
Board of Directors

Directors of a Company

The **Board of Directors** of a company is the group of individuals who are charged with running the company. Other names include board of governors, board of managers, board of advisors, board of regents, board of trustees, and board of visitors. It is often simply referred to as "the board."

The duties of the board of directors and officers of the company are set by the corporate bylaws but are also set by law, specifically by the laws of the state where the business is incorporated.

One of the first tasks in starting a company is to set up a corporate board of directors. These individuals will guide the company through startup and operations, and they have overall responsibility for the operation of the company. In general, the responsibilities of the board of directors include fiduciary responsibility for the financial well-being of the company, responsibility to set the mission and vision of the company, and oversight in setting policy and reviewing actions of employees. Another fiduciary role is to ensure that the rights of minority shareholders, those without controlling interests, are not overlooked by those in control.

Officers of companies, as you will see, have specific duties relating to the overall board of directors duties. In smaller businesses, it is often the case that administrative duties are taken up by board officers. In this case, the liability of the individual is increased. For example, a corporate treasurer, whose duties are restricted to oversight and policy may also take on day-to-day financial responsibilities for paying bills and taxes. Wearing an executive employee hat may be necessary, but be aware that the day-to-day duties subject the individual to different types of liabilities. If payroll taxes are not paid, the corporate treasurer who had the responsibility to see that those taxes were paid may be held personally liable for the non-payment of those taxes. It's important to understand corporate board liability as you select and run your company.

Duties of a Board of Directors

The individuals who are selected to be on the board of directors of a company have overall responsibility for the activities of the company. The board acts on behalf of the shareholders to make overall policy decisions and provide oversight. A corporate board has great power and also great responsibility.

The board has the ultimate decision-making authority and, in general, is empowered to (1) set the company's policy, objectives, and overall direction, (2) adopt bylaws, (3) name members of the advisory, executive, finance, and other committees, (4) hire, monitor, evaluate, and fire the managing director and senior executives, (5) determine and pay the dividend, and (6) issue additional shares. Though all its members might not be engaged in the company's day-to-day operations, the entire board is held liable (under the doctrine of collective responsibility which states that every member who participates (or is supposed to participate) in a decision making group is (1) equally responsible for the consequences of the decisions taken, (2) should fully support and abide by the group's decisions (whether or not he or she participated in the decision making process), otherwise (3) should resign from the group. Specific duties of the board of directors and of individual board members, committees, and officers are set by the corporate bylaws. Here are the primary duties of a corporate board as a whole:

- **Fiduciary responsibility** - Corporate board members have a fiduciary responsibility to care for the finances and legal requirements of the company. They must act in good faith and with a reasonable degree of care, and they must not have any conflicts of interest. That is, the interests of the company must take precedence over personal interests of individual board members.
 - **Mission and Vision** - Board members are responsible for setting the mission of the company and assuring that all actions are related to and adhere to that mission. The board can change the mission, but only after careful deliberation.
 - **Oversight** - Corporate boards of directors do not participate in day-to-day decision-making; instead, they set overall policy, based on the corporate mission and vision, and they exercise an oversight function, reviewing the actions of corporate officers and executives.
 - **Annual Meeting** - At the annual meeting of the company, the board announces the annual dividend, oversees election of corporate board members, elects or appoints officers and key executives, and amends the bylaws, if necessary.
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Duties of Board Members

Here are the primary duties of corporate board members as individuals:

- **Duty of Care**, Board and their members have a duty of care to act in the best interest of the shareholders.
 - **Duty of loyalty**, putting board responsibilities above other outside interests.
 - **Duty of confidentiality**, keeping private the dealings and information from board meetings and company business.
 - **Personal vs. Corporate Assets**
 - Boards have a duty to avoid intermingling corporate and personal assets.
 - **Fiduciary duties**, for financial and legal matters including:
 - Avoiding conflicts of interest
 - Acting in the interest of the company rather than the member's personal interest
 - Providing oversight to assure that all company business is transacted legally
 - Making decisions to protect the assets of the company.
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What is a Fiduciary?

