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Fiduciary Duties Script

FIDUCIARY DUTIES

<Intro Screen – CTU / NHDOJ>

Fade to: <Intro Screen “Fiduciary Duties”>

< Fade in on Nina and David sitting at the desk>

Nina: Hi, and welcome back to our final installment. I’m Nina

< Sub graphic for Nina: Nina, sub “Summer Intern”>

David: And I’m David.

< Sub graphic for David: David, sub “Summer Intern”>

Nina: Today we’re talking about Fiduciary Duties.

David: That’s right.

Nina: Ok, David, before we go any further, I know a lot of people want to know the answer to this question: What are fiduciary duties and who has them?

David: Ok. Fiduciary duties enter the world of trust law from corporate law. Corporations created a position, called a director to act as an intermediary between managers and the owners of a corporation. The directors represent the interest of the

owners by overseeing the managers. Those directors have a fiduciary duty to the shareholders. That was the basis of the Board of Directors.

Nina: So that's directors, but what about trustees?

David: Well, if an organization was created by a trust, then the people who manage the trust are known as trustees. If it is a charitable corporation, then it is a board of directors.

Both fulfill the same governance role towards the organization.

Nina: So there's little difference between a trustee and a director – they both have fiduciary duties.

David: Right.

Nina: But, if the directors of a regular corporation owe their duties to shareholders, who do the directors of a charitable corporation owe their duties to?

David: They owe their duties to the recipients of their services. In general, that is going to be some portion of the public.

Nina: Now, if a director of a regular corporation is not fulfilling their fiduciary duties, shareholders can vote them out. How does that happen in a charitable organization?

David: It is the Attorney General's office that brings actions on behalf of the public in a court of law to enforce fiduciary duties and to protect charitable assets. The only direct power the public has is where they put their donations.

Nina: So, the board of directors or trustees is the group that has fiduciary duties, which come from corporate law, and they owe them to the public. Ok, let's get into the details.

What are the fiduciary duties of the board?

David: There are two main duties; the duty of care, and the duty of loyalty.

Nina (counting on fingers): Care and loyalty. Ok, so, what's the duty of care?

David: The duty of care is actually the easiest of the duties to satisfy. The test the courts use is that of an ordinary and prudent man.

Nina: What does that mean?

David: The court is simply asking if the act is something that an ordinary person would do. In practice this basically means to act rationally. It's not that the decision came out right, just that it was not irrational, and the board acted prudently in making its decision.

Nina: What would an example of breaching the duty of care be?

David: Signing blank checks, for example. Or hiring someone to manage investments for your organization, who has a criminal record of defrauding investors. Things a board would be irresponsible to do.

Nina: So duty of care is just the really extreme violations. What if you bought stock from a company right before a collapse? Is that a breach of the duty of care?

David: Courts generally don't want to second-guess business decisions. The test a court will use is basically whether you acted rationally. The key thing to satisfying the duty of care is process. The board's actions should be deliberate and follow a process.

Nina: Ok, so that's the duty of care. What's the duty of loyalty?

David: The duty of loyalty has more everyday implications for a board of directors. It that a fiduciary must put the corporations' interests ahead of their own.

Nina: That sounds straightforward.

David: Well, in New Hampshire, the duty of loyalty is really seen in the area of conflicts of interest. That's a situation where a fiduciary's interest is not aligned with the corporation's interest. In New Hampshire, the laws on conflicts of interest are outlined in the statute.

<Insert RSA 7:19A, the COI statute>

David: (Voiceover) As you can see, the statute is very detailed. It spends a lot of time defining terms like fiduciary, benefit, and organization. If you are not sure whether or not it applies to you, either contact a lawyer or the Director of Charitable Trusts.

<Back in on team>

Nina: So what all does that entail?

David: We'll get to that statute in a minute. First, however, there are two other major New Hampshire statutes people should know about for conflicts of interest.

<Fade to RSA 7:19a5>

The first is that there can never be loans from the organization to anyone with a fiduciary duty to the organization.

<RSA 7:XXXX>

The other is that each organization must adopt an annual conflict of interest policy.

< Back in on team>

David: Those statutes are pretty straightforward, but the first one is has a lot of details.

For today, we'll just assume you're a director of a standard charitable corporation.

Nina: So what does it mean for what I can and can't do?

David: The statute in New Hampshire is actually unique. It breaks Conflicts of interest down into three levels of business, totaled over the year. The first level is under \$500, the second is between \$500 and \$5000, and the third is over \$5000.

Nina: And that is totaled, over the year. What if the person had two different businesses, like a shirt company and a restaurant?

David: It doesn't matter. The statute simply asks for the total number of dollars between the person who has a fiduciary duty and the organization.

