

# Legal Counsel for Churches

Corporate Governance  
for Churches & Their Leaders

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April | 2021



## Emeritus Directors Can Improve Governance



Church leadership is responsible for making wise decisions. In many instances, the best decisions are the choices that take into consideration the history of the church.

When long-serving church directors decide to step down from the board, the vacancy could leave a void in historical leadership. Church officials who have seen the ministry through its challenges over a course of time bring valuable experience. The church should consider finding a way to tap this source of knowledge for future decisions. This can be done through an Emeritus Director program.

An emeritus director is a former church board member who continues to serve the ministry as an advisor to the current board. In some instances, churches might regard the emeritus officer as a ceremonial role. While honoring one's longevity, service and contributions is a noble purpose, emeritus directors can be quite helpful for corporate governance.

I have observed over the years that most mistakes are made in the early stages of the decision-making process. This is when the church is pondering an idea and weighing its benefit. Church leaders will consider the pros and cons of their choices in today's world. The error often made is failing to recognize the lessons of the past.

History teaches organizations what has worked and what has failed beforehand. This perspective is important to repeat successes and evade reliving failures.

Historical knowledge is important to governing boards. Directors who appreciate the history of the church make better decisions. This appreciation includes knowing the evolution of the congregation's culture and the church's capacity for change.

Churches that want to launch an emeritus program should first consider establishing a policy. The policy may reside in the church bylaws or simply an act of the governing board. The policy should specify the qualifications for being an emeritus director and the terms for service.

In some cases, the emeritus director is invited to attend all board meetings. While the emeritus director may not have voting privileges, his/her opinions are sought for many decisions. I have seen instances when the emeritus director recognized a risk the current board had overlooked.

The emeritus director program also offers a useful avenue for succession planning. Let's be honest. Retiring from a long-held church position can be a difficult decision for many. The opportunity to be named to an emeritus position allows one to remain involved at a slower pace.

Emeritus directors are a good source for training new church leaders. I can not emphasize this enough. New church officials need to be informed on the present ministry processes and rules. An appreciation for legacy work gives emerging leaders a base of knowledge from which to build on for future decisions.

I have seen in some instances where the emeritus director was a mentor to a new board member. The emeritus director would spend time with the recruit to teach lessons about church history, philosophy, and core values. These exchanges can lead to valuable connections that benefit the church.

Emeritus directors can extend the board's work for special projects. Organizations often have a need to explore or perform a function for a limited time. Ad hoc committees may be useful for special projects. Emeritus directors can do this work and report findings to the church board for official action.

Finally, an emeritus director can be an effective coach for the church's pastor and other staff officials. The emeritus director may be less threatening to staff because this individual does not have board voting power.

An emeritus director program is a way to improve corporate governance and improve the effectiveness of the church board. ■

# How Church Directors Get in Trouble



**C**hurch directors have a fiduciary duty to make decisions that are in the best interests of the church. These duties include a duty of care, duty of loyalty and duty of obedience. These responsibilities are the same for any board of directors. No matter the organization, industry or charter, directors must keep a primary focus on the institution's interests.

Board members must act prudently to fulfill their obligations. Courts weigh a director's conduct by comparing his/her actions to someone in similar roles. This is called the "reasonable person" standard. In other words, how would a director of any corporation treat a subject.

So long as church directors follow the guiding principle of these duties, their conduct will usually not be called into question. Occasionally, directors make mistakes and come under legal scrutiny. There is a lesson to be learned in reviewing the ways directors can get in trouble. Here is a list of areas that can trap directors.

**Reviewing Financial Statements:** Church directors should have financial literacy on church matters. This includes understanding the church financial condition, sources of income, expenses, and fiscal obligations. Reviewing financial statements also include the directors' review of any financial audits.

**Travel and Expense Policies:** Directors should pay particular attention to travel and expense policies. These areas can be troublesome because of the opportunity for waste or misappropriation of church funds. It is reasonable for directors to be watchful that the church policies are carefully followed.

**Whistleblower Policies:** Whistleblower policies are useful for helping an organization encourage disclosure of questionable activities. A church's whistleblower policy should grant protections for the whistleblower from retaliation. Directors have an obligation to ensure the policies are managed in a way no whistleblowers' rights are usurped.

**Overseeing Investments:** Church investments offer the institution an opportunity to put its treasury to work for the benefit of the congregation. Investments can be tricky because some instruments carry more risk than other investments. For this reason, church directors should be particularly wary of approving investments they do not understand. Church officers can find themselves in jeopardy by failing to ask questions to get to the bottom-line matter of any investment decision.

