Directors and Officers of
Non-Profit Corporations -
Liabilities, Rights and Insurance

John E. Black, Jr.
Boundas, Skarzynski, Walsh & Black LLC
I. INTRODUCTION – D&O CLAIM TRENDS

Although the possibility of legal action being brought against directors and officers of non-profit corporations is generally less than that of directors and officers of for-profit corporations, the frequency of litigation against directors and officers of non-profit corporations has increased remarkably in recent years. The Non-Profits’ Insurance Alliance of California, a liability pool based in Santa Cruz, California, reported that director and officer claims doubled in the last five years. See, D&O Claims Keep Climbing, Non-Profit Times, July 1, 2002.

Insurers of non-profit organizations report that the vast majority of claims made against directors and officers of non-profit corporations were employment-related, although claims involving anti-trust issues, misallocation of funds and membership disputes are also common. Officials from Chubb Specialty Insurance estimate that employee-related claims comprise 60% to mid-70% of all nonprofit claims, while an official at Philadelphia Insurance Company estimates that at least 85% of nonprofit D&O claims are employment-related. Id. Consistent with this a 2001 D&O liability survey conducted by Tillinghast-Towers Perrin, participating non-profit officials identified employment-related issues as accounting for 89% of claims made against non-profit organizations and their officials.

Detailed information about the losses arising from claims against non-profits and their directors and officers is not readily available. However, insurers have informally indicated that claim payments are increasing. One insurance group’s average loss payment increased from $22,000 in 1996 to $42,000 on claims closed between 1996 and 2001.

II. DUTIES AND RIGHTS OF DIRECTORS AND OFFICERS OF NON-PROFIT CORPORATIONS

A. Duties of Directors and Officers to the Organization

Although directors and officers of non-profit corporations historically have been referred to as “trustees” and were subjected to a fiduciary standard of care, case law and statute over the last twenty years have clarified that the standard of care applicable to directors and officers of non-profit corporations is closer to the standard applied to directors and officers of for-profit corporations. Accord, Stern v. Lucy National Training School, 381 F.Supp. 1003(D.D.C. 1974). Thus, while case law often refers to directors and officers of non-profit corporations as serving in a fiduciary capacity with respect to the corporation and its members, the fiduciary obligations imposed on directors and officers essentially fall into the two broad categories that are applicable to directors and officers of for-profit corporations - the duty of loyalty and the duty of care. See generally, American Bar Association Section of Business Law, Guidebook for Directors of Nonprofit Corporations (1993).

1. Duty of Loyalty.
a. “By assuming his office, the corporate director commits allegiance to the enterprise and acknowledges that the best interest of the corporation and its shareholders must prevail over any individual interest of his own. The basic principle to be observed is that the director shall not use his corporation position to make a personal profit or gain other personal . . . .” American Bar Association Committee on Corporate Law, The Corporate Director’s Guidebook, 33 Bus. Law. 1591, 1599-1600, (1978).

b. Directors are said to be fiduciaries of the corporation. Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985). Courts have recognized, however, that “if directors were held to the same standard as ordinary fiduciaries, the corporation could not conduct business.” Panter v. Marshall Field & Co., 646 F.2d 271, 294 (7th Cir.), cert. denied, 454 U.S. 1092 (1981).

A director may not have any personal interest in the challenged decision. A director cannot “appear on both sides of the transaction nor expect to derive any personal financial benefit from it in the sense of self-dealing, as opposed to a benefit which devolves upon the corporation or all stockholders generally.” Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984). If a plaintiff establishes that a director had such personal interest, the director must demonstrate that the transaction was to the corporation, unless the material facts of the transaction and the director’s interest were disclosed or known and property approved, authorized or ratified.

c. Examples of breach of the duty of loyalty (conflicts of interest and self-dealing):

1) Breaching confidentiality.


5) Corporation lends money to a director or a director’s affiliate.
6) Improper payments, gratuities.

