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BoardSource®

Empowering Boards. Inspiring Leadership.

BoardSource envisions a world where every social sector organization has the leadership it needs to fulfill its mission and advance the public good. Our mission is to inspire and support excellence in nonprofit governance and board and staff leadership.

Established in 1988, BoardSource's work is grounded in the fundamental belief that boards are critical to organizational success. With decades of hands-on experience working with and supporting nonprofit boards, BoardSource is the recognized leader in nonprofit governance and leadership, and a go-to resource for nonprofit board and executive leaders. BoardSource supports a broad and diverse cross-section of social sector organizations with

- leadership initiatives addressing key opportunities and issues within the nonprofit sector
- research and benchmarking of board composition, practices, and performance
- membership and board support programs
- customized diagnostics and performance assessment tools
- a comprehensive library of topic papers, publications, and downloadable infographics, tools, templates and more
- live and virtual education and training
- governance consultants who work directly with nonprofit leaders to design specialized solutions to meet an organization's needs
- a biennial conference that brings together approximately 800 board leaders for two days of learning and sharing

A note to our global readers:

The need for effective board leadership and governance knows no geographic boundaries, and BoardSource is committed to strong social sector board leadership and governance around the globe. While BoardSource uses United States laws and policies as the legal framework for our resources and recommendations, most of our resources do not focus on legal matters but rather on good governance practices, making them relevant to organizations working outside of the United States. We do suggest, however, that you refer to applicable laws in your country regarding financial reporting and other legal and transparency issues.

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ABOUT THE BOARDSOURCE GOVERNANCE SERIES

As BoardSource celebrated its 20th anniversary in 2008, we introduced updated editions of the books in the Governance Series, BoardSource's flagship series created to help nonprofit board members understand their primary roles and responsibilities. BoardSource believes that board members and chief executives who know and understand their mutual responsibilities are better equipped to advance their organizations' missions and, in turn, strengthen their communities.

WHY IS A STRONG BOARD IMPORTANT?

There's no denying that the 1.6 million nonprofit organizations in the United States play a vital role in society, from assisting victims of natural disasters to beautifying our neighborhoods, from educating our children to healing the sick. To ensure that their organizations have the resources, leadership, and oversight necessary to carry out these and other vital activities, nonprofit boards must understand and fulfill their governance responsibilities.

Although there have been headline-worthy scandals by a few nonprofits and their boards, the vast majority try hard every day to be worthy of the public's trust. Nevertheless, BoardSource frequently hears from nonprofit board members and chief executives who say that they are not always sure what the basic components of good governance are or how to educate every board member in them so they can serve their organizations and the public in the best possible manner. The revised Governance Series helps bridge this gap in knowledge.

Within the board's broad roles of setting the organization's direction, ensuring necessary resources, and providing oversight,

board members wear many hats. They are guardians of the mission; they ensure compliance with legal and financial requirements; and they enforce ethical guidelines for their organization. They are policymakers, fundraisers, ambassadors, partners with the chief executive, and strategic thinkers. They monitor progress, evaluate the performance of the organization and the chief executive, and demonstrate integrity in everything they do on behalf of the organization. Because of their many roles, board members need more than enthusiasm for a cause, passion for a mission, or just “good intentions.” They need to understand all of their stewardship responsibilities and perform all of their duties.

WHAT WILL BOARD MEMBERS FIND IN THE BOOKS?

The six books address all of the fundamental elements of service common to most boards, including board member responsibilities, how to structure the board in the most efficient manner, and how to accomplish governance work in the spirit of the mission of the organization.

1. *Ten Basic Responsibilities of Nonprofit Boards, Second Edition* (Book 1) by Richard T. Ingram describes the 10 core areas of board responsibility.
2. *Legal Responsibilities of Nonprofit Boards, Second Edition* (Book 2) by Bruce R. Hopkins, JD, LL.M., elaborates on the board’s legal responsibilities, liabilities, and the oversight it should provide to protect the organization.
3. *Financial Responsibilities of Nonprofit Boards, Second Edition* (Book 3) by Andrew S. Lang, CPA, explains board fiduciary responsibilities in the areas of financial oversight and risk management.
4. *Fundraising Responsibilities of Nonprofit Boards, Second Edition* (Book 4) by James M. Greenfield, ACFRE, FAHP, helps board members understand why they should be actively engaged in ensuring adequate resources for the organization — and how to get involved in fundraising.

