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Managing Risk in a Riskier World

CohnReznick 2015 Not-for-Profit Governance Survey

A CohnReznick LLP Report
JULY 2015

Table of Contents

Methodology

The 2015 CohnReznick Not-for-Profit Governance Survey was distributed via email to not-for-profit industry professionals and board members across the United States. The survey was conducted over eight weeks during the spring of 2015.

Based on feedback from our 2014 survey respondents, the 2015 survey was expanded to 38 questions (27 questions were in last year's survey). To establish trend data, many questions included in the 2015 survey had also been asked and answered the previous year.

The majority of questions focused on the not-for-profit organization's governance and risk management policies. These included questions about the structure of the Board, its various committees, and the role each plays in the organization's governance practices.

470 not-for-profit executives responded to the 2015 CohnReznick Not-for-Profit Governance Survey—an over 80% increase in responses compared to the 2014 survey.

Our thanks goes to everyone who participated in this survey. We hope not-for-profits find the results useful as they continue to refine their organizations' governance policies and discover new ways to avoid risk.

EXECUTIVE SUMMARY

Governance and risk management issues are key concerns for the leaders of not-for-profit organizations. This was confirmed through the responses we received in CohnReznick's 2015 Not-for-Profit Governance Survey. While the vast majority of survey respondents (87%) told us that they had implemented key governance initiatives, about 40% of the organizations said that they are either "somewhat" or "not confident" in their governance practices. With the proliferation of high profile security breaches occurring among well-known companies, we were not surprised that many not-for-profit organizations have doubts surrounding their governance and risk management programs.

Just under one-third of survey respondents said that their organization had conducted an enterprise risk management assessment. This could certainly be one of the more significant factors in the large percentage of respondents stating that they are either somewhat or not confident in their governance practices. Additionally, while nearly three quarters of survey respondents said that their annual board meetings include an educational component, only half said that governance was a topic discussed in board meetings. Less than 20% said that risk management was covered and 25% said that regulatory concerns were covered in board meetings.

One of the issues impacting confidence in governance practices is cybersecurity. Cybersecurity ranked among the top 10 risk issues for just under 60% of the surveyed organizations and among the top three risk issues for one in four organizations.

So, in a time where cyber threats and other risk issues have become more commonplace, how should not-for-profit organizations respond? CohnReznick recommends the following best practices:

1. **A committee of the board should be dedicated to overseeing risk management.** Audit committees usually take on this responsibility as these committees typically include directors with risk management skills.
2. **A committee of the board should be charged with monitoring IT.** Whether it's the finance, executive, or audit committee, the committee should include experienced IT professionals with clearly established objectives and monitoring responsibilities.
3. **Not-for-profit organizations should consider conducting several critical assessments in conjunction with their overall governance practices.** These include:
   a. An assessment of the organization's risk management and cybersecurity policies and procedures
   b. An assessment designed to ensure that the organization's governance practices comply with the current laws within their state and known best governance practices
   c. A board self-assessment at least every three years
4. **Include risk management and cybersecurity topics in the educational programs presented during board meetings.** This will help to ensure that management and board members are fully aware of the latest developments and apprised of potential threats to their organization.

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RESPONDENT PROFILE

Figure 1. Type of Organization

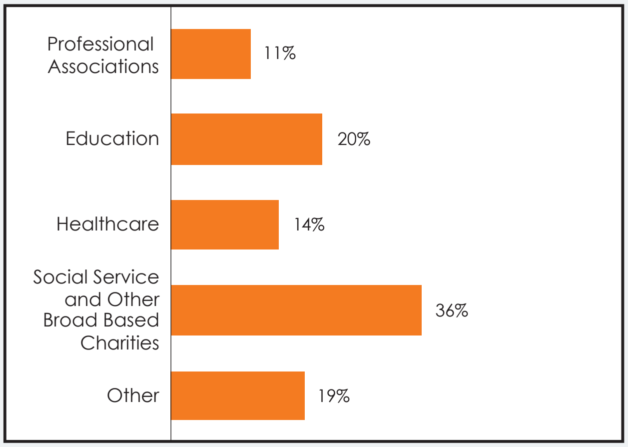


Figure 2. Current Position Within the Organization

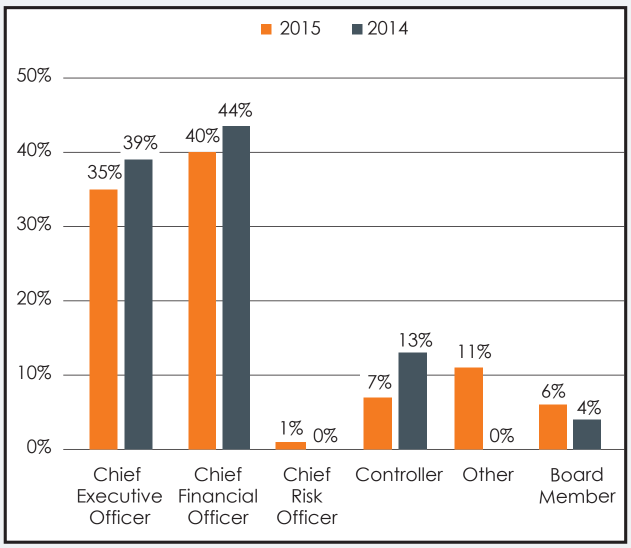
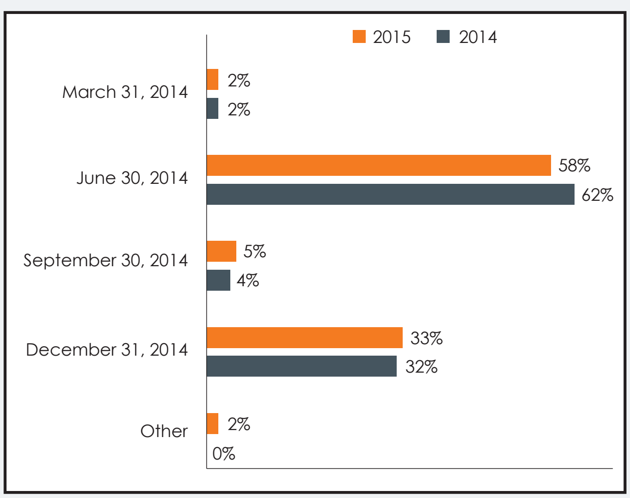


Figure 3. Fiscal Year Close



In order to compare and sort the answers to various questions, and to develop a profile of the survey respondents, we asked a few basic questions about those answering our survey.

Overall, 70% of survey respondents said that they would describe their **type of organization** as either education, healthcare, or social service agency or other broad-based social charities.

1,521,052

The number of charitable organizations in the United States as of May 2015.*

When asked about their **current position within the organization,** 75% of respondents to the 2015 survey said that they were either the Chief Executive Officer or Chief Financial Officer. Other respondents to the 2015 survey included Board Members (6%), Controllers (7%), Chief Risk Officers (1%), and others (11%), which included a myriad of other C-suite level respondents.

More than half of the respondents (58%) stated that their organization has a June 30th **fiscal year end**, with another 33% stating that their fiscal year ended on December 31st. This was very much in line with what respondents reported to us last year.

** The Urban Institute, National Center for Charitable Statistics: http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics/*

Similar to last year, the vast majority of respondents (58%) reported that their **annual revenues** fall in the range of $1 million to $25 million. Twenty percent of respondents reported revenues between $25 million and $100 million, and 10% reported more than $100 million in annual revenues. Unlike last year, we received an increased number of responses this year from organizations with revenues under $1 million (12%). In addition, we asked respondents to tell us about any **change in total revenue for the last fiscal year**. Fifty percent of respondents reported revenue increases for their organization ranging from less than 1% to 5% for their last fiscal year. At the same time, 28% reported an increase of over 5%. This represents a higher number of not-for-profits reporting increases versus last year (41% and 29% respectively). For the 2015 survey, 22% of respondents reported that revenues had decreased during their last fiscal year versus 31% in 2014.

Apart from identifying their type of organization, we asked respondents to **define their mission**. In choosing from a list of descriptions that best stated their organization's mission, most chose "education," "health," or "human services." This was consistent with the respondents from last year's survey.

