RECENT AMENDMENTS TO THE NEW YORK NONPROFIT REVITALIZATION ACT OF 2013

Tax-Exempt Organizations Alert
December 15, 2015

Attorneys

Catherine Eberl
Kenneth Friedman
Adam Perry
Patricia Sandison
Valerie Stevens
William Turkovich
James Wadsworth
Marla Waiss

Practices & Industries

Tax-Exempt Organizations

Existing Revitalization Act

On July 1, 2014, the New York Nonprofit Revitalization Act of 2013 (the Revitalization Act) came into effect and brought about major changes for all New York nonprofit corporations, including education corporations and religious corporations, as well as New York charitable trusts. As a result, we have assisted our nonprofit clients with updating their by-laws; adopting new conflict of interest and, in some cases, whistleblower policies; analyzing which directors meet the "independent director" definition; implementing applicable audit oversight obligations; and taking other steps required by the Revitalization Act. If your New York nonprofit organization has not yet become compliant with the Revitalization Act, please contact us to discuss the necessary steps.

Further Amendments to the Revitalization Act

On December 11, 2015, New York State Governor Andrew Cuomo signed Bill S5868A into law, which amended the Revitalization Act to modify certain key definitions and further clarify certain other provisions of the Act (the "December Amendments"). In addition, previously, on October 26, 2015, the governor executed Bill A7641, which delayed until January 1, 2017 the effective date of the provisions of the Revitalization Act related to the prohibition of employees of a nonprofit corporation from serving as chair of the board (the "October Amendment"). Despite these recent amendments, several important proposals intended to ease the burden on nonprofit organizations were not included in the legislation. If and until these are formally addressed, New York nonprofits are left, in part, to rely upon non-binding guidance from the Office of the Attorney General's Charities Bureau in their attempts to comply with the law.

The December Amendments

The latest amendments, effective as of December 11, 2015, make a number of substantive changes to certain key definitions and other provisions of the Revitalization Act, including the following:

1. Change in the definition of "independent director." The definition of "independent director" has been expanded so that a director who is (or was during the past three years) employed by, has an ownership interest in, and/or is a director

or officer of, the nonprofit's audit firm will no longer qualify as an independent director. In addition, a director will no longer qualify as an independent director if he or she has any relatives who meet the aforementioned description. Specifically, the definition of "independent director" is modified as follows, with the ***[italicized]*** language to be deleted and the underlined language to be added:

Independent director means a director who: (i) is not, and has not been within the last three years, an employee of the corporation or an affiliate, and does not have a relative who is, or has been within the last three years, a key employee of the corporation or an affiliate; (ii) has not received, and does not have a relative who has received, in any of the last three fiscal years, more than $10,000 in direct compensation from the corporation or an affiliate (other than reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director); ***[and]*** (iii) 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 for property or services in an amount which, in any of the last three fiscal years, exceeds the lesser of $25,000 or 2% of such entity's consolidated gross revenues; or (iv) is not and does not have a relative who is a current owner, whether wholly or partially, director, officer or employee of the corporation's outside auditor or who has worked on the corporation's audit at any time during the past three years. For purposes of this ***[subparagraph]*** subdivision, "payment" does not include charitable contributions, dues or fees paid to the corporation for services which the corporation performs as part of its nonprofit purposes, provided that such services are available to individual members of the public on the same terms."

While the new fourth prong of the definition will further complicate the task of finding independent directors and making sure that existing independent directors remain qualified, the new language about dues or fees will provide some relief.

2. Change in the definition of "affiliate." The definition of "affiliate" will now include only entities controlled by, or in control of, the nonprofit. Entities under common control with the nonprofit will no longer be included in the definition of "affiliate". This may prove to be a beneficial change for most nonprofits, particularly complex organizations such as hospital and university systems, as well as corporate foundations, because, by excluding certain entities "under common control," fewer transactions will be deemed to be related party transactions that require certain procedures to be followed, and fewer directors will be disqualified under the definition of "independent director."

