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## DUTIES AND RESPONSIBILITIES OF DIRECTORS OF TEXAS NONPROFIT CORPORATIONS

Directors of nonprofit corporations are responsible for overseeing the affairs of their organization and they are essential to the success of any nonprofit mission. A solid, hardworking board of directors can set the vision and tone of an organization and position it for long term success. A weak, inattentive board can hinder the organization's growth and can cause legal headaches for the directors and the organization alike. The purpose of this memorandum is to describe a director's duties under Texas law so that every director,<sup>1</sup> can maximize his service and minimize his exposure to liability.

### THE DUTIES OF A DIRECTOR

The statutory basis of the director's duties and responsibilities is set forth in the Nonprofit Corporations chapter of the Texas Business Organizations Code, which states, "a director shall discharge his duties in good faith, with ordinary care, and in a manner that the director reasonably believes to be in the best interests of the corporation." Thus, each director is responsible for spending time, effort, and good judgement to oversee the affairs of the corporation. The director who sees his service as an honorary position, or who relies heavily upon the work of other directors or staff, is not performing the duties he agreed to undertake.

Texas courts (as well as case law from throughout the United States) have elaborated on what it means to discharge duties "in good faith, with ordinary care, and in a manner that the director reasonably believes to be in the best interests of the organization." Traditionally, courts hold the directors of any corporation, including a nonprofit corporation to three distinct duties:

1. The duty of loyalty;
2. The duty of care; and
3. The duty of obedience.

A director is liable to the corporation for his actions only if the director breaches one of these fiduciary duties.

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<sup>1</sup>This memo uses the terms "board of directors" and "director." Some nonprofit corporations refer to their governing board members as "trustees" rather than directors. From a legal standpoint, the terminology is irrelevant. A board of trustees of a nonprofit corporation is the same as a board of directors.

Also, this memo uses the masculine pronouns for ease of readability only! Women of course, make excellent directors.

*The Duty of Loyalty* requires that the interests of the organization must prevail over the interests of the director. A director must place the interests of the organization above his own personal interests. There are state and federal statutes that specifically require this, in addition to common law. The organization's conflicts of interest policy should be drafted specifically with those statutes in mind. Specifically, a director should:

- (a) Keep confidential matters confidential. If you are uncertain whether a matter is confidential, assume that it is. Leaking confidential information is a serious violation of the Duty of Loyalty.
- (b) Make sure that the organization has a current conflict of interest policy and abides by it.
- (c) Make sure that all directors are aware of all the interests of the other directors that might relate to the organization's activities.
- (d) Avoid transactions in which you or a family member benefits OR disclose such transactions fully to the board, and then recuse yourself from any vote related to those transactions.
- (e) Do not borrow from the organization, nor let other directors do so.

*The Duty of Care* requires a director to exercise honest business judgment in the performance of his duties, using the diligence, care and skill which prudent people would use in similar circumstances. Specifically, a director should:

- (a) Be familiar with the organization's activities, website, printed material, and media coverage.
- (b) Attend all board meetings; attend your committee meetings; and participate in decision making and policy setting. Also, insist that directors are given adequate time before each meeting to review any written materials (minutes, financial statements, etc). A director will be presumed knowledgeable of the content of these materials.
- (c) Be willing to oppose board or committee action when necessary, and confirm that any negative vote is recorded in the minutes. At the same time, realize that once the board has made a decision to act (or not act) on any given matter, realize that the Duty of Loyalty requires that you support the course of action that the Board has chosen.
- (d) Make sure that employee compensation is reasonable.
- (e) Make sure that the staff submits major financial obligations, fundraising initiatives, and compensation arrangements to the board for review.

- (f) Review financial statements and compare actual numbers to budgeted numbers. It may be advisable for the organization to obtain audit reports from independent accountants. Each director should consider himself or herself responsible for both the accuracy of these statements and the adequacy of financial planning. Be hesitant to approve expenditures in excess of budget.
- (g) Participate in risk assessment and strategic planning. Obviously, this includes making sure that the fundamental activities of the organization are conducted safely. Risk management includes procuring adequate insurance and also protecting intangible assets such as reputation, quality of services, and staff.
- (h) Make sure that the board has adopted fundamental written policies and controls. Examples of policies often adopted are: the quality of services, investments, acceptance of gifts, facilities management, conflicts of interest, confidentiality, personnel decisions, resolution of disputes and (if applicable), the manner in which the corporation deals with governmental regulation and crisis management.

The *Duty of Obedience* requires a director to make sure that the organization follows the law and acts within its mission, as defined by its charter and by statute. A director should:

- (a) Make sure that the organization stays focused on its mission and does not stray from it.
- (b) Ensure that the organization complies with all applicable laws, regulations, and its own internal policies.
- (c) Be acquainted with laws, insurance requirements, and governmental agencies specifically relevant to the organization's activities.

*Realize that consulting experts is OK!* In discharging a duty, a director may, in good faith and with ordinary care, rely on information, opinions, reports, or statements, including financial statements, that are prepared or presented by staff, by a committee of the organization, or by outside professionals hired by the organization (legal counsel, certified public accountants, or any person who the director reasonably believes possesses an expertise in the matter). In addition, the board of directors may contract with qualified investment advisors and delegate investment management duties to those advisors. The board simply must make sure that the experts that it hires and are qualified for the job entrusted to them, and then oversee those experts with good faith and with ordinary care.