Executives’ Views of Factors Affecting Governance Change in a Not-for-Profit Setting

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ABSTRACT

Knowing the factors that executives deem critical to governance change can improve our understanding of how such changes come about and can help us evaluate those changes. Interviews with business and finance executives at 11 colleges reveal the importance to governance change of chief executive and board member leadership and interactions, as well as executive communication style. Costs are clear constraints to action, particularly since benefits are not quantified and are difficult to describe. Efforts to discuss governance with internal stakeholders require persistence to overcome narrow, individualized concerns. Communication about governance to external stakeholders is rare and represents a missed opportunity for stakeholder feedback and the development of trust. Executives appear willing
to adopt governance forms without considering the idiosyncrasies of their institutional field, limiting the working definition of governance and its potential. For corporations and not-for-profit enterprises these findings hold implications for the context in which leadership is exercised and the shape of governance structures. They also pose a fundamental ethical dilemma for leaders to address.

**INTRODUCTION**

Before leaders can initiate effective change, they must understand which environmental conditions and organizational traits are likely to support or obstruct their efforts. To better assess leadership, therefore, we must view these factors from the leader’s perspective. This study elicits firsthand evidence of the factors that executives identify as critical to the pace of change in enterprise governance.

Our aim is to examine some of the antecedents to ethical leadership rather than instances of that leadership. To do so, we investigate executives and governance change. We focus on executives, given the important part they play in their organization’s ethical culture. We look at changes in governance because governance shapes the context in which leadership is exercised. Thus, knowing the factors that executives deem critical to the pace of governance change can help us understand how such changes come about and may aid subsequent evaluation of those changes. Such knowledge is particularly important because many changes in governance practices are incremental rather than revolutionary, accumulating over time to form the organization’s accepted set of behaviors. Therefore, these changes and the process of change can more easily escape attention than would extensive overhauls of governance practices brought about by legislation.

We adopt Blair’s view of governance as “the whole set of legal, cultural, and institutional arrangements that determine what [enterprises] can do, who controls them, how that control is exercised, and how the risks and returns from the activities they undertake are allocated.” Governance change is thus the process of establishing, altering, or ending these arrangements. Treviño’s
person-situation interactionist model helps reveal the importance of governance. The model indicates that situational factors, including such aspects of organizational culture as the enterprise’s “normative structure” and expectations for individual responsibility, interact with individual traits and cognitive development to affect ethical decision making. Governance thus can be viewed as moderating the development and exercise of ethical behavior through its ability to shape an enterprise’s situational factors. For example, governance influences the way executives and others understand “what is and what is not appropriate behavior,” a key component of an organization’s normative structure. Similarly, governance processes establish expectations for individual responsibility implicitly as part of regulating the acquisition and use of learning in the firm or explicitly through such mechanisms as codes of conduct.

Our study examines the setting for governance change as seen by executive business officers at a sample of colleges and universities. As discussed below, these institutions are of interest in this area because of recent attention focused on their governance and because of their accessible structure. Through interviews conducted at a time when many business officers in higher education had reason to think of “next steps” in their organization’s governance, we provide a perspective on executives’ reasoning as the process of change is under consideration, thus avoiding some of the complications involved in retrospective assessments of change. By drawing attention to business officer awareness of governance in the absence of a business disaster, we offer a counterbalance to studies of governance processes brought about by cataclysms and can thus assess some of the steps involved in gradual governance change. Although we focus on a not-for-profit setting, we also draw implications for governance changes in the corporate context.

This work holds practical value as well. We believe it is important for institutions to understand the pace of governance change in their field. It is reasonable to expect that slow responses to the need for change will increase the likelihood that an institution will be forced into costly, stressful action in the face of such crises as financial malfeasance, allegations of illegal acts, challenges to reputation, or disagreements with civic organizations. On the other hand, timely responses can allow an institution to establish or strengthen relationships with significant stakeholders, improve
controls, and increase knowledge of internal operations. Thus, we believe understanding the nature of governance change allows executives better opportunities to show stakeholders how the enterprise is responsive to their concerns while pursuing its mission.

The discussion continues with our motives for examining institutions of higher education and some background on governance challenges at those institutions. We follow this with a description of our method and the presentation of our findings. Implications of the research and suggestions for further investigation conclude the paper.

**GOVERNANCE AND INSTITUTIONS OF HIGHER EDUCATION**

Colleges and universities offer a suitable context for an investigation of governance changes for two reasons. First, as detailed below, different groups have begun to scrutinize not-for-profit governance as a result of publicity over corporate governance failures. Colleges have been caught up in this scrutiny, causing executives to focus attention on governance issues. Second, the business function at a college is usually separately identifiable from other functions, such as faculty affairs, student life, or property maintenance. Not only does this help researchers focus on appropriate participants for their study, but it also facilitates discussion of the different kinds of stakeholders involved, thus enriching the analysis while permitting parallels to the corporate sphere.

This study focuses on college financial executives, since the finance function is central to college business operations. The importance of endowments and financial health to an institution’s survival underscores the vital role that finance plays in governance. Financial executives’ frequent contact with external business advisors (such as lawyers, accountants, and financiers) expands the range of relationships over which their college’s governance procedures must be effective. Simultaneously, it exposes executives to other possible governance structures. Additionally, external pressures for the college to pattern itself on corporate activity, as discussed below, are typically aimed at the institution’s finance function.
A focus on the business side of the institution acknowledges the rise of one particular model of governance in academe. Over the past 50 years, campus governance models have evolved from faculty-dominated collegial systems to rational models led by institutional presidents.\textsuperscript{14} Whereas the collegial model of campus governance, characterized by a strong faculty coming to consensus-based decisions, is still evident in faculty affairs such as tenure and promotion decisions, the rational model of governance increasingly dominates administrative behavior. The rational model emphasizes the enterprise’s values and objectives, alternative courses of action, centralized decision making, understanding of consequences, and maximized goal achievement.\textsuperscript{15} Thus, colleges have implemented such traditional corporate practices as strategic planning, marketing, customer relationship management, outsourcing, and measurement of performance outcomes.

