

Nonprofit Revitalization Act and Executive Compensation Reform Act of 2013: Proposed New York Laws Would Reform Governance Rules for Nonprofits

New York Attorney General Eric Schneiderman is urging the state legislature to enact two bills that would reform the statutory requirements for governance of nonprofit organizations – both not-for-profit corporations and wholly charitable trusts. If the bills become law, they also would expand the Attorney General's enforcement powers and modernize and clarify some of the more mechanical and procedural New York rules applicable to not-for-profit corporations.

The two bills – known as the Nonprofit Revitalization Act and the Executive Compensation Reform Act – follow several rounds of review and comment from the nonprofit community and would represent the largest overhaul of New York nonprofit law since 1970.

In their current form, the bills generally contemplate a January 1, 2014 effective date. Obviously, the results and timing of the Albany legislative process are uncertain. But regardless of the outcome in New York, the bills provide an index of regulators' increasingly high expectations for nonprofit governance and may be a harbinger of things to come both in New York and elsewhere across the country. We will update our readers as the bills progress through the legislative process.

Click [here](#) for an Overview of Applicability. Click [here](#) for a Summary of Proposed New Governance Requirements.

Click [here](#) for Highlights of Proposed Update of the Not-for-Profit Corporation Law and Proposed Expansion of the Attorney General's Enforcement Powers.

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Nonprofit Revitalization Act and Executive Compensation Reform Act of 2013: Overview of Applicability

Applicability is a threshold issue for any organization trying to understand the proposed Nonprofit Revitalization Act and the Executive Compensation Reform Act. This chart shows the architecture of the two bills, so that you can identify the portions that would apply to your organization.

All Not-for-Profit Corporations and Wholly Charitable Trusts	<ul style="list-style-type: none"> → Related Party Transaction Rules (Basic) → Mandatory Conflict of Interest Policy → Basic Compensation Rules → Defined Terms
Not-for-Profit Corporations and Wholly Charitable Trusts with 20 or More Employees and Annual Revenue in Excess of \$1,000,000	<ul style="list-style-type: none"> → Mandatory Whistleblower Policy
Charitable Corporations and Wholly Charitable Trusts ("Charities")	<ul style="list-style-type: none"> → Related Party Transaction Rules (Augmented)
Charities Required to Register to Conduct Charitable Solicitations in New York	<ul style="list-style-type: none"> → Mandatory Compensation Committee or Board Compensation Function (Basic Duties)
If Annual Revenue in Excess of \$500,000	<ul style="list-style-type: none"> → Mandatory Audit Committee or Board Audit Function (Basic Duties)
If Annual Revenue in Excess of \$1,000,000	<ul style="list-style-type: none"> → Mandatory Audit Committee or Board Audit Function (Augmented Duties)
If Annual Revenue In Excess of \$2,000,000	<ul style="list-style-type: none"> → Mandatory Compensation Committee or Board Compensation Function (Augmented Duties)

Nonprofit Revitalization Act and Executive Compensation Reform Act of 2013: Summary of Proposed New Governance Requirements

Covered Organizations	Topic	Summary
<p>All Not-for-Profit Corporations and Wholly Charitable Trusts*</p>	<p>Related Party Transaction Rules (Basic)</p> <p><i>(See augmented rules below applicable only to Charitable Corporations and Wholly Charitable Trusts.)</i></p>	<p>A covered organization may not enter into a related party transaction unless the transaction is fair, reasonable and in the organization’s best interest.</p> <p>A director, officer or key employee who has an interest in a related party transaction must disclose in good faith to the Board or an authorized Board committee the material facts concerning such interest.</p> <p>Additional restrictions and procedures may be set forth in the organization’s governing documents or a policy adopted by the Board.</p> <p>No related party with an interest in a related party transaction may participate in deliberations or vote on the related party transaction.</p>
	<p>Mandatory Conflict of Interest Policy</p>	<p>Each covered organization must adopt a Conflict of Interest Policy.</p> <p><u>Contents of the Conflict of Interest Policy</u></p> <p>The Conflict of Interest Policy, at a minimum, must include:</p> <p>(a) a definition of the circumstances that constitute a conflict of interest;</p> <p>(b) procedures for disclosing a conflict of interest to the Audit Committee, or if no Audit Committee exists, to the Board;</p> <p>(c) a requirement that the conflicted person not be present at or participate in Board or committee deliberations or vote on the matter;</p>

New defined terms under the Nonprofit Revitalization Act and Executive Compensation Reform Act of 2013 appear in this summary in bold. A glossary of defined terms appears at the end of the summary.

