The New York Nonprofit Revitalization Act of 2013
Changes to the Nonprofit Corporation Law

Nancy Sciocchetti, Esq.

Nonprofit Revitalization Act - Background

➢ Enacted: December 18, 2013
➢ Effective: July 1, 2014 (most provisions)
➢ Result of recommendations by the Leadership Committee on Non-Profit Revitalization, a panel appointed by the Attorney General
➢ Intent is to reduce burden to nonprofits, create efficiencies in process, and enhance governance and oversight
➢ Applies to all nonprofits incorporated in New York or operates/solicits charitable contributions in New York
➢ 1st substantial reform of nonprofit laws in over 40 years
➢ Current corporations should review existing internal controls, by-laws, policies, and committee charters
Nonprofit Revitalization Act - Background

➢ Be proactive - the actions corporations need to take can be complicated and may take considerable time to accomplish
➢ The Attorney General’s office recognizes that full compliance may take some time
➢ The Chief of the Charities Bureau has noted that there will be education before enforcement
➢ This year, a corporation just needs to be prepared to show that it is aware of the statute and is making a good faith reasonable effort to come into compliance
➢ For its part, the Attorney General’s office will also look at common issues and see what education is needed

Key Changes

➢ Improve Efficiencies
  • Eliminates letter types
  • Modernizes member meeting communications
  • Modernizes other member and Board communications
  • Restructures committees
  • Simplifies real estate transactions approvals
  • Simplifies approval of significant events
  • Raises financial reporting thresholds
Key Changes

- Strengthen Governance
  - Adds audit oversight responsibilities
  - Expands Conflict of Interest policy requirements
  - Adds Whistleblower policy requirements
  - Expands Related Party Transactions requirements
  - Adds executive compensation restrictions

- Increase Attorney General Authority

Corporation “Types”

- Previously 4 types of nonprofit corporations:
  - Type A
  - Type B
  - Type C
  - Type D

- Under the Act, a corporation is either designated as charitable or non-charitable
  - Charitable
    - Purposes: charitable, educational, religious, scientific, literary, cultural, or prevention of cruelty
    - Formerly: Type B, Type C, and Type D (if formed for charitable purpose)
  - Non-charitable
    - Purposes: all others, including civic, patriotic, social, fraternal, athletic, purpose of operating trade/business
    - Formerly: Type A and Type D (all others)
Certificate of Incorporation

- Must state the corporation’s purpose
- May describe the activities the corporation will undertake (or otherwise state how the purpose will be achieved)

Number of Directors

- If there is a specific range in the by-laws regarding the authorized number of directors, the “entire Board” is the number of directors elected at the most recently held election
- If the by-laws provide for a fixed number of directors, it is that number
- The number of directors may be increased or decreased by amendment of the by-laws, or in the case of a corporation having members, by action of the members, or of the Board under the specific provisions of a by-law adopted by the members
  - However, if the Board is authorized by the by-laws to change the number of directors, whether by amending the by-laws or by taking action under the specific provisions of a by-law adopted by the members, such amendment or action shall require the vote of a majority of the entire board
Committee Types

- No longer a distinction between standing and special committees
- Committees are now either:
  - Committees of the Board
    - Comprised only of directors
    - Have the ability to bind the Board
  - Committees of the corporation
    - May include directors and non-directors
    - Does not have the ability to bind the Board

Board Chair

- The Act prohibits any employee of a nonprofit corporation from serving as board chair
  - Effective 1/1/16
  - CEO and Chair of Board cannot be the same person
Conflict of Interest Policy

- Required for every nonprofit corporation and charitable trust
- Must be a written policy

Conflict of Interest Policy

- Must include the following:
  - Definition of circumstances constituting a conflict of interest
  - Procedure for disclosing conflicts to audit committee or Board of Directors
  - Requirement that conflicted persons not be present at or participate in Board/trustee/committee deliberations or voting on matter giving rise to the conflict
  - Prohibition against any attempt by conflicted person to influence deliberations/votes on matter giving rise to conflict
  - Requirement that the existence/resolution of the conflict be documented in the corporation’s records
  - Procedure for disclosing, addressing, and documenting related party transactions
Conflict of Interest Policy

