ETHICS CONSIDERATIONS AND THE WHO: BOARD MEMBERS

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BIOGRAPHICAL INFORMATION

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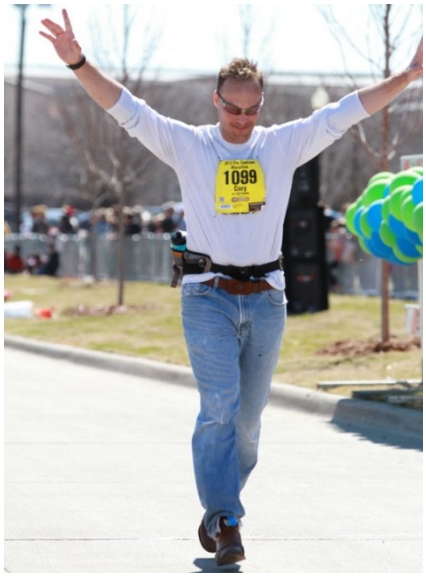
- Freeman Law, PLLC (Dec. 2021-present) www.freemanlaw.com; Weycer, Kaplan, Pulaski & Zuber, PC (2008-Dec. 2021); Hund & Harriger, LLP (2003-2007).
- Mr. Halliburton serves as outside general counsel to a diverse nonprofit / tax-exempt client base as well as for multi-state professional service companies. Results-oriented, with executive-level strategy and an understanding of the intersection of law and business judgment.
- Nonprofit Sector: formation, dissolution, governance, succession, employment law, contracts, intellectual property, tax / tax exemption issues, policy creation, mergers and other. Professional Service Companies: service agreements, employment law matters, and legal strategy.
- Texas Tech University School of Law, *magna cum laude* 2003. SBN 24041044.

Mr. Halliburton's upbringing and diverse experience allows him to apply a valuable perspective to many different business endeavors and legal challenges faced by those he serves. He has presented at tax, legal and business conferences throughout the country and on many legal and business topics affecting tax-exempt entities. He has written and published many professional articles, with a focus on tax-exempt organizations.

Mr. Halliburton and his wife of 24 years, Dr. Jamie Halliburton, a principal in the Grapevine-Colleyville ISD, have three children, a large dog named Bear and one unnamed Red Sex Links chicken. Mr. Halliburton enjoys fly fishing and trekking the Llano River with his kids in a kayak or Old Town canoe. In 2013, he ran the Cowtown Marathon in cowboy boots and blue jeans, donning the ironical bib number 1099. In 2017, he "ran the year," logging 2,030 miles. In May 2021, he and a team of four finished 1st overall in a 50-mile weighted-carry event in Washington, D.C., and in November 2021, the team finished 10th in the GoRuck World Championship 50-mile weighted carry (30 lbs). He also achieved a 2,021-mile run/ruck (30 lbs) combo effort in 2021. Since then, he's rested, mainly.



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I. INTRODUCTION

This article provides a high-level review of select considerations for service on boards of directors of nonprofit organizations as well as considerations for the lawyer who serves as a director on a board of a nonprofit organization.

Many organizations struggle to acquire or maintain a "right" mix of individuals to lead the organization. Some organizations struggle to acquire or maintain *any* individuals to lead the organization. Some individuals expect a place at the board table simply because the individual is a large contributor or otherwise has or may exercise influence over the organization or community. Some organizations require a financial buy-in in order to serve as an officer or director. And, once an individual is seated in the board room, the individual and the organization's expectations of service may not be congruent such that misunderstandings or misfortunes in service result.

In addition, a lawyer who serves on the board of a nonprofit organization should evaluate the ethical responsibilities that exist in that service.

The presentation associated with this article is slotted for 45 minutes, with appropriate allocation of time to ensure participants' receipt of continuing legal education ethics credit. This article is proportionately limited to select and key areas of consideration on these two broad and important topics.

II. OVERVIEW OF THE UNIVERSE THAT IS NONPROFIT ORGANIZATIONS

A. Nonprofit is Not Necessarily Tax-Exempt

"Nonprofit" and "tax exempt" are not synonymous in the world of law and tax.

"Tax exempt" generally means that the entity is, by some act of "legislative grace," exempt from one or more categories of federal or state taxes. *See, e.g.*, *Upjohn Co. v. Rylander*, 38 S.W.3d 600, 606 (Tex. App.—Austin 2000, pet. denied) (noting that "Deductions and [tax] exemptions . . . are matters of 'legislative grace'").

