

The 2006 Grant Thornton LLP
**National Board Governance Survey for
Not-for-Profit Organizations**

Grant Thornton 



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About governance and accountability

Beyond Sarbanes-Oxley, there has been an increased focus on the governance of for-profit and not-for-profit organizations nationwide. In the not-for-profit sector, the Senate Finance Committee has sent letters to several organizations regarding their governance practices. Organizations such as National Association of College and University Business Officers and Independent Sector have released governance guidance, and many constituencies, including donors, have demanded stricter accountability.

The Internal Revenue Service has also increased staff to oversee not-for-profit organizations and added questions designed to increase the transparency of the Form 990 tax return. At the state level, new legislation governing not-for-profit organizations has been passed and more legislation is still pending.

In addition, stakeholders in not-for-profit organizations have raised their expectations, requiring much higher levels of accountability and transparency than in the past.

As a result, governing boards and management teams have taken stronger action in the following areas:

Accountability: Boards take their oversight duties more seriously and management has focused extensively on internal controls and financial reporting.

Transparency: Organizations provide more information about their governance practices, financial condition and results of operations.

Independence: Boards maintain their independence from management, and auditors protect their independence from management and the board. Audit committees have further promoted independence by appointing only outside directors to the audit committee.

For further information, visit Grant Thornton's Web site at www.GrantThornton.com/nfp or contact the Grant Thornton office nearest you.

As national managing partner of Grant Thornton's U.S. not-for-profit industry practice, I am pleased to present the fourth annual **Board Governance Survey for Not-for-Profit Organizations.**

Grant Thornton provides this annual survey as part of our continued thought leadership for the not-for-profit community — a community whose objective we share of serving the “Greater Good.” This year, I am pleased to note that 960 not-for-profit organizations participated in our survey, an increase from 860 in 2005.

Since we began this survey in 2003, demand by various constituencies for fiscal transparency, strong governance and proper stewardship have encouraged not-for-profit organizations to focus on governance issues and policy. According to survey findings, today, almost one-third of all organizations have a governance committee in place.

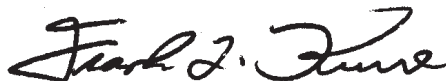
Many organizations have also been engaging in enterprise-wide risk assessments over the past several years to evaluate risks, including environmental, regulatory, governance, financial, and programmatic. Assessing reputational risk, specifically, has become more common to safeguard an organization's good name and reputation.

In addition, not-for-profit boards are ensuring their independence by forming an audit committee (64 percent) and assigning the audit committee the responsibility for hiring and terminating the audit firm, as well as determining the scope of work (40 percent).

Grant Thornton appreciates this opportunity to provide you with this survey of emerging governance trends and best practices. On behalf of Grant Thornton's partners, I invite you to join the Board Governance Institute Education Forum. A membership form is provided in the appendix of this survey report. Membership benefits include timely alerts on emerging accounting, audit, tax, regulatory, and governance issues; invitations to exclusive seminars; and access to our Board Governance Institute Web site. The Web site includes extensive governance resources, such as *ForwardThinking* — a newsletter that highlights board governance “best” and “next” practices.

If you have any questions regarding this survey, or any other topic, please feel free to contact your local Grant Thornton partner or manager, or me directly at Frank.Kurre@gt.com, or 212.542.9530.

Best regards,



Frank L. Kurre
National Managing Partner of Grant Thornton's
Not-for-Profit Industry Practice



Making changes

Has your organization made any significant changes to its governance policies in the last three years?

