

# GUIDE TO **NONPROFIT** **GOVERNANCE** 2026

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## Not-For-Profit Practice Group

### Introduction: Not-For-Profit Governance and “Best Practices”

Not-for-profit organizations play a significant role in our society by undertaking and providing funding for projects that benefit the greater good. They provide services and grants in a wide variety of areas that are of importance to the community, including supporting hospitals, educational institutions, museums and organizations dedicated to assisting those in need. A not-for-profit organization generally may not, however, be formed for financial gain, and generally cannot provide profits or excessive benefits for its insiders, donors or others outside of the charitable class for which the not-for-profit organization is formed and intended to serve. The mission of a not-for-profit organization sets forth the purpose for which the organization was formed and granted special legal not-for-profit status. This mission drives the activities carried out by the organization; the board of directors is responsible for governing the not-for-profit to carry out this mission. The assets of a not-for-profit organization are intended to benefit the public good and are restricted by law toward that use alone. Thus, given the prohibition against use of not-for-profit assets for anything other than the intended charitable objective, the founders, members, directors, officers and managers of a not-for-profit will have less control over a not-for-profit corporation than if they established a for-profit corporation and had conventional rights of equity owners or for-profit directors or management.

Not-for-profit organizations today are operating in an increasingly complex environment characterized by heightened legal and political scrutiny, and rapid technological changes including AI. Effective governance, with its corollaries, transparency and accountability, leads to increased public trust in the organization and a greater willingness by the public to donate funds and services. Effective governance also provides protection from regulatory intrusion.

This outline (i) summarizes steps a not-for-profit organization may wish to consider taking to ensure that it is accountable, transparent and effectively governed by an active and engaged board, and (ii) serves as an introduction to the other documents included in this volume.

Boards of for-profit organizations have worked to restore public confidence and increase investment in the wake of a number of highly public governance failures. Governance frameworks shaped by the Sarbanes-Oxley Act of 2002 (“Sarbanes-Oxley”), the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, and related rules and regulations, and for New York not-for-profit organizations, the Non-Profit Revitalization Act of 2013 have led to increased board engagement. Not-for-profit corporations incorporated under New York law (and, potentially, to a more limited extent, not-for-profit corporations incorporated in other states) are also subject to the governance and oversight rules set forth in the New York Not-for-Profit Corporation Law (the “N-PCL”). Boards of not-for-profit organizations may wish to adapt certain measures that have become “best practices,” even where to do so may not be required by law.

A summary of statutory and case law applicable to not-for-profit organizations in the State of New York, as well as liabilities imposed by the Internal Revenue Service (the “IRS”), are set forth at *Tab 4*.

## I. ROLE OF THE BOARD AND FIDUCIARY DUTIES – AN OVERVIEW

The role of the board of directors of a not-for-profit organization is similar to the role of a for-profit board. In both cases, the organizations are tasked with providing oversight of the organization – essentially, managing other people’s money to accomplish certain goals – and in both cases they are judged by their success in doing so. Yet, there is a very key difference: in the for-profit context, shareholders are able to bring derivative claims to hold corporate directors and officers accountable, whereas in the not-for-profit context there is no private right of action by which the organization can be held accountable when it fails to act in furtherance of its purpose. Although

governmental entities (such as the relevant State Attorney General and the IRS) play an important role in policing and monitoring not-for-profit activities, there is no private right of action available against officers and directors to ensure accountability. Moreover, many not-for-profit boards are responsible for electing directors, compared to elections of directors to for-profit company boards by shareholders. The not-for-profit board is required to ensure that the organization acts in furtherance of its purpose and mission through meaningful oversight of operations and policy guidance in a way that assures integrity and effective management but without requiring board involvement in the organization's day-to-day activities.

The basic duties of directors of not-for-profit and for-profit organizations are virtually the same, even though the organizations are typically governed by different laws and have different constituent relationships. Directors of not-for-profit organizations are required to discharge their duties in accordance with the following basic fiduciary duties, which are discussed in more detail at **Tab 3**:

- **Duty of care:** Act with the care an ordinarily prudent person in a like position would exercise under similar circumstances;
- **Duty of loyalty:** Act in good faith in a manner the director reasonably believes to be in the best interests of the organization; and
- **Duty of obedience:** Act in furtherance of the organization's purpose and ensure that the mission is pursued.

Breaches of fiduciary duty in the not-for-profit context are enforced by the State Attorney General. Enforcement actions can result in significant personal liability for directors, which can be eliminated by exculpation provisions to the extent applicable and minimized through indemnification and/or directors' and officers' insurance. For a discussion of indemnification and insurance, and examples of enforcement actions, see **Tab 3** and **Tab 7**.

## II. BASIC FUNCTIONS OF A NOT-FOR-PROFIT BOARD

The board of a not-for-profit organization is responsible for directing the affairs of the organization in accordance with its purpose and mission. In practice, the board delegates responsibility for managing the day-to-day activities of the organization to managers or staff; however, fiduciary duties cannot be delegated and, therefore, the board retains oversight responsibility for matters that have been delegated. Board service should not be viewed as just an honor – the oversight responsibilities of directors are real, and failure to discharge these legal duties can have unwelcome consequences for the organization and its board members.

The primary functions of the not-for-profit board typically include the following:

- Identifying, reviewing and updating as necessary, the purpose and mission of the organization in accordance with applicable law;
- Selecting, monitoring, evaluating, compensating and – if necessary – replacing the Executive Director/Chief Executive Officer (the “CEO”), and developing and approving succession plans with respect to senior executives of the organization;
- Defining and reevaluating from time-to-time the long-term strategy by which the organization fulfills its purpose and mission, and monitoring the performance of the organization in implementing the strategy;
- Reviewing and approving material capital allocations and expenditures and major transactions;

- Approving budgets, financial plans and financial statements; monitoring and ensuring the integrity of the organization’s financial reporting processes, internal control systems and audit; hiring the independent auditor (if any) and assuring itself of the auditor’s independence;
- Balancing constituency interests in a manner that is consistent with the purpose;
- Understanding the organization’s risk profile and reviewing and overseeing the organization’s management of risks, including financial, operational, technological, cyber and data security, legal and regulatory risks;
- Ensuring compliance with all applicable laws, regulations, policies and ethical standards of the organization (including laws and regulations enforced by the IRS, as well as the organization’s conflict of interest/related party transaction and other policies);
- Assisting in obtaining resources through making personally meaningful financial contributions, fundraising and/or grant-writing; comply with prudent management of funds rules and donor-imposed restrictions; and
- Establishing the composition of the board and its committees and determining governance practices.

The demands of not-for-profit board service can be heavy – board responsibilities are wide-ranging and board service is part-time (and usually voluntary). The board of a not-for-profit organization should consider implementing board processes and structures that can assist directors to more efficiently and effectively fulfill these responsibilities; however, in doing so, the board should bear in mind that board practices should address the unique needs and circumstances of the particular not-for-profit organization – one size does not fit all.

In addition to implementing any governance mechanisms that may be mandated by law, the board should look for governance “best practices” that embody pragmatic solutions that will work given the particular needs and circumstances of the organization, including organizational structure, size, activities, life-cycle stage and funding mechanisms. The goal of “best practice” is to promote active oversight and objective and informed judgment by the board. An effective board provides oversight over the activities of the managers and staff to whom the board has delegated authority. This is necessary to promote the accountable functioning of the organization, including the responsible use of assets that have been entrusted to the organization by others. Board effectiveness can be enhanced by considering the following guiding principles that are common to effective not-for-profit boards.

### **III. COMMON GUIDING PRINCIPLES FOR EFFECTIVE BOARDS**

#### **3.1 Purpose and Mission**

Board accountability begins with the charitable, educational or social purpose and mission of the not-for-profit organization. The purpose and mission are the reason why the organization exists and has been granted legal status as a not-for-profit by the State and/or tax-exempt status by the IRS. The purpose and mission should be the not-for-profit organization’s “polestar” in that they provide a measure of success and guide the organization’s conduct. (This can be compared to the for-profit world “polestar” of the best interests of the corporation and its shareholders, generally through the maximization of value through the efficient production of goods and services.)

The board is charged with ensuring that managers further the purpose and mission, without wasting assets or engaging in self-dealing. Therefore, as a starting point, the board needs to:

- Understand the entity’s purpose and mission, as stated in its certificate of incorporation and tax-exemption application;

- Develop, with management, a strategy for carrying out that purpose and mission; and
- Monitor and assess management’s efforts to carry out that strategy in line with the purpose and mission.

### 3.2 Clear Delineation of Responsibility and Authority

All directors need to understand the role of the board as an entity, as well as their individual duties as fiduciaries and the distinct role of management. The role of the board is one of oversight – directors “direct” – while the role of management is to carry out the day-to-day activities of the organization – managers “manage.” Often members of a not-for-profit board cross the line between oversight and management by becoming overly engaged in the operating activities of the entity, such as the day-to-day work required to fulfill programmatic goals. Board involvement in operating activities can lead to tensions between the board and management/staff. Boards should consider the extent to which their involvement in operating – as opposed to strategic – activities benefits or hinders the ability of management and the organization to perform.

The board may wish to consider defining the respective roles of the board and management with respect to strategic and operational activities in a formal “delegation of authority” that addresses the specific matters the CEO can approve without board approval (for example, items already included in the board-approved budget and items below a particular monetary threshold) and those that require board or board committee approval. For example, the board typically delegates the execution of certain policies and strategic objectives to management. Creating a formal delegation of authority can also help the board identify and communicate expectations about what issues are worthy of board consideration and in what time frame decisions are expected to be made.

### 3.3 Monitoring and Measuring Performance

Active board oversight requires that management performance be evaluated against the specific operational goals that the board has determined will further the agreed strategy in line with the organization’s purpose and mission. The board should then define with management the specific benchmarks (both long-term and short-term) that would indicate successful performance and monitor results achieved by management against those benchmarks. If performance goals are not being met, the board should consider where adjustment may be necessary. For example, improving performance may call for adjusting the strategy and replacing management where necessary. Management changes are inevitable, and the board should ensure that a succession plan for key executives is in place.

