



Grant Thornton

Higher education board member handbook



College and university board of trustee members have a critical responsibility: to direct the institution toward achieving its mission. As a trustee, you have the opportunity to contribute your talent, expertise and dedication to a worthy cause.

Serving on the board of a college or university, particularly a highly visible one, is both an honor and a responsibility. As a trustee, you must remain focused on providing good stewardship of the institution's mission, reputation and resources. The responsibility that comes with providing this stewardship need not be overwhelming, however. When you begin your board tenure with a solid overview of what you need to know and what will be expected of you, your orientation to trusteeship should go smoothly.

As you read through this handbook, you may uncover many questions you didn't know you had. Grant Thornton LLP's Higher Education and Not-for-Profit practice has the answers you're looking for. We're committed to providing outstanding service to meet all of your accounting, tax and advisory needs.

Contents

- 2 The special purpose of a higher education institution
- 4 Trustee roles, responsibilities and liabilities
- 14 Keeping the board effective
- 17 Accountability and integrity
- 22 Financial stewardship
- 28 Operating procedures
- 33 The trustee's role: A recap
- 34 About Grant Thornton

This document supports the marketing of professional services by Grant Thornton LLP. It is not written tax advice directed at the particular facts and circumstances of any person. Persons interested in the subject of this document should contact Grant Thornton or their tax advisor to discuss the potential application of this subject matter to their particular facts and circumstances. Nothing herein shall be construed as imposing a limitation on any person from disclosing the tax treatment or tax structure of any matter addressed. To the extent this document may be considered written tax advice, in accordance with applicable professional regulations, unless expressly stated otherwise, any written advice contained in, forwarded with, or attached to this document is not intended or written by Grant Thornton LLP to be used, and cannot be used, by any person for the purpose of avoiding any penalties that may be imposed under the Internal Revenue Code.

The special purpose of a higher education institution

It is uniquely American to create and sustain voluntary associations that further religious, cultural, professional, social service and educational goals. As early as the 1830s, Alexis de Tocqueville observed the unique propensity of Americans to form voluntary associations to achieve great purposes, which is in contrast with most other nations, where governmental action is expected.

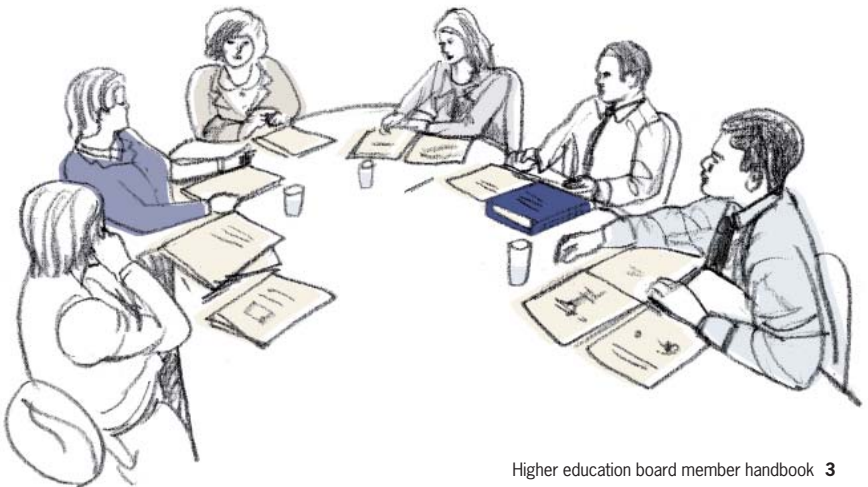
de Tocqueville said:

"Americans of all ages, all conditions, and all dispositions constantly form associations. They have not only commercial and manufacturing companies, in which all take part, but associations of a thousand other kinds, religious, moral, serious, futile, general or restricted, enormous or diminutive. The Americans make associations to give entertainments, to found seminaries, to build inns, to construct churches, to diffuse books, to send missionaries to the antipodes; in this manner they found hospitals, prisons and schools. If it is proposed to inculcate some truth or to foster some feeling by the encouragement of a great example, they form a society. Wherever at the head of some new undertaking you see the government in France, or a man of rank in England, in the United States you will be sure to find an association.

Thus the most democratic country on the face of the earth is that in which men have, in our time, carried to the highest perfection the art of pursuing in common the object of their common desires and have applied this new science to the greatest number of purposes."

Our voluntary associations are neither governments nor for-profit entities. The success of a college or university is measured not by votes or by profits, but rather by the achievement of its unique mission of teaching, expanding knowledge and understanding, and serving the larger community. The functions of a college or university exemplify the American propensity for uniting to promote and advocate for a particular cause. The services provided play a vital role in the community.

Boards of trustees are the agents for directing colleges or universities toward the achievement of their mission. They collect and spend funds held in trust for a specific charitable or educational purpose, and, as such, colleges or universities are provided a tax exemption because their goals support the public good.



