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Non-Profit vs For-Profit Governance

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Food for thought. What is the most fundamental difference between for-profit and non-profit boards of directors - that you have never considered?

By Dennis J. Cagan

I recently attended a conference as a member of the Institute for Excellence in Corporate Governance, part of the Naveen Jindal School of Management, at The University of Texas at Dallas. One of the panels was on the differences between boards of non-profits and for-profits. During the presentation a discussion ensued about what to term a 'non-profit.' Do you call them a 501(c)(3), a non-profit, a not-for-profit, a community service organization, or a charitable organization?

The panel and audience tossed around a variety of terms. One participant noted that she had been on some boards of companies that should have been for-profit, but were in fact non-profit - e.g. not profitable. Perhaps not-for-profit (NFP) would be better? Which term do you like? Regardless, since profitability is not the best differentiator between the two, what is? More importantly, what is the most fundamental difference between the two that effects their respective governance? Why are there so many different governance models among NFPs? What is the difference that is the root cause of management and board issues? And, why is it almost always left un-addressed in establishing and governing these organizations that are a vital part of our communities?

OWNERSHIP

In any company, public or private, you can name every single person or entity that owns shares (or units, percentages) in the enterprise - there legally must be a list. In any NFP, try to name one single owner. Or ask two people who *owns* the entity. If the ownership of a firm is the beneficiary of the fiduciary responsibilities of the board of directors that oversees the organization, and as commonly accepted

if the board reports to the owners, then who does the board of a NFP actually report? You could argue that a governmental NFP, like a school district, is 'owned' by the citizens in that district. You could argue that an NFP like United Way is 'owned' by everyone in the community. Or, you could argue that no one person or group 'owns' either one. How often have you been on the board of an NFP when this has been discussed?

CONCLUSION

It's clear in a public or private company exactly who the shareholders are, and therefore who the board owes its fiduciary responsibilities to. However, with a 501 (c)(3) rarely are directors elected by anyone other than the board itself (although sometimes). Often new nominees are presented by other directors or even the Managing or Executive Director/President/CEO. This has resulted in a certain lack of uniformity in NFP governance. Which has in turn led to an overwhelming number of dysfunctional situations, particularly in the case of younger or smaller organizations. If a board that has the responsibility to oversee an organization, does not know who it reports to, and whom it owes its fiduciary responsibility, how can it really determine on an organizational and operational level, how a decision effects its stakeholders? There are of course ways of clarifying this through bylaws, policies, communications, licensing requirements and more, however the issue should be identified and rectified to enable these valuable community service organizations to do the best job possible in delivering their benefits to the causes and people that need them.

