

Duties of New Directors



Q: At our upcoming annual meeting, we will install new directors. What should I tell them about their responsibilities?

A: Not-for-profit organizations and their boards, like all corporations, are under increasing scrutiny by state and federal agencies. The obligations today, however, are the same as they've always been. To assist newcomers and remind veterans, here are the basics regarding the fiduciary duties of directors:

The duty of care. The duty of care requires a director to exercise the care that a reasonably prudent person would exercise in a like position under similar circumstances. A director who makes decisions with reasonable care and in good faith receives the protection of the "business judgment rule," that is, their decisions will not be second-guessed by a court.

But what constitutes "reasonable care" and "good faith" in this context? Essentially, they require directors to participate in association meetings, read meeting materials ahead of time, and ask questions when necessary. That said, directors don't need to do all the work of the association themselves. In fact, they are expected to delegate tasks to staff or committees, and they may rely on the advice of experts, like attorneys and accountants. In the end, however, each director must exercise his or her own independent judgment in voting on matters coming before the board.

The duty of loyalty. The duty of loyalty requires each director to place the interests of the organization he or she serves

ahead of his or her own personal interests and the interests of any other person or organization. In addition, it requires each director to refrain from using his or her position, or information gained from participation on the board, to further the director's personal financial interests.

In a nutshell, the association's interests come first ... before the director's personal or business interests, and before the interests of a family member or business associate. It would be a breach of one's duty of loyalty, for example, for a director to listen to a board discussion regarding a new initiative or educational program and then use that information to develop a competing or substitute program or initiative. Similarly, but less obviously, a breach also would occur where a director has an idea for an initiative that may be pursued either by the association or by the director personally, and the director pursues the initiative personally without bringing the idea to the association's attention and giving the association the opportunity to pursue it first.

To assist directors in faithfully discharging their duty of loyalty, associations should adopt conflict of interest policies requiring disclosure of any actual, potential or perceived conflicts between the interests of the directors and those of the association. Through such disclosure, the disinterested members of the board can determine whether disclosure by itself is sufficient to protect the association's interests, whether the interested director should be excused from participation in specific activities, or whether the interests of the association and the board member are so different that the interested director should be asked to step down from the board. It should be noted that it is not inherently illegal for a director to perform services for his or her association under the appropriate circumstances. Specifically, directors may do business with their association where the disinterested directors determine, after full disclosure, that the terms of the agreement are fair.

The duty of obedience. The duty of obedience requires directors to support their

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association's rules and policies, as well as board decisions once made. This duty often is a difficult one with which to comply. While the duty of care requires directors to participate in the debate and deliberation of the issues, the duty of obedience requires directors to support board decisions, even those with which they disagreed. If a director feels compelled to speak publicly against the board's decision, he or she should resign from the board.

In addition to meeting their fiduciary duties, directors also must comply with certain statutory requirements. Specifically, for example, associations and their directors are subject to federal and state antitrust laws, civil rights laws and federal employment tax requirements. That said, unless a director was directly and personally involved in committing the violation, it is unlikely that he or she would have personal liability.

Thus, as a practical matter, volunteer directors generally have little personal liability for the actions they take on their organization's behalf unless they act in bad faith or with deliberate disregard for their fiduciary duties. The business judgment rule protects directors against liability for decisions made in good faith, with reasonable care, and in the organization's best interests, even if such decisions turn out to have been "wrong."

Because no one can prevent someone from bringing a lawsuit — even if it's frivolous — many associations indemnify their directors against liability for actions taken in good faith, and they buy insurance to cover any costs and/or losses related to those actions. The best protection from liability, however, is prevention, which may be achieved by educating directors about their legal responsibilities and then assisting them through the adoption and implementation of policies that promote sound corporate governance practices. ■

The answers provided here should not be construed as legal advice or a legal opinion. You are urged to consult a lawyer concerning any specific situations or legal questions you may have.