

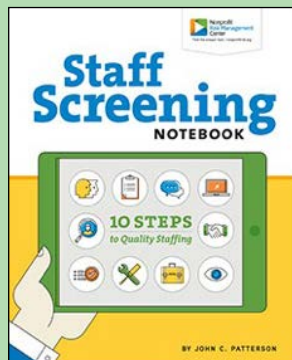
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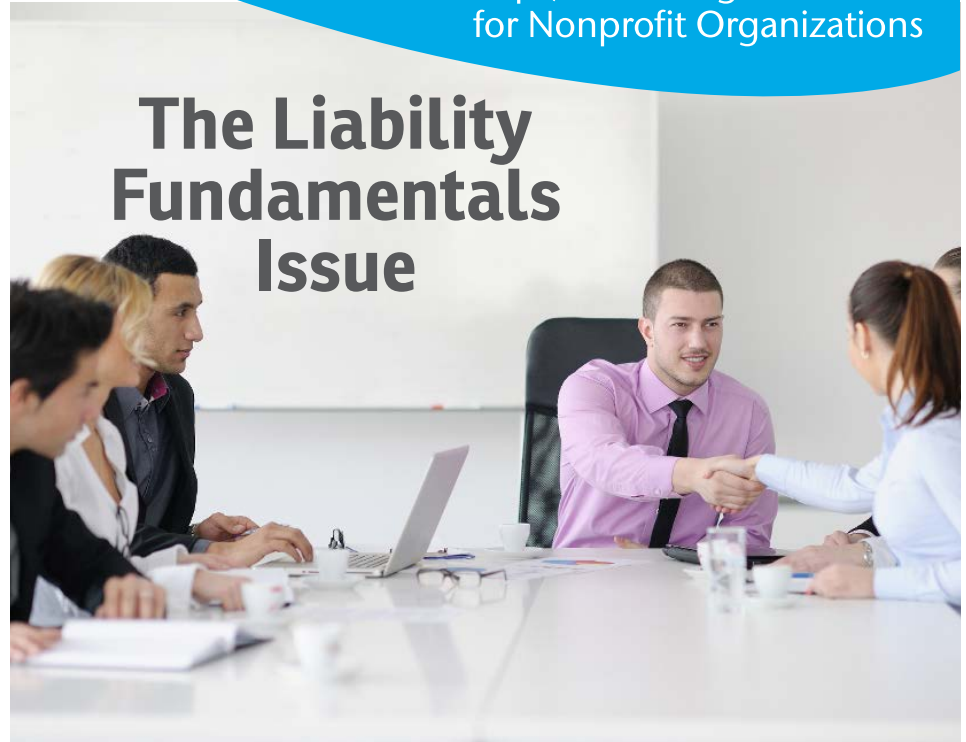


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The Liability Fundamentals Issue

Liability and the Board: What Governing Teams Need to Know

By *Melanie Lockwood Herman*

With more than 1.5 million registered, tax-exempt organizations in the U.S., it's likely that many times that number of Americans currently serve on nonprofit boards. Board service involves a commitment of time, attention, enthusiasm, and in many cases, a personal financial contribution. When you serve on a board you're likely to make new friends and professional connections, and gain an insider's view of the organization's programs and

services. With so many positive aspects of board service, what are the downside risks?

Some of the downside risks of volunteer board service include:

- Discomfort from unmanaged conflict between members of the board or between the board and CEO
- Stress from the knowledge that available financial resources are

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insufficient to support the mission, programs, staffing and obligations of the nonprofit

- Anxiety in the wake of legal claims alleging negligence, defamation, or breach of contract
- The risk of personal liability for your acts or omissions as a board member

The risk of unmanaged conflict should be addressed without delay. Techniques to reduce the likelihood of conflict include conducting an annual, thorough board orientation; resolving to keep the communications channels open between the board and CEO; and choosing how the governing team will deal with conflict before it occurs. For example, one technique is to designate a leader, such as the Board Development Committee Chair, as the point person for addressing occasional bad board behavior. Another technique is to adopt a code of conduct describing the board's aspirations for the way it will work. For example, the code might indicate that board members should never agree how they will vote on an issue prior to a board meeting. Doing so compromises the ability of the board to hear all sides of an issue and collaboratively reach the best possible decision.

The risk of inadequate financing for the nonprofit's mission can be managed by thoughtful deliberations about potential sources of funding, proposed strategies for exploiting those opportunities, and hard decisions about what programs and activities should be continued, bolstered, or shuttered.

This article focuses on the final two risks: legal claims against the board for which the organization is responsible, and the risk of personal liability facing individual board members.

Plaintiffs and Causes of Action in Cases Brought Against the Board

Nonprofit governing teams make countless decisions throughout the fiscal year, from deciding how to allocate financial resources, to determining which programs must be cut to make way for new initiatives. These decisions potentially affect—in positive as well as negative ways—a wide array of stakeholders, from clients and service recipients, to members, neighbors, and vendors, as well as individual and institutional donors. Each of these stakeholders is a potentially aggrieved plaintiff in a lawsuit alleging wrongful decisions by the board. For example:

- Neighbors of a nonprofit bring a lawsuit to halt construction of an addition to the nonprofit's headquarters building, alleging that the addition is too close to the property line.
- The parents of a child who was denied admission to a private school allege discriminatory admissions practices in violation of the law.
- Members of an amateur athletic organization sue the board of a nonprofit after the organization issues new rules governing its competitions.
- A wealthy donor sues the board of the surviving nonprofit after the merger of two organizations. The donor's suit alleges that the merger led to the cancellation of the specific project for which the donor contributed funds.

In each of these cases a court will first determine whether the individual or group bringing the lawsuit has standing to sue in the court where the case has been filed. Standing refers to a legal standard requiring that the

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plaintiff in litigation has a sufficient connection to the actions that are the focus of the suit, such as alleged violations of law, tort damages or the consequences of a contract breach. In most cases this means that the plaintiff has suffered harm directly attributable to the alleged action or inaction of the nonprofit (the defendant). In many cases brought against nonprofits and nonprofit boards, the plaintiff will be deemed to have standing to sue. The next issue for consideration is whether the nonprofit is responsible for the plaintiff's harm or loss.

When is a Nonprofit Liable for the Decisions of the Board?

Whether a nonprofit is liable for harm connected to the decisions of a board depends on a number of considerations. These include: whether a duty was owed by the nonprofit to the plaintiff, whether that duty was breached, and whether members of the board acted in good faith and with ordinary diligence.