Figure 4. Annual Revenues

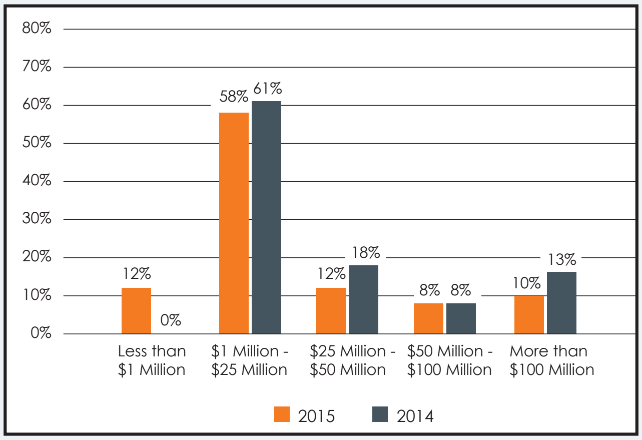


Figure 5. Change in Total Revenue for the Last Fiscal Year

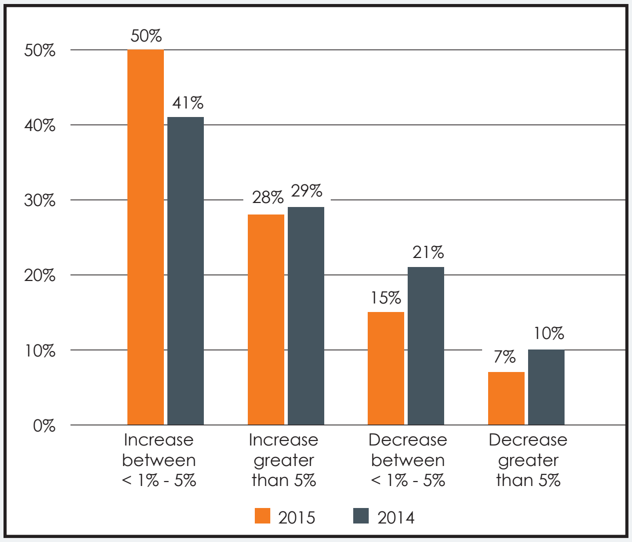


Figure 6. Defining Their Mission

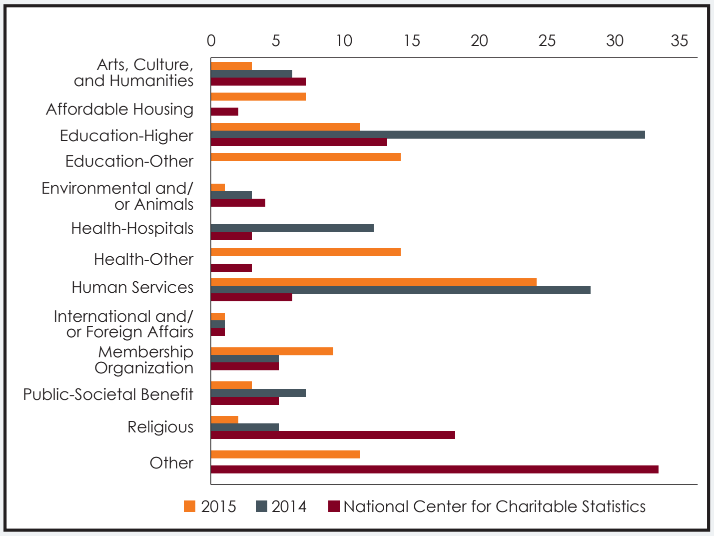
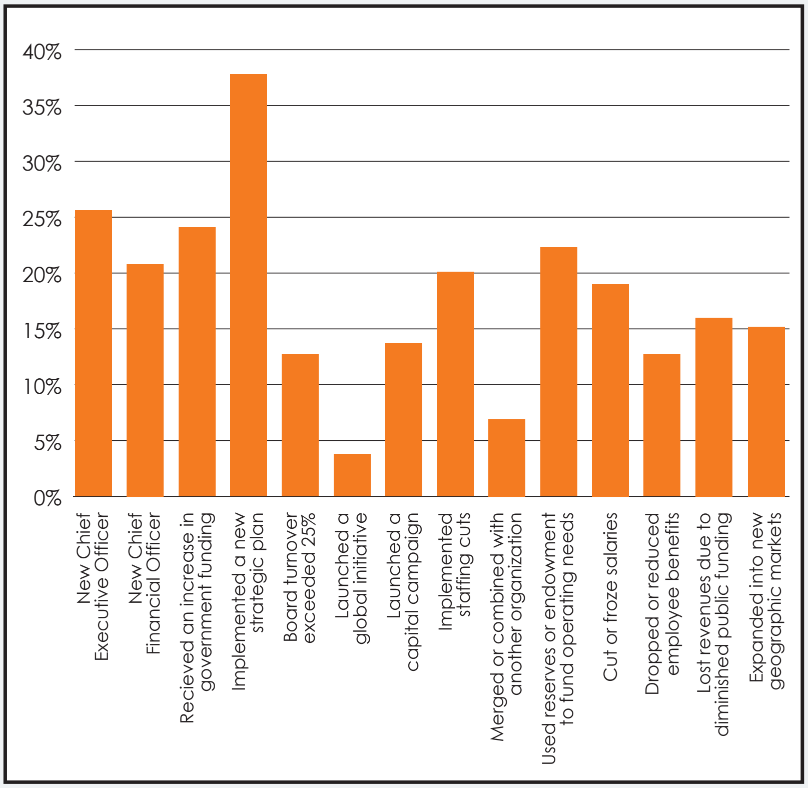


Figure 7. Making Significant Strategic and Organizational Changes Within the Last Two Years



A number of the surveyed organizations, particularly those that described themselves within a sub-segment of broad-based social services organizations, reported **making significant strategic and organizational changes within the last two years**. The most frequently reported changes included implementing a new strategic plan (38%) and changes to top leadership, such as a new Chief Executive Officer (26%) or a new Chief Financial Officer (21%). A significant portion of the organizations (25%) reported an increase in government funding. We also noticed that 39% either implemented staff cuts or mentioned that they cut or froze salaries.

GOVERNANCE

POLICIES AND PRACTICES

Approximately 40% of organizations stated that they are either “somewhat confident” or “not confident” in their governance practices. While this is concerning, it is also somewhat expected. With the recent data breaches to major well-known companies, and the federal government, not-for-profits should re-evaluate their policies and procedures to ensure management and the board are appropriately engaged in IT governance.

Just under 90% of all organizations reported that they have **certain key governance initiatives** in place. These include social media policies (67%); a whistleblower complaint resolution process (77%); a formal record retention policy (90%); and conflict of interest (92%) policy. On the other hand, over 60% of the organizations reported that they did not have an IT steering committee (66%) and did not use an outside organization to record whistleblower complaints (67%). Nearly half of the organizations (46%) do not have, or were unsure if they have, a process in place to assess IT risk.

