
Table of Contents

Preface	xvii
Introduction	xix
Chapter 1	
The Nonprofit Corporation and Its Directors:	
What They Do, How They Do It, and for Whom	1
The Zoology of the Nonprofit World	3
Basic Concepts	3
The Director's Role	5
Director Selection	6
Special Categories of Directors	6
The Corporation's Purpose and How It Affects a Director	8
Defining the Corporation's Purpose and the Persons or	
Interests It Serves	8
Statements of the Corporation's Purpose and Its Constituencies	
Should Be Consistent with the Corporation's Activities	8
Understanding the Corporation's Constituencies and	
Their Representatives	10
Director Accountability to Defined Classes of Persons or Entities	10
Directors Accountability of Mutual Benefit Corporations is	
Similar to That of Business Corporation Directors	10
Director Accountability of Public Benefit and	
Religious Corporations	11
Despite Their Importance, Donors Are Not Considered Part of	
Nonprofit's Legal Constituency	12
Accountability to Members Responsible for Appointing Directors	12
Constitutional Considerations Limiting Public Accountability of	
Religious Corporations	13
Endnotes	13

Suggested Questions for Directors Regarding the Nonprofit Corporation and Its Directors	16
Checklist: The Nonprofit Corporation and Its Directors	17
Chapter 2:	
Duties and Rights of Nonprofit Corporation Directors	23
The Duty of Care	26
Elements of the Duty of Care	26
Reliance	30
Delegation	31
Discharging the Duty of Care: Some Practical Suggestions	34
Regular Schedule of Meetings	34
Executive Sessions	34
Meeting Agenda and Committee Reports	35
Action by Written Consent	35
Board Voting Via E-mail	35
Regular Schedule of Information	36
Rules of Procedure and Minutes	37
The Business Judgment Rule	38
Form 990 Governance Focus Areas	39
Internet Discussions by Board Members	42
Satisfying Other Legal Requirements	43
The Duty of Loyalty	43
Conflicts of Interest: General Principles	43
Corporate Opportunity	49
Confidentiality	49
Directors' Rights	50
Management Access	50
Books and Records	50
Notice of Meetings	51
Right to Dissent and to Have Dissent Recorded	51
Minutes	51
When a Special Duty Applies: The Director with Knowledge of Illegal Activities	52
Ethics and Business Conduct Codes	52
The Duty of Obedience	53
When Is a Director of a Nonprofit Corporation Considered to Be a "Trustee" with Duties Beyond Those Normally Attributed to Directors?	53
When a Director May Be Considered a Trustee	53
When a Director or Trustee Is Not a Trustee under the Law	54

The Impact of the Sarbanes-Oxley Act	54
Panel on the Nonprofit Sector	55
Endnotes	55
Suggested Questions for Directors Regarding Director Duties and Rights	60
Checklist: Duties and Rights of Nonprofit Corporation Directors	61
The Board’s Record of Service	61
The Board’s Procedures	64
Chapter 3:	
Committees, Advisory Bodies, and Officers	69
Board Committees: Introduction	71
Advisory and Auxiliary Bodies: Introduction	72
The Types of Board Committees	72
Special Committees	72
Standing or Permanent Committees	72
Special Committees	73
Purposes of Special Committees	73
Special Committees of Nonboard Members	73
Standing Committees: General Issues	74
Board Use of and Reliance on Committees	74
Committee Creation: Bylaw Description or Board Resolution	74
Committee Exercise of Board Authority	75
Committee Size	75
Conflicts of Interest	75
Descriptions of Common Standing Committees	76
Executive Committee	76
Governance/Nominating Committee	77
Audit Committee	79
Compensation Committee	80
Investment Committee	80
Compliance Committee	81
The Composition of a Committee	81
Committee Procedures, Minutes, and Reports	82
Advisory and Auxiliary Bodies	82
Use of Advisory and Auxiliary Bodies	82
Legal Status of Advisory and Auxiliary Bodies	83
Relationship of Board to Advisory Bodies	84
Relationship of Board to Auxiliary Bodies	84
Scope of Activity of Advisory and Auxiliary Bodies	84

