The Role of Transparency in Association Governance

Anne M. Cordes, CAE, Mark Engle, DM FASAE, Jed R. Mandel, JD

Introduction

The concept of transparency is often evoked by citizens demanding more accountability from government; consumers seeking more information from businesses; shareholders seeking more information from corporations; and, increasingly, members asking for more openness from their associations.

In the name of transparency, some association members ask to be given board meeting agendas and background materials, and to attend and even participate in board discussions, in person or virtually. Some members also evoke the concept of transparency when they press individual officers and directors to share their personal positions on issues. If board members "speak in one voice," as they are obligated to do by their fiduciary duty of obedience, some members suspect the board is not being transparent. The concept of transparency also is frequently associated with responsiveness to member needs and the concept of being member driven.

But there is not a clear understanding of the impact of the policies and practices called for in the name of "transparency" and which are assumed to be beneficial.

When association boards face pressure from members to demonstrate transparency, it is important to have a common understanding of what is meant by the term and to know whether policies and practices requested or demanded in the name of transparency are compatible with effective governance.

This article is a review of the literature about transparency in management and governance and its impact on organizational performance and focuses on the implications for nonprofit associations in light of the behavior and practices of high-functioning boards of directors. The following research questions informed this literature review:

1. Is there a common understanding of the term transparency, and what characterizes transparent behavior in nonprofit governance?
2. What is the impact of transparency on organizational performance?
3. What is the role of transparency in association governance?

Is there a common understanding of the term transparency, and what characterizes transparent behavior in nonprofit governance?

According to *Webster's*, transparency is characterized by "visibility or accessibility of information especially concerning business practices." According to Wikipedia, transparency (as used in science, engineering, business, the humanities, and in a more general social context) implies openness, communication, and accountability.

Kristin Clarke (2010) points to the important role that the Sarbanes-Oxley Act of 2002 has played in creating a new era of transparency and accountability in the corporate world. "Finances, of course, top the list for scrutiny, followed closely by governance and communication." But Clarke points out that, in addition to financial information, GuideStar and others call for "public clarity about how board nominations occur, are vetted, and are executed; how the board and CEO make decisions; how money is allocated; and how the mission is progressing" (p. 3).

In *Transparency: Creating a Culture of Candor*, Warren Bennis, Daniel Goleman, and James O'Toole define transparency as "the free flow of information within an organization and between the organization and its many stakeholders, including the public," and further explain that "When we talk about information flow, we are not talking about some mysterious process. It simply means that critical information gets to the right person at the right time and for the right reason" (pp. 3–4).

Legal obligations

While Renz (2010) states that "… the board has the ultimate authority and responsibility for the performance of a nonprofit organization and….it is the board that ultimately is accountable to the community, to the state, and to clients and beneficiaries" (p. 126), to what extent are association boards legally obligated to share information in the name of transparency? There are several important ways in which the governance of nonprofit organizations, especially associations, differs from that of public bodies, school boards, government agencies, and for-profit corporations, with varying implications for transparency.

For example, nonprofit organizations are not subject to the rules of the U.S. Securities and Exchange Commission (SEC), which might suggest that they are less carefully scrutinized than for-profit corporations. But the Internal Revenue Service (IRS) requires nonprofit organizations to disclose a wealth of information (on the Form 990 Return of Organization Exempt From Income Tax) about the organization's exempt and other activities, finances, governance, and compensation paid to certain persons. That is not required of publicly traded companies. Conversely, of the many governance reforms mandated by the Sarbanes-Oxley Act, only one—dealing with document destruction—applies explicitly to all persons and entities, and thus to nonprofits, although most commentators have concluded that the so-called whistleblower protection provisions also apply to nonprofits.

Nonprofit corporations are created when they apply for and are granted nonprofit corporate status by the act of a government body, usually a state government. Nonprofit corporations maintain their status by complying with the requirements of that government body. Thus, most associations are governed by the nonprofit corporate act of one of the 50 states. While those laws differ, they generally are consistent in not having specific provisions about transparency.

In limited circumstances, organizations that have the authority of the state, receive certain kinds of government funding, or provide certain services to a state, may be subject to Freedom of Information Act requirements and "sunshine laws" that require board meetings to be open to the public. For the most part, such laws do not apply to associations. Indeed, there are no state laws that provide association members the right to attend board of directors meetings or receive unfettered access to association information. In Illinois, for example, voting members have the right to examine—but not copy—the corporation's "books and records of account" and minutes, and to make extracts therefrom, at any reasonable time, but only for a proper purpose. Such requests for records must be made in writing and specify the records sought. If the organization denies the request, the member can file suit. But, if the request is to examine "books and records of account," the voting member bears the burden of proof of a proper purpose. If the request is to examine minutes, the burden of proof is on the organization to show that there is not a proper purpose. (See General Not For Profit Corporation Act of 1986, 805 ILCS 105/107.75.)