The board should utilize its evaluation of management performance in designing and implementing an executive compensation scheme that will compensate executives fairly and includes appropriate incentives for performance. Although not typical, in some cases it may be appropriate to compensate directors for their service on the board of a not-for-profit organization (in addition to reimbursing their reasonable expenses). Not-for-profit organizations that are required to file Forms 990 with the IRS are required to make various disclosures with respect to the process for determining, and the amount of, compensation of executive officers, key employees, directors and trustees – see *Tab 8* and *Tab 9*.

### 3.4 “Following the Money”

Overseeing the finances of the not-for-profit organization is a critical part of the board’s role. Fulfilling this oversight responsibility begins with ensuring that the organization has an effective Chief Financial Officer (“CFO”) or equivalent (such as a bookkeeper or outside accounting firm). Recruiting such a person can be challenging, particularly as not-for-profit salaries are generally lower than those in the for-profit sector. The board should establish open lines of communication with the CFO to facilitate the exchange of information. The board should work with the CFO in developing and approving budgets and financial plans, and should test management assumptions that may be embedded within budgetary analysis. The

board is also responsible for monitoring and ensuring the integrity of the organization’s financial reporting processes (including recordkeeping), internal control systems and audit, and should hire an independent auditor if required by law or as appropriate. For New York not-for-profits, the N-PCL requires entities with gross revenues exceeding certain thresholds to have an audit or review completed by an independent certified public accountant – see **Tab 4**. In addition, the New York Prudent Management of Institutional Funds Act (the “NYPMIFA”) included in the N-PCL requires New York not-for-profits to establish an investment policy to govern the investment and management of the organization’s financial assets, a sample of which can be found in **Tab 22**.

### 3.5 Determining Board Focus and Information Needs

The board’s ability to govern effectively largely depends on how it focuses its time and attention and the information it has available to it. The board should take charge of its own agenda by identifying, articulating, prioritizing and scheduling the issues that the board will address. Usually, board attention – and therefore the board’s agenda – is best focused on “following the money,” setting strategic direction and long-term goals, monitoring management’s progress and results to achieve those goals and ensuring satisfactory compliance with ethical standards, organizational policies and the law.

Board meetings should be structured to make the best use of board time. Meetings should be scheduled well in advance – for example, via an annualized schedule to address foreseeable issues – with additional meetings called when board review with respect to other issues is required. Board meetings should balance management presentations with discussion among directors (including in executive session) and with management. Appropriate reports and analyses furnished in advance facilitate robust discussion at the meeting.

An effective board requires accurate, relevant and timely information relating to the organization and the context in which it operates. The board should identify what information it needs and work with management and advisors to ensure that it obtains such information. Information should be distributed in advance of meetings to enable directors to review the material and reflect on it.

In addition, the board of a not-for-profit organization might find it helpful to adopt governance guidelines it applies in fulfilling its responsibilities, including board functions and processes, as well as the organization’s expectations of directors. Such guidelines should be specific and tailored to the needs and circumstances of the particular not-for-profit organization. Various factors unique to each not-for-profit organization, including, without limitation, organizational structure, activities, life-cycle stage, funding mechanisms and applicable legal requirements, may affect the provisions that should be addressed. The board sets the tone by adopting a governing style that emphasizes: adherence to codes and principles of conduct and ethics; strategic leadership rather than a focus on administrative detail; prospective focus on achieving purpose and mission based on current and anticipated facts; anticipation and preparedness rather than reactivity; collegiality, with respect for diverse viewpoints, and not divisiveness; and consensus building, as opposed to “majority rule.”

### 3.6 Board Size and Composition

Size and composition influence the ability of a board to be effective. Most decision-making groups function best with between seven and ten members. Not-for-profit boards are often much larger, due to their fundraising nature. If downsizing is not practical, a very large board (e.g., of 20 or more members) may wish to consider whether there are ways to facilitate efficient decision-making through the use of committees; for example by creating an executive committee or advisory board that has authority to make decisions on behalf of the board where appropriate (with some exceptions as set forth in the N-PCL). Note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose the composition and scope of an executive committee or similar committee with broad authority to act on behalf of the board – see **Tab 8**.

Board candidates should be selected with a set of criteria in mind that are specific to the needs of the particular not-for-profit organization. The board (through a nominating committee, if there is one) should periodically engage in a review of the composition of the board as a whole, including the balance of independence, business specialization, technical skills, fundraising ability and/or willingness to make personally meaningful gifts, geographic representation and other desired qualities that directors bring to the board (such as integrity and sound judgment) – bearing in mind that a board is more than the sum of its parts and that the right mix of competencies will change as the organization evolves and its circumstances change – and refresh the board where necessary.

It has been observed that board member disengagement harms the organization in a number of ways, and that selection and identification of potential board members should involve a process of looking past a short-term ability to secure funds and should look to the long-term positive or negative impact on the organization that the particular candidate will have. The board should be comprised of directors who are committed to the organization’s purpose and mission. Directors should ensure that they are interested in and understand the activities of the organization, the environment in which it exists and the challenges and risks it faces. They should learn about the structure of the organization by reviewing its governing documents, policies and minutes of board and committee meetings from the past year, as well as any literature produced as part of the organization’s programs. Directors should seek out information from management where required to gain this understanding.

### 3.7 Board Independence

The board should be comprised and organized in a manner that encourages directors to be engaged and to form and express objective judgments about certain issues, such as:

- Evaluation of management performance, compensation and succession planning;
- Approving the organization’s financial objectives and major plans, strategies and actions;
- Oversight of audit, accounting, financial reporting and risk management;
- Review and approval of conflicts of interest and related party transactions; and
- Determination of board composition and governance processes.

The board should include a number of persons who lack material business relationships to the entity and also lack material business and family relationships to senior management and key constituents (including to other directors). The N-PCL requires the board or an audit committee comprised solely of “independent directors” (as defined in the N-PCL) to oversee the accounting and financial reporting process and the audit of financial statements of certain New York not-for-profits, with only independent directors permitted to participate in any board or committee deliberations or voting relating to such matters – see **Tab 18** and **Tab 27**. As discussed in more detail in **Tab 18**, a director of a New York not-for-profit may only be considered “independent” as defined in the N-PCL if:

- The director was not an employee or a “key person” of the organization or “affiliate” of the organization during the past three years;
- The director does not have a “relative” who is, or has been within the last three years, a key person of the organization or an affiliate of the organization;
- The director did not receive and does not have a relative who received total direct compensation exceeding \$10,000 in any of the past three fiscal years from the organization or affiliates other than any reasonable compensation for service as a director;

- The director is not a current employee of and 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 provided payments, property or services to, or received payments, property or services from, the organization or an affiliate thereof (not including charitable contributions, dues or fees paid to the organization for services which the organization performs as part of its nonprofit purposes, or payments made by the organization at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the organization are available to individual members of the public on the same terms, and such services received by the organization are not available from another source) for property or services in an amount that, in any of the last three fiscal years, has exceeded (a) the lesser of \$10,000 or 2% of such other entity's consolidated gross revenue if such other entity's consolidated gross revenue was less than \$500,000, (b) \$25,000 if such other entity's consolidated gross revenue was \$500,000 or more but less than \$10 million and (c) \$100,000 if such other entity's consolidated gross revenue was \$10 million or more;
- The director is not, and does not have a relative who is, a current owner, whether wholly or partially, director, officer or employee of the organization's outside auditor, or has worked on the organization's audit at any time during the last three years.

In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose the number of directors who are considered "independent" in accordance with IRS tests, as well as whether any directors have family or business relationships with officers, directors, trustees or "key employees" of the organization – see **Tab 8**. The IRS tests for "independence" are different in some respects to the bright-line tests set forth in the N-PCL's definition of "independent director," for example, the required "look-back" period is different (the most recent tax year under IRS tests, compared with the past three years under New York tests). As discussed in more detail in **Tab 18**, a director may only be considered "independent" in accordance with IRS tests (with some exceptions) if:

- The director was not compensated as an officer or other employee of the organization or a "related organization" during the most recent tax year;
- The director did not receive total compensation exceeding \$10,000 in the most recent tax year from the organization or related organizations for services provided in the director's capacity as an advisor, consultant or independent contractor other than any reasonable compensation for service as a director; and
- Neither the director, nor any "family member" of the director, was involved in a loan, grant, excess benefit transaction, or a business transaction involving an interested person that is reportable on Schedule L of Form 990, with the organization (whether directly or indirectly through affiliation with another organization) during the most recent tax year.

### 3.8 Board Leadership

An effective board leader is one who is capable of developing a strong but independent working relationship with management, and guiding the board to consensus after free and open discussion of viewpoints. An effective board leader is especially important for:

- Organizing the board agenda with input from management and helping to identify the board's information needs;
- Leading board discussions of management performance and compensation in sessions at which management is not present ("executive sessions"); and

- Encouraging frank but collegial discussions both at the board level and as between the board and management.

The N-PCL requires that no employee of a New York not-for-profit may serve as the chair of the board or hold any other title with similar responsibilities, unless approved by a two-thirds majority of the board.