For example, the board owes the institutional and individual donors of the organization a duty to ensure that donated funds are spent in accordance with the wishes of a donor. To adequately discharge that duty the board may approve a gift acceptance policy; delegate

to the CEO (and her team) responsibility for tracking pledges and grant-supported expenses; and review and accept the budget of the entity, quarterly financial statements and the annual tax filings of the organization. This level of care and due diligence makes it likely that the organization, and not its individual board members, will be held responsible if a court of law finds that the organization breached its duty to the plaintiff.

With rare exceptions, members of a nonprofit board are protected against personal liability due to the following:

- An incorporated entity is responsible for its debts. In the vast majority of circumstances, judgments imposed on a nonprofit by a court of law have to be paid by the organization, not individual directors.
- The bylaws of most nonprofits contain a promise to indemnify board members to the full extent permitted under the relevant state's nonprofit corporation law, for any statement, vote, decision or failure to act because of their role as a director or officer of the organization.
- Nonprofits that purchase general liability ("GL" coverage), professional liability ("PL" coverage), and

Whether a nonprofit is liable for harm connected to the decisions of a board depends on a number of considerations. These include: whether a duty was owed by the nonprofit to the plaintiff, whether that duty was breached, and whether members of the board acted in good faith and with ordinary diligence.

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... board members who act in good faith and with diligence and care, are unlikely to be held personally responsible for their actions on the nonprofit's behalf.

directors' and officers' liability insurance ("D&O" coverage) have taken an extra step to finance the cost of the promise to indemnify members of the board. Each of these policies responds to different types of claims—all of which could be filed against the nonprofit, its board, or both. General liability coverage responds to claims alleging bodily injury and property damage. Professional liability coverage responds to claims alleging negligence in the delivery of professional services. D&O policies respond to claims alleging wrongful management decisions. In some cases defense costs are in addition to the limit of liability, while in other policies funds spent on legal defense reduce the limit available for judgments and settlements.

- Board members who act with good faith and exercise due care are shielded from personal liability for the decisions they make while serving on a board.
- Every state in the United States has a volunteer protection statute that limits in some respect the personal, legal liability of volunteers. Some state volunteer protection laws only protect directors and officers serving nonprofits, while others protect even narrower categories of volunteers, such as firefighters or other emergency service personnel. The federal Volunteer Protection Act of 1997 is similar in some respects to the state laws, but sometimes offers more robust protection. In states where the VPA offers greater protection than the state law, volunteers in that state enjoy the broader protection of the federal law. One

legislative purpose of the VPA was to shift responsibility for harm caused by volunteers away from volunteers and over to the nonprofit organizations they serve.

Personal Liability

The risk of personal criminal or civil liability on the part of individual nonprofit board members is small but difficult to quantify. It is important to note that exercising poor judgment, relying on an expert whose advice is later determined to be faulty, or making a decision based on incomplete information rarely lead to personal liability on the part of individual board members. This means that board members who act in good faith and with diligence and care, are unlikely to be held personally responsible for their actions on the nonprofit's behalf. However, there are a number of specific situations that create or increase the exposure to personal liability, such as:

- Actions and activity that intentionally cause injury, harm or damage to persons or property
- Personal participation in the tortious conduct of a nonprofit's employees (tortious conduct is conduct that subjects the actor to civil liability under the law)
- The knowing approval of criminal acts or active involvement in criminal activities by the organization
- Personal involvement in a contract involving the nonprofit that is tainted by fraud
- Active participation in a transaction approved by the board with an entity in which the board member had a substantial personal or financial interest.

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Risk Tips for Board Liability

Follow the tips below to manage the risk of board liability and reduce the exposure of board members to legal claims and judgments:

1. Provide an annual board

orientation to which new and returning board members are invited. The orientation should address the legal duties of the board, the expectations of all board members, the structure of the organization and its governance function, current board policies and governing documents, and the oversight role of the board with respect to fiscal health, risk, and employment matters.

2. **Provide regular communications to the board to keep the governing body apprised of programmatic developments, major contractual relationships, staffing changes, stakeholder concerns, threatened or ongoing claims and litigation, and fundraising trends and forecasts.** A board kept in the dark is of little use to the management team or the mission of a nonprofit. And when trouble surfaces, an informed board is a valuable partner. A misinformed or neglected board will be unable to provide needed support during a crisis, nor will it be able to boost and sustain the confidence of external stakeholders. And in a worst case scenario an uninformed board

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Don't be Exposed: Put Legal Fears to Rest

If you have ever been intimidated by an onerous contract, have woken up in a cold sweat after a nightmare involving lawyers, or you're simply determined to better understand the legal risks facing the nonprofit you serve, the cure you've been craving is finally available. The brand-new edition of *Exposed: A Legal Field Guide for Nonprofit Executives* offers a tour of the maze-like world of legal liability custom-fit for nonprofit leaders. The principal authors of *Exposed* are two lawyers with decades of experience advising secular and religious nonprofits.

With support from a savvy research and writing team, Melanie Herman and Mark Chopko present an updated version of their book written specifically for non-lawyer nonprofit executives, managers and board members. *Exposed* walks the reader through important legal terms and concepts, and offers practical strategies for managing risk in the increasingly complex world of nonprofit governance and service delivery.

In addition to updated content and fresh advice from start to finish, the second edition of *Exposed* features three brand new chapters covering information technology risks, nonprofit mergers and acquisitions, and risk considerations for nonprofits starting offices and operations overseas. This practical primer will help you overcome the feeling of being exposed to legal liability while providing a jolt of confidence and a do-able list of proactive risk strategies.

- could take action that makes the crisis worse, rather than better.
3. **Keep the board apprised about the steps the organization has taken to protect the nonprofit and its governing team, including the promise of indemnification found in the bylaws and details surrounding the nonprofit's directors' and officers' liability insurance ("D&O") and other liability coverages.** Include the Bylaws and D&O policy wording in material provided to the board as part of its annual orientation and make sure that these and other background items are readily available year-round.
 4. **Hold each and every board member accountable for their commitments, from the beginning of their term of service until the end.** Accountable simply means doing what you have agreed to do. To make accountability a reality, consider designating a member of the board, such as the board chair or the chair of the Board Development Committee, to follow up with board members who fall short of their commitments, such as missing more than an acceptable number of meetings, failing to submit reports for the committees they lead, etc. For more information on holding the board accountable, see: "Enforcing Board Member Responsibilities" at www.nonprofitrisk.org.
 5. **Help the board understand its responsibility to disclose actual and potential conflicts of interest through a thoughtful, annual process.** Explain to the board that conflicts of interest may be inevitable and are not necessarily a bad thing. For example, nonprofits that have two board members who have a family or business relationship must disclose these reportable relationships on the

IRS Form 990, yet whether a conflict of interest exists depends on the circumstances before the board. The key questions are:

- ❑ *Do any board members have potential or actual conflicts of interests?*
- ❑ *If yes, is the conflict of the type that must be reported on the IRS Form 990 or only disclosed in the annual conflict of interest disclosure process?* Family and business relationships must be disclosed on the Form 990, while it is not necessary to disclose to the IRS that a board member serves on the staff of a philanthropic foundation from which the nonprofit receives or intends to solicit funds.
- ❑ *Where conflicts are disclosed, what process will the board use to address the conflict if it becomes necessary to do so?* For example, a board member owns a piece of property that the nonprofit seeks to buy. The conflict should be disclosed to the full board prior to the board's discussion about the purchase and the board should decide, possibly after hearing the recommendation of the executive committee, whether to excuse the member from the discussion and the vote about the purchase, or only from the vote.

