

*Tax-Exempt Organizations Practice Group*

June 7, 2017

## **Further Changes to the New York Not-for-Profit Corporation Law: 2015 and 2016 Amendments**

The New York Non-Profit Revitalization Act of 2013 (the “**NPRA**”) was the first major amendment to the New York Not-for-Profit Corporation Law (the “**N-PCL**”) since it was enacted in 1970. The NPRA was a dramatic overhaul of the N-PCL. For more information on the NPRA, see our January 2014 advisory entitled “[New York Non-Profit Revitalization Act.](#)”

In the last two years, four further amendments (the “**Amendments**”) have been adopted to clarify and improve the provisions of the N-PCL added by the NPRA. The most recent of these Amendments was signed into law on November 29, 2016 and became effective on May 27, 2017. The key changes introduced by the Amendments are described below. Organizations should review their bylaws, conflict of interest and whistleblower policies, and Audit Committee charter to ensure compliance with these Amendments.

### **Governance**

#### *Entire Board*

The NPRA introduced language to liberalize the “entire board” concept found in the N-PCL and make it easier to administer changes to the size of the board for most corporations. The Amendments added some clarifying provisions to help corporations apply these provisions. Now, when a corporation’s bylaws provide that the number of directors may consist of a range between a minimum and maximum number, and the size of the board within that range has not been fixed, the definition of “entire board” means the number of directors within such range that were elected or appointed at the most recent election of directors. If the corporation has a board with staggered terms, the number of directors also includes those whose terms have not yet expired. For corporations that have fixed a number of directors in the bylaws or by board resolution, “entire board” means that fixed number. The Amendments also empowered the board of a membership corporation to change the number of directors, if permitted by the bylaws. Prior to the Amendments, the board of a membership corporation could not change the number of directors without a vote by the members.

#### *Employee as Board Chair*

The Amendments relaxed a restriction, which was introduced by the NPRA but never took effect, barring employees from serving as Chair of the board or holding any other title with similar responsibilities. Effective January 1, 2017, an employee *may* serve as Chair if (i) he or she receives a two-thirds vote of the entire board and (ii) the board contemporaneously documents the basis for such approval.

*Board Committees*

The Amendments added the four items below to the list of matters as to which no committee of any kind may have authority. These restrictions were always implicit in the N-PCL, but this change makes them explicit.

- The election or removal of officers and directors;
- The approval of a merger or plan of dissolution;
- The adoption of a resolution recommending to the members action on the sale, lease, exchange or other disposition of all or substantially all of the assets of a corporation or, if there are no members entitled to vote, the authorization of such transaction; and
- The approval of amendments to the certificate of incorporation.

The Amendments also created a higher voting threshold for appointing the members of the Executive Committee. The law now requires that a majority of the *entire board* must appoint the members of the Executive Committee (or, in the case of a board of 30 or more members, at least 3/4 of the directors present at the time of the vote, if a quorum is present at that time). This is a higher threshold than for other committees of the board, whose members may be appointed by the board in the same manner as the board takes other actions.

*Administration of Conflict of Interest Policy and Whistleblower Policy*

The NPRA added a requirement to the N-PCL that nonprofit corporations with 20 or more employees and annual revenue in excess of \$1 million must adopt a whistleblower policy and distribute it to their directors, officers, employees, and volunteers who provide substantial services to the corporation. The Amendments clarified that this distribution requirement may be satisfied by posting the policy conspicuously in the corporation's offices or on its public website.

The Amendments permit disclosures under the Conflict of Interest Policy and complaints under the whistleblower policy to be made to and investigated by the board *or a committee of the board* (which may include directors who are not "independent directors"). The NPRA had previously introduced provisions to the N-PCL that limited oversight of such activities to independent directors.

The Amendments also added the following restrictions to the whistleblower provisions in the N-PCL:

- directors who are employees may not participate in board or committee deliberations or voting relating to administration of the whistleblower policy; and
- the person who is the subject of a whistleblower complaint may not be present at or participate in board or committee deliberations, or vote on the matter relating to such complaint, but may present information as background or answer questions at a meeting prior to the commencement of deliberations or voting if requested by the board or committee.

## **Related Party Transactions: Changes and Clarifications**

The NPRA refined the procedures and requirements governing transactions with related parties, and the Amendments have revised several related definitions. A “related party” now includes domestic partners and the domestic partners of descendants, as well as “key persons.” “Key person” is a new term with a similar meaning to its predecessor in the NPRA. It replaces the defined term “key employee,” and clarifies that related parties may include individuals with power, influence or management over all or part of the operations or expenditures of a corporation, whether or not such individual is an employee. The Amendments also narrowed the circumstances under which an entity will be considered an “affiliate” of the corporation for purposes of the related party transaction requirements.

