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The Duties, Responsibilities, and Liabilities of a Director

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Board directors have a number of basic duties and responsibilities that have been developed over the centuries through case law. They are not all that onerous. If you apply common sense, you should have no trouble fulfilling these duties. Similarly, you can avoid most liabilities when you act prudently, and there are ways to cover off the risk that remains.

DUTIES AND RESPONSIBILITIES

There are four core duties of a board director: honesty, loyalty, care, and diligence.

Honesty

As a director, you are obligated to act in an honest manner and in good faith. This means that if you have important information that relates to the charity, you must share it with the board. For example, if a director is aware of a suspected wrongdoing or a policy that is not being followed, the director has a duty to share what is known to the board.

Loyalty

You have a duty to be loyal to the ministry when you are serving on the board. This means that you need to avoid any conflicts of interest. For instance, if you are a building contractor and a church board member and your church is going to build an addition in the near future, you need to choose between providing your contracting services and serving as a director. It would be a conflict of interest for you to engage in both activities. It also means that the interests of the ministry come before your own interests. The question is “What’s good for the ministry?” rather than “What’s good for me?”

Care

You also have a duty of care as a director. You are to act prudently and know what the charity is doing. One aspect of your duty to care is to make sure that you are prepared for board meetings. Make sure that you review the board package well ahead of time and pray about any issues of concern.

Another way to demonstrate the duty of care is to take steps to familiarize yourself with the ministry and its programs and policies. Ask questions: How secure is that revenue stream? Do we have a policy and a plan to protect the vulnerable people we serve? What complaints has the ministry received in the last quarter and how have we dealt with them? What legislation imposes requirements on the ministry? Show that you are actively engaged in board work and not just showing up as a disinterested observer.

Diligence

You must be diligent as a director. Make sure that you ask any questions that are on your mind. As the saying goes, the only bad question is the one you had but didn’t ask. Don’t assume that another director with more expertise will look after the matter.

Years ago I was serving on a church board. As a commercial banker with an MBA, I typically had a few questions to ask about the financial statements at every monthly meeting. One month I didn’t have any questions, so I asked none. When the treasurer asked if there were any questions, all the directors looked at me! Someone said, “We leave financial questions to John because he knows what to look for.” I was horrified. First, that put all the pressure on me to ask the questions. But more importantly, it meant that the directors were letting me do their thinking for them. Directors have a responsibility to think for themselves!

LIABILITY

Directors need to be aware of potential liabilities, which are outlined below. The good news is that directors are not held liable for simple errors in judgment. Directors don’t always have the luxury of waiting until every bit of information has been found before making a decision. If decisions do not turn out for the best, they cannot be held liable as long as they are acting within the standard of care.

Breach of Fiduciary Duty

Your fiduciary duties as a director are all about acting in a way that inspires trust and confidence in your faithful service. If you act in a way that does not do that, you are breaking, or breaching, your duty to be a good fiduciary. You can be held personally liable for breaching your fiduciary duty, and there are three ways you can breach this duty at law:

- **Negligence**. Negligence occurs when you cause harm to somebody else through either your action or your inaction. An example of negligence would be if the board decided to save money in the winter by not shovelling the front sidewalk of the church. Someone could get injured by slipping on the sidewalk and file a lawsuit against the church. The board would be considered negligent in this case, because the likelihood of injury could have been reasonably foreseen and prevented.
- **Acting Outside Your Authority**. You would be in a breach of fiduciary duty if you were to act outside of your authority as a director. For example, say your ministry wanted to buy new computers. You happen to be at a store where they have a sale on computers. You go ahead and sign a contract to buy a number of computers, thinking that you could just go to the board for approval. In this situation, you would be acting outside of your authority because you are not authorized to enter into contracts on behalf of the ministry. If the ministry didn't agree with your purchase, or if they wanted a different brand, then you would be held personally and financially responsible for those computers, and you would be in breach of your fiduciary duty.
- **Failure to Invest Resources Prudently**. Directors cannot invest the ministry's money the same way they would invest personal funds because their risk profiles and investment goals are different from the charity's. Investments must be made prudently according to the circumstances of the charity. A failure to invest prudently could result in directors being held liable for losses.

A number of years ago, a church board member was held personally liable for breaching his fiduciary duty. The church had raised $400,000 for a building addition, but this was only half of the money that the church needed. At one board meeting, the church treasurer suggested that the board invest in interest rate swaps for six months so that the church could double its money. One of the board members was a stockbroker and knew that interest rate swaps were very risky in the absence of an underlying business transaction. But because of the board's enthusiasm, the stockbroker did not share his knowledge and did not vote against the motion.

The motion passed, and the church eventually ended up losing the $400,000. A major donor sued the church board for misinvesting the money. In the end, the judge found that all of the board members were unaware of the risks except for the stockbroker, who should have known better. The stockbroker was held personally liable for the $400,000 because there was no record in the minutes of him speaking or voting against the decision.

One lesson to be learned from this example is that if you vote against a motion, you should have your name listed in the minutes as having voted "no." This will be your defence if the matter ever comes up in court. The other lesson is to speak up and share what you are thinking!

Breach of Trust

In addition to breaches in fiduciary duty, you could be held liable as a director for a breach of trust. This can happen in one of two ways. The first would be if the board misused charitable funds or failed to apply charitable property for charitable purposes. This is especially important in the case of special purpose funds, such as a building fund or a mission fund. Using special purpose funds, also known as externally-restricted funds, for anything other than their designated purpose is a breach of trust for which you are held liable. Another example of a breach of trust is to provide remuneration for directors, either directly or indirectly.

Other Liabilities

A 2001 study by the law firm of Gowling Lafleur Henderson LLP, entitled A Study of the Liabilities Facing Directors and Officers of NonProfit Corporations in Canada, found that there are about two hundred statutes across the country that make directors liable for the action or inaction of their organizations. Considering that there are ten provincial, three territorial, and one federal jurisdiction, there are a fewer number of statutes that apply to you. Most of these statutes have to do with health and safety, payroll deductions for taxes, vacation pay, GST/HST, and the environment. You need management to verify to the board that they are in compliance with all legislation and that payments to the Canada Revenue Agency (CRA) are not in dispute.

Protecting Yourself from Liability

Fortunately, while these liabilities do exist, you can easily protect yourself:

- Act in accordance with the standard of care, fulfill your fiduciary duties, and stay within your authority as a director.
- Make sure that there is a good risk management program in place for the board, particularly if the ministry is dealing with vulnerable individuals, such as children.
- Have Directors and Officers Liability Insurance for your board, with an indemnification agreement with the ministry.

With these measures in place, you would pretty much have to do something criminal to be held personally liable. Acting with honesty, care, loyalty, and diligence is not difficult, and the standard is what a reasonably prudent person would do. If you actively participate in the work of the board, understand what the board is voting on, and make informed contributions to board discussions, you should be able to minimize your risks.