Risk Tips for Personal Liability

If it not unusual for some members of a nonprofit board to express concern about the risk of personal liability arising from their volunteer service on the governing body. And although the risk of personal liability being imposed on volunteers is low, there are steps every board member can take to reduce the risk from low to negligible. To minimize exposure

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to personal liability, every current and prospective board member should:

1. **Serve for the right purpose:** Never agree to serve on a nonprofit board as a personal favor to a friend. The sense of satisfaction that service offers comes with a price tag. The cost of service includes the willingness to put personal interests aside while voting on issues before the board, as well as an investment of personal time and other resources to support the mission of the nonprofit.
2. **Pause before accepting a leadership role:** Give careful thought prior to volunteering to serve as an officer or Committee Chair, recognizing that these important roles require additional time and focus in support of the organization's mission.
3. **Come to board and committee meetings fully prepared to share your questions and perspective:** Carefully review background material provided in advance of board meetings and prepare thoughtful questions for which you seek additional information or clarification. Remember that the legal duty of care applicable to every member of the board requires the care and concern of an ordinarily prudent person. Ask: Would I be comfortable making this decision if it required the expenditure or commitment of personal funds? What additional information do I need to feel confident the board is making the best possible decision at this time?
4. **Vote "yes" only when you're confident it's the right thing to do:** Never vote "yes" on a matter before the board if you are unclear about the implications of the decision, if you believe that a "yes" vote is not in the best interests of the nonprofit, or if

you are convinced that further study or reflection is needed on the issue before the board.

5. **Be courageous:** Always vote "no" (versus abstaining) if you disagree with the proposed action before the board. Take the opportunity to explain why you are voting "no" during the comments or questions period.
6. **Listen to the small voice telling you to speak up:** Never tacitly or openly endorse an action you believe is wrong. Always speak up if you believe the organization, or any of its paid or volunteer leaders, are acting in a way that is illegal, unethical, fraudulent or violates regulatory requirements to which the nonprofit must adhere. Speak up if you believe a conflict of interest should be disclosed and discussed prior to a vote on a matter before the board.

The potential for an organization to be held legally responsible for its acts or omissions is a constant companion of every nonprofit mission. And as guardians of a nonprofit's mission as well as its assets, the board has a special responsibility to deliberate and act with care. Doing so not only increases the quality of the decisions made by the board, it also reduces the organization's exposure to legal claims. Armed with the resolve to be adequately prepared for committee and board meetings and the courage to speak up, every member of the board can also reduce the less likely, but still present risk of personal liability.

Melanie Lockwood Herman is Executive Director of the Nonprofit Risk Management Center and the principal author of the Center's new book: *Exposed: A Legal Field Guide for Nonprofit Executives-2nd Edition*. To inquire about bulk orders of *Exposed* or inquire about Melanie's availability for a speaking engagement, contact Kay Nakamura at 703.777.3504 or Kay@nonprofitrisk.org.



Data Privacy and Cyber Liability: What You Don't Know Puts Your Mission at Risk

*By Erin Gloeckner and
Melanie Lockwood Herman*

If you were a long-time donor to a nonprofit, and just learned that your credit card details provided to the nonprofit to make a donation are now in the hands of a hacker, would you ever trust that organization again? In an [article about nonprofits and sensitive data](#) published by the Nonprofit Technology Network (NTEN), the author points out that while data breaches occur at for-profits, government entities and nonprofits alike, consumers may be less willing to trust nonprofits after a data breach. This is because a consumer's relationship with a company or a government entity is largely based on the consumer's need, whereas his or her relationship with a nonprofit is not necessarily need-based. This suggests that nonprofits may be at greater risk for

reputational and financial damage in the wake of data breaches.

Although data breaches seem to be increasingly common, most nonprofit leaders still know very little about the risks that arise from the collection and storage of personal information collected from employees, volunteers, clients and donors. Considering this dark and somewhat frightening landscape, what must you know to understand the exposure and fortify your nonprofit against the associated risks? This article explores:

- Data privacy risks and responsibilities
- What is personally identifiable information?
- Privacy and data breach laws

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- The importance of reaching out for help complying with legal requirements in the wake of a data breach
- Cyber liability insurance basics
- Data security strategies
- Tips for working with tech vendors

Data Privacy Risks and Responsibilities

Many leaders believe that the work of foreign hackers represents the greatest threat to the confidential information their organizations collect. Yet the truth is that many threats to data privacy lives much closer to home. The following common business activities can lead to a data breach and potential liability for a nonprofit:

- Conducting e-commerce on your website, especially collecting credit card data and processing payments online
- Storing and transferring personal employee, client or donor data—for both virtual data and paper records (e.g., sending sensitive data via email or storing sensitive data in the cloud; storing paper records in unprotected filing cabinets that anyone could access)
- Storing personal information on laptops or smartphones
- Allowing partners and/or vendors to access personal information without proper safeguards
- Storing personal information on cloud servers or systems

While it's true that cybercrimes such as hacking, insertion of malicious code into a data system, or the purposeful loss and destruction of data are a valid concern for nonprofit leaders, it's important to recognize that unintentional privacy breaches can be just as costly. A simple example is permitting personal information to



In some states, the mere loss of the device with personally identifiable information is a breach under the law and triggers reporting responsibility, such as the duty to notify the people whose data was lost.

be stored on a laptop or smartphone. The device—and all the vital data on it—could be damaged, lost forever, or it could even fall into the wrong hands. In some states, the mere loss of the device with personally identifiable information is a breach under the law and triggers reporting responsibility, such as the duty to notify the people whose data was lost.

What is Personally Identifiable Information or PII?

