



Governance and management in the not-for-profit sector

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Introduction

This is my final official lecture as Mercers School Memorial Professor of Commerce, an honour which has for the most part been hugely enjoyable. I shall miss Sir Thomas stern gaze at my back, and your penetrating questions from the front, as well as my guests constant ability, from the side, to find important aspects of each lecture topic which I had either omitted or underemphasized, or just, in their view, got wrong. If that makes me the meat in a three dimensional sandwich, it makes me wonder why I ever took on the task. I already miss my greatest historical heroine, Queen Elizabeth the First, over there on the right, who was once described to me by a distinguished American businessman as the best Chief Executive Great Britain has ever had. In that case I'm not sure who her Chairman was, and she certainly had an effective way with her NEDs, either (so rumour has it) selectively seducing them, and/or removing their heads. Now there's an interesting idea for NED mind concentration for the recently announced task force on the role of the NED and a dilemma for those offering D&O (Directors and Officers) insurance. My paranoia has on occasions only been controlled by the thought of the vast well, one or two online audience out there who can do whatever they want in front of their screens, but to me they are the most docile, best behaved of attendees, who never ask a difficult question, snore loudly in the second row, ask unintelligible questions from the back or leave noisily and pointedly just as the lecture reaches its denouement. We seem to date to have avoided dossiers, although some might believe that there are few more inviting, warm and attractive places for a chap down on his luck to lay his head than in this lovely little hall, to the comforting drone of the Professor of Commerce on the topic of Regulation and such matters. Nonetheless, there is nothing like a live audience and I salute those here tonight but we must recognise the importance of those online participants, who represent perhaps the single greatest change in the conduct of the College since Sir Thomas original inspired vision for the propagation of the late 16th century New Learning to the educated man in the street.

[Introduce guests]

My interest in governance and management in the not-for-profit sector has stemmed in the most part from the modern equivalent of the transition from the Fifth to the Sixth Age of Man; from the fair round belly with good capon lined to the lean and slippered pantaloons from a fulltime wage slave to what is called (in my mind rather unattractively) plurality; from a single full time occupation, to a variety of interests. In my case and I suspect in many others it has arisen from long held but suppressed interest in education and the arts, as well as a more vague desire to give something back as a quid pro quo for a professional career which has for the most part treated me well. And so I have a range of non-executive positions in the arts, education and charitable worlds, which not only provide great pleasure, but also a fascinating insight into the way such institutions function and are governed, to go alongside my own academic and professional work as a non executive in the commercial sector. As you now see, my own experience is somewhat similar to that of my guests, although of course Robert is a fulltime CEO of a major charity.

But of course social, legislative and political change have hugely increased the opportunities for NEDships/Governorships/Council memberships of an ever increasing range of not-for-profit institutions: for

example health trusts, schools, universities and colleges of all types, charities, quangos, arts organisations and cooperatives. As a result people, of varying socio-economic class, education level, trade and/or profession, many of whom would only a few years ago never have dreamt of taking on such roles, are assuming positions of importance, responsibility and gubernatorial (my spell-check software has thoroughly approved the use of this word) significance. Thus Jack and I are not necessarily stereotypes of the average board member of a not-for-profit organisation, although Roberts is probably more typical of the CV of the CEO of an important charity these days.

One can conclude that a large number of not-for-profit NEDs (from now on I shall use this acronym to describe anybody who sits on a board or council) have had no prior experience of board level governance. They will in most cases have important skills, which will be of great value if exploited properly, but for many joining such a board is a totally novel experience. They well may be sympathetic to the Chairmans greeting to me on my first appointment as a director: Welcome to the Board and to the thankless task that lies ahead. And so, in that case, it proved, although I always hope that first time board members soon overcome their qualms and get a lot of fun and satisfaction out of the experience.