2. Duty of Care.

a. “In addition to owing a duty of loyalty to the corporation, the corporate director also assumes a duty to act carefully in fulfilling the important task of monitoring and directing the activities of corporate management.” American Bar Association Committee on Corporate Laws, The Corporate Director’s Guidebook, 33 Bus. Law. 1591, 1599-1600 (1978).

b. Standard of Care

1) Some states have a statutory formulation.


3) Model Act: The Revised Model Non-Profit Corporation Act provides that a director should discharge duties in good faith, with the care an ordinarily prudent person in a like position would exercise in similar circumstances, and in a manner reasonably believed to be in the corporation’s best interests.

c. Duty of Care includes duty of attention, which requires the directors to:

1) Attend meetings.

2) Review adequate information concerning action taken by the Board.

3) Generally oversee the corporation’s business.


d. Application of the “Business Judgment Rule”

1) The Business Judgment Rule encourages and protects deliberative decisions that are:
a) informed and made on the basis of reasonable inquiry;
b) made in good faith and without a disabling conflict of interest; and
c) made on a rational basis.

2) Application of the Rule presumes that judgment has been exercised. Thus, the Rule “has no role where directors have either abdicated their functions, or absent a conscious decision failed to act.” Aronson v. Lewis, 473 A.2d at 813.


4) The Rule applies only to informed decisions; directors must inform themselves of all information reasonably available to them and relevant to their decision. Smith v. Vank Gorkom, 488 A.2d at 872-75. The proper standard for determining whether a business judgment was informed is gross negligence. Id.; see also, Treco, Inc. v. Land of Lincoln Savings and Loan, 749 F.23 374 (7th Cir. 1984); Panter v. Marshall Field & Co., 646 F2d 271 (7th Cir.) cert. denied, 454 U.S. 1092 (1982).

3. State law Statutory duties to the Organization or its creditors:

a. Organization activities: adopt bylaws, adopt corporate policies regard personnel, etc.
b. Ongoing activities: adopt budgets, select officers; review corporate personnel, etc.
c. Permissible distributions prior to dissolution.
d. Creditors of a dissolved corporation; claims can be barred with proper notice.
e. Doing business after dissolution: directors can be liable to creditors.

B. Duties of Directors and Officers to Members

The most substantial exposure faced by such directors and officers for for-profit corporations arise from the duties owed directly or indirectly to shareholders, whether the suits are brought by shareholders derivatively on behalf of the
corporation or as a class. However, due to the different structure and purpose of the nonprofit corporation, such suits are a much less significant source of exposure for directors and officers of nonprofit corporations. As discussed in greater detail below, nonprofit corporations do not have a class of persons who have an equity interest in the corporation. While some nonprofit corporations may have members with voting privileges to affect the operation of the corporation, many nonprofit corporations do not even have members. Thus, nonprofit corporations generally do not have a class of persons with a sufficiently significant financial interest in the operation of the corporation to bring a derivative or class action suit. However, where a nonprofit corporation has members, the directors and officers do have duties to the members and may be liable for breaches of those duties. The duties of a director or officer to the membership of a nonprofit corporation are, for the most part, encompassed within the general duty of loyalty and care owed to the corporation itself.

Suits against directors and officers of any corporation for violation of the duty to the shareholders (or members) of the corporation are usually brought in one of three forms. First, the corporation itself may bring suit against the director or officer. Second, several similarly situated shareholders or members may bring a class action suit for the violation of a duty owed directly to those individuals, such as a misrepresentation concerning the corporation’s performance which the shareholders relied upon. Of course, because members of nonprofit corporations often have no voting rights and fewer obligations are owed directly to the members of the nonprofit, class actions are significantly less common in the nonprofit area of corporate law. Third, shareholders or members may bring a derivative lawsuit in the name of the corporation to enforce obligations owed directly to the corporation and indirectly to the person bringing the lawsuit. Although the right to bring a derivative lawsuit is well established in the for-profit sector, the issue is newer to the area of nonprofits and arises most often in relation to religious and mutual benefit corporations, the nonprofits which are most likely to have members.