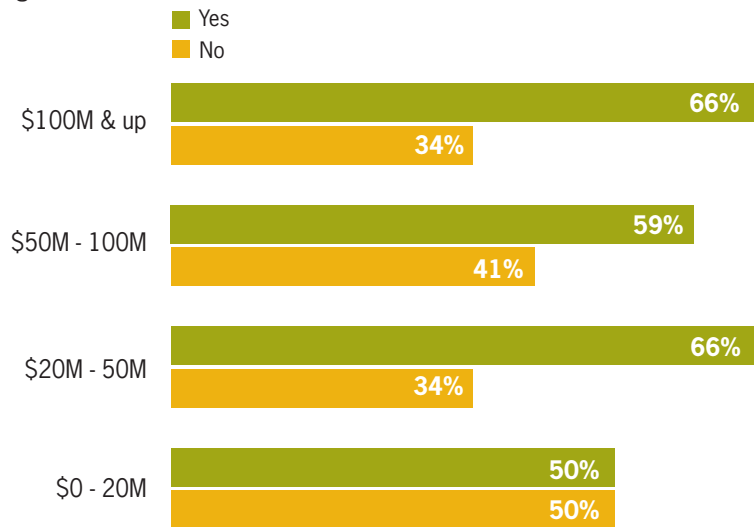
A majority (54 percent) of not-for-profit organizations surveyed indicate that they have made changes to their governance policies in the last three years, reflecting the increased need for governance and accountability many organizations are experiencing.

Changes are much more likely to have occurred in larger not-for-profit organizations that have access to more expertise and information, as well as more extensive stakeholder expectations. Over time, changes are occurring in smaller organizations, but at a slower pace.

Two-thirds of organizations with budgets of \$100 million or more have made governance policy changes, compared to 50 percent with budgets of \$0-20 million.

Governance policy changes

By budget size



“Well-developed governance policies that are properly implemented set the most effective not-for-profit organizations apart. These organizations truly live the concept of serving the ‘Greater Good’ and demonstrate proper stewardship in all that they do. They seek to implement best practices and yearn to understand emerging issues and ‘next’ practices.”

Frank L. Kurre

Grant Thornton

National Managing Partner, Not-for-Profit Industry Practice

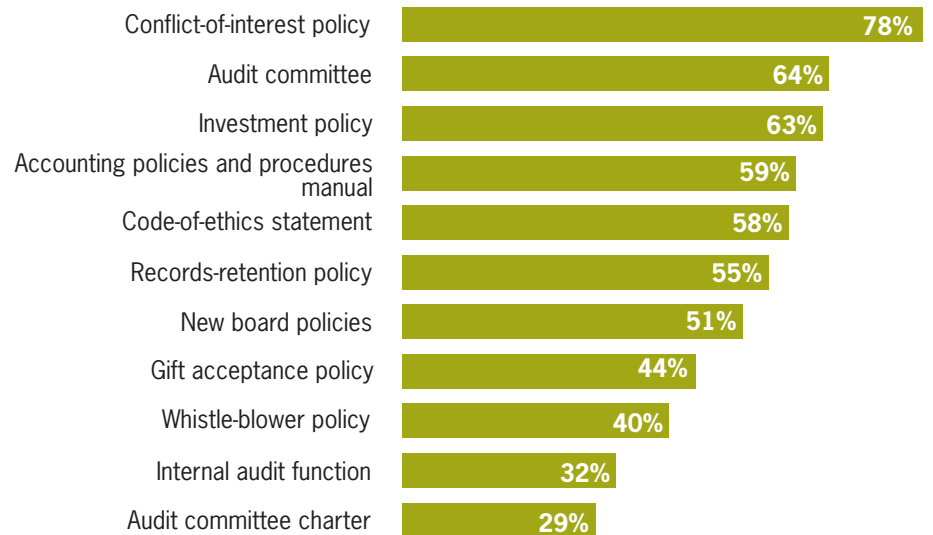
Which, if any, of the following does your organization have?

Not-for-profit organizations continue to implement new policies, procedures and controls to ensure sound governance. According to the survey, more than three-quarters (78 percent) have a conflict-of-interest policy, compared to 67 percent last year; 64 percent have audit committees, compared to 60 percent last year; and, in line with last year's findings, 58 percent of the organizations surveyed have a code-of-ethics statement.

Because of heightened interest about alternative investments, this year's survey respondents were asked if they have an investment policy: Almost two-thirds (63 percent) have such a policy in place.