Trustee roles, responsibilities and liabilities

Once a trustee has been selected, it is important that he or she be brought up to speed as quickly as possible. New trustees should receive a briefing from the chairperson and a tour of the institution's facilities. Further, institutions should offer a formal board orientation program covering such topics as how the board functions, management duties vs. board duties, indemnification and insurance, board committees, information flow, delegation, and authority.

Ideally, the institution should make available a board orientation book or other sourcebook containing the following information:

- The institution's articles of incorporation, bylaws and amendments
- A statement of the institution's history, mission and services
- The institution's strategic plan
- Regular financial and operating reports from the past year
- The most recent audited financial statements, including the management letter
- A copy of the directors' and officers' (D&O) liability policy
- A copy of the Code of Conduct policy
- A contact sheet listing the names, addresses and contact information of trustees
- A list of the institution's key executives
- Rules about expense forms and reimbursement
- A calendar of the upcoming year's board meetings, to include dates, times and locations
- Minutes of meetings held within the past year
- The conflict-of-interest policy and summary of related disclosures
- Copies of any recent regulatory filings, including Form 990
- Results of any governmental audits

While it is not necessary to be conversant with all of that information — in its considerable volume — trustees should be aware of its contents and know when to consult it.

The role of the board of trustees

The board should not be distracted from certain key responsibilities that are essential to its success:

- **Preserving and, when necessary, reshaping the mission** — This is the board's most important role. Trustees need to make certain that a strategic plan is in place describing how the institution will fulfill its mission going forward. In addition, trustees should measure each proposed action against both the institution's mission and its approved plans.
- **Selecting the president** — Another important role for the board is the selection of the president, to provide full-time leadership for the institution and to recommend and implement the policies and programs approved by the board. Sometimes the board's responsibility will include confirmation of those nominated for key positions by the president.
- **Ensuring that the institution is well-managed** — While the board should not manage the institution, it should be satisfied that the institution is managed effectively. To achieve that task, the board should ask enough questions to satisfy itself that a sufficient number of qualified staff members are assigned to key tasks, resources are allocated through a realistic budget consistent with the mission, internal controls are in place to prevent fraud or noncompliance, proper ethical and governance standards are followed, and the programs of the institution have clearly defined purposes and are successful in achieving those purposes.

Trustee roles, responsibilities and liabilities

- **Representing the external world to the institution and the institution to the external world** — The board serves as what is sometimes called “a bridge and a buffer.” Trustees advocate on behalf of the institution, helping to raise awareness of its mission. Hence, trustees are often involved in the solicitation of major donors. It is also important for the board to be sensitive to the environment in which the institution operates. In that capacity, the board should give the institution’s staff important feedback about how policies, plans and programs need to change in response to a changing world.
- **Protecting the institution from external threats** — In the lives of many institutions, issues arise that threaten the autonomy, services or good name of the institution. Such issues include scandals involving the institution — or similar institutions — or political attacks on the purposes or programs of the institution. In these circumstances, trustees need to step forward to explain and defend the institution.
- **Exercising financial stewardship** — The board is responsible for approving the budget as well as major financial transactions, such as the issuance of debt. The board manages the endowment of the institution, usually through an investment committee, and approves the goals of fundraising campaigns. In addition, the board tends to play a major role in supporting capital campaigns by donating personal time and financial resources.

- **Being certain that the board has the right skills and practices to do its job** — The board needs individuals with a strong commitment to the fundamental purpose and mission of the institution. Boards should consider performing an annual inventory of talent to assess whether the right professional capabilities are represented on the board. The board should also include individuals with the specific skills and know-how needed to examine issues through multiple lenses: legal, financial, public relations and communications, management, and professional development, among others. The board must also be attentive to its internal processes, so that its meetings focus only on board-level matters and do so in a way that draws upon the combined knowledge and experience represented at the table.
- **Making sure that the institution is in compliance with laws and regulations** — Being exempt from most taxes does not mean that the institution is exempt from regulation. Far from it. The board should be aware of federal and state laws and regulations that apply to the institution, along with applicable standards set by accreditors, bond covenants and charity watchdog groups.

Trustee roles, responsibilities and liabilities

Your duties as an individual trustee

Your service as a trustee will be most rewarding to you, and you will serve the institution best, if you are able to focus on your key duties:

- **Attend all meetings** — The skills you bring to the table do not matter if you are not present. Trustees who repeatedly miss meetings should be candidates for removal. Their absence can drain the morale of other trustees — and ultimately the morale of others in the institution.
- **Be prepared and informed** — Before each meeting, read the meeting materials sent to you. Come prepared to ask questions and make comments. Stay informed of trends and developments in the type of work that the institution performs so that you can bring a broader perspective. In addition, stay abreast of good governance practices as they evolve.
- **Speak your mind and ask hard questions** — Some institutions have suffered because trustees were more concerned about appearances than they were about discussing difficult or challenging issues. But you must address them when they arise. As a trustee, your primary responsibility is to protect the good name of the institution and to ensure that the institution's staff and money are being used consistent with good practice.
- **Take responsibility for your stewardship of the institution's assets** — The board must make certain that funds are used consistent with the intent of those who have donated them. The board must satisfy itself that sufficient funds are allocated to each function and that those allocations are consistent with its own priorities.