The tool of a derivative lawsuit has traditionally been denied those wishing to control nonprofit directors and officers. Instead, in the past, the full control of these managers was entrusted to the Attorney General of a given state. The general public was held not to have standing to sue nonprofit for alleged failures in fulfilling its corporate purpose or other wrongful acts regarding internal governance. Even members of the nonprofit were held not to have standing due to a lack of financial interest in the corporation. (Lack of financial interest was assumed based on the rule that profits derived from the operation of a nonprofit may not inure to the benefit of its members.) Since the members were assumed to have no financial interest, the common law reasoned they had no standing to sue the corporation. Because the interest that members of mutual benefit corporations (such as clubs and professional trade associates) have in the proper operation of the corporation is now widely recognized, many states now allow derivative suits to be brought against directors and officers of nonprofits. See Boykin, The
The Revised Model Act also allows for derivative lawsuits. However, to discourage frivolous litigation, the Revised Model Act places the following limits on the members’ right to bring a derivative action: (1) derivative actions may only be brought by members having 5% of the voting power or by 50 members, whichever is less, or any director; and (2) defense expenses, including counsel fees, may be awarded against the plaintiff if the court finds that the suit was commenced without reasonable cause.

C. Statutory Duties of Directors and Officers to Third Parties:

1. Employment-related Discrimination:

Most employment related litigation is brought under the federal statutes enacted to protect against discriminatory acts in the workplace, most significantly Title VII of the Civil Rights Act of 1964 as amended by the Civil Rights Act of 1991 (“Title VII”), the Americans with Disabilities (“ADA”), and the Age Discrimination in Employment Act (“ADEA”); coupled with the numerous individual state civil rights laws.

During the past five years, the EEOC reports that the top five most commonly filed suites are: 1) sex discrimination and harassment (30.1%); 2) retaliation (22.2%); 3) race discrimination (13.5%); 4) disability discrimination (12.8%); and 5) age discrimination (8.2%). A few of the more significant federal statutes related to workplace discrimination are discussed briefly below.

   a. Title VII of the Civil Rights Act of 1986

Title VII of the Civil Rights Act of 1964 ("Title VII") as amended by the Civil Rights Act of 1991, 42 U.S.C. §§ 2000 et seq., prohibits discrimination by private sector employers. The Civil Rights Act of 1991 broadened Title VII to allow aggrieved employees the right to a jury trial and the right to recover compensatory and punitive damages. Prior to the Civil Rights Act of 1991, successful claimants were entitled only to awards of back pay and benefits.

Title VII prohibits an "employer" from discriminating on the basis of race, color, religion, sex, or national origin in hiring, discharge, compensation, and any terms, conditions, or privileges of employment. An "employer" is defined under Title VII as any person "engaged in an industry affecting commerce who has 15 or more employees for each working day in each of 20 or more calendar weeks in the current or preceding calendar year." An “employer” can be a sole proprietor, partnership or corporation.

   b. Americans with Disabilities Act of 1990 ("ADA")
The Americans with Disabilities Act ("ADA"), 42 U.S.C. §§ 1201 et seq., forbids employers from discriminating against a "qualified individual" with a "disability" when the discrimination is based on the individual's disability. The ADA affects the application procedures, hiring, promotion, discharge, compensation, job training, and other terms, conditions, and privileges of employment. ADA claims are one of the fastest expanding categories of employment-related litigation. The EEOC reports that from 1995 to 2002, a total of 139,063 charges of discrimination under the ADA were filed. The ADA applies to employers with fifteen or more employees who are employed for the current or preceding year for twenty or more calendar weeks. As with Title VII, a debate exists among the federal circuits as to whether individual supervisors may be held individually liable under the ADA. Again, the majority rule is that there is no individual liability under the ADA.