Boards have much in common

It is a common mistake to believe that boards of not-for-profit organisations are in some way radically different from their commercial counterparts, but the fact is that the differences, if they exist are marginal and nuanced rather than fundamental. Take stakeholders. Stakeholder is of course a buzz word that has cropped up regularly in my lectures and which refers to those who have an interest in the operations and success of the institution in hand. Whilst it is surely true that they will vary in terms of identity and emphasis, many stakeholders will nonetheless be common to both sides: employees, community, environmental interests, suppliers, where appropriate customers. Yes, even customers, as for instance in educational establishments where it is increasingly clear that competition exists and is even being encouraged, so that where the provision of education is seen as being a service to students with a choice. And of course some of these stakeholders in common may move to top priority in the case of not-for-profit institutions formed to help them, as with community and environment. Indeed, every organisation should have one principal stakeholder, not necessarily much ahead of the others, but one which is clearly recognised in the goals of the organisation. Boards need regularly to pause, particularly when faced with difficult decisions and analyse the issues which confront them in the light of the priorities posed by that principal stakeholder.

Now, conventionally, shareholders will be seen, even in todays politically correct world, as the principal stakeholder in commercial organisations, and rarely exist in any other than a nominal form in not for profit organisations. But wait a moment. Examine the accounts of virtually any of the latter and note that there is in most cases a surplus. Indeed in the majority of cases it is necessary, desirable and an aim to create a surplus not always substantial in order to meet the objectives of the organisation, for instance to invest in fixed assets such as IT systems and to guard against future contingencies. So we have the ironic proposition that whilst no such organisation would dream of declaring itself For Profit, a substantial number, indeed possibly the majority, would, if pushed, have to say that they were, in part at least, For Surplus. And in accounting terms, the difference between profit and surplus is a rather subtle one. Why then is generation of a profit in a commercial organisation usually deemed more motivating than generation of a surplus in a not-for-profit one? I shall return to this topic later on.

Moving on to other areas of common ground, it is in my experience quite a usual failing of the not-for-profit sector, and to a lesser extent of commercial entities that their boards concentrate too much on mundane operating matters, even nit picking (a common hole in which to fall with directors of limited board, and narrow, experience of the subject in hand); or are mesmerised to the point of its occupying the bulk of all board meetings by the often wordy requirements of the statutory framework in which their organisation operates.

Yet both of these tendencies belie what is usually considered to be the prime role of any board, bearing in mind the priorities of its stakeholders, namely the setting and supervision of the implementation of strategy for the institution. All boards should regularly review their strategic objectives and ensure that their short term activities and objectives are prioritised to achieve them. This is not usually as difficult in commercial organisations as it is in not-for-profit institutions, where many board members are not trained to think strategically, and where there is even a tendency for management to imagine that strategy is entirely their province and the role of the board is to make sure that the entity remains solvent and does not break the law; put bluntly not to make too much of a nuisance of itself.

That is not to deny all boards the requirement to supervise the day to day operations of the organisation, but this should, unless major problems occur, be very much at a high level and designed to satisfy directors that all is moving in the right direction, within an agreed framework; and not to take over what they have hired and paid executive management to do. Of course there is a balance to be struck here. On the one hand NEDs may have to act fast if there is an operating issue of heavy significance, or if executive management gets ahead of the board or exceeds its mandate and in the latter case, there are as many examples of the detrimental effect of strong willed managers on both sides of the commercial/ not-for-profit divide, always a major worry for competent boards. But it is equally dangerous to be too laid back.

Indeed, boards of all stripes have a major responsibility to ensure that senior management is appropriate for the tasks set them by the board. Again this is not always an easy one for inexperienced not for profit directors to grasp, particularly in its more dynamic sense, management planning and succession. In particular the term of executive appointments has been a significant current issue in governance terms, with consensus in director level jobs coming down around the five year mark with exceptions of course for commercial organisations, based on practical observations about diminishing value added, growing stale, and the need for a fresh pair of eyes. In my experience, not-for-profit organisations often exceed such a rule of thumb by allowing senior managers to stay in their jobs well into injury time, and usually by not being prepared even to plan change in the context of an individual who is perceived to be doing a good job at least for the time being.

