

# Liability and Ethical Considerations of Board Members and Counsel in Fundraising

Planned Giving Council  
of Houston  
Annual Conference  
April 27, 2017  
Houston, Texas

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See Reference Outline:

“Governance of Nonprofit Organizations”  
authored by Darren B. Moore, Megan C.  
Sanders and Michael V. Bourland

*Other helpful information  
and outlines  
may be found at  
[www.moorenprofitlaw.com](http://www.moorenprofitlaw.com)*



# What We'll Cover Today

- o Legal duties of decision-makers of Texas nonprofit corporations
  - o Directors
  - o Officers
  - o Program managers (sometimes)
- o Considering legal duties in fundraising context
- o Role of counsel and development of gift acceptance policy



# Directors (Voting/Advisory): The Collective Wisdom of the Room



- Qualifications for Board Service:  
See governing documents  
(beware of “warm body”)
- Voting board member has  
duties and liabilities imposed by  
law
- Advisory non-voting board  
members, while not having  
liability of voting board  
members helpful as additional  
voices for fundraising and other  
advisory roles



## Generally

- o All decision makers owe fiduciary duties to the charitable organization
- o Fiduciary duty is to act for organization's benefit subordinating own interest
- o Fiduciary duties are equitable duties and are fact-specific, no where is that more prevalent than in fundraising
- o Elements breach of fiduciary duty (1) existence of duty; (2) breach of duty; (3) injury to organization or benefit fiduciary

# The Rules: State Law

## Duty of Care

- Good faith
- Person of ordinary prudence
- Decisions reasonably believe to be in the foundation's best interest
  - May be afforded protection from business judgment rule or trust indenture

## Duty of Loyalty

- Act unselfishly
- Transactions with the foundation (if allowed) must be fair
- Maintain confidentiality
- Don't take foundation's business/investment opportunities

## Duty of Obedience

- Remain faithful to and pursue the goals of the foundation
- Follow the governing documents
- Follow gift restrictions
- Abide by the law/IRC
- Ensure charitable assets are not diverted



# Good Faith

- State of mind denoting honesty of purpose, freedom from intention to defraud...faithful to one's duty
- Objective test based on objective facts





## Ordinary Care and Prudence

- Board must understand organization's mission set forth governing documents to make fundraising decisions/provide fundraising oversight
- Board must seek information regarding fundraising activities
- Board must weigh benefits/detriments of fundraising alternatives
- Board may rely in good faith on legal advisors whose advice the Board believes to be reliable regarding appropriate fundraising activities
- Board must nevertheless exercise independent decisional judgment regarding appropriate fundraising activities



# Ordinary Care



- o Board may delegate activities (fundraising activities) using reasonable care in selecting fundraiser, establishing fundraiser's scope, periodically review fundraiser's actions and confirming conformance with delegation
- o Board cannot delegate oversight of delegated fundraising activities