### 3.9 Policies and Guidelines

The board plays a key role in setting the tone of the organization by establishing policies and guidelines that set forth expectations for behavior within the organization and by assessing whether senior management is promoting an appropriate ethical culture within the organization. These policies should include the following:

- **Board Guidelines:** Board guidelines set forth expectations of directors, which may include board leadership, structures, composition, functions and processes, as well as requirements to make personally meaningful gifts or contribute to fundraising efforts – see **Tab 18**.
- **Conflicts of Interest and Related Party Transactions Policy:** The conflict of interest policy assists directors, officers and others in the organization in identifying, evaluating and resolving conflicts of interest. A conflict of interest arises where a director, officer or other decision-maker has an outside interest or relationship that conflicts or may conflict with his or her ability to act strictly in the best interests of the organization. For example, a board member is said to be conflicted where the not-for-profit organization is considering a commercial transaction with another company in which the board member has a financial interest. The policy should define conflicts of interest and should require that the organization's officers, directors and key persons disclose or annually update their interests that could give rise to conflicts of interest, usually by completing a questionnaire. The conflict of interest policy should also include practices for monitoring proposed or ongoing transactions and dealing with potential or actual conflicts, whether discovered before or after the transaction has occurred. The conflict of interest policy should specify the committee or other body that determines whether a conflict exists and the body that reviews actual conflicts (typically the audit committee or the full board). Persons with a conflict should be prohibited from participating in the deliberations and voting regarding the conflict but are permitted to provide background information and answer questions before deliberations or voting. The N-PCL requires that all New York not-for-profits (a) adopt a conflict of interest policy applicable to directors, officers and key persons which meets the requirements of the N-PCL, and (b) follow specified procedures with respect to related party transactions – see **Tab 23**. In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether they have adopted a conflict of interest policy that meets certain requirements – see **Tab 8**.
- **Code of Business Conduct and Ethics:** This code applies to officers, directors, volunteers, key persons and employees, and requires fulfillment of responsibilities in a manner that furthers the purpose and mission of the organization and complies with law, regulations, ethical standards and policies adopted by the organization – see **Tab 21**.
- **Whistleblower Policy:** The whistleblower policy should contain procedures to receive, investigate and take appropriate action regarding fraud or non-compliance with law or organizational policy, and to protect whistleblowers against retaliation. The policy should encourage officers, directors, employees, key persons and volunteers to come forward with credible information regarding illegal practices or violations of organizational policies, law, regulations and/or ethical standards, and specify that the organization will protect the individual from retaliation, and identify those staff, board members or outside parties to whom such information can be reported. Such procedures are encouraged to be implemented by not-for-profit organizations so as to ensure compliance with applicable provisions of Sarbanes-Oxley, which make it a criminal offense, punishable by fines or up to 10 years of prison, for

anyone, including not-for-profit organizations, to “knowingly, with the intent to retaliate” take any action harmful to an employee for providing information relating to the commission or possible commission of a federal offense. The N-PCL requires that New York not-for-profits with 20 or more employees and annual revenues above \$1 million adopt a whistleblower policy that includes procedures for reporting and investigating violations or suspected violations of law or corporate policies, and anti-retaliation provisions – see **Tab 24**. In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether they have adopted a whistleblower policy that meets certain requirements – see **Tab 8**.

- **Document Retention and Destruction Policy:** The document retention and destruction policy promotes the responsible stewardship of information by ensuring that documents are retained for appropriate periods, sensitive information is protected, and unnecessary records are disposed of in a consistent manner. Not-for-profit organizations are encouraged to implement the procedures set forth in this policy in order to reduce the risk that documents will be inappropriately destroyed and to ensure compliance with applicable provisions of Sarbanes-Oxley which mandate penalties for obstruction of justice caused by the destruction of documents that are, or are anticipated to become, subject to any kind of official proceeding or federal agency investigation. The policy should identify the record retention responsibilities of staff, volunteers and board members for maintaining and documenting the storage and destruction of the organization’s documents and records. Note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether they have adopted a document retention and destruction policy that meets certain requirements – see **Tab 8**. For sample guidelines regarding data collection best practices, see **Tab 26**.
- **Investment Policy:** The investment policy assists the board in protecting the not-for-profit organization’s assets and ensuring any investment of its funds is prudent and in the best interest of the organization. NYPMIFA requires that New York not-for-profit organizations adopt an investment policy that meets the requirements of NYPMIFA including defining the standard of conduct and procedures for directors as well as any officers, managers or third parties authorized to manage or invest the organization’s assets – see **Tab 22**.
- **Other Policies:** If the organization participates in significant grant programs or joint ventures, it should adopt policies governing those activities as well.

### 3.10 Committee Structure & Operations

Appropriate structure and use of board committees can enhance the efficiency and effectiveness of the board. Board committees may be particularly useful with respect to board responsibilities that may involve a conflict of interest for management; such committees should – where possible – be comprised of directors who are independent from management – see **Tab 18**.

In addition to the executive committee (discussed above) key board committees include:

- **Audit Committee:** This committee is responsible for hiring and assuring the independence of the independent auditor (if any) and providing oversight of (a) the audit, review or compilation of financial statements, (b) internal controls and related processes designed to assure the reliability of financial data, and (c) risk management processes. The N-PCL requires that, in the case of any New York not-for-profit required to file an independent certified public accountant’s audit report with the New York Attorney General, either the full board or an audit committee comprised entirely of independent directors (with only independent directors participating in deliberations and voting) is required to (i) provide oversight of the organization’s accounting and financial reporting and the audit of the organization’s financial statements, (ii) annually retain the independent auditor, (iii) review the results of the audit and any related management letter with the independent auditor, and (iv) perform additional audit oversight responsibilities where the not-for-profit is expected to have annual revenues in excess

of \$1 million – see **Tab 27**. In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether they have an audit committee that meets certain requirements – see **Tab 8**.

- **Compensation Committee:** This committee is responsible for determining and reviewing the compensation of the CEO and other senior managers in accordance with objective, documented and comparable information and for ensuring that compensation is tied to the achievement of predetermined performance goals that are keyed to accomplishments relating to the purpose and mission. New York not-for-profits should note that the N-PCL prohibits any person from being present at or otherwise participating in any board or committee deliberation or vote concerning such person’s compensation, although such person may present background information or answer questions prior to the commencement of the relevant deliberations or voting – see **Tab 29**. In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether their process for determining compensation of certain persons included, among other things, review and approval by independent persons – see **Tab 8**.
- **Nominating and Governance Committee:** This committee is responsible for nominating board candidates, ensuring that the size, leadership and composition of the board (and committees, as applicable) are appropriate, and overseeing governance structures and policies – see **Tab 28**.

However, whether a not-for-profit organization would find it useful to establish a particular committee will depend on the needs and circumstances of the organization. For example, an organization with significant financial resources or complex financial arrangements may benefit significantly by establishing an audit committee. In contrast, a small organization with simple financial structures may decide that it would be efficient and effective to entrust responsibility for ensuring the integrity of financial reporting to the entire board. (In either case, some members of the board should be financially literate and at least one director should be sophisticated concerning financial reporting and accounting.)

Committee charters set forth the responsibilities of each committee and clarify whether decisional authority is delegated to the committee or whether the committee is to undertake the background work and make recommendations to the board for board approval.

Not-for-profits with large boards may find it useful to organize an executive committee to take on a number of tasks that might otherwise fall to the full board but can be achieved more efficiently in a smaller group – see **Tab 30**. Additionally, boards of not-for-profit organizations often have a large number of committees that focus on operational or program aspects, for example, finance and investment, strategic planning, development and public relations – see **Tab 31**, **Tab 32**, **Tab 33** and **Tab 34**. Care should be taken that board committees do not unduly proliferate and result in the board becoming over-engaged in operational matters and hampering management’s ability to perform effectively.

### 3.11 Board Self-Evaluation

Although not required by law, the board should regularly evaluate its performance and seek to continually improve its effectiveness in governing the not-for-profit organization as a best practice. Self-evaluations of the board, committees and/or individual directors can be conducted in several ways, including through written questionnaires, individual interviews with directors or through a discussion with the board, and inhouse or using counsel or other third-party facilitator – see **Tab 20**.

### 3.12 Other Governance Practices

- **Minutes and Records:** Boards and their committees should ensure that minutes of their meetings, and actions taken by written consent, are contemporaneously documented. Minutes/records should detail or summarize the deliberative process undertaken by the board and committees as they address

organizational issues in the proper discharge of their fiduciary duties; in this way, the minutes/records serve not only as important reminders as to what has been decided and why, but also serve as evidence as to how the board and committees fulfilled their fiduciary duties. State law may impose requirements in relation to minutes/records. In addition, note that not-for-profit organizations that are required to file Forms 990 with the IRS are required to disclose whether the organization contemporaneously documents the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. Sample minutes are included at **Tab 19**.

- **Financial Statements:** Directors are stewards of a not-for-profit organization’s financial and other resources. The board should ensure that financial resources are used to further the organization’s charitable purpose and mission, and that the organization’s funds are appropriately accounted for by regularly receiving and reviewing up-to-date financial statements and any auditor’s letters or finance and audit committee reports. Smaller organizations may prepare financial statements without any involvement of outside accountants or auditors. Others use outside accountants to prepare compiled or reviewed financial statements, while others obtain audited financial statements. State law may impose audit requirements on certain charities. For example, organizations registered in New York for charitable solicitation purposes with annual gross revenue and support in excess of \$1 million require their financial statements to be audited by an independent certified public accountant and to file with the Attorney General the resulting audited financial report and related financial statements. Many organizations that receive funds from the U.S. Government are required to undergo one or more audits as set forth in the Single Audit Act. However, even if an audit is not required, a charity with substantial assets or revenue should consider obtaining an audit of its financial statements by an independent auditor. A summary of the requirements of Form 990, which is required to be filed with the IRS by certain not-for-profit organizations, is set forth at **Tab 8**.
- **AI Governance:** Not-for-profit organizations are increasingly using AI in their work. Common uses for AI in the not-for-profit sector include internal productivity, communications, development and fundraising. By streamlining routine and administrative tasks, the thoughtful use of AI can enable organizations to focus more directly on strategic priorities and advancing mission-driven work. While AI tools may enhance efficiency and impact, they also introduce legal, ethical, security and reputational risks, such as the potential to produce misinformation or inaccurate results, and data security and privacy concerns. In light of these emerging risks, not-for-profit organizations can consider implementing an AI governance and oversight framework, beginning with internal guidelines or policies governing, among other things, permitted use cases of AI, data input restrictions, requirements for human oversight of AI-generated work, and procedures for evaluating and approving AI tools. Such guardrails ensure that AI is used responsibly and in alignment with the organization’s mission.