It is quite clear and consistent across all states that a long line of case law and, in many instances, state law, obligates directors of all corporations to fulfill their fiduciary duties at all times. Those duties are often at odds with false notions of transparency in corporate governance.

Fiduciary duties of directors

The legal requirements are clear, uniform, and straightforward: Directors have a fiduciary obligation to perform their roles with care, loyalty, and obedience. The duty of care requires that directors perform their functions with competence. They must exercise the care "a reasonably prudent person would exercise in a like position and under similar circumstances." The duty of care requires directors to act in good faith, participate in meetings, be prepared, ask questions when necessary, and exercise independent judgment. The duty of care allows directors to delegate their authority (but never their responsibility) to staff or committees and to rely on the advice of third parties such as attorneys, accountants, and financial advisors in their decision-making.

The duty of loyalty requires directors to faithfully pursue the organization's interests, which must be primary to the financial or other interests of the director or another person or organization. Directors may not use their position, or information gained from their service on the board, to secure a personal benefit or to take a business opportunity that belongs to the organization. The duty of loyalty requires directors to maintain the confidentiality of board discussions; to disclose actual, potential, or perceived conflicts of interest; and, in some cases, to abstain from participating in certain matters to manage conflicts.

The duty of obedience requires directors to faithfully pursue the organization's mission and decisions and abide by its rules and policies. Directors must support, help implement, and not undermine the board's decisions.

Thus, members' requests to attend—or even participate in—board meetings, access an individual board member's voting records, and receive the details of board discussions are all in direct conflict with directors' fiduciary duties to maintain the confidentiality of board deliberations and support the board's decisions. How should association leaders respond to members' requests for more openness, communication, and accountability on the part of boards of directors, both as a corporate body and as individual directors and officers?

What is the impact of transparency on organizational performance?

An exhaustive search of the literature on transparency and organizational performance uncovered little research in the association sector. While much has been written about transparency in fund-raising and the uses of funds in the nonprofit arena in general, this adds little to our understanding of the impact of transparency on performance in associations and is not the focus of this article. Several studies of the impact of transparency on organizational performance in the corporate environment, however, do offer insights.

Transparency in for-profit corporations

Bennis and colleagues (2008) explore "the forces that conspire against candor and transparency within organizations, and the often disastrous results when those qualities are lacking" (p. 3). Their interest is primarily in the healthy flow of information within institutions, where they argue that "followers must feel free to speak openly and leaders must welcome such openness" (pp. 3–4). Drawing on examples from governmental institutions and companies like General Electric, Enron, and Johnson & Johnson, the authors point out that successful outcomes are often linked to open discussion and debate reflecting multiple points of view: "The wisest leaders seek broad counsel … because they need it. There's a compelling reason to become more open to information from people at every level…." (p. 25).

In *The Transparency Paradox* (Bernstein, 2012), which also examines transparency in the for-profit sector, author Ethan S. Bernstein describes a rigorous field experiment at a large mobile phone factory in China, in which he tested the impact of transparent organizational design on workers' productivity and organizational performance. Bernstein points out that organizations' quest for worker productivity and continuous improvement have fueled "a gospel of transparency in the management of organizations," and "most modern-day facilities are designed to provide near-perfect observability of the actions and performance of every employee, line, and function" (p. 182). Empirical evidence suggests that increased awareness of being observed had a negative impact on some aspects of performance. Even a modest increase in privacy—that is, a decrease in the amount of visibility or "transparency"—significantly improved the performance of the group (p. 181).

In *The Transparency Trap* (Bernstein, 2014), published in the *Harvard Business Review* two years after *The Transparency*

Paradox, Bernstein posits that, while "a long stream of research tells us that, in the presence of others, people do better on repetitive, practiced tasks … [they do] … worse on learning tasks that call for creative thinking" (p. 8). The paradox of transparency is that observing workers may counterintuitively reduce their performance. That is, removing physical barriers like walls to increase observability only created the illusion of transparency, as it triggered harder-to-detect hiding behavior and increased the likelihood that the actors would perform for the audience. "[When the walls were removed] it became clear almost immediately that operators were hiding their most innovative techniques from management so as not to 'bear the cost of explaining better ways of doing things to others' or alternatively 'getting into trouble' for doing things differently'" (Bernstein, 2012, p. 188).

