# RESPONSIBILITIES
of
# Not for Profit Corporate Board Members

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**Not-for-profit Corporations**

Corporations can be found in all strata of society. Some are multinational conglomerates while others are regional or local providers of social services. Both business and not for profit corporations hire and retain employees to provide the services and products needed in every aspect of society. Whether these products are tires, food, drink, medication, health care, vitamins, or counseling services, invariably, the service provider is a corporation. American society's quality of self reliance means that generally, instead of looking to government to address all of our social needs or to implement reforms, we often look to corporations.[1] Our collective experience both as consumers and employees of corporations supports this assertion.

As employees, we look to our employers for health care, freedom from harassment and drug use in the workplace, diversity of race and gender, and some form of retirement security. Employees also expect that the corporate activities are conducted in a manner that assures continuity of the employer's existence thereby assuring continued employment.[2]

This is not mere cant. Dependence upon successful corporate entities is interwoven throughout American society. The first line of responsibility for balancing profitability and social responsibility lies with management. However, it is the board of directors' oversight of management that ensures management is effective in achieving this balancing act.[3]

The foregoing is true not only for business corporations, but also for not for profit corporations. Not for profit corporations run our educational institutions, hospitals, and social service agencies, to name a few. Not for profits can range from a relatively small group of individuals who have an abiding commitment to education and demonstrate this by providing dictionaries to elementary school classes for example, to what could colloquially be characterized as "big business."

The not for profit sector in many ways is every bit as sophisticated as its business counterpart. Not for profit corporations control considerable wealth and assets. During 2001, the largest 400 charities raised $43 billion. The Salvation Army alone raised $1.4 billion in both 2000 and 2001.[4]

When one thinks of today's leading medical centers and universities, the sophistication and wealth possessed by not for profit corporations is evident. Billions of dollars in revenues and assets are received, owned, managed, and distributed annually by not for profit corporations. Whether measured by assets owned, revenues derived, or number of employees, many not for profit corporations dwarf in size enterprises normally thought of as "big business" corporations.

While the rules for management of a not for profit corporation are similar to that of its business counterpart, the accountability varies greatly. In either situation, a member's role on the board of directors goes well beyond simply adhering to a set of rules. Moreover, defining a director's role merely by duties and responsibilities to the corporation may also fall short of addressing all the areas in which a director must stay informed. A board member should be mindful that corporations are forever in transition. Businesses are incorporated, some grow and some fail. Anticipating uncertainty requires each director to bring to bear a full array of wit, wisdom, expertise, and experience so that the board may competently attend to the goals, purposes, and circumstances, both foreseen and unforeseen that confront a corporation.[5]

This paper focuses primarily on the duties and responsibilities that boards of directors face in managing a not for profit corporation. Effective, socially responsible management is imperative to ensure a not for profit's continued existence; an existence that remains true to the purposes and goals for which it was formed. Not for profit board members thus serve a pivotal role in determining —or undermining— the success of the corporation as a meaningful provider to the community it serves.

As mentioned earlier, an important distinction between business corporations and not for profit corporations is to whom each are accountable. Business corporations have access to capital markets unlike not for profit corporations. Issuing stock versus not having stockholders is a material distinction between business corporations and not for profits. The primary function of a shareholder is to operate as a check on the board's activities. The principal tool of a shareholder is election of the membership on the board of directors. This theoretically ensures responsible, profitable management of the corporation.

Accountability owed to shareholders is wide-ranging, yet prioritized. For instance, operations that maximize revenues and generate a positive return on a shareholder's investment are top priorities for board members, however that is not all that is required. Social and environmental responsibility, to name but two, are also issues to that may be addressed by the board of directors.