- Must include the following:
  - Requirement that directors/trustees, before initial election/appointment and annually thereafter, must disclose certain potential conflicts of interest
    - Each director must provide a written statement identifying any conflict specified in the Act
  - Conflict means you have a direct financial interest in the outcome that is adverse to the organization
  - Aimed at directors, officers, and key employees, but if someone functions like a director, s/he must follow these rules as well
    - “Key employee” means a person who is in a position to exercise substantial influence over the corporation

Related Party Transactions

- Involves nonprofit corporations (N-PCL § 715) and charitable trusts (EPTL § 712(e))
- For all nonprofit/charitable trusts
  - Generally prohibits any related party transactions unless Board of Directors determine that it is fair, reasonable, and in organizations best interest
- “Key employees” are now covered in addition to directors and officers
  - As noted previously, “key employee” means any person who is in a position to exercise substantial influence over the affairs of the corporation
- Related party transaction does not necessarily involve a financial stake; applies if
  - Related party has a substantial financial interest in a related party transaction
  - When contemplating related party transactions
    Board/trustees/officers/authorized committee of Board must:
    - Consider alternative transaction (prior to entering transaction)
    - Approve transaction by no less than majority of vote of directors/trustees/committee members present at meeting
    - Contemporaneously document the basis for its approval
Related Party Transactions

- If director/trustee/officer/key employee has interest in related party transaction
  - Must disclose material fact in good faith
  - Refrain from participating in deliberations/voting but may provide info beforehand
- May be subject to additional restrictions in certificate of incorporation/by-laws
- Act also gives Attorney General power to take action to enforce these provisions and impose steep penalties

Whistleblower Policy

- Mandatory for nonprofit corporations/charitable trusts:
  - With 20 or more employees AND
  - Revenue of greater than $1 million (prior fiscal year)
- Must prohibit retaliation
Whistleblower Policy

- Must include:
  - Procedures for reporting violations or suspected violations of laws or corporate/trust policies, including procedures for preserving confidentiality for such reported information
  - Requirement that a director and/or officer/employee be designated to administer policy and report to committee or Board (if no committee designated)
  - Requirement that the policy be distributed to all directors/trustees/officers/employees/volunteers with instructions on how to comply
  - Report to audit committee: at least 1 time per year (recommended 4 times per year) and should include a summary of the process (including complaints resolved, complaints outstanding, what was done to resolve issues, etc.)

- Note: Volunteers are included in the policy
- Only interest in illegal activities and fraud (not concerned with personnel issues)

Changes to Annual Reporting

- Applies to charitable organizations (and charitable trusts) which solicit contributions or receive government grants
  - Organizations registered under Exec Law, Article 7-A § 172 and EPTL, Article 8
- Must register with the Attorney General and file a financial report annually
- Increased threshold for heightened financial review requirements for organization
- Effective 7/1/14
  - $250,000 or less → unaudited financial report on forms provided by Attorney General
  - Over $250,000 to $500,000 → independent CPA review report
  - Over $500,000 → independent CPA audit report
Changes to Annual Reporting

- Effective 7/1/17
  - $250,000 or less → unaudited financial report on forms provided by Attorney General
  - Over $250,000 to $750,000 → independent CPA review report
  - Over $750,000 → independent CPA audit report

- Effective 7/1/21
  - $250,000 or less → unaudited financial report on forms provided by Attorney General
  - Over $250k to $1,000,000 → independent CPA review report
  - Over $1,000,000 → independent CPA audit report

After Attorney General reviews independent CPA review report, may require organization to obtain/file with Attorney General independent CPA audit report.

Can make these submissions electronically.

