TIME TO FLIP THE TABLES: BOARD DIVERSITY AND THE FIDUCIARY DUTIES OF NONPROFIT DIRECTORS

Ellen E. Farwell[*]

A call for action to deconstruct structures of discrimination and oppression reverberates throughout U.S. society, including in the nonprofit sector. Nonprofit organizations, specifically their boards of directors, are being asked to reassess the diversity of their leadership (or lack thereof) and to consider whether satisfaction of their charitable missions is more likely when those boards reflect the communities served by such organizations. This Article describes the current state of diversity on nonprofit boards of directors, the impact on organizations when boards are more diverse, and approaches to increasing board diversity. The Article then articulates an argument that nonprofit directors fulfill their fiduciary duties by considering the potential impact of increased board diversity on their organization's ability to accomplish its mission and, where indicated, by diversifying their membership. In conclusion, the Article advocates, on the basis of those fiduciary duties, that state charity regulators should require nonprofit organizations to disclose how they consider diversity in their director selection processes and whether their boards reflect their communities and clients.

TABLE OF CONTENTS

* Faculty Fellow at New England Law | Boston; J.D., Boston College Law School; B.A., Columbia University. The author would like to thank Russell Engler, Gary Monserud, Richard Boskey, Eric Lustig, and Nick Smith for their insightful feedback on earlier drafts of this Article; New England Law Librarians Beth Armstrong and Barry Stearns for tracking down hard to find sources and bringing new ideas and approaches to my attention; the editors at Temple Law Review for their belief in the importance of this project and scrupulous attention to detail; and Addison Kennedy for her invaluable research assistance.

INTRODUCTION

"It is very tempting, when we finally make it to the table, to do everything we can to stay there. We think we are there to preserve our seat, instead of remembering we are there to use our seat."[1] This cautionary statement was made by soccer legend, author, nonprofit leader, and activist Abby Wambach in her May 2022 commencement address at Loyola Marymount University.[2] Though directed at the graduating students and the tables of power at which they may someday sit, the admonition is an apt description of the fiduciary duties of nonprofit boards with respect to board diversity and composition decisions.

Nonprofit charitable corporations are governed by boards of directors, the members of which are almost always volunteers with a deep commitment to the purpose of their organization, community leaders, and generous donors. Pursuant to their fiduciary duties, these directors are charged with using their seats to ensure that their organizations pursue a charitable mission for the benefit of the public.[3] New directors of nonprofit

---

1. Abby Wambach, *Commencement Speech at Loyola Marymount University* (May 7, 2022), https://youtu.be/CSH8geuu2UQ [https://perma.cc/3TDV-VZFR].

2. *Id.*

3. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 2.05 (AM. L. INST. 2022) ("A board . . . holds ultimate responsibility for the affairs of a charity. It has a duty to adopt policies to advance the purposes of the charity it governs and oversee implementation of those policies."); JAMES FISHMAN, STEPHEN SCHWARZ & LLOYD MAYER, NONPROFIT ORGANIZATIONS CASES AND MATERIALS 72 (6th ed. 2021) ("[T]hey must justify themselves on some level that society is benefitting from the philanthropic entity's operation . . . .").

corporations are generally nominated and then elected by existing board members.[4] This structure of self-perpetuating boards reflects the influence of charitable trust law on nonprofit corporate structures and the lack of direct interest holders (e.g., shareholders in business corporations).[5] In this way, nonprofit directors bear responsibility not only for the oversight of an organization's current activities but also for the membership of the organization's future board.[6]

Consistent with the fiduciary duty of care, boards look for new directors who have the expertise and experience that will enable effective oversight of the management and operations of an organization.[7] This expertise may include training and professional experience in the spheres in which the organization operates, general management and business experience, and, in some cases, personal experience as a recipient of services from that or a similar organization.[8] The capacity of a new board member to contribute financially and to connect the organization with other potential sources of funding is

---

4. MODEL NONPROFIT CORP. ACT § 804(b) (AM. BAR ASS'N 2021). While the directors of some nonprofit boards are elected or named by members or sit on a board ex officio based on their position within the organization or elsewhere, the focus of this Article is on self-perpetuating boards which nominate and elect their own successors. *See id.* § 804 cmt. 1.

5. *See* James J. Fishman, *The Development of Nonprofit Corporation Law and an Agenda for Reform*, 34 EMORY L.J. 617, 650–53, 677 (1985) [hereinafter Fishman, *Development*].

6. Copious advice and best practices for fulfilling this responsibility of self-perpetuation abound, with significant emphasis on the need to identify and address the specific needs of each organization. *E.g.*, *Finding the Right Board Members for Your Nonprofit*, NAT'L COUNCIL OF NONPROFITS, https://www.councilofnonprofits.org/tools-resources/finding-the-right-board-members-your-nonprofit [https://perma.cc/4BBX-Z2PF] (last visited Apr. 1, 2023); Lena Eisenstein, *Best Practices for Recruiting Nonprofit Board Members*, BOARDEFFECT (Aug. 16, 2019), https://www.boardeffect.com/blog/best-practices-recruiting-nonprofit-board-members/ [https://perma.cc/EX4E-QY55]; MCKINSEY & CO., NONPROFIT BOARD SELF ASSESSMENT TOOL – LONG FORM, https://www.northwestcf.org/sites/default/files/pdf/McKinsey%20Board%20Assessment%20Tool.pdf [https://perma.cc/52R4-3D3D] (last visited Apr. 1, 2023); COMMONWEALTH OF MASS., OFF. OF THE ATT'Y GEN., THE ATTORNEY GENERAL'S GUIDE FOR BOARD MEMBERS OF CHARITABLE ORGANIZATIONS 11–12 (2022), https://www.mass.gov/files/documents/2022/12/22/2022-12-20%20CHARITIES-GUIDANCE_PUB_V2.pdf [https://perma.cc/9PMT-BRR3].

7. *See* ABA COORDINATING COMM. ON NONPROFIT GOVERNANCE, GUIDE TO NONPROFIT CORPORATE GOVERNANCE IN THE WAKE OF SARBANES-OXLEY, Section III, Principle 1, B, 4 (2005) (describing question of whether "the board is composed of the right mix of individuals, including those who are sufficiently expert in areas applicable to the organization's operations and those whose participation achieves other important goals related to the mission of the organization. . . .") [hereinafter ABA POST-SARBANES-OXLEY GUIDE]. In many organizations, the emphasis on professional expertise to facilitate oversight means seeking board members with financial and legal expertise. *See* INDEP. SECTOR, PRINCIPLES FOR GOOD GOVERNANCE AND ETHICAL PRACTICE: A GUIDE FOR CHARITIES AND FOUNDATIONS 23 (2d ed. 2015) https://independentsector.org/programs/principles-for-good-governance-and-ethical-practice/#principles-anchor-2 [https://perma.cc/E6AG-393U] (explaining that board members should have "financial literacy" or "the ability to understand financial statements, to evaluate the bids of accounting firms.").

8. *See* Kelly LeRoux, *Paternalistic or Participatory Governance? Examining Opportunities for Client Participation in Nonprofit Social Service Organizations*, 69 PUB. ADMIN. REV. 504, 510 (2009) (exploring impact of government funding on client participation, including as members of the board of directors, in social welfare organizations); Julie I. Siciliano, *The Relationship of Board Member Diversity to Organizational Performance*, 15 J. BUS. ETHICS 1313, 1314 (1996) (describing study of occupational diversity of directors).

often a key attribute sought by organizations that rely on charitable contributions.[9] For some charities, the ability of directors to speak on behalf of the organization to legislators, regulators, and business leaders is a key characteristic that leads to the selection of prominent community leaders.[10] In limited cases, the characteristics or experiences of certain nonprofit directors are fixed by law as a condition of government funding or tax exemption.[11]

The various roles played by nonprofit directors create tension among priorities when selecting new board members. Recent public discourse and scholarship has broadened this conversation to query how the personal characteristics and identities of directors impact the efficacy of nonprofit boards.[12] A broader societal reckoning with the value (and in some spaces, paucity) of racial, gender, sexual orientation, and socioeconomic diversity has many nonprofit boards considering their own board composition in a new light.[13] Like their for-profit counterparts, nonprofit boards are asking whether increasing their own diversity is required—for business, moral, or legal reasons.

This Article posits that the compelling business and moral arguments for increasing board diversity, which have yet to drive meaningful change, are foundational to a robust legal argument that the fiduciary duties of nonprofit directors require that boards consider

9. LILLY FAMILY SCH. OF PHILANTHROPY, IND. UNIV., THE IMPACT OF DIVERSITY: UNDERSTANDING HOW NONPROFIT BOARD DIVERSITY AFFECTS PHILANTHROPY, LEADERSHIP, AND BOARD ENGAGEMENT 15 (2018), https://scholarworks.iupui.edu/bitstream/handle/1805/15239/board-diversity180220.pdf [https://perma.cc/9ZS4-YM57] [hereinafter LILLY REPORT].

10. *See id.* at 16.

11. For example, one-third of the directors of public interest legal organizations that receive funding through the federal Legal Services Corporation are required to be eligible as clients of the organization while at least 60% of the directors must be "attorneys who are members of the bar of a State in which the legal assistance is to be provided." 42 U.S.C. § 2996f(c). *See generally* Atinuke O. Adediran, *Nonprofit Board Composition*, 83 OHIO ST. L.J. 357, 391–92 (2022) (comparing the requirements of LSC and non-LSC-funded Public Interest Legal Organizations (PILOs)) [hereinafter Adediran, *Board Composition*]. As a condition of tax exemption, since 1969, the Internal Revenue Service has expected that hospitals maintain a board composed of community members rather than of physicians practicing at the hospital. Rev. Rul. 69-545, 1969-2 C.B. 117. The purpose behind this requirement is to limit the likelihood of self-dealing between the tax-exempt charitable hospital and its directors. *See id.*

12. While this Article focuses largely on arguments and evidence from the last two decades, the demand for more diverse leadership of nonprofit organizations is in no way a creation of this century. *See, e.g.*, Faith R. Rivers, *Bridging the Black-Green-White Divide: The Impact of Diversity in Environmental Nonprofit Organizations*, 33 WM. & MARY ENV'T L. & POL'Y REV. 449, 474–76 (2009) (describing the demand in 1990 by environmental justice organizations that major conservation and environmental groups, like the Sierra Club and the Environmental Defense Fund, increase the diversity of their employees) [hereinafter Rivers, *Divide*].

13. *See, e.g.*, Aly Kassam-Remtulla, *Nonprofits Need To Catch Up on Diversifying Their Boards*, CHI. TRIB. (Jan. 29, 2021, 2:56PM), https://www.chicagotribune.com/opinion/commentary/ct-opinion-nonprofit-boards-diversity-20210129-qtmmdsnhv5as3p3mylc5lbl4ae-story.html [https://perma.cc/C44K-26BC]; Anastasia Reesa Tomkin, *How White People Conquered the Nonprofit Industry*, NONPROFIT Q., (May 26, 2020), https://nonprofitquarterly.org/how-white-people-conquered-the-nonprofit-industry/ [https://perma.cc/W6K9-UBTQ]; James Canales & Barbara Hostetter, *To Advance Racial Equity, Foundation Boards Need To Take an Active Rol*e, CHRON. OF PHILANTHROPY (Jan. 13, 2021), https://www.philanthropy.com/article/to-advance-racial-equity-foundation-boards-need-to-take-an-active-role [https://perma.cc/Y8TT-VPRN].

and, in some cases, take action to increase their own diversity.[14] For purposes of this Article, diversity is intended to mean the inclusion and participation of individuals from groups that have been historically underrepresented within nonprofit boards. Diverse board members might include, without limitation, women, Black people, indigenous people, people of color, LGBTQ+ people, young people, immigrants, people with less formal education, people with disabilities, and people who have lower incomes. The beneficiaries, or clients,[15] and other stakeholders of each nonprofit organization vary based on its charitable purpose, programs, and location. For this reason, this Article does not advocate for the increase of board diversity in any one dimension but instead argues that each board of directors is responsible for considering the forms of increased diversity that could promote its particular mission.

Section I of this Article describes the current state of nonprofit board diversity. Section II outlines three rationales for increasing diversity among nonprofit boards of directors. This Section examines how the arguments and evidence relating to diversity within for-profit businesses can bolster the case for nonprofits, and ways in which board diversity is specifically relevant for nonprofits. Section III examines existing tools for influencing nonprofit board governance and board diversity, including moral persuasion, oversight by the Internal Revenue Service (IRS), state corporate law structuring requirements, and the fiduciary standards to which nonprofit directors are held. Section IV explores the intersection of nonprofit fiduciary duties and the mounting evidence of the meaningful impact of diversity within an organization's leadership. Part IV.A argues that nonprofit boards satisfy their fiduciary duties by considering the possible benefits of diversifying their membership. Part IV.B argues that when a board concludes that greater diversity will further its organization's charitable purposes, directors have a duty to act on that knowledge. The Article then concludes with the policy suggestion that state charity regulators should encourage and monitor compliance with a board's fiduciary duty to consider and embrace diversity through existing state education and disclosure systems.

---

14. Merely increasing the percentage of nonprofit board members who are members of historically underrepresented communities, without meaningful efforts to function in more equitable and inclusive ways, is unlikely to have the desired impacts. *See, e.g.*, MOLLY DELANO BRENNAN & MIECHA RANEA FORBES, KOYA LEADERSHIP PARTNERS, THE GOVERNANCE GAP: EXAMINING DIVERSITY AND EQUITY ON NONPROFIT BOARDS OF DIRECTORS 7 (2019) https://koyapartners.com/wp-content/uploads/2018/12/KOYA_GovernanceGap_FINAL.pdf [https://perma.cc/KMK4-TLNS]; Elizabeth A. Castillo, *Why Are We Still Struggling with Diversity, Equity, and Inclusion in Nonprofit Governance?*, NONPROFIT Q. (Nov. 18, 2018) https://nonprofitquarterly.org/why-are-we-still-struggling-with-diversity-equity-and-inclusion-in-nonprofit-governance/ [https://perma.cc/Y6BT-L92H] (reflecting on a 2018 panel convened by the Association for Research on Nonprofit Organizations and Voluntary Action and stating that "[I]t is not enough to enact change. We must also prepare people and organizations for such major culture shifts."). Arguably any decision made by a nonprofit board, including its policies and practices regarding inclusion of directors, are fiduciary actions. This Article, however, limits its exploration of director fiduciary duties to the recruitment and election of new board members.

15. The term "beneficiary" relates to the grounding of nonprofit law in trust law, but it can carry with it a tone of paternalism. For this reason, many nonprofits prefer to use the term client to refer to those they serve. For purposes of this Article, beneficiaries are defined as those individuals or groups that constitute the charitable class to be served by a charitable organization, and clients are defined as those individuals who are in fact served by a charitable organization.

I. Setting the Table: Board Diversity at Nonprofit Board Tables and Why It Matters

A. Who is Sitting at the Table Today?

The nonprofit sector in the United States constitutes 5.6% of the nation's economy,[16] employs over 12.3 million people,[17] and is the backbone of our society's health care, higher education, arts, elder care, low-income housing, and conservation efforts. BoardSource, a preeminent nonprofit research and support organization, explains that "[t]he individual leaders who compose nonprofit boards reflect an organization's values and beliefs about who should be empowered and entrusted with its most important decisions."[18] This lens, combined with the ubiquitous impact of nonprofits, makes it essential to understand who is sitting (or not sitting) in nonprofit board seats.

In 2019, 78% of directors of nonprofit public charity boards were white[19] while only 60.1% of the population was white.[20] This discouraging statistic reflects minimal change over twenty-five years.[21] Between 1994 and 2015, despite a significant increase in the articulation of board diversity as a priority, the percentage of white nonprofit directors oscillated between 82–91% without consistent downward progress.[22] Certain racial and ethnic groups are particularly underrepresented, and a significant number of organizations lack racial diversity. For example, although Latino and Hispanic

16. *National Income and Products Accounts: Table 1.3.5. Gross Value Added by Sector*, BUREAU OF ECON. ANALYSIS, https://apps.bea.gov/iTable/?reqid=19&step=2&isuri=1&categories=survey#eyJhcHBpZCI6MTksInN0ZXBzIjpbMSwyLDNdLCJkYXRhIjpbWyJjYXRlZ29yaWVzIiwiU3VydmV5Il0sWyJOSVBBX1RhYmxlX0xpc3QiLCIyNCJdXX0= [https://perma.cc/2XJ7-ZYEB] (last visited Apr. 1, 2023) (indicating that in 2021, nonprofit institutions, excluding organizations serving governments or businesses, contributed approximately $5.2 billion to the approximately $92 billion gross domestic product).

17. NAT'L COUNCIL OF NONPROFITS, NONPROFIT IMPACT MATTERS: HOW AMERICA'S CHARITABLE NONPROFITS STRENGTHEN COMMUNITIES AND IMPROVE LIVES 1 (2019). For example, in Massachusetts, nonprofit organizations employ approximately 17% of the workforce. INDEP. SECTOR, THE NONPROFIT SECTOR IN MASSACHUSETTS, https://independentsector.org/wp-content/uploads/2016/12/Massachusetts-2019.pdf [https://perma.cc/2NEZ-NBSZ].

18. BOARDSOURCE, LEADING WITH INTENT: BOARDSOURCE INDEX OF NONPROFIT BOARD PRACTICES 29 (2021), https://leadingwithintent.org/wp-content/uploads/2021/06/2021-Leading-with-Intent-Report.pdf? [https://perma.cc/PPF4-ZQB6] [hereinafter LEADING WITH INTENT 2021].

19. *Id.* at 28. This number reflects the number of board members who identify as white/Caucasian/European. In its tenth version since 1994, LEADING WITH INTENT 2021 reflects information from over 800 nonprofit executives and board chairs representing a broad cross-section of nonprofits in terms of annual revenues, geographic area, and mission focus. *Id.* at 6–7. The 2021 LEADING WITH INTENT REPORT is based on surveys completed between April 23, 2019 and June 25, 2019. *Id.* at 7.

20. *See National Population by Characteristics: 2010-2019*, CENSUS BUREAU https://www.census.gov/data/tables/time-series/demo/popest/2010s-national-detail.html [https://perma.cc/6543-RATP] (Table on Sex, Race and Hispanic Origin) (last visited Apr. 1, 2023). This number reflects the percentage of residents who identify as white and non-Hispanic.

21. *See* Kassam-Remtulla, *supra* note 13.