Even within the context of this rational model, however, relationships require trust in order to develop and endure.\textsuperscript{16} While trust can be established when parties create and sustain mutually beneficial economic relationships,\textsuperscript{17} college leaders must build trust with stakeholders whose relationships with the enterprise range from financial to political to emotional. These include students, staff, faculty, and service providers, as well as alumni/ae, donors, parents, bond agencies, insurers, foundations, and federal, state and local governments. Trust may be constructed using incentivized monitoring mechanisms, as suggested by agency theory,\textsuperscript{18} or stakeholder dialogues, as described by stakeholder theory.\textsuperscript{19} Governance, by establishing and guiding the inner workings of the enterprise, provides both a monitoring system embodied in policies, procedures, and controls, and an avenue for dialogue through the way it connects these items to daily business processes and higher-level planning.

College governance affects many parties. Municipalities are concerned about institutions’ effects on the local economy and civic engagement. Faculty and staff are intimately affected by the financial, operational, and reputational outcomes of their employer’s governance processes. Furthermore, poor governance blights the educational experience for students, parents, and faculty by affecting the campus ethos, access to financial resources, relationships with recruiters, and institutional reputation. Conversely, good governance can support an institution’s ability to distinguish itself in the community and in the marketplace for faculty and students.
This study is set in U.S. institutions. Particulars of the U.S. context, described below, played a part in the study’s motivation, but corollaries can be found in other national settings. In the United States, there is evidence that many consider their trust in not-for-profit institutions, including colleges, to be out of balance or breached. Indeed, institutions of higher learning have not been immune from fraud, malfeasance, corruption, unethical behavior, and lack of concern for stakeholder groups. The press has reported instances of professors falsifying research data, athletic coaches providing players with false academic credits, administrators fraudulently obtaining federal funds, medical schools settling allegations of fraud in their research, and “diploma mills” defending their practices. Other less dramatic issues add to these concerns about pending breakdowns in stakeholder relationships with academe. For example, the U.S. House of Representatives’ Education and Workforce Committee found that “higher education [is] in crisis due to exploding tuition rates, [as] students and parents [are] losing patience with disproportionate cost hikes.” Further evidence of growing public attention to these issues comes from bond rating agencies that have expressed concerns about such aspects of college governance as the financial acuity of trustees, the handling of conflicts of interest, and the institution’s ability to focus on its mission in times of declining financial support.

The role that higher education plays in today’s economy virtually assures that stakeholders will consider the extent to which external interventions are needed to reduce the likelihood of such breaches of trust. For example, shortly after passage of the Sarbanes-Oxley Act of 2002 (the Act), concerns that corporate failures may have counterparts in the not-for-profit arena spurred lawmakers to consider a legislative response that would impose governance guidelines on not-for-profits. On the federal level, the U.S. Senate Finance Committee began deliberations on not-for-profit governance legislation. Even more activity on proposed not-for-profit legislation was driven by states’ attorneys general, since these officials typically have jurisdiction over the not-for-profits located in their state. Thus, within two years of the Act’s passage, 18 states contemplated legislation to regulate not-for-profits’ governance. By 2006, this had increased to 24 states. Although most of the legislative efforts in this time span were related to fund raising, many
were focused on internal control, administrators’ responsibilities, and disclosures, patterned on the Sarbanes-Oxley Act.

Whether legislation is passed or not, not-for-profits have found themselves pressured to consider the Sarbanes-Oxley Act as a model for their governance, even though it was not written with not-for-profits in mind.\(^{28}\) In fact, in response to these external demands, the National Association of College and University Business Officers (NACUBO) proposed guidelines for its members that mirror provisions of the Act.\(^{29}\) Given the publicity that the Act generated in not-for-profit circles, we structured part of each of our interviews to allow participants to discuss governance in terms of their likely responses to “Sarbanes-like” guidelines.\(^{30}\) Other aspects of our investigative method follow.

**METHOD**

We approached the chief financial executive (typically the vice president for finance or the controller) at 13 colleges to initiate our research. We generated contacts through the audit partners at public accounting firms and members of the NACUBO, as well as from our own connections. In order to provide a measure of control for differences caused by institutional size, all of the colleges we contacted could be considered “medium,” that is, having student enrollments approximately in the range of 2,500 to 5,000 or faculty numbering approximately between 200 and 500. Similarly, to control for mission, we chose only private (independent) colleges for our sample. To minimize regional differences, we targeted institutions within approximately 100 miles of the same major U.S. East Coast city. Of the 13 colleges contacted, one did not respond to our request and one declined an interview. At the 11 participating colleges, we conducted 15 semi-structured interviews involving 19 executives. Taken as a whole, the colleges in our sample enroll over 45,000 students (more than 31,000 of whom are undergraduates) and employ over 3,700 faculty. Based on their institutions’ financial reports, the interviewed financial executives collectively were responsible for managing over $5.1 billion of institutional assets, $876 million of revenues and fees, and $2.8 billion in endowments.