Increased filing fee.
Audits - Background

- Oversight of organizations accounting/financial reporting processes and audit of its financial statements must be performed by a designated audit committee of the Board of Directors
  - Comprised of at least 3 independent directors
  - May comprise entire board of the organization but only if independent director/trustees attend/participate in audit committee matters
  - If audit committee performs these duties, the committee must report to the Board of Directors

Audits - Background

- Independent director (defined under N-PCL)/independent trustee (defined under EPTL) is a
  - Director/trustee who:
    - Is not/has not been in last 3 years an employee of the organization or any affiliate
    - Has not received more than $10,000 in direct compensation from the organization/affiliate in any of the last 3 years (other than reimbursement expenses reasonably incurred as director/trustee or reasonable compensation for serving as director/trustee permitted under N-PCL § 202 or trustee commission)
    - Not current employee of/does not have substantial financial interest in any entity that made payments to or received money from organization/affiliate that exceeds $25,000 or 2% of organization’s gross revenue
    - Also cannot be a relative of director/trustee as described in any of the above
  - Only independent director/trustee may participate in deliberations or voting by Board or committee relating to financial oversight and auditing
Audits - Application

For corporations/charitable trusts that solicit charitable contributions and gross revenue exceeds $500,000 the Board or audit committee of independent directors must:

- Oversee accounting/financial reporting processes of organization and audit of its financial statements
- Annually retain and review retention of independent auditor
- Review with independent auditor results of audit
- Oversee the adoption, implementation of, and compliance with any conflict of interest policy or whistleblower policy (unless otherwise performed by another committee consisting solely of independent directors)

Audits - Application

For corporations/charitable trusts that solicit charitable contributions and gross revenue exceeds $1,000,000 the independent director or audit committee of independent directors must:

- Review with independent auditors the scope/planning of the audit prior to commencement of the audit
- Upon completion of the audit, discuss the following with the auditors
  - Any material risks/weaknesses in internal controls identified by the auditor
  - Any restrictions on the scope of the auditor's activity or access to required information
  - Any significant disagreement between auditor and management
  - The adequacy of the corporation's accounting/financial reporting processes
- Annually consider performance/independence of independent auditor
- If these duties are performed by an audit committee, report back to the Board.
Audits - Application

- The audit oversight requirements do not come into effect until January 1, 2015 for corporations with less than $10 million in annual revenue in the last fiscal year ending prior to January 1, 2014

Audits - Enforcement

- The Attorney General will be looking at the following:
  - Whether the organization has an audit committee
  - Whether the audit committee oversees audit/financial reporting
  - Whether the organization retained an independent auditor
  - Whether the organization reviewed the audits
- Why the Attorney General cares about audits
  - One opportunity for an outside professional to evaluate how well management is doing
  - Also an opportunity to look to see if management is effective
  - Internal controls, examine fraud risk, etc.
Publication Requirement

- Did not change
- New York private foundations must still annually publish notices of availability on Form 990-PF for public inspection
  - This means they must make their tax documents available for public inspection
- Must report direct charitable expenses correctly, as well as any transfers to and transactions and relationships with non-charitable exempt organizations

Fundraising Professionals

- Nonprofit must have written contracts with any fundraising professional they engage
  - Contract must contain specific anti-fraud provision
  - Fundraiser must file with Charities Bureau and send written confirmation to nonprofit that in full compliance
- Change in Act (re: Grant Writers)
  - Act exempts individuals hired solely to draft grant applications to government agencies and philanthropic organizations recognized as tax exempt under § 501(c)(3) of the federal tax code
Electronic Communication and Videoconferences

- Corporations can now send the following via e-mail or fax:
  - Notices of meetings sent to members
  - Waivers of notice of meetings by members/directors
  - Consent to corporate actions by member vote
  - Consent to a decision taken without a Board meeting (if in by-laws)
    - Consent without meeting must be unanimous
  - Authorization of members’ proxies
  - Distribution of financial statements can be via any means including email and fax
- For all these communications, the signature of the member/director must be affixed

Electronic Communication and Videoconferences

- Emails must show the member/director authorized sending it
- Videoconferences
  - Directors can participate in Board/committee meetings through videoconference (e.g., Skype, FaceTime)
Notices

- Notices are deemed to be given when directed to the member’s fax number or email address as it appears on the record of members or as on file with the Secretary.
- Faxed or emailed notices will not be deemed to have been given if the corporation is unable to deliver two consecutive notices by these methods or the corporation otherwise becomes aware that notice cannot be delivered by these methods.
- If notice is given by publication, the corporation must also prominently post notice of the meeting on the homepage of its website from the date of publication through the date of the meeting.
  - Notice by publication is only allowed if the corporation has over 500 members.
- Must give notice by mail if requested in writing by a member.