"Nonprofit," in a literal sense, means not making or conducted primarily to make a profit. Despite the colloquial use of the word, most nonprofit organizations indeed desire to make a profit, that is, to receive and retain some amount of earnings for future use. Similarly, not all nonprofit organizations are eligible to receive the same beneficial tax treatments; the beneficial tax regimes vary by organization type.

It is common for an organization to be formed as a nonprofit corporation and to not enjoy an exemption from, for example, federal income tax. In order to enjoy an exemption from a tax, a nonprofit organization must be organized and operated as required by the applicable statutes that afford an exemption from the applicable tax, and, with some exceptions, the nonprofit corporation must apply for and receive a determination of exemption from federal income tax. *See* 26 U.S.C. § 508(c) (excepting churches, integrated auxiliaries, and conventions or associations of churches from the requirement to file an application for exemption from federal income tax).

Chapter 2 of the Texas Business Organizations Code ("TBOC") provides that "[a] corporation formed for the purpose of operating a nonprofit institution, including an institution devoted to a charitable, benevolent, religious, patriotic, civic, cultural, missionary, educational, scientific, social, fraternal, athletic, or aesthetic purpose, may be formed and governed only as a nonprofit corporation under this code and not as a for-profit corporation under this code." TEX. BUS. ORG. CODE § 2.008. Under Chapter 22 of the TBOC, "nonprofit corporation" means "a corporation no part of the income of which is distributable to a member, director, or officer of the corporation, except as provided by Section 22.054[.]" *Id.* at § 22.001(5); *but see id.* at § 22.054 (permitting a nonprofit corporation to pay, for example, reasonable compensation for services rendered and authorizes a few other specific distribution activities). That distribution-limitation requirement is, essentially, an operational matter, not necessarily an organizational matter.

Under Texas law, there is, essentially, no purpose statement requirement in order to qualify as a nonprofit corporation, and a nonprofit corporation may be formed for any lawful purpose not prohibited under Chapter 22 or Chapter 2 of the TBOC. TEX. BUS. ORG. CODE § 22.052; *see id.* at § 2.002 (purposes of nonprofit entity). Chapter 2 of the TBOC provides that a domestic entity may not (1) engage in business that (A) is "expressly unlawful or prohibited by law of this state;" or (B) cannot lawfully be engaged in by the entity under state law; or (2) operate as a bank, trust company, savings association, insurance company, cemetery organization (except where otherwise authorized), or a title company. *See id.* at § 2.003-.003(2)(F).

B. Joint Committee on Taxation Report on Charitable Contributions

On March 17, 2022, the Joint Committee on Taxation published its 49-page report (the "Report") relating to the federal tax treatment of charitable contributions, which may be viewed here: https://www.jct.gov/publications/2022/jcx-2-22/.

C. Key Statistics Noted in the Joint Committee's Report

- As of September 30, 2020, there were approximately 1.75 million Section 501(c)

organizations registered with the IRS, 1.4 million of which were eligible to receive deductible charitable contributions pursuant to Section 170, Title 26 of the Internal Revenue Code ("Code").

- Charitable giving in the U.S. → $471.44 billion in 2020, $324 billion of which was from individuals, with the remainder from foundations, estates, and corporations.
- As a group, religious organizations received the most of all charitable donations (28%), followed by educational institutions (15%), human services organizations (14%), grantmaking foundations (12%), and health organizations (9%).
- Giving to donor advised funds has grown at a rate that far exceeds the rate of growth in overall charitable giving, indicating an increase from $31 billion to $141 billion (an increase of 356%) between 2006 and 2019.
- For 2018, the categories of non-cash contributions were dominated by corporate stocks and other investments ($42.69 billion), with the next highest being conservation easements ($6.5 billion).
- $217.6 billion was the estimated amount that taxpayers would claim as charitable contribution deductions in 2022.

Under Texas law, a nonprofit organization may be formed as a charitable trust, a nonprofit corporation, an unincorporated association, or a limited liability company, provided that, for the latter, the member (and all members) meet certain qualifications. *See* TEX. PROP. CODE §§ 111.001-.006 (Texas Trust Code); *id.* at § 123.001(1), (2) (defining "charitable entity" and "charitable trust" for purposes of attorney general oversight and enforcement of and within the charitable organizations industry); TEX. BUS. ORG. CODE §§ 22.001, *et. seq.* (core statutory regime for Texas nonprofit corporations); *id.* at §§ 101.001, *et. seq.* (core statutory regime for Texas limited liability companies); *id.* at §§ 252.001, *et. seq.* (statutory regime for unincorporated associations).

