



soundwaves

NAVIGATING THE FUTURE

Information and Risk Management Ideas for Not-for-Profit Organizations

What's Up in 2006?

Not-For-Profits Face Familiar Issues and New Rules

Welcome to the new year. As we kick off 2006, *Soundwaves* wants to provide an overview of the landscape for not-for-profit organizations. We know you have lots of people and papers competing for your attention, so we will focus on two critical issues that can help you and your organization manage your affairs and mitigate your risks in the coming months.

Business Judgment Rule

The first issue is the business judgment rule, which acknowledges the right of board members to make sound business decisions on behalf of your organization. If a court decides that the business judgment rule applies, it is saying, in essence, that your directors have acted on an informed basis, in good faith, and in the honest belief that the action they took was in the best interests of your organization. Once that happens, it's up to a plaintiff in a lawsuit to challenge the court's decision and establish facts to rebut the business judgment presumption.

"Various court decisions have honed the scope and application of the business judgment rule," says Ben Fleischer, a partner in the New York/New Jersey law firm of White, Fleischer & Fino. "Directors who want to invoke the rule's protection have a duty to inform themselves, prior to making a business decision, of all material information reasonably available to them. Once informed, they must then act with requisite care in the discharge of their duties." He added that, if board members do not, then they can be held in gross negligence.

In New York, the state's Supreme Court has found that the decisions made by directors can be reviewed if a board acts:

- Outside the scope of its authority;
- In a way that does not legitimately further the corporate or business purpose; or
- In bad faith. Other states have applied the business judgment rule in similar ways.

The New York case that spelled out this standard, *40 West 67th Street v. Pullman*, addressed whether a cooperative association's board of directors had the right to terminate a shareholder-tenant's lease as a result of the person's objectionable conduct. In that case, the court found that the plaintiff had agreed

to submit to the board's authority. As a result, the court wrote that the board may "significantly restrict the bundle of rights a property owner normally enjoys."

A second case dealing with homeowners' associations defines the limits of board authority under the business judgment rule. In a ruling issued November 3, 2005, a New Jersey court found that, before directors can take shelter behind the business judgment rule, they must have the authority to act on a given issue. In *Micheve v. Windham Place*, the court noted, "to determine whether a condominium association has properly exercised its managerial powers under the business judgment rule, the court must consider

1. Whether the association's actions were authorized by statute or by its own bylaws or master deed, and
2. Whether the action was fraudulent, self-dealing, or unconscionable."

The New Jersey court ultimately concluded that the board did not have the authority to take the action it did—in this case imposing a special assessment—and thus the business judgment rule was not applicable. "In other words," explains Fleischer, "the business judgment rule can help protect your board, but you have to be making a decision you have the authority to make in the first place."

Communicating with Donors and Other Stakeholders

The business judgment rule isn't new, but it remains a critical risk management tool for not-for-profits. In an age when donors and other stakeholders are increasingly demanding both accountability and transparency, this rule also provides a road map for savvy decision-making.

Turning to a completely different topic, rules governing the transmission of faxes and e-mails are forcing both companies and not-for-profits to rethink the way they reach out to donors and other key constituencies. While telemarketers mostly use broadcast faxes, e-mail communications play a major role in how not-for-profits communicate with their members.

The Controlling the Assault of Non-Solicited Pornography and Marketing Act of 2003, better known as CAN-SPAM, imposes new requirements on commercial e-mail. Commercial e-mail is defined as messages that are sent primarily for the purpose of advertising or promoting a product or service. Congress and federal regulators specifically declined to make any exemptions for not-for-profits.

CAN-SPAM

"An e-mail from an association to its membership advertising an upcoming seminar where a fee would be charged may be classified as commercial because the e-mail is intended to sell the seminar," says Fleischer. "On the other hand, an e-mail to your membership containing an industry newsletter may not be classified as commercial if the newsletter is solely informational in purpose."

CAN-SPAM subjects commercial e-mails to four key requirements:

- The e-mail must provide accurate header information, including the source, destination, and routing information, together with accurate originating domain name and e-mail address in the "from" line.
- The e-mail must prominently disclose the fact that it contains an advertisement or solicitation.
- The e-mail must provide an opt-out mechanism so that the recipient can refuse future commercial e-mail

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solicitations from the sender. Recipients should be able to either reply to the message or access an unsubscribe page to take their name off the list.

- All commercial e-mail must include the sender's valid mailing address.

The good news for not-for-profits is the law does include an exemption for "transactional or relationship" messages. This means, for example, that a nonprofit can send an e-mail to thank a donor for his or her gift. It also means that you can send e-mails confirming payment of membership dues or confirming registration in a seminar or conference.

Junk Fax Prevention Act

The Junk Fax Prevention Act, enacted in 2005, is the latest effort by Congress to rein in unsolicited advertising. While the target of the law isn't trade associations and other not-for-profits, all organizations need to understand its scope and how to comply.

The law defines a junk fax as "any material advertising the commercial availability or quality of any property, goods, or services which is transmitted to any person without that person's prior express invitation or permission, in writing or otherwise."

The e-mail must provide an **opt-out mechanism.....**so that the recipient can refuse future commercial e-mail solicitations

Under the law, organizations are required to first obtain express permission from anyone with whom it does not maintain an established business relationship before sending a commercial fax. "If there is an established relationship, the organization may send commercial faxes," explains Fleischner. "The first page of the fax, however, must conspicuously display an opt-out notice so that the recipient can request that he or she not receive any further unsolicited faxes."

In order to be in compliance with the Junk Fax Prevention Act, the opt-out message must:

- Be conspicuously printed on the first page of the fax;
- Contain the sender's telephone and fax numbers so the recipient can transmit any opt-out notice request to the sender;
- Contain a "cost-free mechanism,"

such as a toll-free phone number, that the recipient can use to send his or her opt-out message; and

- Permit the recipient to opt-out any time.

Unlike CAN-SPAM, which does not allow individuals to sue organizations, the Junk Fax Prevention Act allows anyone who has illegally received a junk fax to sue and recover up to \$500 in damages per violation. If a court finds that the sender willingly or knowingly violated the law, the court has the discretion to increase the damages awarded to \$1,500 per violation. In other words, know to whom your fax is going before you punch in those numbers.

Soundwaves thanks Ben Fleischner, senior partner in the New York/New Jersey law firm of White, Fleischner & Fino, LLP, for his assistance. White, Fleischner & Fino is a leading insurance and litigation law firm: 140 Broadway, 36th floor, New York, NY 10005; tel.: 212-487-9700; e-mail: baf@wff-law.com.

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