22. BOARDSOURCE, LEADING WITH INTENT: 2017 NATIONAL INDEX OF NONPROFIT BOARD PRACTICES 12 & n.7 (2017), https://leadingwithintent.org/wp-content/uploads/2017/11/LWI-2017.pdf [https://perma.cc/WD6C-9CSN] [hereinafter LEADING WITH INTENT 2017].

individuals constituted 18.5% of the U.S. population in 2019,[23] they filled only 5% of nonprofit board seats.[24] In a 2017 report, BoardSource noted that 27% of organizations they surveyed had an entirely white board.[25] In a 2007 report on more than five thousand nonprofits, among organizations whose clientele were over 50% Hispanic/Latino, approximately one-third had no Hispanic or Latino directors.[26] And, of course, these national statistics do not reflect variation among organizations in different geographic areas or boards of varying sizes.[27]

When considered at the sector-wide level, women have achieved representation on nonprofit boards that is in line with their percentage in the U.S. population. In a 2017 analysis by the Lilly Family School of Philanthropy at Indiana University, women filled 47% of nonprofit board seats, only slightly below their representation in the population of 50.8%.[28] In 2019, BoardSource reported that gender representation had flipped with 53% of directors identifying as women while the percentage of women in the population remained nearly steady.[29] This seemingly significant increase is complicated by the fact that greater numbers of women tend to serve on the entirely volunteer boards of smaller, nonprofits. Women remain underrepresented on boards of larger, more complex nonprofits, which tend to still be predominantly composed of men.[30]

Data regarding other forms of board member diversity is often more difficult to confirm and has not been tracked for as long. In 2019, BoardSource reported that 6% of nonprofit directors identify as gay, lesbian, or bisexual and that 5% identify as having a disability.[31] Scarcer still is information about director socioeconomic status, despite the

---

23. *See* Census Bureau, *supra* note 20. A similarly wide gap exists in the representation of Latinos on for-profit boards. Jeff Green, '*Sea of White': Latino Leaders Fight To Reshape U.S. Boardrooms*, BLOOMBERG (Mar. 22, 2022, 3:35PM EDT), https://www.bloomberg.com/news/articles/2022-03-22/-sea-of-white-latino-leaders-fight-to-reshape-u-s-boardrooms [https://perma.cc/DE7W-C5QH].

24. LEADING WITH INTENT 2021, *supra* note 18, at 28.

25. LEADING WITH INTENT 2017, *supra* note 22, at 12.

26. FRANCIE OSTROWER, THE URB. INST., NONPROFIT GOVERNANCE IN THE UNITED STATES—FINDINGS ON PERFORMANCE AND ACCOUNTABILITY FROM THE FIRST NATIONAL REPRESENTATIVE STUDY 18 (2007), https://webarchive.urban.org/UploadedPDF/411479_Nonprofit_Governance.pdf [https://perma.cc/3VY2-YNFQ].

27. For example, a study of the composition of nonprofit boards and leaders in New York City reported that 64.7% of board members were Caucasian (despite constituting only 31.8% of the city residents). NYC SERV. & NONPROFIT COORDINATING COMM. OF N.Y.C., WHAT LIES BENEATH: THE STATE OF NYC NONPROFIT BOARD DIVERSITY, EQUITY AND INCLUSION 9 (2018) [hereinafter NYC BOARD DIVERSITY].

28. LILLY REPORT, *supra* note 9, at 11.

29. LEADING WITH INTENT 2021, *supra* note 18, at 28.

30. THE WHITE HOUSE PROJECT, BENCHMARKING WOMEN'S LEADERSHIP 79 (2009) (noting that while women made up 43% of nonprofit board members nationwide in the mid-2000s, the average percentage of women on boards of organizations with greater than a $25 million budget was 33%).

31. LEADING WITH INTENT 2021, *supra* note 18, at 28. Estimates of the number of adults in the U.S. who are gay, lesbian, bisexual or transgender range from 4.5% to as high as 8%. *Compare* Kerith J. Conron & Shoshana K. Goldberg, UCLA SCH. OF L. WILLIAMS INST., *Adult LGBT Population in the United States, Fact Sheet,* 1 (June 2020), https://williamsinstitute.law.ucla.edu/wp-content/uploads/LGBT-Adult-US-Pop-Jul-2020.pdf [https://perma.cc/9CRE-U826], *with* Laura Powell, HUM. RTS. CAMPAIGN FOUND., *We Are Here: Understanding the Size of the LGBTQ+ Community* (Dec. 9, 2021), https://www.hrc.org/press-releases/

majority of nonprofit board chairs and CEOs believing this type of diversity is important to their board's ability to provide strategic leadership to the organization.[32]

The specific composition of each nonprofit board should vary based on its mission and needs. Yet, taken as a whole, it is clear that many (perhaps most) nonprofit boards do not represent the multitude of diversity of the communities in which they operate, nor those who they intend to benefit.

B. Why It Matters Who Has a Seat at the Table

Nonprofit directors hold vital leadership roles in a sector that touches the lives of most, if not all, Americans. Many nonprofit charitable organizations serve the traditional, charitable purposes of providing "relief of the poor."[33] Yet, nonprofit health-care and educational organizations, the largest charities in many areas, serve much broader classes of beneficiaries.[34] The wide-reaching influence of nonprofit charities and their directors raises two questions: who are the right people to serve as directors, and what perspectives and experiences do they bring to the board table?

Nonprofit corporations, like for-profit business corporations, are governed by a board of directors.[35] The directors of a business corporation are elected by its shareholders, each of whom holds a financial interest in the corporation and its net assets on dissolution.[36] This relationship between directors and shareholders forms the basis of the traditional doctrine of shareholder primacy, which holds that directors' actions should be aimed at increasing shareholder wealth.[37] As such, directors of for-profit corporations are expected to act in the best interest of the entity and its owners.[38] In contrast, public charities do not have shareholders or owners.[39] Under the foundational doctrine of the

---

we-are-here-lgbtq-adult-population-in-united-states-reaches-at-least-20-million-according-to-human-rights-campaign-foundation-report [https://perma.cc/QA7V-UM86].

32. *See, e.g.*, NYC BOARD DIVERSITY, *supra* note 27, at 26; LEADING WITH INTENT 2021, *supra* note 18, at 51.

33. Treas. Reg. § 1.501(c)(3)-1(d)(2) (as amended in 2017).

34. According to a 2019 Urban Institute report, health care and educational organizations generated 76.5% of the total revenue of public charities. URB. INST., *The Nonprofit Sector in Brief 2019* tbl. 2 (2020), https://nccs.urban.org/publication/nonprofit-sector-brief-2019#type [https://perma.cc/8Z59-AAMX].

35. MODEL NONPROFIT CORP. ACT § 801 (AM. BAR ASS'N 2021).

36. MODEL BUS. CORP. ACT, §§ 6.40, 8.03(c), 14.01(5) (AM. BAR ASS'N., amended 2016).

37. Thomas Lee Hazen, *Diversity on Corporate Boards: Limits of the Business Case and the Connection Between Supporting Rationales and the Appropriate Response of the Law*, 89 N.C. L. REV. 887, 889 (2011) [hereinafter Hazen, *Limits*] (describing Milton Friedman's "belief that corporations have no social responsibility beyond making money for their shareholders"). While the doctrine of shareholder primacy remains a significant concept in corporate law, the notion that a corporation's directors may not consider the interests of any other stakeholders has arguably been eroded with a suggestion that "corporate citizenship" may allow the interests of multiple constituencies to be relevant in board decisions. *See* KENT GREENFIELD, *More Personhood Please*, *in* CORPORATIONS ARE PEOPLE TOO 175, 179–83 (2018).

38. *See* Mary Parmeter, *The Fiduciary Duty to Gender Diversity within Corporate Boards: The Necessary Link Among Shareholder Primacy, The Director Nomination Process and Higher Financial Return*, 32 WIS. J. L. GENDER & SOC'Y 85, 98–100 (2017).

39. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 1.01(a) & cmt. f (AM. L. INST. 2022); MODEL NONPROFIT CORP. ACT, Forward to the Fourth Edition §6 (AM. BAR ASS'N 2021) ("For example, recognizing that nonprofit corporations differ from for profit corporations in that nonprofit corporations do not

nondistribution constraint, charitable nonprofits are precluded from having interest holders who exercise control and personally benefit from the organization's work.[40] Instead, a public charity and its board are expected to operate for the public good and in furtherance of the organization's specified charitable mission.[41] This distinction necessitates that nonprofits more explicitly address the interests of multiple constituencies.

Mounting empirical evidence suggests, at a minimum, a correlation between more diverse governing boards and greater financial success.[42] But the difficulties in identifying causation between board diversity and financial results challenge a purely business-based argument for board diversity.[43] For nonprofits, the business argument is further complicated by the multitude of potential indicators of success beyond mere financial performance.[44] Recent state law changes, along with the actions of the National Association of Securities Dealers Automated Quotations (Nasdaq) and the Securities and Exchange Commission (SEC), have pushed the question of for-profit board diversity to the forefront with mounting disclosure and board membership requirements being adopted or considered across the country.[45] To date, the federal government has not adopted similar requirements for nonprofit corporations, something that only a few states have opted to do[46] Similarly, claims that a lack of board diversity reflects a breach of fiduciary duties have been largely confined to the for-profit sphere (and, as of the writing of this Article, have been unsuccessful).[47] Moral or normative arguments for increasing the diversity of leaders at the board table and throughout society are based on concepts

have shareholders, the Fourth Edition continues to permit nonprofit corporations to have—or not to have—members . . . .").

40. *See* Henry Hansmann, *The Role of Nonprofit Enterprise*, 89 YALE L. J. 837, 838–39 (1980); ABA NONPROFIT ORG. COMM., GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS 6 (Willard L. Boyd & Jeannie Carmedelle Frey, eds., 3rd ed. 2012) [hereinafter ABA GUIDEBOOK].

41. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 1.01 (AM. L. INST. 2022).

42. *See* discussion *infra* Part II.A.

43. *See* discussion *infra* Part II.A.

44. Nonprofits routinely grapple with the challenge of measuring nonfinancial outcomes in reporting to funders and seeking support. Unlike financial indicators of for-profit businesses, how nonprofits measure their success depends greatly on their specific mission, community, and the demands of donors. As such, the evolving tools for correlating financial success with board diversity in the for-profit sector may be ill-adapted to measures of nonprofit achievements. The work of Professor Brian Feinstein and his colleagues at Wharton identifying a correlation between the diversity of Federal Reserve Bank boards and higher Community Reinvestment Act scores as a reflection of lending in underserved communities suggests a possible route for analyzing the performance of nonprofit organizations that operate in a federated model across the country. *See* Brian D. Feinstein, Peter Conti-Brown & Kaleb Nygaard, *Board Diversity Matters: An Empirical Assessment of Community Lending at Federal Reserve-Regulated Banks* (Yale Program on Financial Stability, working paper forthcoming), https://ssrn.com/abstract=4000110 [https://perma.cc/VL6L-RPEY].

45. *See* discussion *infra* Part III.C.

46. *See, e.g.*, Gender Diversity in the Boardroom – Annual Report, H.B. 1116, 2019 Leg., 439th Gen. Assemb., Reg. Sess. (Md. 2019) (requiring corporations, including nonprofits with annual budgets of $5 million or more, to report the number of women on their board on their personal property tax filing).

47. *See, e.g.*, Ocegueda *ex rel*. Facebook v. Zuckerberg, 526 F. Supp. 3d 637, 644, 647 (N.D. Cal. 2021); Klein v. Ellison, No. 20-cv-04439, 2021 WL 2075591 (N.D. Cal. May 24, 2021). *See generally* Chris Brummer & Leo E. Strine, Jr., *Duty and Diversity*, 75 VAND. L. REV. 1, 84–85 (2022).

of equity, fairness, and representation.[48] While compelling to many, including this author, moral arguments alone have shown throughout history to be inadequate in breaking down structures of power.

II. Arguments for Increasing Nonprofit Board Diversity

Questions about the lack of diversity among nonprofit directors are decades old.[49] Arguments in favor of increasing the diversity of nonprofit boards can largely be categorized as performance- or equity-based.[50] Performance-based arguments link the capacity of a nonprofit to achieve its goals with a diverse group of leaders overseeing and driving the organization's financial stability and progress.[51] Such arguments point to the unique objectives of public charities as compelling director diversity for both the economic bottom-line reasons articulated in the context of for-profit businesses and for reasons tied to the particular purposes of public charities. Legal and organizational scholars have long made quantitative and qualitative performance-based arguments for board diversity.[52] Accepting the multiplicity of nonprofit stakeholders and the various measures of success they might apply, one baseline measure of nonprofit performance is financial success and sustainability.[53] In this way, nonprofits are similar to their for-profit

48. *See* discussion *infra* Part II.C.

49. LEADING WITH INTENT 2017, *supra* note 22, at 12; FLOYD MILLS, COUNCIL ON FOUNDS., THE STATE OF CHANGE: AN ANALYSIS OF WOMEN AND PEOPLE OF COLOR IN THE PHILANTHROPIC SECTOR 6 (2017), https://cof.org/sites/default/files/documents/files/2017-Gender-Diversity-Report.pdf [https://perma.cc/A4GN-Y8VK] ("The conversation about diversity in philanthropy is not a new one. Over the past two decades in particular, numerous actors, working both field-wide and at the level of individual organizations, have waded into the debate. . . ."). Scholarship and advocacy relating to the lack of racial, ethnic, or religious diversity on for-profit boards first developed in the middle of the twentieth century. *See* Richard W. Painter, *Board Diversity: A Response to Professor Fried*, 22 STAN. J. L. BUS. & FIN. 173, 212 n.134 (2022) (citing WILLIAM DOMHOFF, WHO RULES AMERICA (1st ed. 1967)). *See generally* Donald Schwartz, *Proxy Power and Social Goals—How Campaign GM Succeeded*, 45 ST. JOHN'S L. REV. 764 (1971) (describing shareholder campaign to pressure General Motors to increase the perspectives of its board of directors and to address other public policy issues).

50. *See* Lisa M. Fairfax, *Board Diversity Revisited: New Rationale, Same Old Story*, 89 N.C. L. REV. 856, 855–857 (2011) [hereinafter Fairfax, *Board Diversity Revisited*] (describing the beliefs driving a shift from moral and social rationales for diversity to business and economic based rationales); Deborah L. Rhode & Amanda K. Packel, *Diversity on Corporate Boards: How Much Difference Does Difference Make*, 39 DEL. J. CORP. L. 377, 382–83 (2014); Geeta Tewari, Emma DeCourcy & Shirley Urena, *The Ethics of Gender Narratives for United States Corporate Boards*, 16 N.Y.U. J. L. & BUS., 221, 245 (2019).

51. *See, e.g.*, Siciliano, *supra* note 8 at 1314–15; Erica E. Harris, *The Impact of Board Diversity and Expertise on Nonprofit Performance*, 25 NONPROFIT MGMT. & LEADERSHIP 113, 119 (2014).

52. *See, e.g.*, Hazen, *Limits*, *supra* note 37, at 888; Yilmaz Arguden, *Why Boards Need More Women*, HARV. BUS. REV. (June 7, 2012), https://hbr.org/2012/06/why-boards-need-more-women [https://perma.cc/JMM3-GZM6] (finding higher share prices and operational performance in companies with boards with a greater percentage of women directors).

53. A common refrain among nonprofit organizations, "no margin, no mission" was coined by Sister Irene Kraus, Chief Executive Office of the Daughters of Charity National Health System. Under her leadership in the early 1990s, the Daughters of Charity system was the largest private, nonprofit hospital chain in the country. John Paul Newport, *Health Care; Mission + Margin: The Nun as CEO*, N.Y. TIMES (June 9, 1991), https://www.nytimes.com/1991/06/09/magazine/health-care-mission-margin-the-nun-as-ceo.html [https://perma.cc/83CL-8RL8].

business counterparts. As such, the discussions around whether diverse for-profit boards lead to better financial performance serve as a reasonable starting point when considering nonprofit board diversity. Yet, financial success is not the paramount objective of nonprofit charities. Accordingly, any assessment of the impact of board diversity must consider the ability of nonprofits to succeed in fulfilling their charitable purposes.[54] Without ignoring or diminishing the value of financial stability and achieving a nonprofit's articulated charitable purposes, equity-based arguments in favor of greater board diversity focus on addressing more far-reaching societal aims such as equality, self-determination, and dismantling racial and gender oppression.

A. Financial Performance & Sustainability

Management consultants, institutional investors, and scholars have all identified a correlation, at least, between the financial performance of a company and the diversity of its board of directors.[55] For example, in 2020, McKinsey & Company reported that companies with the greatest gender diversity had an increased likelihood of above-average profitability.[56] Based on similar observations, institutional investors and underwriters have articulated an expectation that potential investees and companies seeking to go public have boards with racial and gender diversity.[57] For example, in 2018, BlackRock publicly announced an expectation that companies in which it invested would have at least two female directors.[58] It followed this announcement with direct communication to the almost one-third of Russell 1000 companies that did not meet that criteria, explaining that the company "believe[s] that a lack of diversity on the board

---

54. *See* Harris, *supra* note 51.

55. *E.g.,* Brummer & Strine, *supra* note 47, at 88 ("[T]here is, at a minimum, a rational basis for business leaders to conclude that effective DEI policies will help them create and sustain smart, thoughtful, resilient, respected and thus sustainably profitable corporations . . . . [T]here is a basis to infer that inattention and insensitivity to important DEI issues bearing on corporate relationships with employees, customers and business partners is what risks firm value in the twenty-first-century economy."); Lisa M. Fairfax, *The Bottom Line on Board Diversity: A Cost-Benefit Analysis of the Business Rationales for Diversity on Corporate Boards*, 2005 WIS. L. REV. 795, 811; Parmeter, *supra* note 38, at 87–89 ("Boardroom homogeneity or near-homogeneity with a 'token' female board member is a poor economic strategy for corporate boards in terms of financial return and company performance.").

56. SUNDIATU DIXON-FYLE, KEVIN DOLAN, DAME VIVIAN HUNT & SARA PRINCE, MCKINSEY & CO., DIVERSITY WINS: HOW INCLUSION MATTERS, 13–14 (May 19, 2020), https://www.mckinsey.com/featured-insights/diversity-and-inclusion/diversity-wins-how-inclusion-matters [https://perma.cc/U3T6-T5J9].