Limitations on Rights of Members of Advisory and Auxiliary Bodies and Liability Protection	85
Designated Bodies	85
Officers: Introduction	86
Officer Responsibilities	86
Officer Positions	87
Chair and Vice Chair	87
Treasurer	87
Secretary	88
Standards of Conduct for Officers	88
Endnotes	89
Suggested Questions for Directors Regarding Committees, Advisory Bodies, and Officers	90
Checklist: Committees and Advisory Bodies	91
Chapter 4:	
Taxation	97
Introduction	99
Qualifying for Exemption from Federal Income Tax	100
Corporations Exempt from Tax under § 501(c)(3)	100
Particular Advantages of § 501(c)(3) Status	101
General Requirements	101
Limitations on Unrelated Business Activities	102
Limitations on Private Benefit and Private Inurement	102
Limitations on Lobbying	103
The Absolute Prohibition on Political Campaign Activities	103
Special Rules Relating to Public Charities and Private Foundations	104
Definition of Public Charity	104
Restrictions and Taxes on Private Foundations	106
Section 501(c)(4) Organizations: Civic Leagues and Social Welfare Organizations	107
Definition of Social Welfare	108
Comparison of § 501(c)(3) and § 501(c)(4) Exemption Status	108
Section 501(c)(6) Organizations	109
Requirements for Exemption	109
Tax Treatment of Contributions or Dues to a § 501(c)(6) Corporation	110
Obtaining Tax-Exempt Status	110
Unrelated Business Income (UBI)	111

Definition of Unrelated Trade or Business	111
Types of Income Excluded from UBI	112
Use of a Taxable Subsidiary	112
Advertisements vs. Sponsorship Acknowledgements	113
Special Reporting Requirements	114
Noncharitable Contributions	114
Charitable Contributions	115
Charitable Contributions in Return for Items of Value	115
Disclosure of Annual Returns and Exemption Applications	116
Intermediate Sanctions: Excise Tax on Public Charities' Excess	
Benefit Transactions	116
Potential for Imposing Intermediate Sanctions	117
Taxes on Directors, Officers, and Other Managers	118
Procedures for Establishing Reasonableness	118
Governance and IRS Form 990	119
IRS Governance Guidelines	120
Conflict of Interest Disclosures	120
Independence	120
IRS Revocation of Tax-Exempt Status	121
Conclusion	122
Endnotes	122
Suggested Questions for Directors Regarding Taxation	124
Checklist: Taxation	124
Chapter 5:	
Creating For-Profit Subsidiaries and Joint Ventures	129
Engaging in New Activities	131
Furthering Exempt Purposes	132
UBI 132	
Substantiality of Nonexempt Activity	132
Advantages of Establishing Separate For-Profit Subsidiaries	133
Type of Organization	134
Directors or Managers	134
Officers	134
Other Oversight Mechanisms	135
Tax Implications	135
Other Organizational Issues	135
Creating Joint Ventures with For-Profits	136
Joint Venture Policy	137
Taxation of Joint Venture Revenue	138

Endnotes	138
Suggested Questions for Directors Regarding For-Profit Subsidiaries and Joint Ventures	139
Checklist: For-Profit Subsidiaries and Joint Ventures	139
Chapter 6:	
Nonprofits On The Internet: Fundraising, Selling Goods And Services, Lobbying, And Other Activities	143
Potential Hazards and Benefits of Using the Internet	146
Fundraising	146
Charitable Solicitation Registration Requirements	146
Acknowledging Donors' Contributions	148
Allowing Other Organizations to Raise Money for the Corporation	149
Corporate Sponsorship vs. Advertising	152
General Rules	152
Internet Applications	152
Association (Links) with Taxable Entities	154
General Rule	154
Internet Applications	154
Lobbying	155
General Rule	155
Internet Applications	155
Political Activity	157
General Rule	157
Internet Applications	157
Avoiding Copyright and Trademark Infringement	157
General Rule	157
Internet Applications	158
Sales of Goods and Services	158
General Rules	158
Internet Applications	160
Posting Information Returns and Exemption Applications on the Internet	164
General Rule	164
Internet Application	164
Implications of Serving as an Information Exchange	165
Defamation and Other Torts	165
Liability Protection Available by Registration as an Internet Service Provider	165