c. The Equal Pay Act of 1963

The Equal Pay Act, 29 U.S.C. § 206(d), prohibits pay discrimination against employees because of their gender. Claims regarding hiring, firing, and promotion decisions are covered by Title VII, not the Equal Pay Act. Rather, the Equal Pay Act compels businesses to pay equal wages to employees performing substantially equal work, regardless of sex or skill of the individual employees. Pay differentials may be based upon merit, seniority, or any lawful factor other than sex.

d. Age Discrimination in Employment Act (ADEA) of 1967

The Age Discrimination in Employment Act of 1967 ("ADEA"), 29 U.S.C. §§ 621 et seq., bars employers from discriminating against employees over the age of forty on the basis of age with regard to hiring, discharge, compensation, and other terms, conditions, or privileges of employment. As with Title VII and the ADA, a majority of courts hold there is no individual liability for supervisors under the ADEA. The ADEA protects workers employed in an industry affecting commerce that has twenty or more employees for each working day for twenty or more calendar weeks in the year. Under the ADEA, employers are prohibited from (1) failing or refusing to hire, discharging, or discriminating in the compensation of an individual because of age; (2) depriving an individual of employment opportunities or otherwise adversely affecting the employee's status because of age; or (3) reducing an individual's wages to eliminate a wage discrepancy which might violate the ADEA. Employers may not retaliate against an employee for asserting rights protected by the ADEA, or publish any notice or advertisement that expresses any age preference or limitation.

Prohibits any person from conducting the affairs of any enterprise through a pattern of racketeering activity or from acquiring an enterprise through conduct constituting such activity. A “pattern of racketeering activity” is established by showing the commission of at least two enumerated predicate acts within a 10-year period. 18 U.S.C. § 1961(5). The enumerated acts include securities fraud, mail fraud, bankruptcy, obstruction of justice, embezzlement from pension, welfare, and union funds, and others. 18 U.S.C. 1961(1). An “enterprise” may be virtually any association in law or in fact, including corporate entities.” 18 U.S.C. § 1961(4). A person injured by a RICO violation may recover “three-fold the damages he sustains and the cost of the suit, including a reasonable attorneys’ fee.” 18 U.S.C. § 1964(c).

RICO claims are frequently added to traditional corporate litigation, such as anti-trust litigation, e.g., Bunker Ramo Corp. v. United Business Forms, Inc., 713 F.2d 1272 (7th Cir. 1983), and common law fraud, e.g., Schacht v. Brown, 711 F.2d 1343 (7th Cir.) (en banc), cert. denied, 104 S.Ct. 508 (1983).


Section 3(21)(A) of ERISA defines a “fiduciary” as one who has or exercises authority or control over an employee benefit plan. The board of directors of a corporation typically will have the powers, e.g., to appoint and retain administrators of a plan, to invest plan assets, to amend to terminate the plan and others. Directors and officers will be held responsible as fiduciaries to the extent that they exercise authority or control over a plan.

4. Antitrust Laws:

Directors and officers may be held liable in a treble damage action by a person injured by violations of the Sherman Act committed by the defendants within the scope of their duties. Directors and officers may also be held liable to the corporation for damages sustained as a result of any trust violations in which the directors or officers knowingly participated. In this context, however, the Business Judgment Rule is applicable. Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125 (Del. 1963).

5. Taxes:

Foundation Managers, which are defined at Section 4946(b) of the Internal Revenue Code of 1986 as directors, trustees, officers or authorized employees, or persons with similar responsibilities, may be held liable for a percent of certain taxes which may be imposed on private foundations. Among such provisions are Sections 4912(b) (concerning disqualifying
lobbying expenditures), 4941(a) (2) and (b) (2) (concerning self dealing), 4944(a) (2) and (b) (2) (concerning investments which jeopardize the charitable purpose of the foundation), 4945(a) (2) and (b) (2) (concerning taxable expenditures), and 4955(a) (2) and (b) (2) (concerning political contributions). Penalties may also be assessed pursuant to 26 U.S.C.A. § 6684.