The term **fiduciary** refers to a relationship in which one person has a responsibility of care for the assets or rights of another person. A fiduciary is an individual who has this responsibility. The term "fiduciary" is derived from the Latin term for "faith" or "trust."

A fiduciary relationship exists with individuals who handle money or property for others. For example, your employees or contract employees may be fiduciaries, if they handle money or property. Trusted advisers like your accountant or your attorney or your insurance agent may also be fiduciaries. In a company, the board of directors, as a body, has a fiduciary responsibility for the decisions they make with regard to corporate assets and the rights of stockholders.

Liability of Corporate Boards of Directors

What liability do company boards of directors members have in their board positions? Not as much as you might expect. Corporate board members have a good deal of latitude within the scope of their duties as corporate board members. Board members must be free to act in the interest of the shareholders in order to run the company in the best way they see fit and to take appropriate risks to help the company grow. However, if members feel at risk in fulfilling their duties as outlined, the board may purchase

Directors and Officers Liability insurance (D&O) to protect themselves against lawsuits.

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Directors and Officers Liability Insurance (D&O Liability) is purchased by companies to provide financial protection of corporate board members and corporate officers from being held personally responsible for actions of the company. Claims may be made against companies and their boards and officers by employees, stockholders, and consumers/customers. Corporate board members in particular serve without compensation, and they will be reluctant to do so without the protection of this insurance.

D&O Insurance has several primary purposes and sometimes companies purchase this insurance in sections:

- Employment Practices Insurance, which can include claims against the board and executive for discrimination (age, sex, race, disability, etc.), wrongful termination, sexual harassment, and other employment-related allegations.
- Fiduciary Responsibility Liability Insurance, protecting board members against claims of conflicts of interest, acting against the interest of the company, failing to provide oversight for legal or financial dealings, not protecting the assets of the company.
- Public companies may be sued by stockholders who believe that share prices are too low or who lost money on a sale.

No Protection for Intentional Action

D&O Insurance is not designed to protect board members or executives from liability for intentional actions, criminal actions, or actions beyond their scope of duties. Securities fraud, insurance fraud, personal sexual harassment, and other similar kinds of activities are not within the scope of this insurance.

Selecting Your Board of Directors

Selecting a board of directors is an important step as you are starting your company. Your board members will help you make decisions and also satisfy the requirements of the state in which you are incorporating. Here are some things to think about before you select board members.

**How Many
Board
Members
Should There
Be?**

Historically, for small companies, there has been a rule that there needs to be as many Directors as there are Shareholders but this policy has been allowed to morph especially for those companies with only a handful of shareholders. Ohio law states that there needs to be three Officers: a President, Secretary and Treasurer but that one person may hold all three positions. Accordingly, Boards of Directors have also shrunk and may be comprised of one or two members. Such a small board may not be able to function effectively though. The following guidance should therefore be followed.

First, select an uneven number of board members, to avoid ties. The number of board members depends on the size and complexity of the organization. For a small organization, five to seven people is plenty. For a larger, more complex, organization with several committees, you might want 9 to 11 people at minimum. You need enough so that, if several people are not present, you can still have enough to make a decision, and for a quorum.

**What Does a
Good Board
Member Look
Like?**

When you are recruiting board members look for these characteristics:

- Expertise in a specific area which can help your company. For example, many companies include an attorney and a financial advisor on their boards.
- Leadership and management experience, especially in related businesses.
- Commitment to the business. Board members must be interested in the business and its continued well-being. They should not be serving just for the money or for personal interests.
- Time and energy to devote to board duties. Board members will be expected to spend time preparing for and attending board meetings, and to serve on additional committees.
- Integrity and lack of a conflict of interest. Board members will need to sign a conflict of interest statement and they must act in the best interest of the business, not their own individual or business interests. For example, a board member who profits from his or her service on a board of directors may put the entire company in jeopardy.

Of course, each type of small business needs specific kinds of people to serve on its board of directors. But all businesses need individuals with integrity, commitment, and interest as board members.

Boards are generally comprised of both Inside Directors and Outside Directors.

Inside Directors An inside director is a director who is also an employee, officer, major shareholder, or someone similarly connected to the organization. Inside directors represent the interests of the entity's stakeholders, and often have special knowledge of its inner workings, its financial or market position, and so on.

