

# New York Non-Profit Revitalization Act of 2013

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# New York Non-Profit Revitalization Act of 2013

- The Non-Profit Revitalization Act of 2013 (the “Act”) is the first comprehensive update of New York’s Not-for-Profit Corporation Law (the “N-PCL”) since it was enacted nearly fifty years ago.
- If the Act is signed into law by the Governor, most provisions of the Act will become effective on July 1, 2014.

# Legislative history

- May 2012: Attorney General Eric Schneiderman first introduced a bill to amend the N-PCL. While it did not pass in the 2011-2012 legislative session, the initial bill set the stage for the ultimate passage of the Act.
- The initial bill contained many revisions to the N-PCL that were eventually included in the Act, including:
  - The elimination of non-profit corporate types;
  - Streamlined procedures for non-profit corporate formation; and
  - Express permission to use electronic communications to conduct non-profit corporate activities.

# Legislative history

- In the 2012-2013 legislative session, the Attorney General re-introduced legislation to amend the N-PCL, this time breaking the legislation into two separate bills.
  - The first bill, the Act, addressed non-profit oversight generally. The New York Legislature, by a nearly unanimous vote, passed the Act on Friday, June 21, 2013. The Act is now awaiting the Governor's signature.
  - The second bill addressed non-profit executive compensation (the Executive Compensation Reform Act). The legislature has not yet taken action on the Executive Compensation Reform Act.

# What are the goals of the Act?

- To reduce bureaucracy and other costly obstacles to incorporation and operation in New York State.
- To strengthen accountability and enhance charitable governance.
- To strengthen the State's enforcement powers to police nonprofit organizations that misuse their charitable assets.
- To eliminate ambiguities and inconsistencies in the laws that govern nonprofit organizations.

# How does the Act simplify incorporation?

- The Act eliminates the four corporation types (A, B, C, and D) and replaces them with two categories: charitable and non-charitable corporations.
- Corporations formed under the N-PCL will need to identify as either a:
  - Charitable or
  - Non-charitable corporation
- Existing non-profit organizations will not need to file additional paperwork and will be deemed charitable or non-charitable based on their type.
- The Act eliminates the requirement that certain non-profit organizations obtain pre-approval from the NYS Education Department.

# How does the Act simplify the categorization of non-profits?

- A “charitable” corporation is one formed for “charitable purposes.”
- “Charitable purposes” are defined as “purposes contained in the certificate of incorporation of the corporation that are charitable, educational, religious, scientific, literary, cultural or for the prevention of cruelty to children or animals.”
- A “non-charitable corporation” is defined as any corporation formed under the N-PCL, “other than a charitable corporation, including but not limited to one formed for any one or more of the following non-pecuniary purposes: civic, patriotic, political, social, fraternal, athletic, agricultural, horticultural, or animal husbandry, or for the purpose of operating a professional, commercial, industrial, trade or service association.”

# How will existing non-profit organizations be reclassified?

- Charitable if:
  - Type B corporation
  - Type C corporation
  - Type D corporation formed for charitable purposes as defined in the N-PCL
- Non-charitable if:
  - Type A corporations
  - Any other Type D corporation

# How does the Act eliminate certain pre-approvals?

- Currently:
  - Non-profit corporations that had any type of educational purpose in their Certificates of Incorporation were generally required to receive the NYS Department of Education's consent in order to incorporate.
- The Act:
  - Only those organizations that operate a school, college, university or other entity providing post-secondary education, library, museum, or historical society will need approval from the NYS Education Department.
  - In the case of a college or university, the organization would obtain pre-approval from the Regents.
  - Corporations with any other type of educational purpose need only provide a certified copy of their Certificate of Incorporation to the Department of Education within 30 days of receiving confirmation the Certificate was accepted for filing.

# What other changes does the Act make to the incorporation process?

- The Act clarifies that a non-profit organization's Certificate of Incorporation need only state its corporate purpose and that it is not required to include a statement of proposed activities or how it intends to achieve its corporate purpose.
- The Act specifically authorizes the NYS Department of State to make clerical corrections to filings upon receipt of written authorization from the incorporator. This was not previously permitted.