In addition, the Amendments narrowed the definition of “related party transaction” by including carve-outs for certain “*de minimis*” or “ordinary course” transactions. A transaction will not be considered a “related party transaction” if (i) the transaction or the related party’s financial interest is *de minimis*; (ii) the transaction would not customarily be reviewed by the board or boards of similar organizations in the ordinary course of business and is available to others on similar terms; or (iii) the transaction is a benefit to the related party solely as a member of a class of beneficiaries the corporation intends to benefit as part of accomplishing its mission and is available to all similarly situated members of the same class on the same terms.

The Amendments also clarified certain procedures for entering into related party transactions. These include specifics on when a related party can be present while a transaction is being considered, compensation approval procedures, and a clarification that recusal by a director with a conflict will not destroy a quorum. In addition, the Amendments introduced defenses for failure to comply with the related party transaction procedures in a timely manner. The new provisions allow nonprofit organizations to ratify past transactions that were not properly approved, and to use such ratification as a defense in an action brought by the Attorney General if the ratification occurred prior to the action by the Attorney General.

## **Audit Oversight and Changes to the “Independent Director” Definition**

The NPRA added a requirement that for nonprofit corporations that are required to file audited financial statements with the New York Attorney General, the board, or a designated audit committee comprised solely of “independent directors,” must oversee the accounting and financial reporting processes and audit of the corporation according to certain specified procedures, with only independent directors participating in deliberations regarding these matters. Such corporations are those that receive contributions from the public in excess of \$500,000 during the year. On July 1, 2017, this threshold will be raised to \$750,000, and on July 1, 2021, it will be raised to \$1,000,000.

The Amendments made several changes to the definition of “independent director,” which generally make it easier for directors to fit within this definition. The new definition clarifies that a director may receive reimbursement for expenses reasonably incurred as a director or for service as a director without it being

considered “compensation” from the corporation; and that disqualifying “payments” between the corporation and an entity in which a director has ownership or other interest, generally do not include exchanges in the ordinary course of business, such as dues or fees paid to the corporation for services which the corporation performs as part of its nonprofit purposes, or certain payments made by the corporation at fixed or non-negotiable rates or amounts for services received. The new definition also applies the disqualifying payment thresholds in graduated amounts, tying the application of the rule to the size of the corporation’s budget.

At the same time, the Amendments tightened certain of the rules governing when a director with a relationship to the corporation’s outside auditor can be considered an “independent director.” A director is not “independent” if he or she is, or has a relative who is, a current owner, director, officer or employee of the corporation’s outside auditor or who has worked on the corporation’s audit during the past three years.

### **Real Property Transactions by Religious Corporations**

Finally, the Amendments enabled religious corporations to obtain leave of the Attorney General (rather than court approval) to sell or mortgage real property or lease it for more than five years. These streamlined processes for these transactions are similar to those introduced by the NPRA for nonprofit corporations.

### **Conclusion**

Generally, the Amendments clarified the NPRA and, in some instances, streamline compliance with those provisions. Changes to the related party transaction rules and the independent director definition should ease the burdens imposed by the NPRA as originally drafted. Nonprofit corporations may wish to update their bylaws, conflict of interest and whistleblower policies, and/or Audit Committee charter to take advantage of these new provisions.

---

For more information concerning the matters discussed in this publication, please contact **Pamela A. Mann** or another member of the Tax-Exempt Organizations Group listed below, or your regular Carter Ledyard attorney.

**Pamela A. Mann**

(212) 238-8758

[mann@clm.com](mailto:mann@clm.com)

**Anne K. Gerson**

(212) 238-8769

[gerson@clm.com](mailto:gerson@clm.com)

**Jeremy S. Steckel**

(212) 238-8786

[steckel@clm.com](mailto:steckel@clm.com)

**Justin L. Peters**

(212) 238-8661

[peters@clm.com](mailto:peters@clm.com)

Carter Ledyard & Milburn LLP uses Client Advisories to inform clients and other interested parties of noteworthy issues, decisions and legislation which may affect them or their businesses. A Client Advisory does not constitute legal advice or an opinion. This document was not intended or written to be used, and cannot be used, for the purpose of (i) avoiding penalties under the Internal Revenue Code or (ii) promoting, marketing or recommending to another party any transaction or matter addressed herein.

© 2017 Carter Ledyard & Milburn LLP.