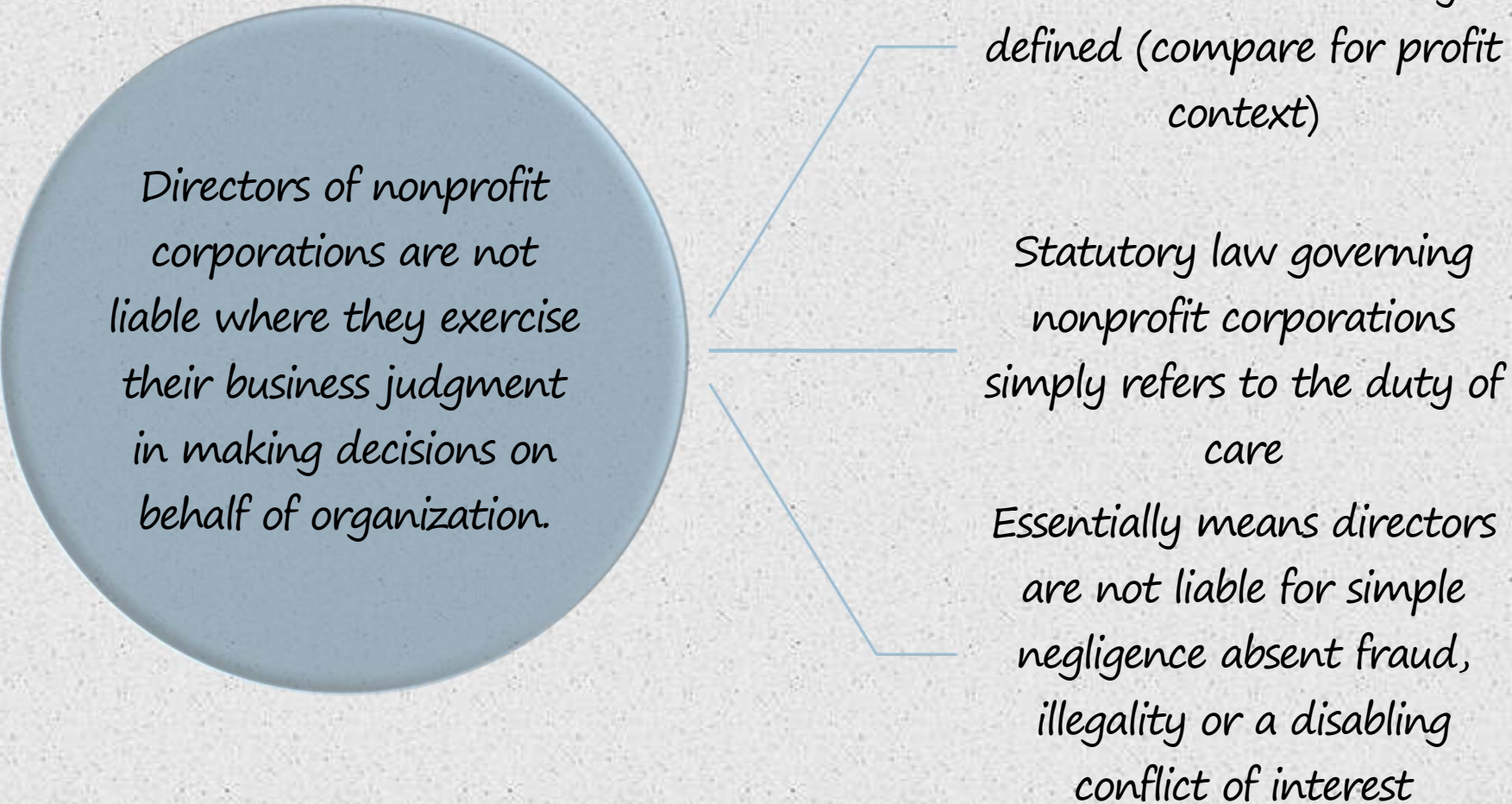
# Best Interest of the Corporation

- Board must make fundraising decisions reasonably believed in best interest organization
- Reasonableness based objective facts available to Board
- Whether proposed fundraising activity corporation's best interest requires review many factors including short-term interests, long-term interests, costs, benefits, and risks





# Duty of Care: Business Judgment Rule and Directors



Directors of nonprofit corporations are not liable where they exercise their business judgment in making decisions on behalf of organization.

Parameters not clearly defined (compare for profit context)

Statutory law governing nonprofit corporations simply refers to the duty of care

Essentially means directors are not liable for simple negligence absent fraud, illegality or a disabling conflict of interest

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# Corporate Opportunity




- Prohibits a decision-maker from usurping corporate opportunities
- Where closely related to corporate operations, must disclose (timely)
- Defenses where no disclosure:
  - Not same line of business
  - Corporation abandoned opportunity
  - Corporation lacked financial resources to pursue the opportunity


# Interested Transactions



*Not inherently unethical or a violation of law: exist on a continuum*





*Key is disclosure and how the decision-maker and board then deal with a disclosed conflict (i.e. upon disclosure the board should provide a disinterested review of the matter)*



*Decision makers should consider adopting a conflict of interest policy*



- 
- o Board member personal interest in fundraising activity – interested board member should recuse from discussion and abstain from vote
  - o Fundraisers must put interests of the corporation first in fundraising, disclosing any conflicts and following procedures to manage conflict
  - o Counsel plays an important role development of conflict of interest policy as it relates to fundraising—Who will it cover?
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# Confidentiality

- Board prohibited from disclosure of non-public domain information in fundraising when dealing with donor/potential donor
- Careful not to misrepresent





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# The Elusive Nature of the Duty of Obedience

- o Pursue the goals of the organization
- o Fidelity to corporate purposes
- o Abide by restrictions imposed by donors
- o Ensure charitable assets are not diverted to non-charitable uses





# Genesis of the Restriction

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graph LR; A((Genesis of the Restriction)) --- B((Express (such as in a gift instrument))); A --- C((Response to solicitation)); A --- D((Arising from governing documents)); B --- E[• This gift is for the express purpose of medical research into cures for the Ebola virus.]; C --- F[• All funds raised will be used for humanitarian aid in Liberia.]; D --- G[• This Corporation is organized and shall be operated for the charitable purpose of animal rescue.];
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Express (such as in a gift instrument)

- This gift is for the express purpose of medical research into cures for the Ebola virus.

Response to solicitation

- All funds raised will be used for humanitarian aid in Liberia.

Arising from governing documents

- This Corporation is organized and shall be operated for the charitable purpose of animal rescue.

# What is the Effect of a Restriction?



- Analogized to the creation of a charitable trust [does not impose duties of trustees on directors]
- Binding on charitable recipient
- Fiduciary duty imposed on directors
- Debate concerning restrictions arising from governing documents



Can future board  
amend organization  
mission to different  
mission?

- o Yes, if inform IRS  
and get approval

What about donor  
intent in prior  
fundraising gifts?