The starting point for understanding a nonprofit's duty to guard personal information is understanding *what constitutes personally identifiable information under the law*. Information found in a telephone books is not protected under the law. Which means that the loss of a paper or electronic file containing donor names and addresses probably doesn't constitute a breach or

trigger state law notification requirements.

In Illinois the definition of "personal information" contained in the Personal Information Protection Act (815 ILCS 530) is "Personal information means an individual's first name or first initial and last name in combination with any one or more of the following data elements, when either the name or the data elements are not encrypted or redacted:

- (1) Social Security number.
- (2) Driver's license number or State identification card number.
- (3) Account number or credit or debit card number, or an account number or credit card number in combination with any required security code, access code, or password that would permit access to an individual's financial account.

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Privacy and Data Breach Laws

Data management and security standards are becoming increasingly complex as data constantly moves between multiple devices and storage sites. So what should nonprofit leaders know about this changing regulatory landscape? Various federal and state privacy regulations require that for-profit and nonprofit businesses *protect personally identifiable information* (PII) no matter where it resides: on a network; on stand-alone systems such as billing, medical, and marketing databases; on remote devices such as laptops or employee-owned cell phones; and of course on paper. Additionally, there are data protection standards for specific industries or specific business practices, such as the PCI Security Standards Council's Payment Card Industry Data Security Standard. This standard requires organizations to enact information security best-practices if they handle major credit cards such as Visa and MasterCard. Failure to comply with these standards can result in enormous fines. Similarly, you might be familiar with federal data security regulations such as HIPAA if your nonprofit handles protected health information (PHI).

According to the National Conference of State Legislatures, 47 states, the District of Columbia, Guam, Puerto Rico and the Virgin Islands have enacted laws that require organizations to notify individuals of security breaches of information involving personally identifiable information. Each of these laws generally has four key components:

1. who must comply
2. what constitutes "personal information"
3. what constitutes a breach (e.g., unauthorized acquisition of data); requirements for notice (e.g., timing or method of notice, who must be notified), and

4. whether there are exemptions.
The most common exemption is for encrypted information.

Make the Call

It is arguably unrealistic to expect that nonprofit executives have the time needed to master the various laws pertaining to data privacy and data breaches. Something every leader must know, however, is who to call if they believe a breach may have occurred. While the state laws are accessible through resources such as NCSL, there are experts in this field that can help you sort through the regulatory language and also walk you through the steps involved to comply in a timely fashion. If your nonprofit purchases cyber liability coverage, you may have access to these experts at no additional cost, as part of the policyholder services provided by your insurer. As with any insurance available to your nonprofit, it's important that you understand what it covers, when coverage is triggered, and what pro-active or responsive risk management support is available.

Cyber Liability Insurance Basics

Your nonprofit's insurance agent or broker is the go-to resource for information about what's covered under the cyber liability policy you already purchase, or one you're considering. Each insurer offers different forms of coverage, but many policies address a few familiar coverage areas. Work with your agent or broker to purchase a policy that adequately protects your nonprofit. Cyber liability policies may include third party coverages (items 1-5 below) and also first party coverages (items 6-7). Third party coverage protects the insured organization against claims that arise from losses suffered by third parties, such as donors or clients. First party coverage protects the insured for its own losses. The following is a list of some of the coverages that may be available through a cyber liability policy:

1. **Notification Expenses:** As discussed above, almost every state has notification requirements for both private and government entities. If a data breach occurred at your nonprofit, it is likely you will be required to notify parties affected by the breach. Spending weeks notifying affected clients, donors and employees could be costly. Coverage for notification expenses will protect your nonprofit from the strain on human and financial resources in the wake of a breach.
2. **Crisis Management:** After a data breach occurs and you've met your notification requirements, your nonprofit could still face harsh criticism and scrutiny from affected stakeholders or the media. These disenchanted former supporters may ask: How could this happen? Why didn't the organization do what was necessary to protect against a breach? Some cyber liability policies offer crisis management coverage to cover the cost of retaining PR help to minimize the damage to your reputation.
3. **Regulatory Investigation Expense:** Since data breach notification laws are subject to change, your commitment to comply may not be good enough. Which means there is always a chance you'll receive a call from a friendly civil servant. Both state and federal agencies can investigate and take action against a nonprofit that is negligent in guarding personally identifiable information. Some cyber liability policies exclude coverage for governmental or regulatory investigation costs, but other policies include it. And some policies will also cover fines and penalties, such as a fine levied for failing to notify the individuals whose data was compromised within the time limit required by law. These fines can be

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“Would the theft of a laptop or other mobile device constitute a data breach? Possibly, if those devices contain unencrypted personally identifiable information. Consider encrypting sensitive data so thieves who access to data can't use it.”

substantial, and are often on a per record basis.

4. **Data Breach Liability:** This coverage will defend your nonprofit against legal claims brought by a stakeholder who suffered a significant financial loss after their personal data was compromised. A typical suit will allege that your nonprofit was negligent in failing to protect the stakeholder's personal information, and that their loss was directly attributable to your nonprofit's negligence.
5. **Content Liability:** Some cyber liability policies offer financial protection related to the content of your website, blog or social media sites. This can range from copyright infringement and intellectual property claims to invasion of privacy or personal media injury (defamation, slander, libel) via electronic content. Some insurers refer to this coverage as “website liability.” Keep in mind that many nonprofits that buy cyber liability coverage principally do so to finance the costs arising from the theft of personally identifiable information, and choose to cover content liability exposures under another policy, such as a media liability policy.
6. **Data Loss & System Damage (or Data Restoration Coverage):** Your current property policy probably covers damage to computers you own, but traditional property policies do not

cover the data stored on computers. Most cyber liability policies cover loss or theft of personally identifiable information (e.g., your clients' home addresses, your employees' Social Security Numbers, etc.). Some policies also include coverage for computer forensic analysis, the process used by an expert to assess the scope of the damage.

7. **Business Interruption:** Many cyber liability policies cover events related to the temporary or long-term shutdown of an insured entity's operations, such as: loss of revenue during the downtime after a hack; denial of service; damage to systems or data caused by a virus; etc. Some nonprofits may find this coverage beneficial, however it is unlikely that most nonprofits would be forced to close their doors while responding to a data breach incident. If your nonprofit would have to close in the event of a data breach, you'll place greater value on having this coverage in place.

Data Security Strategies

To reduce the likelihood and severity of a data breach, consider the following practical strategies.

- **Ensure Regular Software Updates:** Make certain that IT staff or contractors frequently install security patches and updates to your devices' operating software

and other software. Oftentimes, data breaches occur when software is vulnerable due to age or other issues. Software updates typically include new security measures that will help protect your devices and data against harmful malware and viruses.