5. *The Nonprofit Board's Role in Mission, Planning, and Evaluation, Second Edition* (Book 5) by Kay Sprinkel Grace, MA, Amy McClellan, MNO, and John A. Yankey, PhD, shows how to define and communicate the organization's mission and link strategic planning and evaluation to achieve organizational success.
6. *Structures and Practices of Nonprofit Boards, Second Edition* (Book 6) by Charles F. Dambach, MBA, Melissa Davis, and Robert L. Gale offers guidance on how to build and structure the board (size, committees, term limits) and enhance leadership roles and the partnership between the chair and the chief executive.

Each book focuses on one topic, breaking information into manageable amounts that are easy to digest. Readers will find real-world examples that provide insight from effective boards, statistics from BoardSource's *Nonprofit Governance Index 2007* survey of nonprofit organizations, tips and pitfalls, lists of the most important things to remember, end-of-chapter questions, glossaries, and resource lists for further reading. The authors of the books are subject matter experts with years of experience in the nonprofit sector.

WHO SHOULD READ THE BOOKS?

Board members and senior staff, especially chief executives, in nonprofits of all types and sizes will find the information contained in the Governance Series relevant. They can use it to set standards, to develop their own approaches to board work and interacting with board members, and to modify practices as the organization evolves.

There's something in the Governance Series for everyone associated with the board. A board chair, for example, might share Book 5 (*The Nonprofit Board's Role in Mission, Planning, and Evaluation*) with board members before starting a strategic planning process or give Book 4 (*Fundraising Responsibilities of Nonprofit Boards*) to the development committee. Chief executives will find it beneficial to give Book 3 (*Financial Responsibilities of Nonprofit Boards*) to the board treasurer and to

review Book 1 (*Ten Basic Responsibilities of Nonprofit Boards*) and give it, along with Book 6 (*Structures and Practices of Nonprofit Boards*), to senior staff and the board chair to clarify board–chief executive roles and strengthen the partnership with the board. All board members will want to read Book 2 (*Legal Responsibilities of Nonprofit Boards*) so they understand how to protect themselves and the organization. The chair of the governance committee might give new board members all six books. This sharing helps ensure that everyone associated with the board is “on the same page” and has a common understanding of the board’s responsibilities, expectations, and activities.

Board service entails serious obligations, to be sure, but it can also deliver immense satisfaction. A board that knows what is expected of it and performs at the highest level is a strategic resource for its organization and chief executive. And ultimately, this commitment by dedicated board members translates into mission impact in our communities.

The Governance Series was made possible in part through the support of MetLife Foundation.

INTRODUCTION

REASONABLENESS AND PRUDENCE

When joining the board of a nonprofit organization, you take on a set of responsibilities and duties defined by law. Along with attention to programs, finances, and fundraising, nonprofit board members should understand the regulatory environment in which their organizations operate. Fundamental legal principles and complex tax laws govern the work of nonprofit boards and board members.

Nonprofit organizations and their boards do not function in a vacuum. They are important players in the country's societal, economic, and legal framework and must adapt to — and sometimes act as the impetus for — environmental change. Other times, they may fulfill obligations and expectations common in the for-profit and government sectors.

For example, enactment of the Sarbanes-Oxley Act of 2002, passed by the U.S. Congress in the aftermath of various corporate and accounting firm scandals, raised the standards of scrutiny in the private sector for matters such as auditor independence, corporate responsibility, financial disclosure, and conflicts of interest. Aspects of this heightened concern for accountability have carried over into the nonprofit sector, more by practice than by legal requirements.

Thus, the board of a nonprofit organization is challenged with two seemingly contradictory mandates — advancing the good work of the organization and deciding the extent of its accountability to the public. This tension makes board service both difficult and rewarding.