The need for privacy

Bernstein's theory of a transparency paradox (2012) is supported by a vast interdisciplinary body of theory, primarily outside of the management sciences, that argue for the existence of a fundamental human need for privacy—the opposite of transparency—defined as "the ability to control and limit physical, interactional, psychological, and informational access to the self or to one's group" (p. 194).

Research across different industries, cultures, and types of work reveal that it is critical for leaders to mitigate transparency with zones of privacy. Organizations that consistently achieve the most innovative, productive, and thoughtful work from their employees use boundaries like physical barriers around work groups—zones of attention—to avoid exposing every little action to the scrutiny of a crowd and defined periods of experimentation—zones of time—to give employees time to prepare for and experiment within specified windows of privacy (Bernstein, 2014, p. 4).

The work of the board

Can association boards learn from the research about the impact of transparency on performance in the corporate sector? Board members fulfill their responsibilities within the context of the organization and the board as a group. The ability of a group of individuals to come together as a decision-making body is critical to success in each of these areas of responsibility. Nancy Axelrod, in her article *In the Boardroom Culture Counts*, advises that "Leaders of the most effective boards take deliberate steps to transform an assembly of talented individuals into a well-integrated group" characterized by trust, teamwork, candor, and constructive conflict (Axelrod, p. 8). This is supported by Cornforth and Brown's study of nonprofit boards, which reveals that the active management of situational factors that facilitate participation—including supportive meeting structures and group norms that encourage discussion—is closely tied to enhanced organizational performance (Cornforth and Brown, 2014).

Those conclusions echo the results of Jeffery Sonnenfeld's examination (2002) of corporate governance meltdowns at companies such as Enron, WorldCom, and Tyco. In those situations he did not find any broad patterns of corruption or incompetence among the boards. Instead he found that the key difference between those boards and higher-functioning groups was a climate of trust and candor among board members and between the board and management; a willingness to share information with board members openly and on time; a culture in which management encouraged lively discussions of strategic issues by the board and board members felt free to challenge one another's assumptions and conclusions; and a commitment to assessing the performance not only of the board as a group but also of individual board members. Those conclusions support the import of openness among board members, but not necessarily between board members and non-board members.

"What distinguishes exemplary boards is that they are robust, effective social systems.…Team members develop mutual respect; because they respect one another, they develop trust; because they trust one another, they share difficult information; because they all have the same, reasonably complete information, they can challenge one another's conclusions coherently; because a spirited give-and-take becomes the norm, they learn to adjust their own interpretations in response to intelligent questions" (Sonnenfeld, 2002, p. 109). While it is essential for boards to develop trust, having outsiders observe the board tends not to foster that trust.

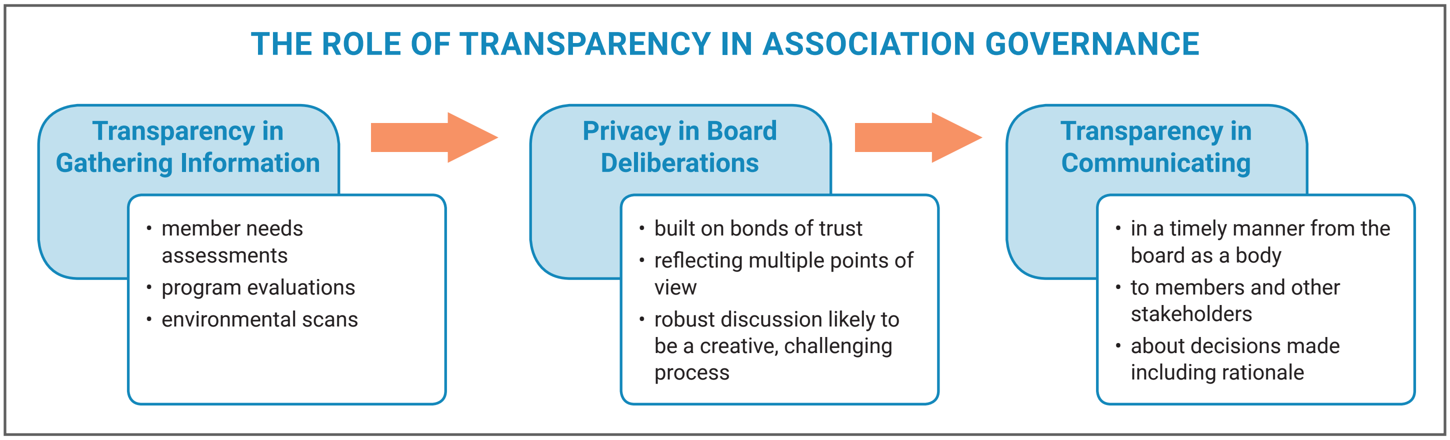
It appears that the same characteristics drive group performance across organizational boundaries. That is, assembly line workers and boards of directors in both for-profit and nonprofit sectors operate most effectively in environments in which they feel safe to be open with each other about what they know and don't know, to change their minds, and to place more importance on the success of the group than on their own performance.