This distinction in accountability influences how the purposes, culture and activities of a corporation are shaped. The absence of shareholders in a not for profit corporation changes the paradigm of the organization from one that answers to owners distinct from itself, into an organization that does not. Governmental oversight in the not for profit arena operates as the check that a shareholder performs in a business corporation. This oversight assures that a not for profit's assets and resources are being exclusively devoted to its charitable purposes.[6]

A not-for-profit board is accountable directly to the institution and the community it serves. A not for profit corporation must jealously devote its assets and revenues exclusively to its not for profit purposes and do so in an effective manner. By this, I wish to connote purposeful, efficient, functional responsibility that avoids a waste of resources. This responsibility assures the corporation's continued existence and fiscal solvency so that it may accomplish its stated mission.

In the context of not for profit corporations, a discussion of directors' duties necessarily focuses on the purposes for which the corporation was formed, namely, its mission statement contained in the certificate of incorporation. These stated purposes are the reasons why the not for profit exists.[7] The recent decision in Manhattan Eye, Ear & Throat Hospital ("MEETH") underscores the paramount role the board's duty of obedience plays in adhering to the not for profit's corporate purposes.

With the current media focus on the collapse of the Enron Corporation, the proper role and accountability of corporations within society is being revisited. This focus on accountability will have far-reaching consequences on employees, financial consultants, investors, and the role or level of involvement regulatory oversight plays in the not for profit sector. My purpose here however, is not to join the ranks of speculators as to the potential fallout of this complicated corporate failure.[8] Rather, I will examine the duties owed by members of boards of directors to a not for profit corporation.

I will now turn to the various provisions of the New Jersey Nonprofit Corporations Act that govern the duties and responsibilities directors owe to the not for profit corporations they serve.

## The Governing Board[9]

New Jersey not for profit corporations are incorporated under the New Jersey Nonprofit Corporation Act, N.J. Stat. Ann. §15A:1-1 et seq. ("Act"). When enacted in 1983, the Act substantially modernized the law of New Jersey dealing with not-for-profit corporations. The stated goal and purpose behind the Act was to make it more compatible with the New Jersey Business Corporation Act, subject to the particular requirements unique to nonprofit corporations. The Act streamlined provisions pertaining to meetings of the governing board and defining the duties and responsibilities of the members of the board.

Under the Act, certain words were given specific definitions. "Board" means the board of trustees or the group of persons vested with management of the business and affairs of the corporation irrespective of the name by which the group is designated. N.J. Stat. Ann. 15A:1-2.[10] Under the New Jersey Nonprofit Corporation Act, a "trustee" means any person serving on the board of a corporation, whether designated as a trustee, director, manager, governor or any other title. N.J. Stat. Ann. §15A:1-2i. Many corporations use the terminology "board of trustees" to designate its governing board. Use of the term "director" instead of "trustee" does not alter the standard of care required by members of the governing board. Comment, N.J. Stat. Ann. §15A: 1-2.

## Standard of Care

The principal provisions governing the standard of care required by trustees is codified in three sections of the New Jersey Nonprofit Corporations Act. N.J. Stat. Ann. §15A:6-12-14.[11]

> Trustees and members of any committee designated by the board shall discharge their duties in good faith and with that degree of diligence, care, and skill that ordinary prudent persons would exercise under similar circumstances in like positions. In discharging their duties, trustees and members of any committee designated by the board shall not be liable if, acting in good faith, they rely on the opinion of counsel for the corporation or upon written reports setting forth financial data concerning the corporation and prepared by an independent public accountant or certified public accountant or firm of accountants or upon financial statements, books of account or reports of the corporation represented to them to be correct by the president, the officer of the corporation having charge of its books or account, or the person presiding at a meeting of the board. N.J. Stat. Ann. §15A:6-14.[12] [Emphasis added].

Trustees are expected to rely on senior management and officers of the corporation. Yet in doing so trustees are not relieved of their fiduciary duty to adhere to the corporate purposes. Trustees serving on boards of nonprofit corporations must act with the same prudence and degree of care as directors of business corporations.[13] Trustees' fiduciary responsibilities encompass reconciling competing interests included within the purposes of running a corporation, including service to the community at large, its employees, donors, and creditors/bondholders.[14]

By accepting the position of trustee, one assumes a duty of loyalty to the corporation. This requires the trustee to support the corporation's mission and purpose without regard to the trustee's personal interest or self-gain. Concomitantly, the trustee also assumes the duty to act in good faith and to exercise due care while carrying out his or her office of trustee.[15] In carrying out these duties, trustees approve corporate actions, advise corporate management, institute policies and auditing procedures that govern the corporation's finances, and monitor management's performance.