57. *See, e.g.*, *Goldman's Playbook for More Diverse Corporate Boards*, N.Y. TIMES (Jan. 24, 2020), https://www.nytimes.com/2020/01/24/business/dealbook/goldman-diversity-boardroom.html [https://perma.cc/NRR7-DRH7]; Anthony Goodman & Rusty O'Kelley, *Institutional Investors Lead Push for Gender-Diverse Boards*, HARV. L. SCH. F. CORP. GOVERNANCE (Apr. 26, 2017), https://corpgov.law.harvard.edu/2017/04/26/institutional-investors-lead-push-for-gender-diverse-boards/ [https://perma.cc/K9BC-BCQL] (explaining that, in 2017, State Street demanded that companies with less than 15% of director seats filled by women take meaningful action to increase gender diversity or risk State Street voting against their directors).

58. Sarah Krouse, *BlackRock: Companies Should Have at Least Two Female Directors*, WALL ST. J. (Feb. 2, 2018) https://www.wsj.com/articles/blackrock-companies-should-have-at-least-two-female-directors-1517598407 [https://perma.cc/5LLE-VKAB].

undermines its ability to make effective strategic decisions. That, in turn, inhibits the company's capacity for long-term growth."[59]

The argument for increasing for-profit company board diversity based on financial performance is not without its critics or limits.[60] While numerous studies have shown a correlation between a greater number of women on a board and increased profitability, some studies find no effect or instead a negative impact on profitability when company boards are more diverse.[61] This lack of clarity, no doubt, in part stems from the fact that some organizations increase the diversity of their boards without adopting policies and practices that facilitate the genuine inclusion of such directors.[62] Importantly, there is also a persistent question about whether board diversity causes, or is merely correlated with, improved performance.[63]

For nonprofit organizations, while financial performance is but one indicator of success, it is nevertheless key.[64] Financial performance allows for the pursuit of an

---

59. *Id.*

60. *See, e.g.*, Jesse M. Fried, *Will NASDAQ's Diversity Rules Harm Investors*, (Eur. Corp. Governance Inst., Working Paper No. 579, 2021), http://ssrn.com/abstract_id=3812642 [https://perma.cc/F9B9-UJKH]; Rhode & Packel, *supra* note 50, at 390.

61. *See, e.g.*, Marcus Noland, Tyler Moran & Barbara Kotschwar, *Is Gender Diversity Profitable? Evidence from a Global Survey* 7 (Peterson Inst. for Int'l Econ., Working Paper No. 16-3, 2016), https://www.piie.com/sites/default/files/documents/wp16-3.pdf [https://perma.cc/W272-UYL8] (describing that the appearance of increased profitability for company boards with higher percentages of female directors becomes statistically insignificant when considering only profitable companies or net margins); Frank Dobbin & Jiwook Jung, *Corporate Board Gender Diversity and Stock Performance: The Competence Gap or Institutional Investor Bias?*, 89 N.C. L. REV. 809, 817–20 (2011); Katharine T. Bartlett, *Showcasing: The Positive Spin*, 89 N.C. L. REV. 1055, 1077–78 (2011). As described by Professor James A. Fanto and his colleagues, the lack of definitive empirical evidence about the impact of for-profit board diversity on company performance mirrors similar evidence about other features of board structure and composition. James A. Fanto, Lawrence M. Solan & John M. Darley, *Justifying Board Diversity*, 89 N.C. L. REV. 901, 918 (2011).

62. *See* Robin J. Ely & David A. Thomas, *Getting Serious About Diversity: Enough Already with the Business Case*, HARV. BUS. REV., Nov.-Dec. 2020, https://hbr.org/2020/11/getting-serious-about-diversity-enough-already-with-the-business-case [https://perma.cc/AK5Y-7CQM] (last visited Apr. 1, 2023) (explaining that "increasing demographic diversity does not, by itself, increase effectiveness; what matters is how an organization harnesses diversity, and whether it's willing to reshape its power structure").

63. *See* Sonja S. Carlson, *"Women Directors": A Term of Art Showcasing the Need for Meaningful Gender Diversity on Corporate Boards*, 11 SEATTLE J. SOC. JUST. 337, 347 (2012) (referring to empirical evidence that makes a "colorable case for a causal relationship"); Sunitha Malepati, *The Future (Public Company Boardroom) is Female: From California SB 826 to a Gender Diversity Listing Standard*, 28 AM. U. J. GENDER, SOC. POL'Y & L. 493, 519 (2020) (referencing studies showing that "more gender-diverse boards in particular outperform predominantly male boards on a range of board functions and corporate performance indicators"). While some studies indicate a causal relationship, others question this relationship. *See, e.g.*, Harris, *supra* note 51, at 127 (highlighting that findings relating board diversity and performance should be "interpreted as associations and not causal relationships" because of the possibility that "directors with specific characteristics are drawn to better performing firms" rather than being the cause of such performance). The persistence of this question, and its importance in considering whether a for-profit board is acting in accordance with the shareholder primacy rule, suggests that further research and the evolution of innovative approaches to identifying the relationship between financial performance and board diversity will continue.

64. For example, a nonprofit's access to credit depends on its financial stability. Large nonprofits, like hospitals, universities, and housing organizations, depend greatly on their creditworthiness in accessing the tax-exempt bond market to enable capital growth. *See* Off. of State & Cmty. Energy Programs, Dep't of Energy,

organization's mission and encourages greater donor support.[65] While there is less research linking nonprofit board diversity and financial performance,[66] a reasonable connection can be drawn between evolving evidence of the impact of board diversity on for-profit financial performance and the likely impact on nonprofit financial performance and sustainability.

B. Mission Performance

Individual donors, foundation grant makers, and bond holders certainly watch a nonprofit's financial performance. But some of those stakeholders—an organization's clients, the general public, and state and federal regulators—are all primarily concerned with an organization's fulfillment of its charitable mission. In contrast with for-profit companies where financial performance is generally (and necessarily) an indicator of success, for public charities, the effective fulfillment of charitable purposes is an even more important indicator. Beneficiaries gain little if an organization limits or reduces its provision of services for the narrow purpose of improving financial results.

As a baseline, achievement of a nonprofit's mission may be measured quantitatively—clients served, acres preserved, research supported, and students educated. Based on the demands of donors and the desire of nonprofit leaders to ensure that they are achieving their charitable objectives, the sector abounds with tools for measuring efficacy and results.[67] But performing on mission looks qualitatively different for each nonprofit. As such, success must be defined in a more nuanced way that incorporates the mission of each organization, which in turn is determined by the very board of directors charged with ensuring its fulfillment.

The circularity in the definition and assessment of success raises the stakes in terms of who sits at the board table, because those with a voice in setting the direction also oversee its implementation. The parameters for success can only be as focused as the view of those setting them.[68] For example, Professor Rivers James identifies a connection between the lack of diversity on the boards of traditional environmental organizations and the detrimental impact of these organizations on communities of color that are most impacted by environmental discrimination.[69] Conversely, in the context of

---

Tax-Exempt Bond Financing for Nonprofit Organizations and Industries, ENERGY.GOV, https://www.energy.gov/scep/tax-exempt-bond-financing-nonprofit-organizations-and-industries [https://perma.cc/V6JR-L6GL] (last visited Apr. 1, 2023).

65. *See generally* HOW TO RESEARCH A NONPROFIT'S FINANCIAL STRENGTH—DEEP-DIVE APPROACH, THE BRIDGESPAN GRP., https://www.bridgespan.org/getmedia/3bdafb57-eda7-44f2-bcf5-e8b6998da565/Donor-Decision-Tool-Researching-a-Nonprofits-Financials-Deep-Dive.pdf [https://perma.cc/NE8G-H2SD] (last visited Apr. 1, 2023).

66. *See* Harris, *supra* note 51, at 113 (noting a "paucity of research relating nonprofit directors to success").

67. *See, e.g.*, John Sawhill & David Williamson, *Measuring What Matters in Nonprofits*, MCKINSEY Q. (May 1, 2001), https://www.mckinsey.com/industries/public-and-social-sector/our-insights/measuring-what-matters-in-nonprofits [https://perma.cc/S3Z7-R39W].

68. Siciliano, *supra* note 8, at 1318 (describing how diverse YMCA boards of directors focused more meaningfully on their organizations' missions).

69. *See* Rivers, *Divide*, *supra* note 12, at 478–80.

public interest legal organizations, Professor Adediran argues that when organizations include clients on their boards they are better equipped to "craft more effective policies and services" and "point out opportunities for improvement."[70] Such organizations are also better situated to recruit and retain paid executive leaders who themselves bring diverse lived experiences to their work and leadership.[71]

The impact of board diversity manifests in how the board itself functions.[72] According to a 2016 study on the connection between nonprofit board diversity and the adoption of effective governance practices, more diverse boards are more likely to engage in effective governance practices, like adopting policies and procedures that promote a sense of shared purpose for collective action.[73] Effective governance practices encourage and facilitate robust and engaged decisionmaking.[74] Specifically, these practices encourage engagement and the challenging of assumptions.[75] In a variety of contexts, including boards of directors, the tendency of homogenous groups to engage in "groupthink" is well documented.[76] The adoption of a single perspective prevents groups from making better decisions and leads groups to "overestimate their objectivity and fail to have the constitution to assess their well-intentioned efforts."[77]

70. Adediran, *Board Composition*, *supra* note 11, at 399. The impact of a board's diversity extends to how the organization engages with clients, both as board members and in other capacities. In a study of nonprofit social service agencies in Michigan, boards which more closely reflected the racial composition of an organization's clients were also more likely to seek input from clients through advisory boards. LeRoux, *supra* note 8, at 511.

71. *See* BRENNAN & FORBES, *supra* note 14, at 4 (describing the challenges that nondiverse boards face in recruiting diverse leaders: "Boards that are overwhelmingly homogeneous are often not even aware of how their composition affects their ability to effectively attract or assess candidates with different backgrounds and experiences.").

72. *See* Rhode & Packel, *supra* note 50, at 398–401.

73. *See* Kathleen Buse, Ruth Sessler Bernstein & Diana Bilimoria, *The Influence of Board Diversity, Board Diversity Policies and Practices, and Board Inclusion Behaviors on Nonprofit Governance Practices*, 133 J. BUS. ETHICS 179, 187 (2016). *But see* William A. Brown, *Racial Diversity and Performance of Nonprofit Boards of Directors*, 7 J. APPLIED MGMT. & ENTREPRENEURSHIP, Oct. 2002, at 43. https://scholar.google.com/citations?view_op=view_citation&hl=en&user=zZ1MPWsAAAAJ&citation_for_view=zZ1MPWsAAAAJ:M3ejUd6NZC8C [https://perma.cc/UR7R-QWC6].

74. William A. Brown, *Exploring the Association Between Board and Organizational Performance in Nonprofit Organizations*, 15 NONPROFIT MGMT. & LEADERSHIP 317, 334 (2005) (describing that in a survey of nonprofit executives and board members "dimensions of board performance were related to effective group processes: educational, analytical, and interpersonal").

75. *See* LILLY REPORT, *supra* note 9, at 14; Rhode & Packel, *supra* note 50, at 395–97, 400–01.

76. *See* Alex Counts, *Spotting and Fixing Dysfunctional Nonprofit Boards*, STAN. SOC. INNOVATION REV. (Oct. 5, 2020), https://ssir.org/articles/entry/spotting_and_fixing_dysfunctional_nonprofit_boards [https://perma.cc/T4NJ-LBPH]; Carlson, *supra* note 63, at 343–44 (quoting Richard A. Bennet, Executive Chairman of Governance Metrics International, explaining that "during the financial crisis [of 2008], we saw examples of boards that were composed of members who were too similar in background and that often may breed 'groupthink.'"); Fanto et al., *supra* note 61, at 913–15; Melanie B. Leslie, *The Wisdom of Crowds? Groupthink and Nonprofit Governance*, 62 FLA. L. REV. 1179, 1190 (2010).

77. Faith Rivers James, *Nonprofit Pluralism and the Public Trust: Constructing a Transparent, Accountable, and Culturally Competent Board Governance Paradigm*, 9 BERKELEY BUS. L.J. 94, 125 (2012) [hereinafter Rivers James, *Pluralism*].

More diverse boards are also better equipped to engage in effective oversight and ensure meaningful compliance with legal, ethical, and industry standards.[78] Weaker oversight by less diverse boards may be the result of complacency and a "blind allegiance to management [that] clearly does not satisfy even the most minimal due diligence obligations."[79] Interestingly, despite the deference to management that less diverse boards may provide, more diverse boards have better collaborative relationships with executive staff.[80]

Furthermore, less diverse boards are more inclined to ignore, excuse, or even encourage detrimental transactions between insiders and the organization.[81] This reality has long been accepted in the context of charitable hospitals. In an effort to regulate the potentially lucrative relationships between physician groups and charitable hospitals, in 1969, the Internal Revenue Service (IRS) described that tax-exempt hospitals should be governed by groups of "independent civic leaders" rather than the insular group of physicians practicing in the hospital.[82] A hospital controlled exclusively by its physicians and their personal advisors, the IRS articulated, would operate for their own private benefit rather than for the public good.[83]

C. Moral Arguments for Diverse Boards

Beyond achieving financial and programmatic success, building a more diverse board of directors may also be a moral imperative for nonprofit organizations in a sense that is not generally applicable to for-profit corporations.[84] This moral demand, which is built upon a belief in self-determination and the importance of countering the nation's history of white oppression and the nonprofit sector's legacy of paternalism, requires that historically nondiverse boards do the hard work of "confront[ing] their own privilege

---

78. *See* Sandra J. Sucher & Shalene Gupta, *What Corporate Boards Can Learn from Boeing's Mistakes*, HARV. BUS. REV. (June 2, 2021), https://hbr.org/2021/06/what-corporate-boards-can-learn-from-boeings-mistakes [https://perma.cc/T4NJ-LBPH] (describing the lack of safety and engineering expertise among Boeing's board of directors, which shareholders allege breached its fiduciary duties when it failed to hold the company accountable for safety issues prior to two crashes killing 346 people).

79. Thomas Lee Hazen & Lisa Love Hazen, *Punctilios and Nonprofit Corporate Governance—A Comprehensive Look at Nonprofit Directors' Fiduciary Duties*, 14 U. PA. J. BUS. L. 347, 398 (2012) [hereinafter Hazen & Hazen, *Punctilios*].

80. *See* Pat Bradshaw, Vic Murray & Jacob Wolpin, *Women on Boards of Nonprofits: What Difference Do They Make?*, 6 NONPROFIT MGMT. & LEADERSHIP241, 248 (1996), (finding a "significant positive relationship between the [proportion of women on the board] and [CEO] satisfaction with the board's performance").

81. Leslie, *supra* note 76, at 1207; *see also* ABA GUIDEBOOK, *supra* note 40, at 306.

82. Rev. Rul. 69-545, 1969-2, C.B. 117.

83. *Id.*

84. While the nonprofit sector is unique in its explicit charge to serve the common good, there is no doubt that values driven decision making is relevant in the for-profit sector as well. *See, e.g.*, David B. Wilkins, *From "Separate is Inherently Unequal" to "Diversity is Good for Business": The Rise of Market-Based Diversity Arguments and the Fate of the Black Corporate Bar*, 117 HARV. L. REV. 1548, 1560 (2004) (arguing for the importance of "an express normative commitment to social justice" in driving diversity in corporate law firms).

and interrogat[ing] the power they hold as gatekeepers."[85] It should be examined independently of the potential for greater director diversity to enhance performance. More democratic participation and wider distribution of decisionmaking authority, distinct from the potential accomplishment of a charitable purpose, is itself a moral good.[86] As articulated by one nonprofit executive,

> If your board is not representative of the community you claim to serve, then you are furthering the injustice you seek to fight . . . . Mostly-white boards and staff of nonprofits and foundations are likelier to ignore the people most affected by injustice.
>
> . . .
>
> Mostly-white boards of foundations and nonprofits that serve marginalized communities are likelier to perpetuate a white savior complex, an insidious dynamic that prevents true social justice from being realized.[87]

As a starting point, increasing the diversity of nonprofit boards may allow for participatory parity among organizational stakeholders. Calls for participatory parity move beyond the traditional concepts of equality, focused on nondiscrimination and equal rights, to more substantive equality, which provides legitimacy to the decisions of the impacted organization.[88] Put more simply, an organization that includes individuals among its directors who share the experiences and identity of the organization's intended beneficiaries operates with greater legitimacy and earns the trust of clients and other stakeholders. That trust and confidence are grounded, in part, in recognition of and respect given to the lived experience and expertise of those board members who represent the community in which the organization operates.[89] This recognition reflects the dignity of both those board members and the organization's beneficiaries. These sentiments seem fairly intuitive when comparing the board of a women's college populated by alumnae and parents of alumnae with the board of a similar institution made up entirely of men who neither attended the school nor sent their daughters there. Yet, it is not as widely accepted that the same is true when we consider a local food pantry whose board includes (or does not include) individuals who have experienced food insecurity.

As described above with respect to mission performance, organizations whose boards reflect and represent the served community are better equipped to identify and adeptly respond to the needs of those communities.[90] They are also less likely to embrace, or be perceived to embrace, policies and practices that carelessly do silent or

---

85. Canales & Hostetter, *supra* note 13 (describing the steps taken by the board of the Barr Foundation, one of the largest private foundations in New England, to express and act on its commitment to racial equity).

86. *See* LeRoux, *supra* note 8, at 506 (describing the "dual goals of democratic participation and enhancing performance").

87. Vu Le, *7 Things You Can Do to Improve the Sad, Pathetic State of Board Diversity*, NONPROFIT QUARTERLY (Sept. 21, 2017), https://nonprofitquarterly.org/7-things-can-improve-sad-pathetic-state-board-diversity/ [https://perma.cc/5F9P-C8EP].

88. Tewari et al., *supra* note 50, at 246–47.

89. *See* LEADING WITH INTENT 2021, *supra* note 18, at 29 ("When boards are populated in a way that disconnects them from the communities their organizations exist to serve, it signals that the organization is not in partnership with the community it seeks to serve. Perhaps even more problematic, it signals that the organizations see this as a perfectly acceptable way of operating.").

