

May 6, 2021

**Liability and Insurance:
For Lake Districts and
Lake Associations**

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Thursdays
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FREE WEBINAR

Minimizing Risk: Duties and Protections of Directors

Presented by Jessica Harrison

Scholz Nonprofit Law LLC

May 6, 2021

Background on Nonprofit Corporations

- What is a “nonprofit organization” under WI law?
 - Corporate entity without owners, with a common goal
 - Organized as a “nonstock corporation” under Chapter 181 or as an “unincorporated association”
 - Both 501c3 and 501c4 tax-exempt organizations are organized as nonstock corporations
- Nonstock corporation is preferable
 - Explicit limitations on liability for Directors, officers and volunteers

The Duties of a Director

Duty of Care
Duty of Loyalty
Duty of Obedience

The Duty of **CARE**

Definition:

- To act in a fully informed manner after the exercise of due diligence appropriate under the circumstances – with the care that an ordinary person would exercise under similar circumstances and in a manner that the director reasonably believes to be in the organization's best interest
- Don't sleep!

Practical steps in making decisions with due care:

- Attend meetings
- Avoid haste, and the appearance of haste, in making decisions
- Prepare adequately
- Ask questions
- Exercise independent judgment
- Record board proceedings
- Avoid giving approval w/o prior knowledge and review

The Business Judgment Rule

- **What?** A series of presumptions related to decisions made by directors
- **Why?**
 - 1) To encourage competent individuals to serve as directors by limiting liability
 - 2) To recognize business decisions involve some risk-taking
 - 3) To prevent plaintiffs/courts from inefficiently second-guessing decisions of directors

The Duty of **LOYALTY**

Definition:

- Requires that an organization's directors always act in the best interests of the organization and its constituents, and to subordinate any personal interest in matters that come before the board to that corporate interest
- Don't steal!

Conflict of Interest/ Duty to Disclose

- A director who has a material or personal interest in a matter before the nonprofit entity must disclose that fact to the board of directors. The Board may decide that there is or is not a need for the conflicted director to recuse himself or herself.
- Annual review of Conflict of Interest policy and Disclosure Statement.

The Duty of **OBEDIENCE**

Definition:

- Requires that an organization's directors comply with the applicable federal, state, and local laws, adhere to the organization's bylaws, and remain the guardians of the mission
- Don't slack!

A Director's Protection from Liability

General Rule:

- Officers, directors, paid staff and volunteers of nonprofit entities generally are protected from personal liability for the acts of the entity, as long as the actions were truly those of the entity and the proper steps were taken to maintain the corporate form and its liability shield.
- In spite of corporate shield, individuals can be held personally liable if they violate any of the three duties: care, loyalty or obedience.
- Note: even then, WI law provides specific protections from personal liability

Statutory Standard:

Wis. Stats. § 181.0855

- Members of the board of directors and officers of a nonprofit corporation are shielded from personal liability that arises from a failure to perform any duty (care, loyalty, obedience) resulting solely from their status as officers and directors **unless actions involved** include:
 - Conflict of interest
 - Violation of criminal law
 - Transaction from which director derived personal benefit
 - Willful misconduct

Indemnification

- Nonprofit corporations required by WI law to indemnify officers/directors against claims of personal liability
- Indemnification rights can be limited or expanded through corporation's documents
- Indemnification is not required if liability was incurred because individual breached or failed to perform a duty he or she owes the corporation

Insurance

- WI law permits nonprofit corporations to purchase and maintain insurance coverage to protect individuals acting as officers, directors, employees
- “D&O” Coverage
- Other types of insurance to consider:
 - Commercial General Liability (CGL)
 - Workers Compensation (required if three or more employees)

Specific Risks for Directors under Federal Tax Law

Liability for Employment Taxes

- Directors can be held liable for failure to collect, account for, and pay income and payroll taxes that have been withheld or should have been withheld.
- No penalty is imposed on unpaid, volunteer member of any board if the member:
 - Is serving in honorary capacity
 - Does not participate in day-to-day financials
 - Does not have actual knowledge of failure to comply
- Note: This exception is **narrowly interpreted**. Generally, officers & directors can be held personally liable even if they did not have a role in day-to-day financials.

Thank you!

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Thanks for joining us!

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*Upcoming
"Thurs @
4" Topics*

May 13 ~ Lake District Treasurer 1: Before the Annual Meeting

May 20 ~ Local Boating Enforcement Grants

May 17 ~ Lake Association Capacity Training

June 3 ~ Electronic Communications, Websites, and Lakekit.net

June 10 ~ Regulating Recreation on Lakes: Carrying Capacity