Typically, members of a board of trustees may be regarded as "inside" or "outside" trustees. An inside trustee is one who actively participates in the day to day management of a corporation, for example, a senior officer. An outside trustee is usually not a full time employee and has no significant relationship to the corporation or its management except as trustee.[16]

"A trustee who is present at a board meeting or any committee thereof, of which the trustee is a member, and which action on any corporate matter referred to in §15A:6-12 is taken, shall be presumed to have agreed to the action taken unless the trustee either dissents at the meeting and his or her dissent is entered in the meeting's minutes or the trustee files a written dissent to the action with the person acting as the secretary of the meeting before or promptly after the adjournment of the meeting." N.J. Stat. Ann. § 15A:6-13. This provision's theory is not to promote acrimony among board members or disrupt the orderly discussion at a meeting, but rather to support full and meaningful participation of all trustees.[17]

## Business Judgment Rule[18]

The "business judgment rule" limits the liability of trustees who act in good faith when performing and carrying out their duties. When a director exercises his or her independent informed judgment, courts are reluctant to re-examine the merits of that judgment. So long as a trustee acts in good faith and with due care under the business judgment rule, he or she cannot be held liable for a "bad" business decisions.

Presumably, trustees act on an informed basis, in good faith, and in the honest belief that any action taken or not taken is in the corporation's best interest. The business judgment rule prevents a substantive review of the merits of a board's decision so long as the decision is made without self-dealing and in good faith while exercising due care. Mere disagreement with the trustees' decision(s) is insufficient to impose liability on a board of trustees. Moreover, a bad decision that was made after the board was informed and had an honest belief that the action or inaction taken was in the best interests of the corporation is likewise insulated from liability.[19]

The rule is presumptive and so therefore, not absolute. Trustees who disregard their duties or abdicate their responsibilities will find no shelter under the business judgment rule. The protection of the business judgment rule will not be available to a director engaged in fraud, criminal activity, bad faith or willful or wanton misconduct.[20]

Trustees are jointly and severally liable to the corporation for the benefit of the corporation and its creditors, members, if any, or other interested persons, to the extent of any injury suffered by those persons as a result of the following actions:

1. Disposition of corporation assets contrary to law, the certificate of incorporation, the bylaws or any terms or conditions subject to which the asset was accepted by the corporation,

2. Distribution of assets to corporate members, during or after dissolution, without paying or making adequate provision to assure payment of corporate debts,

3. Completely liquidating the corporation and distributing its assets, and cessation of operations without dissolving and paying all fees, taxes and other expenses incidental thereto, and

4. Lending monies to an officer, trustee, or employee of the corporation contrary to the provisions of the New Jersey Nonprofit Corporation Act. N.J. Stat. Ann. §15A:6-12.

If a trustee fails to remain adequately informed of all material information reasonably available, they fail to act diligently. Courts review a board's decision-making based on a negligence standard. Under a negligence theory, trustees fail to exercise good business judgment when decisions are made without critically evaluating the merits of the action(s) to the corporation.

[Trustees], however, cannot be held personally liable for the wrongful acts or omissions of corporate officers or employees merely by virtue of their position as trustees. To establish liability of the corporation as a whole, a plaintiff must show either that the trustee had knowledge of the wrongful act, or that by exercising due care, the trustee should have been aware that the situation required action. Lack of knowledge of the wrongdoing is not an absolute defense. Trustees cannot avoid liability by failing to act if they choose to ignore what is going on around them. Trustees are charged with knowledge of facts that they reasonably should have known or would have discovered in carrying out their duties.

Courts have found violations of the duty of care where a trustee was not aware of information contained in the company's annual financial statements that should have alerted him to alleged fraud. 'The existence of red flags that would arouse the suspicion of the ordinarily prudent trustee may trigger a duty to make reasonable inquiries and act with due care regarding the suspicions.' For example, if the trustee is aware of previous misconduct by an officer or employee, closer supervision may be necessary.