Tax Consequences of Providing Internet Access to Others	166
Protecting Electronic Records Information	167
Identity Theft	168
Endnotes	168
Suggested Questions for Directors Regarding Supervision of Internet Activities	170
Checklist: Internet Activities: Fundraising, Selling Goods and Services, Lobbying, and Other Activities	171
 Chapter 7:	
Volunteers	179
Risks Associated with Using Volunteers	181
Minimizing the Corporation's Liability	182
Protecting the Volunteer from Individual Liability	183
Statutes Protecting Volunteers	183
Insurance for Volunteers	184
Indemnification of Volunteers	184
Claims by Volunteers against the Corporation	185
Volunteer or Employee?	185
Employment Laws and the Volunteer	186
Obtaining a Waiver and Release of Liability	186
Workers' Compensation Insurance	187
Ownership of Materials Created by a Volunteer	187
Endnotes	188
Suggested Questions for Directors Regarding Volunteers	188
Checklist: Volunteers	189
 Chapter 8:	
Employees	193
Executive Employment Relationships	196
Chief Executives and Other Management Employees	196
Executive Employment Agreements	196
Evaluation of Chief Executive	196
Employment Laws Applicable to Nonprofit Corporations	197
Federal Equal Employment Opportunity Laws	197
Reasonable Accommodation for Disabilities	198
State and Local Equal Opportunity Laws	199
Equal Opportunity Policies	199
Antiharassment Policies	199
Family and Medical Leave	199

Wage and Hour Issues: Fair Labor Standards Act	200
State Wage and Hour Laws	201
Employee Handbooks and Personnel Policies	202
Grievance Procedures	202
Workplace Violence	202
Employee Benefits.	203
Reasonable Compensation	203
ERISA Requirements	204
Plan Documents	204
Special Rules for Nonprofits	204
Other Laws Relating to Employees	205
Background Checks	205
Employee E-mail Monitoring	205
Identity Theft Protection	206
Tax Withholding and Payroll Taxes	206
Workers' Compensation and Unemployment Insurance	206
Immigration Laws	207
Work for Hire	207
Confidential Information	207
Liability to Others for Acts of Employees	208
Negligent Hiring and Supervision Claims	208
Liability to Employees	208
Wrongful Discharge in Violation of Public Policy	208
Right to Privacy: Disclosure and E-mail Review	208
Lifestyle Discrimination	209
Collective Bargaining	209
Endnotes.	209
Suggested Questions for Directors Regarding Employees.	210
Checklist: Employees.	211

Chapter 9:

Duties of Directors under Special Circumstances: Change in Control, Sale of Unique Assets; and Bankruptcy.	215
Mergers, Sales, and Other Change of Control Events.	217
Application of Duties of Care and Loyalty to Change of Control Decisions	218
Role of State Attorney General	221
Other Regulatory Approvals	221
Other Interest Groups Affected by a Change of Control	222
Summary	222
Disposition of Unique Assets.	223

Circumstances in Which Disposition Issues May Arise	223
Board Considerations in the Sale of Unique Assets.	223
Insolvency and Bankruptcy	224
The “Zone of Insolvency”	224
Interests of Creditors vs. the Charitable Mission	225
Loan/Bond Defaults and Out-of-Court Restructurings	226
Bankruptcies	227
Role of State Attorney General in Bankruptcy	228
General Bankruptcy Process.	229
Retention of Professionals and Appointment of Creditors’ Committee	229
Creation of the Bankruptcy Estate	229
The Automatic Stay.	229
Operation of the Debtor’s Business While in Bankruptcy	230
Assumption and Rejection of Executory Contracts and Unexpired Leases.	230
Avoiding Preferences and Fraudulent Conveyances to Increase the General Estate Available for Distribution to Creditors	230
Summary	232
Endnotes.	232
Suggested Questions for Directors Regarding Duties of Directors under Special Circumstances	234
Mergers, Sales, or Other Change of Control Events	234
Disposition of Unique Assets	234
Checklist: Duties of Directors Under Special Circumstances.	235
 Chapter 10:	
Investments and Expenditure of Endowment Funds	241
Gifts	243
Potential Liability and Other Issues	244
Standards for Investment of Institutional Funds.	244
Investment Committee	245
Investment Policy	245
Delegation of Duties	246
Standards for Expenditure of Endowment Funds	247
Out-of-Date or Impractical Restrictions on Gifts	248
Accounting Treatment of Institutional Funds	249
Donor-Advised Funds	249
Endnotes.	250