- **Watch others at the table** — Check to make sure that other trustees are pulling their weight. Only when the full board acts in cohesion can the institution’s mission be fully accomplished.
- **Remember that integrity is paramount** — The most important asset of your institution is its good name. The second most important asset is the confidence of its donors and sponsors in the institution’s capacity to manage and spend funds prudently. The board should make certain — both in its own practices and policies and those of the staff — that integrity remains the highest priority. If the board sets a good example, the institution will most likely follow it.



Trustee roles, responsibilities and liabilities

Critical distinctions

- **Board vs. management** — Both the institution’s board and its management must have a clear understanding of the distinctive roles of each. Much confusion (and sometimes conflict) occurs when those distinctions aren’t clear.

Boards typically reserve these functions for themselves:

- Setting board policy
- Approving new programs or deleting old ones
- Selection, oversight and compensation of the president
- Approval of the operating budget recommended by management
- Oversight of the endowment

Management is generally responsible for these functions:

- Selection and supervision of staff
- Development, recommendation and implementation of the budget
- Establishment of operating procedures

Trustees do not have individual power or authority. Instead, these powers reside with the full board of trustees. Occasionally, a trustee may become heavily involved in a particular program and work closely with the institution’s staff. In that situation, the trustee should report periodically to the full board to keep it informed. The board sets standards to measure how well management performs — and initiates actions, when necessary, to see that management carries out its obligations.

- **Committees vs. the full board** — Most of the board’s work should be done by its committees. Thus, individual trustees will become knowledgeable in key areas of the board’s work, and the full board will spend less time on any one issue or set of issues. It is good practice to follow a committee’s recommendations unless there are compelling reasons not to do so. Board committees are likely to include budget, finance, audit, personnel, nominating, and program or mission.
- **The external auditor is accountable to the board, not to management** — All boards have a fiduciary responsibility to:
 - know the amount of assets available to the institution;
 - verify that the use of those assets is consistent with the mission of the institution, regulatory requirements and accepted accounting principles; and take steps to minimize the possibility of fraud or conflict of interest

Commissioning an external audit by a qualified public accounting firm is a key element of the board’s responsibility. The accounting firm should be selected by the audit committee on behalf of the board and should present the audited financial statements to both the committee and/or the full board. Grant Thornton’s *Higher education audit committee handbook* booklet provides further information.

Trustee roles, responsibilities and liabilities

Liability

A trustee has a fiduciary obligation to the institution. He or she must act with good faith and loyalty — and always exclusively in the best interests of the institution. To guard against abuse of the good-faith presumption, trustees serving higher education institutions face several kinds of liability:

- Liability to third parties, such as contractors providing services to the institution
- Liability to the institution and its members
- Statutory liability

A board has a legal duty to conserve and protect the institution's assets.

This duty carries with it legal risk, which is why many higher education institutions carry D&O liability insurance. Employers are aware of the potentially unfavorable consequences of board-related litigation; indeed, some employers do not permit

their employees to sit on boards of institutions that do not have adequate D&O liability insurance. A new trustee should know whether the institution carries D&O insurance, and the extent of the insurance coverage. It may be prudent for a trustee or the institution as a whole to have the D&O policy evaluated by independent legal counsel. For additional safety, some states have adopted volunteer-protection statutes for the benefit of uncompensated trustees and trustees. Board members may consider obtaining an individual umbrella policy.

Claims against individual trustees of a higher education institution can arise from multiple scenarios:

- Employees claiming wrongful termination or other violation of their rights
- Governmental entities claiming waste of assets or violation of reporting regulations
- Environmental damage from toxic waste on property an institution acquires

- Service recipients claiming negligent supervision or improper selection of employees and volunteers
- Violation of regulations regarding lobbying efforts



Both federal and state regulations prohibit trustees from engaging in improper dealings with higher education institutions and from knowingly approving excess-benefit transactions involving institution insiders. Indeed, trustees taking such actions are subject to financial penalties. For more information, see “Intermediate sanctions,” p. 18. Likewise, conflicts of interest can be the basis of liability action against a trustee. If a trustee receives an improper or undisclosed personal financial benefit as a result of the institution’s transactions, he or she may be liable to the institution.

The idea of personal liability should not frighten anyone away from board service. But it behooves trustees to familiarize themselves with the protection afforded by the state — and by the institution itself — and to exercise care in making decisions.