In Graham v. Allis-Chalmers Mfg. Co.,[21] the Delaware Supreme Court held that, in making decisions, trustees could rely on the integrity of officers and employees unless something occurs to make them suspicious. The court noted that absent cause for suspicion, trustees have no duty "to install and operate a corporate system of espionage to ferret out wrongdoing, which they have no reason to suspect, exists." However, the complete failure of trustees in establishing procedures to monitor employee compliance could subject trustees to liability for a failure to act with due care.[22]

## Limitation of Liability[23]

Directors may be subject to personal liability under state and federal statutes. Along with many state corporation laws, the Act allows a corporation to include a provision in the articles of incorporation that eliminates or limits the liability of directors to the corporation or its shareholders for money damages for breaches of the duty of care. This provision does not operate to limit liability where the director derived a direct financial benefit to which the director was not entitled, the intentional infliction of harm on the corporation, an unlawful distribution of assets, or an intentional violation of criminal law. Protection from liability generally applies only to monetary liabilities to the corporation and it will not insulate board members from injunctive relief.

## Indemnification[24]

The Act specifies the circumstances in which the corporation is permitted or is required to indemnify its directors against liability and related reasonable costs of defense. The Act's standard for indemnification requires that the individual director has acted in good faith and with a reasonable belief that his or her conduct was in the best interests of the corporation. In criminal proceedings, the director must also have had no reasonable cause to believe his or her conduct was unlawful. The Act empowers corporations to indemnify directors in actions by third parties, including expenses in class actions (including attorneys' fees), judgments, fines, and amounts paid in settlement of the actions.[25]

The Act provides that indemnification for reasonable expenses (including court costs and legal fees) is mandatory if the director has succeeded in defending an action. Indemnification is not mandatory if the director is not wholly successful. In the case of settlements or certain adverse court determinations in third-party actions, indemnification is permitted if authorized by the court, upon a determination by a *majority of directors not involved in the action*, or by opinion of independent legal counsel that the director met the applicable standard of conduct.

Many corporations have charter or bylaw provisions mandating indemnification whenever it is legally permissible. Some corporations have also entered into indemnification contracts with the directors to provide mandatory indemnification whenever the applicable statute permits it. The advantage of an indemnification contract is that it cannot be rescinded without the consent of the director, whereas a charter or bylaw provision may be subject to amendment.

## Advance for Expenses[26]

A corporation may advance funds to the director for expenses reasonably incurred in defense of a matter before a determination has been made that the director is entitled to indemnification. However, the director is required to provide the corporation with a plan to repay any fund advanced if it is ultimately decided that the director is not entitled to indemnification. As a general rule, these advances for expenses are discretionary and made on a case-by-case basis by the board of directors.

## Insurance[27]

Corporations are well advised to purchase director and officer liability insurance under which the corporation is entitled to reimbursement of any payment of indemnity claims. The Act permits a corporation to purchase director and officer liability insurance. This insurance policy may also protect directors from the corporation's failure to pay such indemnity. Various policy exclusions may apply to limit coverage and because the available terms of insurance coverage vary greatly, a corporation is cautioned to pay particular attention to the policy language.

## The Manhattan Eye, Ear & Throat Hospital ("MEETH")

More than a century ago, MEETH established itself as a leading specialized care hospital in New York City. In part due to technological changes and the upheaval in economics surrounding managed care, MEETH found itself stretched to the limit in 1999 trying to meet its financial obligations. From late 1998 through mid-1999, MEETH's board focused on the sale of its facilities and closing of the hospital. Senior management put forth "doomsday scenarios," depleted cash by redeeming outstanding bond indebtedness, and lost sight of the mission. The cart was put before the horse.