90. *See supra* Part II.B.

hidden harm to the community or its beneficiaries.[91] This reality is highlighted by Professor Rivers James in her explanation of the tensions between traditional environmental nonprofits and the environmental justice movement, which has called on the environmental community and the nation to acknowledge the environmental hazards unfairly imposed upon communities of color and demand[ed]"[92] action to "eliminate unfair, unjust, and inequitable conditions and decisions."[93] As described by Professor Rivers James, "the views and perspectives of minorities and low-income people are not well articulated and embraced in organizations where there is insufficient board representation."[94] This failure of representation, in turn, "exposes nonprofits to charges of paternalism, [ir]relevancy and even malevolent intent or effects."[95]

For organizations with charitable missions focused on "address[ing] the legacy impact and ongoing repercussions of inequitable social and institutional practices,"[96] the need to embrace true equity is also a matter of intellectual consistency. An organization that seeks to engender buy-in for equality and equity in the broader world must start by embracing these values internally at its own center of power.

III. Assuming It's a Good Thing, How Do We Flip the Tables?

Whether we look to financial performance and sustainability, mission performance, or a moral demand, there are ample arguments for increasing the diversity of nonprofit boards. There has been, however, insufficient progress toward that objective and an acknowledgment that "private efforts . . . cannot on their own generate structural transformation."[97] Four possible approaches to increasing nonprofit board diversity provide alternative strategies and challenges. These approaches include (1) persuading nonprofit boards to diversify based on their independent goodwill and professed commitment to the mission of their organizations; (2) leveraging the regulatory authority of the IRS over tax-exempt organizations in a manner similar to actions of the SEC with respect to public companies; (3) deploying state corporate law to require more diverse boards, as attempted in recent for-profit business corporation legislation; and (4) expanding the understanding of the confines of nonprofit director fiduciary duties. This Section describes each approach in greater detail and identifies the inherent challenges to the first three approaches. While these difficulties appear to leave few options, Section IV explains why the considerable link between fiduciary duties and the fulfillment of charitable goals makes an expansion of the understanding of these duties ideally suited to driving change in the sector.

91. *See* Rivers, *Divide*, *supra* note 12, at 451–52.

92. *Id.* at 450–52.

93. *Id.* at 451.

94. *Id.* at 478–79.

95. Rivers James, *Pluralism, supra* note 77, at 124.

96. NYC Board Diversity, *supra* note 27, at 5.

97. Anat Alon-Beck, Michal Agmon-Gonnen & Darren Rosenblum, *A Duty to Diversfty*, 75 Vand. L. Rev. En Banc 97, 103–05 (2022) (arguing that moral arguments for increasing board diversity "may be insufficient to spark sufficient change to address the long and deeply entrenched lack of diversity") [hereinafter Alon-Beck et al., *Duty*].

A. Goodwill of Boards

By and large, nonprofit directors believe deeply in their organization's mission and are committed to its success. Their goodwill encourages them to give of their time, talent, and treasure in the belief that doing so will promote the fulfillment of the organization's mission. But if goodwill and knowledge led directly to sector-wide change on board diversity, the composition of nonprofit boards would have changed significantly over the last three decades. Instead, the relative stagnation of board composition indicates that, even when the majority of nonprofit leaders recognize the value of greater diversity, goodwill and knowledge alone are insufficient.[98] For example, in its 2021 Leading with Intent report on the perspectives of nonprofit board chairs and executives, BoardSource reported that almost half of the respondents believed their board did not include the right people to establish trust with the communities served by the organization, and yet, only 28% of respondents indicated that recruiting board members who were members of those communities was a high priority.[99]

Explanations for this disconnect are sundry. While some explanations may reflect a lack of genuine effort or implicit bias, many organizations have made genuine efforts without success.[100] As such, understanding explanations of the barriers to progress is necessary. The need for directors to act as donors, political connectors, and business experts is at times held up as an impediment to increasing board diversity.[101] With respect to directors as donors, an organization that requires a minimum level of philanthropic giving from its directors may express the sentiment that it is difficult to find more diverse individuals who will satisfy the organization's philanthropic demands.[102] A similar

98. *See* LEADING WITH INTENT 2017, *supra* note 22, at 14 ("[D]espite expressing dissatisfaction with current levels of board diversity, the majority of board chairs and chief executives do not report demographic diversity as a high priority in board recruitment.").

99. *See* LEADING WITH INTENT 2021, *supra* note 18, at 3.

100. *See* Michael Peregrine, *California Ushers in a Bold New Era of Board Diversity*, FORBES, (Oct. 2, 2020 6:00 AM) https://www.forbes.com/sites/michaelperegrine/2020/10/02/california-ushers-in-a-bold-new-era-of-board-diversity/?sh=47d054803955 [https://perma.cc/P9C8-JLHD] ("Efforts by the board to improve gender, racial and other diversity over the last several years may have been made in good faith, but they're not likely to be considered sufficient to meet evolving expectations.").

101. *See, e.g.*, Richard H. Levey, *Recruiting Young, Diverse Boards a Challenge*, NONPROFIT TIMES (Aug. 10, 2020), https://www.thenonprofittimes.com/hr/recruiting-young-diverse-boards-a-challenge/ [https://perma.cc/HLH8-T6YW] (describing professional experience expected of new board members as a barrier to inclusion of younger members); Joseph Garcia, *Diversity Recruitment Key to Nonprofit Boards Achieving Mission*, MORRIS INST. FOR PUB. POL'Y, ARIZ. STATE UNIV. (June 7, 2016), https://morrisoninstitute.asu.edu/content/diversity-recruitment-key-nonprofit-boards-achieving-mission [https://perma.cc/HK2K-E95J] (proposing practical steps to reduce barriers to inclusion of more diverse board members); MOLLY DELANO BRENNAN & MIECHA RANEA FORBES, KOYA LEADERSHIP PARTNERS, THE GOVERNANCE GAP, EXAMINING DIVERSITY AND EQUITY ON NONPROFIT BOARDS OF DIRECTORS (Jan. 2019), https://koyapartners.com/wp-content/uploads/2018/12/KOYA_GovernanceGap_FINAL.pdf [https://perma.cc/S2LM-69S2] (addressing assertion that the need for philanthropy precludes recruitment of color).

102. This argument seems unfounded, based on a 2018 study by the Lilly Family School of Philanthropy at Indiana University which described that "[b]oards that have a higher percentage of People of Color did not have any significant differences in fundraising engagement overall." LILLY REPORT, *supra* note 9, at 15. *See also* Harris, *supra* note 51, at 125 (noting that in a study of colleges and universities that "the percentage of

argument is made about challenges in identifying possible directors with the political clout or connections that an organization requires.[103] Likewise, organizations seeking directors with certain professional patina or experience may believe that there is a lack of qualified diverse candidates.[104]

In the for-profit sector, the argument regarding business credentials has been consistently debunked,[105] including by various organizations established to help connect public companies with qualified, diverse board candidates.[106] This argument is equally untrue for nonprofit organizations. Some tie the apparent challenge in recruiting diverse board directors to failures of the recruitment process.[107] For example, when public company boards focus on selecting those who have served as C-level executives and employers deny mid-level executives the opportunity to obtain experience as board members, the circle from which to select directors becomes increasingly smaller and

---

minority board members is positively associated with total contributions"). Similarly, a study of New York City nonprofits found that "women are not less likely to donate than are men, and there are no differences in the dollar amount of giving," which "raises the question of why women are underrepresented on more prestigious and larger boards." Katherine O'Regan & Sharon M. Oster, *Does the Structure and Composition of the Board Matter? The Case of Nonprofit Organizations*, 21 J. L., ECON. & ORG. 205, 222–24 (2005). For an insightful explanation of the complexity of this issue, see Angela E.L. Barnes, *Non-Profit Boards Have Imperative to Change*, CTR. ON HALSTED (Mar. 1, 2021) https://centeronhalsted.medium.com/nonprofit-boards-have-imperative-need-to-change-2881bac7e548 [https://perma.cc/99DF-WLB3].

103. Adediran, *Board Composition*, *supra* note 11 (quoting the CEO of a large public interest law organization that recruits board members with an eye toward "leverage[ing] connections to top elected leaders").

104. *See, e.g.*, Cydney Posner, *California Mandates Quotas for Board Gender Diversity—Will It Fuel a Movement?*, COOLEY PUBCO (Sept. 30, 2018), https://cooleypubco.com/2018/09/30/california-mandates-quotas-for-board-gender-diversity/ [https://perma.cc/23PB-QM6T]. In a 2016 survey of for-profit board directors across the globe, "39% of male directors in the 55-to-60 age group said the 'lack of qualified female candidates' was the primary reason for the low numbers of female directors. However, 69% of female directors in that same age cohort attributed the low numbers to the failure to rank diversity as a top priority in board recruiting." *Id.*

105. Maria Moats & Paul DeNicola, *You Say You Want a More Diverse Board. Here's How to Make It Happen*, HARV. BUS. REV., at 4 (Mar. 11, 2021), https://hbr.org/2021/03/you-say-you-want-a-more-diverse-board-heres-how-to-make-it-happen [https://perma.cc/8UA6-5DWF] (last visited Apr. 1, 2023) ("In reality, there is no shortage of candidates. We see these director candidates every day, and a plethora of respected organizations actively maintain relationships with vetted candidates from underrepresented groups precisely for the purpose of making introductions to boards seeking new members. So the first step to overcoming this obstacle is to realize that the candidate pool is there, and that it's up to boards to find it.").

106. *See, e.g.*, AFR. AM. BD. LEADERSHIP INST., https://www.aabli.org/ [https://perma.cc/VH4D-Q5EE] (last visited Apr. 1, 2023); BOARDREADY, https://www.boardready.io/ [https://perma.cc/96MU-V6DE] (last visited Apr. 1, 2023); HIM FOR HER, https://www.himforher.org/ [https://perma.cc/8L8J-F4Z3] (last visited Apr. 1, 2023).

107. Recruitment criteria and processes may be applied inconsistently to different candidates. One example is the question of whether a director has served on a board before. *See* Joann S. Lublin, *Some Forms Intensify Push for Gender Parity at Board Level*, WALL ST. J. (Aug. 16, 2016, 7:42 PM), https://www.wsj.com/articles/some-firms-intensify-push-for-gender-parity-at-board-level-1471357128 [https://perma.cc/X24S-D5YK] ("'Boards dominated by men have grown used to the male standard of congeniality and so accept a man who's never been a director before,' even though they usually reject women without such experience." (quoting Eleanor Bloxham, a governance consultant)).

more insular.[108] The same is likely true for nonprofits that seek only those candidates who have served on other boards or hold positions of particular influence. Putting aside that there is no actual shortage of qualified diverse candidates, even boards with the very best of intentions may recognize that their existing recruitment practices and personal networks do not reach desired candidates.[109]

Tradition and consistency bias also push against change in nonprofit board composition.[110] When some older nonprofits seek out new board members, they turn to the family members or colleagues of retiring directors.[111] In this way, certain board seats become legacy seats aimed at maintaining the support of a generous family or business. More generally, as nominating committees consider the skills and expertise they seek in new directors, there is a tendency to recruit new board members who possess similar skills and backgrounds as those who are stepping down.[112] This bias toward seeking to replicate the existing board reduces the likelihood of seeking out candidates with new perspectives or experiences.[113] And, intentional or not, the circularity of this process increases social capital for existing board members.[114]

The lack of meaningful change in the composition of nonprofit boards of directors over the last three decades, despite an appreciation by many board leaders of the benefits

108. *See* Alon-Beck et al., *Duty*, *supra* note 97, at 107–08 ("It is a self-perpetuating problem. Candidates are often former or current executives from companies known to other members of the board or C-suite . . . . [who become board] candidates by virtue of their participation in social circles and networks.").

109. Recruiting a more diverse board is only the first step. Boards that succeed in recruiting more diverse directors, but that fail to adopt inclusive policies and practices, are less likely to reap the benefits of greater diversity. *See* Buse et al., *supra* note 73, at 187 (describing that the adoption of policies and practices related to diversity and inclusive behaviors result in improved performance of a board's governance responsibilities).

110. *See* Rick Moyers, *Diverse Boards Make Better Decisions. So Why Are So Many White?*, THE CHRON. OF PHILANTHROPY, (Jan. 9, 2018) https://www.philanthropy.com/article/diverse-boards-make-better-decisions-so-why-are-so-many-so-white/ [https://perma.cc/2FP2-HTWB] ("[A] long history of discriminatory policies and practices, combined with pervasive unconscious bias, has produced a society in which many well-qualified people of color are not part of the informal social networks and systems of power and influence that would lead to their consideration for board service.").

111. Of course, the opportunity to seek new board members depends on more experienced board members stepping down. The lack of director turnover, and the resulting shortage of new leadership, leads many nonprofits to institute term limits and retirement ages. In a blog post addressed to white board members who want to engage in racial equity work, activist and educator Sapna Sopori explains this issue: "[W]ith limited seating, the only way to make room now is for the folks already there to leave. . . . If you believe your nonprofit work is urgent and that work is directly connected to systemic racism . . . , then developing the proper composition of your board to do that work most effectively needs to be just as urgent. Would you be willing to give up your seat before your term limit in order to make space for someone who is more impacted by the decisions being made at the board table?" Sapna Sopori, *The (White) Elephant in the (Board) Room: How White Board Members Can Step Up By Stepping Aside*, SAPNA STRATEGIES, LLC (Aug. 3, 2020) https://sapnastrategies.com/2020/08/03/the-white-elephant-in-the-board-room/ [https://perma.cc/729C-6LQP].

112. Rhode & Packel, *supra* note 50, at 404–05.

113. *See* Rhode & Packel, *supra* note 50, at 405 ("In-group bias keeps women out of the informal networks of advice and support from which appointments are often made. Female directors see exclusion from such networks as the most important reason for women's underrepresentation on corporate boards.").

114. *See* Alon-Beck et al., *Duty*, *supra* note 97, at 108 ("Directors are able to enhance their preexisting social and professional networks, increasing their overall societal influence and prestige.").

of board diversity, makes it clear that goodwill and knowledge alone are inadequate tools to drive change.

B. IRS Regulation

The apparent failure of goodwill raises the question of whether regulator intervention may be necessary to protect the charitable assets and missions of nonprofit organizations from the latent harms of less diverse boards. As a centralized regulator of public charities, the IRS's broad influence on organizational structure and behavior makes it a potential starting point for reshaping the composition of nonprofit boards.[115]

Qualification as exempt from federal income tax is of tremendous value to nonprofit charitable organizations.[116] Organizations that qualify for federal tax-exemption under Internal Revenue Code (I.R.C.) Section 501(c)(3) also benefit in other ways, including the ability to reinvest income into programs and capital expenses, the ability to accept tax-deductible charitable contributions,[117] exemption from unemployment taxes,[118] access to the tax-exempt bond market,[119] and, in most cases, exemption from state income, sales, and property taxes.[120] Due to these lucrative benefits, the structure and operations of such organizations are highly influenced by the requirements for tax-exemption under I.R.C. Section 501(c)(3).[121] Eligibility for qualification as a "501(c)(3)" is determined by the IRS, meaning that the federal taxing authority holds significant influence over the structure and activities of more than 1.5 million public charities.[122] With this authority comes a charge to ensure that the benefits of tax-exemption flow to those organizations structured and operating for the public good.

---

115. *See generally*, Atinuke O. Adediran, *Disclosures for Equity*, 122 Colum. L. Rev. 865 (2022) (arguing that the IRS could drive increased funding for organizations led by minorities and serving communities of color by mandating disclosures of donor information and race data) [hereinafter Adediran, *Disclosures*].

116. For example, in a 2017 study commissioned by the American Hospital Association, Ernst & Young estimated that in 2013 the federal government had foregone an estimated $3.2 billion from tax-exempt nonprofit hospitals based on their tax-exempt status. ERNST & YOUNG, ESTIMATES OF THE FEDERAL REVENUE FORGONE DUE TO THE TAX EXEMPTION OF NON-PROFIT HOSPITALS COMPARED TO THE COMMUNITY BENEFIT THEY PROVIDE, 2013, at 3 (Oct. 2017).

117. I.R.C. § 170(a)(1).

118. Federal Unemployment Tax Act, 26 U.S.C. § 3303(e); *see also Exempt Organizations: What Are Employment Taxes?*, IRS, https://www.irs.gov/charities-non-profits/exempt-organizations-what-are-employment-taxes [https://perma.cc/MF2R-8XX8] (last updated Jun. 16, 2022).

119. I.R.C. § 145; *see also* ERNST & YOUNG, *supra* note 116 (estimating that tax-exempt nonprofit hospitals garnered the benefit of $2.5 billion in reduced borrowing costs through the tax-exempt bond market and $0.3 billion as a result of being exempt from the federal unemployment tax).

120. *See Frequently Asked Questions About Applying for Tax Exemption*, IRS, https://www.irs.gov/charities-non-profits/frequently-asked-questions-about-applying-for-tax-exemption [https://perma.cc/Z292-E5Y2] (last updated Dec. 21, 2022) ("Nonprofit status may make an organization eligible for certain benefits, such as state sales, property and income tax exemptions."); *e.g.*, 61 PA. CODE § 32.21 (2022).

121. I.R.C. § 501(c)(3).

122. NAT'L CTR. FOR CHARITABLE STAT., URB. INST., *The Nonprofit Sector in Brief* (June 16, 2018), https://nccs.urban.org/project/nonprofit-sector-brief [https://perma.cc/39AV-PQBC] (estimating that as of 2016 there were 1.54 million public charities registered with the IRS).

Evidence of the IRS's ability to influence the structure and policies of public charities can be seen in the broad adoption of various IRS-recommended policies and practices that are not statutorily required. In 2008, the IRS published a summary of its perspective on the interplay between nonprofit governance and tax-exemption under I.R.C. Section 501(c)(3), explaining that:

> The Internal Revenue Service believes that a well-governed charity is more likely to obey the tax laws, safeguard charitable assets, and serve charitable interests than one with poor or lax governance. . . . And while the tax law generally does not mandate particular management structures, operational policies, or administrative practices, it is important that each charity be thoughtful about the governance practices that are most appropriate for that charity in assuring sound operations and compliance with the tax law.[123]

The 2008 summary describes that public charity boards should be "informed and active in overseeing a charity's operations and finances," should not tolerate secrecy or neglect, and should not be excessively large or small in number.[124] Perhaps most importantly, the IRS explains that directors should be independent of each other and should not be overly connected through business or family relationships.[125] In defense of its request for information regarding relationships among directors during the exemption application process and on the annual information return of public charities (Form 990), the IRS explains that it "reviews the board composition of charities to determine whether the board represents a broad public interest, and to identify the potential for insider transactions that could result in misuse of charitable assets."[126]

Having already asserted its belief that the composition of a public charity's board relates directly to whether it is entitled to federal tax-exemption, the IRS could add specificity to this position. It could explain that, to "represent[] a sufficiently broad public interest," a public charity needs a board that reflects the diversity of the community in which it operates or serves.[127] Such an expectation could be articulated with varying degrees of specificity.