3. Change in the definition of "entire board." The definition of "entire board" has been further expounded upon to clarify that currently a New York nonprofit can establish what constitutes the "entire board" by setting a range in the by-laws and by setting a specific number of directors within such range by majority vote of the entire board. If, however, the by-laws of the nonprofit provide that the board consists of a range between a minimum and maximum number of directors, and the number within that range has not been set by a majority vote of the entire board, then the default definition of "entire board" will consist of the number of directors within such range that were elected or appointed as of the most recently held election of directors, as well as any directors whose terms have not yet expired.

4. Change in the definition of "relative." The definition of "relative" has been expanded to include the domestic partner of a sibling, child, grandchild, or great grandchild of an individual. This change impacts who meets the criteria as an independent director and which transactions come under the "related party transaction" rules when assessing the

relationships of a nonprofit's or its affiliates' directors, officers, or key employees.

5. Change in the definition of "related party." The definition of "related party" has been expanded to include not only directors, officers, and key employees of the nonprofit corporation and its affiliates but also "any other person who exercises the powers of directors, officers, or key employees over the affairs of the corporation or any affiliate of the corporation."

6. Change in the definition of "key employee." The definition of "key employee," which refers to certain IRS regulations and succeeding provisions, is modified to include the qualification "to the extent such provisions are applicable." This change fell short of a recommended amendment that would have narrowed and clarified the definition of key employee, a definition that matters when determining who is an independent director, what transactions fall under the related party transaction rules, and who may be sued for violating the Not-for-Profit Corporation Law.

7. Clarification regarding board compensation approval. A new sentence has been added to §515(b) of the Not-for-Profit Corporation Law to clarify that no director will be prohibited from deliberating or voting concerning compensation for a service on the board that is to be made available or provided to all directors of the nonprofit on the same or substantially similar terms.

8. To whom a director should give the annual and pre- initial election conflict of interest disclosure statement. The Revitalization Act dictated that directors must give their annual and pre-initial election conflict of interest disclosure statement to the secretary of the nonprofit. The law now permits directors to give their conflict of interest disclosure statements to either the secretary or a designated compliance officer.

9. How to disseminate the whistleblower policy. The Revitalization Act mandates that entities with 20 or more employees and annual gross revenues of $1 million or more adopt a whistleblower policy that follows the criteria set forth in the Revitalization Act. It further provides that a copy of the policy must be given to all directors, officers, employees, and those volunteers who provide substantial services to the corporation. A new sentence has been added that allows a nonprofit to disseminate its whistleblower policy by posting it on the nonprofit's website or at the nonprofit's offices (at a conspicuous location accessible by employees and volunteers) and clarifies that these are among the methods a nonprofit may use to satisfy the distribution requirement.

10. Religious corporation's sale, mortgage, or lease. The amendments will make it possible for a religious corporation to seek either court approval or attorney general consent in order to sell, mortgage, or lease its real property for a term exceeding five years.

The October Amendment: Delayed Effective Date of the No-Employee-As-Chair Rule

The effective date has been delayed until January 1, 2017, for the Revitalization Act's provision that prohibits an employee of a nonprofit from serving as chair of the board or holding any other title with similar responsibilities (such as president, for those organizations that do not have a chair). The effective date was changed from January 1, 2016, to January 1, 2017. For many nonprofits, the no-employee-as-chair prohibition presents no concerns, but some religious corporations have denominational rules that require the pastor (an employee) to serve as chair or president. To address this limited context, it

remains to be seen whether the Legislature will make further changes to the rule. It is also possible that the rule will go into effect in 2017 and be challenged in the courts.

Need Assistance?

Each New York nonprofit should revisit its by-laws, conflict of interest policy, and other charter documents to see if amendments are warranted to bring the documents up to speed with the Revitalization Act amendments. This process will generally be easier than the lengthier changes necessitated last year when the Revitalization Act first took effect. As a result of the amended definitions outlined above, nonprofits should also revisit which persons qualify as independent directors.

We are happy to provide assistance with all aspects of the Revitalization Act and amendments.

For more information, please contact:

Anne F. Downey
716.848.1683
adowney@hodgsonruss.com

Patricia C. Sandison
716.848.1619
psandison@hodgsonruss.com

For charitable trust questions:
Catherine B. Eberl
716.848.1237
ceberl@hodgsonruss.com