Initially, the MEETH board of directors wrestled with the idea of whether to continue the hospital in its current capacity, close it, or seek an affiliation with another hospital. The board instituted a series of committees comprised in part by board members, to evaluate the viability of the various proposals. In addition to the committees, a prominent investment bank was retained to advise the board. Of the three proposals ultimately considered, one proposed to continue MEETH as is, that is, as a hospital with a prominent teaching/residency program. In the end, all three proposals were considered to be deficient. In rejecting these proposals, both the board and the investment bank relied solely on the fair market value of the real estate.

In brief, the board, relying in part upon the investment bank's guidance, decided to sell MEETH's real estate assets to Memorial Sloan Kettering Cancer Center ("MSKCC") and a real estate developer who intended to turn the MEETH properties into apartment buildings.

Like many states, New York law requires involvement of the attorney general, in addition to judicial approval, of any petition for divestiture of assets by a not for profit corporation. When MEETH petitioned for court approval of the sale, the attorney general's office objected. Additionally, the medical staff and other bidders voiced strong objections to the proposed sale of MEETH, stating that the board had not adequately explored all of its options.

The evidentiary hearing in MEETH lasted thirteen days. The court was obligated to analyze whether the "consideration and the terms of the transaction are fair and reasonable" and that the "purposes of the corporation ... will be promoted." In reaching its decision, the court concluded that the board failed to consider proposals that would preserve MEETH's mission as a nonprofit hospital.

The court's decision offers little guidance as to how deeply a board of trustees must investigate potential scenarios, or how long the inquiry must last. The court certainly emphasized though, that receipt of more money in one alternative will not override a proposal offering less money tied to a commitment to preserve and continue the purposes of the corporation. In reaching its determination, the court was greatly influenced by the role of the investment banker.

The investment banker would be paid a "success fee" as a percentage of the value of the consummated transaction, depending, inter alia, on whether the assets of the hospital are acquired or the hospital is the acquiring entity. Fundamentally, no sale means no percentage fee.

The trial court found that this arrangement presented the investment bank with a direct financial inducement to reach an outcome requiring the sale of the real estate. The court noted that on several occasions the investment bank misrepresented aspects of the proposals to the board in an attempt to dissuade the board from doing anything short of selling the assets and closing the hospital. The court found this fee arrangement tainted the integrity of the review process and deprived the board of guidance from a truly independent expert.

Rather than orient itself as "to what is this all about," a premise rooted in its corporate purpose and mission, the board, threatened by financial distress, seized upon selling MEETH's assets. This occurred without exploring first, its obligations as a board in the best interests of MEETH, second, development of a plan and critical path, third, preserving cash and cultivating the substantial resource of the medical staff, and finally, exploring with its creditors, regulators, and the attorney general avenues to preserve its mission.

In deciding to sell all of its assets to MSKCC, MEETH encountered an experience colloquially referred to by this author as "turf battles" or "all or nothing" negotiations when hospitals discuss affiliations. Rather than combining their knowledge and business acumen to hone in on services that may be combined, facilities shared, or efficiencies to be achieved in providing health care, one or more of the institutions insist on a complete take over of the other — a "give us the keys" attitude. MEETH encountered just such a negotiating posture. The inevitable consequence is that discussions break off and no substantive analysis is undertaken. The board loses sight of the corporate mission and instead, the focus becomes which board will survive, rather than how best the corporation's interests may be accomplished.[28]

In this case, the court denied MEETH's petition for court authorization to sell its assets and close the hospital. Denial of the petition demonstrates to board members in other not for profit corporations that diligence in exploring all options, adherence, and obedience to corporate purposes should be the board's *primary* concerns. A sale of substantially all of the assets and termination of the not for profit's existence should be considered as the last resort, not the first.

It seems to me that the duties of loyalty, due care, and obedience to corporate purposes implies a mutual exclusivity, where no true exclusivity exists. When faced with decision making the board members must first turn their focus to the reason the not for profit corporation exists. When a director assumes office, she acknowledges that the corporation's best interests prevail over any self-interest or the interest of the constituency selecting her to the board position.[29]

To be sure, making decisions can be difficult, subject to pressures of time constraints, regulatory requirements, and influences from third parties seeking to achieve their own goals. That does not mean that the board should shrink from its responsibilities. But neither can it act with haste or presume that a regulator, lender, or constituency such as a medical staff, will acquiesce in a precipitous or premature board decision.