84% of respondents reported that their organization has a **written whistleblower policy** in place. This number is consistent with findings from last year’s survey. One in 10 reported having no intention of implementing such a policy, which is also consistent with last year’s findings. Implementing a whistleblower policy along with the necessary procedures, including the use of a tip hotline, is an easy way to defend against fraud. The 2014 Association of Certified Fraud Examiners (ACFE) *Report to the Nations on Occupational Fraud and Abuse* revealed that over the last five years, more than 40% of reports of fraud have come in through tips.[1]

Figure 8. Confidence in Organizational Governance Practices

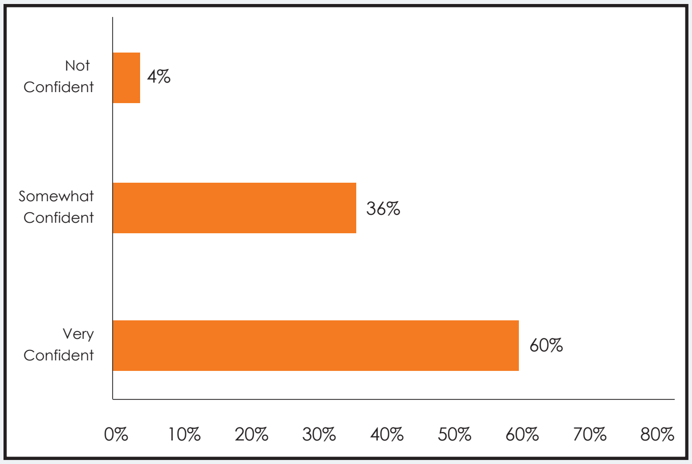


Figure 9. Key Governance Initiatives

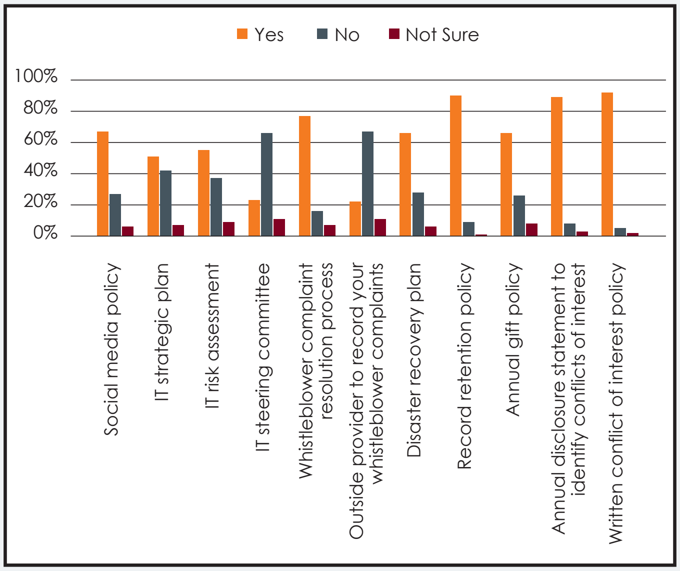
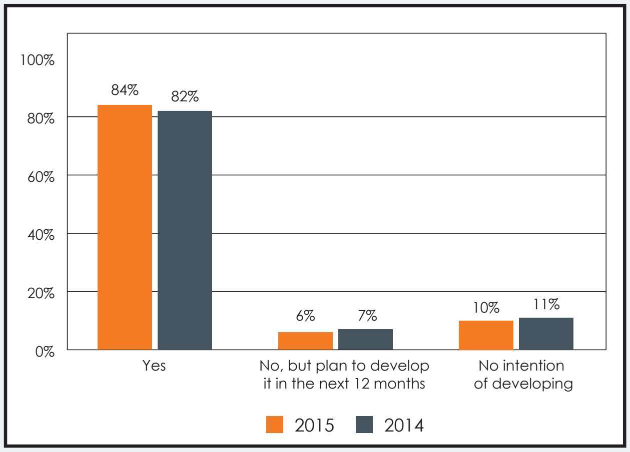


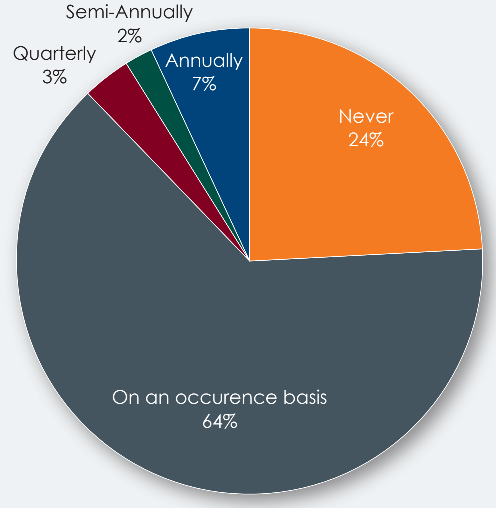
Figure 10. Whistleblower Policy



[1] Association of Certified Fraud Examiners (ACFE), *Report to the Nations on Occupational Fraud and Abuse*, Austin, TX; ACFE, 2014, p.4

Nearly two-thirds of respondents (64%) indicated that their **audit committees monitor whistleblower complaints** as they occur. However, nearly one in four respondents stated that their audit committees NEVER monitor whistleblower complaints. Another fact mentioned in the 2014 Association of Certified Fraud Examiners (ACFE) *Report to the Nations on Occupational Fraud and Abuse* is that proactive data monitoring/analysis reduced fraud incidents by 59.7%. The median loss for firms without these controls was $181,000.[2]

Figure 11. Monitoring Whistleblower Complaints

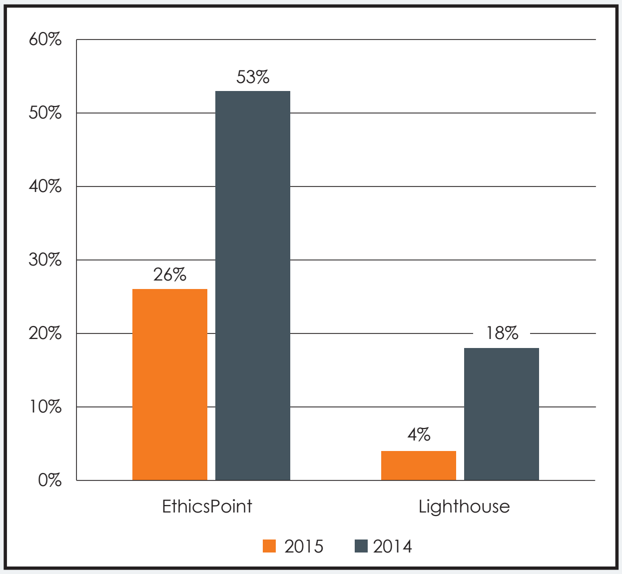


$17.77 billion

The amount of corporate giving. (A 13.7% increase from 2013.)*

Roughly one quarter of the respondents using an **outside service provider for whistleblower complaints** said that they use EthicsPoint (26%). However, that number is just half of what it was in 2014 (53%). The only other outside provider that was consistently named by respondents is Lighthouse. But that number is down from 18% in 2014 to just 4% this year. (Please note by citing the responses, CohnReznick is not recommending these companies).

Figure 12. Outside Whistleblower Provider



2 Association of Certified Fraud Examiners (ACFE), *Report to the Nations on Occupational Fraud and Abuse*, Austin, TX; ACFE, 2014, p.38, Fig 37

* *Giving USA 2014: http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics/*

RISK MANAGEMENT

Figure 13. Enterprise Risk Management Assessment

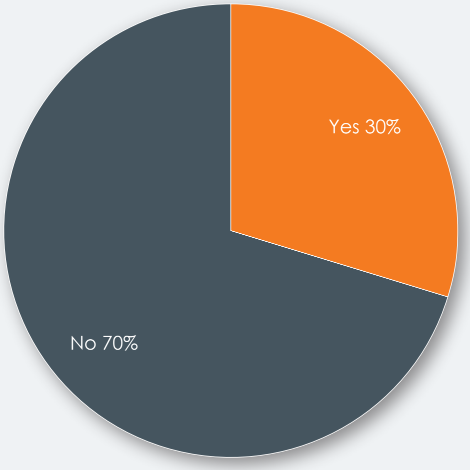


Figure 14. IT Monitoring

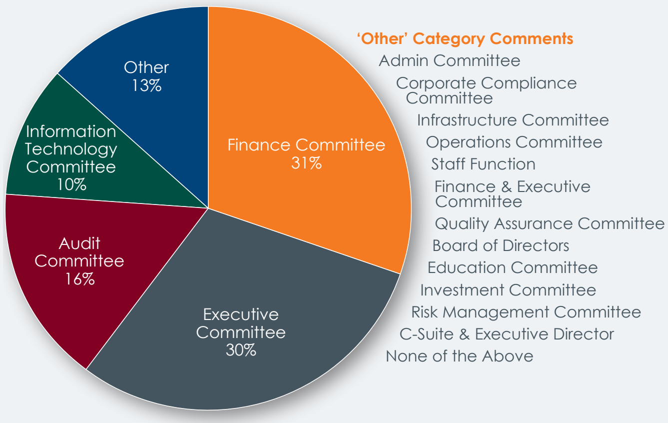


Figure 15. Cybersecurity

Only 30% of survey respondents indicated that their organization has conducted an **enterprise risk management assessment.** This could be among the more significant reasons why 40% of the respondents stated that they are either somewhat confident or not confident in their governance practices.

