

Park-To-Park Trail Association

Loyalty, Duty and Conflict

(Towards a Code of Behavior for Directors of the Park-To-Park Trail Association)

Introduction

This paper is in response to concerns expressed regarding P2P representation on Boards or committees of other organizations. It discusses the nature of organizations, the duties of directors of organizations, several forms of conflict of interest and, finally, some of the real situations encountered by P2P directors.

The following paragraphs (indented) are taken verbatim from a paper entitled "Directors' Liability: A Discussion Paper on Legal Liability, Risk Management and the Role of Directors in Non-Profit Organizations". Funding for its preparation was provided by the Government of Ontario, Ministry of Citizenship – Volunteerism Initiatives. It is published by Volunteer Canada.

2. What is an organization?

Organizations come in a variety of types and sizes, under a variety of names. In this discussion paper, the generic term 'organization' is used. Some organizations are small with no staff and no office, some have a few staff, and some are large entities with many staff and volunteers.

An organization can be 'unincorporated,' and thus have no legal status, or it can be 'incorporated' as a corporation under federal or provincial statutes. This corporation can be for-profit (that is, organized to pursue commercial objectives), or it can be non-profit (that is, organized to fulfill benevolent or charitable purposes).

A non-profit organization can be referred to as:

- a club,
- an association,
- a society,
- a corporation,
- a league or
- a committee (as in the Canadian Olympic Committee)

3. What is a board?

Some organizations are governed by administrative or 'hands-on' boards while others are led by policy-governing boards. Both boards may be called a board of directors, a board of governors or a board of trustees. The responsibility of an organization's board is to:

- provide leadership and direction to the organization; and
- govern the affairs of the organization on behalf of its shareholders (in the case of a for-profit corporation) or its members (in the case of a non-profit organization).

4. What is a director?

A director is an individual who is a member of a governing board of an organization.

Directors of non-profit organizations are volunteers and are rarely paid for their services, while directors of for-profit corporations are usually compensated. As a rule, directors are elected or appointed to their positions on the board. They may also be officers, where an officer fulfills certain corporate roles and functions (such as those duties of a 'president,' 'treasurer' or 'secretary' of the organization). Officers can also be senior staff persons, and in rare circumstances, staff persons can also be directors.

Regardless of the name, size, or type of organization, the role of the director remains fairly constant. Directors and officers of non-profit organizations are responsible for governing the affairs of the organization on behalf of its members. Directors and officers have a relationship of 'trust' with the members of the organization, and it is from this trust relationship that certain important legal duties arise.

5. Legal duties of directors

The basic responsibility of directors is to represent the interest of the members in directing the affairs of the organization, and to do so within the law. This legal duty is described in statutes (such as the *Canada Corporations Act*, provincial business incorporation statutes and provincial societies or non-profit organization statutes) and has been expanded and interpreted in the common law.

In representing the members of the organization and acting as their 'trustee,' directors have three basic duties:

1. The duty of *diligence*: this is the duty to act reasonably, prudently, in good faith and with a view to the best interests of the organization and its members;
2. The duty of *loyalty*: this is the duty to place the interests of the organization first, and to not use one's position as a director to further private interests;
3. The duty of *obedience*: this is the duty to act within the scope of the governing policies of the organization and within the scope of other laws, rules and regulations that apply to the organization.

It is important to note that the duties of directors of non-profit organizations are essentially no different than the duties of directors of for-profit corporations. These duties extend broadly, and are owed to:

- the organization as a whole,
- the organization's members, participants, clients, staff and volunteers,
- other directors and
- anyone else who may be affected by the decisions of the board and the activities of the organization, including the general public.

These three duties are discussed more fully below.

5.1 Duty of diligence

Diligent directors always act prudently and in the best interests of the organization. When performing their duties as directors, they are expected to exercise the same level of care that a reasonable person with similar abilities, skills and experience would exercise in similar circumstances. If a director has a special skill or area of expertise, such as an accountant or lawyer would have, he or she has a duty to achieve a standard of care that corresponds to his or her professional abilities.

