?