It is also true, not least in this context, that the code of governance demanded of quoted companies and increasingly of other smaller entities in the commercial sector, reads across to the not-for-profit sector. Indeed in some cases, the quality of risk reviews by boards, for instance, the latter is ahead of the commercial sector. In addition, the usefulness and need for appropriate board committees is appreciated in both sectors, the most common being those for Audit and for Remuneration. As a footnote, the latter tends to be less well developed in the not-for-profit sector, and in particular in its common usage, not least amongst plcs, of the discussion of more strategic but sensitive management organisational issues, such as those relating to management performance, planning and term of office. Or indeed to executive malfunction where this unfortunately becomes necessary.

Nor indeed does the necessary makeup of boards differ too much between sectors, which is not surprising given the similarity of the tasks before them. There is no doubt, given the nature of human relationships and discussion an optimum number of about 8 and a maximum of 12 members, with a balance between non-executive and executive. Furthermore, just as there tends to be a range of disciplines represented on the executive side, so there is a requirement for a balance of skills and knowledge on the non-executive side. Whilst this is desirable, and eminently possible in the context of commercial entities, it is much more difficult to achieve in not-for-profit organisations who are tied to certain undesirably large sizes either by convention or by stakeholder representation requirement, or by statute.

Even so, working within these constraints, there is a requirement regularly to analyse the skills and knowledge requirements of the board, on which may be overlaid certain representational requirements of NEDs in the case of commercial companies, probably of shareholders; and of not-for-profit entities, of stakeholders of one kind or another. Indeed it should not be forgotten that the skills requirements of the latter are often very broad, only matched by the often rich and diffuse communities from which their board

members might be drawn a huge and fascinating opportunity for bringing the widest range of experience effectively to the board.

Terms of NED appointment too can be contentious. I am a strong, but occasionally flexible, supporter of a maximum of two terms of three years each, for commercial NEDs, and there are good reasons for the same being true of not-for-profit organisation: as with commercial companies, but not I hasten to add true in every case, people grow stale and/or complacent after a while, their knowledge base, and therefore potentially their usefulness diminishes, they become less than objective camping in the executive kraal, if I may verge on the non-PC. Frankly such boards, like most human organisations, need change and fresh set of eyes. Members of the audience familiar with board politics will know how even block buster bombs can be insufficient to dislodge a recalcitrant NED overstaying his usefulness, and I can assure you that the same is all too true of not for profit organisations, in my direct experience. In both cases it can take a Chairman and/or group of senior NEDs of determination and cunning, yet with considerable diplomatic skills gently to extract a well entrenched long server. In both cases the requirement and the resultant problem are similar, and the remedy is certainly identical.

This leads naturally on to the role of the Chairman, which in fact I examined in detail in a lecture during the last academic year, and which has like, or at least parallel, requirements focus in both groups. And in both cases the position plays a pivotal role in the governance and the practical efficiency of the board,. The Chairman it is, who ensures that the strategy is set and adhered to, and that the right executive team are in place to implement it; and who manages the board itself, getting the best out of its members individually, and as a whole, as well as ensuring that it properly discharges its function.

It is certainly evident that the desirable qualities of good Chairmen are not only to be found in the commercial sector, but are available from any walk of life. It raises another interesting point about interchangeability between sectors. We know that commercial people often take jobs as chairs of not-for-profit companies, and we have seen the occasional senior civil servant move from Whitehall to take important commercial chairmanships. In logic, though, could such roles as well be filled by successful figures from the not-for-profit sector: head teachers, CEOs of major charities, or Chairman of non-commercial cooperatives, for instance. There is considerable interchange below board level. Could it also be reflected at the top rung, too?

