



**May 29, 2015**

**Charities Bureau Guidance: *Conflict of Interest Policies Under the Nonprofit 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. The Act was signed into law on December 18, 2013, and most of the provisions of the Act became effective on July 1, 2014.

The New York Attorney General Charities Bureau has issued a number of "Guidance Documents" to assist non-profit organizations in implementing the Act's requirements. While not formal regulatory guidance, these Guidance Documents can provide valuable insight to the Attorney General's interpretation of the Act's requirements.

The Act requires New York not-for-profit corporations to have a Conflict of Interest Policy that complies with the requirements of the Act. The Act also imposes specific requirements on "related party transactions". (For more information on the Act generally, see [here](#).)

On April 13, 2015, the New York Attorney General's Charities Bureau issued Guidance Document 2015-4, V.1.0, *Conflict of Interest Policies Under the Nonprofit Revitalization Act of 2013*. Below is a summary of this Guidance Document:

- Where a director, officer, or key employee has a conflict of interest in an issue coming before the board, the entity has an obligation to make a record of the existence of the conflict and how it was addressed, both with respect to that individual and with respect to the transaction.
- If a director, officer, or key employee has a conflict of interest concerning an issue coming before that director, officer, or key employee, that individual must disclose the circumstances giving rise to the conflict of interest to the person or entity designated by the organization's conflict of interest policy.
- The Guidance defines a "key employee" as follows:
  - Is a current employee who is in a position to exercise substantial influence over the affairs of the corporation;
  - Includes the president, chief executive officer, chief operating officer, treasurer, chief financial officer, and any other person who has ultimate responsibility for implementing the decisions of the governing body, supervising the management, administration, or operation of the organization, or managing the finances of the organization;
  - May also be a key employee, as required to be named in IRS form 990, (a) if his or her compensation is primarily based on revenues derived

from activities of the organization, or of a particular department or function of the organization, that the person controls; (b) if the person has or shares authority to control or determine a substantial portion of the organization's capital expenditures, operating budget, or compensation for employees; or (c) if the person manages a discrete segment or activity of the organization that represents a substantial portion of the activities, assets, income, or expenses of the organization.

- The Guidance indicates that the board has discretion to define the procedures that should be followed for different types of conflicts, including the power to define additional restrictions on transactions between a board member and the corporation, or between the nonprofit's employees and third parties (e.g., no gifts policy).
- City-related nonprofits may define "circumstances that constitute a conflict of interest" to exclude the responsibility of an *ex-officio* director to the electorate or the city appointing official, particularly where such *ex-officio* role is specifically set forth in the nonprofit's enabling legislation, charter or certificate of incorporation. The Guidance acknowledges that the role and definition of the *ex-officio* includes the responsibility of advocating a broader public interest in board discussions, and that role is clear to all non-city directors.
- Organizations may establish procedures for disclosing a conflict of interest to the Audit Committee or the board, including expectations for each class of conflict reporters, forms, record-keeping, custodians; disclosure to other persons within the nonprofit or to third parties, timing, and committee review and action.
- The Guidance recommends that that the board adopt a comprehensive policy that articulates standards of conduct for board members, officers and key employees regarding conflicts of interest, disclosure requirements, reporting requirements, and procedures for mitigation.
- In the case of conflicts that come before the board or a committee, the board may request that the person with the conflict of interest present information as background or answer questions at a committee or board meeting prior to the commencement of deliberations or voting.
- The Act prohibits any attempt by the person with the conflict to improperly influence the deliberations or voting on the matter giving rise to such conflict. The Guidance states that "improperly influence" in this context should have a meaning similar to that used by the Securities and Exchange Commission in addressing improperly influencing audits: coercing, manipulating, misleading, or fraudulently influencing (collectively referred to herein as "improperly influencing") the decision-making when the officer, director or other person knew or should have known that the action, if successful, could result in the outcome which the officer or director could not deliberate or vote on directly.
- Related party transactions include any transaction, agreement, or other arrangement in which a related party has a direct or indirect financial interest and in which the nonprofit or an affiliate participates. The Guidance indicates

that:

- A person has an indirect financial interest in an entity if a relative (as defined in the N-PCL) has an ownership interest in that entity or if the person has ownership in an entity that has ownership in a partnership or professional corporation. This is consistent with the definition of "indirect ownership interest" that is found in the instructions to Form 990, Schedule L.
- A director, officer, or key employee must disclose his or her interest in a transaction, agreement or arrangement *before* the board enters into that related party transaction.
- The Act's record-keeping requirements may not apply to (a) de minimis transactions, (b) transactions or activities that are undertaken in the ordinary course of business by staff of the organization, (c) benefits provided to a related party solely as a member of a class that the corporation intends to benefit as part of the accomplishment of its mission, and (d) transactions related to compensation of employees or directors or reimbursement of reasonable expenses incurred by a related party on behalf of the corporation. Nonetheless, the board member or other related party may not intervene or seek to influence the decision-maker or reviewer in these transactions. The decision-maker, and those responsible for reviewing or influencing these transactions, should not consider or be affected by a related party's involvement in decisions on matters that may affect the decision-maker or those who review or influence the decision.
  - The Guidance indicates that the board of directors has the discretion to define the circumstances that constitute a conflict of interest, including the discretion to define exceptions for de minimis transactions and ordinary course of business transactions not covered by the policy.
  - What constitutes a "de minimis" transaction will depend on the size of the corporation's budget and assets and the size of the transaction.
  - A transaction or activity is in the ordinary course of business if it is consistent either with the corporation's consistently applied past practices in similar transactions or with common practices in the sector in which the corporation operates. For example, the library of a nonprofit university buys a book written by a member of the board, pursuant to a written library acquisitions policy. The Guidance also provides a number of other examples.
  - To qualify for the exception for benefits provided to a related party solely as a member of a class that the corporation intends to benefit as part of the accomplishment of its mission, the benefits must be provided in good faith and without unjustified favoritism towards the related party.
- Transactions related to compensation of employees, officers or directors or reimbursement of reasonable expenses incurred by a related party on behalf of the corporation are not considered related party transactions, unless that individual is otherwise a related party based on some other status, such as

being a relative of another related party.

- However, such transactions must be reasonable and commensurate with services performed, and the person who may benefit may not participate in any board or committee deliberation or vote concerning the compensation (although he or she may be present before deliberations at the request of the board in order to provide information).
- The Policy must require that each director submit to the Secretary prior to initial election to the board, and annually thereafter, a written statement identifying, to the best of the director's knowledge, any entity of which the director is an officer, director, trustee, member, owner, or employee and with which the corporation has a relationship, and any transaction in which the corporation is a participant and in which the director might have a conflicting interest. Likewise, the Guidance indicates that officers and key employees must submit an annual conflicts statement to the Secretary.
  - When initial election to the board is not reasonably foreseeable, for example when board candidates are nominated from the floor at an annual meeting of members held to elect directors, the written statement may be provided to the Secretary promptly after the initial election.
  - Disclosure of conflicts is required; the requirement of disclosure to the Secretary can be satisfied by disclosure to the Secretary's designee as custodian (e.g., the compliance officer), if set forth in the conflict of interest policy.
  - All types of nonprofits are covered.
  - The Secretary must provide a copy of the completed statements to the Chair of the Audit Committee or Board Chair or direct his/her designee/custodian to provide a copy of the completed statements to the Chair of the Audit Committee or Board Chair.

*Note that in some instances the Guidance Documents contradict or provide more lenient standards than the Act, and in other instances they provide more restrictive standards than the Act.*

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