D. Common Law Duties of Directors and Officers to Third Parties:

1. Employment-related Claims:

Increasingly, aggrieved employees seek tort remedies that fall outside the realm of contract law or statute to avoid limits on the amount of compensatory and punitive damages. Often, tort claims are combined with one or more statutory discrimination claims. Commonly asserted tort claims include defamation, intentional interference with contractual rights, and fraud and misrepresentation. Tort causes of action potentially have larger damages awards, because compensation is not merely based on the plaintiff’s salary, but rather on the extent of injury resulting from the tort (often including emotional distress damages). Additionally, in some states punitive damages can be awarded for successful tort claims.

2. General Duties to the Public

Nonprofit corporations and their agents may be sued under tort for their activities. Commonly asserted tort claims include defamation, intentional interference with contractual rights, fraud and misrepresentation and negligence. Contract claims may also be asserted against alleged parties to the contract.

E. Rights and Directors and Officers

1. Indemnification.

   a. Corporate indemnification provides protection for its directors, officer, employees, and agents against the risks of liability that their service to the corporation inevitably entails. Without such protection, it would be difficult to persuade able persons to serve as corporate directors, officer or agents with little or no compensation. This is particularly true in light of the increasing frequency of suits against directors and officers and the increasing costs of defense.

   b. On the other hand, public policy may limit indemnification. Indemnification may not be so broad as to allow directors, officers, employees or agents to use corporate funds to avoid the consequences of wrongful conduct, and arguably should not apply
to liabilities or penalties expressly imposed on directors, officers of employees by statute.

c. The goal of indemnification provisions is to balance these policy considerations and to “seek the middle ground between encouraging fiduciaries to breach their trust, and discouraging them from serving at all.” Johnston, Corporate Indemnification and Liability Insurance for Directors and Officers, 33 Bus. Law. 1993, 1994 (1978).

2. Permissive Indemnification.

a. State corporation statutes allow permissive indemnification by the organization to its agents, defining the outer limits within which a corporation may indemnify its directors, officers, employees and agents voluntarily. Even if the standards for permissive indemnification are not met, such persons may be eligible for court-ordered indemnification.

b. General Standard -

1) Such statutes typically provide that a non-profit corporation may indemnify any of its directors, officers, employees or agents made a party to a proceeding for defense expenses and liability incurred in the proceeding if:

   a) that person is named as a defendant by virtue of that person’s status as a director, officer, employee or agent of the corporation or that person’s service as the request of the corporation as a director, officer, employee or agent of another entity;

   b) that person acted in good faith and in a manner he or she reasonably believed to be in, or not opposed to the best interests of, the corporation; and

   c) in the case of any criminal proceeding, the person had no reasonable cause to believe that his or her conduct was unlawful.

2) The termination of an action by judgment, order, settlement, conviction, or plea of nolo contendere or its equivalent is not of itself determinative that the person did not meet the standard of conduct required for indemnification. Such a determination, however, would be entitled to considerable weight. See MBCA § 8.51(C), Official Comment (1984). Thus, a finding by the board of directors that the standard for indemnification had been
met, where that finding was directly contrary to a judicial finding, might be subject to challenge.

c. Actions By or In the Right of the Corporation -

1) Permissive indemnification is available only for reasonable expenses (including attorneys’ fees); it is not permitted for judgments, fines, or amounts paid in settlement to the corporation.

2) Permissive indemnification for expenses (including attorneys’ fees) is prohibited if the director, officer, employee, trustee or agent is adjudged liable to the corporation.

3) However, the court in which the corporation brought the action may determine, upon application and in view of all relevant circumstances, that the person sued is fairly and reasonably entitled to indemnity for expenses.

d. Determination and Authorization of Permissive Indemnification

1) A corporation may authorize permissive indemnification only after a determination in the specific case that indemnification is permissible because the person has met the required standard of conduct.

2) The determination that the person met the required standard of conduct shall be made:

a) by the board of directors by majority vote of a quorum consisting of directors who were not parties to the proceeding;

b) if a quorum of disinterested directors cannot be obtained, or even if it can be obtained but a quorum of disinterested directors so directs, by independent legal counsel in a written opinion; or

c) if a quorum of disinterested directors cannot be obtained, then by a majority vote of a committee duly designated by the board of directors consisting solely of two or more directors not at the time parties to the proceeding; or

d) by the members entitled to vote, if any.