For additional insights and as a way of corroborating the views expressed by the college executives, we asked three of our
participating institutions if we could contact their audit committee. We were successful in interviewing two audit committee chairs. We also contacted partners and principals at three public accounting firms to get their views on governance in higher education. The three public accounting firms that we visited included the two firms that audit over 75% of the colleges in the region and a third firm that is closely involved in providing outsourced financial and internal control services to many of the research participants. Our interviews at these three firms involved seven executives. The list of our interviews appears in Appendix 1.

We used semi-structured interviews to gather our data. The semi-structured interview introduces a measure of consistency in data gathering across participants, while also allowing for the active construction of dialogue between the researcher and the participant. Each interview lasted between one and two hours. Except for the interviews with audit committee chairs, which were conducted by telephone, all interviews took place in person, with at least two of the authors present. In the structured part of our interviews, we asked participants for personal and institutional background information, as well as for details on setting institutional objectives, assessing risks, gathering information, communicating with stakeholders, and monitoring governance processes. We asked specifically about the roles of key decision makers in the business of the institution and about perceptions of Sarbanes-like provisions for governance at the participants’ institutions. Appendix 2 contains an outline of our interview protocol. Each interviewer took notes during the interview. Interviewers compared their notes for completeness and key topics covered immediately after the interview. Interviewers typed their notes and compared them again shortly thereafter. The research team met to discuss significant themes emerging from a review of all of the notes, where these themes were identified as those with frequent mentions among the body of participants and with no significant contradictory evidence noted.

**FINDINGS AND ANALYSIS**

The structured part of the interviews and respondents’ overall comments distinguished between the people involved in governance
and the processes of governance. The following discussion uses these broad categories. We summarize our key findings in Table 1.

**People**

It was typical for participants, without prompting, to mention discussions with the board or its audit committee about proposed governance legislation. For nearly two thirds of the colleges in the sample, internal deliberations on the issue were initiated or brought to the fore by board members who were dealing with the Sarbanes-Oxley Act at their corporations and who wanted to know the college’s attitude toward controls and governance. In the words of one audit committee chair, the Act presented the college with “a chance to do things a little differently” (Interview 15). But it appears that having such boundary-spanning trustees is not enough to

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**TABLE 1  Summary of Key Findings**

**People involved in governance change**
- Trustees dealing with similar issues at their firms often are the ones to raise questions about the college’s attitude towards controls and governance, or to keep governance issues under scrutiny.
- College presidents are instrumental in setting the tone for planning approaches to governance change and for communications about governance.
- The interaction between trustees and college executives may be self-reinforcing, supporting an atmosphere of more open communications among executives while leading trustees to take more strategic roles.

**Processes of governance change**
- Institutions are likely to take less costly steps in governance change first, such as forming an audit committee, summarizing control structures, or writing codes of conduct, ethics codes, conflict-of-interest statements, and whistleblower policies.
- A desire to save costs leads institutions to consider collaborations such as an outsourced, shared internal audit function or membership in a consortium to share suggestions for good governance practices.
- Communications use informal and formal channels and range from providing information to attempts at stakeholder engagement, despite difficulties in getting some stakeholders to look beyond their own concerns.
- Communicating about governance to internal stakeholders (staff, faculty) is more common than communicating to external parties (civic groups, students, applicants and their families, alumni/ae, donors).
- Discussions about governance change seem to follow a generalized, corporate pattern, thus minimizing institutions’ unique aspects.
move the discussion of governance along; the president must provide direction and momentum. As one vice president remarked, governance planning and communications were assisted by the tone set by his college’s president, who “gets buy-in from me and everyone else [as] a real implementer . . . into teamwork, teamwork, teamwork” (Interview 11). This was echoed by another financial vice president, who contrasted his current president as a “consensus builder” with the predecessor president, who “was a dictator—very closed-door, not open to new ideas” (Interview 17). The notion that the president could keep governance change off the institution’s agenda for a time came across in a third vice-president’s comment that his president is “not a forceful, ‘here’s my vision’ [sort] . . . I don’t know if he has a vision other than maintaining [our] position” (Interview 13). Thus, even when trustees actively spur executives to examine the state of the institution’s governance, it appears that the president’s attitude toward decision making is a key factor in enabling the governance discussion to take a form that can lead to change.

This interaction between the board’s inquiries and the president’s leadership seems to be self-reinforcing. In the instances where we noted that governance questions introduced by the board found a receptive audience among the college’s executives, the role of the board also seemed to be changing. More specifically, trustees who saw this receptivity on the part of the executives were also characterized as being strategically oriented rather than caught up in daily campus affairs. Discussing this transition, a chief operating officer described his board’s former involvement in such details as determining the amounts of individual student scholarships, saying, “Everyone wanted to be involved in everything. They all had their fingers in the pie instead of smelling the pie” (Interview 5). With the board’s increasing trust in the administration, however, he saw their emphasis shift to long-term planning. At the other extreme are boards that remain “very much internally focused . . . [not considering] where does the institution want to be down the road,” leading to discussions that are really just a “reaffirmation” of what the college is today, rather than a plan for what it can achieve (Interview 13).

The relationships between the trustees and president seem to find parallels in other executives’ internal leadership, as shown by their communication style. The same respondent who talked of his teamwork-oriented president remarked on the “close community”
of business executives, with “no fiefdoms or silos [and] no nasty e-mails” (Interview 11), while the participant who commented on his president’s lack of vision noted how his institution “doesn’t have a real hardwired management style—the VPs don’t communicate as effectively as they should” (Interview 13). At the same time, communication style seems to vary more with executives who are open to new ideas. In illustrating his efforts to build trust on campus and with board members, for example, one officer talked about communicating “not in a preachy way, but in a ‘doesn’t-this-make-sense’ way,” which included showing “that we’re thoughtful about what we’re doing” (Interview 5). A controller described discussions that were “more fact based” (Interview 6) rather than gossipy. Another vice-president mentioned consensus-building conversations that tried to establish rapport with potential dissenters by focusing on the question, “Even if you wouldn’t support this measure, would you go along with it?” (Interview 19).