Roughly 60% of respondents stated that either their **Finance Committee or Executive Committee is charged with monitoring IT**. Only 10% of organizations said that they have a separate IT committee, while another 16% indicated that IT was monitored by their board's audit committee and another 13% stated that another (not listed) committee monitors IT.

Nearly 25% of the respondents counted **cybersecurity among the top three risks** to their organization. Another 57% said that cybersecurity was one of their top 10 risks. Fewer than 20% of respondents stated that cybersecurity was not a concern of their organization.

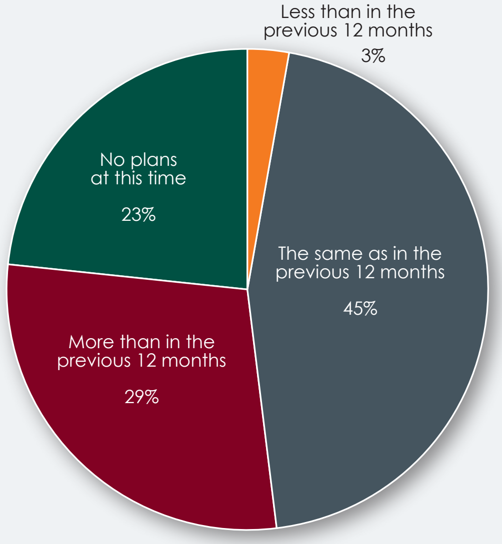
This is concerning and a bit of a contradiction as just 11% of organizations stated that they had a risk committee or an IT committee later in the survey, with most placing IT monitoring within the audit or finance committees. Also, in the following question, it seems that some organizations (29%) plan to spend more money, some as much as 100% more, than last year on their data security efforts. Just 3% said that they would be spending less. 45% expected their organization would be spending about the same on data security as it did the prior year. So the question here is: who is really monitoring IT? Whether it's the finance, executive, or audit committee, we believe that some committee of the board should monitor IT. That committee should include experienced IT professionals and ought to have a set of clear objectives to enable it to fulfill IT monitoring responsibilities.

Do you have the right "experts" on your audit and finance committee?

When those organizations **planning to spend more on data security** were asked to give a percentage of the expected increase, nearly half (47%) anticipate a spending increase of 1%-10% over the coming year. 13% of respondents anticipate spending would increase by up to 25%. One quarter of respondents said that they were not sure of the level of spending their organization is planning to improve data security over the coming year.

CohnReznick advises not-for-profits to have a committee of the board dedicated to the oversight of risk management. Furthermore, we believe audit committees usually take on this stewardship responsibility, as they typically include directors with risk management skills.

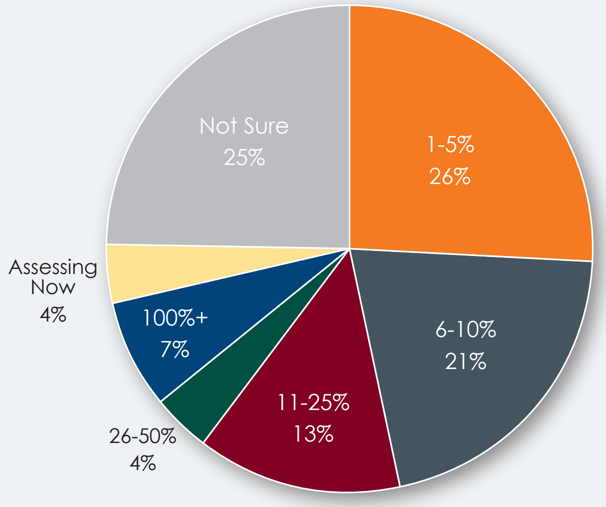
Figure 16. Data Security Spending Over Next 12 Months



***The AICPA Audit Committee Toolkit: Not-for-Profit Entities ("Toolkit")*, includes both required and best practices which suggest:**

- The audit committee could be responsible for the oversight and response to enterprise risk management activities.
- The audit committee should periodically reassess the list of top enterprise risks.
- The audit committee should determine who in management is responsible for each of these risks.[3]

Figure 17. Data Security Spending Anticipated Increase/Decrease



[3] American Institute of Certified Public Accountants (AICPA), *The AICPA Audit Committee Toolkit: Not-for-Profit Entities*, 3rd Edition, New York, NY, Chapter 1, p.6

Figure 18. Conflicts of Interest: Audit Committee Oversight

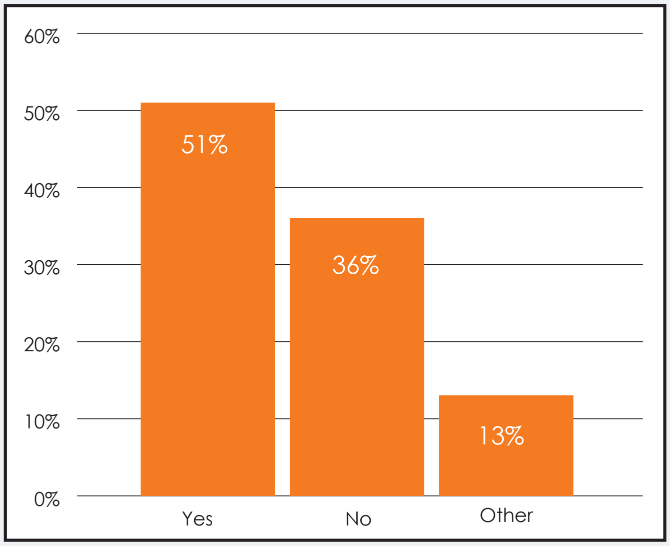
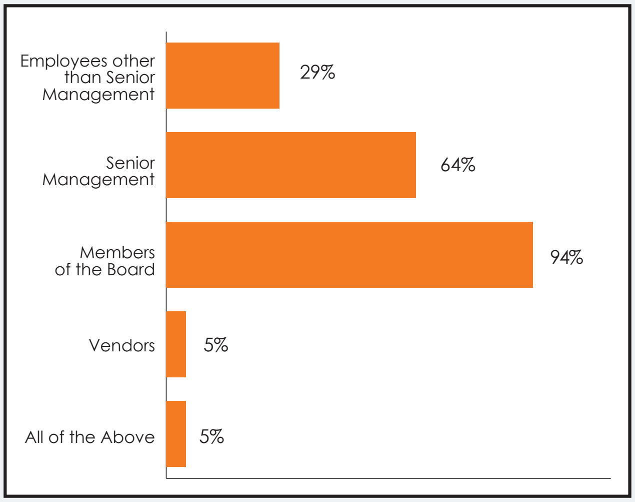


Figure 19. Conflicts of Interest: Annual Disclosure Statements



Roughly half (51%) of the respondents reported that their **audit committee monitors disclosed conflicts of interest.** 36% advised that their audit committees did not do this monitoring and 13% responded as "other." Generally, this "other" response meant that a committee other than audit was charged with disclosed conflicts of interest monitoring, such as the Board, executive committee or a governance committee.

95.4%

Percentage of households that give to charity.[*]

The Toolkit suggests that the identification and reporting of conflicts of interest is the responsibility of the audit committee. *The Toolkit* also suggests that a conflict of interest questionnaire should be completed by all employees.[4] When respondents were asked to check all areas that applied to their organization, 94% reported that their organization obtains **annual conflict of interest disclosure statements** from board members and 64% reported obtaining these disclosure statements from senior management. Only 29% of respondents stated that they obtain conflict of interest disclosure statements from other employees and vendors in addition to senior management and board members. Many large not-for-profit organizations require an annual conflict of interested disclosure statement from all employees and vendors. CohnReznick believes that this is a best practice that should be implemented by all not-for-profit organizations in an effort to prevent fraud.