3. Mandatory Indemnification.
a. A director, officer, employee or agent is entitled to mandatory indemnification against reasonable expenses incurred by him or her in defense of a proceeding (including attorneys’ fees) to the extent he or she was wholly successful on the merits or otherwise.


2) A defendant is “wholly successful” only if the entire proceeding is resolved on a basis that involves a finding of non-liability. MBCA § 8.52, Official Comment (1984). A defendant may be entitled to indemnification under this standard if he has prevailed on the basis of technical defenses not related to the merits. See, e.g., Dorman v. Humphrey, 106 N.Y.S.2d 142 (N.Y. App. Div. 1951) (statute of limitations); but see Galdi v. Berg, 359 F.Supp. 698 (D. Del. 1973) (directors not entitled to indemnification for suit which was dismissed on ground that prior suit was pending on same issue).

3) Settlements which involve no payment or assumption of liability by the person to be indemnified have been held to constitute success “on the merits or otherwise” within the meaning of the Illinois Business Corporation Act. Wisener v. Air Express International Corp., 583 F.2d 579, 583 (2d Cir. 1978) (However, court based decision on by-laws mandating broadest indemnification permissible under Illinois law); B&B Investment Club v. Kleinert’s Inc., 472 F.Supp. 787, 789-91 (E.D. Pa. 1979). It is not clear, however, whether a settlement involving payment could be considered a “wholly successful” resolution of litigation.


4. Court-ordered Indemnification.

State statutes typically permit court-ordered indemnification in actions by or in the right of the corporation where the person has been adjudged liable for negligence or misconduct in the performance of a duty to the corporation and, therefore, cannot receive permissive indemnification. The court may order indemnification in such circumstances if it finds it appropriate in view of all the circumstances.


The statute usually permits the corporation to provide broader indemnification rights than those expressly provided by statute.

III. LEGISLATION LIMITING THE LIABILITY OF DIRECTORS AND OFFICERS OF NON-PROFIT CORPORATIONS FOR BREACHES OF THEIR FIDUCIARY DUTIES

A. General Scope of State Immunity Statutes For Directors, Officers And Other Persons Serving with Non-Profit Corporations:

1. The so-called “insurance crisis” in the mid 1980s led many states to reform legislation to limit the potential liability of directors or officers and other persons serving with not-for-profit corporation. Illinois was among those states which limited the liability of uncompensated directors and officers. The key provisions of this statute, Ill.Rev.Stat. ch.32 § 108.70, are set forth below:

   a. Uncompensated directors and officers are not liable and may not be sued for, damages resulting from the exercise of judgment or discretion in connection with their duties or responsibilities, unless they acted willfully or wantonly.

   b. Directors of certain non-profit corporations (agricultural corporations, professional associations, commercial associations, industrial associations, trade associations, electrification cooperatives and telephone cooperatives) are not liable, and may not be sued, for damages resulting from the exercise of judgment or discretion in connection with their duties or responsibilities, unless (a) the directors earn over $5,000 per year in compensation; or (b) the directors acted willfully or wantonly.

   c. A volunteer is not liable, and may not be sued, for damages resulting from an act or omission in rendering services, unless that person acted willfully or wantonly.

   d. “Willful or wanton conduct” is defined as “a course of action which shows an actual or deliberate intention to cause harm or which, if not intentional, shows an utter indifference to or conscience disregard for the safety of others or the property.”
e. The limitation of the liability of the above persons does not in any way reduce the liability of the corporation.

