

## Legal Duties of Association Board Members

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Association officers, directors, committee members, and others involved in the association's governance structure are often unclear as to their roles and responsibilities. And for good reason - some rights and obligations are determined by law, others by the association's articles of incorporation and bylaws, and still others by written policies and procedures or more informal arrangements. The following article is designed to clarify the delegation of duties, explain the fiduciary duties imposed by law on association officers and directors, and suggest ways to protect volunteer leaders from personal liability.

### **Roles and Responsibilities.**

The *board of directors* is the governing body of the association, responsible for the ultimate direction of the management of the affairs of the organization. The board is responsible for *policymaking*, while employees (and to a certain extent, officers) are responsible for *executing day-to-day management* to implement board-made policy. However, the ultimate legal responsibility for the actions (and inactions) of the association rests with the board.

The board can act legally only by consensus (majority vote of a quorum in most cases) and only at a *duly constituted and conducted meeting*, or by *unanimous written consent* (in most states, boards cannot act by mail, fax or electronic ballot). The board may delegate authority to act on its behalf to others such as committees, but, in such cases, the board is still legally responsible for any actions taken by the committees or persons to whom it delegates authority. An *individual* board member has no individual management authority simply by virtue of being a member of the board. However, the board may delegate additional authority to a board member such as when it appoints board members to committees. In a similar fashion, an *officer* has only the management authority specifically delegated in the bylaws or by the board (although the delegated authority can be general and broad).

*Committees* have no management authority except for that delegated to them by the bylaws or by the board. Furthermore, under most state nonprofit corporation laws, certain functions may not be delegated by the board to committees. For example, in many states, the board may not delegate to committees the power to elect officers, fill vacancies on the board or any of its committees, amend the bylaws, or approve a plan of merger or dissolution.

*Employees* have no management authority except that specifically delegated to them in the bylaws or by the board. For example, most associations' bylaws delegate to the chief staff executive the responsibility for the day-to-day operations of the association's office(s), including the responsibility to hire, train, supervise, coordinate, and terminate the professional staff of the association, as well as the responsibility for all staffing and salary administration within guidelines established by the board.

*Members* have no management authority, as such authority is held by the board of directors. However, state nonprofit corporation laws generally reserve to members the right to remove officers and directors and to amend the association's articles of incorporation, among other rights. Under some associations' bylaws, certain matters, such as the amendment of the bylaws or the election of officers and directors, must be submitted to the membership for a vote. However, most other matters generally are not submitted to the full membership, but rather are handled by the board, one or more of its committees, or the officers or employees of the association.

## **Fiduciary Duty.**

Those in positions of responsibility and authority in the governance structure of an association - both volunteers who serve without compensation and employed staff - have a fiduciary duty to the organization, including duties of care, loyalty and obedience. In short, this means they are required to act *reasonably, prudently and in the best interests of the organization*, to *avoid negligence and fraud*, and to *avoid conflicts of interest*. In the event that the fiduciary duties of care, loyalty or obedience are breached, the individual breaching the duty is potentially liable to the association for any damages caused to the association as a result of the breach. This fiduciary duty is a duty to the association as a whole; even those who only serve on a particular committee or task force owe the fiduciary obligation to the entire association.

### **1. Duty of Care**

This duty is very broad, requiring officers and directors to exercise *ordinary and reasonable care* in the performance of their duties, exhibiting honesty and good faith. Officers and directors must act in a manner which they believe to be *in the best interests of the association*, and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances. The "business judgement rule" protects officers and directors from personal liability for actions made in poor judgment as long as there is a reasonable basis to indicate that the action was undertaken with due care and in good faith.

### **2. Duty of Loyalty**

This is a duty of faithfulness to the association. This means that officers and directors must give undivided allegiance to the association when making decisions affecting the association. In other words, officers and directors cannot put personal interests above the interests of the association. Personal interests may include outside business, professional or financial interests, interests arising from involvement in other organizations, and the interests of family members, among others. Officers and directors should be careful to disclose even *potential* conflicts of interest to the board of directors, and should recuse themselves from deliberation and voting on matters in which they have personal interests. For pervasive and continuing conflicts - such as a director of the association concurrently serving on the board of a competing association - resignation from the individual's association leadership post or from the outside conflicting responsibility may be required. Officers and directors can have business dealings with the association, but such transactions must be subject to considerable scrutiny. In such event, officers and directors must fully disclose any personal interests to the board of directors, and the terms of any transaction must be fair to the association. In addition, state nonprofit corporation statutes frequently provide specific procedures for dealing with transactions in which officers or directors have conflicts of interest.

### **3. Duty of Obedience**

This duty requires officers and directors to act in accordance with the organization's articles of incorporation, bylaws and other governing documents, as well as all applicable laws and regulations.

**Reliance on experts.** Unless an officer or director has knowledge that makes reliance unwarranted, an officer or director, in performing his or her duties to the organization, may rely on written or oral information, opinions, reports, or statements prepared or presented by: (i) officers or employees of the association whom the officer or director believes in good faith to be reliable and competent in the matters presented; (ii) legal counsel, public accountants, or other persons as to matters which the officer or director believes in good faith to be within the person's professional or expert competence; or (iii) in the case of reliance by directors, a committee of the board on which the director does not serve if the director believes in good faith that the committee merits confidence.