4 American Institute of Certified Public Accountants (AICPA), *The AICPA Audit Committee Toolkit: Not-for-Profit Entities*, 3rd Edition, New York, NY, Chapter 9, p.73

* *Center on Philanthropy of Indiana University: http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics/*

BOARDS AND COMMITTEES

Over one third of organizations (36%) reported that their **board was comprised of 20 or more members**. Another 33% reported boards with 10-15 members and 18% reported having 15-20 board members. The board profile for the 2015 survey is fairly similar to the 2014 survey with one notable exception. There are more organizations with 10-15 members in 2015 (33% in 2015 versus 22% in 2014.) We believe boards with fewer than 25 members are best suited to govern most not-for-profit organizations because they can be more focused and nimble in their decision making and, consequently, more strategic and engaged in fulfilling mission outcomes.

Nearly three quarters of respondents (71%) noted that their **board members have term limits**. When asked about the length of those terms, most (64%) noted that their organization has term limits of three years, which is consistent with the BoardSource 2014 Nonprofit Governance Index.[5]

Only 43% of respondents stated that their **board has conducted a self-assessment** within the last three years. The remaining respondents reported that they had not conducted (37%) or were unsure if they had conducted (20%) a board self-assessment within a three-year period. CohnReznick recommends that boards conduct a self-assessment at least every three years.

Figure 20. Board Size

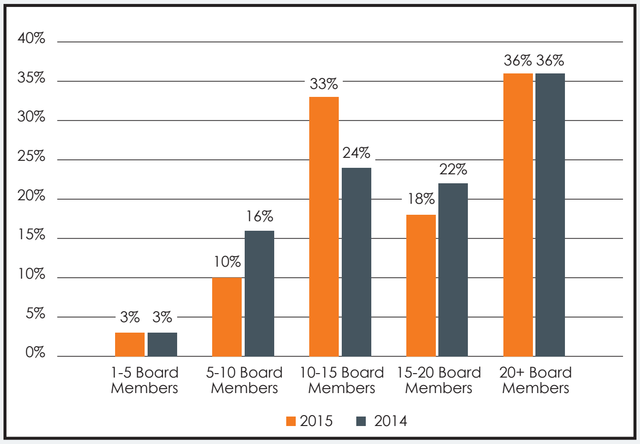


Figure 21. Board Term Limits

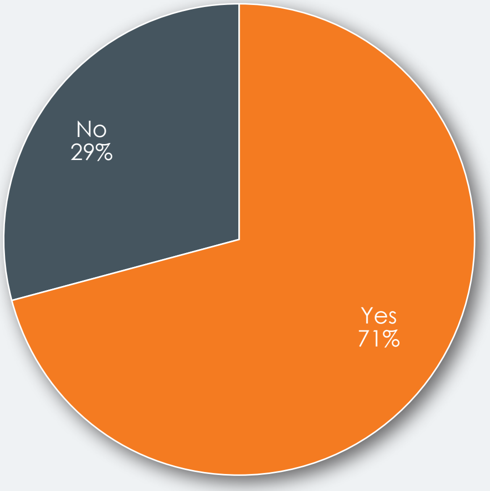
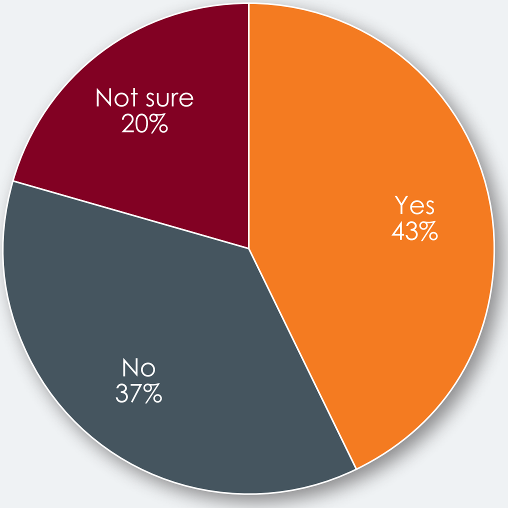
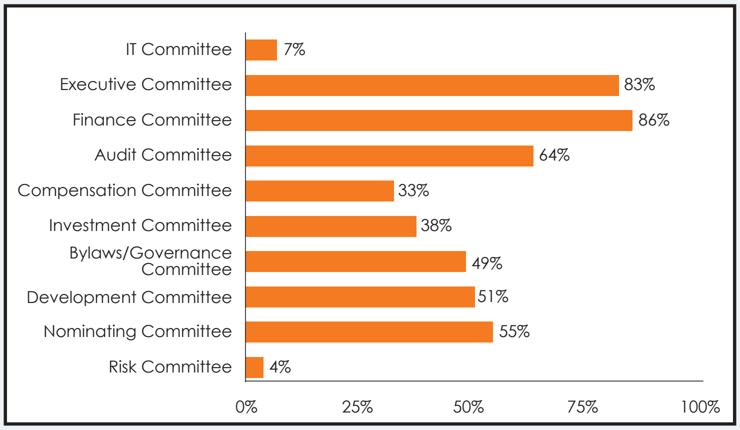


Figure 22. Board Self-Assessment



5 BoardSource, *Leading with Intent, A National Index of Nonprofit Board Practices*, 2015, p.8, Fig.4, http://leadingwithintent.org/wp-content/uploads/2015/01/LWI-Report-2.pdf

Figure 23. Organizational Committees



As businesses and not-for-profits experience more fraud and cyber-attacks than ever before, they need to be more vigilant in their practices. The business world is getting more complicated and those charged with governance need to manage the uncertainties by employing effective risk management practices, including enterprise risk assessments. As more states pass laws on these issues, such as the New York Nonprofit Revitalization Act, organizations need to be aware of the consequences of non-compliance.

While most (85%) of the respondent organizations noted that they have **multiple committees present within their organization**, when asked to check all of the committees present within their organization, only 64% stated that they have an audit committee. Eighty-three percent of respondent organizations checked that they have an executive committee, with 86% actually stating that they have a finance committee.

As stated earlier, 80% of the organizations surveyed noted that their organization's cybersecurity is among their top three or at least top 10 concerns. However, only 4% and 7%, respectively, stated that they have a risk or IT committee. According to the Association of Certified Fraud Examiners (ACFE) 2014 *Report to the Nations*[6], organizations that implemented proactive data monitoring and analysis saw a 59.7% reduction in loss based on having the aforementioned controls in place. This was the highest overall reduction in loss, according to the report. Based on this information, CohnReznick recommends that organizations discuss and re-evaluate current cybersecurity practices and develop a plan to manage them moving forward.

The Council of Nonprofits currently lists 26 states with laws in place requiring charitable not-for-profits to conduct an independent audit under certain circumstances. In addition, 24 states require annual submission of audited financial statements. Some of these states include California, Connecticut, Florida, Georgia, Hawaii, Maryland, Massachusetts, New Jersey, New York, North Carolina, Pennsylvania, Rhode Island, and Virginia.[7]

We are seeing a trend that indicates governmental bodies are showing increased interest in the role of the board. Consequently, the expectations have been elevated.

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6 American Institute of Certified Public Accountants (AICPA), *The AICPA Audit Committee Toolkit: Not-for-Profit Entities,* 3rd Edition, New York, NY, p.38

7 National Council of Nonprofits, State Law Nonprofit Audit Requirements, https://www.councilofnonprofits.org/nonprofit-audit-guide/state-law-audit-requirements

CohnReznick suggests that, to the extent it hasn't done so recently, an organization's board, in cooperation with management, conducts an assessment to ensure governance practices comply with the current laws within the organization's state and known best governance practices.

Almost half of the organizations (48%) **reported having an audit committee** comprised of four to six board members. Forty-two percent have audit committees with one to three board members and 10% reported having audit committees with six or more board members.

Most of the organizations (32%) reported that **their audit committees meets on a quarterly basis**. Twenty-two percent of audit committees met semi-annually and 19% met on an annual basis. Our experience is that the best functioning audit committees have four to six members and meet quarterly.

Eighty-two percent of respondents stated that their **audit committee has at least one member who is a financial expert**. However 14% reported that their audit committee lacks a financial expert. CohnReznick believes that it is always a good idea to have a financial expert on your board. A financial expert can provide industry insight and can translate the issues and jargon associated with financial statements and applicable new regulations. In addition, they are trained to look for specific abnormalities and are more likely to spot an issue.