- **Encrypt Sensitive Data:** Would the theft of a laptop or other mobile device constitute a data breach? Possibly, if those devices contain unencrypted personally identifiable information. Consider encrypting sensitive data so thieves who access to data can't use it. If you work with protected health information and you are thereby required to comply with HIPAA, review this list of recommended protocols for securing mobile devices from www.HealthIT.gov. Consider the pros and cons of encryption. On the downside, encryption costs money and slows down response time. As a result, some experts suggest that organizations encrypt only data on mobile devices, or strictly prohibit the storage of personally identifiable information on mobile devices.
- **Schedule Data Security Training:** Some cyber liability policies offer proactive risk management resources, such as educational materials or access to helpful training on data security. Your data security efforts will be fruitless if your employees do not follow your protocols. Remember that human error is a major source of cyber liability exposure, an exposure you can mitigate by adopting clear policies and providing appropriate training. Topics you might want to cover in your training include: BYOD policies, network security protocols, encryption instructions, relationships with tech vendors,

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data breach notification laws, information on the nonprofit's cyber liability coverage, and your insurer's requirements for filing cyber liability claims. Ensure that your employees recognize how easily a data breach can occur, and how detrimental a breach could be to your nonprofit's mission.

- **Adopt a BYOD Policy:** Establish a Bring Your Own Device (BYOD) policy that clarifies whether employees may access PII on their personal devices (laptops, cell phones, etc.). Communicate the policy to employees, including instructions on what type of data may be accessed on personal devices, procedures for accessing data securely (e.g., through a secure network), and procedures for storing and transmitting data securely (e.g., using encryption). You might also decide to offer resources to employees such as [AT&T Toggle](#), a BYOD solution that allows employees to switch from 'work mode' to 'personal mode' on a smartphone. Whatever your BYOD policy is, aim to strike a balance between protecting nonprofit's data and upholding the privacy rights of your employees.

To prepare your nonprofit for the breach you hope will never happen, consider the following important questions.

- **What constitutes a data breach?** State security breach laws generally define what constitutes sensitive information. But no two state laws are identical. In some cases, such as Florida, a data breach is an actual breach. Florida Title XIX, Chapter 282 defines "breach" as: "a confirmed event that compromises the confidentiality, integrity, or availability of information

or data." In other states a data breach has occurred if there is reasonable belief that a data breach occurred, even without hard evidence of an actual breach.

- **Who must we notify?** Most states require organizations to notify all consumers affected by the data breach. Some states also require you to notify the state attorney general or consumer reporting agencies.
- **How should we contact our customers?** Some states require that specific communication methods are used to notify consumers of a data breach. For example, some states prohibit using pre-recorded phone calls, while other states only allow you to email consumers whom you have permission to contact via email.
- **How quickly must we contact our customers?** Every state notification law includes a timeframe for data breach notification. If you fail to notify your consumers within the appropriate timeframe, your nonprofit could face litigation and harsh fines.
- **What resources are available from our insurance providers?** As indicated previously, some insurers provide proactive risk management help, and have experts on call to either answer or help you determine the answers to the questions that follow. Keep cyber liability insurance information close at hand so that you're ready to make the call when you need to.
- **What changes should we consider?** Once you've addressed the crisis at hand and have complied with insurer and regulatory agency requirements, take time to consider lessons learned from the incident and the need for changes in policy,

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practice and training. Consider conducting a risk assessment focused on data privacy exposures, identifying training needs for staff, and updating internal policies that concerning the collection, storage and protection of personal information from clients, donors and employees.

Tips for Working with Tech Vendors

Aside from using the strategies above to mitigate potential data privacy exposures, remember to establish a process for vetting tech vendors if you outsource any IT processes or rely on a vendor for third-party “cloud” storage. Outsourcing IT support and/or data storage may be wise if your nonprofit lacks the personnel expertise or resources to manage data internally, but beware of placing too much trust in a tech vendor. Resolve to become a discerning consumer so you can distinguish dependable tech vendors from those unworthy of your trust. Take the time required to negotiate a contract with your tech vendor that ensures the support or services you need while adequately protecting your nonprofit against harm or loss caused by the vendor’s negligence. For starters, consider asking these questions before you engage with a prospective tech vendor:

- **What warranties or protections does the vendor offer in the event of their negligence?** Require that your tech vendors carry errors and omissions coverage to protect your nonprofit against claims stemming from the vendor’s negligence. Having this coverage won’t insulate your nonprofit from a data breach claim, but you might be able to subrogate a claim against your vendor if turns out they were negligent, such as by failing to install an available patch

when your contract indicated their responsibilities to do so. Never sign a tech contract absolving the company for its own negligence.

- **Do I understand my nonprofit’s tech needs and existing IT infrastructure?** What must I do (or who must I consult with) to understand these things before I engage a tech vendor?
- **Can this particular vendor meet all of our technical requirements?** Can this vendor integrate its services seamlessly with our existing internal IT functions?
- **Does this vendor have a good reputation in the market and amongst its client base?**
- **Is this vendor willing to include a training and/or support package with our contract (e.g., if your nonprofit has limited IT personnel or resources)?**
- **What is the vendor’s response time when its clients experience emergencies such as data breaches?**
- **Will my nonprofit still retain full ownership rights to any electronic documents and property that we store with the vendor (e.g., cloud storage vendors)?** What are our rights and responsibilities as owners?
- **What is the vendor’s dispute resolution process?**
- **Are the vendor’s payment terms reasonable and compatible with our accounts payable process?**

Erin Gloeckner is Project Manager and Melanie Lockwood Herman is Executive Director at the Nonprofit Risk Management Center. They welcome your questions about data privacy risks and cyber liability at 703.777.3504 and Erin@nonprofitrisk.org or Melanie@nonprofitrisk.org.