---

123. IRS, GOVERNANCE AND RELATED TOPICS - 501(C)(3) ORGANIZATIONS 1 (Feb. 4, 2008), https://www.irs.gov/pub/irs-tege/governance_practices.pdf [https://perma.cc/MB5B-ZUFC] [hereinafter IRS Governance]; *see also* RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 2.05 cmt. g (AM. L. INST. 2021) (describing governance practices endorsed by the IRS on the basis of the belief that "good governance is more likely to lead to tax compliance"); Steven T. Miller, Comm'r, Tax-Exempt and Gov't Entities, IRS, Remarks at the Western Conf. on Tax Exempt Orgs., Los Angeles, California, Nonprofit Governance 2–3 (Nov. 20, 2008), https://www.irs.gov/pub/irs-tege/stm_loyolagovernance_112008.pdf [https://perma.cc/L2BW-CSPP] (arguing that while the IRS did not intend to "second guess" how nonprofits run their organizations, that "[g]overnance practices influence whether an organization is operated to further exempt purposes, and whether the organization serves public, rather than private, interests").

124. IRS Governance, *supra* note 123, at 2–3.

125. *Id.* at 3.

126. *Id.*

127. Rivers James, *Pluralism*, *supra* note 77, at 134 (quoting IRS Governance, *supra* note 123, at 2). While this Article explores the possibility of utilizing the tax system to influence board diversity primarily through disclosure, Professor Anne L. Alstott has proposed an intriguing incentive-based system which would provide refundable tax credits to organizations that meet certain board diversity standards. Anne L. Alstott, *Gender Quotas for Corporate Boards: Options for Legal Design in the United States* (Yale L. Sch., Public Law Research Paper No. 489, 2013).

On one end of the spectrum, the IRS could ask organizations to describe on their application for recognition of exemption (Form 1023) and Form 990 how their boards ensure their own diversity in furtherance of representing a broad public interest. Such a question would be consistent with existing questions on Form 990.[128] The possibility of oversight by a federal regulator of board diversity offers another parallel between nonprofits and their for-profit company counterparts. In 2009, as part of broader disclosure reforms, the SEC adopted rules requiring public companies to disclose in their annual shareholder proxy statement whether and how their board's nominating committee "considers diversity in identifying nominees for director."[129] The SEC's authority to adopt such a requirement is based on its charge to protect investors, including through the provision of information deemed significant to making investment decisions.[130] While some scholars and practitioners saw the SEC rule as a useful step toward recognition of the value of diverse boards, others believed that the failure of the rule to define diversity or to require disclosure of actual board composition undercut its likelihood of driving change.[131] Similar concerns might be raised about a broad question on nonprofit board diversity policies.

On the other end of the spectrum, the IRS could focus on quantitative representation by articulating a fixed measure to assess the diversity of an organization's board. For example, it could set an expectation that the percentage of an organization's board members from historically underrepresented groups should mirror the percentage of organization clients from that same historically underrepresented group or that the organization explain why this expectation is not met. Such a requirement would be akin to Nasdaq's board diversity listing rules, as approved by the SEC in 2021, which require that the majority of Nasdaq-listed companies have at least two diverse board members or explain why they do not.[132] Listed companies which do not comply with the requirement to explain their failure to meet the minimum target may be delisted from the exchange.[133] This kind of quantitative standard is unlikely without a change to the IRS's scope of authority under the I.R.C.

---

128. *See* IRS Form 990, Part VI, Section B (2021), https://www.irs.gov/pub/irs-pdf/f990.pdf [https://perma.cc/U357-X43P]. This form includes questions about policies on executive compensation, document retention, whistleblowers, joint ventures, and conflicts of interest. *Id.*

129. 17 C.F.R. § 229.407(c)(2)(vi) (2022).

130. Hazen, *Limits*, *supra* note 37, at 894–95 & n.36.

131. *See* Fairfax, *Board Diversity Revisited*, *supra* note 50, at 874–76 (acknowledging the possibility that the SEC rule "could facilitate future changes in board diversity," while cautioning that the lack of a definition of diversity or an affirmative requirement that companies adopt a policy on board diversity might "undermine its ability to positively impact board diversity"); Hazen, *Limits*, *supra* note 37, at 896 (describing the new rules and arguing that "the SEC could have given investors even more meaningful information on board diversity had it required disclosure of the ethnicity, race, and gender of existing board members").

132. Nasdaq Rule 5605(f)(2), https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/nasdaq-5600-series [https://perma.cc/8JRN-NFHK]. Under this rule, a diverse director is one who self-identifies as female, an underrepresented minority, or LGBTQ+. *Id.*

133. *See* Nasdaq Rule 5605(f)(6)(A), https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/nasdaq-5600-series [https://perma.cc/8JRN-NFHK]; Nasdaq Rule 5810(c)(3), https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/nasdaq-5800-series [https://perma.cc/H9SF-Z7D7].

Alternatively, rather than setting a quantitative standard, the IRS could require that charities disclose aggregated demographic information about their directors.[134] Accepting that Form 1023 already inquires as to the qualifications of an organization's directors, it would not be a significant burden or invasion of privacy to request more specific information that would allow for a qualitative assessment of a board's diversity.[135] Such a requirement would track Nasdaq's mandate that listed companies provide "disclosure, in an aggregated form, of information on the voluntary self-identified gender, racial characteristics, and LGBTQ+ status of [a] company's board"[136] to provide investors with relevant information to evaluate companies in which they might invest.[137]

While the IRS's 2008 assertion that it had an interest in the governance practices of public charities was met with skepticism by many in the sector,[138] its monitoring of governance-related practices has become widely accepted.[139] Its articulation of board diversity expectations could impact the practices and policies of organizations concerned with maintaining their tax-exempt status and avoiding the IRS's scrutiny.[140]

Yet, the IRS's power to set expectations and require transparency should not be overstated. Due to limitations on the Service's authority and the infrequency with which

---

134. *See* Rivers James, *Pluralism*, *supra* note 77, at 135–36; Adediran, *Disclosures*, *supra* note 115, at 907–08.

135. *See* IRS Form 1023, Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code, Part V, Question 3a (OMB No. 1545-0056) (Rev. Dec. 2017), https://www.irs.gov/pub/irs-pdf/f1023.pdf [https://perma.cc/J29Q-SL5Y]; Adediran, *Disclosures*, *supra* note 115, at 910–11.

136. *See* U.S. SEC. & EXCHANGE COMM., *Statement on Nasdaq's Diversity Proposals – A Positive First Step for Investors* (Aug. 6, 2021), https://www.sec.gov/news/public-statement/statement-nasdaq-diversity-080621 [https://perma.cc/KAL8-KDFU]; Nasdaq Rule 5606, https://listingcenter.nasdaq.com/rulebook/nasdaq/rules/nasdaq-5600-series [https://perma.cc/WQT8-5XTC].

137. Securities Exchange Act Release No. 34-92590 at 5 (Aug. 6, 2021) (order approving SR-NASDAQ-2020-081 and SR-NASDAQ-2020-082) https://www.sec.gov/rules/sro/nasdaq/2021/34-92590.pdf [https://perma.cc/Y9CA-82GX].

138. *See, e.g.*, Karen Donnelly, Note, *Good Governance: Has the IRS Usurped the Business Judgment of Tax-Exempt Organizations in the Name of Transparency and Accountability?*, 79 UMKC L. REV. 163, 166 (2010); James J. Fishman, *Stealth Preemption: The IRS's Nonprofit Corporate Governance Initiative*, 29 VA. TAX REV. 545 (2010) [hereinafter Fishman, *Stealth*]; Miller, *supra* note 123 (describing that the IRS's public discussion of nonprofit governance was met with "reluctance, indignation, and even anger"); Marcus S. Owens, *Charities and Governance: Is the IRS Subject to Challenge?*, TAX ANALYST (2008), https://ncpl.law.nyu.edu/wp-content/uploads/pdfs/2007/Conf2007_Owens.pdf [https://perma.cc/MQ2J-W9M8] (describing the process leading to the IRS's statements on governance, the issuance of a revised Form 990 and possible approaches for organizations to challenge the appropriateness of IRS questions relating to governance).

139. *See, e.g.*, Hazen & Hazen, *Punctilios, supra* note 79, at 397 (acknowledging that while the IRS cannot and does not "require better governance practices," its guidance in this area is designed "to strongly encourage transparency and accountability").

140. ADVISORY COMM. ON TAX EXEMPT & GOV'T ENTITIES (ACT), IRS, THE APPROPRIATE ROLE OF THE INTERNAL REVENUE SERVICE WITH RESPECT TO TAX-EXEMPT ORGANIZATION GOOD GOVERNANCE ISSUES 6 (2008), https://www.irs.gov/pub/irs-tege/executive_summary_actgovernancerept.pdf [https://perma.cc/7P22-UWT3]. The IRS's own advisory committee cautioned that "the IRS merely asking about specific governance practices is a powerful force that can drive behavior." *Id.*

it exercises its authority to revoke the tax-exempt status of organizations,[141] disclosure requirements alone may not have sufficient bite.[142] As with the current Form 1023 and Form 990 questions that ask organizations to describe or confirm the existence of policies which are not required by law, additional questions about board diversity would merely encourage change without requiring it or altering the IRS's authority to enforce its aspirations.[143] In the context of significant controversies about interested party transactions in the mid-1990s, Congress gave the IRS the ability to impose penalties short of revocation, called "intermediate sanctions," against directors who participate in or approve transactions that provide an excess benefit to an organization insider.[144] The statutory clarity regarding the prohibition on insiders receiving excess benefits, the lack of enforcement mechanisms short of revocation and the consensus on the IRS's role in policing inappropriate financial benefits made intermediate sanctions legislation politically feasible.[145] It is unimaginable in today's political climate to envision a consensus about the IRS exercising oversight over the diversity of nonprofit boards.[146] Without such consensus, though, the IRS has limited ability to reign in or direct the conduct of nonprofit boards on an issue which few would argue should jeopardize the exempt status of most charities. One might more realistically imagine that the IRS could follow the leadership of the sector and others in monitoring and encouraging transparency in the future.

C. State Corporate Law

Acknowledging the limits of goodwill and federal regulation in effecting change to nonprofit board diversity, we turn to the more parochial tools of state law. Nonprofit corporations are creatures of state law. Accordingly, their structure and that of their boards are determined by the parameters of nonprofit corporate statutes. Mandatory statutory structuring offers an opportunity for states to direct the composition of

---

141. *See* FISHMAN ET AL., *supra* note 3, at 468–69.

142. Professor Atinuke Adediran alternately proposes that were the IRS to require disclosure of board member race on Form 990 that the potential penalty could be based on the current penalty for nondisclosure of $20 per day, up to $10,000. Adediran, *Disclosures*, *supra* note 115, at 915–16.

143. *See* Donnelly, *supra* note 138, at 180–82. Recognizing the potential limitations on the IRS's ability to "expand its authority to collect . . . race data," Professor Adediran suggests that Congress could amend the IRS's authority to explicitly allow for the collection of racial data about board members. Adediran, *Disclosures*, *supra* note 115, at 916.

144. *See* Pub. L. No. 104-268, 110 Stat. 1475 (1996) (codified as amended at I.R.C. § 4958).

145. FISHMAN ET AL., *supra* note 3, at 469; *see also* 141 CONG. REC. E1765 (daily ed. Sept. 12, 1995) (remarks of Hon. Fortney Pete Stark) (describing examples of instances where insiders "enriched themselves at the public's expense while nonprofit organizations have been looted").

146. *See, e.g.*, Improving Corporate Governance Through Diversity Act, H.R. 5084, 116th Cong. (2019), https://www.congress.gov/bill/116th-congress/house-bill/5084 [https://perma.cc/GTJ8-87H8]. This proposed federal legislation would require annual public company proxy statements to include the racial, ethnic, and gender composition of their board, director nominees, and executive officers and disclosure of any plan to promote racial, ethnic, and gender diversity among these group. Since passing in the House in November 2019, the bill has stalled in the Senate Committee on Banking, Housing and Urban Affairs. *See id.*

nonprofit boards formed under (or possibly even operating under) their corporate laws.[147] Disclosure requirements can create transparency and create space for public pressure, even without dictating structure.[148] To date, only Maryland has adopted state corporate legislation relating to nonprofit board diversity.[149] Nevertheless, state efforts relating to for-profit corporations provide a model for consideration.

1. State Board Composition Requirements

In early 2023, legislators in New York reintroduced a bill that would require that nonprofit boards receiving state funds to mirror the ethnic demographics of the communities they serve.[150] This proposed nonprofit legislation follows efforts by states, including California and Washington,[151] to add board diversity requirements to their for-profit corporate laws. California's two board diversity laws, SB-826, requiring that public companies headquartered in the state include at least one woman on their board, and AB-979, requiring that these same corporations include directors from underrepresented communities,[152] have been heralded as examples of effective drivers of change[153] and at the same time have faced a multitude of unsurprising legal

147. As noted elsewhere, caution should be taken in thinking that requiring a numerical increase in the percentage of directors on a nonprofit board from historically underrepresented groups will de facto lead to more equitable and just outcomes. As described by Professor Geeta Tewari and colleagues, statutes requiring that women (or other underrepresented groups) fill a certain percentage of seats on a board do not "address the informal social norms and structural inequalities that result in the 'exclusions of some citizens from some domains of participation.'" Tewari, et al., *supra* note 50, at 249 (quoting Ruth Rubio-Marín, *A New European Parity-Democracy Sex Equality Model and Why It Won't Fly in the United States*, 60 AM. J. COMP. L. 99, 111 (2012)).

148. For example, in 2011, Professor Lisa Fairfax argued that the SEC's 2009 rule requiring disclosure of public company board diversity policies and their implementation "could increase public scrutiny of existing policies, thereby encouraging corporations to ensure that those policies produce results." Fairfax, *Board Diversity Revisited*, *supra* note 50, at 874. *See generally* Evelyn Brody, *Sunshine and Shadows on Charity Governance: Public Disclosure as a Regulatory Tool*, 12 FLA. TAX REV. 183, 213 (2012).

149. Gender Diversity in the Boardroom – Annual Report, H.B. 1116, 440th Gen. Assemb. (Md. 2019) https://mgaleg.maryland.gov/2019RS/Chapters_noln/CH_513_hb1116e.pdf [https://perma.cc/D82C-JLYB]; Luwanda Jenkins, *New "Gender Diversity in the Boardroom" Law Places Maryland Companies on Notice"*, THE DAILY RECORD (Nov. 22, 2019), https://thedailyrecord.com/2019/11/22/new-gender-diversity-in-the-boardroom-law-places-maryland-companies-on-notice/ [https://perma.cc/93VA-NVHB].

150. A.B. 753, 2023–2024 Leg., Reg. Sess. (N.Y. 2023). Sponsors of an earlier version of the bill argue that nonprofit boards that reflect the diversity of the communities they serve are better able to "fully understand the needs of those communities and remain accountable to them," because directors can "relate to shared experiences of those communities and better identify problems and solutions that are within their scope of service to address." *Senate Bill S5791*, N.Y. STATE SENATE, https://www.nysenate.gov/legislation/bills/2021/s5971 [https://perma.cc/P3KT-BMYN] (last visited Apr. 1, 2023).

151. WASH. REV. CODE § 23B.08.120 (2021).

152. CAL. CORP. CODE § 301.3(a) (West 2018); CAL. CORP. CODE § 301.4 (a), (e)(1) (West 2020).

153. *See* Michal Lev-Ram, *Exclusive: California's Board Diversity Law Led to 670 Board Seats Filled by Women, Report Finds*, FORTUNE, (Oct. 13, 2020, 8:11 AM), https://fortune.com/2020/10/13/california-boards-diversity-jennifer-siebel-newsom/ [https://perma.cc/85B2-6VJH] (last visited Apr. 1, 2023).

challenges.[154] To date, the challenges have succeeded in making the future of these and similar laws bleak.[155]

Three of the primary challenges to the California laws are that the statutes require unlawful employment discrimination,[156] allow for unnecessary and overreaching government interference with private business decisions, and interfere with interstate commerce.[157] The first two arguments against California's laws may be less compelling were a similar law to be adopted for nonprofits. First, while for-profit businesses generally pay their directors, nonprofit directors typically act in a voluntary capacity and therefore are not entitled to the same protections against employment-based discrimination.[158] Second, given their unique status under both state and federal law, the affairs of nonprofit corporations are already subject to significant government intervention.[159] For example, by tying the receipt of state funding to its board diversity requirements, the proposed New York bill might circumvent challenges by establishing a more substantial government interest in the requirement. California has been unsuccessful in arguing that it had compelling state interest in remediating past discrimination and in healthy businesses in passing SB-826.[160] As a funder of nonprofit activities and an advocate for the public good, a state may be better able to defend its compelling interest in nonprofit board diversity than its general interest in promoting business. As to the third argument, if the courts considering the challenges to the California statutes continue to find the interstate commerce challenge compelling, this would apply equally and disastrously to similar statutes regulating nonprofit

---

154. *See, e.g.*, Michael Burdick, *SB 826*, Assemb. Floor Analysis No. 0004503, 2017–2018 Legislature, Reg. Sess. 4 (Cal. 2018), [https://perma.cc/7XZD-NQYK] ("[T]his bill, if enacted into law, would likely be challenged on equal protection grounds . . . . In addition to equal protection concerns, this bill may conflict with the internal affairs doctrine."); S. Rules Comm., *AB 979*, S. Floor Analyses, 2019–2020 Legislature, Reg. Sess. 6–7 (Cal. 2020), [https://perma.cc/M8HF-4PNH]; Ltr. from Edmund G. Brown, Jr., Governor of Cal., to the Members of the California State Senate (Sept. 30, 2018), [https://perma.cc/JPN7-ZMR6].

155. *See, e.g.*, Crest v. Padilla, Case No. 19STCV27561 (Cal. Super. Ct. May 13, 2022) (striking down requirement that public company boards include women), https://www.documentcloud.org/documents/22016185-crest-v-padilla-verdict-ca-may-2022 [https://perma.cc/789D-7M49]; Crest v. Padilla, Case No. 20STCV37513, 2022 WL 1073294, at *19–20 (Cal. Super. Ct. April 1, 2022) (striking down requirement that boards include members of historically underrepresented groups). Temporary injunctions which allowed for continued collection of information by the Secretary of State's office while the State appeals these decisions were vacated in December 2022, forcing the State to cease all related expenditures. Order, Dec. 1, 2022, *Crest*, Case No. 19STCV27561; Order, Dec. 1, 2022, *Crest*, Case No. 20STCV37513.