Directors have a responsibility to act cautiously and to try to anticipate the consequences of their decisions and actions before they undertake them. They are honest and forthright in their dealings with members, with the public and with each other. Directors are also well informed about the activities and finances of the organization. They have an obligation to foresee potential risks inherent in a situation and to take reasonable steps to manage those risks.

5.2 *Duty of loyalty*

Directors are required to put the interests of the organization first. These interests will always take precedence over any other interest, including a director's personal interests. As well, directors who are involved in more than one organization may find that they cannot be loyal to both.

Loyal directors will avoid putting themselves in a situation of a conflict of interest. When this is unavoidable, they will act properly in disclosing the conflict and ensure that they play no part in discussing, influencing or making decisions relating to that conflict.

Confidentiality is also an important aspect of the duty of loyalty. Directors have an obligation to keep organizational business private, and to not discuss certain matters with people outside the organization. Confidential matters may include:

- information about personnel and
- information about clients served by the organization, the organization's finances or legal matters.

A board acts as one entity. Loyal directors support the decisions of the board, even if they might not personally agree with the decisions and might not have voted to support the decisions in the board meeting.

5.3 *Duty of obedience*

Nearly all non-profit organizations are 'private tribunals' (that is, autonomous organizations that have the power to write rules, make decisions and take actions that affect their members and participants). Legally, private tribunals are recognized as having a contractual relationship with their members. This relationship is defined in the organization's governing documents, which include:

- its constitution;
- bylaws;
- policies, and
- rules and regulations.

Directors have a duty to comply with the organization's governing documents, and to ensure that staff and committees of the organization do as well. Over time, organizations may move away from their legal purpose, and policies may become out of date and no longer reflect the practices of the organization. Obedient directors ensure that governing documents remain current and accurate, and oversee the process that is used to amend and update governing documents.

Directors also have a duty to obey external laws and rules that are imposed upon organizations. A wide range of laws and statutes apply to corporations and individuals: the obedient director ensures that the organization complies with these. In particular, an

organization that is an employer has many statutory responsibilities to its employees. These responsibilities include:

- paying wages;
- providing paid time off for holidays;
- making deductions from wages and remitting these to the government;
- providing a safe workplace; and
- protecting employees from discrimination and harassment

Director Duty and the P2P

P2P is an organization. Specifically, it is a not for profit corporation without capital share. It does not own anything of value and does not pay a profit to members or share holders. It does not have employees, though P2P does have long term contracts for full time services with one or more individuals. P2P is governed by a board of directors which is largely “hands-on”. P2P’s directors do not receive compensation for their services.

P2P’s directors, like those of any other organization, are subject to duties of diligence, loyalty and obedience. Directors who fail to recognize and exercise these duties are breaching the trust relationship they have with the organization’s members. They may also be breaking the law.

P2P’s directors are frequently nominated by P2P member organizations. The nomination is voted on at P2P’s annual general meeting. Prior to this election process, the individual may have been appointed by the P2P Board of Directors and served a partial term. Either way, every director is ultimately elected by a process involving the organization’s entire membership. Hence, his or her duties of diligence, loyalty and obedience are to the entire membership – not just to the organization responsible for the nomination.

In many cases, people elected to the P2P Board of Directors retain a directorship or even an executive position on their parent organization – the one that nominated them to the P2P Board. This means that they also have duties of diligence, loyalty and obedience to a second organization. This is not necessarily a problem but it may put the individual in a conflict of interest situation. This is not necessarily a problem both as long as it is recognized and properly dealt with.

Conflict of Interest

Conflict of interest can assume several basic forms. First, conflict might center on personal interests or it might center on duties an individual owes to an organization. Secondly, the gains or losses involved might be material or social. The alternatives are summarized in the following table:

	Personal interest	Organizational interests
Material gain / loss	Conflict of interest arises when an organization to which an individual owes duties of diligence, loyalty and obedience is in a position to do something which could bring profit to the individual or cause him/her financial loss. e.g. the individual is a director of a trails organization whose actions are affecting land values where the individual is an owner.	An individual duly elected to two different organizations owes duties of diligence, loyalty and obedience to each. The individual is in a conflict of interest situation if circumstances allow one organization to materially profit at the expense of the other e.g. both organizations are trying to win the same contract.

