



The New York Non-Profit Revitalization Act
Susan Golden and Sharon Connelly

Dance/NYC Town Hall: June 1, 2015



Background

- **The New York Non-Profit Revitalization Act**

- First major revision to the New York Not-for-Profit Corporation Law in over 40 years
- Amended the Not-for-Profit Corporation Law, the Estates, Powers and Trusts Law, the Executive Law and other State laws applicable to not-for-profit corporations
- Most changes became effective on July 1, 2014



Background

▪ **Changes/Guidance**

- Legislation
 - Amended in 2014 to make technical corrections
 - Amended in 2014 to delay the effective date of prohibition on employees serving as chair of a nonprofit's board until January 1, 2016
- NY State Attorney General's Charities Bureau has published guidance in response to the Act, available at http://www.charitiesnys.com/nonprofit_rev_act_guidance.jsp



Background

- **Purpose**

- To reduce unnecessary and outdated burdens on nonprofits
- To enhance nonprofit governance and oversight to prevent fraud and improve public trust
- Codified certain “best practices”



Background

- **Applicability**

- Generally applies only to not-for-profit corporations (and trusts) that are incorporated in New York

- **Exceptions:**

- Audit committee provisions
- Submission of annual financial reports (both apply to charities soliciting in New York)

- **Charities vs. Non-Charities**

- Charitable – formed for charitable purposes (charitable, educational, religious, scientific, literary, cultural, or for the prevention of cruelty to children or animals)
- Non-charitable – formed for any other purpose
- Charitable organizations are subject to certain enhanced requirements (i.e., approval of Related Party Transactions)



Topics for Discussion

- **Modernization and Streamlining**
 - Improved Incorporation/Amendment Process
 - Limit on Disclosure of Personal Information
 - Communication Procedures and Video Conferencing
 - Approval of Fundamental Transactions

- **Enhanced Governance Requirements**
 - Board Independence
 - Audit Procedures
 - Related Party Transactions
 - Conflict of Interest Policy
 - Whistleblower Policy
 - Approval of Real Estate Transactions
 - Committees
 - Executive Compensation



Modernization and Streamlining

- **Improved Incorporation/Amendment Process**

- Eliminates Corporate “Types”
- Statement of Purposes
 - Specific purposes no longer need to be included
 - Express statement that no consent or approval is required
- Minimizes Agency Pre-Approvals for Some Organizations
- Non-material corrections may be made by the Department of State

- **Disclosure of Personal Information**

- Previously required to allow inspection of names and residential addresses of officers and directors upon request by members, creditors and state officials; now only names must be provided



Modernization and Streamlining

- **Modernized Communications**

- Electronic Communications:
 - Meeting Notice (Members)
 - Waiver of Notice (Members and Directors)
 - Unanimous Consent (Members and Directors)
 - Proxy (Members)
- Video Conferencing (Directors)
 - All board members can hear each other at the same time
 - Each director can participate in all matters before the board

- **Attorney General Option for Merger, Dissolution, and Fundamental Transactions**

- In lieu of both court approval and notice to Attorney General



Modernization and Streamlining

- **Recommendations:**

- Solicit emails from members and directors with express stated purpose of using for notice; adopt electronic communications policy
- Check articles of incorporation and by-laws to make sure not overly restrictive on submission of unanimous written consent electronically or participation in meeting via electronic communication
- If contemplating a fundamental transaction, consider seeking approval of Attorney General



Enhanced Governance Requirements

- Board Independence
- Audit Procedures
- Related Party Transactions
- Conflict of Interest Policy
- Whistleblower Policy
- Approval of Real Estate Transactions
- Committees
- Executive Compensation



Governance: Board Independence

- **Independent Directors:**
 - Has not been an **employee** of, or does not have a **relative** that was a **key employee of**, the corporation or an affiliate of the corporation in past **three** years
 - Has not received, and does not have a relative who has received, more than **\$10,000** in **direct compensation** from the corporation or an affiliate in any of the last three years (other than expense reimbursement or reasonable compensation as a director)
 - Is not a **current employee** of or does not have substantial financial interest in, and does not have a **relative** who is a **current officer** of or has a substantial financial interest in, an entity that **made or received payments** from the corporation or an affiliate of more than **\$25,000 or 2%** of such entity's gross revenue (whichever is less) in any of the last three years
 - Excludes charitable contributions
 - Recommendation: Consider whether any directors are employees or owners of contractors, vendors or other service providers