- o A court has stated  
“those who give to a  
home for abandoned  
animals do not  
anticipate a future  
board amending the  
charity’s purpose to  
become research  
vivisection”
- o No clear law in  
Texas

# What if we don't understand the restriction?

- o Uniform Declaratory Judgments Act – statutory authority court construe terms of grant agreement/construe terms of gift constituting a charitable trust
- o Proceeding to construe charitable trust (including restricted gift to corporation) “proceeding involving a charitable trust”





# What if We Can't Follow the Restriction?



- General Rule: Restrictions are binding
- Traditional method of modification: cy pres/equitable deviation
- Statutory enactments of cy pres concepts
  - Texas Property Code Section 112.054
  - UPMIFA Section 163.007

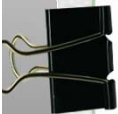
# What if we choose to ignore the restriction?

- o Texas Attorney General
- o Nonprofit Corporation/Association:
  - o Organization (directors, officers and/or members may have standing to bring derivative claim)
- o Charitable Trust
  - o Co-Trustees; named beneficiaries
- o Donors in limited circumstances



Standing  
to  
enforce  
a breach





*Donor may bring suit by*

- Gift contract rights may create special interest in gift*
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# As opposed to modification, can we return the donation?

- Generally no – gifts given to charity are to be used for charitable purposes
- Exceptions:
  - Right of reverter
  - Lack of general charitable intent and restricted purpose fails
  - Conditional gift and condition fails
- May create tax issues for donor







# Introduction to Gifts Inappropriate to Mission

- Donor give gifts intended certain programs/projects
- Donor restrictions vary, including to benefit individuals as scholarship gifts, purpose, investment, administration, naming rights, endowment gifts
- Care should be exercised to insure restriction appropriate to organization mission and appropriate from tax considerations perspective of donor and organization

# Common Concerns from the Donee's/ Organization's Perspective in Accepting Gifts Resulting from Fundraising Activities

## Gift Acceptance

- o Primary concern of organization whether can or should accept gift in deciding, determination made of how gift fits within organization's mission

## Issues in Gift Acceptance

- o Liability associated asset?
- o Managing gift cost - what is true value of gift to organization?
- o Restrictions on gift by donor?
- o How asset owned by donor?





# Why have a Gift Acceptance Policy?

- o Protect organization from unanticipated liabilities
- o Enhance relationship between organization and (prospective) donors
  - o Uniform expectations
  - o Terms governing restricted gifts
  - o Enhance likelihood that restricted gifts will be potentially deductible
  - o Evaluate donor's motives in giving
- o Preserve organization's tax exemption/good governance
  - o Reduce risks of excise taxes
  - o Duties of care, loyalty
  - o Substantiation
- o Set standard terms for restricted gifts
  - o Incorporate into fundraising appeals and specific agreements
  - o Use of donations if have changed circumstances

# Considerations for a Gift Acceptance Policy

- Does the gift have conditions that unacceptably tie up the use of the property?
- Will the type of property tie up other assets of the organization, such as incurring expenses for holding and/or maintaining the property?
- Will gifts of real estate will be accepted, and if so, will they be conditioned upon an inspection and evaluation?
- Will acceptance of the gift hinder or promote the mission?
- The organization's directors and officers must exercise prudence in investing and managing the organization's assets
- It may or may not be prudent to accept particular gifts
  - Does acceptance create negative publicity for the organization?
- Need to weigh each gift versus the best interest of the organization as a whole.



# Essential Elements

Types of property that will/will not be accepted

Absolute prohibition; who has discretion as to other gifts (approval process)

Types of gift vehicles

Whether to accept restricted gifts, and if so, what types

Provisions unique to gifts of real estate, business interests, and other unusual gifts

Type of acknowledgments of gifts, and when to provide to donors

May want to include provisions requiring organization to notify public of the policy Especially with broad fundraising

Insiders should not benefit personally from fees related to gifts received and should not participate in any activity which could be deemed a conflict of interest.

No finder's fee or other private benefit to anyone for gift development.

\*Advice to all prospective donors→


# Ess

Types of property that will/will not be accepted

Absolute prohibition; who has discretion as to other gifts (approval process)

Provisions unique to gifts of real estate, business interests, and other unusual

Insiders should not be personally from fees related to gifts received and should not participate in any activity which could be deemed a conflict of interest.



- Advise all prospective donors to seek their own legal/tax counsel in any and all aspects of the proposed gift (and if necessary, the organization should assist the donor in securing independent counsel).

- Donors often want to use the services of the organization's attorney and are willing to waive any conflicts of interest. This should be done only after careful consideration and explanation and documentation of all potential risks to the donor. A disclosure/waiver letter is imperative.



The information set forth in this outline should not be considered legal advice, because every fact pattern is unique. The information set forth herein is solely for purposes of discussion and to guide practitioners in their thinking regarding the issues addressed herein. Non-lawyers are advised to consult an attorney before undertaking any issues addressed herein.