References to “directors” include trustees of wholly charitable trusts. References to the “Board” refer to a Board of Directors or other governing body of a corporation and to the collective trustees of a wholly charitable trust.

*Unless otherwise specified, references to “not-for-profit corporations” include both charitable and non-charitable not-for-profit corporations (such as those formed for social, fraternal or political purposes). The bills clearly apply to New York not-for-profit corporations and New York wholly charitable trusts. Some portions of the bills also apply in certain circumstances to non-New York charities required to register to conduct charitable solicitations in New York. The applicability, if any, of the remaining portions of the bills to non-New York organizations that conduct activities or hold property in New York is not stated.

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Covered Organizations	Topic	Summary
<p>All Not-for-Profit Corporations and Wholly Charitable Trusts*(cont'd)</p>	<p>Mandatory Conflict of Interest Policy (cont'd)</p>	<p>(d) a prohibition of any attempt by the conflicted person to influence the deliberations or vote on the matter;</p> <p>(e) a requirement that the existence and resolution of the conflict be documented in organization records, including minutes of any meeting where the conflict is discussed or voted on; and</p> <p>(f) procedures for disclosing, addressing and documenting related party transactions.</p> <p>The Policy must also require that, prior to initial election and annually thereafter, each director submit to the secretary a signed written statement identifying (1) any entity of which the director is an officer, director, trustee, member, owner or employee, with which the organization has a relationship and (2) any transaction in which the organization is a participant and in which the director might have a conflicting interest. The secretary must provide copies of all such statements to the chair of the Audit Committee or, if none, to the chair of the Board.</p>
	<p>Basic Compensation Rules</p> <p><i>(See additional compensation-related rules below applicable to certain Charitable Corporations and Wholly Charitable Trusts that are required to register to conduct charitable solicitations in New York.)</i></p>	<p>Total compensation paid to any employee must be fair, reasonable and commensurate with the services the employee provides to the organization.</p> <p>No employee or other individual who may benefit from compensation or benefits provided by the organization may be present at or otherwise participate in any Board or committee deliberation or vote concerning such compensation or benefits.</p>

Covered Organizations	Topic	Summary
<p>Not-for-Profit Corporations and Wholly Charitable Trusts with 20 or More Employees and Annual Revenue in Excess of \$1,000,000</p>	<p>Mandatory Whistleblower Policy</p>	<p>Each covered organization must adopt a Whistleblower Policy that protects from retaliation persons who report suspected improper conduct.</p> <p><u>Contents of the Whistleblower Policy</u></p> <p>The Whistleblower Policy must provide that no director, officer, employee or volunteer who in good faith reports any action or suspected action taken by or within the organization that is illegal, fraudulent or in violation of any policy of the organization shall suffer intimidation, harassment, discrimination or other retaliation or, in the case of employees, adverse employment consequences.</p> <p>The Whistleblower Policy must include:</p> <p>(a) procedures (including confidentiality provisions) for reporting violations or suspected violations of laws or organization policies;</p> <p>(b) a requirement that an employee, officer or director be designated to administer the Policy and report to the Audit Committee, another committee of independent directors or the Board; and</p> <p>(c) a requirement that a copy of the Policy be distributed to all directors, officers, employees and volunteers.</p>
<p>Charitable Corporations and Wholly Charitable Trusts (“Charities”)</p>	<p>Related Party Transaction Rules (Augmented)</p>	<p>If a related party of a covered organization has a substantial financial interest in a related party transaction, the Board or authorized Board committee must:</p> <p>(a) prior to entering into the transaction, consider alternative transactions to the extent available;</p> <p>(b) approve the transaction by not less than a majority vote of the directors or committee members present at the meeting; and</p> <p>(c) contemporaneously document in writing the basis for its approval of the transaction, including consideration of any alternative transactions.</p>