To summarize this area, we can say that the roles of the institution’s trustees and president were prominent in respondents’ discussions. Trustees who actively span the boundaries between corporations and not-for-profits influence executives to examine governance issues that have corporate parallels, such as potential adaptation of the Sarbanes-Oxley Act to not-for-profits, or support those officers who have begun these examinations. Presidents who lead their executive team in examining governance are those who have a vision that they join to a style that invites communication. Trustees and the president appear to interact as leaders in setting the course for governance deliberations.

**Processes**

It is interesting to note that when our respondents talked about governance, nearly all of the activities they described concerned processes rather than structures. The only mention of structural changes came from two colleges that were considering adding a committee to their board (an audit committee for one and a self-evaluation committee for the other) and from one college that was questioning the role of its unionized faculty in managerial decision making. Drawing on the interview data, this “process” dimension emphasizes two themes: costs and benefits, and transparency and stakeholder engagement.
Costs and Benefits  Governance-related activity reflects executives’ perceptions of critical governance factors as tempered by pragmatic concerns. Our respondents’ sensitivity to practical matters means that their activities can be arrayed along a continuum that ranges from planning to operating-process change to strategic change. For example, while all the participating institutions were aware of at least the overall intent of the Sarbanes-Oxley Act and had discussed it with their board, in five instances these discussions led to a formal status report. Typically this was a matrix or summary comparing provisions in the Act to NACUBO’s (2003) recommendations for college adaptation of the Act, their state attorney general’s proposed legislative provisions, and the college’s present or targeted status. Such reports are an example of the early stages of planning governance changes, showing how the executives match general external factors to individual institutional particulars.

Moving beyond the planning stage, all respondents had at least begun work on some less controversial governance best-practice provisions. Thus, 10 of the 11 institutions had a written code of conduct, ethics code, conflict-of-interest policy, or whistleblower provision in place. All but one college had an audit committee of the board of trustees, and nearly two-thirds had a financial expert on the committee or were taking steps to add one. Only three mentioned requiring limits to the years an audit partner could serve the college or requiring that separate firms be hired for auditing and consulting.

While part of best practices, these steps are the less costly of those that can be taken. One respondent summed up the importance of costs by viewing these decisions as issues involving “not a cost savings, but how to avoid the costs” (Interview 6). Further evidence that costs are clearly a constraint to changes in processes was provided when nearly all of the participants said they were not considering such changes as having the president and CFO certify the reliability of the internal control system. The corporate corollary to this has been cited as particularly costly for firms in terms of both money and staff time. Corroboration that our respondents were not unusual in their concern for costs comes from a NACUBO survey of national trends in college governance, which found that a clear majority of independent colleges had a designated financial expert on their audit committee and had implemented ethics codes and whistleblower policies, but only one third had the CFO publicly certify financial statements and barely a quarter had the president or chancellor certify them.
Efforts to save costs also led four respondents to participate in a college consortium arrangement to outsource the internal audit function to a public accounting firm that does not audit any of the consortium’s members. Under this agreement, the audit firm would conduct in-depth assessments of one operating cycle at each participant, resulting in recommendations that would serve as a template for the other consortium members to adopt. In this fashion, each participant has one important process scrutinized while receiving guidance for improving other processes. (We noted two other respondents were exploring establishing similar consortia.) Although this falls short of an ideal internal audit arrangement, respondents noted that experience has shown that their operations are not extensive enough individually to merit hiring their own internal auditor. As one audit committee chair described it, the college’s former internal auditor was “pulled in 47 different directions—more as a special projects person than as an internal auditor” (Interview 15).

Another explicit constraint to undertaking more extensive governance changes was the uncertainty over benefits. No participant quantified the benefits of good governance. At best, one saw “significant efficiencies from the administrative side” in complying with NACUBO’s (2003) recommendations (Interview 5), while another talked about “collateral benefits” that he hoped the economy would enjoy from a “swing to stringency” following corporate implementation of the Act (Interview 15). In general, however, respondents shared with us the sense that the difficulty in quantifying benefits made it hard to convince parties both in and beyond the financial function to undertake process changes. Our general discussion expands on this point.

Transparency and Stakeholder Engagement Executives from over one third of the sample colleges discussed their efforts to open planning and business deliberations up to a wider community within their institution. Although these instances ranged from improved transparency of decision making to active engagement of internal stakeholders, all can be seen as steps toward linking governance processes to strategic focus. For example, one chief operating officer posts some of his memos on a website meant primarily for internal use, but available even to those outside the institution. Four respondents mentioned “town meetings,” run either by the president or other business executives, to stimulate
discussion among faculty and staff about business issues, and to
give the executives a chance to describe their activities. Others
mentioned formal or informal meetings with salaried employees,
faculty, and students. These sessions included the formation of
budget advisory groups consisting of representatives from these
stakeholder populations, and direct contact between the executives
and representatives of student government associations.

Although the goal of this expanded outreach seemed to be, in
the words of one executive, the development of “a community that
understands that decisions have to be made” (Interview 5), partici-
pants noted other benefits. As one respondent mentioned, prior to
more transparent communications, “staff felt very comfortable
reporting whatever they wanted to the president directly” (Interview
6), which gave issues a sense of crisis, whether warranted or not. It
also tied up officers’ time in trying to determine whether the report
represented an individual’s isolated concerns or was a view shared
more generally on campus. The same was true for executives who
were “pushing an agenda” (Interview 13) directly with the president
rather than sitting down with their colleagues to work through their
concerns. For some institutions, therefore, showing that the execu-
tives actively solicit input from other stakeholders has enabled
them to put potentially contentious issues into context while
seeking their resolution.

