

ATOS MID-YEAR COMMITTEE/OFFICER ACTIVITY REPORT FORM (2012)

Name of Activity: **BYLAWS & POLICIES COMMITTEE (Legal Advisor)**
(Please fill out separate form for each activity.)

Committee Chair/Officer Name: **Jack Moelmann (Chairperson)**
R. Jelani Eddington (Legal Advisor)

Date of Report: **January 19, 2012**

1. Actions completed since the 2011 annual meeting: (Please bullet actions completed.)

- Researched the question regarding repealing/amending ATOS Bylaws § 4.2(e) relating to “competing organizations.” For the reasons detailed in the attached memo, it is the suggestion of the Legal Advisor to retain the bylaw in place as it currently stands.
- Reviewed and proposed change to Bylaw § 4.2(c) and Policy ¶ 5(n) regarding the selection of the ATOS Youth Representative To The Board.
- Updated the ATOS Bylaws, Policies, and Corporate Profile per relevant votes of the Board.

2. Actions begun but incomplete since the mid-year meeting: (Please bullet actions begun.)

- Ongoing process of providing legal advice to the Committee and Board of issues affecting Bylaws & Policies.

3. Goals to be reached by the 2012 Annual Meeting: (Please bullet goals.)

4. Amount budgeted for your committee: **\$0.00**
Amount expended by your committee: **\$0.00**

5. Comments: (Any bulleted special notations, problems, or suggestions should be included here.)

6. Motions:

I submit for consideration the following motion relating to revisions of the ATOS Bylaws & Policies. The proposal is explained in the accompanying attached memo.

- Amendment of Bylaw § 4.2(c) and Policy ¶ 5(n) requiring the Board to approve the selection of the Youth Representative to the Board (see attached memo)

MEMO TO THE ATOS BOARD OF DIRECTORS

TO: COL(R) Michael W. Hartley, Chairman;
Mr. Bob Evans, Secretary; ATOS Board of Directors
Mr. Jack Moelmann, Chairman, Bylaws & Policies Committee

FROM: R. Jelani Eddington, Legal Advisor for Bylaws & Policies

DATE: January 19, 2012

RE: ATOS Bylaws § 4.2(e) (“Competing Organizations”)

SUMMARY

In response to the Board’s consideration of a proposal to repeal ATOS Bylaws § 4.2(e) relating to competing organizations, I submit the following material for review. For the reasons that follow, there are many important practical as well as legal reasons to leave the bylaw in place.

The theatre organ industry in which ATOS operates is an extremely limited marketplace that—at least for the time being—is shrinking. Over the past several years, ATOS has been aggressively pursuing fundraising dollars from a relatively small pool of donors, and has been undertaking various strategic planning efforts and initiatives aimed at (among other things) reversing the declining trends in ATOS membership.

Any organization that does the same thing that ATOS does (*i.e.*, promoting the art of the theatre organ) in the same limited, shrinking market as ATOS will necessarily be competing for the same members and the same fundraising dollars as ATOS. No matter how cordial the relationship may be between such groups, its organizational interests will necessarily be in tension, and opportunities abound for conflicts of interest—even unintentional ones.

The identity of potential donors for ATOS is highly confidential, as are the non-public draft initiatives under consideration by the Board and/or Executive Committee relating to the Strategic Plan. If that highly sensitive and confidential information is disclosed (even inadvertently) to another organization seeking the very same potential fundraising dollars and members as ATOS, ATOS’ legitimate business interests will be damaged.

Bylaws Section 4.2(e) serves an important function by ensuring that any person who is a director on another organization that does the same thing as ATOS in the same limited market must relinquish his or her seat *prior to* qualifying to run for the board of ATOS. The purpose of the bylaw has never been to keep any individual off the Board. To the contrary, all eligible members are welcomed to serve ATOS, so long as that service does not violate the director’s fiduciary duties to ATOS. Section 4.2(e) helps to ensure that the director’s fiduciary duty will be preserved.

DISCUSSION

I. BACKGROUND OF SECTION 4.2(E)

ATOS Bylaws § 4.2(e) was adopted on April 15, 2009 as a qualification for candidates seeking a position on the ATOS Board. Two years prior to the adoption of this Bylaw, a new international organization, Theatre Organ Society International (TOSI), was formed. According to its bylaws,¹ the purpose of TOSI is:

¹ Available at <http://theatreorgansocietyinternational.com/documents.htm>

- To preserve and promote the theatre organ and its artform;
- To further public appreciation of the theatre organ and its music with concerts and educational programs;
- To encourage talented musicians to preserve the art of theatre organ playing.²

These stated purposes were **substantially identical** to those set forth in ATOS Bylaws § 1.4³:

- The preservation and enhancement of the theatre organ;
- To further public appreciation of the theatre pipe organ and its music with educational programs and concerts;
- To encourage talented musicians to preserve the art of theatre organ playing, through competitions and awards

In addition, many operative provisions of the TOSI bylaws—including the format, structure, and organization of the TOSI bylaws—were nearly **verbatim copies** of their ATOS counterparts. For example, the TOSI Executive Director had a similar job description as the ATOS President/CEO, as both were responsible at the time for the “day-to-day operations” of their respective organizations.⁴

These striking similarities led the Board to conclude that TOSI had the same corporate purpose and objectives as ATOS—promoting the theatre organ and its music throughout the United States and abroad—and was carrying out those objectives in the same limited national/international market as ATOS.

Over the past several years, ATOS—through its Strategic Plan Initiative and otherwise—has spent nearly \$200,000 to reverse the trend of declining membership and to solicit substantial fundraising dollars. To this end, ATOS has engaged the services of a paid President/CEO and grant writer. ATOS has also undertaken several initiatives for increasing membership. Many of these activities involve highly confidential and sensitive information, such as the identities of potential donors to ATOS as well as working drafts of the Strategic Plan. If divulged—even inadvertently—this information could seriously harm ATOS’ legitimate business interests.

Frequently repeating the *mantra* that a GM director would never be permitted to serve on the board of Chrysler, and recognizing that one cannot “serve two masters,” ATOS attorney Dolton McAlpin drafted Section 4.2(e) which required a potential candidate to relinquish his seat on a competing organization (as defined) prior to qualifying to run for the ATOS Board. Section 4.2(e) does not prevent anyone from running for and/or serving on the ATOS Board—it merely requires that the director resign the other board seat **first**.

Out of a concern for fairness, and recognizing that changing a qualification after nominations had already been opened might be of questionable legality, the Board exempted from its scope any person who was currently running for a seat on the Board. Nor did the Board limit Section 4.2(e) to any specific organization. Rather, the Board defined the term “competing organization” with care so as to delineate those organizations for which these concerns would be the most appropriate.

² TOSI Bylaws § 1.2. The TOSI website explained that “[w]e are a membership organization for public and charitable purposes whose mission is to promote and present theatre organ performance as an internationally recognized art form.”

³ ATOS Bylaws § 1.4(d) included as a purpose to promote and foster organ building—a purpose not included in the TOSI bylaws.

⁴ Compare TOSI Bylaw § 4.2(c) (Executive Director a non-voting position “essentially involved in the membership processing activities **and day to day operation of the Society**”) with ATOS Bylaw § 5a.1 (President/CEO a non-voting position “responsible for the **day-to-day management of the Society**” and other duties assigned by Board).

II. APPLICABILITY OF COMPETING ORGANIZATION BYLAW

By its terms, Section 4.2(e) prevents a person from serving on the ATOS Board **at the same time** he or she serves on the Board of a “competing organization.” The text of Section 4.2(e) clearly sets forth two tests for determining whether any organization is “competing”.

In order to be a “competing organization”, an organization must:

- (1) be a ***national*** or ***international*** public, charitable, or private organization; and
- (2) ***promote the theatre organ*** and the ***performance of its music***.⁵

Both elements of the test must be satisfied to bring the organization within the meaning of Section 4.2(e). In order to ascertain whether an organization is “competing,” it is necessary to examine the nature and purpose of the organization and the market in which it operates. Examples of a competing organization would likely include TOSI (for the reasons discussed above), the Theatre Organ Society of Australia, the Cinema Organ Society, or any other such organization operating in a national and/or international market that promotes the theatre organ and the performance of its music.

By contrast, a non-ATOS-affiliated organization centered around a ***single instrument*** or ***local geographic area*** would not be a “national” or “international” charitable organization and would therefore not be a “competing organization.” Such examples would likely include the Rochester Theatre Organ Society, Dickinson Theatre Organ Society, or other similar local groups.

Furthermore, an organization with a primary purpose ***other than*** to “promote the theatre organ and the performance of its music” would not be a competing organization. Examples of such organizations would likely include the American Guild of Organists, the Organ Historical Society, or other similar groups not primarily focused on promoting the theatre organ and its music.

These distinctions are not academic. The Board spent a great deal of time discussing and drafting Section 4.2(e) to clearly identify only those organizations with purposes that might come into tension with those of ATOS. At the same time, because it would be impossible to draft a definitive and exhaustive list of “competing” and “non-competing” organizations, the Board has consistently relied on the specific definition in Section 4.2(e) to resolve any questions concerning whether an organization is covered or exempted from the bylaw.