# How does the Act modernize non-profit operation?

- The Act permits the use of email and video technology for board meetings and other procedures. The prior law was generally silent on the issue of electronic means of communication.
- The Act expressly permits non-profit organizations to transmit notices, waivers, consents, and other communications via facsimile and electronic mail.
- The Act authorizes unanimous written consents by email for board, committee, and member actions.
- The Act allows board and committee members to participate in meetings via videoconference and other electronic means as long as all participants can hear each other at the same time.
- The Act also permits notice of member meetings via website (in addition to newspaper publication for corporations of more than 500 members).

# How does the Act affect the approval process for real estate transactions?

- For real estate transactions, including purchases, sales and leases (as landlord) of real property, that would not constitute the purchase or disposition of all or substantially all of the corporation's assets:
  - The Act permits approval by a simple majority rather than a 2/3 majority; and
  - The Act permits approval at the committee level in lieu of board approval.
- Board approval requirements for leasing real property (as a tenant) appear to have been eliminated.

# How does the Act affect other corporate transactions?

- For corporate transactions that previously required court approval, the Act would permit non-profit organizations to seek only Attorney General approval instead of court approval.
- This includes sales of all or substantially all of a non-profit's assets, mergers, changes in corporate purpose, and asset dissolutions.

# What are the changes to financial reporting requirements?

- Currently, there are three annual gross revenue brackets which dictate the level of financial reporting required of organizations that register with the NYS Attorney General's Charities Bureau.
- The Act:
  - Incrementally raises the annual gross revenue threshold for the required financial reports over the next decade.
  - Reduces the financial reporting burdens on small organizations.

# What financial reporting changes take effect July 1, 2014?

- **Highest Bracket:**
  - Organizations with annual gross revenue in excess of \$500,000 must file annual audited financial statements.
- **Middle Bracket:**
  - Organizations with annual gross revenue of at least \$250,000 but not more than \$500,000 must file an annual financial statement, including a CPA's review report.
- **Lowest Bracket:**
  - Organizations with annual gross revenue of less than \$250,000 are only required to file unaudited financial reports.

# What financial reporting changes take effect July 1, 2017?

- **Highest Bracket:**
  - Organizations with annual gross revenue in excess of \$750,000 must file annual audited financial statements.
- **Middle Bracket:**
  - Organizations with annual gross revenue of at least \$250,000 but not more than \$750,000 must file an annual financial statement, including a CPA's review report.
- **Lowest Bracket:**
  - No further changes. Organizations with annual gross revenue of less than \$250,000 are still only required to file unaudited financial reports.

# What financial reporting changes take effect July 1, 2021?

- Highest Bracket:
  - Organizations with annual gross revenue in excess of \$1,000,000 must file annual audited financial statements.
- Middle Bracket:
  - Organizations with annual gross revenue of at least \$250,000 but not more than \$1,000,000 must file an annual financial statement, including a CPA's review report.
- Lowest Bracket:
  - No further changes. Organizations with annual gross revenue of less than \$250,000 are still only required to file unaudited financial reports.

# What are the new audit committee requirements?

- The Act requires non-profits that (i) are required to register to solicit contributions in New York and (ii) have annual gross revenue in excess of \$500,000 to:
  - Have the board or an audit committee composed solely of independent directors perform the following duties:
    - Oversee the accounting and financial reporting processes;
    - Oversee the audit of the non-profit's financial statements;
    - Annually retain or renew the retention of an independent auditor to conduct the audit; and
    - Review the results of the audit and any related management letter with the independent auditor.

# What are the new audit committee requirements?

- In addition, for non-profits that (i) are required to register to solicit contributions in New York and (ii) have annual gross revenue in excess of \$1,000,000, the board or an audit committee composed solely of independent directors must perform the additional duties below:
  - Review with the independent auditor the scope and planning of the audit prior to the audit;
  - Upon completion of the audit, review and discuss with the independent auditor:
    - Any identified material risks and weaknesses in internal controls;
    - 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 of the non-profit's accounting and financial reporting;
  - Annually consider the performance and independence of the independent auditor; and
  - If these duties are performed by an Audit Committee, then they must report on their activities to the board.