Finally, according to the Association of Certified Fraud Examiners (ACFE) *2014 Report to the Nations*[8], the types of fraud schemes that were committed against the respondent organizations with less than 100 employees included those that could easily be seen by a member of the board or audit committee with a financial background. These schemes included billing (28.7%), check tampering (22.1%), skimming (17.1%), expense reimbursements (16.5%), payroll (16.5%), and cash on hand (12.0%), and register disbursements (3.2%).

Figure 24. Audit Committee: Size

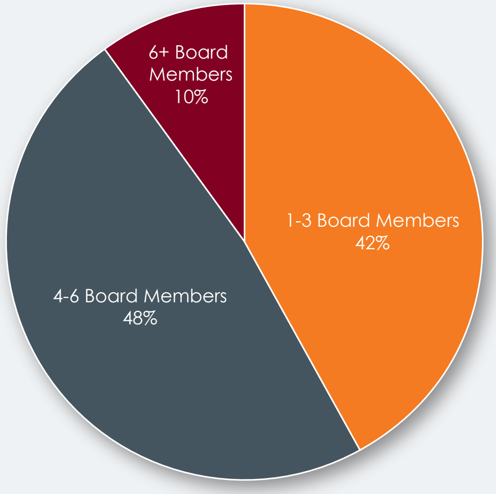


Figure 25. Audit Committee: Frequency of Meetings

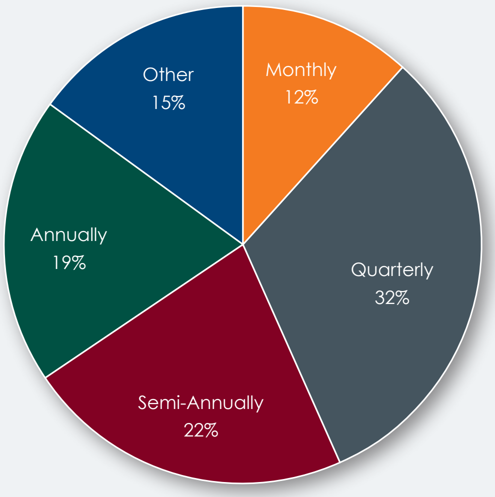
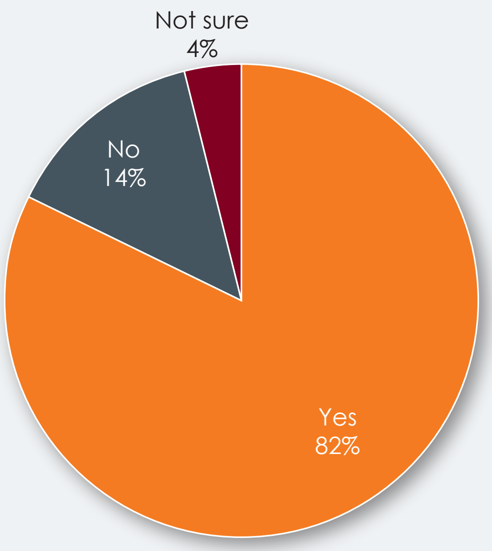


Figure 26. Audit Committee: Financial Expert



8 American Institute of Certified Public Accountants (AICPA), *The AICPA Audit Committee Toolkit: Not-for-Profit Entities*, 3rd Edition, New York, NY, p.26

Figure 27. Audit Committee: Charter

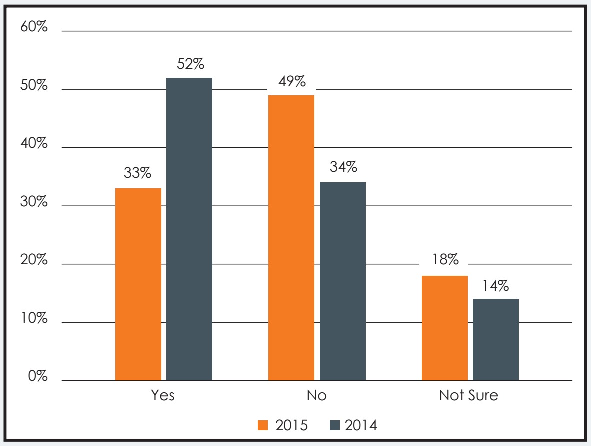


Figure 28. Board Knowledge of Governance Policies

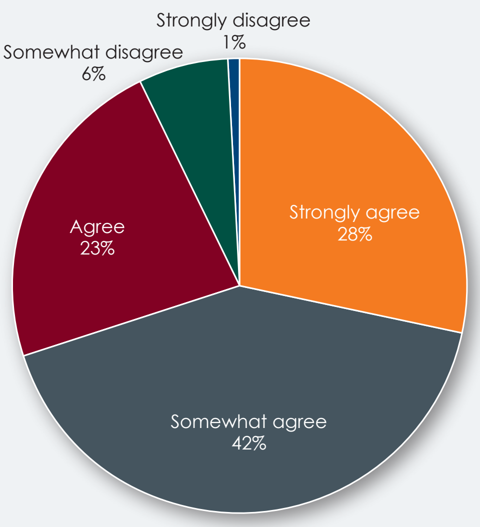
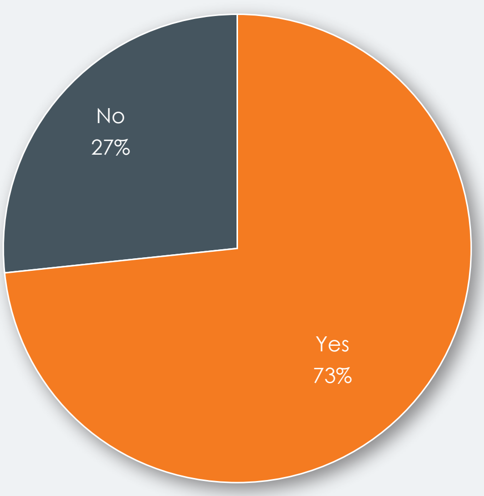


Figure 29. Board Meetings: Educational Component



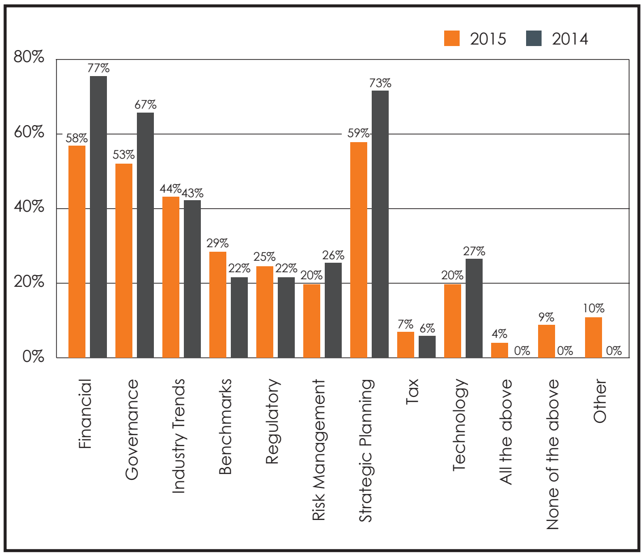
For the 2015 CohnReznick survey, there was a significant decline in respondents reporting that their **audit committee has a charter** when compared to 2014. In 2015, just 33% reported having a charter versus 52% in 2014.

Seventy percent of respondents were at least somewhat in agreement that their **board members have a working knowledge of their organization's governance policies**. But among these respondents, only 28% said that they "strongly agree" with this proposition.

Seventy-three percent of the 2015 survey respondents reported that their **annual board meetings include an educational component.**

Board meetings for the surveyed organizations covered a range of topics. When respondents were asked to click all options that apply, the topic of governance ranked fairly high on the list (53% for 2015 respondents, 67% for 2014 respondents), risk management and regulatory issues were not as widely covered in board meeting agendas. Just 20% of 2015 survey respondents stated that risk management was a topic covered in their board meetings.

