

## **MEMORANDUM**

TO: Board of Directors, SGC International  
FROM: Alexandra Rissi  
DATE: June 13, 2017  
RE: Governance Recommendations

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### **BACKGROUND**

The Board of Directors of SGC International (“SGCI”) has asked for our advice regarding payments made to the Conference Coordinator and board governance best practices going forward.

SGCI’s 2017 Conference Handbook provides that the Conference Coordinator is a paid staff member of SGCI. The Conference Coordinator facilitates planning and implementation of the annual SGCI conference and is compensated through a \$15,000 USD honorarium payable in three installments and “an additional bonus of 10% of SGCI hosted conference revenue after all accounts are settled.” The Conference Coordinator is a signatory on SGCI accounts related to the conferences and has authority to make purchases for conference related business. Additionally, the current Conference Coordinator serves in a separate capacity as a voting member of the SGCI Board.

In previous years, the Conference Coordinator has been responsible for calculating her bonus after accounting for all conference revenue and expenses. Recently, there has been some concern about how the bonus has been calculated and whether such calculation has resulted in an overpayment. A review of conference revenue and expense statements for 2016 and 2017 reveal that an overpayment may have been made when revenue is calculated net of SGCI contributions. However, the payment guidelines are not clear that the bonus is to be calculated net of SGCI contributions. Although payments made to conference coordinators in the past have been made net of SGCI contributions, this practice is not included in the payment guidelines.

### **RECOMMENDATIONS**

Our review has resulted in some recommendations regarding the calculation of the bonus but focuses more deeply on governance as clearer policies and procedures, segregation of duties, and better conflict management would go a long way to avoiding issues like this in the future.

With regard to the calculation of the bonus, the language of the bonus payment calculation provided in the 2017 Conference Handbook does not provide sufficient clarity regarding how to calculate the bonus to determine whether the 2016 and 2017 bonus payments were accurate. As the Conference Handbook is currently worded, there are multiple ways to calculate the bonus payment. Although calculations provided by an independent accountant show a variance of between \$1,000 USD and \$3,000 USD, this variance could be based on information that was known to the Conference Coordinator and not reflected in the 2016 and 2017 revenue and expense

statements provided. For instance, some line items were miscalculated in the revenue and expense statements and some revenue items were not further broken down into line item detail.<sup>1</sup>

The bonus payments made in 2016 and 2017 appear to have been calculated net of SGCI contributions, which is similar to how payments were calculated in past years. Due to the ambiguity of the payment terms, it is possible that the Conference Coordinator used a reasonable method to calculate the bonus and SGCI need not take further action to recover any amount of the payment.

To reconcile the amount paid to the Conference Coordinator and the amounts calculated by the independent accountant, the Board should ask the Conference Coordinator to provide details regarding how she calculated revenue and expenses for the conference broken down into greater detail. Future contracts should provide a detailed example of how to calculate the bonus and should be capped at an amount that is reasonable based on the services performed.

Going forward, SGCI should implement policies and procedures that ensure proper segregation of duties and conflict management. To eliminate conflicts of interest, we recommend that any Board member who wishes to contract with SGCI as a vendor on an ongoing basis should step down from his or her Board position while acting as a vendor. If other factors make stepping down impractical, then at a minimum, the conflicted Board member should disclose the conflict and recuse him or herself from discussions and votes regarding the matter. This includes leaving the meeting room when the matter is discussed and voted on.

Additionally, contracts with vendors should be negotiated at arm's length to ensure that they are fair to SGCI and that payment is justified in light of the work performed and comparable to payment of similarly situated service providers. SGCI should obtain fee quotes from multiple providers to ensure compensation is reasonable in light of the work performed. SGCI should also ensure that vendors report to the chief executive or to independent members of the Board or a Board committee.

Where payment is to be made in the form of a revenue based bonus, the bonus calculation should be clear (consider including an example) and should be capped to ensure that the bonus does not result in excessive compensation that is not commensurate with the work performed.

A. Bylaws. SGCI should revise its bylaws to clarify and simplify SGCI's governance structure. Many nonprofits include provisions in their bylaws that are old-fashioned, unnecessary, redundant, or that complicate rather than streamline governance. Generally, bylaws should not include information that will change frequently. Rather, they should reflect the fundamental rules governing SGCI that are not likely to change. Staff job descriptions, detailed committee charters, rules for conducting the annual meeting, guidelines for events, etc. are better suited for board resolutions or SGCI's policies and procedures manual.

Further, processes and procedures that are ignored in practice should be left out. If the Board is not going to carefully adhere to procedures, it is better to omit them. If the processes and

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<sup>1</sup> The 2016 and 2017 revenue and expense statements both contained mathematical errors which increased the variance. Once corrected, the variance for 2016 is \$(1,280.23) USD and \$(3,346.77) USD for 2017.

procedures called for in the bylaws are not followed, those who disagree with Board action may find a way to challenge that action based on a technicality.