Many not-for-profit organizations are establishing new internal audit functions or are enhancing existing functions to give the board and stakeholders more confidence in the organization's internal controls over business risk, compliance and financial reporting. Almost one-third (32 percent) of the survey respondents report that they have an internal audit function — a percentage that is likely to continue to increase in the future. It is also likely that the trend of outsourcing an internal audit function (i.e., organizations hiring an outside professional audit firm to provide internal audit services) will grow.

Board committees, policies



Policies

What is the most important task of your board today?

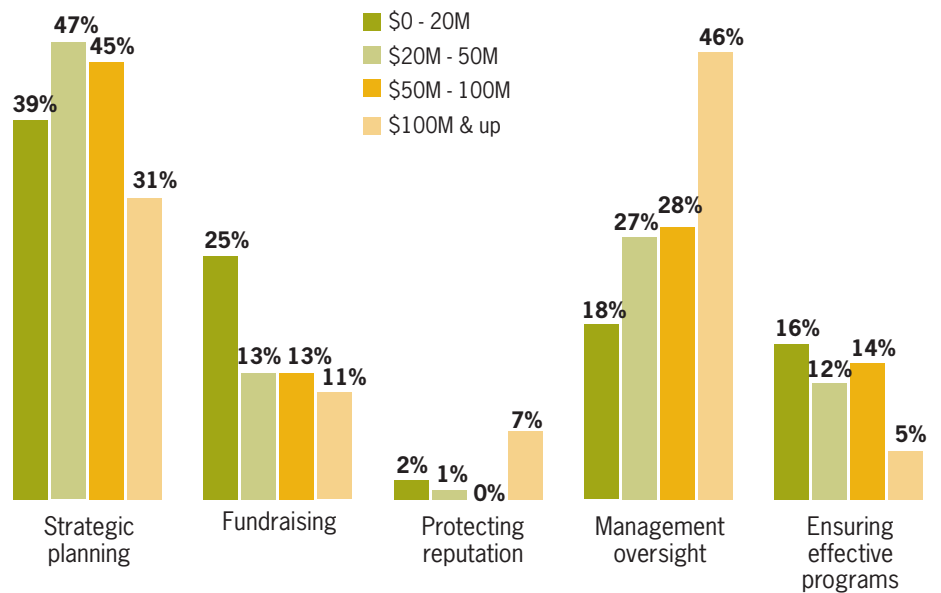
The board has certain key responsibilities that are essential to an organization's success. Four out of 10 survey respondents say strategic planning is the board's most important task, and 22 percent say fundraising and oversight of management are the board's most important tasks. For 14 percent of respondents, ensuring effective programs is most important and, surprisingly, only 3 percent say that protecting the organization's reputation is the board's most important task.

Looking at the findings by size, oversight of management is most often cited (46 percent) among organizations with budgets of \$100 million or more. Management is often responsible for strategic planning in larger organizations, which is likely why strategic planning falls lower (31 percent) among this group.

Fundraising is a more important task among boards of organizations with budgets of \$0-20 million (25 percent), since the revenue streams of smaller organizations are, in many cases, less likely to be established and reliable.

Most important board task

By budget size



“Demands on not-for-profit board members continue to mount. Meeting these demands requires a commitment of time and expertise, a commitment to shaping the direction of the organization, and a commitment to protecting the interests of the people who support the organization and are served by it.”

Larry Ladd
Grant Thornton
National Higher Education Practice Director

If your organization has a conflict-of-interest policy, who signs it?

A conflict-of-interest policy protects the independence of board members, management, staff, the external auditor, and other vendors, so that each entity performs only its role and is not compromised in any way.

Consistent with the 2005 survey’s findings, nine out of 10 (89 percent) respondents require their board members to sign a conflict-of-interest policy. Half of survey respondents require executives to sign the policy — an increase from 43 percent in 2005 — and 36 percent require all employees to sign.

Who signs the conflict-of-interest policy?