156. *See, e.g.*, Compl. for Declaratory and Injunctive Relief ¶ 10, Alliance for Fair Bd. Recruitment v. Weber, No. 2:21CV05644 (C.D. Cal. July 12, 2021) [https://perma.cc/7NDC-FXPY] (arguing that S.B. 826 and S.B. 979 require corporations to discriminate on the basis of sex and race).

157. *See* Joseph A. Grundfest, *Mandating Gender Diversity in the Corporate Boardroom: The Inevitable Failure of California's SB 826*, (Rock Ctr. for Corp. Governance at Stanford Univ., Working Paper Series No. 232, Sept. 2018), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3248791 [https://perma.cc/96YT-QMET] (last visited Apr. 1, 2023).

158. *See* Fichman v. Media Center, 512 F.3d 1157 (9th Cir. 2008) (holding that volunteer directors of nonprofits were not employees for purposes of the Americans with Disabilities Act or Age Discrimination in Employment Act).

159. *See generally* Fishman, *Stealth*, *supra* note 138, at 550–57.

160. *See* Crest v. Padilla, Case No. 20 STCV 37513, 2022 WL 1073294, at *18 (Cal. Super. Ct. Apr. 1, 2022).

corporations. In light of the successful challenges to the California laws thus far, there is no clear route to meaningful increased board diversity through new state corporate composition requirements.[161]

2. State Disclosure Requirements

Other states have taken a less direct, and therefore less controversial, approach focused on increasing transparency and collecting information about board diversity.[162] For example, Maryland adopted legislation in 2019 that requires all business entities with annual operating budgets or sales of $5 million or more—including nonprofit corporations—to report the number of women on their boards.[163] The state comptroller is required to provide an annual report of the information collected to the state legislature.[164] Reported data from individual companies, however, is not made publicly available under the statute.

New York took a similar approach, with the stated objectives of ensuring "women are included in discussions and decisions that affect corporate actions and profitability" and taking a "proactive approach to address historical inequality and end discriminatory practices."[165] Beginning in 2022 and every four years thereafter, the Departments of State and Taxation & Finance are required to report on the number of women who serve on corporate boards of corporations doing business in the state.[166] Like the Maryland disclosure law, the New York statute does not provide for public disclosure of entity-level data.[167] Interestingly, despite calls for a broader approach, both Maryland and New York focused exclusively on gender diversity and chose not to require the disclosure of racial or ethnic diversity.[168]

Without follow-through or organization-level public disclosure, reporting can be expected to have limited or at least greatly delayed impact. Despite the sponsors of the New York bill intending that business corporations be required to "prepare an annual

161. In spite of this, state legislatures continue to consider legislation that would do just this. For example, a bill introduced in the Hawaii legislature in January 2023 would require that the boards of publicly-held, domestic corporations whose primary offices are in the state include a minimum number of both male and female or nonbinary directors. H.B. 1191, 32nd Leg. (Haw. 2023).

162. Some legislative proposals to collect information about the diversity of nonprofit boards have been resisted by the sector. For example, a 2007 bill proposed in California which would have required disclosure by large private foundations of the demographic composition of their staffs and boards was vehemently objected to by foundations and philanthropic sector organizations. *See* Rivers James, *Pluralism*, *supra* note 77, at 111–13.

163. Gender Diversity in the Boardroom – Annual Report, H.B. 1116, 440th Gen. Assemb. (Md. 2019) https://mgaleg.maryland.gov/2019RS/Chapters_noln/CH_513_hb1116e.pdf [https://perma.cc/L2L9-643X] (requiring corporations to report the number of women on their boards on their personal property tax filings).

164. *See, e.g.*, COMPTROLLER OF MARYLAND, 2021 REPORT ON GENDER DIVERSITY IN THE BOARDROOM, (Jan. 26, 2021) https://www.marylandtaxes.gov/reports/pdf/Comptrollers_Report_Gender_Diversity_in_the_Boardroom.pdf [https://perma.cc/ET97-EFPK].

165. S.B. 4278, 2019–2020 Leg., Reg., Sess. (N.Y. 2019), https://www.nysenate.gov/legislation/bills/2019/S4278 [https://perma.cc/4WNF-TWGN].

166. S. Res. 4278, 2019-2020 Leg., Reg. Sess. (N.Y. 2019).

167. *See id.*

168. *See, e.g.*, Ltr. to Gov. Andrew Cuomo from Judge Nelson Diaz, Treasurer of the Latino Corp. Directors Ass'n (Dec. 9, 2019) (in N.Y. Bill Jacket, S.B. 4278, Ch. 747 (2019), available on Westlaw).

report of actions taken to promote gender diversity on their boards and future action plans," as enacted, the law requires only that a report of current data be provided to the state.[169] The first report, issued in February 2022, indicated that 25.8% of the directors of domestic and foreign business corporations registered to do business in New York were women.[170] While this number pales in comparison to the estimated 53% of people living in New York identifying as women, the statute provides no clear next step or imperative for change.[171] Moreover, data aggregation means that companies with few or no women directors are not subject to public scrutiny. While data collection may be a necessary precursor to change, disclosure alone seems unlikely to meaningfully drive change.

D. Nonprofit Fiduciary Duties

Moral persuasion has failed to compel significant increases in nonprofit board diversity. As described above, the potential for IRS regulation or state corporate law to produce meaningful progress is dim. Given these challenges, a more robust explication of director fiduciary duties may be the best tool to drive progress. Nonprofit directors owe fiduciary duties of care[172] and loyalty[173] to their organizations. Though not universally acknowledged and sometimes subsumed within the duty of care or loyalty,[174] many scholars and some courts add to the list of duties owed by nonprofit directors a distinct duty of obedience.[175] This Section begins by describing each of these fiduciary duties and then briefly addresses how they are enforced.

---

169. N.Y. Spons. Memo., 2019 S.B. 4278.

170. N.Y. DEPT. OF STATE, REPORT: WOMEN ON CORPORATE BOARDS PURSUANT TO THE WOMEN ON CORPORATE BOARDS STUDY ACT (Feb. 1, 2022) https://dos.ny.gov/system/files/documents/2022/02/women-on-corporate-boards-2022_0.pdf [https://perma.cc/5NRA-JRC8].

171. *See* S.B. 4278, 2019 Leg., Reg. Sess. (N.Y. 2019) In its first annual report, the Maryland Comptroller reported similar data. COMPTROLLER OF MD., 2021 REPORT ON BOARD DIVERSITY (Jan. 26, 2021). Of the approximately 62,000 businesses that reported the number of women on their boards, women represented 30.64% of board members. *Id.* When the reporting companies were more narrowly defined to include only those headquartered in Maryland and to exclude sole-proprietorships, 38.8% of directors were women. *Id.*

172. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.03 (AM. L. INST. 2022); MODEL NONPROFIT CORP. ACT § 830(a)(1) and (2) (AM. BAR ASS'N 2021).

173. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.03 (AM. L. INST. 2022); MODEL NONPROFIT CORP. ACT § 8.30(a)(3) (AM. BAR ASS'N 2021).

174. *See, e.g.*, Alan Palmiter, *Duty of Obedience: The Forgotten Duty*, 55 N.Y. L. SCH. L. REV. 457, 469–70 (2010) (explaining that the Revised Model Nonprofit Corporation Act "assumes the duty of obedience is subsumed in the duties of care and loyalty").

175. *See, e.g.*, Summers v. Cherokee Children & Family Services, Inc., et al., 112 S.W.3d 486, 504 (2002) ("The central purpose of fiduciary duties of officers and directors of nonprofit corporations is to ensure that a corporation's resources are used to achieve the corporation's purposes. . . .") (quoting *Developments in the Law—Nonprofit Corporations*, 105 HARV. L. REV. 1578, 1601 (1992)); Thomas Lee Hazen & Lisa Love Hazen, *Duties of Nonprofit Corporate Directors—Emphasizing Oversight Responsibilities*, 90 N.C. L. REV. 101, 120–25 (2012).

1. Duty of Care

The duty of care requires that nonprofit directors "act in good faith with the care a person of ordinary prudence in a like position would exercise under similar circumstances."[176] This action and process-focused duty requires that directors oversee the organization and make decisions with a "degree of diligence, attention, care and skill."[177] Practically, this duty focuses on the level and type of attention paid by directors and whether they seek and rely on adequate information when making decisions.[178] Breaches of the duty of care are most likely when directors ignore or neglect to seek relevant information when making decisions or fail entirely to engage in oversight.[179] Importantly, the duty of care does not impose a fixed standard of diligence and is not limited to a certain type of decision or subject matter.[180] Instead, by focusing on a director's actions relative to that of a person "in a like position . . . under similar circumstances," the duty of care imposes expectations on directors based on their knowledge, expertise, and role within the organization with respect to all decisions and actions (or inactions) which they undertake.[181] As such, the duty of care attaches to all material board actions, including but not limited to the approval of budgets and major transactions, the hiring and supervision of the CEO, and most importantly here, the operation and perpetuation of the board itself.[182]

In the seminal case applying a traditional corporate standard of care to nonprofit directors, the D.C. District Court in *Stern v. Lucy Webb Hayes National Training School for Deaconesses and Missionaries*,[183] found that volunteer directors of Sibley Hospital who did not object over a span of ten years when committee meetings were not held and who disregarded annual audit reports failed to exercise "even the most cursory supervision" over management and its handling of the organization's charitable funds.[184] The court condemned the "[t]otal abdication of the [directors'] supervisory role,"[185] and in doing so, highlighted the "duty of attention,"[186] which demands that directors engage in substantive meetings and request and review materials relevant to their decisions.[187]

---

176. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.03(a) (AM. L. INST. 2022).

177. FISHMAN ET AL., *supra* note 3, at 152.

178. *See* RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.03 cmt. a (AM. L. INST. 2022); ABA GUIDEBOOK, *supra* note 40, at 26–29.

179. *See* RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.02 cmt. a (AM. L. INST. 2022).

180. Harvey J. Goldschmid, *The Fiduciary Duties of Nonprofit Directors and Officers: Paradoxes, Problems and Proposed Reforms*, 23 J. CORP. L. 631, 641–43 (1998).

181. *See id.* at §2.03 cmt. b.

182. *See* Michael W. Peregrine & James R. Schwartz, *Revisiting the Duty of Care of the Nonprofit Director*, 36 J. HEALTH L. 183, 188–89 (2003).

183. 381 F. Supp. 1003 (D.D.C. 1974).

184. *Id.* at 1016. Nonprofit fiduciary standards evolved from both trust and business corporation standards, but are now generally acknowledged to more closely reflect the standards applied to directors of for-profit business corporations. *See* Evelyn Brody, *Charity Governance: What's Trust Law Got to Do with It?,* 80 CHICAGO KENT L. REV. 641, 651–55 (2005); Fishman, *Development*, *supra* note 5, at 645–50.

185. *Stern*, 381 F. Supp. at 1014.

186. FISHMAN ET AL., *supra* note 3, at 152.

187. *See Stern*, 381 F. Supp. at 2014.

This duty of attention requires active participation by directors, including "tak[ing] steps to become knowledgeable about background facts and circumstances before taking action."[188]

In addition to the obligation to pay attention, the duty of care requires informed decisionmaking.[189] Indicia that a board has engaged in informed decisionmaking includes evidence that the board received written or oral presentations supporting a decision, heard from outside experts, and had the time and opportunity to deliberate on a decision.[190] A failure to engage in informed decisionmaking is described in *In re Lemington Home for the Aged*.[191] In this case, unsecured creditors of a nursing home successfully argued that the organization's directors breached their duty of care by failing to remove the organization's CEO despite receiving specific and reliable reports of her actual incompetence, mismanagement, and failure to provide the services for which she was being compensated.[192] The court explained that by ignoring their actual knowledge of mismanagement, the nursing home's directors had "stuck their heads in the sand in the face of repeated signs" of mismanagement.[193]

More recently, the U.S. Bankruptcy Court determined that a bankruptcy trustee had sufficiently alleged a duty of care claim[194] against the directors of a charity who had failed to monitor or develop any monitoring system with respect to the organization's assumption of debt.[195] Despite the existence of a policy that limited the organization's ability to take on extensive debt and being aware that the organization intended to enter into a number of loans that would leave the organization effectively insolvent, the directors, "though aware of the looming, future problem, did nothing to stop or limit the impact borrowing."[196] In short, to satisfy their duty of care, directors must not ignore information that illuminates an impending risk to the organization or policies intended to protect the organization from such risks.[197]

188. FISHMAN ET AL., *supra* note 3, at 152–53.

189. *Id.*

190. *Id.*

191. 777 F.3d 620 (3d Cir. 2015).

192. *Id.* at 624–30.

193. *Id.* at 630.

194. The claim was based on an alleged breach of the *Caremark* duty of care. In re Wonderwork, Inc., 626 B.R. 94, 121 (Bankr. S.D.N.Y. 2020). Following the development of for-profit corporate law, the duty of care has been described as encompassing a duty to monitor an organization's compliance with law. *See* Alon-Beck et al., *Duty*, *supra* note 97, at 113. This component of the duty of care requires that directors "attempt in good faith to assure that a corporate information and reporting system, which the board concludes is adequate, exists." In re Caremark Int'l Inc. Derivative Litig., 698 A.2d 959, 970 (Del. Ch. 1996). A failure to satisfy this obligation exists when directors act (or fail to act) in bad faith, which is defined as "a systematic and sustained failure to address compliance" together with a "conscious knowing failure to serve the firm." Alon-Beck et al., *Duty*, *supra* note 97, at 113 (referencing Stone ex rel. AmSouth Bancorporation v. Ritter, 911 A.2d 362 (Del. 2006) (en banc)).

195. *Wonderwork*, Inc., 626 B.R. at 121; In re Wonderwork, Inc., Case No. 16-13607, Final Report of Jason R. Lilien, Examiner, page 1 (Bankr. S.D.N.Y. Nov. 03, 2017).

196. *Wonderwork*, 626 B.R. at 121 (Bankr. S.D.N.Y. 2020).

197. *See id.*

Liability for and inquiries into breaches of the duty of care are limited by the best judgment rule, also called the business judgment rule.[198] This rule provides a defense against a duty of care claim when a nonprofit director can demonstrate that they made a good faith decision after being adequately informed, regardless of the eventual outcome of such a decision.[199] Directors are not protected from liability, however, when they fail to "consider all material facts reasonably available," have a conflict of interest, "do not act in good faith," or "act in a manner that cannot be attributed to a rational business purpose."[200] Furthermore, the rule protects against liability only when directors have exercised discretion and made a deliberate decision.[201] In short, a director may be held liable when they act with "'conscious indifference' or an 'I don't care' attitude."[202] The effect of this rule is to make paramount the processes through which directors make decisions. If the process is meaningful and the decision is made in good faith, a board's decision will not be second-guessed by a court.[203]

2. Duty of Loyalty

The duty of loyalty consists of both affirmative and negative obligations relating to the interests of the organization and its directors.[204] Affirmatively, it requires that a director "act in good faith" and in a manner they reasonably believe "to be in the best interests of the charity in light of its purposes."[205] At the same time, a director must not

---

198. The business judgment rule, a protective doctrine developed in the context of for-profit corporations, has been adopted and adapted in the nonprofit context. *See* Oberly v. Kirby, 592 A.2d 445, 462 (Del. 1991) (describing that the decisions of charitable fiduciaries, including with respect to the election of directors, are owed deference so long as they do not pose "a palpable and identifiable threat" to the charitable organization's goals).

199. FISHMAN ET AL., *supra* note 3, at 154; *see also* Adediran, *Board Composition*, *supra* note 11, at 374 ("Simply, the board will likely satisfy its duty of care if it acts with common sense and informed judgment even though its assessment is fundamentally flawed.").

200. Armenian Assembly of Am., Inc. v. Cafesjian, 772 F. Supp. 2d 20, 104 (D.D.C. 2011) (quoting Behradrezaee v. Dashtara, 910 A.2d 349, 361 (D.C. 2006)).

201. *See* Panel of New York State Board of Regents, Report and Recommendations After a Hearing to the Full Board of Regents at 30, Committee to Save Adelphi v. Diamandopoulos (Feb. 5, 1997), https://folio.iupui.edu/bitstream/handle/10244/502/THE%20COMMITTEE%20TO%20SAVE%20ADELPHI.pdf?sequence=1 [https://perma.cc/S9PN-LKN3] (describing the inapplicability of the business judgement rule when the trustees of a university acted "blindly, recklessly and heedlessly" in failing to analyze or approve the compensation of the president). In some states, including Delaware, the protections available to nonprofit directors go even further to preclude liability unless the director engaged in an "act or omission constituting willful and wanton or grossly negligent conduct." DEL. CODE ANN. tit. 10 § 8133 (2022).

202. Sama v. Mullaney (In re Wonderwork, Inc.), 611 B.R. 169, 198 (Bankr. S.D.N.Y. 2020).

203. *See* Michael W. Peregrine & James R. Schwarz, *The Business Judgment Rule and Other Protections for the Conduct of Not-for-Profit Directors*, 33 J. HEALTH L. 455, 455–56 (2000); Joseph Mead & Michael Pollack, *Courts, Constituencies, and the Enforcement of Fiduciary Duties in the Nonprofit Sector*, 77 U. PITT. L. REV. 281, 303 (2016).

204. *See* Brummer & Strine, *supra* note 47, at 69–70.

205. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 2.02(a) (AM. L. INST. 2022). Notwithstanding that a director must act in a manner they believe to be in the best interest of the charity, the commentary to the Restatement clarifies that the duty of loyalty is owed "to the purposes of the charity," rather than to the charitable organization itself. *Id.* cmt. a. As such, directors may be expected to make decisions that

"caus[e] harm . . . by acts such as unfair self-dealing or the usurpation of corporate opportunities."[206] Collectively, these obligations require that directors make decisions that further the interests of the organization, rather than promoting their own interests or the interests of a select group to the detriment of the organization.[207] Practically, this duty is often most relevant when a director's financial interests conflict with the organization's interests in a proposed transaction or when a director abuses their position to defraud or divert organizational assets.[208] The duty of loyalty is not, however, narrowly confined to the protection of organizational financial interests.[209]

The confluence of the affirmative and negative obligations under the duty of loyalty is evident in *Fitzgerald v. National Rifle Association of America*,[210] where the directors of a nonprofit corporation were found to have breached their duty of loyalty to the organization.[211] On behalf of its directors, the National Rifle Association of America (NRA) refused to publish a paid advertisement from a member of the organization who sought to run as a candidate for the board of directors.[212] Explaining that "it is well established that the directors and officers cannot manipulate the affairs of the corporation primarily with the intent of securing control of the corporation to one faction," the court held that the directors were prohibited from using organization resources to "perpetuate themselves in office."[213] Rather than focusing on financial conflicts of interest, the court in *Fitzgerald* identifies the interest of directors in maintaining their authority and power as being in potential conflict with the best interests of the organization.[214]

---

further the charitable purposes but negatively impact, or even lead to the dissolution of, the charitable organization. *Id.*

206. Brummer & Strine, *supra* note 47, at 69 (footnote omitted).

207. Mead & Pollack, *supra* note 203, at 305–06. *See* Armenian Assembly of Am., Inc. v. Cafesjian, 772 F. Supp. 2d 20, 103 (D.D.C. 2011) (explaining that to satisfy their duty of loyalty, a director "must manage the corporation solely in its best interest, not as a vehicle for promoting their personal beliefs or causes" (quoting Friends of Tilden Park, Inc. v. District of Columbia, 806 A.2d 1201, 1210 (D.C. 2002))); Shepherd of the Valley Lutheran Church v. Hope Lutheran Church, 626 N.W.2d 436, 442 (Minn. Ct. App. 2001) (upholding a jury verdict that an officer who secretly acted for the benefit of one faction of a church congregation had acted in ways that conflicted with the interests of the organization).

208. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 2.02(a) cmt. a, Reporters Note 5 (AM. L. INST. 2022).

209. See RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. § 2.02(a) cmt. a (AM. L. INST. 2022).

210. 383 F. Supp. 162 (D.N.J. 1974).

211. *Id.* at 167. As a case relating to the rights of members of a nonprofit corporation in relation to its board of directors, this decision in many ways is more akin to a for-profit fiduciary duty claim. Nevertheless, the NRA was organized as a New York not-for-profit corporation. *Id.* at 165.

212. *See id.* at 166.

213. *Id.* at 165, 166; *see also* Shepherd of the Valley Lutheran Church v. Hope Lutheran Church, 626 N.W.2d 436, 442 (Minn. Ct. App. 2001) (describing that nonprofit fiduciary duties are "owed to all persons who have equal interests" and not just to those with whom a director agrees).

214. *See Fitzgerald*, 383 F. Supp. at 166.

3. Duty of Obedience

The duty of obedience requires that nonprofit directors "ensure that the corporation acts within its proper purpose and mission"[215] because the "perpetuation of particular activities are central to the *raison d'etre* of [a charitable] organization."[216] Though not universally recognized and infrequently relied upon by courts,[217] the duty of obedience is described as being "central to the legitimacy of the [nonprofit] corporation"[218] and as "the foundation on which the duties of care and loyalty ultimately rest."[219] When viewed as such, this duty is the means by which nonprofit directors are held accountable for the impact of their decisions and whether their organization operates in a manner consistent with its specified mission.[220] As such, directors are expected to be "principally concerned about the effective performance of the nonprofit's mission."[221] As described by Professor Rivers James, the duty of obedience "limits directors' activities to those which are in accord with an organization's mission."[222]

In *Manhattan Eye, Ear & Throat Hospital v. Spitzer*,[223] the New York County Supreme Court rejected a struggling hospital's plan to sell all of its real estate.[224] Having decided that a sale of its Manhattan real estate was necessary, the hospital board then concluded it was necessary to "deprioritize" its current mission of operating a teaching hospital and instead open outpatient treatment centers.[225] In the process of considering potential purchasers of the real estate, the hospital received multiple merger proposals which would have resulted in the hospital's board being dissolved but the operation of the teaching hospital continuing.[226] Explaining that the job of the board was to take "all reasonable efforts to preserve the mission which has been the object of its

215. Hazen & Hazen, *Punctilios*, *supra* note 79, at 377–78; *see also* Palmiter, *supra* note 174, at 466–71.

216. Manhattan Eye, Ear & Throat Hosp. v. Spitzer, 715 N.Y.S.2d 575, 593 (N.Y. Sup. Ct. 1999) (quoting VICTORIA B. BJORKLUND, DANIEL L. KURTZ, JAMES J. FISHMAN & KAREN ALINAUSKAS, NEW YORK NONPROFIT LAW AND PRACTICE: WITH TAX ANALYSIS 414, § 11-4(a) (1997)).

217. *See* Jeremy Benjamin, Note, *Reinvigorating Nonprofit Directors' Duty of Obedience*, 30 CARDOZO L. REV. 1677, 1690 (2009).

218. Palmiter, *supra* note 174, at 467.

219. Rob Atkinson, *Obedience as the Foundation of Fiduciary Duty*, 34 J. CORP. L. 43, 45 (2008).

220. Anna Gentry, Comment, *Corporate Personhood and Nonprofit Director Duty of Obedience: Legal Implications That Necessitate Expanded Standing to Sue*, 23 GEO. MASON L. REV. 165, 179 (2015) ("[U]nlike the corporate directors who must answer to shareholders, a nonprofit director without a fiduciary duty of obedience effectively becomes an agent without a principal."). *See, e.g.*, Queen of Angels Hosp. v. Younger, 136 Cal. Rptr. 36, 41 (Cal. Ct. App. 1977) (finding that an organization's proposed use of its assets to operate medical clinics rather than a hospital, as required in its governing documents, would be impermissible); *Manhattan Eye, Ear & Throat Hosp.*, 715 N.Y.S.2d at 593–97; *infra* notes 223–228.

221. Summers v. Cherokee Children & Fam. Servs., Inc., 112 S.W.3d 486, 504 (Tenn. Ct. App. 2002) (quoting Harvey J. Goldschmid, *The Fiduciary Duties of Nonprofit Directors and Officers: Paradoxes, Problems and Proposed Reforms*, 23 J. CORP. L. 631, 641 (1998)).

222. Rivers James, *Pluralism*, *supra* note 77, at 102.

223. 715 N.Y.S.2d 575 (N.Y. Sup. Ct. 1999).

224. *Id.* at 597.

225. *Id.* at 582, 596.

226. *Id.* at 583, 588–92.

stewardship,"[227] the court determined that the board had failed to center the hospital's stated charitable purpose in its decision making. Instead, the court held that "[i]t appear[ed] that the Board confused preservation of the Hospital with preservation of the Board, when the appropriate calculus should be what is good for the Hospital is good for the Board."[228] In essence, the charitable organization's mission must be centered, with all other decisions and priorities being ancillary.

4. Standing to Bring Fiduciary Breach Claims

While the fiduciary duties of nonprofit directors largely mirror and have principally evolved out of similar duties owed by directors of for-profit corporations, the means of enforcing nonprofit and for-profit fiduciary duties are distinct. In contrast with the ability of shareholders to bring derivative fiduciary breach claims, nonprofits' interest holders largely lack such recourse.[229] With limited exceptions, standing to bring a claim of breach of nonprofit fiduciary duties is limited to the attorney general in the state in which a charity operates and to fellow directors.[230] This limitation generally precludes many direct stakeholders—including an organization's clients, beneficiaries, and donors—from holding nonprofit directors accountable for breaches of their fiduciary duties.[231] While the debate about appropriate standing is outside the scope of this Article, the current state of the law emphasizes the central role of attorneys general as state charity regulators in ensuring that nonprofit directors fulfill their duties.

---

227. *Id.* at 595.

228. *Id.* at 596.

229. ABA GUIDEBOOK, *supra* note 40, at 11 (describing how "the absence of a mechanism for direct action and oversight by beneficiaries on nonprofit organizations leaves an accountability vacuum"). Nonprofit stakeholders also lack other means of influence available to shareholders, like proxy access, which can allow shareholders to nominate director candidates. *See generally* Margeaux Bergman, *How the "Exception" Becomes the Standard*, 17 HASTINGS BUS. L.J. 405 (2021).

230. *See* Commonwealth v. New Foundations, Inc., 182 A.3d 1059, 1070 (Pa. Commw. Ct. 2018) ("[I]t is the duty of the Attorney General to ensure that the purpose of the charity remains charitable and to take such action necessary to make sure the charity carries out it[s] charitable purpose and take necessary corrective action."); Mead & Pollack, *supra* note 203, at 297–98. In the case of a membership nonprofit corporation, members may also have standing to bring such a claim. Given the focus of this Article on public charities, which typically are not membership corporations, such standing is outside the scope of consideration here. In the event of a nonprofit corporation's bankruptcy, the bankruptcy trustee may also have standing to bring fiduciary duty claims against directors. *See, e.g.*, In re Wonderwork, Inc., 626 B.R. 94 (Bankr. S.D.N.Y. 2020); In re Lemington for the Aged v. Baldwin, 777 F.3d 620 (3d Cir. 2015); In re Newark Watershed Conservation & Dev. Corp. v. Watkins-Breashear, 560 B.R. 129 (Bankr. D.N.J. 2016).

231. *See generally* Rob Atkinson, *Unsettled Standing: Who (Else) Should Enforce the Duties of Charitable Fiduciaries?*, 23 J. CORP. L. 655 (1998); Gentry, *supra* note 220; Joshua B. Nix, *The Things People Do When No One Is Looking: An Argument for the Expansion of Standing in the Charitable Sector*, 14 U. MIAMI BUS. L. REV. 147, 176–78 (2005).

IV. A FIDUCIARY DUTY TO FLIP THE TABLES

In both legal and practical ways, nonprofit directors' duties of care, loyalty, and obedience set the guardrails within which boards endeavor to operate.[232] In the few and infrequent situations where claims are brought against directors, the failure to meet minimal expectations of director conduct are alarming.[233] In some situations, seemingly egregious director conduct is not challenged in court, but is instead used as an instructive story to shape the conduct of other charities.[234] Far more frequently, the good and effective work of nonprofit boards is shaped by the expectations of "normatively good behavior," as encapsulated in the fiduciary duties of directors.[235] One can hope that as focus on the beneficial impact of board diversity is recognized and related action is viewed as part of those normative expectations, any hesitancy or apathy of boards which has prevented their goodwill from leading to increased diversity will be outweighed by the adoption of accepted and expected practices.[236] Although there is little discussion in published fiduciary duty claim decisions about the actions of nonprofit boards and their nominating committees with respect to new director selection,[237] the centrality of these decisions to the fulfillment of a public charity's mission suggests that the processes and decisions regarding director selection should be subject to rigorous scrutiny.[238]

---

232. *See* Anat Alon-Beck, Michal Agmon-Gonnen & Darren Rosenblum, *No More Old Boys Club: Institutional Investors' Fiduciary Duty to Advance Board Gender Diversity*, 55 U.C. DAVIS L. REV. 445, 450 (2021) [hereinafter Alon-Beck et al., *No More Old Boys Club*].

233. *See, e.g.*, *Wonderwork*, 626 B.R. 94; Panel of N.Y. State Bd. of Regents, Report and Recommendations After a Hearing to the Full Board of Regents, Comm. To Save Adelphi v. Diamandopoulos at 33, (Feb. 5, 1997).

234. *See* Evelyn Brody, *The Limits of Charity Fiduciary Law*, 57 MD. L. REV. 1400, 1409–10 (1998) ("Reform rather than punishment is generally the goal of the charity regulator . . . ."). *See, e.g.*, Ltr. to Comm'r Carlos Santiago from Off. of the Att'y Gen., Commonwealth of Mass., (Mar. 13, 2019). In a fourteen-page letter to the Commissioner of Education, the Non-Profit/Public Charities Division of Office of the Attorney General of Massachusetts highlighted the conduct and communications of the board of directors of Mount Ida College prior to its precipitous closure. Despite concluding that the board's "decision-making fell short of what is expected of a charitable board in meeting its obligations," the attorney general's office determined that the school's closure and lack of assets meant that "pursuing litigation would be costly, time-consuming, and of limited public benefit," and that public disclosure of the office's investigative findings would be more likely to prevent similar failures by others. *Id.* at 2–3.

235. Alon-Beck et al., *Duty*, *supra* note 97, at 100. As described by Professors Chris Brummer and Leo E. Strine, Jr., also former Chief Justice and Chancellor of the State of Delaware, "as a matter of director reputation and public scrutiny, the directors' normative duty to act with due care still has great importance." Brummer & Strine, *supra* note 47, at 69.

236. Brummer & Strine, *supra* note 47, at 92 (describing that "history shows that our ability to stay focused on issues of inequality is erratic," and yet "fiduciary duty pushes [directors] . . . to focus on these important issues as part of their duty to promote the best interests of the corporation").

237. ABA GUIDEBOOK, *supra* note 40, at 77. *But see* Oberly v. Kirby, 592 A.2d 445, 463 (Del. 1991) (explaining that the sole member of a nonstock corporation did not violate his fiduciary duties by naming his wife and children as members and directors).

238. As recognized by Professor Alon-Beck and her colleagues, "[f]iduciary duties may seem at first blush an odd location within corporate law for . . . equality," and yet they are an established site where the "State articulates the behavior expected of duty holders . . . to act in ways that reflect widely accepted public governance norms." Alon-Beck et al., *No More Old Boys' Club*, *supra* note 232, at 450.

This final Section argues that existing nonprofit director fiduciary duties necessitate that charitable boards take affirmative steps to consider the potential impact a more diverse board would have on the accomplishment of their missions. Once aware of the potential benefit, a board may also have a duty to act to elevate the interests of the organizations over their own interests by electing directors whose expertise and life experiences will promote fulfillment of the organization's charitable mission.[239] Here, the duty of care's demand to pay attention and make informed decisions creates the process by which boards satisfy the duties of loyalty and obedience to center the best interests and mission of their organizations.[240] Woven together in this way, the duties of care, loyalty, and obedience require an attentiveness to board composition that has not been sufficiently articulated as a legal duty. Enforcement and oversight of the fulfillment of these duties, focusing on the duty of care's process demands, can best be accomplished through existing state charity disclosure processes.

A. Duty of Care & Board Diversity

As described by the Charities Division of the Office of the New York State Attorney General in a guide for new nonprofit directors, "[i]n exercising the duty of care, a responsible board of directors should, among other things . . . [e]ncourage diversity among board members. Diversity will help [e]nsure a board committed to serve the organization's mission with a range of appropriate skills and interests."[241] This articulation of attentiveness to board composition as a component of the duty of care is an example of how state attorneys general should describe a more robust understanding of the duty of care.[242]

In satisfying their duty of care, nonprofit directors are expected to pull their heads out of the sand[243] and attend to the realities of their organization and the world around

---

239. *See infra* Part IV.A.2.

240. *See infra* Part IV.A.

241. CHARITIES BUREAU, OFF. OF THE N.Y. STATE ATT'Y GEN., RIGHT FROM THE START: RESPONSIBILITIES OF DIRECTORS OF NOT-FOR-PROFIT CORPORATIONS, 5–6 (May 15, 2015), https://ag.ny.gov/sites/default/files/2023-02/directors-notforprofit-corporations.pdf [https://perma.cc/PW7V-BLMB].

242. In the context of a state law seemingly aimed at limiting insider transactions, the New Hampshire Attorney General's Office includes a section in its guide for nonprofit directors entitled "The Board Must Be Diverse." The guide then proceeds in the next section to describe the fiduciary duties of directors without linking the two concepts. CHARITABLE TRUSTS UNIT, OFF. OF THE ATT'Y GEN. OF N.H., GUIDEBOOK FOR NEW HAMPSHIRE CHARITABLE ORGANIZATIONS 3–4 (2022), https://www.doj.nh.gov/charitable-trusts/documents/guidebook-non-profit-organizations.pdf [https://perma.cc/MZ7K-78VY]. In a guide funded by the Illinois State Treasurer's Officer Charitable Trust Program and endorsed by the state Attorney General, one key principle described is that an organization's board should "ensure[] that its members are competent and knowledgeable, and [that it] includes and seeks diverse points of view and experience as needed to provide credible and effective oversight of all aspects of the nonprofit's work." FOREFRONT, ILLINOIS NONPROFIT PRINCIPLES AND BEST PRACTICES 2020 5 (2020), https://myforefront.org/wp-content/uploads/2019/09/Nonprofit-Best-Practices-2020.pdf [https://perma.cc/6FXE-QKB2] (last visited Apr. 1, 2023). Though this guide does not explicitly refer to fiduciary duties, it appears intended to describe the steps boards should take to fulfill those duties. See *id*.

243. *See* In Re Lemington Home for the Aged, 777 F.3d 620, 630 (3d. Cir. 2015).

it. When that reality calls for diligence and action, nonprofit directors satisfy their duty by fulfilling the "duty of attention" and engaging in informed decisionmaking.[244] Notwithstanding the general deference to the business or best judgment of a board, failure to acknowledge readily apparent facts or to act on such information can constitute a breach of the fiduciary duty of care.[245]

One of the essential responsibilities of a nonprofit board is the selection and recruitment of new board members.[246] In carrying out this responsibility, directors should be aware of their organization's specific needs along with readily available information about the sector. As the benefits of increased board diversity are better and more clearly articulated, it becomes increasingly important for boards to be held accountable for failing to recognize and act on this compelling reality.

Various approaches to expanding the diversity of boards have been proposed, but many focus on ensuring that the pool of those considered is as broad as possible.[247] For nonprofits, which generally elect directors from a consensus slate, the nominating committee's role in setting director criteria, seeking a broad pool of candidates and recommending a diverse slate is paramount.[248] This work typically begins when the nominating committee evaluates the expertise and experiences the board needs and identifies existing gaps.[249] Having identified the board's needs, the nominating committee then seeks out possible candidates. As in the for-profit sector, increasing board diversity may require that the nominating committee look outside of its existing networks in establishing a pipeline of candidates.[250]

Though the duty of care does not prescribe the outcome of board decisions, it requires that if a decision is to be protected by the best judgment rule, that the decision must be made in good faith by an adequately informed board.[251] Practically speaking, then, boards need guidance about the processes by which they can meet this process standard. With respect to the diversity of their board, there are two discrete steps a board should take to "act in good faith with the care a person of ordinary prudence in a like position would exercise under similar circumstances." [252] First, in satisfying the duty of attention, boards should gather sufficient information to be aware of and understand the

244. FISHMAN ET AL., *supra* note 3, at 153.

245. *See generally* In re Lemington Home for the Aged, 777 F.3d 620 (3d Cir. 2015).