Despite these good intentions, the results of this outreach are
uncertain. For example, two respondents found that forums to dis-
cuss internal issues were poorly attended. As one noted, low atten-
dance does not always reflect disinterest, but may suggest that
discussions over the issue are occurring informally in hallways and
over lunch (Interview 17). However, informal communications pose
hazards such as the persistence of rumors, a limited ability to get
informed responses from knowledgeable parties, and an increased
likelihood of disenfranchising important stakeholders or of leaving
them uninformed.

Faculty present a particular challenge to business officers’ efforts
at engagement in governance. While over half of the institutions
reported active faculty involvement, we heard repeatedly that it was
difficult to get the faculty interested in matters that lay outside their
academic discipline or their particular needs. The faculty who were
interested in such matters would participate, but “it’s the same
fifteen, with the same questions” (Interview 5). For others, faculty
were seen as being “far removed” from understanding this process. “It goes right over their head. [They’re] missing the bigger picture of strategic planning” (Interview 7). According to the respondents, narrowed interests could be to blame in these instances: “Faculty tend to think the most important item in [the budget] is their salary” (Interview 17). One treasurer hypothesized that the difficulty with engaging faculty was that faculty “thought leaders” were able to garner sufficient resources from grants or by contract, meaning they felt that they did not need to be involved in discussions of campus resource allocations. Therefore, the faculty members who did participate were those who generally were not sufficiently influential to lead other faculty (Interview 7).

In spite of the exasperation voiced over faculty, nearly all the officers we talked with were trying to increase faculty participation. One controller noted that faculty were “critical . . . [we] want them to buy in to what we’re doing” (Interview 10), a view reinforced by another controller, who remarked that “it’s good to get faculty involved,” which should not be difficult because “they’re not shy” (Interview 6).

Participants generally acknowledged that external stakeholders were important to their institution, yet there was surprisingly little discussion about involving those stakeholders in governance discussions. As one controller put it, “Who would know if we adopted SOX [the Sarbanes-Oxley Act] and why would they care?” (Interview 2). Even though two of the institutions were in the early stages of enterprise risk management, neither had progressed to the point of involving external stakeholders in the process.35 We address this “gap” concerning external parties below.

Gaps One way to characterize the way our participants discussed governance processes is to see these activities as signals sent along selected paths in an established network of relations. Thus, beyond the content of their on-campus discussions about governance, executives’ interactions are reminders to internal parties of the importance of business policies and procedures, including finances and internal controls. Similarly, executives’ dealings with trustees are a sign of the administration’s willingness to entertain the views of those who do not have daily operational responsibilities—again, a signal that goes beyond the content of the interaction. Executives may also be hoping that lawmakers read college governance activity as a sign that legislation is not necessary or that it can be modest in
scope, if the activity is interpreted as the education community’s effort to follow best practices voluntarily.\textsuperscript{36}

At the same time, as we have described it, this activity involves select paths in an established network. That is, information is being communicated to those parties who are usually contacted when governance matters come to the fore. This led us to consider what we did not hear in our interviews, for equally important to our study are those areas in which we heard of no activity taking place, even among participants who could be considered “more aware.” Two issues stood out: the extent of communication and the under-appreciation of higher education’s unique characteristics.

While communications about governance activities seemed to be strong among the respondents’ business executives and staff, discussion of these matters with stakeholders such as alumni/ae, citizens’ groups, donors, students, applicants and applicants’ families appeared nearly nonexistent. Indeed, one audit committee chair considered communicating to some of these groups “a nonissue”—that is, since the trustees had heard no complaints from these stakeholders, they saw no need to contact them (Interview 20). In fact, this represents a missed opportunity for the institution. Expanded stakeholder engagement can give enterprises a chance to strengthen relationships, receive input, and set themselves apart from their peers.\textsuperscript{37} Similarly, although many respondents were aware of the features that distinguish higher education as a social institution, their discussions did not integrate these features into a distinct approach to governance. Rather than focus on education’s unique aspects, our participants approached governance in a way that was not significantly different from corporate attitudes. We discuss the implications of both of these gaps in the following section.

\section*{GENERAL DISCUSSION}

The following picture emerges from our field data. Presidential leadership style and inquiries or insistence from boundary-spanning trustees set the stage for governance discussions and interact to build trust and change roles. Executive-to-executive communication style, part of the “atmosphere” of the institution, can facilitate or dampen those discussions. Governance activity ranges from planning to risk management, but less costly efforts are the first undertaken,
particularly since benefits are difficult to quantify and hard to discuss with involved parties. Costs here should be considered not strictly in monetary terms, but also as personal costs during implementation efforts. The concern for costs leads to a receptivity toward collaboration across institutions in the form of consortia. At the same time, executives acknowledge their nonexecutive internal community. This leads to activities that range from simply providing more information about decisions that are being made (or that already have been made) to genuine efforts at internal stakeholder engagement. Those trying to engage find it difficult to get some constituencies to look past their own, narrower, concerns. Informal communications may make formal channels look underused. Finally, we note the absence of two factors that we feel contribute to effective governance changes: communications about governance activity to parties external to the institution and acknowledgment of the idiosyncrasies of the broader field, here, higher education.