Governance: Board Independence

- Does not contain an exemption for membership dues, which could trigger the “\$25,000 or 2%” definition of independence
- Should be noted by an organization whose board consists of employees of member entities
- Only independent directors may participate in any board or committee deliberations or voting relating to audit, conflict of interest or whistleblower matters
 - Attorney General guidance acknowledges that it may take time for some organizations to elect or select board or committee members in order to comply with this requirement
- Employees may not serve as chair of the board or in an officer position with similar responsibilities (effective January 1, 2016)
 - A proposed bill would delay this prohibition until January 1, 2017
 - There is discussion of possible repeal of this provision due to unexpected levels of resistance from not-for-profits



Governance: Audit Procedures

- **New Thresholds for Financial Reports to Attorney General's Office**
 - **July 1, 2014** (*original or extended annual report filing date*)
 - **Gross Revenue <\$250,000** – unaudited financial report signed by chief financial officer and president
 - **Gross Revenues from \$250,000 to \$500,000** – annual financial report accompanied by independent certified public accountant's review report (*previously required at \$100,000*)
 - **Gross Revenues >\$500,000** – annual financial statement accompanied by independent certified public accountant's audit report (*previously required at \$250,000*)
 - **July 1, 2017** – audit report thresholds increase to >\$750,000
 - **July 1, 2021** – audit report thresholds increase to >\$1,000,000
 - Also eliminated requirement that all nonprofits that use paid fundraisers submit audited financial statements, regardless of gross revenues



Governance: Audit Procedures

- **Mandatory Audit Oversight**

- Audit committee comprised of “independent directors” or full board oversight with only “independent directors” participating
- Applies to nonprofits required to submit independent auditor report to the Attorney General under charitable solicitations law (NY Exec. Law 172-b)

- **Responsible for:**

- Overseeing accounting and financial reporting practices
- Retaining an independent auditor
- Reviewing the results of the audit
- Overseeing conflict of interest and whistleblower policies (unless overseen by another committee of independent directors or independent directors on board)



Governance: Audit Procedures

- **Additional responsibilities for organizations with revenues over \$1 million:**
 - Review of scope and planning of audit
 - Additional post-audit review and discussion with auditor:
 - Any material risks and weaknesses
 - Any restrictions on the auditor's activities
 - Any significant disagreements between the auditor and management
 - Adequacy of accounting and financial reporting processes
 - Consideration of performance and independence of auditor
 - Reporting of committee's activities to the board



Governance: Audit Procedures

Attorney General Audit Committee Guidance:

- Issued February 24, 2015
- Recognizes that audit committees may require assistance from others with accounting financial expertise, as long as formal deliberations and voting are limited to independent directors
- Recognizes that organizations may need time to make changes to their by-laws and committee structure and to develop new procedures
- Organizations that are not yet in compliance with these requirements should have a written plan with a timetable to achieve compliance



Governance: Related Party Transactions

- **Who is a Related Party?**

- (1) any **director, officer, or key employee** of the corporation or any **affiliate** of the corporation;
- (2) any **relative** of any director, officer, or key employee of the corporation or any affiliate of the corporation; or
- (3) any **entity** in which any individual described in (1) or (2) has a **35 percent or greater ownership or beneficial interest** or, in the case of a partnership or professional corporation, a **direct or indirect ownership interest in excess of five percent**.

- **Related Parties do not include:**

- Any entity in which an individual described in (1) or (2) is an **officer, director or employee** (unless there is also a prohibited financial interest)
- Any person or entity with which an individual described in (1) or (2) has any **nonfinancial interest** or **relationship**



Governance: Related Party Transactions

▪ Is there a Related Party Transaction?

