

OFFICE OF THE ATTORNEY GENERAL

**GUIDE FOR
BOARD MEMBERS
OF CHARITABLE
ORGANIZATIONS**

DECEMBER 2022

ATTORNEY GENERAL'S GUIDE FOR BOARD MEMBERS OF CHARITABLE ORGANIZATIONS

December 2022



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INTRODUCTION

This guide is provided by the Attorney General's Office to help board members of charitable nonprofit organizations carry out their important responsibilities. As a board member you have both the privilege and the responsibility of participating in the governance of an organization that is operated not for the benefit of private individuals, but for the benefit of the public. As the agency of the Commonwealth charged with protecting the public's interest in your organization's activities, the Attorney General's Office deeply appreciates your willingness to serve as a board member and recognizes that your hard work and dedication perform an extremely important service for all citizens of the Commonwealth.

While portions of this guide may be helpful and applicable to all nonprofit organizations, it should be emphasized that it is specifically designed for board members and trustees of those nonprofit organizations (e.g., charitable nonprofit corporations, trusts, unincorporated associations, and LLCs) that are "public charities." What constitutes a public charity is not widely understood, and people are often surprised to learn that these organizations range in size, scope and complexity from our largest universities and health care systems to small, neighborhood-based social service organizations. As a general rule these otherwise diverse organizations are linked not just by nonprofit status, but also because they operate on an exclusively charitable basis and collect, hold and expend funds solely for the benefit of the public.

Examples of nonprofit organizations that **are** public charities include philanthropic organizations as well as most of our hospitals, colleges and universities, social service providers, cultural organizations, parent-teacher associations/organizations, and youth sports leagues. Examples of nonprofit organizations that **are not** public charities and are therefore not regulated by the Non-Profit Organizations/Public Charities Division of the Attorney General's Office, include chambers of commerce, labor unions, social clubs, civic associations and similar organizations that benefit only their members. If you have any doubt regarding your organization's status, you should consult legal counsel or contact the **Non-Profit Organizations/Public Charities Division** of the Attorney General's Office at (617) 963-2101.

Often we are asked what we believe are the most important things board members can do to best serve their organizations. Here are our recommendations in key areas of stewardship. While this guide is not intended to prescribe the exact manner in which a Massachusetts public charity board must function, and while we recognize that the size, form and structure of boards vary greatly, we believe that this guide will help all board members and trustees do their jobs well.

I. BOARD MEMBERS HAVE RESPONSIBILITIES

If you are a member of the board of directors of a charitable organization, you and your fellow board members are responsible for governing the organization.

The law imposes upon you two primary duties: the duty of care, and the duty of loyalty. The **duty of care** means that you must act with such care as an ordinarily prudent person would employ in your position. The **duty of loyalty** means that you must act in good faith and in a manner that you reasonably believe is in the best interest of the organization, in light of its purposes. Because a charitable organization exists to further a charitable mission, it is appropriate to view these fiduciary duties as **duties you owe to the charitable mission** of the organization at least as much as, and in some circumstances even more than, to the organization itself.

As discussed throughout this guide, it is your job to oversee the executive director (ED) or chief executive officer (CEO) and other senior leaders, and to see that the organization is faithfully carrying out its charitable purposes without extravagance or waste.

THIS MEANS:

- You should evaluate your existing commitments and obligations to ensure that you have adequate time and energy to dedicate to your role on the board.
- You should attend board meetings and meetings of committees on which you serve. You should make sure that you receive detailed information beforehand about matters that are going to be voted on at a meeting.
- You should carefully read all of the material that you receive and prepare yourself to ask questions.
- You should use your own judgment and not simply take the word of your CEO or fellow board members.

- Your entire board should periodically complete a self-assessment about how well the board is performing its oversight and leadership functions. Among other criteria, a good self-assessment will take into consideration your organization’s mission and industry, consider how well the organization is furthering its charitable purposes, and evaluate the organization’s diversity, including, but not limited to diversity in leadership and representation from the community the organization serves. To get started, your board may consider using a self-assessment tool. For example, resources related to board self-assessments can be found at <https://www.councilofnonprofits.org/tools-resources/self-assessments-nonprofit-boards>.

IN SHORT:

You are responsible for helping ensure your organization is fulfilling its charitable purpose and you should be aware of and informed about every major action the charity takes.

II. EDUCATE YOURSELF

Board members of a charity should be knowledgeable about their role in the governing process, the mission of the organization, and the unique operational, legal, and financial issues facing the organization.

