

# A General Overview of a Board Member's Responsibilities

Meet the Challenge: Be the Most Effective Board Member You Can Be

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# The General Principles

A board member is a fiduciary of the non-profit organization. The board member acts “on behalf” of the non-profit organization with regard to all actions taken and decisions made.

The board responsibilities can be divided into internal responsibilities and external responsibilities. Internally, the board member must understand and implement the non-profit organization’s mission, provide financial oversight, and monitor conflicts of interest. Externally, the board member must participate in fundraising, advocate for the non-profit organization, encourage community building and participate in outreach.

# The Fundamental Legal Duties

Each board member has three legal duties:

(1) The Duty of Care

(2) The Duty of Loyalty

(3) The Duty of Obedience

# The Duty of Care

Under the duty of care, the board member ensures the prudent use of all of the assets of the non-profit organization, including the facility or space used by the non-profit organization, the executives and staff of the non-profit organization and the good will of the non-profit organization. In addition, each board member has a responsibility to participate actively in making decisions on behalf of the non-profit organization and to exercise his or her best judgment while making these decisions.

# The Duty of Loyalty

Under the duty of loyalty, each board member ensures that the activities of the non-profit are advancing the mission of the non-profit, must recognize and report conflicts of interest, and make decisions that are in best interest of the non-profit organization. Under this duty, each board member must place the interests of the non-profit organization before his or her personal and professional interests when acting as a decision maker for the non-profit organization.

# The Duty of Obedience

Under the duty of obedience, each board member ensures that the non-profit organization obeys applicable laws and regulations, follows its Articles and bylaws, and adheres to its stated charitable purposes and mission.

# Some Context – Maine Statutory Guidance

The three legal duties are incorporated into Maine non-profit corporation laws.

Specifically, 13-B MRS §717(1) provides that a director shall discharge the director's duties: (A) in good faith; (B) with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and (C) in a manner the director reasonably believes to be in the best interests of the [non-profit] corporation.



# Board Member – Reliance Upon Information (the Good Faith Standard)

In order to make decisions on behalf of the non-profit organization, the board member must rely upon information presented by others.

Under 13-B MRS §717(2), a director is entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by: (A) one or more officers or employees of the non-profit organization whom the director reasonably believes to be reliable and competent in the matters presented, (B) legal counsel or accountant or other person as to matters the director reasonably believes are within the person's professional or expert competence, or (C) a committee of the board of which the director is not a member, as to the matters within its scope, if the director reasonably believes the committee merits confidence.

# Conflict of Interest

One of the primary duties of a board member is to protect the non-profit organization from entering into a transaction or arrangement where a board member has a conflict of interest.

With regard to a board member, a conflict of interest is a violation of the duty of loyalty. In particular, a conflict of interest arises when the objectivity of a board member is influenced by a private interest of the board member with regard to a proposed transaction or arrangement. Sometimes a conflict arises because of financial interest of the board member and sometimes a conflict arises because of a duality of interests of the board member.

# Conflict of Interest Policy

In order to protect against the occurrence of a conflict of interest, a non-profit organization should have a conflict of interest policy.

The policy should (a) require a board member to disclose any actual or possible conflict of interest, (b) outline the process of the remainder of the board to determine if the situation constitutes a conflict of interest, (c) describe the procedures for addressing the conflict of interest, and set forth any consequences of violating the conflict of interest policy.

The policy should also require appropriate record keeping of the board or committee proceedings when a possible conflict situation arises, the outcome of all deliberations, and the resolutions by the board of directors.

# Maine Law Conflict of Interest Rules

Under 13-B MRS §718, a “conflict of interest transaction” is a transaction in which a director (or officer) of a corporation has a direct or indirect financial interest.

For these purposes, a director (or officer) has an indirect interest in a transaction if (A) another entity in which the director (or officer) has a material interest or in which the director (or officer) is a general partner is a party to the transaction, or (B) another entity of which the director (or officer) is a director, officer or trustee is a party to the transaction.

Importantly, a conflict of interest transaction is not voidable or grounds for imposing liability on a director (or officer) if the transaction (a) was fair at the time it was entered into or (b) is approved as provided in 13-B MRS §718 by the board or the Attorney General.