How much information should be considered, or time consumed in deliberation will vary with the complexity of the issue to be decided. Not only must the corporate goals be established, reviewed and followed, but the manner in which the corporation conducts itself is of equal importance. When the MEETH board accepted the recommendation of its financial advisor, it appeared not to inquire into any competing or alternative interests concurrently expressed by potential affiliates. The initial examination of whether or not the corporate purposes themselves ought to be revised appears to have gotten lost in the shuffle. A well-defined plan and solicitation of bids to implement the plan's goals would have served better. Although the MEETH experience received publicity, at least in my experience, it is not unique.

Planning and ongoing evaluation of the corporation's activities is critical. Annual self-evaluation of the board as to goals established, whether accomplished or not is an essential tool in meeting the board's duties.

## Conclusion[30]

The Corporate Director's Guidebook published by the American Bar Association summarizes corporate directors guidelines to include:

- A director must exercise independent judgment for the overall benefit of the corporation.

- To meet the duty of care standard, a director must be diligent and invest significant amounts of time and energy in monitoring management's conduct of the business and compliance with the corporation's operating and administrative procedures.

- When making boardroom decisions, a director should be comfortable that the board is appropriately informed and has had the time to deliberate carefully.

- A director is entitled to rely on performance by others of properly delegated functions and on reports, opinions, information and statements of the corporation's officers, legal counsel, accountants, employees and committees of the board on which the director does not serve, when under the circumstances it is reasonable to do so.

- The duty of loyalty requires that a director not use her or his corporate position for an unauthorized personal benefit, gain or other advantage expense of the corporation.

- Conflicts of interest (including corporate opportunity situations and a director's transactions with the corporation) are not inherently improper. Although such transactions were once void or voidable under common law, corporation statutes provide procedures under which they may be properly disclosed and dealt with. It is the manner in which an interested director and the board deal with a conflict situation that determines the propriety of the transaction and the director's conduct.

- Increasing shareholder and regulatory activism have raised expectations and requirements for board oversight.[31]

Identifying issues deserving of scrutiny is easy. Achieving solutions to opportunities and problems in the ever changing circumstances of modern society many times proves to be elusive. Nevertheless, thoughtful consideration by board members is the approach most likely to carry the day. Such continuing diligence is the means to accomplish the salutary purposes for which not for profit corporations exist.