246. *See* ABA GUIDEBOOK, *supra* note 40, at 77 (explaining "the process used to determine board nominations obviously is of great importance to the corporation's future and its ability to carry out the corporation's mission"); Peggy Sasso, *Searching for Trust in the Not-for-Profit Boardroom: Looking Beyond the Duty of Obedience to Ensure Accountability*, 50 UCLA L. REV. 1485, 1509 (2003).

247. *See, e.g.*, Alon-Beck et al., *Duty*, *supra* note 97, at 109 (arguing that a slate which contains an equal number of men and women is more likely to produce a representative board).

248. *See generally* NAT'L COUNCIL OF NONPROFITS, *supra* note 6.

249. *See* Hazen & Hazen, *Punctilios*, *supra* note 79, at 399 (explaining that some failures of effective board oversight are attributed to the failure of an organization to have "appropriate selection criteria" which in turn leads to "too many rubber stamp directors").

250. *See supra* Part III.A.

251. *See* discussion *supra* Part III.D.1.

252. RESTATEMENT OF THE L., CHARITABLE NONPROFIT ORGS. §2.03(a) (AM. L. INST. 2022).

potential benefits of increasing board diversity.[253] Second, with this knowledge in mind, boards should make informed decisions to seek out and elect a slate of directors with the greatest potential to drive the organization's fulfillment of its mission.[254]

1. Gathering Information

As described above, extensive scholarship analyzes and describes the impact of diverse leadership on organizations.[255] The arc of this work, even accepting certain challenges to establishing a causal relationship, suggests that more diverse boards lead to better financial performance.[256] Even more importantly, nonprofit organizations with more diverse boards are better situated to accomplish their charitable missions.[257] These broad sector-wide conclusions deserve to be considered and then applied in the context of each specific nonprofit organization. In the same way that nonprofit boards consider the professional expertise of their directors, boards should also consider the importance of the lived experiences that their directors bring to the table.

A board that turns a blind eye to information regarding the potential benefits of diversifying its own membership might be perceived as adopting a stance similar to the Sibley Hospital board in *Stern*, which acquiesced to a lack of meetings or information for nearly a decade.[258] A board's refusal to engage for an extended period of time does not negate the reality of the world around it. A board acting reasonably and in good faith cannot eschew information about how its own membership impacts the potential success of the organization.[259]

2. Seeking Out and Electing Directors

Directors, armed with knowledge, are held responsible when they fail to act.[260] A board that is aware of the potential benefits of increasing its own diversity and chooses not to act on this knowledge is acting like the board in *Lemington*, which was aware of its CEO's failures but chose to look away.[261] "If directors intentionally avoid diverse, potential nominees or [do] not practice due diligence in searching for the most capable candidates" to support a charity's mission and operations, they have failed to demonstrate a minimal level of attention or care.[262] Instead of looking away or avoiding diverse candidates, a board that is aware of the potential benefits of diversity and is exercising

253. *See supra* Part III.D.1.

254. *See supra* Part III.D.1.

255. *See supra* Part II.

256. *See* discussion *supra* Part II.A.

257. *See* discussion *supra* Part II.B.

258. *See* Stern v. Lucy Webb Hayes Nat'l Training Sch. for Deaconesses & Missionaries, 381 F. Supp. 1003 (D.D.C. 1974); *supra* Part III.D.1.

259. *See* Parmeter, *supra* note 38, at 104 (explaining that shareholders of a for-profit corporation could reasonably bring a claim against directors for failing to act as fiduciaries if those directors "intentionally avoid diverse, potential nominees or did not practice due diligence in searching for the most capable candidates to maximize financial return for the shareholders").

260. *See supra* Part III.D.1.

261. *See* In re Lemington Home for the Aged, 777 F.3d 620 (3d Cir. 2015); *supra* Part III.D.1.

262. *See* Parmeter, *supra* note 38, at 104.

its duty of care will establish a process for identifying and electing directors who have the greatest potential to advance the organization's mission.

These two steps are consistent with and should ideally be part of a routine and broader process of evaluating and adapting (as necessary) the structure of the board. As described by the American Bar Association's Coordinating Committee on Nonprofit Governance, a board structure review should include establishing a comprehensive "process to critically review how effectively the board oversees organization operations and management," gathering information from a wide swath of those within the organization and peer organizations, documenting what is learned, what changes are recommended, and how the board responds to those recommendations.[263] The effectiveness of such a review process depends, in part, on there being "no sacred cows," meaning no structures or policies that are above scrutiny and reconsideration.[264] Collectively, the implementation of a meaningful process for considering the potential value of a more diverse board and the development of responsive board recruitment policies will demonstrate that a board is acting in good faith. Such a demonstration will allow a nonprofit board, regardless of its ultimate board composition, to rely on the best judgment rule in rebutting allegations of a failure to meet the duty of care.[265]

B. Duty of Loyalty & Board Diversity

The duty of loyalty is generally invoked in instances where a director's financial interests are at stake, and it is not commonly associated with the actions of the nominating committee.[266] Yet, the requirement to prioritize an organization's interests over an individual director's interests applies in nonfinancial contexts. As in *Fitzgerald*, the duty of loyalty is at stake when directors act to protect their own roles and to replicate a like-minded board.[267] When directors, as organization leaders, act in a manner that preserves their power, there is a question of whether they are acting in the best interest of the nonprofit. As discussed by Professor Alon-Beck and colleagues, through the nomination and election of new directors, "[d]irectors are able to enhance their preexisting social and professional networks, increasing their overall societal influence and prestige."[268] The reciprocal benefits that directors may reap, whether social, business, political, or otherwise, by selecting like-minded people to serve with them on a nonprofit board cannot be ignored.

Furthermore, when boards consist of like-minded, externally connected individuals, there is a higher risk that directors may hesitate to dissent or may be more likely to

263. ABA POST-SARBANES-OXLEY GUIDE, *supra* note 7, at § III.B ¶ 6.

264. *Id.*

265. *See* Bergman, *supra* note 229, at 416–17. While the business judgement or best judgment rule arguably creates a "steep uphill battle . . . to demonstrate directors have breached their fiduciary duty for failing to diversify their boards," *id.* at 417, the standard by which director action is judged should be used as a guide in determining the minimum standards by which boards operate.

266. *See e.g.,* GUIDEBOOK FOR NEW HAMPSHIRE CHARITABLE ORGANIZATIONS, *supra* note 242, at 7–8.

267. Fitzgerald v. Nat'l Rifle Ass'n of Am., 383 F. Supp. 162, 166 (D.N.J. 1974).

268. Alon-Beck et al., *Duty*, *supra* note 97, at 108. While Professor Alon-Beck and her colleagues are focused on for-profit company directors and the way power is leveraged when directors serve on interlocking boards, the observation is equally true when directors act in the charitable sector.

approve transactions that involve financial conflicts of interest.[269] The IRS and many states already require disclosure of business and family relationships among nonprofit directors to prevent and detect interested party transactions that are not in the best interest of the organization.[270] The disclosure requirements proposed below should similarly provide insight into whether a board's examination of the potential value of increased diversity and resulting actions have resulted in a more or less interlocked board.

Admittedly, it is unlikely that social benefits or attenuated indirect financial benefits that a director receives from resisting efforts to increase board diversity would create a clear breach of that director's duty of loyalty to the organization. Nevertheless, situating the discussion around efforts to increase board diversity within the duty of loyalty importantly separates the discussion of what is best for the organization from what may be preferential or beneficial to its directors. In turn, it undergirds the essential focus on directors' fulfillment of their duty of care with respect to board composition.

C. Duty of Obedience & Board Diversity

The duty of obedience underpins, with respect to the diversity of nonprofit boards, the more concrete and identifiable duties of care and loyalty. The duty of obedience's focus on centering the organization's charitable mission "should obligate a board of directors to address its own composition" to prioritize the fulfillment of that mission.[271] Such centering of the organizational mission contrasts with the decisions made by the Manhattan Eye, Ear & Throat board, which appeared to prioritize the board's survival over the mission's continuation.[272] A more diverse board that is more representative of the communities served by an organization is more likely to be "culturally competent to govern and oversee effective work toward the organization's mission."[273] Assembling and maintaining such a board is a step toward fulfillment of the board's duty of obedience and the organization's charitable purposes.

D. Enforcing Duties of Diversity

Without wading into the lively debate about whether standing should be expanded to create greater accountability or narrowed to encourage participation and thoughtful risk-taking, this author recognizes that the power of redefined fiduciary duties as tools of

269. *See, e.g.*, Panel of New York State Bd. of Regents, Report and Recommendations After a Hearing to the Full Board of Regents, Comm. to Save Adelphi v. Diamandopoulos at 33, (Feb. 5, 1997) (describing failure of trustees to seek alternatives to insurance broker and advertising services provided by fellow trustees).

270. *See, e.g.,* IRS Form 990, Part VI, Section A, Line 2 (2021); FLA. DEP'T OF AGRIC. AND CONSUMER SERVS., DIV. OF CONSUMER SERVS., Solicitation of Contributions Supplemental Financial Disclosure, 2-3 (FDACS-10114 Rev. 11/14), https://forms.fdacs.gov/10114.pdf [https://perma.cc/S75Z-APH2]; COMMONWEALTH OF MASS., OFF. OF THE ATT'Y GEN., Non-Profit Organizations/Public Charities Division, Form PC, 6 (2020), https://www.mass.gov/doc/form-pc-2020-update/download [https://perma.cc/M5DR-SJBZ] (last visited Apr. 1, 2023).

271. Rivers, *Divide*, *supra* note 12, at 480.

272. *See* Manhattan Eye, Ear & Throat Hosp. v. Spitzer, 715 N.Y.S.2d 575 (N.Y. Sup. Ct. 1999); *supra* Part III.D.3.

273. Rivers James, *Pluralism*, *supra* note 77, at 103.

litigation is somewhat limited.[274] Nevertheless, more precise articulation of how a board's decisions with respect to its own composition implicate satisfaction of directors' fiduciary duties has the potential to influence how boards act, the information collected by state attorneys general, and how stakeholders are emboldened to hold boards accountable. State attorneys general have the ability, through educational efforts, existing disclosure processes, and targeted inquiries, to hold nonprofit boards accountable for satisfying their fiduciary duties relating to board diversity.[275]

Following the lead of states like New York, state charity regulators should articulate a robust understanding of nonprofit fiduciary duties that demands that directors consider how their board's composition impacts their organization's ability to accomplish its charitable mission. Such an articulation, through new guidance to directors and communications with the sector, has the potential to educate and influence nonprofit directors and leaders.

In addition to explicit education of directors, state charity regulators should leverage existing disclosure processes to hold nonprofit boards accountable. Disclosure does more than merely alert regulators to possible breaches; it educates and creates a measuring tool by which boards can assess their own compliance.[276] By illuminating otherwise inaccessible information, public disclosures also create space for public scrutiny and oversight.[277] The process of collecting information to be reported, together

274. If standing were expanded to allow more broadly for fiduciary breach claims to be brought by classes of beneficiaries, one can envision beneficiaries following the lead of shareholders of companies like Facebook and Oracle in alleging breaches based on the failure to align a board's actions with its professed commitment to greater diversity. *See, e.g.*, Natalie Ocegueda derivatively on behalf of Facebook v. Mark Zuckerberg et al., 526 F.Supp.3d 637 (N.D. Cal. 2021) (granting defendant's motion to dismiss a shareholder derivative claim alleging breaches of fiduciary duties of candor, good faith, and loyalty in failing to create a more substantively diverse and equitable company).

275. The varying degree to which state attorneys general engage in active oversight and engagement with the nonprofit organizations operating in their state, and have the resources necessary to do so, suggests that undertaking these efforts may be more feasible for some state charity regulators than others. *See generally* SHIRLEY ADELSTEIN & ELIZABETH T. BORIS, STATE REGULATION OF THE CHARITABLE SECTOR: ENFORCEMENT, OUTREACH, STRUCTURE AND STAFFING (Feb. 16, 2018), https://www.urban.org/sites/default/files/publication/96582/state_regulation_of_the_charitable_sector.pdf [https://perma.cc/Y6MA-QD47].

276. *See* Evelyn Brody, *Sunshine and Shadows on Charity Governance: Public Disclosure as a Regulatory Tool*, 12 FLA. TAX REV. 183, 213 (2012) ("Public disclosure – even in the absence of enforcement action –is useful because knowing that information will be disclosed induces the fiduciaries to pay more (and better) attention not just to how they report, but also to what they do."). For example, a study published in 2013 by then Massachusetts Attorney General Martha Coakley's office regarding CEO compensation raised awareness of executive compensation practices at some of the state's largest health care and education nonprofits. *See* Todd Wallack, *Martha Coakley Targets Nonprofit CEO Pay*, BOSTON GLOBE (Dec. 20, 2013, 12:14 AM), https://www.bostonglobe.com/metro/2013/12/19/massachusetts-attorney-general-raises-questions-about-nonprofit-executive-pay/RLy3owyQKcKk7nPgUkwjCO/story.html [https://perma.cc/LW2T-4MAR].

277. For example, many state charity regulators require that nonprofits disclose their transactions with directors and their related entities. *See, e.g.*, COMMONWEALTH OF MASS., OFF. OF THE ATT'Y GEN., Non-Profit Organizations/Public Charities Division, Form PC, 6 (2020), https://www.mass.gov/doc/form-pc-2020-update/download [https://perma.cc/M5DR-SJBZ] (last visited Apr. 1, 2023); FLORIDA DEP'T OF AGRICULTURE AND CONSUMER SERVICES, DIV. OF CONSUMER SERVICES, Solicitation of Contributions Supplemental Financial Disclosure (FDACS-10114 Rev. 11/14), https://forms.fdacs.gov/10114.pdf [https://perma.cc/S75Z-APH2].

with the regulator's parameters for reporting, can afford a nonprofit the opportunity to reevaluate existing processes.

When grounded in directors' fiduciary duties and subject to entity-level public disclosure, state charity regulator-required disclosure would avoid the limitations identified with respect to possible disclosure requirements under state corporate law or as potentially imposed by the IRS. In many states, existing structures for the public disclosure of charity filings could mitigate the hidden nature of entity-level data under the current New York and Maryland board diversity disclosure laws.[278] Building on the SEC's disclosure requirements,[279] state charity regulators could require disclosure of board diversity policies by nonprofit organizations as a means of monitoring compliance with the process demands of the duty of care. This focus on process is grounded in the duty of care's emphasis on whether a board of directors is paying attention and making informed decisions.[280] To facilitate compliance and broad adoption, states could provide sample policies that guide nonprofits in meaningfully considering their organization's needs and how their board membership may further its purposes. While each organization's approach necessarily should reflect how its unique charitable purpose and programs impact the relevancy of various forms of board diversity, a model policy could encourage organizations with limited resources to adopt a meaningful policy.

Building on the disclosure requirements of Nasdaq, state charity regulators could also ask nonprofits to provide aggregated racial, ethnic, gender, disability status, and sexual orientation data from their boards. Regulators might go one step further by asking nonprofits to provide comparable data, to the extent available, for the organization's clients. If a nonprofit's aggregate data does not reflect either the organization's clients or the broader community, state regulators could require an explanation of the disconnect, akin to the Nasdaq requirements.[281]

Finally, state attorneys general that embrace a robust understanding of nonprofit fiduciary duties, which encompasses an obligation to consider board diversity, should examine the impact of board composition when investigating other alleged breaches of fiduciary duties. The enforcement authority of state attorneys general with respect to fiduciary duties affords them authority, which the IRS arguably lacks under existing law, to hold nonprofits accountable.[282] Admittedly, investigations or litigation narrowly focused on a failure of attentiveness or informed decisionmaking with respect to board diversity are unlikely. Yet, by scrutinizing board nomination processes and holding directors accountable for prioritizing the satisfaction of their organization's charitable

---

278. Many states make individual charities' annual reports available to the public. *E.g.*, *Registered Charitable Organizations and Paid Solicitors*, ALASKA DEP'T OF L., CONSUMER PROTECTION UNIT, https://law.alaska.gov/department/civil/consumer/charities_list.html [https://perma.cc/7G52-2P47] (last visited Apr. 1, 2023); *Registry Verification Search*, STATE OF CAL. DEP'T OF JUST., https://rct.doj.ca.gov/Verification/Web/Search.aspx?facility=Y [https://perma.cc/2VZ3-9TAJ] (last visited Apr. 1, 2023); *Charities*, N.C. SEC'Y OF STATE, https://www.sosnc.gov/divisions/charities [https://perma.cc/BRD2-PNKD] (last visited Apr. 1, 2023).

279. *See supra* Part III.B.

280. See *supra* Part III.D.1.

281. *See supra* Part III.B.

282. SHIRLEY ADELSTEIN & ELIZABETH T. BORIS, STATE REGULATION OF THE CHARITABLE SECTOR: ENFORCEMENT, OUTREACH, STRUCTURE AND STAFFING (Feb. 16, 2018), https://www.urban.org/sites/default/files/publication/96582/state_regulation_of_the_charitable_sector.pdf [https://perma.cc/2HFS-QAGS].

mission, state attorneys general have the capacity to drive meaningful change in the leadership and success of nonprofit organizations.

CONCLUSION

The nonprofit sector holds a unique and influential position in U.S. society, and the directors of public charities hold seats at tables of significant power. There is a broad and growing consensus that greater diversity on nonprofit boards leads to better financial and mission performance and furthers underlying objectives of equality. Yet, there has been insufficient change to the composition of nonprofit boards over the last three decades. The goodwill and good intentions of boards that recognize the value of increasing their diversity are vital but alone have been insufficient. Models of regulator intervention at the federal and state business corporate law level, while intriguing, face similar hurdles and unique challenges related to the oversight system for nonprofits.

Application of long-standing understandings of nonprofit director fiduciary duties to the question of board composition and diversity demonstrates the potential for meaningful progress. The demands of attentiveness and informed decisionmaking, that undergird the duty of care, require that nonprofit directors be attuned to the relevance of diversity in recruiting new directors. The duty of loyalty mandates that boards, which by design are self-perpetuating, consider the possible benefit of breaking the cycle of replication and instead add new voices, perspectives, and lived experiences to the table. Only by prioritizing the organization's best interests, and eschewing possible self-interest in maintaining effective control, do nonprofit directors demonstrate their loyalty and obedience to an organization's charitable mission. State attorneys general, on behalf of all stakeholders, are uniquely situated to articulate and foster compliance with a newly articulated duty to flip the tables of power.