- Any transaction in which a related party has a financial interest and in which the corporation or any affiliate is a participant
 - Attorney General guidance indicates that either a direct or indirect financial interest triggers these requirements

▪ Basic Requirements for all Related Party Transactions:

- **Fair, reasonable** and in the corporation's best interest
- Directors, officers and key employees who have an interest in a related-party transaction must **disclose** such interest to the board
- Related parties **may not participate in deliberations or voting**, but may provide information



Governance: Related Party Transactions

- **Additional Requirements: If the related party has a substantial financial interest in the transaction, charitable organizations must also:**
 - Consider **alternative transactions** to the extent available
 - Approve the transaction by not less than a **majority vote** of the directors or committee members present at the meeting
 - **Document** the basis for approval, including alternative transactions considered
- **Issues:**
 - Additional procedural requirements imposed:
 - Prior law required either that transaction was fair and reasonable or interest of related party was disclosed and their vote was not required for approval
 - Prior law did not require consideration of alternative transactions or documentation of basis for approval
 - No exception in statute for *de minimis* transactions or transactions that are clearly reasonable (i.e., substantially reduced prices)
 - Renewing a contract with an existing service provider could trigger these requirements



Governance: Related Party Transactions

Attorney General Guidance:

- Conflict of Interest Policy Guidance (issued April 13, 2015) addresses related party transactions
- Indicates that either a direct or indirect financial interest triggers these requirements
- Indicates that “record-keeping requirements” for related party transactions may not apply to four types of transactions which would not ordinarily require board approval (examples included in guidance):
 - *De minimis* transactions
 - Transactions undertaken in the ordinary course of business by staff
 - Benefits provided to the related party as a member of a class that the nonprofit intends to benefit
 - Compensation of employees and directors
- Additional guidance on related party transactions is anticipated



Governance: Conflict of Interest Policy

- Act requires **all** nonprofits incorporated in New York to adopt a conflict of interest policy covering directors, officers, and key employees
- Must include:
 - (1) A **definition** of circumstances that constitute a conflict of interest
 - (2) Procedures for **disclosing** a conflict to the audit committee or the board
 - (3) A requirement that the person with a conflict of interest **not be present at or participate** in board or committee deliberations or voting on the matter giving rise to the conflict
 - Note: Pay attention to quorum and voting requirements when conflicted parties leave the meeting for a particular vote
 - (4) A prohibition on any attempt by the person with the conflict to **influence board** deliberations
 - (5) **Documentation procedures** for detailing the existence and resolution of the conflict, and
 - (6) Procedures for disclosing, addressing and documenting related-party transactions



Governance: Conflict of Interest Policy

- The Act provides that, **prior to the initial election of any director**, and **annually** thereafter, directors must:
 - Complete, sign, and submit a written statement identifying any potential conflict
- Recommendations:
 - Also solicit conflict of interest statements from **officers** and **key employees**
 - Consider expanding the definition of key employee in your policy to include volunteers or others with substantial influence (if applicable)
 - The written statement should also include information from which **independent director status** and **potential related party transactions** can be determined
- The adoption, implementation of, and compliance with the conflict of interest policy must be overseen by the independent directors on **board** or a designated **audit or other committee** comprised solely of independent directors



Governance: Conflict of Interest Policy

Attorney General Guidance on Conflict of Interest Policies:

- Issued April 13, 2015
- Explains who is included in the definition of “key employee”
- Provides context for the minimum statutory requirements
- Provides additional recommendations
- Confirms that body adopting the policy has the discretion to determine the circumstances that constitute a conflict of interest, including the discretion to define exceptions for *de minimis* transactions, ordinary course of business transactions, and circumstances specific to the organization



Governance: Whistleblower Policy

Required for nonprofits incorporated in New York having:

- 20 or more employees **and**
- Annual revenue in excess of \$1 million in the prior fiscal year

The whistleblower policy must include the following provisions:

- (1) Procedures for the reporting of violations or suspected violations of laws or corporate policies, including procedures for preserving the confidentiality of reported information;
- (2) A requirement that an employee, officer or director of the corporation be designated to administer the whistleblower policy and to report to the audit committee or other committee of independent directors or, if there are no such committees, to the board; and
- (3) A requirement that a copy of the policy be distributed to all directors, officers, employees and to volunteers who provide substantial services to the corporation.