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## ENDNOTES

[1] Ira M. Millstein, *The Responsible Board*, THE BUSINESS LAWYER, vol. 52, February, 1997, at 407.
[2] Id. at 408-09.
[3] Id. at 409.
[4] June Kronholz, *The Dictionary Lady Is Spreading the Word to South Carolina Kids*, WALL ST. J., March 4, 2002, at A1.
[5] The author has chosen not to deal with issues of corporation formation, or the distinctions among limited liability companies, limited partnerships, and other statutory organizations. Additionally, certain business enterprises may be served by both not for profit and business corporations, for example, the nursing home industry. An example of a nursing home chain materially adversely impacted by a redirection of Medicare funding is Integrated Health Services, Inc., now in bankruptcy with billions of dollars owed to creditors. This corporation is a $3 billion a year colossus with 86,000 employees working at 400 facilities that house 47,000 nursing beds located in 47 states, and is under control of a creditors' committee. An issue pending in a lawsuit filed in the bankruptcy proceeding is a charge that the board approved a series of unconscionable executive compensation arrangements, including forgiveness of approximately $59 million in loans to executives and payment of approximately $24 million in taxes related to such forgiveness. Lucette Lagnado, *How a Nursing-Home Empire Built on Medicare Collapsed*, WALL ST. J., May 24, 2002, at A1, A8.
[6] Not for profit corporations are extensively regulated. Regulatory oversight varies depending upon funding sources and the character of the corporation. Religious corporations may receive different treatment than non-religious affiliated institutions. Generally speaking, the sale, lease, exchange or other disposition of all or substantially all the assets of certain not for profit corporations may require court approval and state attorney general review. *See generally*, A GUIDE TO SALES AND OTHER DISPOSITIONS OF ASSETS PURSUANT TO NOT-FOR-PROFIT CORPORATION LAW §§510-511 AND RELIGIOUS CORPORATIONS LAW §12. *available at* http://www.oag.state.ny.us/charities/booklets/corporation_religion_not_for_profit.html
[7] Queen of Angels Hospital v. Younger, 66 Cal. App. 3d 359 (1977). Focusing upon the stated purposes for which a corporation is organized is inherent to observance of the board of directors duties of loyalty and due care to the corporation that they serve. Oftentimes discussions of responsibilities of board members omit to emphasize the duty of obedience to corporate purposes by limiting the discussion to the traditional formulation of duties of good faith, loyalty and due care. Particularly in the contest of not for profit corporations, but not exclusively in that context, thoughtful consideration requires that analysis emphasize the reason the corporation exists. Michael W. Peregrine, Esq. & James R. Schwartz, Esq., *Nonprofit Corporations: The M&A Process and the Meaning of MEETH,* HEALTH LAW DIGEST, vol. 28, May, 2000; *In re* Manhattan Eye, Ear & Throat Hospital, 715 N.Y.S. 2d 575 (1999).
[8] *See e.g.*, Michael Schroeder & Greg Hitt, *Big Accounting Firms Break Ties With Andersen to Resist Changes*, WALL ST. J., March 4, 2002; John D. McKinnon, *Enron Corp. Lobbied to Postpone Paying Taxes on Foreign Profit*, WALL ST. J. March 4, 2002 at A4. Reliance on legal standards alone may not be enough. The Enron situation has been described as a crisis "not of illegality, but of legality," because much of what was done may be within the bounds of law. Mark A. Sargent, *The Real Scandal: Enron's "crimes" Were Legal*, COMMONWEALTH, March 8, 2002.
[9] GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS, 2002 A.B.A. Sec. Bus. L.Rep. 29.
[10] "Bylaws" refers to the code of rules adopted to regulate or manage the corporation's affairs irrespective of the name by which these rules are designated. N.J. STAT. ANN. §15A:1-2c (2002). A "member" is distinct from a person serving on the governing board, N.J. STAT. ANN. §15A:1-2h (2002). If the certificate of incorporation designates that the corporation will have members, the members will elect persons to the governing board. Discussion of such members is beyond the scope of this paper. A common example of the member's role is to act as a parent corporation of two or more corporations. The corporate member acts as a holding company that elects individuals to the boards of the two corporations. The two corporations' certificates of incorporation and the certificate of incorporation of member corporation set forth in detail the provisions governing the relationship.
[11] The activities of a corporation shall be managed by its board, except as otherwise provided in this Act or in its certificate of incorporation. Trustees shall be at least 18 years of age and do not require United States citizenship, New Jersey residency status, or to be members of the corporation unless expressly stated in the certificate of incorporation or bylaws. The certificate of incorporation or bylaws may prescribe other qualifications for trustees.

N.J. STAT. ANN. §15A:6-1 (2002). N.J. STAT. ANN. §15A:2-8a (6) (2002) provides that the certificate of incorporation or bylaws may specify the method of selecting trustees. Selection of trustees is not limited to election by members or trustees; any method may be used. For example, some or all trustees may be elected by a different group or by the board of a different corporation; trustees may be designated by reason of their office; or trustees may be selected from specified constituent or delegate groups. Comment, N.J. STAT. ANN. §15A:2-8 (2002).

[12] The New York and Pennsylvania statutes governing the standards of care required of boards of directors in not for profit corporations are substantially similar to the requirements set forth in N.J. STAT. ANN. §15A:1-1 et seq. *See,* 15 PA. CONS. STAT. § 5712 (2001) and NY N-PC LAW § 717 (Consol. 2002).

