The New York Non-Profit Revitalization Act

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Background

- **The New York Non-Profit Revitalization Act**
  - First major revision to the New York Not-for-Profit Corporation Law in over 40 years
  - Most changes become effective on July 1, 2014
  - NY State Attorney General's Charities Bureau is updating forms and publications and drafting new guidance in response to the Act, which will be available at http://www.charitiesnys.com/nonprofit_rev_act_guidance.jsp
  - A technical corrections bill and a bill to delay the effective date of certain provisions have been proposed in the NY State Legislature
  - Codifies certain "best practices"
  - Relationship to IRS regulations

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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)

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Topics for Discussion

- **Modernization and Streamlining of Procedures**
  - Improved Incorporation Process
  - Disclosure of Personal Information
  - Communication Procedures
  - Approval of Fundamental Transactions
- **Changed Governance Requirements**
  - Audit Procedures
  - Related Party Transactions
  - Conflict of Interest Policy
  - Whistleblower Policy
  - Approval of Real Estate Transactions
  - Committees
  - Executive Compensation

Modernization and Streamlining

- **Improved Incorporation Process**
  - Eliminates Corporate “Types”
  - Minimizes Agency Pre-Approvals for Some Organizations

- **Disclosure of Personal Information**
  - Previously required to allow inspection of <u>names and residential addresses</u> of officers and directors upon request by members, creditors and state officials; now only <u>names</u> must be provided

Modernization and Streamlining

- **Modernized Communications**
  - Email:
    - Meeting Notice (Members)
    - Waiver of Notice (Members and Directors)
    - Unanimous Consent (Members and Directors)
    - Proxy (Members)
  - Video Conferencing (Directors)

- **Attorney General Option for Merger, Dissolution, and Fundamental Transactions**
  - In lieu of <u>both</u> court approval <u>and</u> notice to Attorney General

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Modernization and Streamlining

- **Recommendations:**
  - If new incorporation, check the purposes clause
  - Solicit emails from members and directors with express stated purpose of using for notice; adopt electronic communications policy
  - Check articles of incorporation and bylaws 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

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 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**
  - For nonprofits required to submit independent auditor report under charitable solicitations law (NY Exec. Law 172-b)

- **Audit committee composed of "independent directors" or full board oversight with only "independent directors" participating**

- **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
  - Post-audit review and discussion with auditor
  - Consideration of performance and independence of auditor
  - Reporting of committee's activities to the board

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
- Employees may not serve as chair of the board or in an officer position with similar responsibilities (effective July 1, 2015)

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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

  (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 <u>do not include</u>:**
  - 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

- **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

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Governance: Related Party Transactions

- **Additional Requirements: If the related party has a <u>substantial financial interest</u> in the transaction, <u>charitable organizations</u> 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:
    - Current Not-for-Profit Corporation Law requires <u>either</u> that transaction was fair and reasonable <u>or</u> interest of related party was disclosed and their vote was not required for approval
    - Current Not-for-Profit Corporation Law <u>does not require</u> consideration of alternative transactions or documentation of basis for approval
  - No exception 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: Conflict of Interest Policy

Act requires **<u>all</u>** nonprofits 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

(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** <u>related-party transactions</u>

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

- Recommendation: 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** composed solely of independent directors

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Governance: Whistleblower Policy

- **Required for nonprofits having:**
  - 20 or more employees **and**
  - Annual revenue in excess of $1 million in the prior fiscal year
- **The whistleblower policy shall 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, and employees, as well as to volunteers who provide substantial services to the corporation.

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 as a routine matter)

- **If not "all or substantially all" of assets**
  - Delegation to committee is allowed
  - Approval by majority of directors <u>or</u> majority of authorized committee
  - Committee must report back to board

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Real Estate Transactions

- **If “all or substantially all” of assets**
  - Delegation to committee <u>not</u> permitted
  - Boards with less than 21 members: approval by <u>two-thirds</u> of entire board
  - Boards with 21 or more members: approval by <u>majority</u> 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 <u>or</u> court approval (for charitable corporation)

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Real Estate Transactions

- **Changes from Current Law:**
  - Allows delegation to committee for certain transactions
  - No longer requires both court approval and notice to Attorney General

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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**
  - 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

- 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

Questions?

contact information

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