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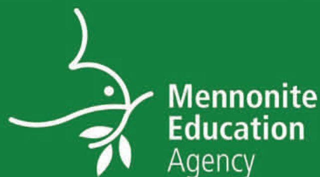

stepping up

for board members of Mennonite educational institutions

The CEO appraisal: A vital process

By Rick Stiffney, president/CEO, Mennonite Health Services Alliance

The quality of the board-CEO relationship is crucial to the well-being of a dynamic, growing organization. Seldom, if ever, can an organization be highly successful if the board-CEO relationship is dysfunctional. I know many CEOs who want good feedback about their work. I have worked with CEOs who had been asked to resign or were fired because of implicit and unarticulated board expectations that should have been addressed in an earlier appraisal. I have interacted with numerous board chairs who believe it's important to do some kind of regular appraisal but aren't sure where to begin.

A well-designed executive appraisal can contribute to a strong and healthy relationship between the CEO and board. In addition, a thoughtful appraisal will usually lead to more effective long-term organizational performance. A poorly designed and badly facilitated process can diminish trust and performance.

There is some difference of opinion about the content of executive appraisals. Some argue that the expectations of the CEO are essentially summed up in performance expectations for the organization as a whole—if the organization is hitting all its performance targets, then the CEO is doing an acceptable job. Others suggest that expectations of CEO performance are broader than corporate performance measures. However, the key issue is that a well-designed executive appraisal provides an opportunity to review performance against agreed-upon expectations or goals as determined by the board and the CEO. An effective appraisal results in clarity on key expectations for the future.

A well-designed process provides an opportunity for all board members to offer their input. This process should include a self-assessment by the CEO as well as comments by the CEO on the work of the board. An effective CEO appraisal sets an example for senior staff that accountability, openness to feedback, and ongoing improvement are important hallmarks for the organization.

Here are some suggestions for improving the practice of CEO appraisals:

Schedule the appraisal on a regular basis. Some type of executive performance review is important at least once a year.

Think no surprise. An executive appraisal is not an occasion to blindside a CEO with concerns that should have been discussed earlier. The ongoing use of executive sessions of the board with the CEO as well as a healthy relationship between the board chair and CEO can diminish surprises. "Surprises" are typically a sign of unhealthy communication.

Designate leadership. It is essential that the board clarify which board member(s) will provide leadership for the appraisal process. Such board leadership demonstrates the board's support of the CEO and its commitment to excellence. It is

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Tidying up your management letter

By Lynn K. Suter, attorney-at-law, Lenhart Obenshain PC

The Internal Revenue Service has joined the regulatory efforts to enhance corporate governance practices—this time, in the area of nonprofit governance. *The new Form 990, released in December 2008, now asks whether the nonprofit has a written conflict-of-interest policy, whistleblower policy, and document retention and destruction policy.* The IRS does not *require* these policies, but the wise nonprofit organization should adopt them. Among other reasons, the failure to have these policies may be noted on your auditor's letter to management

Both the IRS and the American Institute of Certified Public Accountants (AICPA) have released a sample conflict-of-interest policies. Your organization's policy should include the key IRS provisions, but check with your outside auditors to see if they will expect it to also include the AICPA provisions.

The IRS sample conflict-of-interest policy focuses on transactions with an "interested party" (officer, director, or board committee member) and on compensation decisions. It provides a process for approval of a transaction with an interested party after certain due diligence is conducted. The sample policy also bars officers and directors from voting on their own compensation. Interested parties must annually affirm that they understand the policy and agree to comply with it. The organization must conduct a periodic review to prevent violation of tax-exempt status, including verifying that compensation reflects arms' length standards and reviewing conflict transactions.