III. SERVING ON THE BOARD OF A COMPETING ORGANIZATION AT THE SAME TIME AS SERVICE ON THE ATOS BOARD CAN VIOLATE A DIRECTOR’S FIDUCIARY DUTY.

As the Board considered in 2009, there are very serious legal ramifications raised by a director who serves simultaneously on the boards of organizations that do the same thing in the same limited market. In the ***for-profit*** context, (such as General Motors and Chrysler), such simultaneous service is ***strictly forbidden*** under the federal antitrust laws.⁶

In the non-profit context, simultaneous service on competing boards can also be problematic. In language similar to the Board’s concerns, the California Supreme Court recently observed:

[N]o person can, at one and the same time, faithfully serve two masters representing diverse or inconsistent interests....⁷

One of the most fundamental principles of corporate law is the fiduciary ***duty of loyalty*** imposed on each corporate director. California law (as the law of all states) strictly requires that directors owe a duty of loyalty, care, and obedience in the management of corporate affairs and in

⁵ Section 4.2(e) clarifies that ATOS Chapters are ***not*** competing within the meaning of the Bylaw.

⁶ CLAYTON ACT, 15 U.S.C. § 19 (expressly prohibiting interlocking directorates on boards of directors of large for-profit companies).

⁷ *Lexin v. Superior Ct. San Diego Co.*, 222 P.3d 214, 228-29 (Cal. 2010)

performance of their official duties.⁸ That duty requires that the corporate director “must act in good faith for the interests of the corporation or its [members] with due care and diligence and within the bounds of their authority.”⁹ This duty of loyalty also prohibits self-dealing.¹⁰

A director who serves on the boards of more than one organization owes this same undivided fiduciary duty to **each corporation**.¹¹ Not surprisingly, when the interests of the two corporations are divergent or in tension—as they are when corporations do the same thing in the same limited market—California courts have found the duty of loyalty to be violated.¹² At a minimum, courts have been quick to point out the ripe opportunity for conflicts of interest.¹³

Importantly, according to California caselaw, the simultaneous service on boards of corporations **when those corporations compete with one another or have interests that are in tension**, can lead to a violation of a director’s fiduciary duty.

In the case of ATOS, no matter how cordial its relationship may be with another organization, where that organization is soliciting memberships and fundraising dollars from the same limited pool of theatre organ enthusiasts and potential donors as ATOS, there is ample cause for concern when directors sit on the boards of both organizations. That concern reaches far beyond any one single organization. Section 4.2(e) addresses that concern by requiring the director to relinquish his or her seat **prior to** qualifying to run for or serve on the ATOS Board.

IV. VIOLATION OF THE DUTY OF CARE CAN SUBJECT THE DIRECTOR TO PERSONAL LIABILITY

A finding of a violation of the duty of loyalty could be disastrous for the individual director involved and could similarly ensnare ATOS in unwanted litigation.

While directors of a non-profit organization are generally immune from personal liability under federal and state law,¹⁴ if a violation of the duty of loyalty is found, that director may be personally liable.¹⁵ In the event that a director were found personally liable, he or she might seek indemnification from ATOS, thereby drawing ATOS into litigation and possibly implicating its D&O liability policy.¹⁶ The potential exposure to personal liability of a director and the likely indemnification claim against ATOS provides another solid reason to maintain Section 4.2(e) in place.

⁸ Professional Hockey Corp. v. World Hockey Ass’n, 143 Cal. App. 3d 410, 414 (Cal. App. 1983)

⁹ Id. See also CAL. CORP. CODE § 5230(a) (“A director shall perform the duties of a director...in good faith, in a manner that director believes to be in the best interests of the corporation and with such care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances.”)

¹⁰ Cal. Corp. Code § 5233. ATOS Bylaws §§ 4.18-4.19.

¹¹ Professional Hockey Corp. v. World Hockey Ass’n, 143 Cal. App. 3d 410, 415 (Cal. App. 1983)

¹² Ravens Cove Townhomes, Inc. v. Knuppe Development Co., Inc., 114 Cal. App. 3d 783 (Ct. App. 1981) (duty of loyalty breached where corporate directors of a non-profit homeowners association simultaneously served as employees of condominium development company)

¹³ Lee v. Interins. Exchange, 50 Cal. App. 4th 694, 717 (Cal. App. 1996)

¹⁴ VOLUNTEER PROTECTION ACT OF 1996, 42 U.S.C. § 14501 et seq. Cal. Corp. Code §§ 5047.5, 5239.