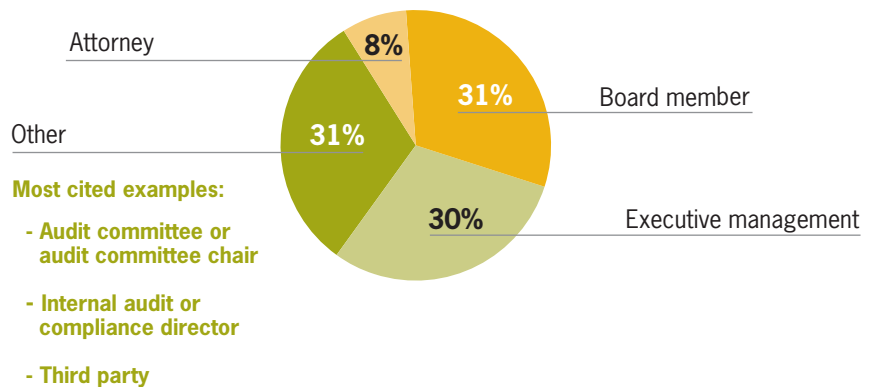


Who are whistle-blower complaints submitted to in your organization?

Whistle-blower policies provide a channel through which employees can anonymously report concerns regarding internal controls and financial reporting. Three out of 10 survey respondents with a whistle-blower policy say a board member (31 percent) or a member of executive management (30 percent) receives the complaints. And, 8 percent say they are submitted to legal counsel.

Among the 31 percent who cite that complaints go to “other” sources, the most cited examples include the audit committee or audit chair, internal audit or compliance director and a third party.

Who are whistle-blower complaints submitted to?



Board structure

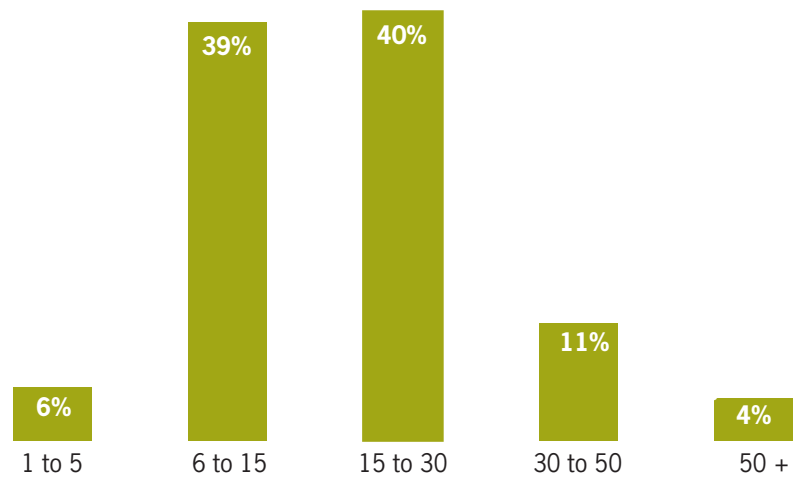
How many directors/trustees serve on your board?

Consistent with findings from the 2005 survey, 39 percent of respondents say they have 6 to 15 board members and 40 percent have 15 to 30 board members.

Between 6 and 30 board members is considered to be an appropriate number for the majority of organizations. On the lower end of the spectrum, fewer than five members is generally considered too few to function effectively.

Some larger organizations can, however, have more than 30 board members as a result of including significant donors on the board to assist in fundraising. These boards often put most of the governance responsibility on the executive committee, which ensures effective management and governance.

Number of directors/trustees



“Whether the board is composed of five or 30 members, managing the makeup, skills and education of the board should be an ongoing process. Board members need to consider not only the current composition of the board, but also plan for future membership and leadership, while evaluating overall board effectiveness.”