Figure 30. Board Meetings: Educational Topics



$22.55

The estimated dollar value of volunteer time for 2013.*

In the discussion as to which committees are **tasked with specific responsibilities**, overall the full board seems to take on the responsibility for annual budgets (83%) and bylaw changes (85%). However, executive compensation is more likely to be handled by the compensation committee (96%) or the executive committee (82%). As we would expect, the auditor's reports are typically handled by the audit committee (98%) and risk assessments are handled by the risk or IT committee, when they're present. Fundraising initiatives are typically handled by the development committee (99%), if present, or by the full board if not.

Just 20% of 2015 survey respondents stated that risk management was a topic covered in their board meetings.

Please note that respondents were asked to check all committees within their organizations that fit the requested criteria.

* The Urban Institute: http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics/

Figure 30A. Full Board

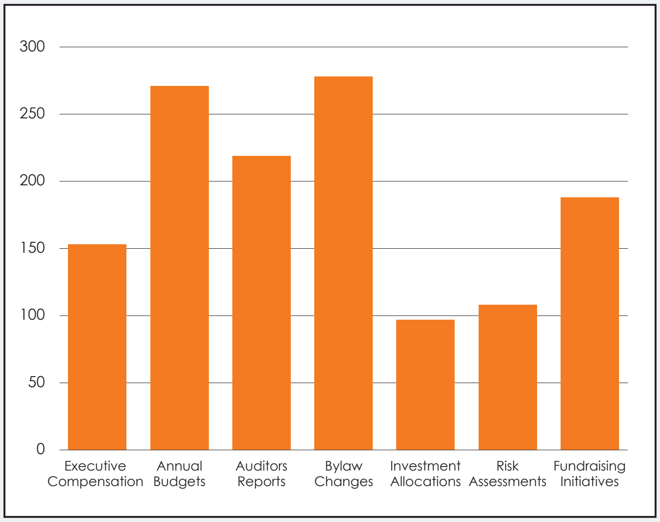


Figure 30B. Audit Committee

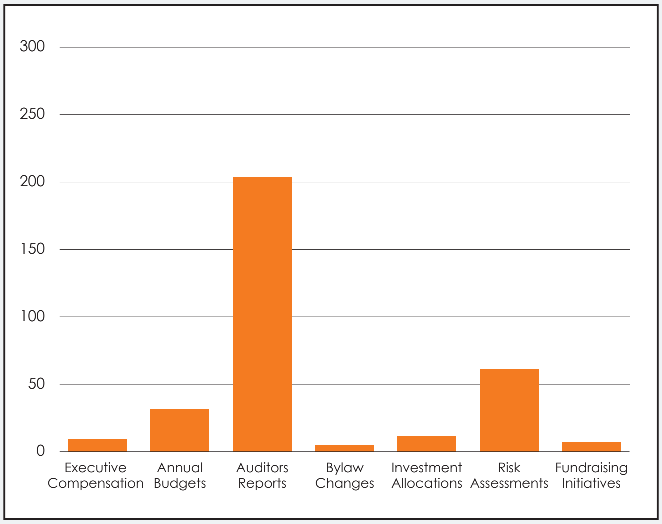


Figure 30C. Executive Committee

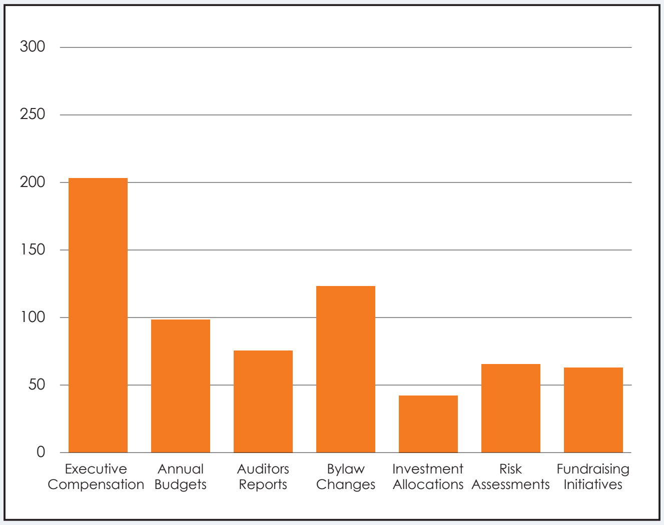


Figure 30D. Compensation Committee

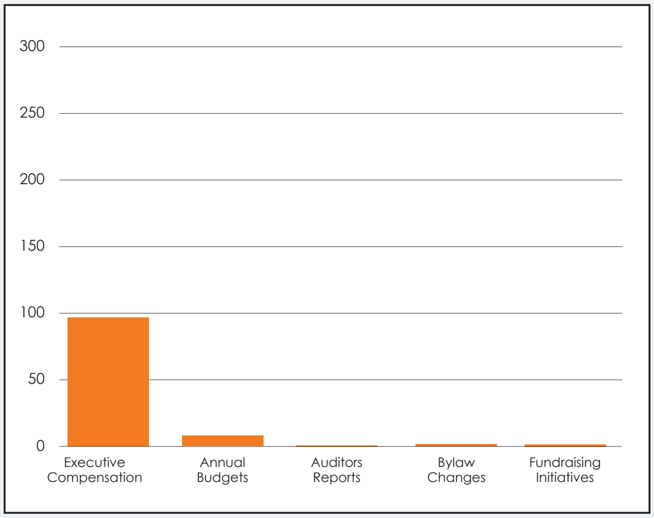


Figure 30G. Development Committee

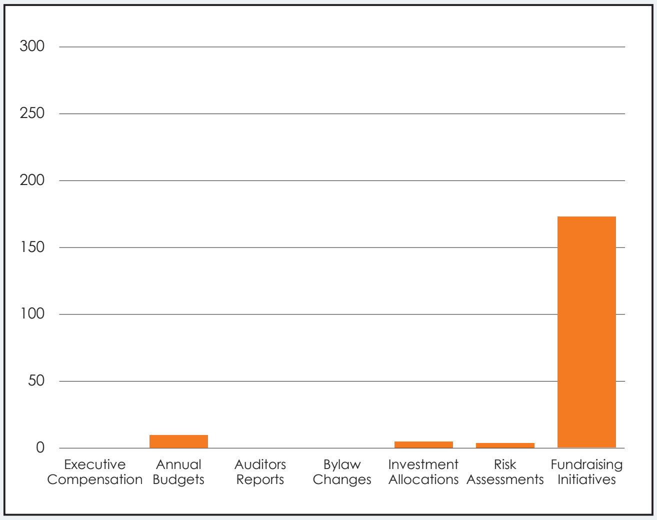


Figure 30E. Bylaws/Governance Committee

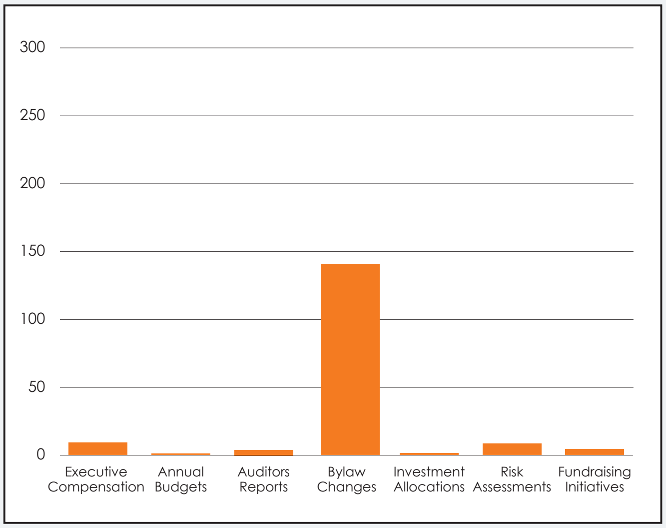