Finally in this discussion of board similarities come the knowledge issues. It is obvious that all boards have a duty to ensure not only that the information provided by management, both financial and qualitative, is useful and appropriate, but also that it is adequate. But they also have to ensure that, in addition to whatever professional and other skills and abilities they bring to the board, they also understand the work, objectives and challenges faced by the entity, commercial or otherwise, and keep themselves constantly up to date. There are a number of recent cases of corporate collapse/scandal, Enron being the most obvious recent example, where it is clear that the board either did not understand what was going on and/or were not told, and from which both commercial and not-for-profit sectors could learn. There could be a number of reasons for these failures: for instance not investing enough time and effort to get to grips with the business and its risks and opportunities at the outset and then keeping such knowledge up to scratch; and/or not asking management the right questions, and probing intelligently until satisfied; and/or not insisting that management provide the right information, properly annotated, on a regular basis. And there is beginning to be more than just a sneaking feeling that NEDs, particularly in the plc environment are simply not spending enough time at the job to do it properly. The days of reading the board papers in the train or car on the way to the monthly board meeting and then vanishing in a cloud of dust as soon as the meeting was declared closed are over although I can think of one NED stalwart who used to annoy management intensely by never reading the lovingly prepared and (we thought) highly professional papers, but always, instantly and with no apparent disadvantage, getting to the heart of the issue that we had taken many man hours to express articulately on paper.

The same challenges exist of course for not-for-profit NEDs, but with a significant twist. The vast majority of

commercial NEDs are paid, and some do nothing but NED work. If they feel that they need to put in more time to get the job done, they will be likely to get appropriate compensation. Even if they don't, they will usually take the view that they wish to do the job professionally, and that if this requires more work, then they must spare the time. On the other hand not-for-profit NEDs are usually not paid, and even when they are it is usually at a much lower rate. I have argued that the burdens of office are substantial, and not dissimilar between the two sectors, although there is probably more catching up to do in the not for profit sector than in the commercial sector. To add further burdens to their existing load, for the most part unpaid, may well be asking too much. Yet one cannot but think that requirements of NED office will call for increasing expenditure of time; and this will certainly affect some institutions in the not for profit sector, a major potential challenge for the future.

Finally in this analysis of comparatives comes training. I do not in this case mean training in relation to activities of the entity itself, although this is clearly of great importance; but training in governance, that is what it means to be a director and what responsibilities and duties fall on the shoulders of directors, as well as the other increasingly well worn features of modern boards. But it is here above all that there is most likely to be a difference between NEDs in the two camps. Governance is a developing art, and even experienced businessmen would admit that sitting on a commercial board for the first time in one's life can be a daunting experience, and that it usually takes a while to become an effective, participating member. Objectively this can require education, advice, seminars, even counselling, not least because such activities become a short cut to full effectiveness.

But how much more is this needed for people who have little senior management experience but have the potential to become very useful and contributing members of not-for-profit boards, because of their knowledge and skills base? For my firm conclusion is that there is no substitute for well thought out, appropriate, interesting and stimulating training for board initiates in the not-for-profit sector. The problems associated with obtaining it are likely to be much more associated with willingness on the part of the trainee and commitment of his/her time, than it will be a matter of financial resource, since much such training is now available free, for instance through government and other sponsored programmes. It is arguable that such opportunities should be close to compulsory in order to place all NEDs in a position to become fully contributing members. Boards should be both cold blooded and relentless about appropriate training.

So do managers

Moving to management, rather than governance, consider the following attributes:

- Leadership
- Ability to judge and motivate people
- Ability to relate to, understand, be respected by and just plain get on with other people: called in the jargon interpersonal skills
- Objective driven with Knowledge of the operation and its relevant strategic and immediate objectives
- General financial literacy

It would be far from controversial to say that this would be a sensible menu for at least some of the requirements for success in both commercial and not for profit environments. It would of course only be a commercial equivalent of Superman who would have all of these characteristics in abundance, but they would be a good starting point, and anybody with them in any sensible degree would no doubt be, in principle, welcome in any senior management team in either camp.

There are in addition two parallel qualities which are key ingredients in each case. In a for-profit environment it is usually a compliment for a manager to be called commercial or with good commercial

instincts. This may also be a requirement in select not-for-profit environments, but more often there will be a need for a type of nous, partly learned, partly intuitive appropriate to the environment, vital but particular to the entity and its purpose. A good head teacher will instinctively understand school situations in which he or she may find himself, or the head of, say, a medical charity the way in which to manage doctors and research people skills not necessarily much good to a commercial manager, but a huge help in doing the job on hand.

