

New York Not-for-Profit Corporation Law: 2016 Amendments

April 18, 2017 | **CLIENT ALERTS**

On November 28, 2016, Governor Cuomo signed into law amendments to the New York Not-For-Profit Corporation Law (the "NPCL") that will become effective May 27, 2017 (the "Amendments"). The Amendments build upon the 2015 amendments to the Nonprofit Revitalization Act that Governor Cuomo signed into law in 2013 and generally improve and clarify certain NPCL terms, particularly with respect to corporate governance of New York non-profit corporations.

The Amendments generally provide the NPCL with more clarity and more favorable terms that are helpful to non-profit corporations in New York. The Amendments include the following important changes:

Definition of "key person."

Definition of related party and process for approval of related party transactions.

The Board Chair may also be an employee of the corporation.

Definition of "independent directors" that are required for any audit committees.

Appointment process and authority of board committees.

It does not appear that any sanctions or penalties would be imposed if a corporation chooses not to adopt these changes. However, a New York non-profit corporation should consider reviewing and revising its bylaws, conflict of interest policy and, if applicable, whistleblower policy, to take advantage of the clarity and broader scope generally afforded by the Amendments. In addition, all nonprofits that conduct activity in New York should confirm their registration status and, if applicable, annual filings, with the New York Charities Bureau.

"Key Person"

The Amendments replace the concept of "key employee" with "key person," which, among other things, broadens the scope of who may not be considered an independent director for purposes of board and board-appointed committee composition. This change also affects who may be considered a related party in the context of related party transactions and conflicts of interest.

Specifically, a "key person" is a person (other than a director or officer of the corporation) who has responsibilities or the power to influence the corporation in a similar way to officers and directors of the corporation, regardless of whether or not such person is an employee. A "key person" may also be one who manages the corporation, or a segment thereof, that "represents a substantial portion of the activities, assets, income or expenses of the corporation" or one who, either alone or with others, "controls or determines a substantial portion of the corporation's capital expenditures or operating budget."^[1]

"Related Party Transaction"

The Amendments broaden the pool of people who may be considered a "related party", as the definition now includes key persons. However, the Amendments simultaneously ease the standard of what constitutes a "Related Party Transaction."

As such, a Related Party Transaction does not exist (1) where the transaction itself or the related party's financial interest in the transaction is "de minimis"; (2) if the transaction is one that would not be customarily reviewed by the board or boards of similar organizations and are available to others on the same or similar terms; or (3) if the transaction constitutes a benefit provided to a related party only as a member of a class of the beneficiaries that the corporation intends to benefit as a part of its mission, as long as the benefit is available to similarly situated members of the same class on the same terms.[2]

Board Chair

The Amendments remove the prohibition on employees serving as the chair of the board. The Amendments allow the board, by a supermajority vote, to approve such appointment as long as (1) the board contemporaneously documents, in writing, the basis for the approval and (2) the board chair employee will not be considered an independent director.[3]

Independent Directors

Under the New York Not-for-Profit Corporation Law, audit committees (to the extent appointed) are required to be comprised solely of independent directors. In addition, to the extent a corporation does not have an audit committee, only independent directors may participate in board or committee deliberations related to any required audit oversight of the corporation. With respect to the independent director requirement, for purposes of the foregoing and as otherwise may be applicable in the NPCL, the Amendments have maintained the criteria for an independent director and have introduced an additional test for independence based on a sliding scale of the corporation's gross revenues and a director's financial interest in an entity that has provided or received payments, property or services to the corporation or an affiliate of the corporation in the last three fiscal years.[4]

Board Executive Committee

With respect to board-appointed committees, the Amendments have updated how the committees may be appointed and what their powers and authorities are. Specifically, a committee of a board consisting of three or more directors may be appointed by the corporation's certificate of incorporation, by-laws, or board by majority vote of a quorum of the directors.[5] However, a supermajority vote of the entire board is required to appoint members of an executive committee and, in the event a board consists of 30 or more members, a vote of three-quarters of the members present at a meeting is required to appoint such a committee.[6] The by-laws may also permit directors who also hold certain positions of the corporation to be ex-officio members of specific committees.

The Amendments further provide that the board may grant the authority of the board, pursuant to a board resolution or the terms of the by-laws of certificate of incorporation, to committees. While the board may grant to such committees limited general powers, a board appointed committee may allow the corporation to enter into a related party transaction if such committee deems it to be fair, reasonable and in the corporation's best interest at the time of the transaction. The Amendments also clarify that the following actions may not be approved by a committee of a not-for-profit corporation: (a) election or removal of officers and directors; (b) approval of a merger or plan of

dissolution; (c) adoption of resolutions recommending to the members the sale of substantially all of the assets of the corporation or similar transaction; (d) amendment to the Certificate of Incorporation. [7]

For purposes of clarity with respect to the updates made to this definition, the Amendments to the NPCL also include revised definitions of the terms "compensation" and "payment."

Conflict of Interest & Whistleblower Policies

While the NPCL previously required a New York non-profit corporation to adopt a conflict of interest policy, the Amendments clarify that now the board must adopt such policy.[8] The Amendments also remove the prior requirements that only independent directors may oversee the implementation of, and compliance with, the corporation's conflict of interest policy and, to the extent applicable, whistleblower policy, and that such policies be administered by either an audit committee consisting of independent directors or the board. Instead, the Amendments provide that the board or any board-appointed committee may administer these policies.[9] The flexibility to provide oversight of conflicts and compliance matters to a committee other than an audit committee may be useful to corporations that either have distinct committees to handle such functions (e.g., compliance or conflicts of interest committees) or split those functions between separate committees (e.g., governance committee to handle conflicts issues and audit committee to handle compliance). In the case of the whistleblower policy, the Amendments provide that an employee who is also a director may not take part in any board or committee deliberation concerning the administration of such policy.[10] Likewise, a person who is the subject of a whistleblower complaint may not be present at, or participate in, a board or committee deliberation or vote on the matter relating to the complaint.

Registration with the Charities Bureau

Although not necessarily connected to the Amendments, it is worth noting that, unless otherwise exempted, Section 7-A of the New York Executive Law generally requires charitable organizations (including those not formed under New York Law) to register with the New York Charities Bureau if such organization solicits contributions from New York residents, foundations, corporations, government agencies and other New York entities. Likewise, the New York Estates, Powers and Trusts Law also requires that charitable organizations formed in New York or that otherwise conduct activity in New York register with the Charities Bureau unless otherwise exempted. In order to register, a nonprofit organization must complete and submit a Form CHAR410, and subsequently file with the Charities Bureau the Form CHAR500 on an annual basis.

For questions related to not-for-profit corporations other than healthcare organizations, please contact Brendan J. Rich, Corporate & Securities Practice Group Leader, brich@lippes.com. Questions related to not-for-profit healthcare institutions can be directed to either Scott V. Carroll, Healthcare Practice Team Leader, scarroll@lippes.com or Elise M. DeRose, ederose@lippes.com.

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