One drafting tip. Consider including language in your conflict-of-interest policy such as, "This policy is intended to supplement but not replace any applicable state and federal laws governing conflict of interest applicable to the [name of organization], including without limitation, [cite state law statute]" in order to avail your organization of any "savings" provision in the law. For example, in Virginia, even a conflict transaction that has not been properly handled will not be voidable if it was nonetheless "fair to the corporation." In other words, as you articulate your good process for dealing with conflicts, be sure to keep intact any statutory safety net. Sample conflict-of-interest policies can be found at http://www.irs.gov/instructions/i1023/ar03.html (See Instructions for Form 1023 - Additional Material) and http://www.aicpa.org/audcommctr/toolkitsnpo/Independence_and_Related_Topics.htm

A whistleblower policy either invites or requires employees (sometimes volunteers, directors and others) to report suspected violations of law or policy, and provides a chain of command for reporting and investigation. Importantly, the policy states that retaliation against the "whistleblower" will not be permitted. Since retaliation against whistle-blowers in federal investigations is now illegal under Sarbanes Oxley, it is important for organizations to understand the policy and its implications. The IRS has not published a sample policy, but AICPA has. It can be found at http://www.aicpa.org/audcommctr/toolkitsnpo/Whistleblower_Tracking.htm.

A document retention and destruction policy delineates the length of time different types of documents should be retained. If followed, it helps protects the organizations from being accused of destroying records that the accuser believes would incriminate the organization. Its more benign purpose is to bring clarity to the recurring "Should we keep this?" question. Sample policies are available on the web, i.e., www.achsnatl.org/ASAE_Jacobs.doc.

Stepping Up
July 2009

Editor: Rachel Nussbaum Eby
Design: Design by raNE

This newsletter is produced by Mennonite Education Agency for board members of Mennonite educational institutions and is distributed by e-mail. **The mission of *Stepping Up* is...**

to provide some insights, suggestions and resource ideas to help strengthen boards and emphasize those unique features that reflect Anabaptist-Mennonite theological understandings.

If you have questions or comments about the information in *Stepping Up*, feel free to e-mail the editor: rachelne@MennoniteEducation.org. *Stepping Up* can also be viewed on the MEA Web site: www.MennoniteEducation.org/BoardDevelopment.

The CEO Appraisal

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difficult for CEOs to lead their own evaluation process and becomes a burden if asked to do so.

Use professional resources. Although occasionally a review can be handled informally and in-house, the use of well-designed resources adds depth and quality to the appraisal process and its outcomes. In some cases, the engagement of an external resource person to deepen the quality of communication can be helpful.

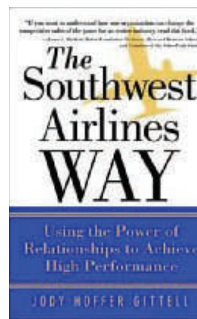
Request a CEO self-assessment. The appraisal process should provide a way for the CEO to assess his or her own performance. Such a self-appraisal will include evaluating performance against expectations, stating potential goals going forward, outlining needs for ongoing growth and development, and offering ideas on how the board might strengthen its own performance to complement the performance of the CEO.

Focus on results. Too many evaluations result in affirmation but offer little clarification about specific expectations going forward. The point isn't to add to the volume of expectations but rather to be very clear about expectations and then focus on them during the next evaluation.

Consider thoughtful use of 360 assessments. A 360 assessment provides an opportunity for senior staff to provide some input. Opinions differ on whether such involvement is appropriate. In most cases, occasional engagement of direct reports can be helpful. In general this should not be done more frequently than once every three years. Further, if it is done, it must be done in such a way that senior staff has no reason to believe that there will be any recrimination. Their contribution must be treated with utmost confidentiality and be handled by the board.

Link compensation. Most CEOs of not-for-profit organizations are not motivated primarily by compensation. However, neither is compensation irrelevant. Opinions vary on the issue of linking compensation to specific performance results (performance-based compensation). However, good practice suggests holding discussions about compensation and benefits soon after the appraisal has been conducted.

HIGHLIGHTED BOOK



Review by Carlos Romero, executive director, MEA

I was intrigued by this book by Jody Hoffer Gittell. Like so many *Stepping Up* readers, I have traveled on many airlines and naturally compare and rate my experiences. I picked up the book since I was curious about what Southwest had done to make it the only airline that has consistently made a profit.