THIS MEANS:

- You should have a copy of, and be familiar with, the articles of organization of your organization and the bylaws of your board. Understand the organization's indemnification policy and any insurance policies that may apply.
- Board members should regularly attend training on fiduciary obligations, sub-sector specific trainings relevant to your organization (e.g., higher education, health care, animal welfare), and trainings on good governance practices, including diversity and equity issues, implicit or unconscious racial or ethnic biases, and other matters that impact effective board composition and functioning.
- Particular attention should be given to providing orientation to new board members.
- Programs and materials should draw on the expertise of specialists in the fields related to your board responsibilities.
- The organization should have a board manual which should include, among other things, governing documents, copies of the most recent regulatory filings (e.g., IRS Form 990 and audited financial statements), budget, and other orientation materials, including this guide.

IN SHORT:

As a board member, you must take the initiative to educate yourself on an ongoing basis about your role and responsibilities, and the board as a whole must take responsibility for its own training and orientation.

III. YOU HAVE THE RIGHT TO INFORMATION

In order to carry out your legal responsibilities as a board member, you must be able to make informed judgments about important matters affecting the organization. The law permits you to reasonably rely on information from the organization's staff, lawyer, auditor, outside advisors, and board committees in making those judgments. If you do not have adequate information, you have the right to get it.

THIS MEANS:

- You have the right to have reasonable access to management.
- You have the right to have reasonable access to internal information of the organization.
- You have the right to have reasonable access to the organization's principal advisors, such as its auditors or attorneys, for example.
- Senior management must be willing to facilitate board access to the books and records of the organization.
- Senior management must be willing to facilitate communications between the board and the principal advisors of the organization.
- The board has the right, if necessary, to engage the services of outside advisors at the organization's expense to assist it with a particular matter.

IN SHORT:

You have the right to obtain the information you need to carry out your responsibilities as a board member.

IV. PAY CLOSE ATTENTION TO FINANCIAL MATTERS

As a board member you have primary responsibility for making sure that the charity is financially accountable, that it is not allowing charitable assets to be used inappropriately or diverted to private interests, that it has mechanisms in place to keep it fiscally sound, and that it is properly using any restricted funds it may have.

THIS MEANS:

- The board should make sure that a realistic annual budget is developed.
- The budget should be developed early enough that the entire board can be involved in its review and approval before the beginning of the fiscal year.
- The board has an obligation to act as a responsible fiscal steward, regularly considering the organization's short- and long-term financial health and acting accordingly.
- The board should be sure that the charity has adequate internal accounting systems and controls. At a minimum, the board should discuss and approve all delegations of its signatory authority, put these delegations in writing, and review them annually. In addition, the board should consider requiring board action on large or especially significant contracts or grants, and on all transactions involving real estate, borrowing, or sale/disposal of large assets. Board members should expect management to produce timely and accurate income and expense statements, balance sheets, and budget status reports, and should expect to receive these in advance of board meetings. These reports ought to be easily understood by the majority of board members and board members should take an active role in reviewing and questioning the information in them.
- The board should require periodic confirmation from management that required filings with relevant government agencies, such as the Internal Revenue Service, the Secretary of the Commonwealth, and the Non-Profit Organizations/Public Charities Division of the Attorney General's Office, are up to date. The board should also ensure that employee

withholdings, insurance premiums and wages are properly and timely administered.

- The board should consider the value of having independent audits and maintaining standing audit and finance committees. However, if these committees are established, the full board should still receive and act on the report of the independent auditor, receive periodic financial reports, and approve the budget.
- The board should make sure that fundraising is done honestly and with integrity. The board also should make sure that any contract with an outside professional fundraiser is fair and reasonable, and that the fundraiser's performance is monitored.
- The board should confirm that any restricted gift to the charity is separately accounted for, and that the funds are being used in accordance with the terms of the restriction. If the terms of any existing restriction on funds conflict with the organization's mission or public policy (e.g., restrictions that are discriminatory overtly or in operation), the board should direct management to seek modification of those terms, which may be available by judicial modification, by agreement of the donor, or in some cases, by administrative modification through the Attorney General's Office. The board should ensure that the organization has a system in place to prevent the acceptance of gifts with restrictions that conflict with the organization's values, public policy, or the public good (e.g., restrictions that could exacerbate racial and ethnic inequities).

IN SHORT:

The board should be informed about all aspects of the organization's finances and is ultimately responsible for the financial health and integrity of the organization.

V. MAKE SURE YOUR BOARD IS VITAL AND DIVERSE

A charity's board should be vigorous and responsive to the mission of the charity. You should make sure that your board's process for selecting new members assures diversity of viewpoints and representation, and allows for rotation of board members and officers (e.g., by including term limits for board members and officers). As a board member, you are responsible for ensuring that the public and charitable role of the organization will be carried out in a way that is effective in furthering the mission of the charity and that avoids or ameliorates apparent or actual inequities, including in access to the organization's services.