Kim McCormick

Grant Thornton

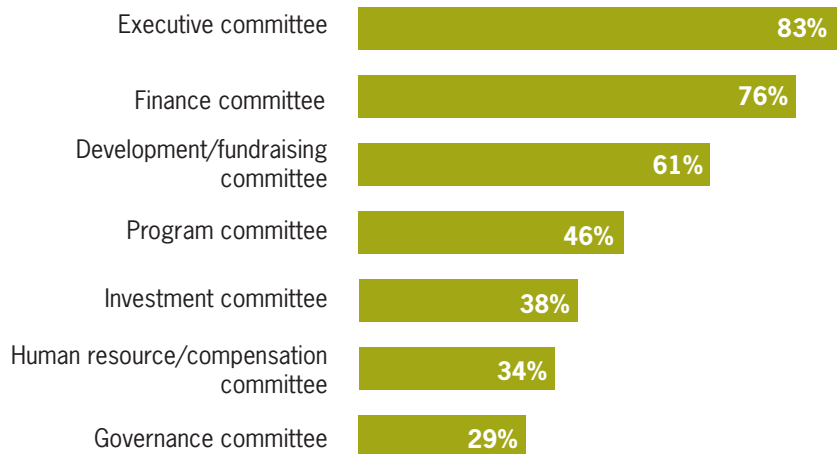
Assurance Partner and West Region Not-for-Profit Practice Leader

Which of the following board committees does your organization have?

Boards generally appoint committees to focus on particular areas of board responsibility. Because committees are essential subsets of the full board, they can devote a good deal of time to an issue before bringing it to the entire board — maximizing the effectiveness of the time that the full board spends on an issue.

More than eight out of 10 (83 percent) survey respondents have an executive committee, 76 percent have a finance committee and 61 percent have a development/fundraising committee. As referenced in the “making changes” section on page three, 64 percent of not-for-profit organizations also have an audit committee.

Board committees

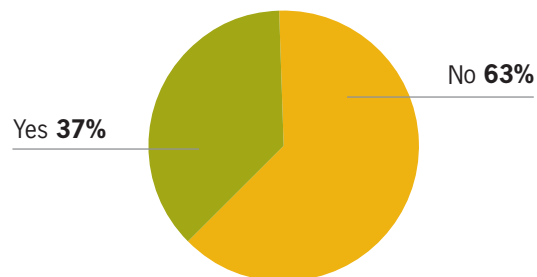


Does your board perform an annual self assessment of its performance?

Self assessments can help boards determine how well they are carrying out their responsibilities and identify areas in need of improvement.

While only 37 percent of survey respondents say they do perform self assessments, this is an area that is beginning to build momentum in the not-for-profit industry. The fact that these boards are taking the time to perform self assessments indicates a desire for greater accountability.

Annual board self assessment

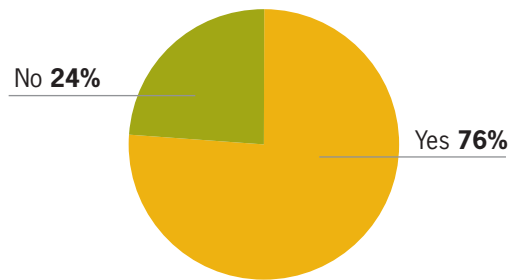


Do your board members/trustees have term limits?

Three-quarters (76 percent) of survey respondents say their board members or trustees do have assigned term limits.

Term limits have many associated benefits, including an increase in new ideas and different perspectives, a lower risk of the board becoming too closely aligned with management, and the opportunity to invite new board members who have experience in areas the board is lacking.

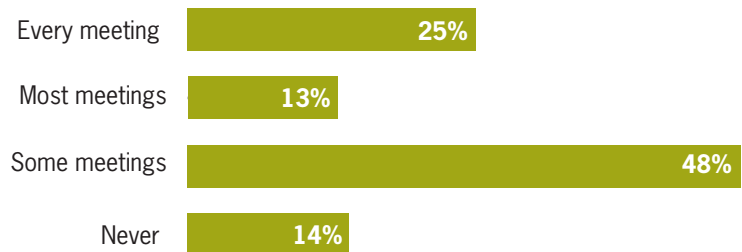
Board member term limits



How often does your board meet in executive session?

Over the past four years, there has been a significant trend toward the use of “executive session” for board and committee meetings. Executive session is that portion of a board or committee meeting during which non-board members are excused and board members have an opportunity to discuss issues among themselves.