Typical inside directors are associates of, and the Officers of the Company including:

The President - The corporate President usually serves as Chairman of the Board (aka board chairman) and is responsible for the overall functioning of the board of directors and ensures that all appropriate actions are taken. Specifically, the board chair/president:

- Ensures that an agenda is planned for each board meeting
- Presides over meetings of the board of directors and the annual meeting
- Serves as supervisor/liaison with corporate executives reporting to the board
- Serves as primary spokesperson for the organization
- Signs specific documents on behalf of the board of directors and the company.

Corporate Vice President - The vice president of a company may have no specific duties but should be able to fill the duties of president if required. Often, the vice president chairs specific committees or has other regular duties, as determined by the board in its bylaws or on an ad-hoc basis.

Corporate Board Secretary - The secretary of the board of directors has overall responsibility to create and maintain corporate records and other important company documents. Included in this responsibility:

- Act in the role of a secretary
- Record minutes of all board meetings and minutes of all committees as needed. Minutes must be taken in a specific form and all board and committee actions must be recorded.
- Keep records of all policies approved by the board.
- Maintain a calendar of corporate events, including the date of the annual meeting and budget approval dates.
- Maintain personnel and payroll records for executive employees reporting directly to the board of directors.
- Keep all records in a safe place and make sure all documents are in good order in case of audits.

Corporate Board Treasurer - The treasurer of the board of directors has primary responsibility for the financial well-being of the company, but does not take day-to-day responsibility. Included in the board treasurer's duties are:

- Creating and maintaining the company's annual budget for each fiscal (financial) year. This responsibility includes presenting the budget to the board for approval.
- Creating, implementing, and reviewing financial policies for the company.
- Reviewing investment activities of the company
- Overseeing the annual financial audit of the company (if public) and other audits of corporate records and finances.
- Chairing the board's finance committee

Other Executives of the Organization, such as its chief financial officer (CFO)

Large Shareholders (who may or may not also be employees or officers)

Representatives of Other Stakeholders, such as labor unions or major lenders.

Advisors, such as the corporate attorney or accountant.

An inside director who is employed as a manager or executive of the organization is sometimes referred to as an executive director (not to be confused with the title executive director sometimes used for the CEO position). Executive directors often have a specified area of responsibility in the organization, such as finance, marketing, human resources, or production.

**Outside
Directors**

An outside director is a member of the board who is not otherwise employed by or engaged with the organization, and does not represent any of its stakeholders. Typical examples include a director who is president of a firm in a different industry or someone who is a member of the community in which the organization is located.

Outside directors bring outside experience and perspective to the board. They keep a watchful eye on the inside directors and on the way the organization is run. Outside directors are often useful in handling disputes

between inside directors, or between shareholders and the board. They are thought to be advantageous because they can be objective and present little risk of conflict of interest. On the other hand, they might lack familiarity with the specific issues connected to the organization's governance.

**Board of Directors
Compensation**

As soon as you start inviting individuals to your board of directors, you will be asked about compensation. Outside board members (those who are not also executives of the company) are typically compensated, but the level and type of compensation depends on the size and type of company.

- Travel Reimbursement - Almost every company compensates its board members for travel expenses to attend board meetings and retreats. If your board is local, you may not have to spend much for travel, but if you have directors coming from another city, you should at minimum compensate them for mileage or air fare, lodging, and per diem for incidentals.
 - Directors of Small Private Companies - Directors of small closely-held companies are typically not compensated directly with cash, because there is little cash available for this purpose and because they usually are willing to serve without such direct compensation. If a potential board member wants to be compensated directly, this person probably will not make a good board member, because he or she is more interested in the money than the service.
 - Directors of Public Companies - If your company is publicly traded, you may want to offer stock options to your directors. An agreement should be signed before options are granted, so it is clear when these options will be vested, what happens if the director leaves, and under what circumstances the stock options may be exercised.
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**Why Not
Directly
Compensate
Board
Members**

It is not a good idea to provide board members with direct compensation. Directors have fiduciary responsibility, and being compensated interferes with that responsibility. Being compensated could be considered a conflict of interest for directors. At the least, it causes directors to work for the money, not the benefit of the company. Beyond paying for their expenses, there is no requirement that you compensate these individuals.

