

You've Been Asked to be a Charitable Board Member: *What Are Your Responsibilities and How Do You Protect Yourself*

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Serving as a director, trustee, or other member of the governing body of a charitable organization provides a valuable community service, and can be personally rewarding as well. However, before agreeing to serve on a board, you should understand your responsibilities and ask a few basic questions.

The board of a charitable organization, just like the board of a for-profit organization, is responsible for the general management and control of the organization. The officers of the organization, on the other hand, carry out the day to day operations of the organization and implement the policies/vision developed by the board.

State Law Responsibilities

Board members owe fiduciary obligations to the organization, and are bound to act in good faith and in the best interest of the organization. Often, these responsibilities are identified in terms of the following three duties:

- **Duty of Care.** Generally, a director must exercise the diligence, skill, and care of an ordinary person managing his or her personal affairs in similar circumstances. Directors need not be perfect, but they must use the same type of care in making board decisions that they would use in making decisions for their individual business. Directors should be informed of the organization's activities and take advantage of director orientation sessions, retreats, and available training programs.

- **Duty of Loyalty.** Board members are only permitted to act in the interest of the organization. Directors can not use information obtained as a director for their personal gain (or the gain of a family member/related business). The organization should adopt a policy for dealing with transactions involving directors that requires full disclosure of the director's interest in the transaction, and the approval of the transaction by a majority of disinterested directors.

- **Duty of Obedience.** Directors must remain faithful to the mission of the organization, and follow all rules applicable to the organization. Directors should not depart from the stated mission of the organization, since such a departure could jeopardize the organization's tax exempt status. Similarly, charitable organizations are subject to significant restrictions regarding political and legislative activities, as well as significant regulations and restrictions in other areas.

Tax Law Responsibilities

Charitable organizations, unlike their for-profit counterparts, enjoy a special tax status under Section 501(c)(3) of the Internal Revenue Code. This status permits the charity to receive tax deductible donations and not pay income tax on its exempt function income. However, because of these valuable rights, charitable organizations are subject to additional rules which are designed to insure that they operate exclusively for the public's benefit.

All charitable organizations are subject to rules prohibiting "private inurement" and "private benefit". Also, many charitable organizations are also subject to the lesser known "intermediate sanctions" rules which provide that a charitable organization's management (officers, directors, etc.) can be personally assessed a penalty tax when they permit the organization to engage in an "excess benefit transaction". Additionally, an "insider" in the charitable organization who engages in such a transaction is also subject to personal liability for a penalty tax. The potential for intermediate sanctions tax often arises when compensation is established for the organization's management team. Also, intermediate sanctions exposure arises when a charitable organization engages in transactions with vendors or customers who are insiders.

Director's Protections from Liability

Generally, directors who act within the scope of their authority on the board are not liable for the debts or civil wrongs of the organization. In addition, the Articles of Incorporation of a corporation may contain a provision which insulates directors from liability for good faith mistakes in judgment when dealing with affairs of the organization. Similarly, the Articles of Incorporation may contain provisions which require or permit the organization to indemnify its directors if they are personally sued while acting within the scope of their role as a director.

In addition to these "internal" protections, charitable organizations should strongly consider carrying directors and officers liability insurance (including coverages for employment practices, intermediate sanctions, etc.) to provide coverage in the event that the board members are sued. Finally, in the case of volunteer board members, Kansas law generally provides immunity from liability where the charitable organization carries liability insurance.

Charitable Board Member continued on page 2

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A Few Suggestions For Serving as a Director

The days of being an "honorary" or "passive" board member are over. Directors should attend meetings regularly and keep well informed of a charitable organization's activities. Likewise, directors should insist that their organization comply with all state and federal laws, and obtain professional advice when appropriate.

Directors should be familiar with the organization's governing documents (Articles of Incorporation, Bylaws, policies, etc.) and request a board member orientation session if it is not otherwise offered. Directors should also ask questions when appropriate and insist upon complete and accurate disclosure of the details of all significant transactions. Directors should avoid personal/business relationships that place them in a conflict of interest with the organization, and where those circumstances are unavoidable, the organization should follow its conflict of interest policy and/or intermediatesanctions policy in approving those transactions.

Finally, in circumstances where a director disagrees with board action, the director should make his or her dissent noted on the record and follow up to ensure that the objection is recorded in the board minutes/corporate record.

Conclusion

Serving on the board of a charitable organization can be a great experience and a wonderful way to give back to the community. By using common sense, and where appropriate the advice of professionals (accountants, lawyers, investment managers, etc.), being a director will be a fulfilling experience for both you and the charitable organization. ■

For Further Information

Foulston Siefkin regularly counsels clients on issues relating to Tax Exempt Organizations. If you are interested in additional information regarding this Legal Insight, or if you would like to discuss specific ways in which the author can help you, call **Kevin J. Arnel** at (316)291-9761, or email him at karnel@foulston.com. The firm's diverse clientele includes private and public sector employers of all sizes, from Fortune 500 companies to small businesses and non-profit organizations. For more information on the firm, please visit our website at www.foulston.com.

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