Voting – Real Estate Transactions

- Reduced vote for purchase, sale, mortgage, lease, or other disposition of real property.
  - Reduced from 2/3 of entire Board to a majority.
    - Unless the purchase/disposition constitutes all or substantially all assets of the corporation.
      - Then vote of 2/3 of entire Board is required (or by majority if there are 21 or more directors).
  - Definition of “entire Board”:
    - Total number of all directors entitled to vote which the corporation would have if there were no vacancies OR
    - If, according to by-laws it is a fixed number of directors, then it is that number OR
    - If, according to by-laws the number shall be a range, it is the number of directors within the range elected at the most recent election.
  - The Board may delegate approval to a committee if it does not involve all or substantially all of the corporation’s assets.
Mergers and Consolidations

- Merger: combination of two or more corporations into a single corporation which is one of the constituent corporations
- Consolidation: combination of two or more corporations into new corporation
- Attorney General can approve
- For educational nonprofits chartered by regents, consolidations and mergers can be granted by regents
- Application to Attorney General should include:
  - All information required for court approval
  - Consents/approvals required under § 404
  - Statement as to whether anyone objected or may reasonably object
- Corporation may seek court approval at any time upon notice to Attorney General

Distribution of Assets

- Corporation seeking to dispose all/substantially all assets may petition Attorney General (instead of Supreme Court)
- Petition must set forth:
  - All information required in court petition
  - Statement of solvency
  - Statement as to whether anyone objected or may reasonably object
- Attorney General may authorize if fair and reasonable
- Corporation may use this procedure unless
  - Insolvent or would become insolvent as a result of transaction
  - Attorney General concludes Supreme Court should review
Dissolution of Nonprofit Corporations

- Attorney General may approve the plan of dissolution for charitable and non-charitable N-PCL corporations
- May apply to Supreme Court upon notice
- The Act deletes procedures for dissolution of corporations with minimal assets without Court or Attorney General approval

Summary of Attorney General Approval

- Attorney General (Charities Bureau) can now approve:
  - Sale, lease, exchange, or other disposition of all/substantially all corporate assets
    - Exception: if a corporation is insolvent, or will become insolvent as a result of the transaction
  - Amendments to purposes/powers in Certificate of Incorporation
  - Mergers/consolidations of charitable corporations
  - Plan of dissolution of charitable/non-charitable corporations holding assets required to be used for a specific purpose
- Corporations may still seek court approval at any time or appeal the Attorney General’s denial of a transaction
- Attorney General may require corporation to seek court approval
Increased Attorney General Enforcement Authority

- Attorney General may enjoin, void or rescind any completed or proposed related party transaction that is not reasonable or in the best interests of the corporation at the time of approval
  - Attorney General may also seek restitution or the removal of directors or officers in such cases
- Attorney General may impose double damages in the case of willful and intentional conduct
- Attorney General may bring action against any corporation that is not in compliance with N-PCL approval requirements or charities registration requirements
  - But as previously noted, the Chief of the Charities Bureau has noted that there will be education before enforcement

Next Steps

- Adopt and implement new policies
  - Conflict of Interest
  - Related Party Transactions
  - Whistleblower
- Review and amend corporate by-laws
- Implement operational changes regarding corporate governance (e.g., sending and documenting notices and consents)
- Review committee constitution and structure for compliance
- Conduct Board and leadership education on changes
Questions?

Nancy Sciocchetti, Esq.
(518) 462-5601
nsciocchetti@oalaw.com

O’Connell & Aronowitz
54 State Street, Albany, NY 12207