A nominating process that invites openness, variety, and change is important to achieving this goal. The board should develop an equitable and inclusive board recruitment practice that encourages a diverse pool of candidates.

THIS MEANS:

- Your nominating process should reach candidates whose commitment, skills, life experience, background, perspective, or other characteristics will serve the organization and its needs.
- The nominating process should actively seek out and recruit board members who reflect diverse racial and ethnic backgrounds, experiences, and skills. Importantly, representation on the board should include individuals connected to and reflective of the community that the organization is serving.
- The board should regularly review qualifications for new board members, including any financial contribution expectations to ensure that they do not deter consideration of a more diverse group of candidates.
- A larger candidate pool may result if you include non-board members as well as board members on your nominating committee.
- Term limits for board members are an effective way to ensure board vitality.

If your board does not have term limits, board members should be reviewed

periodically to confirm that they remain interested in and suitable for the board and that they are still able to commit the necessary time to their role on the board. Rotation off the board, assignments to off-board committees, and designation as emeritus members are other ways to achieve a vigorous board while retaining the value long-time board members can bring to the organization.

IN SHORT:

To avoid becoming labeled as a closed club for “insiders only,” choose board members who have an interest in the organization’s mission, represent diverse viewpoints and diverse racial and ethnic backgrounds, experiences, and skills.

VI. CHOOSE AND EVALUATE YOUR ORGANIZATION'S LEADERSHIP CAREFULLY

Hiring the organization's leadership, including its CEO or ED, is one of the most important tasks you have as a board member. It is the job of the board to engage in a selection process that will allow the board to find the right person to carry out the charity's purpose efficiently and effectively, and to do so through equitable recruitment, hiring, and compensation practices that encourage a diverse pool of applicants.

THIS MEANS:

- The board should form a search committee at the beginning of the hiring process for any leadership positions, including the CEO or ED position. If the board does not create a written job description for the position prior to hiring, it should at least develop a profile of the sort of leader it believes the organization's mission and current needs require.
- The board should regularly consider whether there is representation from diverse racial and ethnic backgrounds in its leadership, including representation from individuals connected to and reflective of the community that the organization is serving.
- A majority of the search committee members should be board members, but it may be beneficial to include staff members, a diversity officer, or others knowledgeable about the organization and its mission on the committee.
- If the size of the board permits, the entire board should interview the final candidates and participate in contacting their references.
- The entire board should make the final decision to hire the CEO or ED.
- After the CEO or ED is hired, the board should periodically review and assess their performance and commitment to the organization, keeping in mind that the board has the authority to discharge as well as hire senior leadership.

IN SHORT:

Board members should actively participate in hiring the organization's leadership and should do so through equitable recruitment, hiring, and compensation practices that encourage a diverse pool of applicants.

VII. GET INVOLVED IN SETTING EXECUTIVE COMPENSATION

The board is responsible for setting the compensation of the organization's CEO and, where appropriate, other senior managers. When setting executive compensation, you should be mindful that the public, which supports the charity and uses its services, is interested in knowing the amount. This information is provided to the public on the Attorney General's Office's Form PC and the Internal Revenue Service Form 990, both of which are posted on the Attorney General's Office's filing search page at <https://www.mass.gov/service-details/search-public-charities-filings>. In addition, Forms 990 are available on the Internal Revenue Service search page at <https://apps.irs.gov/app/eos/> as well as third party sites like <https://www.guidestar.org/> and <https://www.charitynavigator.org/>

In addition, both the IRS and the Non-Profit Organizations/Public Charities Division from time to time scrutinize the reasonableness of a charity's executive compensation and the process used by the board to determine this compensation. Complaints of excessive compensation or private benefit, whether from regulators or from the public, can expose the organization and its board members to legal action and risk reputational harm.

THIS MEANS:

- Every board member should know what members of senior leadership are paid, including the value of any non-salary compensation, such as the use of an automobile, retirement funds, etc.
- Even if a compensation committee is used, the entire board remains responsible for compensation decisions and must be fully informed. In setting compensation, you should consider the performance of your CEO and senior managers and the compensation provided to other similarly situated executives in the field. If the board chooses to engage a compensation consultant to gather or review this information, it should not rely solely on the recommendations of the consultant. Board members are responsible for determining what level of compensation is

reasonable for their organization, taking into account other important factors such as the concerns of donors, the impact on the charity's mission and finances, and the organization's reputation. In evaluating the impact compensation may have on the organization's reputation, the board should take into consideration the perception of senior leadership's compensation as a whole, including any compensation that leaders receive from positions held because of, but outside of, their role at the charity (e.g., for-profit board membership compensation).

