

# THE LIABILITY LANDSCAPE FOR DIRECTORS AND OFFICERS OF NON-PROFITS

In the non-profit world, there often is some confusion about the potential scope of personal liability for the directors and officers of a non-profit organization. Some mistakenly believe that, because they are working on behalf of such an organization, there are absolute protections against such risk. In fact, however, directors, trustees and officers of non-profit corporations may be subject to the same forms of personal liability under Massachusetts law as directors of for-profit corporations. Liability may arise with respect to a director's own acts and omissions, and a director may also be sued or held liable as a representative of the corporation. Liability may be to third parties, as in claims for negligence or intentional harm, defamation, breach of contract, or employment-related issues. Directors also may be subject to personal liability *vis-à-vis* the corporation itself when there is a mishandling or misappropriation of funds or other breach of fiduciary duty.

## *Charitable Immunity and its Limits*

There are, of course, some limits to the personal liability of non-profit board members and officers that are not found in the for-profit world. In Massachusetts, a charity is not liable for more than \$20,000 in damages for injuries ("torts") caused by the organization while conducting activities that are directly related to its charitable mission.<sup>1</sup> This limit would extend to a non-profit corporation's officers and directors in circumstances where under general rules of corporate law those individuals might be subject to personal liability as representatives of the corporation. The limit does *not* apply to activities that are incidental to an organization's mission, such as operating a gift shop or food concession, even if the purpose of those activities is to support the charity's mission.<sup>2</sup> Thus damages would *not* be capped at \$20,000 if they arose from a fundraising activity, unless that activity was itself part of an organization's mission, such as a fundraising concert given by students of a music school. The limit on damages also does *not* apply to non-tort claims such as claims for breach of contract or claims under the Massachusetts consumer protection statute.

Charitable immunity has other important limits as well. It does not apply where a party seeks injunctive relief, *i.e.*, a court order requiring or prohibiting certain acts, and it also does not cover claims under federal law, such as civil rights laws or ERISA claims. Nor does charitable immunity under Massachusetts law offer protection from liability under the laws of other states; although some states have charitable immunity, many do not. Further, the protection provided in principle by the Massachusetts charitable immunity statute may be limited by a court under the circumstances of a particular case. Finally, charitable immunity does not protect non-profit directors and officers against personal liability with respect to claims for breach of fiduciary duty brought by the Commonwealth's Attorney General.

## *Limits on Volunteers' Liability*

Uncompensated officers and directors of non-profit corporations are afforded additional liability protection in Massachusetts for acts or omissions in connection with their corporate duties, except where their acts or omissions arise from activities that are not directly related to the organization's mission (even if carried out to raise funds to support the mission), are grossly negligent, or in certain other limited circumstances.<sup>3</sup> Volunteer officers and directors of non-profit educational institutions, in particular, are more broadly protected from liability than volunteer officers and directors of other types of non-profit organizations in that protection for the former extends to claims arising out of activities that are unrelated to the organization's mission.<sup>4</sup> Volunteers generally are not given protection under Massachusetts law but are protected by federal law against

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<sup>1</sup> M.G.L. c. 231, § 85K.

<sup>2</sup> *Id.*

<sup>3</sup> M.G.L. c. 231, §85W.

<sup>4</sup> M.G.L. c. 231, § 85K.

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claims arising from acts performed within the scope of a volunteer's responsibilities in an organization.<sup>5</sup> The federal law affording this protection applies by its terms to unpaid officers and directors along with other volunteers, but it has not been fully tested in court and thus it is unclear how it would be applied in conjunction with state liability laws. It also is subject to limits and exceptions, such as where a volunteer acts outside of his responsibilities or where injuries were caused by a volunteer's operation of a motor vehicle.<sup>6</sup>

### *Indemnification and Other Protections Provided by the Corporation*

Non-profit corporations in Massachusetts are allowed to limit directors' and officers' potential personal liability to the corporation itself.<sup>7</sup> Such limits must be included in a corporation's articles of incorporation and do not cover breaches of an officer's or director's duty of loyalty to the corporation, acts or omissions which are intentional or not in good faith, or transactions from which an officer or director derived an improper personal benefit. Liability cannot be limited for acts or omissions dating from before the effective date of the relevant provision in an organization's articles of organization, so amending the articles will not provide retroactive protection to an organization's officers and directors.

Another rule of Massachusetts law permits a non-profit corporation to indemnify its officers and directors for costs incurred by them in defending claims against them in their role as officers and directors. This protection typically is established through a provision in the organization's articles of incorporation or by-laws, or even by a vote of its directors or members (if any).<sup>8</sup> Many non-profit corporations include such rights to indemnification in their organizing documents but make it ultimately subject to the directors' or members' discretion, requiring a vote to trigger the indemnification rights. This approach preserves an organization's control over the circumstances in which the indemnification is provided, but it does not provide much assurance to potential or even current directors and officers. Other complications may arise when an organization seeks to indemnify its officers and directors. For example, restricted funds would ordinarily not be available for indemnification coverage, and large expenditures from general endowment funds for indemnification purposes potentially may be considered an improper use of those funds.

### *Director and Officer Insurance*

Because of the limits of charitable immunity and of other broader liability protections for directors and officers of non-profit corporations, most large organizations and even many small organizations obtain director and officer insurance to provide further liability coverage. Any non-profit is advised to conduct a formal assessment of its liability risk profile and to then consider the available risk management tools to minimize the risk of liability for the organization itself and those who lead it.

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<sup>5</sup> 42 U.S.C. § 14503.

<sup>6</sup> *Id.*, § 14503 (a)(1), (a)(4).

<sup>7</sup> M.G.L. c. 180, § 3.

<sup>8</sup> M.G.L. c. 180, § 6.