What is the role of transparency in association governance?

Can the robust social systems that characterize effective organizations be developed in a group that is under surveillance? Bernstein's research suggests that the visibility created by transparency can leave employees feeling exposed, self-conscious, and inhibited (Bernstein, 2014, p. 8). As a result, they may actively conceal what they are doing—even when they are making improvements. This in turn reduces productivity and, paradoxically, transparency. Similarly, boards of directors may respond to members' demands to observe board meetings by "performing" as expected in public board meetings, by reading reports or discussing noncontroversial topics. In turn, boards may call executive sessions more often to "hide" their most effective behaviors while dealing with substantive issues and thus, in the eyes of would-be observers, decreasing transparency.

Instead, associations can function most productively and achieve the highest levels of organizational performance by balancing transparency and privacy, aiming for

- openness in gathering information for informed decision-making on the part of the board
- respect for zones of privacy that the board needs to build a robust culture
- timely communication to members and other stakeholders about board decisions, including process and rationale.



Transparency in gathering information

According to Bennis et al. (2008), "Whenever a tight-knit decision-making group fails to collect all relevant data and candidly analyze it, bad decisions are liable to be made" (p. 39). This is supported in Cornforth and Brown's work on nonprofit boards, where the best decisions are made not when one individual directs and decides but through a negotiated and shared process that works to mitigate individual and group biases (Cornforth and Brown, 2014, p. 88). It is an axiom of association management that "The most productive association leaders will be sensitive to the membership's needs, wants, and interests. You can accomplish this by ensuring that the greatest number of voices will be heard so that the decisions of the board are truly representative of your industry or profession" (Yep, 2016, p. 34).

Thus, association members with the organization's best interests in mind are encouraged to respond to surveys, complete program evaluation forms, and participate responsibly in elections to do their part to ensure that the right information gets to the right people at the right time.

Privacy in board deliberations

Research shows that "Even when everyone involved had only the best of intentions, being observed distorted behavior instead of improving it" (Bernstein, 2014), while "even a modest increase in group-level privacy sustainably and significantly improves … performance. Qualitative evidence suggests that privacy is important in supporting productive deviance, localized experimentation, distraction avoidance, and continuous improvement" (Bernstein, 2012).

To nurture these behaviors, leaders are advised to be intentional about seeking all of the available information, particularly about members' needs and the broader environment in which the association operates, and to ensure that diverse points of view are represented and considered. The research conducted by Taylor, Chait, and Holland (1996, p. 45) in the nonprofit sector indicates that the most effective boards continuously draw upon members' multiple perspectives to avoid the trap of "group think." Encouraging active dissent and welcoming the opinion of a devil's advocate, for example, increase the likelihood of a better outcome (Cornforth and Brown, 2014). Similarly, efforts should be made to draw out introverts, who typically shine when creative approaches are needed (Tobenkin, 2012).

Transparency in communicating decisions

Bennis et al. (2008) note that "It almost goes without saying that complete transparency is not possible–nor is it even desirable, in many instances." Associations may have legitimate interests in withholding information from time to time and under certain circumstances. "Not all discussions or processes should be public. The concept [of transparency] should not be interpreted as a decree to disclose every document or require guests at every meeting" (Harris, 2015).

Nevertheless, transparency can be achieved by "getting critical information to the right person at the right time and for the right reason" (Bennis et al., 2008, pp. 3-4). With the widespread use of social media, leaders can no longer hope to hide awkward or damaging information. Boards of directors are advised to be clear about their business practices—for example, who makes decisions, when, and how—and to share important information in a timely manner with members and even other stakeholders who may have an interest in the issue. While association members may request details about board discussions or individual director's and officer's votes, members have no right to such information. Associations should strive to educate their members about the board's fiduciary duties and what constitutes best governance practices.

Conclusion

Accountability practices and safeguards designed to prevent abuse—like association members observing board meetings—"will be meaningless if they are activated without attending to the manner in which board members work together, where they decide to spend their time, and how management and the board interact with one another" (Axelrod, 2013, p. 14). Associations are best served when members can share information about their needs, and boards are allowed time and space, free from attention and judgment, to develop a culture conducive to effective governance. By balancing transparency and privacy, associations can function most productively and achieve the highest levels of organizational performance.

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