Nina: Ok, so, less than \$500, between \$500 and \$5000, and over \$5000. What does the law state about the first one, under \$500?

David: This one's easy. If the total of the financial benefit of the director over the year is under \$500, the law says there is no conflict of interest. You don't have to do anything. The only thing is to keep track of it, and make sure it doesn't go over \$500.

Nina: So under \$500, nothing. What if it goes over \$500?

David: Well, if the organization does between \$500 and \$5000 of business with someone with a fiduciary duty, then it becomes more complicated. The court says now there is a conflict of interest, and three things must happen.

<Fade out to listing of the three requirements>

David, voiceover: The first thing is that there must be full disclosure of material facts of the transaction to the governing board and the Director of Charitable Trusts at the Attorney General's Office. Second, the person with the conflict of interest cannot participate in the discussions, and must recuse himself from the vote. Third, the board must record in the minutes why it chose the action it did.

<Back in on team>

Nina: Recuse?

David: It just means that they can not vote on that particular issue. The final thing is that the transaction has to be approved by a 2/3 vote of the remaining members.

Nina: So that's really four things.

David: If you want to look at it that way.

Nina: That level sounds fairly strict. What's the over \$5000 requirement that's even tougher than that?

David: The last conflict of interest area is when the annual business is over \$5000 with the particular person.

Nina: So if over five thousand dollars, what's the difference?

<Fade to listing of the functions>

David: If the person does more than \$5000 in business in a year with the organization, then everything in the \$500 to \$5000 level applies, but there is one additional requirement that the organization publish a legal notice in the local newspaper.

<Back in on team>

Nina: Ok, just so I remember all of this. (fingers counting) If the business does more than \$5000 with a person, then (one finger) they have to disclose to the board and the AG's office, (two fingers) the person has to recuse himself, (three fingers) the board must record in the minutes why they made the decision, (four fingers) they have to publish in a local newspaper, (five fingers) and it has to go through with a two-thirds vote.

David: That's everything.

Nina: How about if we walk through an example?

David: Sure thing Nina. Say we have a little league team that needs a sponsor, so they go to Joe who owns Joe's Sporting Goods.

Nina (smiling): Good old Joe.

David: So Joe agrees to be a sponsor, if he is made a member of the board. They happily put him on the board. Now the team needs shirts. Joe offers to sell them 25 shirts for \$15 dollars each, the standard price.

Nina: How much is that?

David: It's only \$375.

Nina: So under \$500.

David: Exactly. So Joe can sell them the shirts without a problem. The team doesn't have to disclose anything, and Joe doesn't have to recuse himself. Moving on in time, though, a few games later, the team is having a stellar year, so the board wants to buy the kids hats for \$10 each.

Nina: And they go back to Joe.

David: They would, but since that is \$250 in hats, and with the \$375 earlier, this would be \$625 in total business with Joe for the year. So the board has two options: they can get hats from someone else, or they can comply with the conflict of interest laws.

Nina: We'll assume they go with Joe.

David (smiling): It wouldn't be much of an example if they didn't. So, now that total annual business is over \$500 with Joe, they must comply with the law. The transaction must be disclosed to the board and the attorney general, Joe can't be part of the talks on who to buy the hats from, and he definitely can't vote on the issue. Plus, since the total for the year is going to be over \$500, Joe also has to disclose the shirt sale when they report all conflict of interest transactions to the AG's office.

Nina: So the law requires they disclose the sale of the shirts, too.

David: Exactly. With me so far?

Nina: I think so.

David: Ok. So, finally, the team has a great season, and makes it to the Little League World Series. Donations come in, and the board wants to get the kids matching uniforms. They are going to cost \$200 each – shoes, gloves, the works.

Nina: Back to Joe's!

David: So now, this transaction will be \$5000 alone, plus the earlier sales, puts them over \$5000 for the year. Under the Conflict of Interest laws, Joe still can't vote, the board has to disclose everything dealing with Joe's and Joe, the board has to record in the minutes why they're making the decision, and now, they must also publish a legal notice in a paper that they're doing more than \$5000 in business with Joe and Joe's Sporting Goods.

Nina: And that's it.

David: That's it.

Nina: Anything else about conflicts of interest our watchers should know?

David: Just remember that there can not be any loans to officers or directors, the organization has to adopt an annual conflict of interest policy, keep track of the dollar business amounts and comply with the law.

Nina: Well, that sounds like a lot of things for the board to keep track of. Thanks for going into all that detail David.

David: Thanks for listening.

Nina: And that about wraps it up here at the Charitable Trusts Unit. Thanks for
watching.

<Closing Credits>