B. Segregation of Duties. Ideally, SGCI should implement an internal control system that segregates duties so that the duties of authorization (signing a check or approving a transfer of funds), custody (having access to blank checks or the ability to establish a funds transfer), and recordkeeping (the ability to record the transaction in the accounting system) are divided between multiple individuals such that no one individual may complete a transaction from start to finish. Finally, SGCI's disbursements policy should require reconciliation of bank accounts in a timely manner by someone who is independent of the accounts payable process. The bank reconciliation should also include a review of the bank statement and check images that are returned with the bank statement for unusual transactions.

C. Policies and Procedures. Policies and procedures are the Board's plan for how to run SGCI. Policies guide SGCI in its daily course of action, and steer the Board as it works to fulfill SGCI's mission. Not only do policies provide direction, but they also make it easier for the Board to handle difficult situations in the most objective and ethical way.

Policies are different from bylaws. Policies, as distinct from bylaws, focus on an organization's daily operations and practices. The policies address issues related to the Board, but also issues related to finances, conflicts of interest, personnel, donations and more.

Some organizations set dozens of policies and others run fine on just a few. Below is a summary of the key governance policies that we recommend SGCI consider implementing.

1. Conflict of Interest Policy. A Conflict of Interest Policy is a de facto Internal Revenue Service requirement. If a member of the governing body is found to have a conflict of interest with respect to a financial transaction that results in excessive payments, it can put both the nonprofit and the governing body member at risk.

To manage conflicts and avoid penalties, we recommend SGCI take steps to address the conflict and record those steps in its meeting minutes. Such steps could include the member with the conflict disclosing the conflict, not participating further in any decision making related to the matter creating the conflict (and leaving the meeting room during discussions and votes on the matter) or stepping down from the governing body. All such actions must be carefully documented in contemporaneous meeting minutes.

The situation could also be addressed by utilizing a process in which SGCI generates disinterested bids or hires a consultant to examine the terms of the relationship and in light of the analysis determines that the terms of the compensation arrangement are fair and reasonable. Another option is for the tax-exempt organization to end a business relationship that gives rise to the conflict.

Each director should sign a conflict of interest disclosure annually, and the Board should review the policy annually. If a Board or staff member violates the policy, SGCI should consider taking disciplinary steps.

2. Compensation Policy. A compensation policy aims to provide procedures by which exempt organizations may determine reasonable compensation for their officers, staff, and directors. A compensation policy both defines the individuals whose compensation must be reported on Form 990 and assures that the review and approval of compensation for such individuals are conducted according to Internal Revenue Code procedures and related regulations. A compensation policy provides a consistent basis for compensation decisions; provides a procedural framework for making such decisions; increases compliance with federal and state laws; reduces risk to SGCI and its officers and directors for compensation which constitutes an improper private benefit, private inurement, or excess benefit transaction; and enhances the confidence of donors, members, and supporters of SGCI. Importantly for SGCI, a compensation policy will ensure that the Board has sufficient oversight of all compensation, including the manner in which it is calculated and payable.

Additionally, SGCI should avoid compensation arrangements in which individuals are awarded a bonus based on revenue. In these situations, it is possible for the individual to obtain a windfall that is not comparable to the work performed. Such a windfall may be seen by the IRS as an impermissible excess benefit transaction, subjecting SGCI and those who approved the excess benefit transaction to penalties. Should SGCI decide to pay compensation based on revenue, the Board should retain the authority to approve such compensation before it is paid and cap it at a reasonable amount commensurate with the work performed.

3. Signature Authority Policy. A signature authority policy delegates permission to execute transactions and permission to approve transactions for execution up to established limits. In situations where SGCI will contract with vendors, SGCI should retain ultimate authority to approve transactions which are negotiated by the vendor. However, vendors should not have authority to bind SGCI. Rather, vendors should report to the Board or a Board authorized committee, which will then have authority to assent to contracts negotiated by the vendor.

## CONCLUSION

To summarize our recommendations, we recommend that the following changes occur as soon as possible:

- Obtain additional detail about how the 2016 and 2017 bonuses were calculated to determine whether the payments were accurate;
- Restate Bylaws,
- Segregate duties such that different people are responsible for authorization, custody, recordkeeping and reconciliation;
- Implement a Conflict of Interest Policy;
- Implement a Compensation Policy; and
- Implement a Signature Authority Policy.

Going forward, we recommend that SGCI require Board members who wish to work as vendors step down from the Board to eliminate conflicts and establish committees to oversee vendors, negotiate vendor contracts, and approve payments.