Similarly there will be a need to understand, react to and perhaps even anticipate the environment in which the service provided by any institution operates, or the requirements and expectations of its principal stakeholders. In a commercial environment it is easy to identify: it is called marketing, or at least the requirement to understand the market environment for the products sold. This word may also be appropriate in a not for profit environment, but there may also be a need for more subtle interpretations for that sector: such as knowledge of fundraising sources for many charities dependent for their activities on giving, the ability to recruit not just students but also staff in the educational sector, awareness of the demands, structure, likely patrons and clients of a particular branch of the arts in an arts related organisation, or comprehension in a hospital trust of the complexities of NHS funding and structure.

I now return to the old chestnut about management and employees motivation under a profit oriented environment without, or preferably, with employee shareholdings, which states, quite simply, that employees of any stripe are more focussed, more productive, better motivated and more flexible within that framework, than in a not-for-profit entity. I find this conventional wisdom somewhat counterintuitive, for I have seen highly motivated, hugely productive employees, who would adorn any kind of organisation, across all my not-for-profit interests in the arts, music, educational and charitable worlds without any sniff of a profit motive, nor the slightest interest in anything as sophisticated as a shareholding. I have incidentally more than anecdotal evidence that the same is true of many public sector industries, contrary to the Thatcherite precepts of casting off the chains of public sector constraints. I was for many years on the board of the Post Office (as it then very properly and descriptively was) in the days, mainly in the 80s and early 90s when, I am glad to say, it was recognised as being one of the best, if not the best post office in the world. What struck me in the case of that basic, not always very glamorous industry was the commitment and pride of its managers and most of its employees, those who were not held in the practical or ideological grip of some not always very enlightened union reactionaries. For the most part, they loved their employer, were proud be part of it, worked hard and with a purpose, and thus created a well run concern delivering quality to its major stakeholders, its customers. It was not the profit motive that would have saved the Post Office from its current mire, had it gone into the private sector. It would have been removal of the icy and restrictive imprint of the Treasury on every important decision; not some notional financial incentive which would supposedly and at a stroke have released a wave of apparently pent up employee motivations.

Transferable lessons

It is clear that, when analysed, there is, with some nuances, a high degree of overlap in terms of board and senior management requirements. So what, in reality can the commercial sector learn from its not for profit counterpart, and vice versa? It is never wise to draw sweeping conclusions from statistical input limited by ones own experience and that of friends, acquaintances and colleagues. Nonetheless the former Post Office example illustrates how a public sector company with clearly identified principal stakeholders (customers), and an agreed and understood strategic mission can successfully emulate the private sector. Unfortunately these strategic qualities are all too often lacking in the not for profit sector, whereas the commercial sector, particularly amongst quoted companies, is increasingly focussing on the need for and importance of them.

There are of course honourable exceptions, and Im sure that Roberts WWFUK is one of them, but its up for debate that not for profit organisations are less strategically aware, less driven by identified strategic objectives, based on value and benefit to the principal stakeholders, more inclined to live in the now, and

less to look ahead at the change and opportunities that lie ahead.

Commercial organisations seem also to be better at generating and making good use of appropriate and timely management information, both financial and non financial. The advantages of having a dashboard with a sensible and informative set of dials available to board and management is a lesson in many cases yet to be learned. The modern buzz expression key performance indicators or KPIs is still little appreciated, with the concomitant need for quality management time identifying the right KPIs for each level and making sure that they are available on time, and accurate.

It is also my experience that, on balance, they are rigid structurally, less flexible and with tortuous decision making processes. They could learn from the lean, empowered and flat (ie with the minimum layers of management) of successful commercial operations. The latter's processes of delegation and empowerment (that is giving managers and employees a degree of total responsibility for decisions at a certain level) make a significant contribution to their forward momentum.