The book highlighted **11 basic principles** that served as the core of the organization's leadership and management philosophy. The principles are:

1. Lead with credibility and caring
2. Invest in frontline caring
3. Hire and train for relational competence
4. Use conflicts to build relationships
5. Bridge the work/family divide
6. Create boundary spanners
7. Measure performance broadly
8. Keep jobs flexible at the boundaries
9. Make unions your partners, not adversaries
10. Build relationships with your suppliers
11. Maintain financial reserves

I discovered that these principles easily translated to my work at MEA. I observed that their emphasis on maintaining quality relationships with persons of all levels and roles is quite Anabaptist. Gittell notes:

> "For Southwest's leaders, taking care of business literally means taking care of relationships. They see these relationships—with their employees, among their employees, and with outside parties—as the foundation of competitive advantage, through good times and bad. They see the quality of these relationships not as a success factor, but as the most essential success factor."

You can "look inside" this book on Amazon.

Case Study: A Not-So-Happy Hour

Excerpt from *Board Member*, a publication of BoardSource

Editor's Note: *MEA Executive Director Carlos Romero was one of three executives/board members asked by BoardSource to respond to the case study reprinted in the left column. I have only included Carlos' response in the right column.* Click here to view a PDF of the complete article.

Every fourth Friday evening, Betsy Koltrane Jones, chief executive of a regional nonprofit resource center, met for drinks with a group of other nonprofit chief executives to decompress. Serving as a chief executive can be a somewhat lonely undertaking, and Betsy appreciated the support she received from her peers.

At the most recent "happy hour," Ralph, chief executive of a local food bank, shared an experience that involved one of his organization's board members. Little did he know that his story would strike a nerve with everyone at the table.

"I lost a key employee this past month," Ralph said. "Laura, my chief financial officer, left the food bank. It seems that one of my board members was quite impressed with her, because he offered her a position with his firm at a salary the food bank couldn't come close to matching."

"Hmm," said Carolina. "I have a board member who asked one of my staff members — during the course of a private dinner party they both happened to be attending — if I was a likeable person."

"One of my board members — a gentleman who happens to serve on several local boards — called me a few months ago asking for the contact information for one of our major donors," chimed in Rose. "I later learned that he asked that donor to support one of the other organizations he serves."

"We have a board member who asks our human resources director to hire one of her relatives or friends every time we post a job opening. These 'candidates' never come close to meeting the minimum qualifications. It's a waste of our time to go through the process of interviewing them," added Daniel.

"You're all familiar with our annual golf tournament," said Tomas. "Well, the board member who chaired the event last year requested that he be included in the 'private' lessons with a PGA pro awarded to the tournament's winner. He felt he 'deserved' the lessons due to his hard work on behalf of the organization."

"Don't let your IT expert attend a board meeting," advised Chuck. "Every time ours does, he can't get out of the boardroom without members asking if they can stop by his office with their malfunctioning personal computers."

Betsy shook her head in dismay as she listened to her colleagues share one board member blunder after another. They were laughing, but Betsy could see that most of those seated around the table were frustrated by the inappropriate behavior. And yet most also felt it was better to put up with the blunders than to call attention to them. Often, they said, the individuals committing the fiduciary faux pas were among their boards' most generous members. The chief executives didn't want to risk embarrassing and perhaps offending valuable board members. Betsy, however, wasn't convinced, and that weekend, she mulled over the following question: How could she, the nonprofit resource center, and her peers go about putting an end to these and other inappropriate — and sometimes unethical — behaviors?

Response:

Having a clear understanding of how board members should interact with an organization's staff is an important characteristic of an effective board, yet this is one of those areas in which challenges and frustrations are very common. In situations like this, it is always most effective for the chief executive to be able to refer to clearly written governance policies. Betsy should inform her colleagues of their organizations' need for a policy that speaks to the accountability of the chief executive. At my agency, one of our policies states the following: "The board will not give direction to persons who report directly or indirectly to the Executive Director."

The organizations should also develop board member codes of ethics and conflict-of-interest policies, which should be reviewed annually by the board and be part of the orientation process of new members. Having clear policies would allow the chief executives mentioned [in the case study] to communicate with their board chairs and then have conversations with the board members who acted inappropriately. When communicating with board members concerning their behavior, the board chair needs to be involved. If the behavior relates to the chair, the board policies should speak to the process the chief executive needs to follow to confront the situation.

Many times this type of behavior is the result of ignorance rather than malice. Nevertheless, the behavior needs to be addressed as part of an ongoing process of making a board stronger.

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