Conflicts of Interest

Most companies are concerned about **conflicts of interest** for their executives and corporate board members. A board member, for example, needs to be focused on the concerns of the company, not on outside interests. Board

members cannot let their personal interests interfere with the decisions they make as directors. So, almost all companies have conflict of interest policies and statement which they require directors to sign. Here are some details about these policies:

A conflict of interest policy should be prepared by your company's attorney and signed by all board members at the first (organizational) board meeting, or when they join the board. No board member should be allowed to serve without signing this policy.

Outside Interests

Conflict of interest policies require board members to disclose outside interests conflicting with the interests of the company. These potential conflicts of interest include relationships or responsibilities (personal, financial, and others). The policy allows board members to keep a director from participating in discussion, reporting, or voting on an issue. The member may also recuse (excuse) himself or herself from that issue.

Continuing Conflict of Interest

If a conflict of interest is significant, ongoing, and irreconcilable, and if it impedes the ability of the individual to carry out duties of the position, a conflict of interest policy gives the organization the right to remove the person from the position.

Typical Conflict of Interest Policy

A conflict of interest policy for a board of directors might include:

- Definitions, such as "interested person" and "financial interest"
- Discussion of the duty to disclose and determining whether a conflict of interest exists
- Procedures for addressing the conflict of interest, by the individual or the board
- What happens if the board determines or has reasonable cause to believe that a violation of conflict of interest has occurred
- Discussion of director compensation from the organization and its effect on board function
- Requirement for annual review of the conflict of interest policy, disclosure of outside interests, and re-signing of the policy.
- The signed conflict of interest policies for each board member are part of the corporate records and must be kept in the corporate records

book or file.

Corporate Officers

Officers of a Company The [Directors of a Company](#) appoints and hires [Officer\(s\)](#) to manage the day-to-day affairs of the company . Officer(s) handle all of the daily decisions required to run a business and the scope of their duties depends on the size of the company.

Officers of a Company, A Company usually has the following officers:

title	role	responsibility
President	carries out the most important functions	performing the more important responsibilities including signing contracts or developing strategies for the Company
Vice-President (not required)	can act for the President when needed	acting for the President, or assisting the President, as needed
Secretary	organizes corporate records and meetings	Maintaining the corporate records and correlates the organizational affairs of the Company
Treasurer	manages the financial affairs of the Company	ensuring the financial welfare of the Company from obtaining loans, to overseeing the accounting department.

Large companies may delegate duties. However the officer positions of a small company are usually filled by a single person who will carry out all or most of these responsibilities.

Stockholders of a Corporation The stockholders are the people who started and own the company for their mutual benefit.

[Stockholders](#) (or Shareholder) invest money, property, labor (also referred to as sweat equity) or something else of value into the corporation. In return, the stockholders will own a part of the corporation relative to the amount they

invested. Stockholders provide the means by which the corporation is able to buy machinery, inventories, pay rent and start operations.

o provide evidence of their ownership and investment, the corporation will issue these individuals a stock certificate. That is why they are referred to as “stockholders.” These stocks represent ownership in a particular corporation, and are similar to those bought/sold in the New York stock exchanges; only the stocks of larger corporations are traded on an exchange.

stockholders control the corporation by appointing directors who will oversee the activities of the corporation.

Visual Diagram of a Corporate Structure

Below is a diagram that displays the participants in the corporate world:

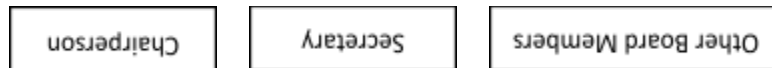
Note: Most of these positions are held by one or two people; owners of small business corporations may do everything themselves, (ex.) from being the chairman of the board to delivery truck driver.

Shareholders (or Members)



Shareholders elect and control the Directors thru voting)

Directors



Directors appoint, hire and control the Officers)

Officers



Officers run the company subject to Director control)