[13] *See*, *Perils and Pitfalls*, HEALTH CARE LAW SUPPLEMENT, N.J.L.J., December 6, 1999.

[14] Id.

[15] The enumerated duties of good faith, due care, and loyalty are far from unique to New Jersey. The Revised Model Business Corporation Act defines the duty of care to include acting in good faith; with the care an ordinary prudent person in a like position would exercise under similar circumstances and in a manner he or she reasonably believes to be in the best interests of the corporation. REV. MODEL BUS. CORP. § 8.30 (1985).

[16] *Protecting Directors and Officers of Hospitals and Healthcare Organizations from Civil Liability*, AMERICAN HEALTH LAWYERS ASSOCIATION, HEALTH LAWYERS: EXPERT SERIES, June, 1999.

[17] Trustees and directors, in contrast to shareholders for example, have no authority under applicable statutory provisions to designate a proxy. The business of a governing board is to be conducted at a meeting "at which a quorum was present and acting throughout" where a free exchange of ideas can occur and an informed determination achieved by the appropriate representation of the board, in most cases a majority. In the absence of a meeting, unanimous consent is the standard required to be met to justify board action. N.J. STAT. ANN. 15A:6-7 (2002).

[18] GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS, 2002 A.B.A. Sec. Bus. L.Rep. 28-202. The various duties and protections for directors as described in this article are adapted from this guidebook.

[19] Id. at 28.

[20] Id. at 30.

[21] Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125 (1963).

[22] *Protecting Directors and Officers, supra* note 12, at page 7.

[23] GUIDEBOOK FOR NONPROFIT CORPORATIONS, 187-90 (2002).

[24] Id. at 190-93.

[25] In derivative actions brought in the name of the corporation itself, indemnification may be allowed for expenses (including attorneys' fees), but when a director has been found liable, indemnification is allowed only with court approval. Further, the Model Act provides that amounts paid in settlement of a derivative action may be indemnified if approved by a court.

[26] GUIDEBOOK FOR NONPROFIT CORPORATIONS, 192 (2002).

[27] GUIDEBOOK FOR NONPROFIT CORPORATIONS, 193-199 (2002).

[28] MEETH, 715 N.Y.S.2d at 578.

[29] GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS, *supra* note 18 at 29, 173.

[30] *See, generally*, GUIDEBOOK FOR NONPROFIT CORPORATIONS 2002 A.B.A. Sec. Bus. L.Rep.

[31] Michael Orey, *Cashing In On Shareholder Suits*, WALL ST. J., April 25, 2000, at D1.

Not-for-profit organizations are types of organizations that do not earn profits for its owners. All of the money earned by or donated to a not-for-profit organization is used in pursuing the organization's objectives and keeping it running.ï»¿ï»¿ Typically, organizations in the nonprofit sector are tax-exempt charities or other types of public service organizations, and as such, they are not required to pay most taxes. In a nonprofit organization, income is not distributed to the group's members, directors, or officers. There are also nonprofit corporations known as non-stock corporatio... Not-for-Profit Audit Committee Guidebook. Contents 4 Accountability and independence: Guiding principles of the audit committee 6 Basic roles and responsibilities. 11 Users of the financial statements 12 The insiderâ€™s perspective: Working within a not-for-profit organization 14 Working with the external auditors 18 The monitoring function of the audit committee 21 Appendix I: Selecting the external auditors 23 Appendix II: Sample audit committee charter 26 About Grant Thornton LLPâ€™s services to not-for-profit organizations.Â  Member liability Board members of not-for-profit organizations face potential personal legal liabilities. The question of whether serving on an audit committee entails any further legal risk is a legitimate one. Applies to for-profit and nonprofit Boards, unless marked differently. Perhaps the best way to benefit from this topic is first to scan the subtopics in the following table, including how they are arranged on this page. The left side of the table lists the typical topics in Board operations, and the right side lists the typical functions in an organization that a Board must oversee. Also, if you are looking for a very specific subtopic or article about Boards on this page, you might use the "find" function in your browser, and enter the keyword(s) in order to search this page for tho