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## Not-For-Profit Practice Group

### Key Governance Provisions of the New York Not-for-Profit Corporation Law

The New York Not-for-Profit Corporation Law (the “N-PCL”) governs the formation, operation and dissolution of not-for-profit corporations in New York State. Below we provide a comprehensive overview of the key provisions of the N-PCL, as amended.<sup>1</sup>

New York not-for-profit corporations should review their governance structure, oversight functions, policies, and day-to-day operations to ensure compliance with the N-PCL. Most of the provisions summarized below apply to not-for-profit corporations incorporated under New York law (regardless of whether they are tax-exempt under Section 501(c)(3) of the Internal Revenue Code of 1986, as amended (the “Code”). Provisions described under “Independent Audit Oversight” relating to financial audits and reporting also apply to not-for-profit organizations incorporated elsewhere but registered in New York for charitable solicitation purposes.<sup>2</sup>

Set forth below is a chart summarizing the applicability of the N-PCL, followed by a summary of its key provisions. At the end of this summary, we include recommendations on “what to do now.”

## I. NOT-FOR-PROFIT CORPORATIONS TO WHICH THE LAW APPLIES

Type of Entity	Scope of Applicability
<p><b><i>New York not-for-profits:</i></b></p> <ul style="list-style-type: none"> <li>Not-for-profit corporations incorporated or that is authorized to conduct or that conducts any activities in the State of New York (referred to in this chart as “NY NFPs”)</li> </ul>	Entire N-PCL except where noted below
<ul style="list-style-type: none"> <li>NY NFPs that are not registered in NY for charitable solicitation purposes</li> </ul>	Not required to comply with any provisions discussed under “Independent Audit Oversight” below
<ul style="list-style-type: none"> <li>NY NFPs that have annual revenues of \$1 million or less</li> </ul>	Not required to comply with certain provisions discussed under “Independent Audit Oversight” below
<ul style="list-style-type: none"> <li>NY NFPs that have annual revenue of \$1 million or less and/or less than 20 employees<sup>3</sup></li> </ul>	Not required to comply with any provisions discussed under “Whistleblower Policy” below
<p><b><i>Not-for-profits incorporated outside of New York:</i></b></p> <ul style="list-style-type: none"> <li>Registered in NY for charitable solicitation purposes and with gross revenues in excess of the thresholds described in “Raising Thresholds Requiring an Independent Audit or Review”</li> </ul>	Required to comply with provisions discussed under “Independent Audit Oversight” below

### 1.1 Internal Governance

There are notable requirements applicable to New York not-for-profit organizations, including:

- Employee Board Chair.** In order for an employee to serve as chair of the board or hold any other title with similar responsibilities, the board must approve such appointment by a two-thirds vote of the “entire” board (i.e., including vacancies) and document in writing the rationale for approval. No employee serving as chair of the board can be considered an “independent director” (as discussed below).<sup>4</sup>
- Raising Thresholds Requiring an Independent Audit or Accountant Review.** The New York Executive Law raises the gross revenue and the N-PCL supports thresholds that trigger the requirement that not-for-profits that are registered in New York for charitable solicitation purposes obtain and file with the New York Attorney General an independent certified public accountant audit report or review report, as set forth below. In addition, charitable organizations which use paid fundraisers are no longer required to obtain an audit report unless they meet the gross revenue and support thresholds. As of July 1, 2021 (and current at the time of writing), the thresholds for both Audit Reports and Review Reports are as follows:

Requirement	Gross Revenue & Support Threshold Applicability
	As of July 1, 2021
<b>Audit report</b>	In excess of \$1 million
<b>Review report</b>	\$250,000 to \$1 million

- **Independent Audit Oversight.** In the case of any not-for-profits required to file an independent certified public accountant’s audit report with the Attorney General, either the full board or an audit committee comprised entirely of independent directors (with only independent directors participating in deliberations and voting) is required to:
  - oversee the accounting and financial reporting processes of the organization and the audit of the organization’s financial statements;
  - annually retain the independent auditor;
  - review the results of the audit and any related management letter with the independent auditor; and
  - in the case of a New York not-for-profit expected to have annual revenues in excess of \$1 million:
    - review with the independent auditor the scope and planning of the audit prior to its commencement;
    - upon completion of the audit, 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 of the corporation’s accounting and financial reporting processes; and
    - annually consider the performance and independence of the independent auditor;
    - if the items above are performed by an audit committee, report on the audit committee’s activities to the board.
- **Independent Directors.** The N-PCL requires the board or an audit committee composed of “independent” directors to oversee the audit (if any) as discussed above, with only independent directors able to participate in any board or committee deliberations or voting relating to such matters. The N-PCL generally requires that committees of the board<sup>5</sup> have at least three members. The N-PCL defines an “independent director” as a director who:
  - is not, and has not been within the last three years, an employee or a “key person”<sup>6</sup> of the corporation or an “affiliate”<sup>7</sup> of the corporation, and does not have a “relative”<sup>8</sup> who is, or has been within the last three years, a key person 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 three fiscal years, more than \$10,000 in direct compensation from the corporation or an affiliate of the corporation, other than reasonable compensation for service as a director or expenses reasonably incurred as a director; 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 provided payments<sup>9</sup>, property or services to, or received payments, property or services from, the corporation or an affiliate thereof for property or services in an amount that, in any of the last three fiscal years, exceeds:

- the lesser of \$10,000 or 2% of such other entity’s consolidated gross revenues if the entity’s consolidated gross revenue was less than \$500,000 dollars,
  - \$25,000 if the entity’s consolidated gross revenue was \$500,000 or more but less than \$10,000,000 or
  - \$100,000 if the entity’s consolidated gross revenue was \$10,000,000 or more;<sup>10</sup> or
- 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.
- **Mandatory Related Party Transaction Procedures and Ability of Attorney General to Unwind.** Prior to undertaking a transaction with a “related party,”<sup>11</sup> the board, or an authorized committee of the board, of a New York not-for-profit must first determine if the proposed transaction is fair, reasonable, and in the corporation’s best interest. This requirement applies to all transactions that meet the definition of a “related party transaction.” In addition, where a related party has a “substantial financial interest” in a proposed transaction, the board (or authorized committee) must follow certain procedural requirements, including the consideration of alternative transactions to the extent available, majority board or committee approval, and contemporaneous documentation of the board’s considerations and decision.<sup>12</sup> Notably, the N-PCL enhances the power of the Attorney General to bring an action to enjoin, void, or rescind related party transactions that have been entered into without complying with applicable procedural requirements, as well as to remove directors or officers, order payment of double the amount of certain improperly obtained benefits, or seek restitution.<sup>13</sup>
  - **Conflict of Interest Policy.**<sup>14</sup> The N-PCL requires that the board of each New York not-for-profit corporation – regardless of size – must adopt and oversee a conflict of interest policy applicable to directors, officers and key persons.<sup>15</sup> The N-PCL requires that such policy, among other things: (i) define the circumstances that constitute a conflict; (ii) include procedures for disclosing, addressing and documenting a conflict of interest, potential conflict of interest or related party transaction and for determining whether a conflict exists; (iii) prohibit a conflicted person from participating in deliberations or voting or influencing the vote; and (iv) require directors to disclose to the corporation (upon joining the board and annually thereafter) any entities with which they are affiliated and with which the corporation has a relationship, and any corporate transactions possibly giving rise to a conflict for the director. IRS Form 990 also requires disclosure of whether the organization has a conflict of interest policy.
  - **Whistleblower Policy.** The board of each New York not-for-profit corporation that has 20 or more employees and annual revenue above \$1 million must adopt and oversee a whistleblower policy that includes anti-retaliation provisions and procedures for reporting and investigating violations or suspected violations of law or corporate policies. In addition, the policy must designate a specific employee, officer or director to administer the policy and report to the audit committee or the full board, except that directors who are employees may not participate in any board or committee deliberations or voting relating to administration of the whistleblower policy. Only those persons not subject to a whistleblower complaint may participate in any board or committee deliberations or vote on matters relating to the policy. The N-PCL requires that the policy be distributed to all directors, officers, employees and to volunteers who provide substantial services to the corporation, and provides that posting the policy on the corporation’s website or at the corporation’s offices (in a conspicuous, accessible location) will satisfy the distribution requirement. Some not-for-profits have previously adopted whistleblower policies in response to applicable provisions of the Sarbanes-Oxley Act prohibiting retaliation against whistleblowers. IRS Form 990 also requires disclosure of whether the organization has a whistleblower policy.<sup>16</sup>

- **Board Vacancies.** The N-PCL allows that directors elected or appointed to fill a vacancy in an unexpired term will hold office until either the end of the term that the director was elected or appointed to fill or until the end of a term determined by the board that ends at an annual meeting. Under previous law, a director elected or appointed to fill a vacancy in an unexpired term would, by default, hold office until the organization's next annual meeting.<sup>17</sup>

## 1.2 Streamlined Corporate Transactions

The N-PCL streamlines the process for approving certain corporate transactions, including:

- **Approval Process for Certain Transactions.** Pursuant to the N-PCL, certain transactions only require Attorney General approval. However, court approval (i) is still required if the corporation is insolvent or would become insolvent as a result of the transaction or if the Attorney General concludes that court approval is appropriate and (ii) is still available to the organization if the Attorney General does not approve the transaction.<sup>18</sup>
- **Majority Vote for Routine Real Estate Transactions.** The N-PCL requires only a majority of the board or authorized committee to approve routine real estate transactions (such as the purchase, sale, mortgage or lease of real property that does not constitute, after giving effect to the transaction, all or substantially all of the assets of the not-for-profit). However, a real estate transaction that constitutes an acquisition (after giving effect to the transaction) or disposition of all or substantially all of the assets of the not-for-profit still requires the approval of two-thirds of the entire board (or a majority of the entire board if there are 21 or more directors).<sup>19</sup>