IN SHORT:

Your process for setting executive compensation, the amount of such compensation, and the terms of such compensation should all be well documented, approved by the full board, and be sensitive to public concerns and regulatory oversight.

VIII. BEWARE OF CONFLICTS OF INTEREST

As a member of the board, you may find yourself in situations in which your board service conflicts with another aspect of your personal or professional life. For example, you, a business you control or benefit from financially, a member of your family, or a close friend may be considering whether or not to engage in a transaction with the organization on whose board you are sitting. Further, you may serve on other boards and the work of those organizations may overlap or could appear to compete with one another. Although not an exhaustive list, situations such as these present a potential conflict between your own interests and your duty as a board member to be absolutely loyal to the organization and its mission. It also may look questionable to the public.

Because of these problems, a board member should be cautious about entering into a business relationship with the charity the board member is overseeing, and the charity's board should be very cautious about allowing the charity to enter into such a relationship. Such a transaction should not occur unless the board determines it is clearly in the best interest of the charity. Prior to the board vote, the board member should fully disclose their financial interest to the entire board, and the conflicted board member should not vote on any aspect of the arrangement or be present when the board is deliberating or voting on any aspect of the arrangement. Upon notice of the conflict, the entire board should consider whether the proposed transaction or relationship is clearly in the best interest of the charity, including consideration of the public perception of any such transaction and the impact that may have on the charity's reputation.

THIS MEANS:

- You should ensure that your board has a policy for dealing with conflicts of interest.
- The policy should include a procedure for the annual written disclosure by all board members, senior leaders and key decision makers in the organization of their business involvements with the charity and their other board memberships and business interests, both for-profit and charitable.

The information disclosed should be circulated to all board members and be updated throughout the year as necessary. The Attorney General's Non-Profit Organizations/Public Charities Division requires that the value and terms of these related party transactions be disclosed on the organization's annual Form PC filing.

- Your conflict-of-interest policy should address the issues raised if board members or other senior managers have or might acquire investments that may affect or be affected by the charity's investment or operational decisions. In addition, it should address other conflicts that can be reasonably foreseen, based on the organization's charitable activities. For example, a grant-making organization should consider how to address grant applications from an entity that has an employee or board member serving on the grant-making organization's board.
- In addition to the disclosure of financial interests and conflicts of interest, the policy should also include a procedure for the withdrawal from discussion and voting by the board member or senior leader with a conflict. This procedure should be followed whenever the charity enters into a business transaction with a board member or senior leader, or with an entity in which a board member or senior leader has an interest.
- It may be advisable to obtain an outside evaluation or appraisal of any major business transaction that is being proposed between the charity and a board member or leader or any entity in which a board member or leader has an interest. This evaluation is to assure that the proposal is feasible, the terms are favorable to the charity, and the potential pitfalls of such a transaction, including any potential harm to the charity's reputation, have been identified.
- The board should carefully consider the pros and cons of entering into relationships, such as management contracts, the creation of subsidiary entities (whether they are for-profits or nonprofits), and other transactions that involve inherent conflicts of interest because the board's duties of care and loyalty are being divided among several entities or delegated, even in part, to another entity.
- Because of the sensitivity of conflict-of-interest issues, you may want to require that transactions involving these issues receive a greater-than-majority vote.

IN SHORT:

Any conflicted transaction should be scrutinized very closely by the board, both because of the dynamic it creates within the board and because of the predictable skepticism with which the public and regulators will view the transaction, no matter how scrupulously a careful policy is followed.

IX. OTHER RESOURCES TO ASSIST YOU IN YOUR RESPONSIBILITIES

The Attorney General's website provides access to a number of useful publications, advisories, guidance documents, and reports produced by the Non-Profit Organizations/Public Charities Division. These may be viewed online or downloaded from <https://www.mass.gov/information-for-existing-charities>. In addition, all forms and instructions issued by the Division are also available on the website at www.mass.gov/ago/charities.

For further education and information, consider the following resources:

- IRS Educational Resources and Guidance for Exempt Organizations: <https://www.irs.gov/charities-non-profits/educational-resources-and-guidance-for-exempt-organizations>
- Board Accountability and Best Practices: <https://www.councilofnonprofits.org/tools-resources-tags/Accountability>
- Board Governance and Planning: <https://boardsource.org/>
- Diversity, Equity, and Inclusion Guidance: <https://www.councilofnonprofits.org/tools-resources-categories/diversity-equity-and-inclusion>
- Association of Governing Boards of Universities and Colleges: <https://agb.org/>
- Lawyers Clearinghouse: <https://www.lawyersclearinghouse.org/>
- Massachusetts Nonprofit Network: <http://massnonprofitnet.org/>
- Nonprofit Profiles:
 - o <https://guidestar.org/>
 - o <https://www.charitynavigator.org/>



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