Executive session



Eighty-six percent of the survey respondents’ boards meet in executive session during at least some meetings. Incorporating executive session into all board and committee meetings as part of the standard agenda avoids causing undue stress to management. Many organizations have come to consider the use of executive session as a best practice.

Audit committee

If your organization has an audit committee, who does it include?

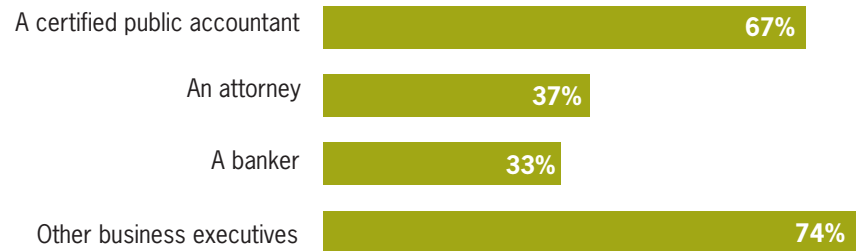
Sarbanes-Oxley encourages at least one financial expert be included on public company audit committees. While not-for-profit organizations are not required to follow the same standard, a financial expert — preferably a professional auditor with significant not-for-profit industry specific skills — has the expert knowledge of accounting, controls and risk management that are critical skills needed for effective audit committees.

Two-thirds (67 percent) do include a certified public accountant on their audit committee — the same percentage as 2005. Almost four out of 10 (37 percent) include an attorney and 33 percent include a banker on their audit committee.

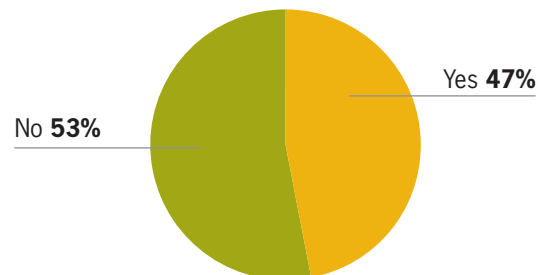
Does your auditor meet with the full board of directors/trustees?

Almost half (47 percent) of survey respondents say their auditor meets with the full board. As a best practice, the organization's audit partner should attend a full board meeting once a year to briefly present the audit results and be available for any questions.

If you have an audit committee, does it include...



Auditor meeting with the full board of directors/trustees



How often does your audit committee or appropriate board committee meet with your auditor?

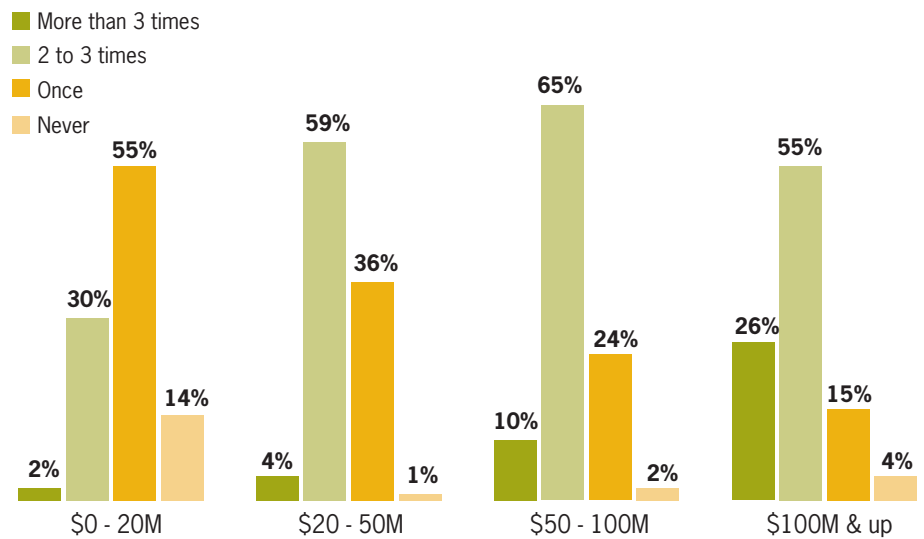
Forty-six percent of survey respondents meet with their auditors once a year and 38 percent meet two to three times a year. A full 10 percent, however, say they never meet with their auditors.