The near-two million organizations referenced in the Joint Committee Report does not include the multitude of other nonprofit organizations that are organized and operated pursuant to Section 501(c) of the Internal Revenue Code that are not eligible to receive deductible charitable contributions, such as trade associations and others.

Indeed, the nonprofit organizations sector plays a significant function in the U.S. society and economy.

Nonprofit organizations exist in many shapes and sizes. They include religious organizations, churches, schools, health and human services organizations, arts foundations and societies, social organizations, trade associations (which includes an association or society for nearly every profession that exists plus some), animal-focused organizations, environmental organizations, civil rights-focused groups, veterans organizations, and many others.

Each and every one of those millions upon millions of nonprofit organizations is governed, directed, and managed by individuals who are elected or appointed, in some fashion, pursuant to applicable law and/or the applicable governing documents of the organization.

III. CHAPTER 22 OF THE TBOC, FOR EXAMPLE.

Chapter 22 ("Chapter 22") of the Texas Business Organizations Code ("TBOC") is sometimes referred to as the Texas Nonprofit Corporations Act. Chapter 22 provides the general statutory provisions for nonprofit corporations incorporated under Texas law as well as certain requirements for foreign nonprofit corporations. *See id.* at § 22.001(3) (defining "corporation" as a "domestic nonprofit corporation subject to this chapter.").

Multiple other chapters of the TBOC are woven into Chapter 22. For example, a nonprofit corporation may be formed for any lawful purpose not prohibited under Chapter 22 or Chapter 2. *Id.* at § 22.052; *see id.* at § 2.002 (setting forth permissible, non-exclusive purposes of a nonprofit entity). Chapter 22 also cross-references to statutes in other chapters of the TBOC, including Chapters 3, 6, 10, 11. *See, e.g., id.* at §§ 22.002 (cross-reference to Section 6.002, TBOC), 22.109(b) (cross-reference to Chapter 3), 22.164(a)(3) (cross-reference to Section 11.151, TBOC), and 22.251(a) (cross-reference to Chapter 10, TBOC).

The lawyer for a Texas nonprofit corporation and, perhaps to a lesser extent, the officers and directors of the organization, should become familiar with Chapter 22 and its workings with other chapters of the TBOC as well as with the corporation's internal governance structure. In this regard, a Texas nonprofit corporation may be formed only by complying with the filing requirements of Chapter 3 of the TBOC, which requires the filing of a certificate of formation with the Texas Secretary of State in accordance with Chapter 4 of the TBOC. *See id.* at § 3.001(a), 4.001(a)(1).

And, a nonprofit corporation may have bylaws, being "the rules adopted to regulate or manage the corporation, regardless of the name used to designate the rules." *See id.* at § 22.001(2). In some instances, the certificate of formation or bylaws control a matter that may be covered by Chapter 22. In other instances, Chapter 22 may control, even if the certificate of formation or bylaws provide a conflicting result. Chapter 22 has various statutory provisions that will not apply, if the particular matter is otherwise addressed in the corporation's certificate of formation or bylaws. *See, e.g.*, *id.* at § 22.159(a) (addressing requirements for a quorum of members and providing "Unless otherwise provided by the certificate of formation or bylaws of a corporation, . . ."), 22.103(a) (providing, "[a] provision

of a certificate of formation . . . that is inconsistent with a bylaw controls over the bylaw", with one exception regarding a change in the number of directors, as provided in section 22.103(b)).

IV. THE BOARD OF DIRECTORS

Under Chapter 22, the "board of directors" of a Texas nonprofit corporation "means the group of persons vested with the management of the affairs of the corporation, regardless of the name used to designate the group." *Id.* at § 22.001(1). An attorney for a Texas nonprofit corporation, as well as all individuals who serve as an officer or director of any nonprofit organization, should understand the fiduciary duties owed by those decision-makers, mainly, that they must discharge their duties in good faith, with ordinary care, and in a manner the director reasonably believes is in the best interest of the corporation. *See id.* at § 22.221 (setting forth the general standards for directors of a nonprofit corporation to discharge their duties); *id.* at § 22.235 (setting forth similar standards for officer liability and conduct).