**Willful ignorance and intentional wrongdoing.** Directors cannot remain willfully ignorant of the affairs of the association. A director appointed as treasurer, for example, with limited knowledge of finance cannot simply rely on the representations and reports of staff or auditors that "all is well" with the association's finances. Moreover, officers and directors acting *outside of or abusing* their authority as officers and directors may be subject to personal liability arising from such actions. Furthermore, officers or directors who, in the course of the association's work, *intentionally* cause injury or damage to persons or property may be personally liable, even though the activity was carried out on behalf of the association.

### **Reducing Personal Liability Risk.**

Association officers and directors can help minimize their risk of personal liability by doing the following:

- Being thoroughly and completely prepared before making decisions.
- Becoming actively involved in deliberations during board meetings, commenting as appropriate, and making inquiries and asking questions where prudent and when such a need is indicated by the circumstances.
- Making decisions deliberately and without undue haste or pressure.
- Insisting that meeting minutes accurately reflect the vote counts (including dissenting votes and abstentions) on actions taken at meetings.
- Requesting that legal consultation be sought on any matter that has unclear legal ramifications.
- Requesting that the association's accountants assess and evaluate any matter that has significant financial ramifications.
- Obtaining and carefully reviewing both audited and unaudited periodic financial reports of the association.
- Attending the association's meetings and reading the association's publications carefully to keep fully apprised of the organization's policies and activities.
- Reviewing from time to time the association's articles of incorporation, bylaws and other governing documents.
- Avoiding completely any conflicts of interest in dealing with the association and fully disclosing any potential conflicts.

### **Liability Protection.**

If preventive risk management fails, the liability of association officers and directors can be limited through indemnification by the association, insurance purchased by the association, and state volunteer protection laws.

### **Apparent Authority.**

In the landmark 1982 case, *American Society of Mechanical Engineers v. Hydrolevel*, the U.S. Supreme Court determined that an association can be held liable for the actions of its officers, directors and other volunteers (including actions which bind the association financially), even when the association does not know about, approve of, or benefit from those actions, as long as the volunteer reasonably *appears* to outsiders to be acting with the association's approval (i.e., with its "apparent authority"). The Supreme Court made clear that associations are to be held strictly liable for the activities of volunteers that have even the apparent authority of the association. Even if an association volunteer does not in fact have

authority to act in a particular manner on behalf of the association, the law will nevertheless hold the association liable if third parties reasonably *believe* that the volunteer had such authority. The law thus requires an association to take reasonable steps to ensure that the scope of its agents' (e.g., officers, directors and committee members') authority is clear to third parties, and that agents are not able to hold themselves out to third parties as having authority beyond that which has been vested in them by the association - for example, by regulating access to association letterhead stationery.

### **Antitrust.**

Associations are subject to strict scrutiny under both federal and state antitrust laws. The Sherman Act, the principal federal antitrust statute, prohibits "contracts, combinations, or conspiracies ... in restraint of trade." By their very nature, associations are a "combination" of competitors, so one element of a possible antitrust violation is always present, and only some action by the association that unreasonably restrains trade needs to occur for there to be an antitrust violation. Consequently, associations are common targets of antitrust plaintiffs and prosecutors.

The consequences for violating the antitrust laws can be severe. A conviction can carry stiff fines for the association and its offending leaders, jail sentences for individuals who participated in the violation, and a court order dissolving the association or seriously curtailing its activities. The antitrust laws can be enforced against associations, association members, and the association's employees by both government agencies and private parties (such as competitors and consumers) through treble (triple) damage actions. As the Sherman Act is a criminal conspiracy statute, an executive who attends a meeting at which competitors engage in illegal discussions may be held criminally responsible, even if he or she says nothing at the meeting. The executive's attendance at the meeting may be sufficient to imply acquiescence in the discussion, making him or her liable to as great a penalty as those who actively participated in the illegal agreement.

Common antitrust claims against associations include price-fixing (any explicit or implicit understanding affecting the price of a member's product or service is prohibited, even if the understanding would benefit consumers), group boycotts / concerted refusals to deal, customer allocation or territorial division, bid-rigging, and illegal tying arrangements. Antitrust-sensitive areas of association activity include membership restrictions, standard setting, certification and self-regulation, statistical surveys, and information exchange programs, among others.

To avoid antitrust liability, associations should adopt a formal antitrust compliance program, and this policy should be distributed regularly to all association officers, directors, committee members, and employees. The policy should require, among other conditions, that all association meetings be regularly scheduled - with agendas prepared in advance and reviewed by legal counsel - and that members be prohibited from holding "rump" meetings. Above all else, members should be free to make business decisions based on the dictates of the market - not the dictates of the association. Any deviation from this general principle, such as adoption of a Code of Ethics that infringes on members' ability to make fully independent business decisions, should be approved by legal counsel.

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