Social gain / loss	Conflict of interest arises when an organization to which an individual owes duties of diligence, loyalty and obedience is in a position to do something which could enhance or harm the individual's social standing e.g. a trails organization is considering support of a political party when one of its directors might be running for office.	The individual is also in a conflict of interest situation if the actions of one organization that he or she serves might affect the credibility or reputation of another for which he is a director.
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Some of the behaviors which might be compromised when a person is in conflict are:

- honestly representing the interest of the members in directing the affairs of the organization, (and doing so within the law)
- the ability to foresee potential risks inherent in a situation and to take reasonable steps to manage those risks.
- directors who are involved in more than one organization may find that they cannot be loyal to both.
- the ability to keep organizational business private
- the ability to comply with the organization's governing documents

Serving Situations (examples)

- 1) A member of the Board of Directors of the P2P is asked to represent P2P at a meeting or sit on a committee of another organization: As a P2P director, this person's first duty is to the P2P. On any issue, the position of the P2P, if the P2P has a formal position, must take precedent over that of the individual. If the P2P does not have a declared position on the issue, then the individual must make a best judgment call as to what the P2P position might be and present that. If commitment of P2P policy or resources is involved, the individual should present the position as tentative and needing confirmation by the P2P Board.
- 2) The P2P nominates an individual (not a P2P director) to sit on the Board of another organization: Because they were nominated by P2P, there will likely be an expectation that they bring some knowledge of P2P and sensitivity to P2P practices and values. However, their duties of diligence, loyalty and obedience are to the board on which they sit, not to P2P.
- 3) An P2P director is elected to the Board of another organization: This person becomes a director of two organizations and has duties of diligence, loyalty and obedience to each. Each organization might expect the individual to have knowledge and understanding of the other and to make beneficial use of that knowledge. However, neither organization should expect him or her to break a confidentiality commitment. Further, the individual is in definite conflict if the ends of one organization might be advanced at the expense of the other.
- 4) A director of another organization is elected to the P2P Board: This person has a divided loyalty and neither loyalty takes precedent by being first. If the best interests of one organization are counter to the best interests of the other, then the individual must declare a

conflict of interest and withdraw from the discussion.

- 5) Communicating through cross directorships: Many organizations nominate directors to the P2P Board with the expectation that they will report back on P2P activities. This is a good way of communicating between organizations and not necessarily a problem. However, the individual who agrees to become a P2P director is also agreeing to the director's duties – including that of confidentiality. The individual and nominating organization must both understand that a director of P2P cannot reveal information which might harm P2P.
- 6) Board Meeting Guests: P2P has an established practice of open meetings and fairly public minutes. This means that guests might frequently have access to information which should, at a minimum, be used with discretion. The director who invited the visitor should be sensitive to this and alert the visitor to the need to respect the nature of the exchange.
- 7) Privileged Information: P2P Directors in the course of their duties are frequently exposed to information which, while not labeled “confidential” or “private”, is still privileged. Release of information outside of the P2P Board should always be questioned with respect to the impact of that release on P2P. Discussion of an issue in an open meeting does not justify its widespread distribution. If the distribution turns out to be harmful to P2P, then its distribution would still be a breach of confidentiality.

What to do

When a director finds him or herself in a conflict of interest, he should acknowledge the conflict and withdraw from the discussion. He or she does not have to reveal the nature of the conflict but once declared, he must not participate in discussion of the issue or do anything else that might influence the outcome.

Directors, or potential directors, should try to anticipate and avoid conflict situations. The trust relationship between a director and the organization and its members is an issue of professionalism and personal integrity. It might also have legal implications as it represents a contract.