Limitations of the Study

Our analysis and recommendations are tempered by the usual limitations of field research. Our interviews were conducted at a subset of the private institutions in higher education, concentrated in one region. We believe governance issues are even more complicated at institutions with multiple campuses or with a significant research presence that draws on private or government funding. Similarly, the interplay between state government and academe is more involved at public (state) institutions of higher education, requiring some differences in governance responses. The focus of our research meant that we did not interview representatives from several important stakeholder groups, such as students, parents, or faculty, who could supplement the views expressed by the executives. Since the field of higher education has particular governance issues, other factors may prove more salient in corporations or governmental agencies. At the same time, we orient our discussion below to be generally applicable across fields, particularly as we note that the executives in our study did not use the unique factors of higher education to frame their governance actions. Finally, we chose an interview methodology in order to arrive at insights deeper than those afforded by surveys, while covering more instances than can be accommodated in a thorough case study. However, in-depth
case studies or surveys would provide useful extensions of this investigation.

**Implications for Ethical Leadership**

In the words of a public accounting firm partner, issues of governance are “motherhood and apple pie” topics (Interview 3)—that is, they are basic and make good business sense. One obvious lesson from our work is that external shocks are not necessary for governance change. In fact, waiting for a shock to hit is costly. Three of the respondents recalled periods of crisis that their colleges had endured and that had subsided before this study took place. In all these cases, participants noted that these periods were marked by stress, distrust, and high costs. It appears only reasonable, then, that institutions would want to minimize their exposure to possible crises arising from lapses in oversight of operations or mission. Even gradual change in governance can help here. Beyond this, the lesson for a corporate sector that is still recovering from legislated mandates for improved governance is that change can still be afoot at competitors, albeit in barely noticeable increments. Thus, no firm can afford to put aside movement toward improved governance.

For most of our participants, and for many firms, the bigger challenge is to shift focus from governance details (e.g., internal control steps, financial statement certification, the intricacies of whistleblower policies) to strategy (how governance supports institutional growth, how governance processes inform strategic planning). To assist in this shift, we draw three important implications from our findings.

**Concerns for Context** If executives view the factors that affect changes in governance purely from a pragmatic perspective, they can unwittingly limit the potential benefits of good governance at their institutions. For example, governance can lead an institution to be more open and inviting to participation, giving workers a sense of personal investment. Governance can also shape an institution into a leader on issues such as fair treatment of customers and resource stewardship. That is, governance processes and attitudes toward governance help build organizational culture, and it is organizational culture that “can contribute to an individual’s moral development by allowing organizational members decision making responsibility and by encouraging role-taking opportunities.”

If
executives' perceptions of what is important to the pace of governance change stop at the immediately practical, then thoughts on what governance can bring about will never reach their full potential. In other words, the role of governance gets defined by what can be accomplished here and now. Rather than simply producing a pragmatic attitude in applying ethical reasoning, this limitation can keep executives from reaching their own full potential as ethical leaders.

To avoid restricting the potential breadth of governance, executives not only must seek other views (discussed further below) but also must understand how they can differentiate their organization from others. For example, throughout our discussions, our respondents discussed adapting a corporate model of governance. Perhaps this is understandable, given the background of trustees and financial executives, and NACUBO’s emphasis on mirroring the Sarbanes-Oxley Act. However, institutions of higher education are different from corporations. The way in which the tenure system defines the work and social relationships of faculty to the institution, the need to collaborate with employers recruiting students, the roles of students, community perceptions of these generally long-lived institutions, and the social mission of the college—all set colleges apart from other enterprises and need to be incorporated into governance mechanisms more consciously than we heard in our interviews.

Taking such differences into consideration can produce college governance processes that are not part of the corporate model. Similarly, corporations need to consider idiosyncratic elements in devising their governance processes. These elements are the foundations of the corporate culture that distinguishes firms from one another. They are perhaps most publicized and easiest to picture in the case of corporations that have emphasized philanthropic or social ideals, but such distinguishing marks are present in all firms by virtue of the individuality of those who make up the enterprise.

Concerns for Action Executives' views of these critical factors may not only define the potential of governance but also may limit its actual forms. If governance changes are constrained by costs or the difficulty of describing benefits, and if governance processes are narrowed by customary communication channels or restricted trust, then the range of changes possible shrinks, and the likelihood for effective, far-reaching change in the absence of a crisis is reduced. For example, executives may be satisfied with issuing
codes of conduct or initiating whistleblower policies without troubling themselves about whether the codes are understood and followed or the policies are monitored for effectiveness. If communications are restricted to internal parties, executives are unlikely to consider the benefits of or need for wider-ranging governance aids, such as stakeholder advisory groups or periodic stakeholder dialogues. This again points to a need for communication that tests the validity and strength of the perceived constraints. Scenario building—thinking through “what if” situations in groups—can help executives with this examination.

In addition, enterprises can benefit from learning how to cooperate on matters of governance. For example, we mentioned above how a local consortium of colleges is outsourcing its members’ internal audit function. One participant even discussed his hopes that his college’s approach to enterprise risk management would serve as a shared model for other members of the consortium (Interview 7). Colleges that are outside of such formal arrangements are likely to experience higher costs as they explore and try to devise new governance structures or implement governance changes. Of course, colleges enjoy an opportunity to cooperate with their peers that is not duplicated in the corporate world. Yet, corollaries to this cooperation exist among firms seeking to reduce exploration costs. In the corporate sector, industry or trade associations fill many of the roles of college consortia by collecting examples of best practices, providing instruction, and generating industry-wide guidelines—activities that can be adapted to sharing ideas on corporate governance issues. Partnerships born of supply-chain connections offer another avenue to explore effective governance change, as suggested by the literature on ethical behavior within supply chains.40