Keeping the board effective

Managing the makeup, skills and education of the board is an ongoing process. Boards should not only consider their current composition, but also plan for future membership and leadership — and, at the same time, evaluate overall board effectiveness.

In what ways can they do this?

- **Recruiting, retaining and rewarding good trustees** — The institution's success depends in part on the board's commitment. While trustees are sometimes appointed by external agencies or elected by constituents, in most cases the board selects its new members directly. A key board responsibility, in those cases, is to recruit trustees who will help the institution achieve its mission and remain active in the board's work. The board should be attentive to ways to make board service exciting and rewarding, including formal recognition of achievement.
- **Providing continuity of board leadership** — The board should have a succession plan, formal or informal, that identifies future board chairs, committee chairs and other leadership roles.
- **Balancing the skills of trustees** — Optimally, each trustee should possess at least one of several essential skills — budgeting, financial management, investments, human resources and legal matters — as well as a working knowledge of the academic programs of the institution.
- **Evaluating the board's effectiveness** — The board should create processes to determine whether it is functioning effectively in support of the institution's purpose. The board should ask whether it is following the practices recommended in this booklet,

as well as other practices that trustees collectively agree are important. The board should then develop one or more evaluation tools to facilitate the assessment. The board might also find ways to ask its various stakeholders to assess its effectiveness.

- **Managing the board's size** — The size of a board represents a difficult balance between diversity of views and skills, and the board's functional effectiveness. The smaller the board, the more likely that it will be able to perform its functions comprehensively, particularly as they relate to management. The larger the board, the more diverse its membership will be, but the less likely it will be to reach clear decisions quickly. Larger boards typically rely on the committees to work through issues and to report to the full board.

- **Monitoring board continuity and turnover** — Both continuity and turnover are essential features of good trusteeship practices. Continuity provides institutional memory. Turnover brings fresh perspective. In general, it is good practice to set term limits for trustees.



Keeping the board effective

- **Providing opportunities for education and orientation** — The education of trustees should not be limited to their orientation. On a regular basis, time should be set aside to cover topics such as the predicted effects of pending legislation, tips for reading financial statements, or fundraising techniques for trustees. Periodically, the board should ask itself important questions: Are we true to our mission? Is our mission well-defined? Boards should also have annual retreats to discuss the alignment of the institution's mission with its goals.
- **Planning in advance of meetings** — Efficient and effective meetings are essential to a well-functioning board. Boards should ensure that meeting agendas are planned well in advance. Consent agendas are being used more often to reduce the time spent on nonessential issues — that is, items that require formal board approval but for which there is no need for board discussion before taking a vote. The board meeting thus involves only the discussion of critical issues and the presentation of resolutions requiring a board vote.

Accountability and integrity

A trustee is a link between the higher education institution and the constituencies that support it and are served by it. Those constituencies are increasingly holding trustees legally and ethically accountable for the actions or inactions of institutions.

The institution's most valuable asset is its good name, and a trustee's top priority should be protecting its reputation. Good practice, as well as the expectations of donors and regulators, requires a high level of attention to the issues of financial reporting, controls and assessment of risk. The board must be confident that adequate systems are in place for controlling, administering and planning the use of resources.

Policies

To mitigate potential risks, boards should consider instituting the following policies:

- **Code of ethics** — Trustees should adopt a code of high standards in ethical behavior that applies to the board, management and staff across the institution.
- **Conflict of interest (and disclosure)** — The board should have a conflict-of-interest policy across the institution ensuring the independence of the board, management, staff, the external auditor and other vendors from one another, so that each entity performs only its role and is not compromised in any way.
- **Whistleblower** — The board should have a policy in place for trustees, staff and other stakeholders to raise issues about the institution's ethical or financial practices. The policy should clarify how to raise such issues and how to prohibit retribution for raising them.

Accountability and integrity

Intermediate sanctions

The IRS monitors higher education institutions and can impose intermediate sanctions for awarding unreasonable salaries and benefits or, alternatively, for allowing trustees or other interested parties to provide goods or services to the institution for more than they are worth.

The test is whether the benefit provided to the insider (generally a trustee or staff member) exceeds the value of the consideration the institution receives. This consideration can consist of services provided in exchange for compensation. The IRS can impose a monetary sanction in cases of improper dealings involving institutions exempt under Sections 501(c)(3) and 501(c)(4).

In addition, as of January 1, 2010, trustees who knowingly and willfully approve such a transaction are jointly and severally liable for a 10 percent tax, limited to \$20,000 per transaction. Insiders covered by the law include persons who have a substantial influence over the institution's affairs. This could include members of the governing body (the board), the president and CFO, and others who are determined to have such influence.

Once someone is covered by this definition, family members and any controlled businesses they own are also included. If the IRS imposes penalties, the details, including names and amounts, must be shown on Form 990 filings, which are available to the public.