¹⁵ 42 U.S.C. § 14503(a) (liability shield does not apply where harm was caused by “willful misconduct”, “gross negligence” or “reckless misconduct”); Cal. Corp. Code § 5047.5(c) (liability shield does not apply to self-dealing transactions or conflict of interest)

¹⁶ Cal. Corp. Code § 5238; ATOS Bylaw § 4.16

MEMO TO THE ATOS BOARD OF DIRECTORS

TO: COL(R) Michael W. Hartley, Chairman;
Mr. Bob Evans, Secretary; ATOS Board of Directors
Mr. Jack Moelmann, Chairman, Bylaws & Policies Committee
Mr. Nathan Avakian, Youth Representative To The Board

FROM: R. Jelani Eddington, Legal Advisor for Bylaws & Policies

DATE: January 19, 2012

RE: Bylaw & Policy Change Proposal – Youth Representative Selection

BACKGROUND

The position of Youth Representative To The Board has been in existence since 2001 and has been an extremely valuable position on the ATOS Board.

In 2007, the Board and the membership changed ATOS Bylaw §§ 4.2 and 4.4 to make the Youth Representative a non-voting director. Two years later, the California legislature amended § 5047 of the Corporations Code, requiring that any person identified as a “director” in a corporation’s Articles or Bylaws have the same rights (including voting rights) as all other directors.

In response to this change in state law, ATOS amended its bylaws in 2010 to permit all directors, including the Youth Representative, to vote on all matters before the Board. Because the Youth Representative was considered a director, the Board also amended Policy ¶ 5(n) to require the Youth Representative to be at least 18 years of age.

Currently, under Policy ¶ 5(n), the Youth Representative Subcommittee of the Youth Initiatives Committee is responsible for selecting and overseeing the Youth Representative. During many selection cycles, subcommittee members were *not* Board members. Because the Youth Representative now takes a far more active policy-making roll by casting a vote on all matters before the Board, it is suggested that the Board—rather than the Youth Representative Subcommittee—approve the selection of the Youth Representative.

Such a change would have several advantages. First, the change would treat the Youth Representative similarly to the current officer positions which are appointed by the Board. Second, the change would eliminate the possibility that a *non*-Board member with no accountability to the membership could select a voting member of the Board. Third, the change would increase accountability of the position by ensuring that—just like the officer positions—the Youth Representative would be selected by (and could also be removed by) the Board.

PROPOSAL

Current Bylaw § 4.2(c) & Policy ¶ 5(n):

Bylaw § 4.2(c): Ex-Officio Directors. There shall be two Ex-Officio Directors who shall be (i) the Immediate Past Chairman, and (ii) the ATOS Youth Representative to the Board. For the purposes of this Section 4.2, the person serving as Chairman upon the expiration of the term shall be considered the Immediate Past Chairman. The person selected by or with the authority of the Board to be ATOS Youth Representative to the Board shall serve as ATOS Youth Representative.

Policy ¶ 5(n): YOUTH REPRESENTATIVE TO THE BOARD OF DIRECTORS. The position of ATOS Youth Representative To The Board shall be open to any person who has attained the age of 18 but not exceeded the age of 24 as of March 1st in the year in which the Youth Representative position is filled. The Youth Representative Subcommittee of the Youth Initiatives Committee shall establish the applicable rules and guidelines for the Youth Representative position.

Proposed Amendments:

Bylaw § 4.2(c): Ex-Officio Directors. There shall be two Ex-Officio Directors who shall be (i) the Immediate Past Chairman, and (ii) the ATOS Youth Representative to the Board. For the purposes of this Section 4.2, the person serving as Chairman upon the expiration of the term shall be considered the Immediate Past Chairman. The person selected by or with the authority **consent** of the Board to be ATOS Youth Representative to the Board shall serve as ATOS Youth Representative. ***The ATOS Youth Representative to the Board may be removed, either with or without cause, by the Board of Directors at any regular or special meeting thereof.***

Policy ¶ 5(n): (n) YOUTH REPRESENTATIVE TO THE BOARD OF DIRECTORS. The position of ATOS Youth Representative To The Board shall be open to any person who has attained the age of 18 but not exceeded the age of 24 as of March 1st in the year in which the Youth Representative position is filled. The Youth Representative Subcommittee of the Youth Initiatives Committee shall ***report to the Board the most qualified person identified by the Subcommittee for the position, and, upon the affirmative vote of the Board, that person shall serve as the Youth Representative.*** ***The Subcommittee shall*** establish the applicable rules and guidelines for the Youth Representative position.

PROPOSED MOTION:

<p>That Bylaws § 4.2(c) and Policy ¶ 5(n) be amended in accordance with the January 19, 2012 memo from the Legal Advisor to the Bylaws & Policy Committee.</p>