## 1.3 Simplified Formation and Day-to Day Operations

The N-PCL includes features designed to simplify and reduce statutory and administrative requirements considered to be burdensome, including:

- **Permitting Electronic Meetings, Consent and Communications.** The N-PCL expressly permits electronic technology for certain meetings, notices, waivers, proxies and other communications, and allows boards or committees to take action by written consent in electronic form. To the extent members or directors of a not-for profit are required or permitted to take action by vote, the N-PCL allows such action to be taken without a meeting, upon the written or electronic consent of all the members or directors entitled to vote on the action.<sup>20</sup> In certain cases, the N-PCL permits website posting in lieu of newspaper publications.
- **Simplifying Categories of Not-for-Profits.** Not-for-profit corporations are categorized as “charitable” or “non-charitable” under the N-PCL. A “charitable corporation” means any corporation formed or deemed to be formed for charitable purposes. “Charitable purposes” are defined to mean purposes contained in the certificate of incorporation that are charitable, educational, religious, scientific, literary, cultural, or for the prevention of cruelty to children or animals. A “non-charitable corporation” means any not-for-profit corporation 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 relate to animal husbandry or for the purpose of operating a professional, commercial, industrial, trade, or service association. Type A not-for-profits incorporated before July 1, 2014 are deemed “non-charitable,” Type B and C not-for-profits incorporated before July 1, 2014 are deemed “charitable,” and Type D corporations formed before July 1, 2014 are deemed “charitable” or “non-charitable” depending on the purposes as reflected in their existing charters.<sup>21</sup>
- **Eliminating State Education Department Consent for Certain Entities.** The N-PCL does not require not-for-profits to obtain advance approval of the New York State Education Department for

formation. Previously, not-for-profits involved in any type of education were required to obtain pre-approval from the State Education Department or the regents of the state university system. Under the N-PCL, State Education Department approval is only required for a school, library, museum, or historical society; note that the approval of the regents of the state university system is required for a college or university. Other not-for-profits whose charters include a purpose for which a corporation might be chartered by the regents of the state university system are required only to provide the Commissioner of Education with a certified copy of the certificate of incorporation within 30 business days after formation.<sup>22</sup>

- **Permitting Correction of Typographical or Similar Non-Material Errors in Certificates or Instruments.** The N-PCL allows certificates and other instruments relating to not-for-profits that contain typographical or non-material errors to be corrected by e-mailing the New York Department of State.<sup>23</sup>

## II. WHAT TO DO NOW (IF YOU HAVE NOT DONE SO YET!)

- Review corporate governance policies and procedures for compliance with the N-PCL. In particular, bylaws, corporate governance guidelines, committee charters, codes of conduct, whistleblower and conflict of interest or related party transaction policies should be reviewed.
- Review the organization's board leadership structure and succession plan to ensure that if an employee is chair of the board, appropriate procedures have been followed.
- Determine which directors qualify as "independent" in accordance with the N-PCL's independence standards and, if necessary, plan to elect or appoint independent directors who are responsible for providing oversight of the organization's audit (where applicable).
- Confirm whether it is anticipated that the organization's gross revenues are such that the organization's financial statements are required to be audited or reviewed by an independent certified public accountant in light of the applicable thresholds.

## ENDNOTES

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<sup>1</sup> This summary focuses primarily on not-for-profit corporations, but readers should be aware that there are alternative structures that may be utilized such as trusts or LLCs (and note that New York does not have an LLC statute expressly permitting the formation of a not-for-profit LLC).

<sup>2</sup> Certain provisions of the N-PCL also apply to charitable trusts that are subject to the New York Estates, Powers and Trusts Law.

<sup>3</sup> N-PCL § 712-a requires corporations that file “an independent certified public accountant’s *audit* report” to oversee the accounting and financial reporting processes of the corporation. Effective July 2021, the thresholds in NY CLS Exec § 172-b (which determine which corporations have to comply with the audit oversight provisions in 712-a) have changed. Only corporations with revenues in excess of \$1 million in revenues have to file “an independent certified public accountant’s audit report.” Corporations with revenues of at least \$250,000 but less than \$1 million have to file annual financial reports with “independent certified public accountant’s *review* reports”, so the oversight provisions do not apply to them. N-PCL § 715-b requires corporations that have twenty or more employees *and* have revenues in excess of \$1 million to adopt a whistleblower policy.

<sup>4</sup> No employee of a New York not-for-profit shall serve as chair of the board or hold any other title with similar responsibilities, unless the board approves such employee serving as the chair by a two-thirds vote of the entire board and contemporaneously documents in writing the basis for approval. *See* N-PCL § 713(f).

<sup>5</sup> The N-PCL distinguishes between (i) committees of the board, which may bind the board and which may be composed solely of directors, and (ii) the more advisory in nature committees of the corporation, which may not bind the board and which may include non-directors. *See* N-PCL § 712(e).

<sup>6</sup> A “key person” is defined as any person, other than a director or officer, whether or not an employee of the corporation, who (i) has responsibilities or exercises powers of influence over the corporation as a whole similar to a director or officers; (ii) manages the corporation, or a segment of the corporation that represents a substantial portion of the activities, assets, income or expenses of the corporation or (iii) alone or with others controls or determines a substantial portion of the corporation’s capital expenditures or budget. *See* N-PCL § 102(a)(25).

<sup>7</sup> An “affiliate” of a corporation is defined as any entity controlled by, or in control of, such corporation. *See* N-PCL § 102(a)(19).

<sup>8</sup> A “relative” of an individual means (i) his or her spouse or domestic partner; (ii) his or her ancestors, brothers and sisters (whether whole or half blood), children (whether natural or adopted), grandchildren, great-grandchildren; or (iii) the spouse or domestic partner of his or her brothers, sisters, children, grandchildren, and great-grandchildren. *See* N-PCL § 102(a)(22).

<sup>9</sup> “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 or payments made by the corporation at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the corporation are available to individual members of the public on the same terms, and such services received by the corporation are not available from another source.

<sup>10</sup> While the terms “related party” and “independent director” are also relevant for the purposes of compliance with the tax laws, it should be noted that tax laws and the N-PCL differ in their definitions of these terms.

<sup>11</sup> A “related party” is defined by the N-PCL as: (i) any director, officer, or key person of the corporation or any of its affiliates; (ii) any relative of any director, officer, or key person of the corporation or its affiliates; or (iii) any entity in which an individual described in clause (i) or (ii) has a 35 percent 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 percent. The N-PCL defines a “related party transaction” as any transaction, agreement, or other arrangement in which a “related party” has a financial interest and in which the corporation or any of its affiliates is a participant, other than a transaction in which (i) the transaction or the related party’s financial interest is *de minimis*; (ii) the transaction would not customarily be reviewed by the board or boards of similar organizations in the ordinary course of business and is available to others on similar terms or (iii) the transaction is a benefit to a related party solely as a member of a class that the corporation intends to benefit as part of its mission, and the benefit is available to all similarly situated members of the class on the same terms. *See* N-PCL § 102(a)(23)-(24).

<sup>12</sup> For a number of years, the Code has imposed analogous rules setting parameters around “related party” transactions. The so-called “intermediate sanctions” provisions of Code Section 4958 establish specific guidelines, similar (but not identical) to the procedures required under the N-PCL, that serve to protect the not-for-profit organization from violating the prohibition against private inurement and thereby incurring penalties. Notably, the Code’s guidelines in this area are not mandatory, but merely establish a “safe harbor,” whereas the N-PCL *requires* that a not-for-profit take specific steps prior to participating in a related party transaction. The N-PCL provides that in an action by any person or entity other than the Attorney General, it is a defense that the transaction was fair, reasonable, and in the corporation’s best interest at the time the corporation approved the transaction.

<sup>13</sup> The N-PCL provides that a corporation has a defense to an action by the Attorney General with respect to a related party transaction that was not approved in accordance with the N-PCL if several requirements are met in advance of any request for information from the Attorney General; namely that (i) the transaction was ratified in good faith; (ii) alternatives were considered; (iii) the reason for the violation and ratification were documented in writing and (iv) procedures were put in place to ensure future compliance. *See* N-PCL § 715(j).

<sup>14</sup> The N-PCL requires that such policy, among other things: (i) define the circumstances that constitute a conflict; (ii) include procedures for disclosing a conflict of interest to the board or to a committee of the board, and procedures for the board or committee to determine whether a conflict exists, (iii) require that the person with the conflict not be present at or participate in board or committee deliberation or vote on the matter giving rise to such conflict; (iv) prohibit attempts by the person with the conflict from influencing improperly the deliberation or voting on the matter giving rise to such conflict (although the person may present information as background or answer questions at a committee or board meeting prior to the commencement of deliberations or voting relating thereto); (v) require that the existence and resolution of the conflict be documented in the corporation’s records, including in the minutes of any meeting at which the conflict was discussed or voted upon; (vi) include procedures for disclosing, addressing, and documenting related party transactions; and (vii) require directors to disclose to the organization (upon joining the board and annually thereafter) any entities with which they are affiliated and with which the organization has a relationship, and any corporate transactions possibly giving rise to a conflict with respect to the director. *See* N-PCL § 715-a.

<sup>15</sup> IRS Form 990 (the annual tax return filed by most not-for-profit organizations) requires disclosure of whether the organization has a conflict of interest policy. The tax law (and IRS Form 990) does not require that an organization have a conflicts policy; however, the IRS believes that the absence of a conflicts policy is a factor suggesting substandard corporate governance, which (the IRS maintains) may lead to violation of tax law principles applicable to exempt organizations and therefore warrants heightened scrutiny.