Sections 22.221 and 22.235 in Chapter 22 capture but do not necessarily wholly supplant, common law concepts of the duty of care, the duty of loyalty, or the duty of obedience, each of which have similar but differing qualities. And, as indicated above, not all nonprofit organizations are formed as nonprofit corporations, so the duties that have been developed by common law may still play a vital role in establishing the conduct guardrails for those who serve as an officer or director of a nonprofit organization not governed by Chapter 22.

"Ordinary care" basically means that the person exercise the degree of care that a person of ordinary prudence would exercise in the same or similar circumstances. If a director or an officer, for example, has special expertise in a particular matter, the ordinary care standard means that degree of care that a person with similar expertise would exercise in the same or similar circumstances. In executing the duty of care, the board of directors of a Texas nonprofit corporation may contract with and rely on experts, such as attorneys. *See id.* at § 22.228.

Common examples of breach (or potential breach) of these duties and standards of conduct include transactions that involve a conflict of interest and not properly presented and approved, usurpation of opportunity of the nonprofit corporation, and unauthorized disclosure of confidential information of the corporation. The lawyer for the nonprofit corporation should regularly remind decision-makers of these important and real fiduciary duties.

V. DIRECTOR-SELECTION AND REMOVAL PROCESSES

It is important to know the governance structure of the entity. For example, under Chapter 22, a Texas nonprofit corporation may have one or more classes of members or may have no members. TEX. BUS. ORG. CODE § 22.151(a). If the corporation has members, the articles of organization or bylaws must include (1) a designation of each class; (2) the manner of appointment of the members of each class; and (3) the qualifications and rights of the members of each class. *Id.* at § 22.151(b)-(b)(3). And, if a nonprofit corporation has members with voting rights, those members have a statutory right to vote on "fundamental action" proposed to be taken by the corporation, such as a winding up, a plan of merger, and even for amending the certificate of formation. *See id.* at § 22.164(a)-(c)(3) (listing ten fundamental actions and member rights regarding same).

Conversely, a Texas nonprofit corporation or other nonprofit organization may be governed solely by a board of directors, *see id.* at § 22.201, or the management of the corporation or organization may be vested, in whole or in part, in a particular class of members. *See id.* at § 22.202(a)-(b).

The rights and responsibilities of those within a particular governing body—whether as a board or in a particular membership class—will play a role in molding fiduciary conduct as well as legal counsel provided for the organization's use and benefit.

How an organization selects and appoints directors is usually set forth in the organization's governing documents, such as bylaws, and most statutory regimes give deference to whatever election or removal processes are contained in the governing documents. Chapter 22 or other applicable statutory regime that governs the organization, as well as the organization's governing documents are the primary sources for understanding the governance requirements for the particular organization, including for the selection, election, appointment or removal of officers, directors, and other decision-makers within the governance regime of the organization.

If the organization has members with voting rights, and if those rights include the right to select, nominate, and/or elect directors to the governing body, due care should be put forth to ensure that those rights and the processes for effecting same are honored, including for notices, voting procedures, and records-retention for minutes, ballots, and other evidence of the governance process installed to honor the governing documents and members' rights.

An organization's governing documents may have what is commonly referred to as a "self-perpetuating board of directors," meaning, generally, that the board of directors is the sole body involved in the succession

of director positions. Below is an example bylaw provision:

A. Directors – Number, Term and Qualifications.

The powers of the Organization shall be exercised by or under the authority of, and the property, business, and affairs of the Organization shall be managed under the direction of a board of not less than three (3) Directors, as may be determined by the Board from time to time, provided that the number of Directors shall not be decreased to less than three (3) and that no decrease in the number of Directors shall have the effect of shortening the term of any incumbent Director. Each Director shall serve for a term of three (3) years, and the Board may stagger the election for succession planning or other legitimate purposes. A person who meets any qualification requirements to be a Director and who has been duly nominated may be elected as a Director. Directors shall be elected by the majority vote of the Board. Directors shall be elected at the annual meeting of the Board. Each Director shall hold office until a successor is elected and qualified. A Director may be elected to succeed himself or herself as Director.

Chapter 22 provides the following statutory provision for the term of office of a director of a Texas nonprofit corporation:

Sec. 22.208. TERM OF OFFICE.

(a) Unless the director resigns or is removed, a director on the initial board of directors of a corporation holds office until the first annual election of directors or for the period specified in the certificate of formation or bylaws of the corporation. Directors other than the initial directors are elected, appointed, or designated for the terms provided by the certificate of formation or bylaws.