Figure 30H. Investment Committee

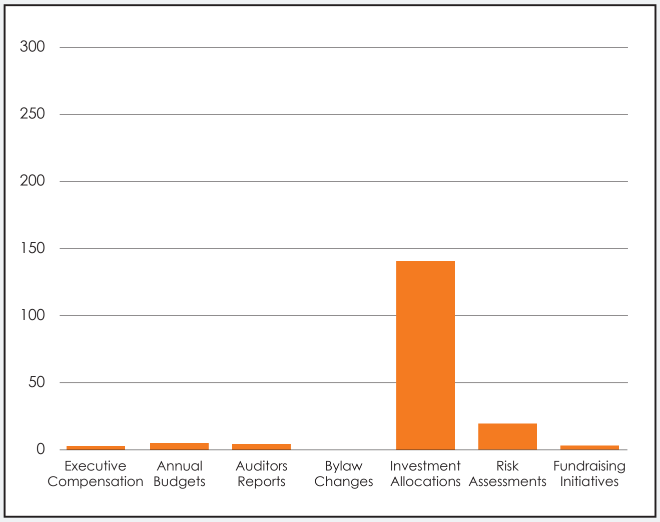


Figure 30F. Finance Committee

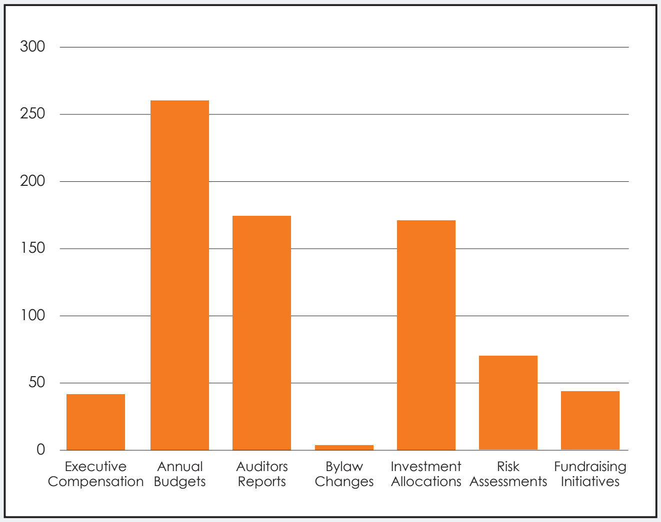


Figure 30I. IT Committee

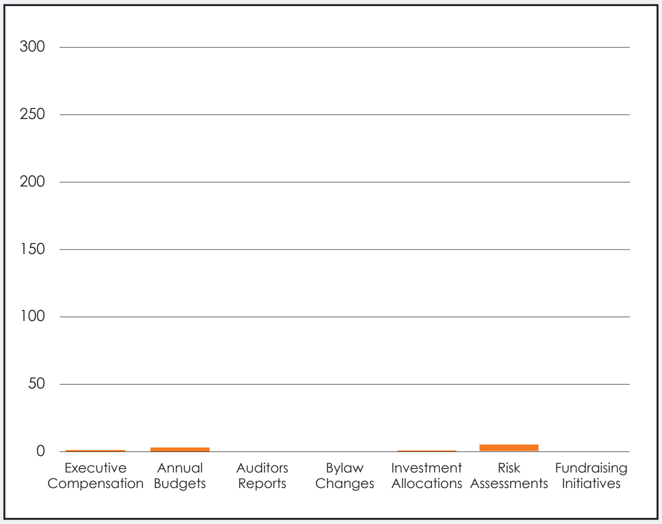


Figure 30J. Risk Committee

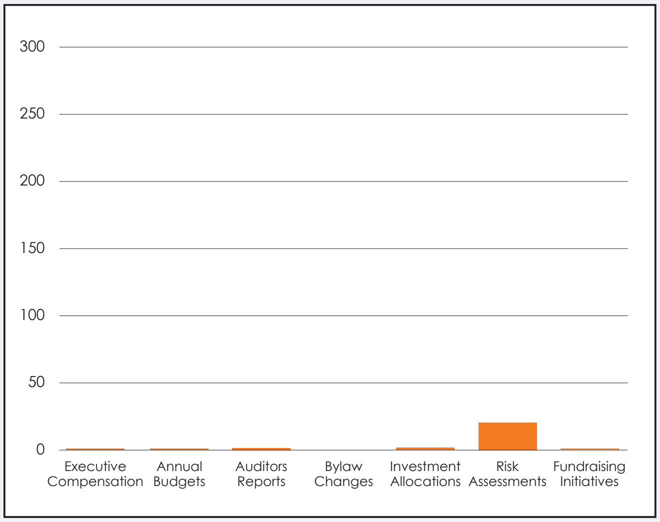


Figure 30K. Nominating Committee

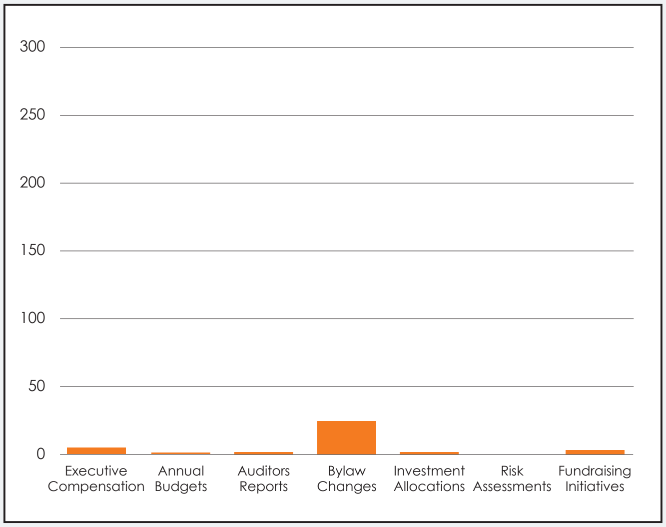


Figure 31. Annual Contribution

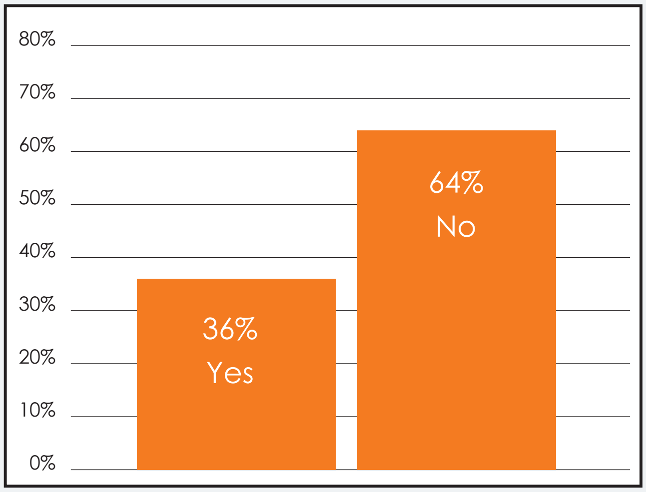
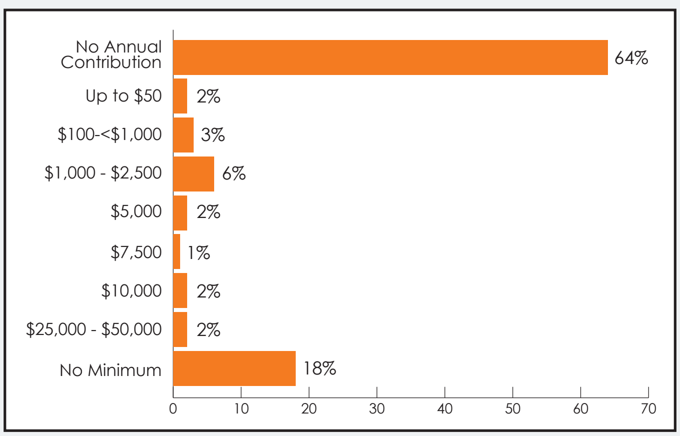


Figure 32. Minimum Contribution



$175 billion

The estimated value of 64.5 million volunteers with 7.9 billion hours of service.*

36% of respondents reported that their **directors are required to make an annual contribution to their organization**. While the majority (64%) do not require a minimum contribution, 6% require an annual contribution of $1,000 to $2,500 and 5% require annual contributions between $5,000 and $10,000, with 2% requiring annual contributions of between $25,000 and $50,000 "give or get."

* *Independent Sector: http://www.nptrust.org/philanthropic-resources/charitable-giving-statistics/*

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In addition to providing these organizations with a comprehensive array of tax and accounting services, we also help them identify work flow inefficiencies, implement stringent governance and internal controls processes, leverage technology and IT infrastructure, and more effectively manage capital and planned giving campaigns.

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