Data Privacy and Cyber Liability Resources:

2014 Security Breach Legislation.

National Conference of State

Legislatures. www.ncsl.org/research/telecommunications-and-information-technology/2014-security-breach-legislation.aspx

http://netdiligence.com/files/WP_Cyber_EXEC_SUMM.pdf

<http://searchsecurity.techtarget.com/feature/Is-cyberinsurance-worth-the-risk>

www.phly.com/files/cyber%20nps31-1830.pdf

<http://jpins.com/2014/07/02/are-non-profits-at-risk-for-cyber-liability-claims/>

www.mcguirewoods.com/Client-Resources/Alerts/2013/12/A-Nonprofit-Buyers-Guide-to-Cyber-Insurance.aspx

www.charityfirst.com/cyber_liability_insurance_non_profits/

www.nonprofitinsuranceblog.com/do-nonprofits-need-to-worry-about-data-breach-lawsuits/

www.rollinsinsurance.com/nonprofitguard/what-does-cyber-liability-cover-6-coverages-you-should-know-about

Nonprofit Risk Management Center Articles

Risk in the Cloud www.nonprofitrisk.org/library/articles/Risk_in_the_Cloud.shtml

Tech Risk Q&A www.nonprofitrisk.org/library/articles/Tech_Risk_Q_and_A.shtml

Insurance for Cyber Risks www.nonprofitrisk.org/library/articles/Insurance_for_Cyber_Risks.shtml



Travel Safe: Managing the Legal Risks that Arise from International Operations

by Jefferson C. Glassie, Esq., FASAE, and partner Whiteford, Taylor & Preston, LLP

Nonprofit organizations are becoming increasingly active in global activities, which are very complex because of cultural, linguistic, operational, and risk issues. Adding to the complexity are legal issues. When does United States law apply, and when does the law of the local country apply? And what exactly are local laws that nonprofits have to watch out for? It's not possible to know the laws of all the countries around the world, so how does one manage some of the key legal risks?

Here is a list of some of the more important legal concerns, with some guiding principles that nonprofit leaders should be aware of before venturing overseas.

1. Trademark – This may be the most important issue of all. In the United States, nonprofit organizations

obtain rights to trademarks, i.e., their names, acronyms, design logos, and slogans, simply through use in commerce. Registration is not required, but is advisable to enhance protections. In most other countries, however, trademark ownership is based on registration with the relevant authorities. These countries are “first to file” jurisdictions, so if a nonprofit starts conducting activities in another country, the first step is to register the organization's important trademarks. Otherwise, someone else could register and start using the nonprofit's name! That would not be cool! So, don't be the nonprofit manager who surrenders your organization's name and marks in other countries. Engage the services of trademark counsel,

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Travel Safe: Managing the Legal Risks that Arise from International Operations
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identify and prioritize the countries where you may conduct programs, and make sure registrations are filed for important marks. It is essential for truly global nonprofits to have a trademark portfolio to protect their marks globally.

2. **Overseas Offices** – Many activities can be conducted without an office in the local country, but it's important to understand when one may cross the line and be required to register with the corporate authorities. Simply having a single employee or agent in a country is unlikely to trigger corporate registration requirements, but having several employees, an office, and a bank account for funds will likely necessitate registration. It's important to think of this before activities become substantial. In some cases nonprofits open offices in other countries without setting up new local, legal entities; these are usually called "branch offices" and will require registration. Or, the nonprofit may want to establish a separate legal entity for liability purposes and that will entail setting up a corporate-type organization under the laws of the local country. Keep in mind that other countries don't have the same type of corporate structures we do in the United States, so the options will have to be explored with local legal counsel and sometimes the requirements can be unfamiliar, complex, and arcane. It might even be appropriate or advantageous to operate as a for-profit entity in certain countries, so keep an open mind as to the options!
3. **Employees/Contractors** – Other countries often have similar concepts in this area as in the United States. Independent contractors must be

autonomous, generally will have other clients, and should have clearly written contractor agreements. Many countries have very broad laws when it comes to employees, and mandate significant benefits during and after employment termination, more so than in the United States where "employment at will" is the default employment relationship in all states except Montana. It is critical to make sure that employees and contractors are properly identified and treated correctly under local law, or there could be significant obligations or penalties if the nonprofit does not comply. Of course, proper visas or work permits are necessary if using employees from outside the local country and, again, legal advice is important to ensure compliance.

4. **Tax** – A variety of issues arise when a nonprofit operates overseas. First, United States law applicable to tax exempt organization applies globally. So, limitations imposed on U.S. tax exempts will apply when conducting activities outside the United States. A Section 501(c)(3) charitable organization can engage in international activities, but the restrictions imposed on lobbying, political activities, and the intermediate sanctions rules will still apply. If revenues are received from fee-for-service/consulting activities or from advertising, those would be considered unrelated business income tax ("UBIT") just like in the U.S. Second, while most nations recognize charities and consider them tax exempt, the definitions applicable in other jurisdictions are different and may not cover educational or similar more professional types of activities than Section 501(c)(3) in the U.S., much less have a tax exemption category

for trade or professional associations exempt in the United States under Section 501(c)(6). Third, there are value added taxes ("VAT") in many countries, which we don't have in the U.S. Also, many nations impose "withholding" taxes on the amount of dividend, royalty, or interest paid to a parent or affiliated entity outside the country. So, it's really important to understand tax obligations in other countries before engaging in significant activities that might be considered to constitute a "permanent establishment" for tax purposes in other nations.

5. **Privacy, Spam, and Cybersecurity** – The United States has a patchwork of laws in this area that can make compliance somewhat complex, and other countries have similar laws, such as the European Privacy Directive, that is applicable to U.S. nonprofits. It's important to understand that U.S. nonprofit organizations may have "personally identifiable information" (PII) about nationals of other countries that can be impacted by laws in those countries, may unknowingly have information about U.S. citizens in servers outside of the U.S., and are increasingly subject to hacker attacks and data breaches that can give rise to liability. As one of the new liability concerns, nonprofit managers must devote significant energy to ensure compliance with domestic and foreign laws regarding protection of data and information, such as adoption of written information security plans mandated by certain state laws. The new Canadian anti-spam law also will ultimately require U.S. organizations to get "opt-in" consent from Canadian donors,

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Note that it's generally advisable for international contracts to have arbitration clauses, as the international arbitration treaty provides for enforcement of arbitral awards in subscribing countries, whereas court decisions will probably not be given effect in other countries.

members, or stakeholders in order to send Canadian stakeholders email messages.

6. **Insurance** – Most nonprofits arrange for sufficient insurance to protect the organization from claims of bodily injury and property damage, and also to protect directors, officers, staff, and volunteers from claims of wrongful or negligent acts under standard commercial liability policies and Directors' and Officers' (D&O) insurance, respectively. Although these policies may cover claims for actions anywhere around the world, they are likely to only respond if the suit is brought in the United States. Therefore, it's essential to ensure that international activities are properly and adequately insured. Extra travel insurance is generally advisable for staff or volunteers working outside the United States.
7. **Export Controls and Embargoes** – In many respects, export controls are less significant nowadays than in the last century, but the United States embargoes of certain countries and nationals remain very strict and high profile. The main countries targeted are Cuba, Iran, Sudan, and North Korea, although specific sanctions are in place with respect to other countries such as Somalia, Syria, Russia, etc. For nonprofits with a global mission, it is important to ensure compliance with the embargoes, which are administered by the Office of Foreign Assets Control of the Treasury Department. These regulations can be highly technical and arcane.
8. **Contracts** – It is critical that arrangements with individuals and organizations in other countries be subject to written contracts.