**Compensation and Performance:** The church board is usually responsible for hiring and monitoring the pastor as the chief executive officer. The church directors should understand the pastor's compensation package. This includes incentives, bonuses, perks and fringe benefits. Periodic performance reviews help demonstrate to a court that the board actively monitors the pastor's performance.

**Micromanaging Staff:** A board's chief role is to set policies, develop strategies and make fundamental decisions for the church. When a board micromanages the church's staff, the directors often lose focus on the big picture of guiding the church. This creates a duty of care risk for the board. The reasonable person standard suggests other directors in a like position may not be so focused on micro matters.

**Legal Compliance:** All organizations must comply with relevant laws. This includes churches. Some laws regulate employment, tax, traffic, and operational matters. A prudent church board understands the rules that apply to their institution and ensures a compliance program is in place to avoid violating the laws.

**Confidentiality:** All directors have an obligation to treat sensitive discussions with confidentiality. As board members, directors gain insight into delicate information about the church. Some matters concern privileged information about church families. Other matters involve corporate transactions and church business. Directors owe the church a duty to protect confidential information.

**Independence:** Church directors owe the church the duty to remain independent. This means directors should make decisions that are not unduly influenced by others, including other directors. Church officials' decisions should be made with the directors' judgment for what is best for the church.

**Conflicts of Interest:** A conflict of interest will get a director in hot water as quick as any action. When a director is perceived to have an ulterior motive or interest in a transaction that works against the best interest of the church, the director should disclose the conflict. Failure to self-disclose conflicts can lead to personal liability.

**The Consequences:** Church directors who violate their fiduciary duties may find themselves facing personal liability. This means a director's personal assets could be the subject of civil penalties and fines. Most protections directors enjoy against personal liabilities, such as insurance, indemnifications, and waivers, often evaporate when fiduciary duties are violated.

A church board should be diligent about its practices and conduct. This discipline will help improve the ministry. Moreover, adherence to good governance will protect everyone from negative publicity, financial damages and inefficiencies. ■



# Harmless?

All Contracts Look Harmless at First.

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CORPORATE GOVERNANCE | COMMERCIAL TRANSACTIONS | CONTRACT LAW

## Small Print Can Lead to Big Problems



Most contracts come with small print. This is the language that includes the underlying terms of the deal. Don't be misled by the size of the font. Small prints in contracts can make a big difference.

Some parties dismiss the importance of some contract terms. There are several misconceptions that cause one to treat some clauses less seriously.

Some believe the small print is a necessary formality in legal agreements and therefore should be accepted as inevitable. They figure all other parties had accepted the terms and therefore this should be normal. This is not always so.

Each party should be willing to negotiate all terms. Church leaders should be extra cautious when dealing with a party who refuses to discuss all aspects of the contract.

Some parties fail to recognize the small print. It may be thought so long as the main scope of work is properly spelled out, the deal is safe. Each term has potential consequences. Churches should understand these provisions are there for a reason. One should ask for the reason each clause exists.

A church leader may think that all small print applies to both parties equally. In many instances the fine print serves to protect the interests of the party who wrote the contract. If a church is presented a writing that was prepared by the other party's lawyer, treat the terms with healthy caution.

Small print can seem intimidating. Lawyers often use terms of art that have exact legal implications. While a church official may understand the common meaning of a phrase, the courts may apply a different standard. If there is any doubt about what a term means, church leaders should seek counsel to interpret small print.

A party often includes every conceivable outcome in the small print. This is because the party may have learned through experience to address various contingencies. This is why contracts are sometimes lengthy. This can be good for both parties if the terms are understood and agreed to by all. Church leaders should read the fine print carefully to make sure no detail is left unexamined.

Church leaders should think what could go wrong that would cause a legal dispute to arise. This exercise will help explain why some terms are included in the first place. Understanding the impact of each fine printed clause helps put the issue in context.

Small print create an understanding for the basic functions of the transaction. Some terms include who has responsibility for breaches. Delivery terms determine who accepts the liability for goods in transit that are being shipped. Other small print assign which court has jurisdiction over disputes and therefore the choice of laws that will be applied.

Finally, some small print may be incorporated by reference. This means there are other terms referenced in a separate document. Just because you don't see all the fine print does not necessarily mean other conditions do not apply.

Always ask to see all the terms that pertain to the deal. When in doubt, seek legal counsel to ensure you understand the small print. ■

*Legal Counsel for Churches* is a service provided by M Smith Law, PLLC for members of the religious community. This periodical is intended to help churches and their officials become better prepared to address important legal and governance issues. We hope you find *Legal Counsel for Churches* a valuable resource. For each issue, we try to raise relevant issues and offer some practical alternatives. We welcome your comments and input.

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