Suggested Questions for Directors Regarding Investments and Expenditure of Endowment Funds	251
Checklist: Investments and Expenditure of Endowment Funds	251
Chapter 11:	
Director Liability Risks and Protections	255
The Director’s Exposure to Liability	257
Avoiding Liability Risks	258
Director Indemnification	259
Discretionary Indemnification	259
Mandatory Indemnification	260
Advancement of Expenses.	260
Third-Party Indemnification.	261
Attorney General Notice	262
Protecting Directors through Insurance	262
Directors and Officers (D&O) Insurance.	262
D&O Policy Coverage Review to Determine Who and What is Covered	263
Impact of Dual Roles of a Director on D&O Coverage.	263
The Nature of “Claims-Made” Policies	264
Policy Coverage.	264
Types of Coverage.	265
Losses Covered	265
Policy Exclusions	266
The Application.	266
Statutory Protections for Directors	267
Eliminating Liability to Third Parties	267
Eliminating Liability for Monetary Damages to the Corporation or Its Members	268
Limitations of Liability Protection Statutes.	268
Protection against Certain Kinds of Claims	269
Conflicting Interests: The Director and Legal Counsel	269
Summary	270
Endnotes	270
Suggested Questions for Directors Regarding Director Liability	273
Checklist: Director Liability	274
Chapter 12:	
The Legal Environment of the Nonprofit Corporation	277
The Board’s Responsibility	279

Understanding the Corporation's Legal Environment	279
Role of Legal Counsel	280
What We Mean by Law	280
Predictable Acts by Authorities	281
Private Acts (Contracts) That Bind the Corporation.	281
Litigation	281
Analysis of the Corporation's Legal Environment.	282
Identifying Potential Areas of Legal Exposure	282
Annual Review	282
The Corporation's Contractual Environment.	283
The Litigation Environment	283
The Corporation's Political/Legal Environment	285
Restrictions on Involvement in Political Arena	285
How Nonprofits Are Affected by the Legal/ Political Environment	285
Keeping the Board and Others Aware of the Impact of Proposed Legal Changes.	286
Choice of Counsel.	286
Differences among Kinds of Nonprofit Corporations.	286
Budgeting for Predictable and Recurrent Legal Needs	287
Selecting Counsel	288
Understanding the Corporation's Rights and Obligations vis à vis Its Legal Counsel.	289
Use of Volunteer Lawyers	290
Responsibility for Monitoring the Corporation's Tax Environment	291
Special Issues of the Board Member As Counsel	291
Who Is the Client?	293
Endnotes.	293
Suggested Questions for Directors Regarding the Corporation's Legal Environment and Selection of Counsel	294
Legal Environment	294
Selection of Counsel.	295
Checklist: The Legal Environment of the Nonprofit Corporation	296
 Chapter 13:	
Director Orientation and Revitalization	299
New Director Orientation and Materials.	301
Orientation	301
Directors' Manuals or Websites	302
New Director Review of Information	304

Board Revitalization: Retreats, Strategic Planning, and Self-Evaluation	305
Board Retreats	305
Reviewing the Board Decision-Making Process	306
Evaluating Whether the Board Needs to Be Restructured	306
Information-Gathering for Strategic Planning and Mission Measurement	308
Quantifying Success for a Nonprofit Corporation	309
Other Sources of Information, Inspiration, and Guidance	311
Endnotes	312
Suggested Questions for Directors Regarding Director Orientation and Revitalization	312
Checklist: Director Orientation and Revitalization	313
Appendices	315
Appendix A: Tax-Exempt Organization Reference Chart	317
Organization Reference Chart from; Tax-Exempt Status for Your Organization; Internal Revenue Service Publication 557 (Rev. October 2011)	317
Appendix B: Suggested Publications, Periodicals, and Websites	323
Publications	323
Periodicals	324
Useful websites and organizations	325
Index	329