# Conflict of Interest Transaction – Approval Process

With regard to a public benefit corporation (think a tax-exempt organization) a transaction in which a director has a conflict of interest may be approved (before or after the transaction) by the board of directors or the appropriate committee if the material facts of the transaction and the director's interest are disclosed to the board or the committee, and the transaction is fair and equitable to the corporation as of the date the transaction is authorized, approved or ratified. The party asserting fairness has the burden of asserting fairness.

The board may request the Attorney General or the Superior Court (in an action in which the Attorney General is a party) to approve the transaction. The “fair and equitable” standard applies and burden of asserting fairness is the same.

# Conflict of Interest - Protections

A non-profit organization should take pro-active steps to recognize possible conflict of interest situations and educate the board members about the correct procedures when dealing with a possible conflict of interest.

- (a) Annual disclosure form of the board member's and his or her family's relationships with other for-profit and non-profit organizations.
- (b) Discuss possible conflict situations at one board meeting each year.
- (c) A small group of the board (perhaps an executive committee) should meet before every board meeting to discuss any disclosed conflicts of interest.

# Excess Benefit Transactions

The Code contains conflict of interest rules in section 4958 concerning excess benefit transactions. These rules are called “intermediate sanction rules” because they fall between taking no action regarding the excess benefit transaction and revocation of the tax-exempt status of the participating tax-exempt organization.

Section 4958 imposes an excise tax on excess benefit transactions between a disqualified person and an applicable tax-exempt organization. The disqualified person who benefits from the excess benefit transaction is liable for the excise tax. In addition, an “organization manager” of the applicable tax-exempt organization may also be subject to an excise tax.

# Tax-Exempt Organizations Involved

The excess benefit transaction rules apply to an “applicable tax-exempt organization” which is defined as:

- (a) Tax-exempt public charities (section 501(c)(3)),
- (b) Exempt social welfare organizations (section 501(c)(4)), or
- (c) Exempt health insurance issuers.

Note that a private foundation is not subject to these rules. Rather a private foundation is subject to the self-dealing rules and the excise taxes imposed by section 4941.



# A Disqualified Person

A “disqualified person” means (a) a person who is in a position to exercise substantial influence over the affairs of the tax-exempt organization, (b) a member of such influential person’s family, and (c) an entity in which such influential person or his or her family own more than a 35% interest.

For these purposes, the influential person includes a voting member of the board of directors, the organization’s president, chief executive officer, chief operating officer or chief financial officer, or a person with similar powers.

The definition of family is broad and includes certain lineal ascendants, lineal descendants, spouses of the included lineal ascendants and descendants, and siblings.

# The Excess Benefit Transaction

Under section 4958(c)(1) of the Code, the term “excess benefit transaction” is defined as any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) received for providing the benefit.

So, the measurement is a comparison between (a) the value of the benefit provided by the tax-exempt organization to the disqualified person and (b) the value of the consideration provided by the disqualified person to the tax-exempt organization. If the amount of (a) is greater than (b), then there is an “excess benefit.”

# The Excess Benefit Transaction

Examples of transactions that are covered by the excess benefit rules include:

- (a) Compensation paid to the disqualified person,
- (b) Rental arrangements,
- (c) Borrowing arrangements,
- (d) Revenue sharing arrangements, and
- (e) Sales of assets between the tax-exempt organization and the disqualified person.

# Presumption of Reasonableness

A compensation arrangement and other transactions between the tax-exempt organization and the disqualified person are presumed to be reasonable (and therefore are not treated as excess benefit transactions) if:

- (a) the transaction was approved by an independent board of directors or committee (the members of the board or committee who are not related to, or controlled by, the disqualified person or any person involved in the transaction),
- (b) The board or committee obtained and relied upon comparability data and
- (c) The board or committee appropriately documented the basis of its decisions.

# Maine Law – Requirement of Financially Independent Board

Maine law requires that the board of a tax-exempt organization be independent with regard to financial (compensation) transactions.

Under 13-B MRS §713-A, no more than 49% of the individuals on the board of a public benefit corporation (think a tax-exempt charitable organization) may be financially interested persons.

A “financially interested person” is (a) an individual who has received or is entitled to receive compensation for personal services rendered to the public benefit corporation within the previous 12 months; and (b) the spouse, brother, sister, parent or child of the individual receiving compensation.

It should be noted that the failure of a board to comply with this independence requirement does not affect the validity or enforceability of any transaction entered into by the corporation.

# Questions?

Thanks for being a great audience!