Covered Organizations	Topic	Summary
<p>Charities Required to Register to Conduct Charitable Solicitations in New York</p>	<p>Mandatory Compensation Committee or Board Compensation Function (Basic Duties)</p> <p><i>(See augmented duties below if annual revenue in excess of \$2,000,000.)</i></p>	<p>Either each covered organization must have a Compensation Committee consisting of independent directors, or the independent directors on its Board must perform the duties of a Compensation Committee.</p> <p><u>Basic Duties of the Compensation Committee</u></p> <p>The Compensation Committee or the independent directors on the Board must:</p> <p>(a) review and approve the total compensation paid to the organization’s principal executive officer; and</p> <p>(b) determine that the total compensation paid to the principal executive officer is fair, reasonable and commensurate with the services provided.</p> <p>The review and approval must occur whenever the term of employment, if any, of the principal executive officer is renewed or extended and whenever the compensation is materially changed.</p> <p><u>Compensation Consultant</u></p> <p>The Compensation Committee or the independent directors on the Board must be directly responsible for the appointment, compensation and oversight of any compensation consultant retained to assist the Committee or the independent directors with their work. Any such consultant must report directly to the Compensation Committee or the independent directors.</p> <p>The Compensation Committee or the independent directors on the Board must approve the compensation peer group recommended by the consultant to develop comparable data.</p> <p>Prior to retaining the consultant, the Compensation Committee or the independent directors on the Board must determine the consultant’s independence and the consultant’s qualification to render advice concerning compensation.</p> <p>A compensation consultant may not be deemed independent in certain circumstances – e.g., if within the preceding two years the consultant has received compensation from the organization, other than reasonable amounts paid for compensation consulting.</p>

Covered Organizations	Topic	Summary
<p>Charities Required to Register to Conduct Charitable Solicitations in New York with Annual Revenue in Excess of \$500,000</p>	<p>Mandatory Audit Committee or Board Audit Function (Basic Duties)</p> <p><i>(See augmented duties below if annual revenue in excess of \$1,000,000.)</i></p>	<p>Either each covered organization must have an Audit Committee consisting of independent directors, or the independent directors on its Board must perform the duties of an Audit Committee.</p> <p><u>Basic Duties of the Audit Committee</u></p> <p>The Audit Committee or the independent directors on the Board must:</p> <ul style="list-style-type: none"> (a) annually retain or renew the retention of an independent auditor; (b) review and discuss with the independent auditor the results of the audit (including the management letter); and (c) oversee the adoption and implementation of, and compliance with, any Conflict of Interest Policy or Whistleblower Policy (unless performed by another committee consisting solely of independent directors).
<p>Charities Required to Register to Conduct Charitable Solicitations in New York with Annual Revenue in Excess of \$1,000,000</p>	<p>Mandatory Audit Committee or Board Audit Function (Augmented Duties)</p>	<p><u>Augmented Duties of the Audit Committee</u></p> <p>In addition to the basic duties listed above, the Audit Committee or the independent directors on the Board of a covered organization must:</p> <ul style="list-style-type: none"> (a) review with the independent auditor the scope and planning of the audit; (b) review and discuss with the independent auditor any material risks and weaknesses in internal controls identified by the auditor, any restrictions on the scope of the auditor’s activities or access to requested information, any significant disagreements between the auditor and management and the adequacy and performance of the accounting and financial reporting processes; (c) annually consider the performance and independence of the auditor; and (d) if the duties are performed by an Audit Committee, report its activities to the Board.

Covered Organizations	Topic	Summary
<p>Charities Required to Register to Conduct Charitable Solicitations in New York with Annual Revenue in Excess of \$2,000,000</p>	<p>Mandatory Compensation Committee or Board Compensation Function (Augmented Duties)</p>	<p><u>Augmented Duties of the Compensation Committee</u></p> <p>In addition to the basic duties listed above, the Compensation Committee or the independent directors on the Board of a covered organization must:</p> <p>(a) review the total compensation paid to the organization’s top five highest compensated employees who are officers or key employees and whose compensation exceeds \$150,000 or a greater amount set by the Attorney General;</p> <p>(b) determine that the total compensation paid to any such employee is fair, reasonable and commensurate with the services provided, taking into consideration, at a minimum, the factors listed below;</p> <p>(c) make and keep a contemporaneous written record describing the basis for the determination; and</p> <p>(d) approve by not less than a majority vote the total compensation paid to each such employee.</p> <p>The review and approval must occur whenever the term of employment, if any, of the employee is renewed or extended and whenever the compensation is materially changed.</p> <p><u>Factors to Consider</u></p> <p>Factors that the Compensation Committee or independent directors on the Board must consider are:</p> <p>(a) the total compensation provided to the employee by the organization and all affiliates;</p> <p>(b) relevant data on the total compensation paid to individuals serving in similar positions at organizations of similar size, type, purpose and scope;</p> <p>(c) the employee’s qualifications and performance; and</p> <p>(d) the overall financial condition of the organization.</p>