<sup>16</sup> The N-PCL requires New York not-for-profits that have 20 or more employees and annual revenue in excess of \$1 million in the prior year to have a whistleblower policy adopted and overseen by the corporation’s board of directors to protect from retaliation persons who report suspected improper conduct. Such whistleblower policy must include procedures for reporting of violations or suspected violations of law or corporate policies, including procedures for preserving the confidentiality of reported information. In addition, the whistleblower policy: (i) must designate a specific employee, officer or director of the organization to administer the policy and report to the board or an authorized committee thereof, except that directors who are employees may not participate in any board or committee deliberations or voting relating to administration of the whistleblower policy; (ii) require that the person who is subject of the whistleblower complaint not be present at or participate in board or committee deliberations relating to such complaint (although the person may present information as background or answer questions at a committee or board meeting prior to the commencement of deliberations or voting relating thereto); and (iii) require that a copy of the policy be distributed to all directors, officers, employees and volunteers who provide substantial services to the corporation. *See* N-PCL § 715-b.

<sup>17</sup> *See* N-PCL § 705(c).

<sup>18</sup> *See* N-PCL § 511-a.

<sup>19</sup> *See* N-PCL § 509.

<sup>20</sup> *See* N-PCL §§ 614(a) and 708(b).

<sup>21</sup> *See* N-PCL § 201.

<sup>22</sup> *See* N-PCL § 404(d).

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<sup>23</sup> See N-PCL § 105.

## Not-For-Profit Practice Group

### Duties and Liabilities of Directors of Not-For-Profit Organizations

#### I. BACKGROUND FOR NOT-FOR-PROFIT ORGANIZATIONS

The defining characteristic of a tax-exempt not-for-profit organization is that it cannot distribute profits to those who control it or to its directors<sup>1</sup> or officers.<sup>2</sup> Instead, a not-for-profit corporation is organized “exclusively for a purpose or purposes, not for pecuniary profit or financial gain,” and “no part of the assets, income or profit of which is distributable to, or inures to the benefit of, its members, directors or officers except to the extent permitted under this statute.”<sup>3</sup> Despite the name, the distinguishing characteristic is not a lack of profits, but the prohibition on pecuniary gain, and it is that prohibition – rather than statutory type of the not-for-profit corporation<sup>4</sup> – that informs many of the liabilities and duties of its directors and officers.<sup>5</sup> The discussion below provides a general overview of the duties and liabilities of directors and officers of not-for-profit corporations under New York law.

#### II. ROLE AND PURPOSE OF THE BOARD OF DIRECTORS IN NOT-FOR-PROFIT CORPORATIONS

Like their for-profit counterparts, not-for-profit organizations generally are managed by and under the direction of a board of directors.<sup>6</sup> The board typically delegates responsibility for the day-to-day management of the organization to a management team appointed by the board. Nonetheless, the board remains liable for breaches of its duties, even if the board does not retain management powers.<sup>7</sup> This is important because:

- Most not-for-profit directors are volunteers and, as such, may incorrectly assume that they have few legal responsibilities or potential liabilities; and
- Not-for-profit directors often operate on a part-time schedule and do not devote much time to their directorships.

#### III. DUTIES OF NOT-FOR-PROFIT DIRECTORS AND OFFICERS

Like their for-profit counterparts, the directors and officers of not-for-profit corporations are fiduciaries of the organizations they serve.<sup>8</sup> The New York Not-for-Profit Corporation Law (“N-PCL”) and New York courts have defined three broad fiduciary duties which directors and officers of not-for-profits owe to their organizations: the duties of care, loyalty and obedience.

##### 3.1 The Duty of Care

The duty of care applicable to not-for-profit directors and officers is set forth in N-PCL § 717:

Directors, officers, and key persons shall discharge the duties of their respective positions in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.<sup>9</sup>

The duty of care applicable to the directors and officers of not-for-profits is closely modeled on the New York Business Corporation Law (“BCL”) for-profit model,<sup>10</sup> and the legal expectation and legislative presumption is that courts will apply the standards uniformly.<sup>11</sup>

Broadly speaking, the duty of care requires directors and officers of a not-for-profit organization to be “attentive to the organization’s activities and finances” and to “actively oversee the way in which its assets are managed.”<sup>12</sup>

While the specific actions a director or officer must take in order to oversee the affairs of his or her organization may vary depending on the context, fulfilling this duty typically requires directors and officers to:

- attend and participate in meetings;
- read and understand financial documents or other key materials;
- ensure that the funds of the not-for-profit are properly managed;
- ask questions; and
- exercise sound and independent judgment.<sup>13</sup>

In essence, the duty of care requires directors and officers to take reasonable steps in order to “remain informed and attentive in making decisions and overseeing the corporation’s business.”<sup>14</sup> But directors and officers need not have *perfect* knowledge or oversight. Rather, directors and officers must devote “the care that a person in a like position would reasonably believe appropriate for a member of a governing body under similar circumstances.”<sup>15</sup> “‘Like position’ refers to the individual director, his or her specific function, expertise, and length of service; an insider with greater knowledge may be held to a higher standard than a director recently appointed who has had no affiliation with the organization.”<sup>16</sup> Thus, evaluating what is reasonable or appropriate under the circumstances necessarily requires taking into account “basic attributes of common sense, practical wisdom, and informed judgment generally associated with the position of a corporate director.”<sup>17</sup>

Practically speaking, one of the key duties of any director is to provide oversight of the organization and management. Within the for-profit context, adequate oversight means investigating “red flags” and other potential issues when they arise. Thus, while a director need not oversee every aspect of a corporation’s day-to-day management, “[i]t is the directors’ duty to make necessary inquiries” where “suspicions are aroused, or should be aroused.”<sup>18</sup> Notably, directors are not required to “ferret out wrongdoing” absent a specific warning or other obvious “red flag.”<sup>19</sup> Therefore, a director could breach the duty of care (or potentially act in bad faith, which is a breach of the duty of loyalty discussed in Section 3.2 below) if she fails “to devote attention to ongoing oversight of the activities and affairs of the corporation . . . when particular facts and circumstances of significant concern materialize that would alert a reasonably attentive director to the need.”<sup>20</sup> These same principles apply to not-for-profit corporations as well.<sup>21</sup>

#### A. Good Faith Reliance on Information Under the Duty of Care

Directors and officers are obligated to keep themselves reasonably informed of the affairs of the corporation. Because directors and officers must always remain engaged and exercise independent judgment, they are not permitted to simply “rubber stamp” the advice or recommendations of those upon whom they rely.<sup>22</sup> Importantly, however, directors and officers can fulfill their duty of care by relying on key persons, including key employees or outside advisors and specialists, to provide them with the information upon which they rely when making decisions.

Specifically, N-PCL § 717(b) provides: “In discharging their duties, directors, officers, and key persons, when acting in good faith, may rely on information, opinions, reports or statements including financial statements and other financial data, in each case prepared or presented by:<sup>23</sup>

- One or more officers or employees of the corporation, whom the director believes to be reliable and competent in the matters presented;<sup>24</sup>
- Counsel, public accountants or other persons as to matters that the directors, officers or key persons believe to be within such person’s professional or expert competence;<sup>25</sup> or

- A committee of the board upon which they do not serve, duly designated in accordance with a provision of the certificate of incorporation or the bylaws, as to matters within its designated authority, which committee the directors, officers or key persons believe to merit confidence, so long as in so relying they shall be acting in good faith and with [the requisite] degree of care.”<sup>26</sup>

In essence, subsection 717(b) authorizes directors and officers to rely on information provided to them by employees and advisors, who are often closer to the day-to-day management of the organization and who may have firsthand knowledge or expertise regarding the matters to be considered. This subsection also authorizes directors and officers to rely on information provided to them by duly designated committees of the board upon which they do not serve. However, this subsection does not shield directors and officers if their reliance is not in good faith and with the same degree of care specified in N-PCL § 717(a), such as where the director or officer actually knows that the information is incorrect, or where the director or officer should have known that the information was incorrect.<sup>27</sup>

When relying on an “expert” opinion, diligence requires that the board investigate the expert’s qualifications and ascertain his or her competence. For reliance to be defensible, it must be placed upon experts who are competent in their fields; competence generally implies expertise.<sup>28</sup> The director must review the material provided by the expert and follow up with any questions presented by that material. “If all a director knows about a report is the conclusion, he is not acting in good faith or with the required diligence.”<sup>29</sup> The protection of good faith reliance may be forfeited where directors selectively follow or disregard professional advice.<sup>30</sup>

## B. The Duty of Care In the Context of Investment Decisions

New York not-for-profit organizations are subject to compliance with the Uniform Prudent Management of Institutional Funds Act (“UPMIFA”) rules, which have been codified in New York as the New York Prudent Management of Institutional Funds Act (“NYPMIFA”).<sup>31</sup> These rules impose a statutory duty of care for managing not-for-profit funds, expenditure rules for endowment funds, and rules required for delegation of investment management, and could lead to increased scrutiny by the Attorney General or the IRS. Regardless of the statutory mandate, the rules provide a roadmap for the prudent exercise of the duty of care with respect to the investment and management of funds entrusted to a not-for-profit organization, including the following considerations:

- *Reasonable Costs.* A not-for-profit organization should incur only those investment fees and costs which are appropriate and reasonable in relation to its assets, purposes, and the skills available to it.<sup>32</sup>
- *Investment Factors.* The board should consider the following factors when managing and investing funds: (a) general economic conditions; (b) the possible effect of inflation or deflation; (c) expected tax consequences, if any, of investment decisions or strategies; (d) the role that each investment or course of action plays within the overall investment portfolio of the fund; (e) the expected total return from income and the appreciation of investments; (f) other resources of the organization; (g) the needs of the organization to make distributions and to preserve capital; and (h) an asset’s special relationship or special value, if any, to the purposes of the organization.<sup>33</sup>
- *Investment Strategy and Policy.* Investment decisions should not be made in isolation but in the context of an overall investment strategy having risk and return objectives reasonably suited to the organization.<sup>34</sup> Not-for-profit organizations should have a written investment policy setting forth guidelines on investments and delegation of management and investment functions in accordance with applicable law.<sup>35</sup> A not-for-profit organization should make reasonable efforts to verify facts relevant to the management and investment of its fund.<sup>36</sup>
- *Diversification.* Not-for-profit organizations should diversify their investments unless the organization prudently determines that the purposes of its investments are better served without diversification because of special circumstances.<sup>37</sup> Decisions to not diversify should be reviewed at least annually.<sup>38</sup>