2. Keys Areas of Remaining Liability.
   a. No compensated officers or employees are protected by the statute.
   b. No directors who receive compensation, unless they work for the not-for-profit corporations identified in paragraph 1.b. above, are protected.
   c. No directors who received more than $5,000 in compensation per year, even if they work for the non-profit corporations identified in 1.b. above, are protected.
   d. The corporation itself is not protected.
   e. All directors, officers, and volunteers who are accused of acting willfully or wantonly may still be sued.
   f. Even directors or officers who otherwise may be immunized as noted above may be liable and may incur defense fees and expenses in: (a) lawsuits which do not seek damages or (b) lawsuits for damages where the director or officer is accused of not exercising judgment or discretion, that is, where the director or officer is accused of failing to act at all.
   g. The immunity does not apply to causes of action under federal law, such as a Title VII claim of discrimination.
   h. Even where directors, officers or volunteers are entitled to immunity, they may be sued and may incur substantial defense fees and expenses in establishing that they are entitled to immunity.

B. Scope of Federal Volunteer Protection Act For Directors, Officers And Other Persons Serving with Non-Profit Corporations:

The Volunteer Protection Act of 1997 was adopted to protect volunteers from personal financial liability in cases where they have acted in good faith in carrying out official duties and functions of a nonprofit organization or governmental agency.

1. The Act defines “volunteer” as an individual, performing services for a nonprofit organization or a governmental entity, who does not receive compensation (other than reasonable reimbursement or allowance for expenses actually incurred), or any other thing of value in lieu of compensation, in excess of $500 per year. The term specifically includes...
a volunteer serving as a director, officer, or trustee of a nonprofit organization.

A “nonprofit organization” under the Act means:

* any organization which is described in section 501(c)(3) and exempt from tax under section 501(a) of the Internal Revenue Code and which does not practice any action which constitutes a hate crime (ii) and

* any not-for-profit organization which is organized and conducted for public benefit and operated primarily for charitable, civic, education, religious, welfare, or health purposes, and which does not practice any action which constitutes a hate crime (iii).

2. The Act provides that a volunteer of a nonprofit organization shall not be liable of the organization if:

* the volunteer was acting within the scope of his or her responsibilities in the nonprofit organization at the time of the act or omission

* if appropriate or required, the volunteer was properly licensed, certified, or authorized by the appropriate authorities for the activities or practice in the State in which the harm occurred

* the harm was not caused by willful or criminal misconduct, gross negligence, reckless misconduct, or a conscious, flagrant indifference to the rights or safety of the individual harmed by the volunteer and

* the harm was not caused by the volunteer operating a motor vehicle, vessel, aircraft, or other vehicle for which the State requires the operator or the owner of the vehicle, craft, or vessel to possess an operator’s license or maintain insurance.

3. Assuming the volunteer was acting within the scope of his or her responsibility, a volunteer’s liability is limited to the amount of such loss allocated to him or her in direct proportion to the percentage of responsibility for the harm to the claimant allocated to the defendant volunteer by the court.

4. The Act also states that punitive damages may not be awarded against a volunteer in an action brought for harm based on his or her acts within the scope of the volunteer’s responsibilities to a nonprofit organization unless the claimant establishes by clear and convincing evidence that the harm was proximately caused by an action of such volunteer which constitutes
willful or criminal misconduct, or a conscious, flagrant indifference to the rights or safety of the individual harmed.

5. Key Areas of Remaining Liability.

a. The limitations on volunteer liability do not apply to any misconduct that:

* constitutes a crime of violence or act of international terrorism for which he or she has been convicted in any court

* constitutes a hate crime

* involves a sexual offense, as defined by applicable State law, for which the defendant volunteer has been convicted in any court

* involves misconduct for which he or she has been found to have violated a Federal or State civil rights law, or

* occurred in conjunction with the defendant volunteer being under the influence (as determined pursuant to applicable State law) of intoxicating alcohol or any drug at the time.

b. No directors, officers or employees compensated above $500 per year are protected under the Act.

c. The corporation is not protected under the Act.

d. Even where directors, officers or volunteers are entitled to immunity, they may be sued and may incur substantial defense fees and expenses in establishing that they are entitled to immunity.