(b) In the absence of a provision in the certificate of formation or bylaws setting the term of office for directors, a director holds office until the next annual election of directors and until a successor is elected, appointed, or designated and qualified.

(c) A director may be removed from office as provided in Section 22.211.

An organization's governing documents may allow the governing body (including members, if there are members with such rights) to remove a director, with or without cause, or the governance may require some level of "cause" or other reason to exist before a director may be removed. Many times the body of individuals who appointed the individual to a director position has a right to fill any vacancy in that position, but that is not always the case; due care should be taken when filling a vacancy caused by a removal, with a close look at the organization's governing documents.

Chapter 22 provides the following statutory provision for the removal of a director of a Texas nonprofit corporation:

Sec. 22.211. REMOVAL OF DIRECTOR.

(a) A director of a corporation may be removed from office under any procedure provided by the certificate of formation or bylaws of the corporation.

(b) In the absence of a provision for removal in the certificate of formation or bylaws, a director may be removed from office, with or without cause, by the persons entitled to elect, designate, or appoint the director. If the director was elected to office, removal requires an affirmative vote equal to the vote necessary to elect the director.

Further, organizations that require some level of "cause" to remove a director should carefully evaluate the established condition-for-removal as well as the process that must be installed for removal of a director pursuant to the standards contained in the governing documents.

Below is an example bylaw provision for removal of a director without cause:

B. Removal of Director.

The Board of Directors may vote to remove a Director at any time, with or without good cause. A meeting to consider the removal of a Director may be called with notice to the Board members. The notice of the meeting shall state that the issue of possible removal of the Director will be on the agenda.

VI. MANDATED CONTRIBUTIONS AS A CONDITION FOR BOARD SERVICE

Some organizations have a "pay-to-play" governance philosophy, meaning, if a person wants a seat in the board room, the individual is expected to contribute to the organization. Individuals who contribute to such organizations may want to ensure that a charitable contribution tax benefit is received. However, under section 170, Title 26 of the Internal Revenue Code, does a director on a nonprofit board of directors have a right to deduct as a charitable contribution, an amount the director gives to the organization when the organization–by policy, bylaw, or other mandate–required the contribution as a condition for service on the organization's board of directors?

Essentially: Are contributions made under organizational prescription or mandate deductible as a charitable contribution by the contributing director?

If that director's tax return is audited, is the amount contributed deductible as a charitable contribution under section 170, or might the IRS deny the charitable deduction, assess penalties, or make other adverse determinations against the individual director/taxpayer?

Maybe, or maybe not, but that is not this tax practitioner's prerogative to decide here. *See* IRS Circular 203 § 10.37(a)(2)(vi) (providing that a tax practitioner must "Not, in evaluating a Federal tax matter, take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit.").

A. What is a "gift" for income tax purposes.

Section 102(a) of the Internal Revenue Code provides: "Gross income does not include the value of property acquired by gift, bequest, devise, or inheritance." In *Commissioner v. Duberstein*, 363 U.S. 278 (1960), the U.S. Supreme Court defined a gift under IRC section 102 as a transfer that proceeds from a detached and disinterested generosity, out of affection, respect, admiration, charity or like impulses. The donor's intent is controlling, rather than donor characterization of the transaction. The IRS and the courts examine objectively whether a gift occurs based on the facts and if those facts support a donor that intended a transfer based on affection. Detached and disinterested generosity is critical. If a transfer is made out of an expectation (or even a moral duty) on the recipient's part, the transfer may not be qualified as a gift under IRS section 102 because the "gift" did not arise out of a detached and disinterred generosity.

B. What is a "charitable contribution" under IRC section 170?

Pursuant to Code section 170(a)(1), "[t]here shall be allowed as a deduction any charitable contribution (as defined in subsection (c)) payment of which is made within the taxable year. A charitable contribution shall be allowable as a deduction only if verified under regulations prescribed by the Secretary." As used in section 170(a), the term "charitable contribution" is synonymous with the word "gift," being a voluntary transfer of property by the owner to another without consideration–a detached and disinterested generosity, motivated by affection, respect, admiration, charity, or like impulses. *See Comm'r v. Lobue*, 351 U.S. 243, 246 (1956); *Robertson v. United States*, 343 U.S. 711, 714 (1952); *DeJong v. Comm'r*, 36 T.C. 896, 899 (1961), *aff'd* 309 F.2d 373 (9th Cir. 1962); *Consolidated Investors Group v. Comm'r*, T.C. Memo 2009-290, at 48-49 (2009). A gift is not compelled by the constraining force of any moral or legal duty. *Bogardus v. Comm'r*, 302 U.S. 34, 41 (1937).