Ethical Dilemmas Our findings illustrate the tensions executives face. To identify factors that can affect governance change, they must blend their monitoring of the environment with their knowledge of their organization. Both the environmental monitoring and the development of organizational knowledge involve parties outside of the executive offices. Engaging these outsiders can raise their expectations by appearing to offer them input into governance-formation decisions. Even if executives do not actively engage these parties, the executives’ awareness of the parties’ needs, wants, current state, and personalities can exert pressure
on the executives to consider these parties in governance decisions. But executives are also keenly aware of the costs of change and of the problems in describing and measuring the benefits of change. Thus, it is difficult, under normal circumstances, to justify extensive governance changes that would keep all parties’ interests in balance. Shocks to the system, such as legislated changes, may bring about balance, but only at great cost and effort, and possibly great loss of trust. Furthermore, mandated changes tend to be codified in a way that discourages adaptation to local circumstances and that ignores the need for gradual modification as conditions change. Thus, incremental governance change, responsive to an individual enterprise’s evolving needs, offers a less costly chance at balance, given an aware and understanding executive team. Yet herein lies the ethical dilemma for executives on a path of incremental governance change: at any one point as change occurs some constituents are likely to feel left behind. Rather than wait for gradual change to catch up to them, the parties that feel disenfranchised can act in ways that will precipitate a true crisis, either by disregarding established policies and procedures or by shifting loyalties away from the enterprise.

Executives’ ethical leadership must therefore include the ability to understand how and where inequities may be perceived during the course of change, keep constituent loyalties, and bring balance to the governance process. This requires not only awareness and understanding, but wider communications about governance than we heard our participants discuss. Thus, the final implication we draw is that organizations must expand the way they communicate. Governance activity sends a signal to stakeholders about the characteristics of the institution. But for this to deepen or re-establish trust within the stakeholder network, or to distinguish the particular enterprise, there must be effective communication about the particulars of governance—motives, processes, and structures. Both deeper communication within the institution (in our example, to nonbusiness staff, faculty, and students) and broader communication outside it (here, to alumni/ae, donors, and civic organizations) are needed to improve all parties’ appreciation of the importance of governance, and to better assess the institution’s mission and different groups’ roles in that mission. What an audit partner told us about colleges is likely true of many enterprises: they are excellent at identifying their stakeholders, but not at communicating
with them (Interview 3). In fact, stakeholder engagement can be a complex undertaking for all parties involved.\textsuperscript{41} For example, in our interviews, some executives took lack of inquiries from stakeholders as a sign of their disinterest. Thus, most of our respondents with rated debt said their bond rating agencies had not asked them about governance, but were concerned with admissions and enrollment management. Yet, poor governance affects both of those areas. Clear communication about processes and controls involving admissions and enrollment would show the agencies that the institution is not only monitoring these concerns but also understands their connection to financial viability, institutional mission, and campus atmosphere. Whether the enterprise is for-profit or not, stakeholder engagement can force it to think through the connections between governance and processes, and between processes and mission.

\textbf{Directions for Further Research}

Finally, our study reveals areas worth further academic research. For example, we have noted the importance of synergies between trustee experience and presidential leadership. What communication channels between boards and top executives are most effective in achieving these synergies? What mix of experience on the board best supports a given chief executive leadership style? How do the answers to these questions vary in the for-profit and the not-for-profit fields? Within not-for-profits, the influence of financial executives on overall institutional governance, while considerable, is constrained by the weaker connections that these executives have to non-business functions. Similarly, not-for-profit governance must consider issues that are not under business officers’ direct supervision. How do non-business processes, such as those involving civic engagement, affect governance? Which network structures or communication styles improve the coordination of business-oriented and non-business processes within the institution? The corollary to this in the corporate sector is the role of philanthropy or social issue advocacy that some firms have undertaken. How are these efforts best coordinated with “standard” lines of business within a given corporate governance structure? Answers to these and similar questions would help our understanding of the role that governance structures play in ethical leadership.
NOTES


3. At the same time we acknowledge that executives must deal with important factors that they may not have identified as critical. Our thanks go to an anonymous reviewer for reminding us of this.


11. For ease of exposition, we use college to represent college and university throughout the remainder of this paper.


13. For a discussion of boundary-spanning activity in financial


24. The Sarbanes-Oxley Act focuses on financial controls and governance processes that affect financial operations. It imposes rules and restrictions on executives within public corporations, and is designed to affect the behavior of auditors, lawyers, and financial advisors in their dealings with those companies. Among the Act’s provisions that are most cited as having potential parallels to not-for-profit governance are those that require the CEO and CFO to certify that the financial statements fairly present the company’s condition, and to certify the effectiveness of the company’s controls over financial reporting. Other often-cited provisions require adoption of a code of ethics and a whistleblower policy, call for an independent audit committee with a designated “financial expert,” prohibit auditors from providing non-audit services to their audit clients, and require audit partners to be changed after a specified number of years on the engagement.

25. J. Hempel and A. Borrus, “Now the nonprofits need cleaning up.”


30. During the period in which we conducted our interviews, state attorneys general increased their deliberations on adapting provisions of the Sarbanes-Oxley Act to not-for-profit governance.


32. The costliness of this step arises because it has been interpreted as requiring extensive documentation of internal control processes and
authorizations as well as thorough testing of internal control details. In a survey of its members, the Financial Executives Institute found that average costs for first-time compliance with this provision were approximately $550,000 for companies with less than $100 million in revenues and about $826,000 for those with revenues between $100 million and $500 million. See “Why controllers at most private companies are not voluntarily complying with Sarbanes-Oxley,” The Controller’s Report (February, 2005): pp. 1–5.