# What is an independent director?

- A director who:
  - is not, and has not been within the last three years, an employee of the corporation or an affiliate of the corporation, and does not have a relative who is, or has been within the last 3 years, a key employee of the corporation or an affiliate of the corporation;
  - has not received, and does not have a relative who has received, in any of the last 3 fiscal years, more than \$10,000 in direct compensation from the corporation or an affiliate of the corporation (other than reimbursement for expenses reasonably incurred as a director or reasonable compensation or service as a director as permitted by law); and
  - 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 has made payments to, or received payments from, the corporation or an affiliate of the corporation for property or services in an amount which, in any of the last 3 fiscal years, exceeds the lesser of \$25,000 or 2% of such entity consolidated gross revenues. “Payment” does not include charitable contributions.

# What are the changes to related party transactions?

- Current state law provides limited guidelines and safe harbors to transactions between non-profit organizations and interested parties.
- The Act requires boards to actively assess and approve transactions between the organization and any “related party.”
- These new provisions of the N-PCL are in addition to the current federal requirements and IRS Form 990 disclosures.

# New definitions applicable to related party transactions

- A “related party” is:
  - Any director, officer, or key employee of the corporation or any affiliate of the corporation;
  - Any relative of any director, officer, or key employee of the corporation or any affiliate of the corporation; or
  - Any entity in which any individual described above 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 five percent.
- A “related party transaction” is any transaction, agreement, or any other arrangement in which a related party has a financial interest and in which the corporation or any affiliate of the corporation is a participant.

# What new requirements apply to related party transactions?

- The Act requires the director, officer, or key employee who has an interest in a related party transaction to disclose the material facts concerning his or her interest.
- If the board determines that the transaction is (1) fair, (2) reasonable, and (3) in the best interests of the organization, then the non-profit may enter into a related party transaction.
- In addition, if the non-profit is a charitable corporation, the Act requires the board to (1) consider alternative available transactions, (2) approve the transaction by no less than a majority vote, and (3) contemporaneously document their approval on the basis of finding the transaction fair, reasonable, and in the best interests of the organization.
- The Act explicitly grants the Attorney General standing to enforce an action to enjoin, void, or rescind any actual or proposed “related party transaction” that violates any of the above provisions.

# What are the changes to oversight and accountability?

- The IRS encourages non-profit organizations to adopt conflicts of interest and whistleblower policies by requiring disclosure of such policies (or lack thereof) on the IRS Form 990.
- Currently, New York State law does not address conflicts of interest policies or whistleblower policies.

# What are the changes to oversight and accountability?

- The Act requires all organizations to adopt a **conflict of interest policy**.
- The Act requires organizations with (1) twenty or more employees and (2) an annual revenue in excess of \$1,000,000 in the prior fiscal year to adopt a **whistleblower policy**.

# How do organizations meet the Conflict of Interest policy requirement?

- The Act requires organizations to adopt a Conflict of Interest policy that includes a minimum of six provisions prescribed by the Act.
- The policy is meant to govern related parties and related party transactions.
- If a non-profit has previously adopted and possesses a conflict of interest policy pursuant to federal, state, or local laws that is substantially consistent with the Act's requirements, then it will be deemed in compliance.

# What are the six requirements for a Conflict of Interest policy?

- The policy must include:
  - A definition of the circumstances that constitute a conflict of interest;
  - Procedures for disclosing a conflict of interest;
  - A requirement that the conflicted person not be present at or participate in deliberations or a vote on the matter;
  - A prohibition of any attempt by the conflicted person to influence improperly the deliberations or vote on the matter;
  - A requirement that the existences and resolution of the conflict be documented in organization records; and
  - Procedures for disclosing, addressing, and documenting related party transactions.

# How do organizations meet the Whistleblower policy requirement?

- The policy must provide that no related party who in good faith reports any suspected improper conduct, including fraud, illegal conduct, or violations of the non-profit's policies shall suffer intimidation, harassment, discrimination, other retaliation, or adverse employment consequences.
- In addition, the policy must (1) provide procedures for reporting actions or suspected actions, (2) name a designated employee, officer, or director to administer the policy, and (3) be distributed to anyone who provides substantial services to the organization.
- If a non-profit has adopted and possesses a whistleblower policy pursuant to federal, state, or local laws that is substantially consistent with the Act's requirements, then it will be deemed in compliance.