As a trustee, you need to make sure the institution has procedures in place to prevent conflicts of interest and transactions involving excess benefits and disqualified persons. D&O insurance policies may or may not cover these penalties.



The board — or a committee that has no conflicts of interest with the person whose transaction is under consideration — should approve all transactions involving insiders. You should also make sure that all compensation and benefits, including those provided to you as a trustee, are properly disclosed on Form 990. To the extent that these compensation and benefit amounts are taxable, they should be reported on Form 1099 or Form W-2, as appropriate.

Failure to properly document and report compensation and benefits is likely to result in automatic violations of these rules. Benefits that are paid or provided but are not properly reported and disclosed are considered automatic excess benefits, regardless of the reasonableness of the amounts.

Accountability and integrity

Other regulatory/tax compliance issues

The board should ask management sufficient questions to satisfy itself that the institution is not violating laws or regulations made by the host of agencies that regulate the institution.

Of special importance to colleges and universities are the regulations and compliance issues related to the receipt of federal financial aid and sponsored research. Penalties for noncompliance are significant and can lead to loss of both funding and institutional reputation.

An important tax issue is unrelated business income (UBI). The IRS will impose a tax liability on certain activities of a higher education institution if those activities are found to be business activities unrelated to the institution's tax-exempt purpose and not otherwise excluded from UBI in the Internal Revenue Code (IRC).

Higher education institutions may face other tax issues:

- State, local and foreign taxes
- Charitable registrations
- Foreign regulatory filings pertaining to investments
- Escheat and unclaimed property laws

Internal controls

Internal controls enable the board and the institution to perform several functions:

- Verify that transactions are properly authorized
- Ensure that assets are safeguarded
- Confirm that transactions are properly recorded and reported
- Prevent fraud and misstatements related to financial reporting

The board needs to ask questions and be vigilant about the effectiveness of the institution's internal controls and operating procedures. Items under consideration should include receipt of funds, personnel and

payroll procedures, authorization of disbursements, and handling of cash. The board should ask questions not only about financial resources and personnel procedures, but also about assets such as buildings, land, equipment and securities.

An effective internal control system will have a well-designed set of policies and procedures relating not only to transactions but also to record retention. Important files and information should be maintained and remain accessible for a reasonable period of time.

High-quality internal financial reporting

The board should expect to receive from management regular financial reports comparing financial results with budgetary predictions and reporting on the status of assets. The board should also expect management to make financial disclosures — consistent with the board’s own reports — to trustees, contributors and other stakeholders.

To meet the board’s need to evaluate the effectiveness of programs, many higher education institutions provide detailed internal statements that directly relate expenses shown on their financial statements to specific programs or functions. This functional approach makes it easier for trustees to analyze and compare costs.

The external audit

To provide the board and the institution’s other constituencies with confidence in the financial information and internal controls of the institution, the board should appoint a respected public accounting firm to conduct an audit of the financial records and processes of the institution.

The public accounting firm is responsible for providing the board with an independent opinion. Independence both from the board and from management is an essential feature of good practice with respect to the external audit. Neither management nor trustees should attempt to influence the opinion of the public accounting firm.

Financial stewardship

While the corporate standard for success — profitability — may not be appropriate in higher education institutions, sound financial management is crucial to the vitality of every college and university. Strong financial management is a necessary tool in competing for every dollar of tuition and fees as well as for every contributed dollar. An institution that is soundly managed is more likely to attract that dollar than one that is not.

Several aspects of financial management are of special concern to higher education trustees: budgeting, overseeing assets and raising revenue.

Budgeting and financial planning

The budget translates the hard-to-quantify goals of a higher education institution into measurable terms. It can be a powerful device for monitoring the institution's activities. This function is especially important because revenue shortfalls or uncontrolled expenses can sap the confidence of the institution's stakeholders and supporters.

Generally, the full board of an institution is involved only at certain stages in the budget process: establishing overall goals and activities that set the budget process in motion, approving the final budget, and comparing the institution's financial results with both its budget and its goals.

The board usually has a finance or budget committee that provides detailed oversight of these critical functions. This committee reviews management's recommendations for the next year's budget. Management handles most of the actual budgeting, with the CFO or budget director driving the process.

Committee members should ask difficult questions both of themselves and of management:

- What priorities are reflected in the proposed budget?
- What trade-offs have been made?
- How realistic is it for us to expect to be able to raise X number of dollars in contributions, fees or membership dues this year?
- How realistic is it for us to expect to increase the cost of services by Y percent?

Not surprisingly, when difficult questions must be asked, the budget may go through several revisions before reaching the full board. At that point, the extent to which the budget is further revised may vary widely from institution to institution. Sometimes boards are comfortable with making a decision based only on management's recommendations, and many budgets require few changes by the full board. Even so, a board should be fully aware of the institution's financial condition. To that end, it is the board's prerogative to ask difficult questions regarding the budget and to request revisions as needed. Further, the board must compare the financial estimates and goals established in the budget with actual results, and investigate variances.