Unfortunately bureaucracy and lack of delegation is an epidemic disease in not-for-profit organisations, and one which significantly impedes their progress, down even to the vast and depressing piles of board papers which so many seem to produce. For my money, no set of board papers should (perhaps excluding appendices) take more than two hours to read, and should concentrate on high level strategic matters, not on operating minutiae. I once served on a Regional Health Authority in West London. The papers for the meeting arrived the previous night, carried, all 10 inches of them, by a muscular courier, ready to be read, with little pleasure, by an already knackered board member. The meetings were interminable, and the best bits as one had always been led to believe kept till last, when only the activists remained. I couldn't hack it for very long, and I'm afraid that this experience is being undergone not just within the NHS, but also on the boards of schools and charities etc, all over the country. It is the thought of the bureaucracy and the paperwork combined I must say with the apprehension of inadequacy that puts off so many potentially excellent NEDs of not-for-profit organisations.

But it's not all one way traffic, for there are in my mind several key lessons that the commercial world can learn. For instance there is usually albeit often unfocussed a greater sense of contribution in not-for-profit organisations, of doing something worthwhile for justifiable motives, just by the nature of the entity; and this leads to greater collaboration, both between peers working together in teams, and in the way in which managers reach decisions, by a more concerted process. It is true in organisations of any kind that managers will often have to take decisions for which they alone are responsible, but the ability to seek others' opinions not only makes them feel more included in the team, but also provides greater and deeper input for the decision. While, unfortunately, as I have argued, managers tend to be less empowered in the not-for-profit sector, and thus the benefits of collaboration may thereby be diluted, this basic ingredient for good decision making is certainly there.

In addition, such organisations tend to be more transparent, more open to scrutiny, both within and without, as compared with the often rather secretive corporate community; the latter may be driven by the power seeking or paranoia of individuals, worries about excessive and uncontrolled public disclosure for quoted companies, or a feeling that keeping matters secret is in some way more beneficial for the company. In contrast for institutions like mutuals, transparency comes with the territory, in that the beneficiaries or stakeholders in the entity will or at least should always require to a reasonable extent to know what is going on in their cooperative, while for others, like schools, it is part of the culture. This cultural issue is important, for it can not only build respect and understanding of the organisation externally, but can create a very positive attitude in a workforce who might otherwise be demotivated by an inherent feeling of being kept in the dark.

The corollary of transparency is the way in which information is disbursed and to whom, generally called communications. The ability to provide more information, to be open clearly provides a great advantage, as

do the potentially less socially or politically divisive messages of not for profit organisations many of them use this opportunity very effectively. And of course the stock in trade of many such organisations is in the area of media and communications; their reason for existence may be to make the public aware of their stakeholders interests or plights. In many others much could be learned about communications, it is fair to say, but the combination of a culture of transparency and well thought out and effective communications is one where some non commercial companies are world leaders. No better example than Roberts organisation, a good point at which to recap my points and then hand over to Robert and Jack for their no doubt trenchant observations.

The role and objectives of boards, or their equivalent, is broadly similar in both commercial and not-for-profit sectors, but in each case the burgeoning duties of NEDs could require greater time commitment than in the past.

In particular, directors with important skills other than the commercial can be great contributors, but appropriate training will in most cases be essential.

Nor are management, as opposed to board, requirements so different, and it is not proven that For Profit provides any superior motivation. In any event many not-for-profit organisations are, at least in part, For Surplus.

The not-for-profit sector might in principle learn from the strategic awareness and focus, the quality of management information, and the delegation and empowerment, combined with lack of bureaucracy found in the commercial world; while the latter could draw from the sense of collaboration, transparency and communications skills of the best of not-for-profit organisations.

And to end on a frivolous note, may I remind you of Lady Bracknells caustic analysis of charity, which she would undoubtedly have applied to the whole of the voluntary sector: Charity, dear Miss Prism, charity! None of us are perfect. I myself am peculiarly susceptible to draughts.

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