C. Fifth Circuit, as an Example.

According to the Fifth Circuit, a contribution is a gift only if it is "not intended as a return of value or made because of any intent to repay another what is his due, but bestowed only because of *personal affection or regard or pity*, or from general motives of philanthropy or charity." *Schall v. Comm'r*, 174 F.2d 893, 894 (5th Cir. 1949) (emphasis added) (quoting *Bass v. Hawley*, 62 F.2d 721, 723 (5th Cir. 1933) (honorarium gift because no future services promised or provided), *rev'g* 11 T.C. 111 (1948). "A gift can be made only out of "personal affection or regard or pity, or from general motives of philanthropy or charity."" *Brown v. Comm'r*, T.C. Memo 2019-69 (U.S. Tax Court 2019) (quoting *Schall*, 174 F2d. at 894).

D. Contemporaneous Written Acknowledgement.

Pursuant to Code section 170(f)(8)(B), contemporaneous written acknowledgements must include the amount of cash and a description (but not value) of any property other than cash contributed, whether the recipient provided any goods or services in consideration for the contribution, and a good faith estimate of the value of any such goods or services.

Can an organization honestly acknowledge as such if the gift in question was compelled by the organization in exchange for a seat at the board table?

Can or must the organization qualify the acknowledgement based on the *quid pro quo* nature of the "gift"?

E. Joint Committee on Taxation's Perspective.

In the Joint Committee on Taxation Report on Tax Treatment of Charitable Contributions (March 11, 2022), *supra*, the Committee guidance or committee comments included the following:

- Page 8 of 51 of Report: "To be deductible, a charitable contribution generally must meet several threshold requirements. The recipient organization must be eligible to receive deductible charitable contributions. The transfer must be made with gratuitous intent and without the expectation of a benefit of substantial economic value in return."
- Page 12 of 51 of Report: "The term "contribution or gift" is generally interpreted to mean a voluntary transfer of money or other property without receipt of adequate consideration and with donative intent. A payment or other transfer to a charity (regardless of whether it is called a "contribution") is not deductible if it is made in exchange or in return for an economic benefit."
- Footnote 50 on page 13 of 15 of Report: "Intangible return benefits and certain low-cost items given in exchange for a contribution do not reduce the value of the charitable deduction." *But see Brown v. Comm'r*, T.C. Memo 2019-69 (U.S.

> Tax Court 2019) (addressing gifts made by congregants for benefit of pastor and finding that the expectation of giving rendered the "gifts" not so to the recipient pastor; "But in the profane world of tax law, a payment can still be for services rendered even if the payor does not receive an economic benefit from it.").]

Ultimately, this is a business decision for the organization, and the deductibility of such mandated contributions depends on many factors, including the donor's intent. If the organization mandates giving in exchange for permitted board service, the organization should consider whether and how it may disclose the *potential* tax consequences to the donating directors.

For contributions over $250, the donor must receive a contemporaneous written acknowledgement as required by IRC section 170, including a statement that no goods or services were provided in exchange of the gift. The organization may disclose to each director that they should consult with their tax consultant as to the deductibility of the contributions made in compliance with the organization's mandate. Or, the organization may decide that the return benefit of being allowed to serve is intangible and not the type of return consideration that disqualifies the giving as a charitable contribution, and thus, the organization may decide to issue unqualified written acknowledgments of gift.

If the IRS audits the director's tax return and determines that the contribution to the organization was given as an expectation or legal or moral obligation to the organization and not by detached generosity or philanthropic motive, the contribution may not be deductible as a charitable contribution. Penalties could be assessed against and other adverse consequences could befall upon the individual director.

The organization may appropriately "soften" the mandate so that the organization substantially avoids all these potential adverse consequences to donating directors. The organization can "educate" those serving as to what is meant by the "expectation," and that could serve to fill any gap-of-concern among those who believe a written mandate for giving is necessary. And, the organization may monitor expected director giving to see if corrective action or further encouragement is needed to spur a director to meet the organization's expectation of director-giving. Upon audit, all of those efforts, actions, factors, and circumstances will likely be evaluated in the analysis of whether an individual's gift was, indeed, a charitable contribution as defined by the Internal Revenue Code.