Financial stewardship

Overseeing assets

The audited financial statements provide a clear measurement of the institution's financial assets; therefore, the board should evaluate those statements closely. Any significant increase or decrease in assets should be examined in terms of the institution's overall effectiveness. The board should find ways to assess the quality of the institution's human and physical assets, even though this is not reflected in the financial statements. Another financial asset requiring special attention by the board is the institution's endowment. The board should make certain that the endowment is overseen and managed in accordance with good practice — and that its investment return equals or exceeds that of endowments held by institutions of comparable size and scope. The board should also satisfy itself that the institution's investment policy is consistent with the board's tolerance level for risk and volatility.

A board faced with a severe financial shortfall should seek recommendations from the president and then choose the route best suited to getting the institution back on its feet.

Raising revenue

Most higher education institutions rely on fundraising activities to provide financial resources for their programs. Some institutions set minimum fundraising requirements for trustees; these standards are often referred to as give-or-get policies. For example, to remain on the board, a member would be required to raise \$5,000 annually through making personal contributions or soliciting them from others.

Institutional fundraising usually includes annual campaigns to support the operating budget and capital campaigns to raise funds for facilities and the endowment. Board involvement in capital campaigns is critical to their success, with trustees providing personal leadership and making personal gifts.

The board must monitor both the management of funds and the cost of raising them. The management of funds includes the appropriate recording of gifts, the monitoring of cash vs. pledges, and decisions about using particular gifts. The cost of raising funds must be closely watched and accurately reported to ensure its reasonableness and conformity to industry standards.

Tax-exempt status

While more than 20 categories of tax exemption are provided for by the IRS, most higher education institutions derive their tax exemptions from Section 501(c)(3) — Charitable, educational, religious or scientific institutions.

Each institution is subject to rules that control the types of activities it can carry on within its particular tax-exempt classification.

The extent to which the IRC allows lobbying, for instance, varies among the tax-exempt classifications. Lobbying — attempting to influence legislation — is allowed for a 501(c)(3) institution, but its lobbying is limited to an “insubstantial amount” of its activities. A 501(c)(3) institution may, however, make an election under Section 501(h) of the IRC to quantify the amount it can spend on lobbying.

As part of good financial stewardship, a trustee of a higher education institution must understand the purpose of the institution’s tax exemption and what types of activities would threaten it. The tax exemption itself is often the institution’s greatest asset, and losing it would be devastating.

Political activities, as opposed to legislative activities, pose problems for higher education institutions. For example, 501(c)(3) institutions are strictly prohibited from using funds to attempt to influence the election of a candidate for office. Any use of funds for such a purpose is grounds for revocation of a 501(c)(3) institution's tax exemption. Other institutions remain exempt but are subject to excise tax if they spend money for political purposes. Since neither result is desirable, trustees must monitor an institution's political activities and policies carefully.

Private inurement can also lead the IRS to revoke an institution's tax-exempt status. Private inurement results when an institution's assets or earnings are used for the benefit of an individual, as opposed to the institution itself. For example, private inurement may result if an institution pays compensation at a level that is unreasonably high compared with the level of effort and responsibility of the recipient.

Again, trustees must monitor the activities of the institution and its officers to ensure that no private inurement occurs.

Full disclosure

The public has a large stake in the operations of the higher education sector. Various tax exemptions granted to higher education institutions — such as property tax exemptions and sales tax exclusions — represent billions of dollars in lost tax revenue. Deductions of donations to 501(c)(3) institutions disclosed in personal income tax filings alone account for billions more in lost tax dollars each year.

In exchange for these benefits, higher education institutions are expected to provide full financial disclosure, implement efficient management practices and engage in ethical behavior. Contributors and other stakeholders are no longer satisfied with glossy annual reports.

To obtain the detailed information they're looking for, many potential contributors and members examine an institution's Form 990 filings. Charity watchdogs, the IRS and institutions themselves are required to make copies of these informational returns available to anyone who asks for them.

Form 990 disclosures include the following:

- The names and compensation of an institution's directors and officers
- Details of financial transactions between the institution and a trustee or a group with which he or she is affiliated
- Information regarding the institution's assets, liabilities, income sources, revenues and expenses

In addition to making Form 990 filings available, boards should consider posting clear and concise financial narratives, charts and other disclosures on the institution's website.



Operating procedures

Now that you have a well-educated, well-rounded board that is kept informed of its duties, responsibilities and liabilities, what's next? To effectively oversee the institution's operations, boards should employ a number of strategies and procedures.

Committees

Boards generally appoint committees to focus on particular areas of responsibility. Committees are essentially subsets of the full board. Specialists in one or two issues can examine them in detail during committee meetings — thus minimizing the time the full board must devote to those issues and maximizing the effectiveness of the full board.