- *Timing of Investment Decisions.* Not-for-profit organizations should carry out decisions concerning the retention or disposition of property or to rebalance a portfolio within a reasonable time after receiving such property.<sup>39</sup>
- *Delegation of Management and Investment Functions.* Not-for-profit organizations should: (a) carefully carry out decisions concerning the selection, retention or termination of investment advisors, including assessing any conflicts of interest or other factors affecting their independence; (b) carefully monitor an investment advisor's performance and compliance; and (c) provide that each contract delegating authority to an investment advisor should be terminable upon no more than 60 days' notice.<sup>40</sup>

### 3.2 The Duty of Loyalty

"The duty of loyalty requires directors to exercise their powers in good faith and in the best interests of the corporation, rather in their own interests or the interest of another entity or person."<sup>41</sup> In essence, the duty of loyalty requires directors and officers to "pursue the interests and mission of the charitable organization with undivided allegiance" and to make sure that there is no conflict between his or her personal interest and the interests of the organization.<sup>42</sup> Thus, "the duty of loyalty is transgressed when a corporate fiduciary . . . uses his or her corporate office . . . to promote, advance or effectuate a transaction between the corporation and such person (or an entity in which the fiduciary has a substantial economic interest, directly or indirectly) and that transaction is not substantively fair to the corporation."<sup>43</sup> The following are classic examples of situations that implicate the duty of loyalty:<sup>44</sup>

- A director appearing on both sides of a transaction;
- A director receiving a personal benefit from a transaction;<sup>45</sup> or
- A director usurping or appropriating a financial opportunity for his or her own personal gain.<sup>46</sup>

In addition, the duty of loyalty requires directors to act in "good faith," which courts have equated with acting according to "rules of conscientious fairness, morality and honesty in purpose."<sup>47</sup> Accordingly, courts have stated that acting in good faith requires "the exercise of an honest judgment, and an honest and unbiased consideration of any fact or circumstances affecting the general interest of the corporation."<sup>48</sup>

### 3.3 The Duty of Obedience

The duty of obedience concerns a director's obligation to ensure that the mission of the not-for-profit organization is upheld and perpetuated. This duty is not stated explicitly in the N-PCL, and is not codified in any statute relating to not-for-profit organizations, but it does find support in N-PCL § 202(a)<sup>49</sup> and 402(a)(2),<sup>50</sup> which require a not-for-profit organization to have a purpose in order to incorporate and to act in furtherance of that purpose. The duty of obedience is at issue in the following circumstances:

- Diversion of corporate resources away from the stated purpose, no matter how worthy the use, is not legally justifiable and exposes the director to liability for breaching the duty of obedience.<sup>51</sup>
- In the context of a merger or sale of all or substantially all of its assets, the organization must present a verified position to the Attorney General or the requisite supreme or county court setting forth "[t]hat the consideration and the terms of the sale, lease, exchange or other disposition of the assets of the corporation are fair and reasonable to the corporation, and that the purposes of the corporation, or the interests of its members will be promoted thereby."<sup>52</sup> Examples of transactions implicating the duty of obedience include:
  - *Manhattan Eye, Ear and Throat Hosp. v. Spitzer.* The trustees of the hospital sought court approval to sell the hospital facilities and the land to a cancer hospital and real estate developer. As part of

this sale, the hospital would close certain programs that were mandated by its corporate purpose. Noting that the board failed or refused to consider other sale alternatives that would have allowed the hospital to continue as a specialty hospital in its chosen fields, the court found the board breached its duty of obedience, holding that “the proposed use of the assets involves a new and fundamentally different corporate purpose.”<sup>53</sup>

- *Agudist Council of Greater N.Y. v. Imperial Sales Co.* A synagogue’s sale of its property housing a senior center was invalidated because preservation of a service for seniors was an explicit organizational purpose.<sup>54</sup>
- *Matter of 51-53 W. 129th St. HDFC v. Attorney General of the State of N.Y.* Two not-for-profit Housing Development Fund Companies petitioned the Supreme Court, New York County, for approval under N-PCL § 511 to sell substantially all of their assets. The Supreme Court denied the petitions, and the Appellate Division, First Department, unanimously affirmed. Although the purchase prices were commercially reasonable, the court held that the corporations’ purpose, the provision of low-income housing, was “clearly served better by disapproval,” because both proposed sales were to the same for-profit landlord, whereas disapproval would result in the properties being transferred to qualified third-party, low-income landlords.<sup>55</sup>
- However, *In the Matter of the Application of Sculpture Ctr., Inc.*, the New York Supreme Court allowed the sale of a building belonging to the Friends of the Sculpture Center, as the proceeds were only to be used to buy a larger building in a different location, thus preserving the organization’s purpose.<sup>56</sup>

## IV. STANDARDS OF JUDICIAL REVIEW

New York applies two tiers of review for evaluating a director’s decision making: the business judgment rule and entire fairness.<sup>57</sup> The standard of review depends on the relationship of the directors to the particular matter at hand, and varies based on whether the members of the board:

- Were disinterested and independent (in which case the business judgment rule likely applies); or
- Confronted conflicts of interests (in which case entire fairness likely applies).

### 4.1 The Business Judgment Rule

The business judgment rule is the default standard of review in New York and protects director decision-making from second-guessing by the courts. The business judgment rule creates a presumption that “in making a business decision the directors of a corporation acted on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company.”<sup>58</sup>

In order to challenge a decision made by the board, the party challenging the decision must overcome the presumption of director disinterestedness and independence by showing a breach of the duty of care or loyalty, such as bad faith, fraud, or self-dealing. If the party challenging a decision fails to overcome that presumption, then the business judgment rule applies and a court will not examine the merits of the underlying business decision.<sup>59</sup> This rule reflects New York’s longstanding belief that businesspeople, not courts, are better positioned to know what is in the best interest of the organizations they manage. The business judgment rule has been recognized and accepted by New York courts in the context of not-for-profit organizations.<sup>60</sup>

- *Consumers Union of U.S., Inc.* (New York Court of Appeals) (rejecting challenge to conversion of defendant entity from a not-for-profit to a for-profit corporation and stating that, even if New York statutes expressly permitting such conversion did not preempt plaintiff’s challenge, “the business judgment rule . . . bars plaintiffs’ claims”).<sup>61</sup>

- *Higgins v. NYSE* (dismissing challenge to the proposed merger of the NYSE and Archipelago and breach of fiduciary duty claims against NYSE’s board and CEO and holding that, under *Consumers Union*, the business judgment rule protects decisions made by disinterested and independent directors of a not-for-profit organization).<sup>62</sup>

New York courts have also applied the business judgment rule in cases involving residential cooperative boards, religious corporations, and educational institutions regulated by the New York State Board of Regents.<sup>63</sup>

## 4.2 The Entire Fairness Standard

Where a board lacks a majority of disinterested and independent directors, as well as in other circumstances where there may be conflicts in a decision or transaction, courts will review such decision or transaction under the more onerous entire fairness standard of review.<sup>64</sup> Whereas courts defer to the decisions made by directors where the business judgment rule applies, the opposite is true under entire fairness: “the burden shifts to the interested directors . . . to prove good faith and the entire fairness of [their decision].”<sup>65</sup> Among other things, courts may look to see whether directors were candid in disclosing all material facts known to them, including any potential conflicts of interests they may have. Courts may also examine the substantive fairness of a transaction into which the not-for-profit enters, including conducting inquiries into the timing of the transaction, the nature and extent of any negotiations that preceded the transaction, and the “fair value” of the transaction.<sup>66</sup> Because these inquiries are fact intensive and because the board bears the burden of proving the fairness of the transaction, entire fairness cases generally cannot be dismissed on the pleadings. Winning these cases often requires going to trial, making entire fairness claims among the most expensive and difficult type of cases to defend.

- *Spitzer v. Schussel* (denying motion to dismiss and refusing to apply the business judgment rule where plaintiff alleged facts showing “bad faith and self dealing, or decisions affected by inherent conflicts of interest”).<sup>67</sup>

## V. POTENTIAL LIABILITIES OF NOT-FOR-PROFIT DIRECTORS & OFFICERS

### 5.1 Enforcement of Duties and Liabilities

Unlike in for-profit corporations where stockholders (among others) are capable of enforcing director and officer duties and liabilities, there is no comparable constituency in a not-for-profit corporation.<sup>68</sup> Accordingly, the N-PCL identifies the following persons as potential enforcers of director and officer duties and liabilities:

- The Attorney General,<sup>69</sup>
- The corporation itself,<sup>70</sup> or
- On behalf of the corporation: any director or officer of the corporation;<sup>71</sup> a receiver, trustee in bankruptcy, or judgment creditor;<sup>72</sup> a member of the corporation, in limited derivative cases;<sup>73</sup> or, if the certificate of incorporation or by-laws so provide, by any holder of a subvention certificate or any other contributor to the corporation of cash or property of the value of \$1,000 or more.<sup>74</sup>

In addition, the IRS and other government agencies may also play a role in enforcing director and officer duties, including through “cooperative prosecution” among multiple agencies.