VII. ETHICAL CONSIDERATIONS FOR THE LAWYER ON THE NONPROFIT BOARD

Many nonprofit organizations operate and succeed from the monetary and non-monetary contributions of community leaders and businesses. Within that scope of contributors, lawyers are commonly asked to serve as volunteer officers or directors on boards of directors for nonprofit organizations. By such service, a non-fungible *quid pro quo* relationship generally always arises between the lawyer and the organization—the organization benefits from an individual that is (presumably) educated, thoughtful, ethical, and strategic, and the lawyer benefits by gaining a sense of community and access to a potential network of referral sources.

The lawyer who serves as an officer or director of a nonprofit organization must remain vigilant of circumstances that implicate the Texas Disciplinary Rules of Professional Conduct. Below is a non-exclusive list of those Rules that may be implicated in a lawyer's volunteer service as an officer or director of a nonprofit organization.

Select Texas Disciplinary Rules of Professional Conduct		
Rule	**Excerpts or Summary**	**Consideration for the Lawyer "on the Board"**
Rule 1.01 Competent and Diligent Representation	(a) A lawyer shall not accept or continue employment in a legal matter which the lawyer knows or should know is beyond the lawyer's competence, unless: (1) another lawyer who is competent to handle the matter is, with the prior informed consent of the client, associated in the matter; or (2) the advice or assistance of the lawyer is reasonably required in an emergency and the lawyer limits the advice and assistance to that which is reasonably necessary in the circumstances.	A lawyer who serves as an officer or director of a nonprofit organization is often presumed to know everything about the legal and tax matters that the corporation may face. A lawyer should be careful not to knowingly or unknowingly turn the officer or director "hat" to that of legal advisor, especially in areas for which the lawyer has no experience. The laws on topics such as tax-exemption, tax, and nonprofit organizations can be complex and riddled with nuances that not every lawyer may be aware. The lawyer should stay in his or her lane and avoid stepping into the shoes of the nonprofit organization's lawyer when, in reality, the organization's best interest dictate that the lawyer should not be there.
Rule 1.06 Conflict of Interest: General Rule	(a) A lawyer is prohibited from representing opposing parties in the same litigation. (b) Except where proper disclosure is made to and consent is received from a client pursuant to Rule 1.06(c), a lawyer shall not represent a person if the representation of that person: (1) involves a substantially related matter in which that person's interests are materially and directly adverse to the interests of another client of the lawyer or the lawyer's law firm; or (2) reasonably appears to be adversely limited by the lawyer's or law firm's responsibilities to another client or to a third person or by the lawyer's or law firm's own interests.	Rule 1.06 contains the general rule for conflicts of interest and prohibits or limits a lawyer from engaging in a representation that results in certain conflicts of interest. When serving as a decision-maker for a nonprofit organization, the lawyer must evaluate all interests that may be implicated by that service, including those of the organization, the clients of the lawyer, the lawyer's law firm, and the lawyer. A lawyer's duty of loyalty can be conflicted. As a director or officer of a nonprofit organization, the lawyer must act in a manner that is in the best interest of the organization. If those interests are adverse to the interests of the lawyer's client or to a client of the law firm, the lawyer is in a conflicted situation and must manage the situation so as to not violate applicable fiduciary standards (such as sections 22.221 or 22.235 of the TBOC) or Rule 1.06 of the Tex. Disc. R. Prof'l Conduct.
Rule 1.08 Conflict of Interest: Prohibited Transactions	(a) A lawyer shall not enter into a business transaction with a client unless: (1) the transaction and terms on which the lawyer acquires the interest are fair and reasonable to the client and are fully disclosed in a manner which can be reasonably understood by the client; (2) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; and (3) the client consents in writing thereto.	At a high level, Rule 1.08 prohibits a lawyer from taking advantage of a client. Rule 1.08 provides ethical guardrails and restrictions for certain transactions between a lawyer and a client. If the lawyer serves on a board of a nonprofit organization, and if the lawyer proposes that the lawyer or the lawyer's law firm represent that organization, then the processes required by Rule 1.08 should be followed.