Misunderstandings can easily arise based on cultural, language, and other differences, so it's vital to make sure that contracts are signed, and that specifications and deliverables are clearly described. Any creation or use of intellectual property should be addressed in the contract, to ensure that the nonprofit organization holds and retains rights in copyrighted material, and that only authorized uses of intellectual property, including trademarks, are permitted. Note that it's generally advisable for international contracts to have arbitration clauses, as the international arbitration treaty provides for enforcement of arbitral awards in subscribing countries, whereas court decisions will probably not be given effect in other countries.

These are just some of the main legal principles for nonprofit leaders in organizations conducting or considering activities outside of the U.S. The advice of counsel based in the U.S. and also the country where your nonprofit is headed may be required depending on the circumstances. And certain nonprofit activities such as certification, accreditation, and standards setting will require additional review. An ounce of prevention in terms of planning in advance is worth a pound of cure, because international situations can become complex very quickly. When taking your nonprofit's mission overseas, resolve to plan for success, but be prepared for trouble.

Jefferson Glassie is author of *International Legal Issues for Nonprofit Organizations* (2nd Ed. 2010) published by the American Society of Association Executives. Jeff welcomes your comments and questions about the topics covered in this article at JGlassie@wtplaw.com or (202) 689-3156.



Waivers and Young Participants

By *Melanie Lockwood Herman*

Except in very rare instances*, a contract signed by a minor** is voidable by the minor until he or she reaches the age of majority. A “voidable” contract is legally binding on both parties unless the minor chooses to void the contract, at which time it will no longer be enforced. Often without knowing exactly why, the leaders of most youth-serving organizations recognize the inherent weakness in asking children to sign contracts. Therefore, it has become common practice to either ask parents or guardians to waive their right to sue the nonprofit for injuries their child sustains, or to ask both the child participant and a parent or guardian to execute a waiver. This article explores some of the issues related to the use of waivers by youth-serving nonprofits, including:

- How state court rulings differ on the enforceability of parental waivers
- Key considerations in careful waiver drafting

- Using a Participant Agreement as an alternative to a waiver

It's a Different World

Prior to drafting a waiver for a youth-serving program or activity, it is helpful to understand how the state courts differ in their treatment of waivers. There are three general categories into which case law on waivers can be grouped.¹ The first category consists of the 12 states where prior rulings have shown that courts will, in some cases, enforce waivers to protect either schools, other nonprofit or public-serving organizations, or both nonprofit and commercial entities. These states are: Arizona, Alaska, California, Connecticut, Colorado, Florida, Indiana, North Dakota, Ohio, Massachusetts, Minnesota, and Wisconsin.

The second category of states consists of those that take a polar opposite position from the state courts in the first category. In the following 17 states

the courts consistently reject waivers signed by a parent on behalf of a minor child: Alabama, Arkansas, Hawaii, Iowa, Illinois, Louisiana, Maine, Michigan, Montana, New Jersey, Pennsylvania, Tennessee, Texas, Utah, Virginia, Washington and West Virginia.

The third and final category consists of 21 states where there is inadequate information to predict, with any degree of certainty, whether a court will enforce parental waivers. All of the states not listed in the first and second categories fall into the third category. These states are: Delaware, Georgia, Idaho, Kansas, Kentucky, Maryland, Missouri, Mississippi, North Carolina, Nebraska, Nevada, New Hampshire, New Mexico, New York, Oklahoma, Oregon, Rhode Island, South Carolina, South Dakota, Vermont and Wyoming.

*The exceptions to the rule providing that minors lack capacity to enter into a contract are 1) when a minor enters into a contract to provide support for an illegitimate child; 2) a contract with a bail bonds provider; 3) when the contract has been approved by a court; 4) in some cases where the minor has received benefits per the contract.

**Children under the age of 18 in all states except Missouri and Alabama are minors. In MO and AL minors are people under the age of 19.

10 Tips for Careful Waiver Drafting

If your nonprofit decides to use waivers for certain activities, make certain you take care in drafting. Keep in mind that even in states where waivers are generally enforced, sloppy drafting could render the waiver unenforceable. Follow the steps below to create waivers that have a greater likelihood of holding up.

1. **Use a proper title** – Always use the term “Waiver” or phrase “Waiver and Release of Liability” as the title of your form. Never use a misleading title such as “sign-up sheet.”

¹ *Waivers & Releases of Liability*-8th Edition, by Doyice J. Cotton and Mary B. Cotton

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2. **Keep it simple** – Limit the purpose and content of the waiver to your request that a parent waive the right to sue for injuries suffered by their child while participating in a program or activity sponsored by your nonprofit. Waiver language buried in a longer document covering a multitude of topics increases the likelihood of disfavor by a reviewing court.
3. **Be truthful and tell it like it is** – Make certain that your waiver contains no fraudulent statements or misrepresentations. For example, don't indicate that participants may inspect your equipment and facilities if there is no opportunity to do so. Don't tell parents there is no insurance for the event, if, in fact, there is. Also, clearly describe the specific activity in which the participant will be involved. Refrain from using a single waiver to cover multiple activities of different types, such as "field trips" or "outdoors activities."
4. **Note and describe inherent risks** – Include a separate paragraph in the waiver alerting the participant to the inherent risks of the activity. Draft a representative list of inherent risks associated with the specific program or activity covered by the waiver.
5. **Note the special risks pertinent to the activity, outdoor/indoor location, or type of facility.** Remember that your nonprofit is in the best position to describe the terrain, conditions, physical fitness required, etc., as well as the dangers or unpleasant conditions associated with the activity.
6. **Include an assumption of risk statement that affirms the participant's voluntary participation.** For example: "I acknowledge and accept the inherent and special risks associated with hiking Big Mountain and certify that I am voluntarily participating in the hike on June 10th."
7. **Use readable type** – While it's okay to use boldface, underline and italics to highlight key terms, don't make the mistake of putting important or lengthy sections in ALL CAPS, WHICH ARE HARD TO READ.
8. **Don't promise a safe environment or safe experience** – Although your nonprofit will do its best to provide a safe and enjoyable experience for participants, it's never wise to promise safety. A reviewing court may regard a promise of safety as an express

continued on next page

Sample Agreement to Participate in a Hiking Trip "Rock On for Kids"

Rock On for Kids will be sponsoring a hiking trip on Big Mountain on Saturday, June 10th. Members of the club who have completed their community service hours and are at least 12 years of age are eligible to participate.