Some committees typically focus on the institution's purpose, programs and mission. Other committees are more general in nature: finance and budget, audit, investment, executive, development/fundraising, and

nominating. The nominating committee is often appointed to select candidates for open board positions. And a board's executive committee is often empowered to act for the full board between meetings.

Boards should guard against appointing too many standing committees. Sometimes a problem arises for which a task force or an ad hoc committee may be more appropriate than a standing committee. A task force or an ad hoc committee is similar to a standing committee, except that it is not a permanent appointment. Once it recommends a solution to a problem or completes its project, the task force or ad hoc committee disbands.

All trustees should serve on one or more board committees based on their skills and talents. A new trustee should come prepared with an idea of which committee he or she would most like to join.

Information flow to trustees

If the board is to have a significant role in governing an institution, and if trustees are to minimize their exposure to legal liability, the information available to them about the institution's affairs is crucial.

Trustees should ask themselves several questions:

- Is the information adequate without being overwhelming?
- Is it available when needed?
- Are the special needs of the board of directors considered?
- Above all, is the information accurate?

An effective communication system has several components:

- A specific agenda for each meeting
- Advance distribution of as much material as possible; preferably material should reach each trustee at least one week before the meeting

- A standard report package for each board meeting
- Periodic, timely mailing by the president of key letters, memos, releases, industry reports and presentations; topics should include budgets, profit plans, the institution's long-range plan, significant policies and procedures, and committee reports
- Meeting minutes, all of which should be reviewed for accuracy

Obviously, much of the information a prudent board requires is of a financial nature: current operating results, comparisons of actual with budget, a statement of financial position, and the president's or CFO's report. Quarterly income projections are useful for helping trustees anticipate problems and judge actual performance. Trustees may also benefit from a review of cash and working capital forecasts, capital expenditure plans, employee pension plan information, and, of course, data pertinent to specific problems or concerns the institution faces.

Operating procedures

Preparing for board meetings

A trustee owes it to himself or herself, the other trustees, and the institution to be thoroughly apprised of all issues. A trustee should be familiar with the information provided in advance of a board meeting. The amount of preparation time will vary from board to board, depending on the nature of the institution and the problems it faces. Spending one hour in preparation for each hour of the board meeting is a good rule of thumb. A trustee should arrive at board meetings prepared to ask intelligent, probing questions and to take the initiative in dealing with the institution's problems. A trustee should always keep in mind that he or she will be held legally accountable for actions or inactions.

If after reviewing the materials in the information packet, a trustee has additional questions or needs further clarification, he or she should contact the chairperson and discuss any concerns before the board meeting. The chairperson can then be prepared if further discussion at the meeting is warranted.

How to build a better board

Evaluations of each trustee should cover such subjects as attendance at board and committee meetings, participation in board discussions, constructive criticisms and suggestions, preparedness for meetings, and availability to the president.

If evaluations reveal that there is underperformance, the chairperson is responsible for discussing the matter with the trustee, giving that person the choice between improving his or her performance or resigning. If that conversation does not produce the desired results, the underperforming trustee's name should be withheld from the list of candidates for renomination.

Trustees also need to assess whether their committee chairs are properly and effectively leading the committee and helping the institution meet its goals. To form an effective board, trustees must have a clear understanding of the strengths and weaknesses of the overall institution, its mission, and what it seeks to accomplish. Such an understanding can be gained through nothing less than a comprehensive review of the institution and its people. Only after this review will it be possible to establish a profile for the type of individual and specific expertise the board may lack.

Board criteria and selection

Trustees may have diverse backgrounds and come from varying socioeconomic levels. They frequently hold full-time managerial positions in the for-profit sector and bring skills developed there to the board.

But no matter their individual backgrounds, those on the board should collectively possess a number of critical traits, many of which are obvious: honesty, good judgment, common sense, perspective, conscientiousness, independence, intelligence, objectivity, the willingness to take positions and to question, and the courage to act. Trustees must also have good people skills. They must be able to judge people and their performance accurately — and, at the same time, they must get along well with others.

Overall management expertise is important. Trustees should be able to understand and interpret financial and operating reports and help form institutional policies, plans and objectives. Good trustees should be able to assess their information needs and be willing to learn about the institution and develop familiarity with the industry and marketplace in which the institution operates. In addition, trustees should be familiar with the federal, state and local laws that affect the institution.

Operating procedures

Trustees should also be aware of their public and social responsibilities. Their actions and behavior should enhance the institution's reputation — and should certainly not detract from it.

It is rare to find all of those traits and qualifications in any one trustee, but the board as a whole should possess them. A prudent board screens for critical attributes, just as management vets and interviews prospective employees. Candidates should be interviewed by several trustees, including the chairperson.

Potential trustees should be asked several key questions:

- Are they qualified and willing to serve?
- Will they be able to give the time and commitment necessary to complete the task?
- Are they able and willing to support the institution's fundraising?
- Will their appointment and performance reflect well on the institution and its mission?