IV. LIABILITY INSURANCE FOR DIRECTORS AND OFFICERS OF NON-PROFIT CORPORATIONS

Director and Officer (“D&O”) liability policies issued to non-profit corporations provide coverage for a variety of risks that typically befall the directors and officers as a result of their status as directors and officers or of acts or omissions in their capacity as directors and officers. Policies typically offer coverage for employees, volunteers and the corporation itself.

Generally, non-profit D&O policies afford claims-made coverage and insure defense costs on a duty-to-defend basis. The scope of standard D&O coverage is discussed below.

A. “Claims-Made” Coverage.
1. Definition of “Claim”.

Generally, a “claim” must at least be a demand for relief. See, Bensalem Township v. Western World Insurance Company, 609 F.Supp. 1343 (D.C.Pa. 1985) (EEOC Charge not containing a demand was not a claim). Most policies, however, define a “claim” as a written demand or a legal or administrative proceeding.

2. Extended Coverage.

D&O policies typically provide that coverage for an extended period of time, but only for claims based upon prior “wrongful acts”, may be purchased if the insurer cancels or refuses to renew the policy. Many policies provide that a change in renewal terms does not constitute constructive refusal to renew.


Most policies require notice of claims within 30-60 days or “as soon as practicable”. Whether notice was provides “as soon as practicable” is determined under applicable state law. Some states require that the insurer demonstrate prejudice as a result of late notice for the insurer to avoid coverage, see Reliance Insurance Co. v. St. Paul Insurance Companies, 239 N.W.2d 922 (Minn. 1976).

B. Defense Expenses - Duty to Indemnify vs. Duty to Indemnify

1. Duty to Defend

In recent years, most D&O policies have been written on a “duty to defend” basis. Win most states, if the insurer has the duty to defend any aspect of a case, the insurer is obligated to provide a defense for the entire lawsuit. However, case law recognizes that where loss can be readily apportioned between covered and uncovered claims, the insurer is not obligated for that portion of the defense attributable to the uncovered claim. See Sentex Systems v. Hartford Accident & Indemnity Company, 882 F. Supp. 930 (C.D. Cal. 1995), aff’d, 93 F.3d 578 (9th Cir. 1996). Whether defense costs are part of or in addition to the limit of liability of the policy is usually addressed in the policy.

2. Duty to Indemnify

Policies written on an “indemnity” basis provide that the carrier is not obligated to undertake the defense of the case, but is merely obligated to indemnify the insured for defense expenses incurred in the litigation. Usually, the policy will require the insurer’s consent to the insured’s incurrence of defense fees and expenses. Whether the insurer has the
obligation to pay legal fees and expenses as incurred typically is provided in the policy.

C. Limitations on Coverage.

1. Exclusions. Most D&O policies exclude claims:
   a. based upon the directors or officers gaining in fact any personal profit or advantage;
   b. brought about or contributed to in fact by fraud, dishonesty or the criminal act of any directors or officer (however, many policies provide that the insured is to be defended as to any such claims unless a judgment or other final adjudication adverse to the insured established that acts of active or deliberate dishonesty, fraud or criminal act committed by the insured were material to the cause of action);
   c. arising out of pollution;
   d. arising out of or in any way involving ERISA or any employee benefit plan of the insured;
   e. for bodily injury, sickness, mental anguish, disease or death of any person;
   f. arising out of or in any way involving damage to or destruction of tangible property including loss of use thereof;
   g. for false arrest, invasion of privacy, assault or battery;
   h. arising out of or in any way involving libel, slander, defamation or wrongful eviction;
   i. to the extent coverage is provided under other policy;
   j. which were the subject of notice to prior insurer or
   k. based upon the service of directors or officers as directors, officers of employees of any other entity, regardless of whether such service is at the request and director of the corporation.

2. Limitation on Reimbursable “Loss”. Many D&O policies except from the definition of reimbursable “Loss” any punitive damages, taxes, fines or penalties imposed by law, the trebled portion of trebled damages, or matters uninsurable as a matter of applicable law.