



KROKIDAS & BLUESTEIN LLP

CLIENT ALERT

FIRST CIRCUIT WEIGHS IN ON NONPROFIT FIDUCIARY DUTIES

Although Massachusetts remains in a state of emergency, and most businesses are operating under Governor Baker's stay at home advisory, the courts continue to decide noteworthy cases.

On March 25, 2020, the First Circuit Court of Appeals (the "First Circuit") issued a decision in ongoing litigation which involved breach of fiduciary duty claims made by students against a nonprofit college, its Board of Trustees, and key officers and administrators. In disposing of the plaintiffs' claims, the First Circuit held that nonprofit directors and officers owe fiduciary duties to the institution and not to its students, and that claims of financial mismanagement may only be brought by the Attorney General's Office.

Mount Ida College ("Mount Ida") announced in April 2018 that it was permanently closing its doors following its May commencement. The sudden closure followed a period of financial distress during which Mount Ida operated at a deficit for several years. Students received only six weeks' notice of the closing. Transfer deadlines to many other schools had passed or were imminent. Although the Mount Ida president announced that students in good academic standing would be offered admission by UMass Dartmouth, only about 250 of 1,300 students ultimately transferred to UMass Dartmouth.

Current and prospective students filed a class action suit asserting, among other claims, that Mount Ida, its Board of Trustees, and certain key officers and administrators breached a fiduciary duty owed to the students by concealing knowledge of Mount Ida's financial distress. Rejecting this argument, the First Circuit explained that although Massachusetts state law imposes a fiduciary duty on the officers and directors of a nonprofit corporation, that duty is owed to the corporation itself and not the students. The First Circuit cited Chapter 180, Section 6C, of the Massachusetts General Laws, which provides that an officer or director of a nonprofit corporation is required to perform his or her duties in good faith and in a manner that he or she "reasonably believes to be in the best interests of the corporation...." The First Circuit also quoted Massachusetts case law, stating that "[d]irectors of a corporation stand in a fiduciary relationship to that corporation and have a duty to protect its interests 'above every other obligation.'"

The First Circuit noted that because earlier disclosure of Mount Ida's financial distress might have endangered the school's ability to recover, or could have made its financial distress

even worse, the imposition of a duty to the students would have conflicted with the defendants' statutorily imposed duty to Mount Ida. The First Circuit determined that it had no authority to impose a contradictory duty in light of Massachusetts statutory language and precedent.

The First Circuit distinguished its decision from the Supreme Judicial Court's recent recognition of a "special relationship" that might exist between a university and certain individual students. In 2018, the SJC held that duties can arise in the context of particular university employees who fail to act reasonably to alleviate risk where they have knowledge that a certain student is at high risk of suicide. The First Circuit, however, viewed this special relationship as arising from a narrow set of circumstances and noted that the SJC's ruling did not create a fiduciary duty to the entire student body.

The First Circuit provided yet another reason for rejecting the breach of fiduciary duty claims, explaining that only the Attorney General may bring a claim of mismanagement of a charitable organization under Massachusetts law. The First Circuit again supported its analysis by reference to both the Massachusetts statute and case law. Massachusetts General Laws, Chapter 12, Section 8 states that "[t]he attorney general shall enforce the due application of funds given or appropriated to public charities within the commonwealth and prevent breaches of trust in the administration thereof." According to the First Circuit, none of the special standing exceptions described in Massachusetts case law which might allow an individual to bring a fiduciary duty claim against an institution applied to the Mount Ida situation.

Note: While the Mount Ida case was pending, the Massachusetts legislature adopted Chapter 113 of the Acts of 2019, An Act to Support Improved Financial Stability in Higher Education. The new law, among other things, requires certain institutions of higher learning to immediately notify the Massachusetts Board of Higher Education of any known financial liabilities or risks which are reasonably likely to result in the imminent closure of the institution, or otherwise negatively affect the institution's ability to fulfill its obligations to current and admitted students.

If you have any questions about the Mount Ida College case, or the fiduciary duties of officers, directors and trustees more generally, please contact Attorneys Elka Sachs, esachs@kb-law.com, or Eric Reustle, ereustle@kb-law.com.