Before selecting new members, a board should obtain:

- Biographical data concerning all candidates
- Candidate references provided by individuals not affiliated with the institution
- Signed conflict-of-interest statements and disclosures of any potential conflicts of interest

After a candidate has been approved, it is in the best interests of the institution to orient the new trustee quickly to his or her role. The quicker the orientation, the more valuable the trustee's relationship will be to others at the table.

The trustee's role:

A recap

Acting through the board as a whole, each trustee fulfills several functions:

- Determines the institution's goals and policies
- Selects and evaluates the president
- Monitors the overall management of the institution
- Evaluates the institution's programs against its purposes
- Oversees financial management of the institution and participates in fundraising
- Serves as a link between the institution and its constituents

Demands on the trustees of higher education institutions continue to mount. Meeting these demands requires commitment of time and expertise, commitment to shaping the direction of the institution, and commitment to protecting the interests of the people who support it and are served by it.

When a higher education institution faces financial or managerial difficulties, the expertise and contributions of the board can make recovery easier. And when an institution thrives, its trustees can see the tangible benefits of their efforts.



About Grant Thornton

The people in the independent firms of Grant Thornton International Ltd provide personalized attention and the highest quality service to public and private clients in more than 100 countries. Grant Thornton LLP is the U.S. member firm of Grant Thornton International Ltd, one of the six global audit, tax and advisory organizations. Grant Thornton International Ltd and its member firms are not a worldwide partnership, as each member firm is a separate and distinct legal entity.

In the U. S., visit Grant Thornton LLP at www.GrantThornton.com.

Institutions serving higher education boards of trustees

Association of Governing Boards

www.agb.org

American Council on Education

www.acenet.edu

National Association of College and University Business Officers

www.nacubo.org

Other Grant Thornton resources

- *Planned giving: A trustee's perspective*
- *Higher education audit committee handbook*
- *Grant Thornton national board governance survey for not-for-profit organizations*
- *OnCourse newsletter*
- *Not-for-Profit Alerts and Special Bulletins*

To request any of these publications or to receive additional information about Grant Thornton's Higher Education practice, contact:

Frank Kurre

Managing Partner
Higher education Practice
T 212.542.9530
E Frank.Kurre@gt.com

Or visit www.GrantThornton.com/highered.

Offices of Grant Thornton LLP

National Office

175 West Jackson Boulevard
Chicago, IL 60604
312.856.0200

National Tax Office

1900 M Street, NW, Suite 300
Washington, DC 20036
202.296.7800

Arizona

Phoenix 602.474.3400

California

Irvine 949.553.1600
Los Angeles 213.627.1717
Sacramento 916.449.3991
San Diego 858.704.8000
San Francisco 415.986.3900
San Jose 408.275.9000
Woodland Hills 818.936.5100

Colorado

Denver 303.813.4000

Florida

Fort Lauderdale 954.768.9900
Miami 305.341.8040
Orlando 407.481.5100
Tampa 813.229.7201

Georgia

Atlanta 404.330.2000

Hawaii

Honolulu 808.536.0066

Illinois

Chicago 312.856.0200
Oakbrook Terrace 630.873.2500

Kansas

Wichita 316.265.3231

Maryland

Baltimore 410.685.4000

Massachusetts

Boston 617.723.7900

Michigan

Detroit 248.262.1950

Minnesota

Minneapolis 612.332.0001

Missouri

Kansas City 816.412.2400
St. Louis 314.735.2200

Nevada

Reno 775.786.1520

New Jersey

Edison 732.516.5500

New Mexico

Albuquerque 505.855.7900

New York

Long Island 631.249.6001

Downtown 212.422.1000

Midtown 212.599.0100

North Carolina

Charlotte 704.632.3500

Greensboro 336.271.3900

Raleigh 919.881.2700

Ohio

Cincinnati 513.762.5000

Cleveland 216.771.1400

Oklahoma

Oklahoma City 405.218.2800

Tulsa 918.877.0800

Oregon

Portland 503.222.3562

Pennsylvania

Philadelphia 215.561.4200

South Carolina

Columbia 803.231.3100

Texas

Austin 512.391.6821

Dallas 214.561.2300

Houston 832.476.3600

San Antonio 210.881.1800

Utah

Salt Lake City 801.415.1000

Virginia

Alexandria 703.837.4400

McLean 703.847.7500

Washington

Seattle 206.623.1121

Washington, D.C.

Washington, D.C. 202.296.7800

Wisconsin

Appleton 920.968.6700

Madison 608.257.6761

Milwaukee 414.289.8200

Content in this publication is not intended to answer specific questions or suggest suitability of action in a particular case. For additional information on the issues discussed, consult a Grant Thornton client-service partner.



© Grant Thornton LLP
All rights reserved
U.S. member firm of Grant Thornton International Ltd