More than half (55 percent) of organizations with budgets of \$0-20 million meet with the auditor once a year, while those with budgets of \$20-50 million (59 percent), \$50-100 million (65 percent) and \$100 million or more (55 percent), meet with the auditors two to three times a year.

To be effective, audit committees should meet with their auditors at least twice a year — once to review the plan for the external audit and again to receive the results of that audit. Many committees also meet with the auditor at other times to review their assessment of the organization’s internal controls and risk management.

Frequency of auditor meeting with audit committee

Per year (by budget size)



“Overseeing the audit process is not an easy task for even the most well-equipped board or audit committee. To ensure expectations are in line on both sides of the process, boards should meet with the external auditor at least twice a year. These meetings provide an invaluable opportunity for the board to raise questions or concerns with the auditor.”

Frank Jakosz
 Grant Thornton
 Assurance Partner and Midwest Region Not-for-Profit Practice Leader

Independence

Who in your organization is responsible for hiring and terminating the audit firm and determining the scope of work?

Under Sarbanes-Oxley, the audit committee or the board is responsible for hiring and overseeing the work of the external auditor. Although not-for-profit organizations are not required by law to follow this policy, 40 percent say the audit or other appropriate committee is responsible for overseeing the audit firm, and 35 percent say the board manages this process. Looking at survey findings by size, only the smallest organizations are likely to say the board hires, oversees and terminates the audit firm. All other segments say the audit or appropriate committee is responsible for these duties.

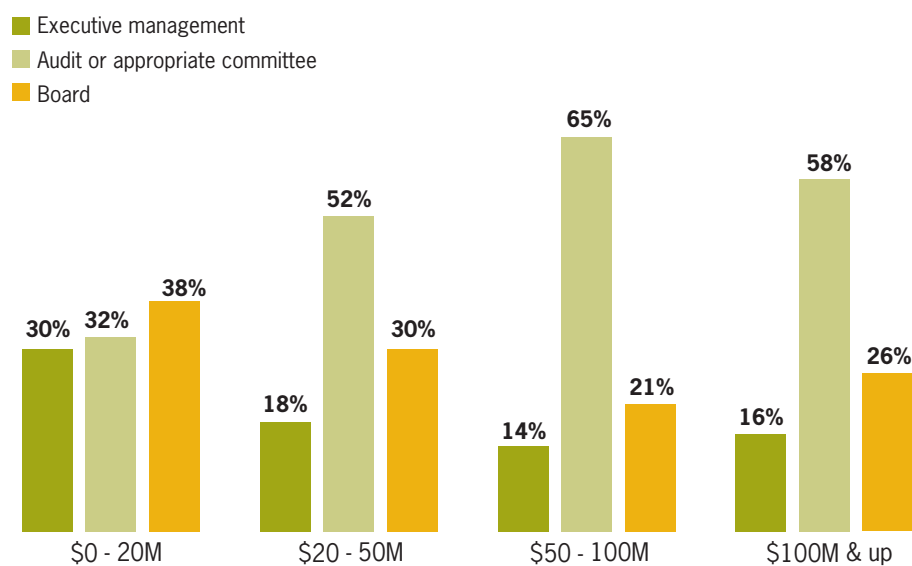
Has your audit committee established a policy requiring their pre-approval before engaging the audit firm to perform any special projects beyond the scope of the audit?

Having audit committee pre-approval for work outside the scope of the audit demonstrates that the board and its audit committee are the auditor's client. Consistent with findings from the 2005 survey, more than half (53 percent) of survey respondents require audit committee pre-approval of non-audit services. It is surprising, however, given the intense focus on independence that this percentage is not even higher.