33. S. Menditto and J. Shedd, “On the transparency track,” NACUBO Business Officer (May, 2005): 28–32. National Association of College and University Business Officers, The Sarbanes-Oxley Act of 2002: Recommendations for Higher Education. Survey Results. 2005. Retrieved July 28, 2008 at http://www.nacubo.org/documents/research/Sox_Survey_Results.xls. In particular, of more than 200 independent colleges responding to questions about the state of their governance now and its expected state within 12 months, 95% said they had or would have a financial expert on their audit committee, 72% said they had or would have a code of ethics, and 69% reported having or planning on having a confidential complaint mechanism. At the same time, 33% said the CFO publicly certifies the financial statements and 27% reported the same of the president or chancellor.

34. Again this finding is echoed in the NACUBO (2004) survey results, as only 28% of 212 responding independent colleges said they had an internal auditor. Another 6% planned on hiring an internal auditor within the coming 12 months.

35. Enterprise risk management involves a comprehensive look at organizational activities, going beyond the financial and business administration. It requires an understanding of risk that includes operations, reputation, and strategy, as well as financial concerns. A thorough process analysis, including interviews with those responsible for operations, leads to mapping and evaluating the key risks in each area. Information systems are established to provide accountability and feedback on control efforts, while explicit responsibility is assigned for monitoring the development of processes and the workings of controls. See The Committee of Sponsoring Organizations of the Treadway Commission (COSO), Enterprise Risk Management—Integrated Framework (Jersey City, NJ: COSO, 2004).

36. We also heard of more explicit contact, including college legal counsel discussing governance issues with an attorney general’s staff.


**APPENDIX 1  List of Interviews**

<table>
<thead>
<tr>
<th>Interview</th>
<th>Institution</th>
<th>Participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>College A</td>
<td>VP—business/finance and treasurer</td>
</tr>
<tr>
<td>2</td>
<td>College B</td>
<td>Financial VP/treasurer; associate VP for finance; controller; director of planning and budgeting</td>
</tr>
<tr>
<td>3</td>
<td>CPA firm X</td>
<td>Audit partner</td>
</tr>
<tr>
<td>4</td>
<td>CPA firm Y</td>
<td>National leader of higher education and nonprofit practice; national leader of education advisory services; audit partner; audit practice researcher</td>
</tr>
<tr>
<td>5</td>
<td>College C</td>
<td>Chief operating officer; university counsel</td>
</tr>
<tr>
<td>6</td>
<td>College C</td>
<td>Associate VP for financial management/controller</td>
</tr>
<tr>
<td>7</td>
<td>College C</td>
<td>University treasurer/chief investment officer</td>
</tr>
<tr>
<td>8</td>
<td>College D</td>
<td>Associate treasurer/director of accounting services</td>
</tr>
<tr>
<td>9</td>
<td>College E</td>
<td>VP—finance/treasurer</td>
</tr>
<tr>
<td>10</td>
<td>College F</td>
<td>Controller</td>
</tr>
<tr>
<td>11</td>
<td>College G</td>
<td>VP—business affairs/treasurer</td>
</tr>
<tr>
<td>12</td>
<td>College H</td>
<td>Chief financial officer</td>
</tr>
<tr>
<td>13</td>
<td>College I</td>
<td>VP—administration and finance</td>
</tr>
<tr>
<td>14</td>
<td>College E</td>
<td>Controller</td>
</tr>
<tr>
<td>15</td>
<td>College C</td>
<td>Chair, audit committee</td>
</tr>
<tr>
<td>16</td>
<td>College J</td>
<td>VP/treasurer</td>
</tr>
<tr>
<td>17</td>
<td>College K</td>
<td>VP—finance and administration</td>
</tr>
<tr>
<td>18</td>
<td>CPA firm Z</td>
<td>National director, higher education practice; audit partner</td>
</tr>
<tr>
<td>19</td>
<td>College F</td>
<td>Chief of staff/associate VP for planning</td>
</tr>
<tr>
<td>20</td>
<td>College D</td>
<td>Chair, audit committee</td>
</tr>
</tbody>
</table>
APPENDIX 2  Outline of Interview Protocol

Introductions to team, research purpose, and method
Participant’s professional background
Institutional background
• Description of the general atmosphere for business and institutional governance (Probes: formal, informal, cooperative, competitive, crisis-mode, planned, cautious, risk-taking. Guiding values: What is important to the people who make institution-wide decisions here?)

Setting objectives and decision making
• Responsibility for setting objectives
• Degree of formality to this process
• (Lead in) Decision making usually is a mix of planning and reaction. To what extent are governance and business issues here reactions to external or internal pressures, rather than part of a long-term plan?
• External and internal factors weighed when considering institution’s governance
• Methods decision makers use to become aware of issues
• Examples of important issues that decision makers are considering

Assessing factors
• Method of assessing the potential effect of these factors on the institution (Probes: formal cost-benefit methods, seat-of-the-pants, stakeholder survey, mix of formal and informal methods)

Response to issues
• Responsibility for responding
• President’s role
• Trustees’ role

Activities
• Procedures to ensure the institution’s response to issues is carried out

Communications
• Communication with stakeholders (Probes: when, how, responsibility, content, differences between internal and external stakeholders)
• Stakeholder responses

Monitoring the effect of decisions
• Method

Example of the process
Sarbanes-like regulation
• (Lead in) One governance issue that we know some colleges and universities are wrestling with is proposed legislation similar to the Sarbanes-Oxley Act.
• Awareness of the Act, source of awareness
• Extent of discussion at institution, motivation for discussion
• Parties involved
• General reaction, specific steps taken

Wrap-up
• Concerns participant would like to raise
• Permission for follow-up
• Thanks