FULFILLING FIDUCIARY RESPONSIBILITIES

Fundamental to the legal aspects of board membership is the concept of fiduciary responsibility. The control of a nonprofit

organization is usually vested in its governing body, typically called the board of directors. The members of this board, charged with exercising responsibility over the organization and its resources, are considered fiduciaries. This concept of fiduciary responsibility extends to the accountability board members have assumed to both advance their organization's mission and oversee its assets.

Fiduciaries are held to a standard known as the test of reasonableness and prudence. This centuries-old test has its basis in English common law and the standards developed concerning governance of charitable trusts. In contemporary terms, this standard means that board members are expected to regard and treat the nonprofit organization's assets and other resources with the same care with which they would treat their own resources.

Because the board of directors is ultimately responsible for a nonprofit organization's activities, it often becomes the prime target when problems arise. The general argument often made against boards in these circumstances — and the one against which board members should defend themselves — is guilt by omission. This situation arises when board members have been passive or otherwise inactive in overseeing the activities of the nonprofit organization and, consequently, may have failed to adhere to the standards of fiduciary responsibility. To protect against these charges, board members must demonstrate that they appropriately discharged the requisite duties. Ignorance is not an acceptable excuse when a legal problem demands the board's attention.

GETTING SOUND ADVICE

Charged with oversight, board members inevitably struggle with the limitations created by their part-time (at best) involvement and their volunteer status. No board member can know everything. Boards must rely, to various extents, on independent professionals that the organization may retain.

Acknowledging that sound legal advice requires legal counsel, most organizations make considerable use of lawyers. An organization may have an ongoing relationship with one or more lawyers, who may be in private practice or employed by

the organization. The lawyer may serve as a volunteer (perhaps as a board member) or be compensated (at full or reduced rates) for services rendered. In any case, board members should have access to the organization's lawyer, within reason; legal fees can mount if access to the lawyer is not monitored and limited.

Some organizations have their lawyer present at every meeting of the board or at least a portion of the meeting (sometimes with staff not present). Others have a lawyer available by telephone, should a question involving a legal matter arise. Some have their lawyer review drafts of board meeting minutes and/or annual information returns. A few organizations have a periodic legal audit.

The matter of lawyers on the board is tricky business. Like all of the other board members, the lawyers serve primarily as fiduciaries. Their role is not simply to provide free services for the board or the organization but to bring a new perspective and exercise vigilance. Although they will certainly speak up in the face of legal issues that come before the board, to the extent that those issues are within their range of expertise, board members with legal experience are not a substitute for the use of inside or outside legal counsel. Lawyers are sometimes asked to give opinions on the propriety of a board action, so having a lawyer on the board may put that lawyer in the awkward position of passing judgment on his or her own actions.

Also, most lawyers today specialize, so a lawyer on the board is not necessarily competent to advise an organization on nonprofit law. Finally, having a lawyer on the board — even one who specializes in nonprofit law — does not absolve the rest of the board members from being aware of their own responsibilities and duties under the law.

An understanding of the basic concepts and rules can go a long way toward helping a board member avoid personal liability. Simply put, board members need to ask

- What kind of oversight and policy judgments am I expected to provide and make?
- When and how can I be found personally liable?
- How can I avoid, or at least minimize, personal liability?

This book provides a starting point for answering these questions. While it offers a preliminary understanding of the legal landscape you must navigate as a member of a nonprofit board, this book does not and cannot substitute for the counsel of trained professionals.

Chapter 1 discusses the concept of fiduciary responsibility and the collective duties of care, loyalty, and obedience. Chapter 2 delves into the different forms that nonprofit organizations can take and describes how board members are elected. Chapter 3 summarizes the strategies for protecting board members from personal liability, while Chapter 4 outlines the policies and procedures that, increasingly, are becoming best practices within the nonprofit sector. The Conclusion offers some important things to remember when trying to minimize liability.

A list of discussion questions appears at the end of each chapter. These questions are designed to prompt board dialogue, either during a board retreat or at regular times set aside on the board meeting agenda. The Appendix presents several samples of recommended board policies, which may be adapted for use in any nonprofit. This book also offers a glossary of legal terms and concepts that apply to nonprofit organizations.