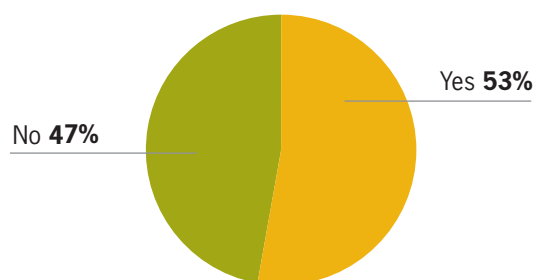
The audit committee should monitor the independence of the external auditor and

Engaging the audit firm

By budget size



Special project pre-approval



avoid any real or perceived conflicts with the auditor's primary task. Any non-audit services create the possibility of impaired independence and thus should be reported to and approved by the audit committee.

Some audit committees require pre-approval of any additional services performed by the external auditor above a certain dollar threshold (i.e., \$25,000).

Appendix

About Grant Thornton LLP

Grant Thornton is dedicated to serving a broad range of not-for-profit organizations, including colleges and universities, trade and professional associations, religious organizations, social and human service organizations, foundations, and health care organizations.

As a member of one of the largest international accounting and business advisory organizations, Grant Thornton offers a complete array of services designed specifically to help our not-for-profit clients meet their financial and business needs.

In addition to providing audit and tax services, our professionals help not-for-profit organizations improve their business operations, develop strategic plans, and assess information technology systems.

We also provide business advisory services for mergers and alliances, compensation and benefits planning for executives, risk management, internal audit consulting, and governance consulting for boards of directors.

The *Grant Thornton National Board Governance Survey for Not-for-Profit Organizations* is published by Grant Thornton LLP. It is not intended to answer specific questions or suggest suitability of action in a particular case.

For more information on the survey or Grant Thornton's not-for-profit industry practice, visit our Web site at www.GrantThornton.com/nfp.

About the survey

Grant Thornton conducted the *Grant Thornton National Board Governance Survey for Not-for-Profit Organizations* Sept. 1 through Sept. 22, 2006. Responses to the Web-based survey were received

from 960 not-for-profit chief executive officers, chief financial officers and board members of higher education institutions, trade and professional associations, social and human service organizations, religious

organizations, cultural organizations, health care organizations, and foundations. Respondents cover 46 states, the District of Columbia and 14 percent from outside the United States.

Survey respondents

Industry

Social or human services organization	39%
Trade or professional association	16%
Higher education	15%
Health care	10%
Cultural organization	10%
Religious organization	5%
Foundation	5%

Organizations' total annual budget

> \$100 million	8%
\$50-100 million	7%
\$20-50 million	11%
< \$20 million	74%

Title

President/chief executive officer/ executive director	33%
Chief financial officer/finance director	23%
Board member	9%
Controller	6%
Chief operating officer	4%
Board treasurer/finance committee chair	3%
Audit committee chair	1%
Other	21%

Offices of Grant Thornton LLP

National Office

175 West Jackson Boulevard
Chicago, IL 60604
312.856.0200

International

175 West Jackson Boulevard
Chicago, IL 60604
312.856.0200

National Tax Office

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

Arizona

Phoenix 602.474.3400

California

Irvine 949.553.1600
Los Angeles 213.627.1717
San Francisco 415.986.3900
San Jose 408.275.9000
Woodland Hills 818.936.5100

Colorado

Denver 303.813.4000

Florida

Miami 305.341.8040
North Palm Beach 561.684.9496
Orlando 407.481.5100
Tampa 813.229.7201
Weston 954.768.9900

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

Nevada

Reno 775.786.1520

New Jersey

Edison 732.516.5500

New Mexico

Albuquerque 505.855.7900

New York

Long Island 631.249.6001
New York - Downtown 212.422.1000
New York - 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

Dallas 214.561.2300
Houston 832.476.3600

Utah

Salt Lake City 801.531.6888

Washington

Seattle 206.623.1121

Washington, DC

Alexandria, VA 703.837.4400
McLean, VA 703.847.7500
Washington, DC 202.296.7800

Wisconsin

Appleton 920.968.6700
Fond du Lac 920.906.1940
Madison 608.257.6761
Milwaukee 414.289.8200

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