Rule 1.12 Organization as a Client	(a) A lawyer employed or retained by an organization represents the entity. While the lawyer . . . may report to . . . an entity's . . . authorized constituents, in the situations described in paragraph (b) the lawyer shall proceed as reasonably necessary in the best interest of the organization without involving unreasonable risks of disrupting the organization and of revealing information relating to the representation to persons outside the organization. (b) A lawyer representing an organization must take reasonable remedial actions whenever the lawyer learns or knows that: (1) an officer, employee, or other person associated with the organization has committed or intends to commit a violation of a legal obligation to the organization or a violation of law which reasonably might be imputed to the organization; (2) the violation is likely to result in substantial injury to the organization; and (3) the violation is related to a matter within the scope of the lawyers representation of the organization.	If a lawyer of the nonprofit organization also serves as an officer or director of the organization, the lawyer will need to carefully and clearly communicate which "hat" the lawyer is wearing when taking any action. Appropriate and timely disclosure should be made to all within the organization with whom the lawyer interacts. This can be a difficult web to navigate, and if a lawyer or the lawyer's law firm represents the nonprofit organization, a recommended course of action is to resign from decision-making positions for the corporation and to remain solely in the capacity of lawyer for the organization.
Rule 1.13 Conflicts: Public Interests Activities	"A lawyer serving as a director, officer or member of a legal services, civic, charitable or law reform organization, apart from the law firm in which the lawyer practices, shall not knowingly participate in a decision or action of the organization: (a) if participating in the decision would violate the lawyers obligations to a client under Rule 1.06; or (b) where the decision could have a material adverse effect on the representation of any client of the organization whose interests are adverse to a client of the lawyer."	Comment 1 to this Rule provides that lawyers are encouraged to engage in community service, and, with two exceptions, they may do so, even if the organization has interests adverse to a client of the lawyer or else serves persons having such adverse interests. However, if the lawyer is asked to participate in a decision that is adverse to the interests of the lawyer's client, the lawyer should abstain from the decision and recuse himself or herself from obtaining confidential information of the organization about the matter.
Rule 2.01 Advisor	"In advising or otherwise representing a client, a lawyer shall exercise independent professional judgment and render candid advice."	Independence—a key attribute of any lawyer and of any officer or director of a nonprofit organization. A lawyer's service as an officer or director for a nonprofit organization may impact the lawyer's ability to provide candid advice to clients, and the lawyer should remain vigilant of his or her independence and ability to provide candid advice given the duties also owed to the nonprofit.

SAMPLE DIRECTOR AND OFFICER CONFIDENTIALITY COMMITMENT FORM

Organization Name
Confidentiality and Non-Disclosure Commitment

Officers and directors of Organization ("Organization") who are permitted to attend Board or Executive Committee meetings, may engage in discussions that are intended and, at times, required by fiduciary duty, law, or contract, to remain confidential and not disclosed to others. The Organization's confidentiality expectations and legal requirements protect the Organization, its employees, donors, business partners, and the communities served by the Organization.

As used herein, the term "Confidential Information" includes all information, data, financial or personnel records or information, and discussions that relate to the proprietary or confidential business, personnel, facilities, services, and processes of the Organization that are not publicly known or publicly disseminated by the Organization. Confidential Information may include information regarding the Organization, operations, policies, procedures, strategic plans, contracts, finances, and investments, as well as information about individuals, employees, donors, and business partners. Confidential Information includes the internal deliberations and decisions of the Board of Directors with respect to any of the above.

The Organization's internal strategic decisions and directions involve the sharing of private, Confidential Information with members of the Organization's management—officers, directors, and select employees or volunteers—who will have access to Confidential Information as needed to perform their duties to and for the Organization. All such Confidential Information must remain in the strictest confidence. Any disclosure to any third party could result in legal liability for the Organization and the disclosing individual.

By signing this statement, the undersigned acknowledges the obligation to keep all Confidential Information disclosed to the undersigned, including during or in relation to a meeting of the Board of Directors or any committee, confidential and to not disclose such information to any third party, unless compelled by law.

The undersigned acknowledges that Confidential Information made available to the undersigned shall remain confidential and that any copies of Confidential Information documents remain the exclusive property of the Organization. All records containing Confidential Information shall, upon request of the Organization, be promptly returned to the Organization. The undersigned acknowledges the obligation to promptly notify the Organization's appropriate officers or management upon discovery of any unauthorized use or disclosure of Confidential Information and to reasonably cooperate to help the Organization regain possession of the Confidential Information.

Signature: _____

Print Name: _____

Position(s): _____

Date: _____