Governance: Whistleblower Policy

Attorney general guidance on whistleblower policies:

- Issued April 13, 2015
- Advisory guidance on required policy terms and terminology
- Recommended best practices



Real Estate Transactions

- **Special voting requirements for purchase, sale, mortgage, lease, exchange or other disposal of real property**
 - Leasing as a tenant is not subject to these enhanced voting requirements (can be approved pursuant to the organization's standard policies and procedures)
- **If not "all or substantially all" of assets**
 - Delegation to committee is allowed
 - Approval by majority of directors or majority of authorized committee
 - Committee must report back to board



Real Estate Transactions

- **If “all or substantially all” of assets**

- Delegation to committee not permitted
- Boards with less than 21 members: approval by two-thirds of entire board
- Boards with 21 or more members: approval by majority of entire board
- Counting of “entire board” clarified
- For a disposition: If there are members entitled to vote: two-thirds vote of members, after vote and recommendation by board
- Approval by NY State Attorney General’s Office or court approval (for charitable corporation)



Real Estate Transactions

- **Changes from Prior Law:**

- Allows delegation to committee for certain transactions
- No longer requires both court approval and notice to Attorney General



Committees

▪ **Board Committees**

- Eliminates distinction between “standing” and “special” board committees
- May be formed in by-laws or by resolution of a majority of entire board
- Appointment of members requires vote of majority of entire board
- At least three members required
- All committee members must be directors
- Non-directors may serve in an advisory, non-voting role
- Committee may be vested with board authority, subject to certain limitations contained in the Not-for-Profit Corporation Law



Committees

- **Committees of the Corporation**

- May be formed in by-laws or by resolution of board or members
- Non-directors may serve as members
- Appointment of members by same procedure used to name officers or as set forth in by-laws
- Cannot be vested with any authority of the board
- Generally used for advisory purposes or to carry out specific events or activities
- Can be used to involve volunteers or recruit new directors



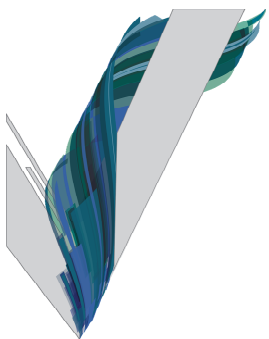
Executive Compensation

- Permits payment of reasonable compensation to members, directors and officers for services
 - Note that many non-profits do not compensate directors and officers for their service on the board
- Attorney General guidance indicates that transactions related to compensation are not related party transactions
 - However, the person who will benefit from compensation decision may not be present at or otherwise participate in board or committee deliberation or vote
 - Exception: board or committee may request information, background or response to questions prior to beginning deliberations or voting
- Note: benefits and severance payments must also be reasonable
 - An employment contract that provides for full payment if dismissed without cause could result in excessive severance payments



Recommendations

- Review and revise by-laws as needed:
 - Review voting requirements
 - Consider adding definition of “entire board”
 - Remove distinction between standing and special committees; distinguish between committees of the board and committees of the corporation
 - Consider adding prohibition on employee service as chair
 - Consider adding email provision for notices, waiver of notices and unanimous written consent
 - Consider adding video conference meeting option
- Adopt or update policies:
 - Conflicts of Interest
 - Whistleblower (if required or as a “best practice”)
 - Audit Oversight (or include in Audit Committee Charter)
 - Communications
- Develop a plan for having an adequate number of “independent directors”
- Develop a plan and timetable for compliance if cannot be accomplished immediately



Questions?



contact information

YOUR VENABLE TEAM

Susan Golden, Counsel

sgolden@venable.com

t 212.370.6254

f 212.307.5598

Sharon Connelly, Associate

smconnelly@venable.com

t 212.370.6278

f 212.307.5598

www.Venable.com/nonprofits

<https://twitter.com/nonprofitlaw>

www.YouTube.com/user/VenableNonprofits