DEFINED TERMS

affiliate	An entity controlled by an organization, in control of the organization or under common control with the organization.
independent auditor	The certified public accountant performing the audit of the financial statements of the organization.
independent director	<p>A director who:</p> <p>(a) in the last three years, was not an employee of the organization or any affiliate and did not have a relative who was a key employee of the organization or any affiliate;</p> <p>(b) in each of the last three fiscal years, did not receive (and did not have a relative who received) more than \$10,000 in direct compensation from the organization or any affiliate (other than reimbursement of expenses or reasonable compensation for services as a director); and</p> <p>(c) is not a current employee of or does not have a substantial financial interest in (and does not have a relative who is a current officer of or has a substantial financial interest in) any entity that made payments to (or received payments from) the organization or any affiliate for property or services in an amount which, in each of the last three fiscal years, exceeded the lesser of \$25,000 or 2% of the entity's consolidated gross revenue.</p>
key employee	Any person who is in a position to exercise substantial influence over the affairs of the organization, as referenced in the U.S. Internal Revenue Code and regulatory provisions governing "excess benefit transactions."
related party transaction	Any transaction, agreement or other arrangement in which a related party has a financial interest and in which the organization or an affiliate is a participant.
related party	Any director, officer or key employee of an organization or an affiliate ; any relative of any such individual; and any entity in which any such individual or relative has a 35% 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 5%.
relative	A spouse, domestic partner, child, grandchild, sibling, half-sibling, ancestor, or spouse or domestic partner of a child, grandchild, sibling or half-sibling.
total compensation	Any compensation, whether paid or accrued, by or on behalf of an organization or an affiliate for services rendered to, on behalf of or at the request of the organization, including, but not limited to, salary, bonus and deferred compensation, and any benefits having monetary value provided by or on behalf of the organization or any affiliate , including, but not limited to, housing allowances, living expenses, perquisites, fringe benefits, employer contributions to defined contribution retirement plans and other retirement benefits.

Nonprofit Revitalization Act and Executive Compensation Reform Act of 2013: Highlights of Proposed Update of the Not-for-Profit Corporation Law and Proposed Expansion of the Attorney General's Enforcement Powers

The Nonprofit Revitalization Act of 2013 contains a number of provisions designed to update certain features of the current New York Not-for-Profit Corporation Law and expand the enforcement tools available to the New York Attorney General. These provisions, if enacted, would:

- Establish rules for ***conducting certain corporate activities electronically***, including:
 - Email notice and waiver of notice of member meetings;
 - Email waiver of notice of board meetings;
 - Notice of member meetings by website posting, in addition to publication in a newspaper, if a corporation has more than 500 members;
 - Email proxy voting for members and unanimous written consent via email for member, board and committee actions; and
 - Videoconferencing for board and committee meetings.
- Redefine the phrase "***entire board***" so that, if the bylaws provide for a range between a minimum and maximum number of directors, the "entire board" consists of the number of directors elected at the most recently held election of directors.
 - *This amendment would eliminate the cumbersome process requiring that members or boards "fix" the number of directors constituting the entire board and the inadvertent existence of "vacancies" or unauthorized seats simply because the number of directors was not "re-fixed" to reflect the election of a lesser or greater number of directors than the number "fixed" under or pursuant to the bylaws.*
- End the requirement for board approval for ***leasing real property from a third party***.
- Permit ***committee authorization of the purchase or disposition of real property***, unless the transaction involves all or substantially all of the corporation's assets, in which case the board's approval would be necessary.
- State that "***committees of the corporation***" (*i.e., committees that include non-directors*) ***may not "have the authority to bind the board."***

- End the requirement that private foundations publish notice of availability for **public inspection of Form 990-PF**.
- Confer **discretion on the Attorney General to grant certain approvals that now require a court proceeding**, namely, approvals of “assets” dissolutions; the change, elimination or addition of a purpose or power of a charitable corporation; and the sale, lease, exchange or other disposition of all or substantially all of a corporation’s assets.
- Simplify the categories of not-for-profit corporation into **“charitable corporations”** and **“non-charitable corporations.”**
 - *Existing types of corporations – known as Types A, B, C and D – would be assigned to one category or the other. Although there would be some nuances for Type D corporations, all existing Type B and C corporations would become charitable corporations under the legislation and all Type A corporations would become non-charitable corporations.*
- Empower the Attorney General to commence proceedings to **enjoin, void or rescind a related party transaction or proposed related party transaction**, including a compensation arrangement with an officer, director, trustee or key employee, if the transaction violates any law or is otherwise not fair, reasonable or in the best interests of the corporation.
- Grant the Attorney General specific authority to seek other relief with regard to related party transactions, such as **damages, restitution, removal and/or an accounting**, including **double damages** in cases of “willful conduct.”

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