The Hiking Trip will involve a one-hour bus ride, followed by a one-hour walk to the base of the mountain. After the walk, participants will climb and hike on Big Mountain. Although we are hopeful for good weather, it could be cold and rainy. The temperature will go down as we climb the mountain. A participant who isn't dressed properly will quickly become uncomfortable. Participation in any outdoor, physical activity such as the Hiking Trip sponsored by Rock On for Kids, involves certain inherent risks. These risks include minor injuries such as bug bites, scrapes, bruises and strains, as well as more significant and even catastrophic injuries, such as severe sunburn, heat stroke, hypothermia, frost bite, lightning strike, animal attack, broken bones, concussions, paralysis and death.

Rock On for Kids takes the safety of all participants very seriously, however, the organization cannot guarantee the safety of any participant.

Please review the following rules. It is your responsibility to ask questions about these rules before you sign this Participant Agreement.

Safety Rules and Participant Requirements

Participants must:

- Be dressed for the weather and the activity – in layers and with a waterproof outer jacket, hiking boots and warm socks.
- Bring a lightweight water bottle that can be attached to a belt or waistband.
- Follow all instructions provided by adult leaders during the hike. These instructions may include, but are not limited to: do not touch or disturb plant or wildlife, do not stray from the path, do not run, do not attempt to pass the hiker in front of you unless directed to do so, keep cell phones in a zipped compartment unless the group stops to take photographs at the direction of the hike leader.
- Use any and all equipment and supplies as instructed.

*Waivers and Young Participants
continued from page 18*

or implied warranty, or evidence that any harm suffered by a plaintiff participant must have resulted from gross, rather than ordinary negligence.

9. Make the waiver section of the document clear – Ensure that the waiver is clearly drafted and applies to injuries arising from inherent risks or from the nonprofit’s ordinary negligence.

10. Remember “who” and “what” – Reference which parties seek protection and refer to the negligence of the parties. Some states require that the word “negligence” appear in an enforceable waiver.

Waiver Alternative

If your organization has decided not to require that parents of young clients or participants execute waivers, consider

using a Participant Agreement. A Participant Agreement offers several salutary effects. First, in contrast with waivers, which are always perceived as negative, a participant agreement may be perceived as a positive. Second, a participant agreement explains the risks of a particular activity as well as your organization’s important rules related to the activity. Participant agreements give parents the opportunity to make informed decisions about whether to allow a child to participate. Keep in mind that as with a waiver, it doesn’t make sense to only ask the child to sign. A better approach is to request that the minor and the parents sign the agreement.

When using Participant Agreements, always strive to explain the risks and the rules of the activity orally to the participant and their parents, versus

relying on the form to communicate these key messages. Invite participants and their parents to ask questions about any aspect of the activity, and never ask a parent or child to sign an agreement minutes before the activity is set to begin. Here are some important items to include in an Agreement to Participate:

- *Specific description of the activity* – Be specific, and never vague, about the activity in which the child will participate. Note whether the activity is strenuous, intense or unfamiliar. Note the conditions, such as: “the course will be muddy and it may be cold and windy the entire day.”
- *No guarantee of safety* – Remind the participant and parents that your nonprofit cannot ensure the safety of participants. For example: “Activities such as this have inherent risks.

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Participant Acknowledgement of Risks, Rules and Requirements

1. I have read and understand the inherent and special risks associated with hiking on Big Mountain as well as the Safety Rules and Participant Requirements established by Rock On for Kids.
2. I believe I have the physical fitness necessary to participate safely in the hiking trip described in this Participant Waiver. I promise to notify a trip leader if I feel I am unable to continue with the hike for any reason.
3. I want to disclose the following health-related conditions (check all that apply):
 diabetes seizures asthma heart issues
 other _____

Participant Name _____
 Participant Signature _____ Date _____

Parent/Guardian Acknowledgement of Risks, Rules and Requirements and Permission to Treat

1. I have read and understand the risks associated with hiking on Big Mountain as well as the Safety Rules and Participant Requirements established by Rock On for Kids.
2. I believe that my child, _____, has the physical fitness necessary to participate safely in the hiking trip described in this Participant Agreement.
3. My child has the following health-related conditions (check all that apply):
 diabetes seizures asthma heart issues
 other _____

4. I hereby grant permission for emergency medical treatment to be provided to my child, as needed, and I agree to bear financial responsibility for such treatment.
 Parent/Guardian Name _____
 Parent/Guardian Signature _____
 Date _____

*Waivers and Young Participants
continued from page 19*

Although precautions will be taken, it is not possible to ensure the safety of participants.”

- **Possible injuries** – Include a description of some of the injuries a participant could suffer. For example, “Rock-climbing is inherently dangerous, and participants may suffer cuts, scrapes, bruises and sprains while climbing. Serious injuries are also possible, including broken bones, paralysis or death.”
- **Safety rules** – Include a list of specific rules to which the participant must adhere. Take the time to list as many rules as you can imagine would apply to the activity, but also include language indicating

that additional rules may apply. For example: “The following are examples of the rules that apply to all participants.”

- **Other requirements** – List other requirements and expectations of participants, such as your requirement that the participant notify a responsible adult if they become aware of a hazardous condition, broken or malfunctioning safety device, or violation of safety rules by a leader or other participant.
- **Confirmation of ability to participate** – Ask the participant to affirm that they are capable of participating safely. Also ask the participant to list any physical conditions or illnesses

that could affect their ability to participate safely, such as allergies, asthma, etc.

- **Permission to treat** – Ask the parent to specifically consent to the provision of emergency medical treatment and accept financial responsibility for such treatment.

Melanie Lockwood Herman is Executive Director of the Nonprofit Risk Management Center and the principal author of the Center's new book: *Exposed: A Legal Field Guide for Nonprofit Executives-2nd Edition*. To inquire about bulk orders of *Exposed* or inquire about Melanie's availability for a speaking engagement, contact Kay Nakamura at 703.777.3504 or Kay@nonprofitrisk.org.

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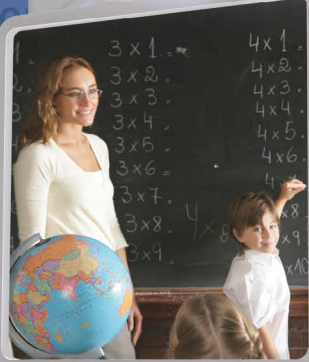
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