

SERVING ON A NONPROFIT BOARD

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I. DUTIES OF A NONPROFIT DIRECTOR

A. Duty of Care.

A director must act with care that an ordinary person would exercise under similar circumstances and in a manner that the director reasonably believes to be in the best interest of the corporation. In other words, directors (and officers) must be informed and act in good faith.

1. Business Judgment Rule. Provides that officers and directors are protected from liability if they exercise reasonable business judgment, even if a decision turns out to be in error. Decisions must be reasonably informed and made in good faith in order to qualify for protection under the business judgment rule.

2. Corporate Formalities. Directors must follow the law, the Articles of Incorporation, and the Bylaws. A board should maintain good records as a court will look to objective evidence to determine whether the directors have met the duty of care. Minutes should show that directors possessed sufficient information to make a decision, examined the alternatives, and voted on an informed basis. Directors may receive additional protection by relying on information from outside sources that a director reasonably believes to be accurate (*e.g.*, legal and accounting advice).

3. Attendance. Regular attendance at board and committee meetings and careful review of information presented to directors are essential to fulfilling the duty of care. Board process relies on group decision-making dynamics and full participation is key to the governance process. Boards should meet on a regular basis.

4. Statutory Liability Protections. Oregon law limits liability to gross negligence or intentional misconduct for “qualified directors.” A qualified director is (essentially) one who (1) serves on an organization exempt under Section 501 of the Internal Revenue Code and (2) serves without compensation. In addition, the Articles of Incorporation may limit the liability of a director or officer to a corporation or its members for conduct as a director or officer.

5. Indemnification. Oregon law provides some circumstances where the corporation must indemnify its directors. The organization has the option to indemnify under certain circumstances. The organization may not indemnify a

director if the corporation sued the director and won, or if the director improperly received personal benefits.

B. Duty of Loyalty.

Each director (and officer) has a duty of loyalty to the corporation. This means that a director must put his or her self-interest or the interest of another person or entity aside and act only in the best interests of the corporation.

1. Confidentiality. A director should not disclose information about the organization unless the information has already been disclosed, is of public record, or the board of directors has specifically authorized the director to disclose the information.

2. Conflict of Interest. A director has a conflict of interest whenever he or she has a material interest in a proposed transaction. Oregon law provides a process for approval of a transaction with an interested director.

3. Federal Tax Law. Note that conflict-of-interest (“self-dealing”) transactions may be subject to stricter scrutiny and process under federal tax law than required under the Oregon Nonprofit Corporation Act.

C. Duty of Obedience.

Directors have a duty to comply the organization’s articles of incorporation and bylaws, to carry out the organization’s exempt purpose, to ensure that the organization’s funds are used for lawful purposes, and to cause the organization to comply with state and federal laws that relate to the manner in which it conducts its business.

II. RELATIONSHIP WITH CEO AND EMPLOYEES

The Board of Directors is responsible for adopting or approving the significant policies governing the organization’s mission, strategy, and authority, the operating and capital budgets, major transactions, and other material matters. The Board also hires the executive director and assesses his or her performance. The executive director is responsible for the day-to-day management of the affairs of the organization and the implementation of Board policies. She or he reports directly to the Board of Directors. Except when specifically authorized, directors should not deal directly with employees on matters relating to the conduct of their duties but, instead, should communicate through the CEO.

III. POTENTIAL LIABILITY

A. Derivative Action.

A charity or someone acting on its behalf may sue a director for breach of the duty of care or loyalty where breach injures the corporation itself.

B. Third Party Suits.

An outside party can sue a charity and its directors for personal or financial injury based on the charity's actions.

C. Statutory Violations.

1. Failure to Pay Employment Taxes. Directors can be held liable for failing to withhold employment taxes, or failing to pay unemployment insurance, or worker's compensation insurance. Directors may be held strictly liable (personally).

2. Private Foundation Penalties/Intermediate Sanctions. Private foundations are subject to an additional set of regulations under the Internal Revenue Code. Violations of certain regulations (*e.g.*, self-dealing) can result in a tax on "foundation managers" (*i.e.*, directors). In addition, directors and officers of a public charity can be taxed on excess benefit transactions under the intermediate sanctions rules. All such taxes must be paid personally by the director or officer and may not be reimbursed by the entity without additional penalties.

3. Attorney General Oversight. The Oregon Attorney General is charged with overseeing charitable entities – corporations and trusts. The Attorney General may bring a proceeding against a charity or join in an action brought by others.

IV. BEST PRACTICES

A. Attend Meetings and Pay Attention.

Directors get in trouble if they "knew or should have known." Most often it is the latter. Read and understand budgets, financial statements and reports. Ask questions, and probe deeper if things don't seem right. Beware of relying solely on information provided by staff. Seek outside accounting or legal advice, if necessary.

B. Review Governing Documents and Maintain Records.

Bylaws and board policies should be current and should accurately reflect how the board functions. The board should record accurate minutes and votes, and document discussions. Minutes should be circulated, corrected, and approved. Remember – process is important!

C. Ensure the Entity Completes all Required Filings.

Annual income tax returns (Form 990 or 990-PF); DOJ—Charitable Activities Section report (Form CT-12); annual corporate report; state employment tax filings.