#### A. The Attorney General

In recent years, in the not-for-profit arena, the Attorney General has been the primary enforcement agent.<sup>75</sup> In addition to being empowered to seek the dissolution of the corporation in certain instances,<sup>76</sup> the Attorney General

may sue not-for-profit directors and officers for their misconduct or breaches of fiduciary duty under several statutory provisions:<sup>77</sup>

- N-PCL § 112 (power to initiate an action or special proceedings against directors or officers);
- N-PCL § 715 (power to enjoin, void or rescind a related party transaction, and/or seek restitution, an account of profits, director and officer removal and other penalties);
- N-PCL § 719 (liability of directors in certain cases); and
- N-PCL § 720 (power to initiate suits against directors and officers seeking certain types of relief).

In addition, the Attorney General has authority under the N-PCL to regulate fundamental changes and to play a role in overseeing major developments and transactions at a not-for-profit corporation which require approval of the Attorney General or the Supreme Court of the State of New York, such as:

- Amendments to certificates of incorporation that change an organization's purpose;<sup>78</sup>
- Sale, lease, exchange, or other disposition of all or substantially all the assets of the organization;<sup>79</sup>
- Mergers and consolidations;<sup>80</sup> and
- Dissolution.<sup>81</sup>

This oversight can lead to an investigation of whether directors and officers have satisfactorily discharged their duties in deciding to dispose of some or all of the organization's assets.

- *Manhattan Eye, Ear & Throat Hospital and Mem'l Sloan Kettering Cancer Center et al. v. Eliot Spitzer*. "Since as a type B, i.e., charitable, corporation, Manhattan Eye, Ear & Throat Hospital ('MEETH') does not have shareholders, the Attorney General, acting as *parens patriae*, is statutorily involved whenever such a charity seeks to dispose of all, or substantially all, of its assets, as MEETH resolved to do."<sup>82</sup>

## B. The Internal Revenue Service

The IRS has an important role to play in policing not-for-profit organizations and their directors and officers, using intermediate sanctions or revocation of tax-exempt status as a means of encouraging not-for-profit directors and officers to fulfill their fiduciary duties.<sup>83</sup>

## C. Cooperative Prosecution

A not-for-profit organization whose directors are accused of violating their duties may face cooperative prosecution by several entities, including the Attorney General, the IRS, and any other regulatory body that has oversight of the corporation. For example:

- *Kamehameha Schools* (an educational not-for-profit corporation whose board violated its duties). The IRS, instead of simply imposing sanctions, cooperated with the Hawaii Attorney General in formulating an agreement with Kamehameha mandating implementation of a new governance regime and on the payment of a fine imposed by the Hawaii Attorney General.<sup>84</sup>
- *Comm. to Save Adelphi v. Diamandopoulos, et al.* The Board of Regents of the State of New York and the New York Attorney General instituted simultaneous actions.<sup>85</sup>

## 5.2 Liability of Directors in Certain Cases

### A. N-PCL § 719

In addition to the general fiduciary duties of care and loyalty discussed above, N-PCL § 719 provides for certain situations relating to financial decision-making/fiscal management in which directors who vote for or concur in the action can be “jointly and severally liable to the corporation” for any damages that arise from the decision.<sup>86</sup> These specifically enumerated areas include:

- **Cash or Property Distributions.** Any distribution of the corporation’s cash or property to members, directors or officers, other than a distribution permitted under N-PCL § 515 (such as the payment of reasonable compensation), may create liability.<sup>87</sup> Dividends are prohibited, but certain distributions of cash or property are authorized upon the corporation’s dissolution or final liquidation.<sup>88</sup>
- **Security Redemptions.** Any redemption of capital certificates, such as bonds or security interests, member’s capital contributions, or subvention certificates, may give rise to liability unless statutory prescriptions are followed.<sup>89</sup>
- **Interest Payments.** Payment of fixed or contingent periodic sums to the holders of subvention certificates or of interest to the holders or beneficiaries of bonds to the extent such payment is contrary to N-PCL §§ 504 or 506.<sup>90</sup>
- **Dissolution and Distribution of Assets.** Dissolution must be accomplished according to statute.<sup>91</sup> A failure to pay for all known liabilities of the corporation could create liability. Dissolution is covered in N-PCL Article 10 and Article 11.
- **Corporate Loans.** Corporate loans to directors and officers are illegal in most cases.<sup>92</sup> They are discussed in more detail below.

Notably, if a director is present at a board or committee meeting where an action is taken and such action does not comply with the statutes listed above, a director’s *concurrence is assumed unless his or her dissent is recorded* in the minutes of the meeting or otherwise delivered in writing.<sup>93</sup> Further, if a director is not present at the relevant meeting, he or she is assumed to concur unless dissent is delivered or sent by registered mail or filed in the minutes of the proceedings, within a reasonable time after learning of such action.<sup>94</sup>

In circumstances where liability is found, a director against whom a claim is successfully made is entitled to contribution from other concurring directors.<sup>95</sup>

### B. Loans to Directors

N-PCL § 716 prohibits loans from a not-for-profit corporation to its directors, officers, or key persons, or to any corporation, firm, or association in which one or more of the non-profit’s directors, officers, or key persons are directors, officers, or key persons or hold a substantial financial interest.<sup>96</sup> A loan that violates § 716 is considered a violation of the director’s duty to the corporation.<sup>97</sup>

- Exceptions:
  - Loans through the purchase of bonds, debentures or similar obligations of the type customarily sold in public offerings or through ordinary deposit of funds in a bank.<sup>98</sup>
  - Loans between two charitable organizations. However, directors should inform themselves of and must properly resolve and document any potential conflicts of interest, such as a director who serves on both boards.<sup>99</sup>

### C. N-PCL § 715 – Related Party Transactions

The Revitalization Act revised N-PCL § 715 to address “related party transactions.”<sup>100</sup> Under the Revitalization Act, the board of a New York not-for-profit (or an authorized board committee (the “Committee”)) must determine that a related party transaction is fair, reasonable and in the corporation’s best interest at the time of such determination.<sup>101</sup> Further, any director, officer or “key person”<sup>102</sup> who has an interest in a related party transaction must disclose in good faith to the board, or the Committee, the material facts concerning their interest. In addition, for transactions involving a charitable organization in which a related party has a “substantial financial interest” (which is not defined in the N-PCL), boards or Committees must follow certain procedural requirements, including consideration of alternative transactions to the extent available, obtaining majority board or committee approval and contemporaneously documenting the board or Committee’s considerations and decision.<sup>103</sup> Interested officers and directors may not participate in deliberations or voting relating to the transaction at issue; however, they may be requested to present information concerning the transaction at a board or committee meeting prior to the commencement of deliberations or voting relating thereto.<sup>104</sup>

The Revitalization Act’s definition of a “related party transaction” allows a transaction with a related party to proceed without board review if the transaction: (i) is of limited monetary value; (ii) would not usually be reviewed by the board in the ordinary course of business and is available to others on the same or similar terms; or (iii) provides a charitable benefit to a member of a charitable class where the benefit is available to others on similar terms.<sup>105</sup> The Revitalization Act also provides for certain defenses against claims brought by the attorney general or any other person or entity that a related party transaction violated its approval requirements, provided that, among other things, the transaction was “fair, reasonable, and in the corporation’s best interest at the time the corporation approved the transaction.”<sup>106</sup>

The Revitalization Act also requires that all New York not-for-profit corporations – regardless of size – have a conflict of interest policy applicable to directors, officers, and key persons. While some not-for-profits may have previously adopted a conflict of interest policy, disclosure of which is required by IRS Form 990, the Revitalization Act expressly mandates the adoption of such policy.<sup>107</sup> The Revitalization Act requires that such policy, among other things:

- Define the circumstances that constitute a conflict;<sup>108</sup>
- Include procedures for disclosing conflicts, possible conflicts to the board or to a committee of the board, and procedures for the board or committee to determine whether a conflict exists;<sup>109</sup>
- Prohibit a conflicted person from participating in deliberations or voting or improperly influencing the vote on the matter giving the rise to the conflict;<sup>110</sup>
- Include procedures for disclosing, addressing and documenting related party transactions;<sup>111</sup> and
- Require directors to disclose to the corporation (upon joining the board and annually thereafter) any entities with which they are affiliated and with which the corporation has a relationship, and any corporate transactions possibly giving rise to a conflict for the director.<sup>112</sup> The board must oversee the adoption and implementation of, and compliance with, the policy.<sup>113</sup>

### D. Compensation of Directors and Officers

N-PCL § 202(a)(12) sets the standard for appropriate compensation of officers and directors:

“Each corporation, subject to any limitations provided in this chapter or any other statute or its certificate of incorporation, shall have power in furtherance of its corporate purposes . . . [t]o elect or appoint officers, employees and other agents of the corporation, define their duties, fix their

reasonable compensation and the reasonable compensation of directors . . . . Such compensation shall be *commensurate* with services performed.”<sup>114</sup>

N-PCL § 515(b) further provides that a “corporation may pay compensation in a reasonable amount to members, directors, or officers for services rendered.”

Commentators and courts have focused on the “commensurate” language in the statute. Given the not-for-profit ethos of charitable organizations, “[t]he clear implication is that legislators are less tolerant of excessive executive compensation in the nonprofit arena than they are in the business community.”<sup>115</sup> Therefore, it is important for boards to exercise diligence in reviewing and approving compensation programs.

Furthermore, the IRS recently imposed stricter disclosure requirements on executive pay. Any organization filing a Form 990 must list all of its current officers, directors, and trustees, regardless of whether any compensation was paid to such individuals. The organization must also list up to 20 current employees who satisfy the definition of “key person” (persons other than directors or officers who hold positions to exercise substantial influence over the organization),<sup>116</sup> and its five current highest-compensated employees with reportable compensation of at least \$100,000 from the organization and related organizations who are not officers, directors, trustees, or key persons of the organization.<sup>117</sup>

In addition, the IRS recently added a requirement to Form 990 to require disclosure relating to embezzlement and fraud. Specifically, Form 990 requires that the organization report if it became “aware during the year of a significant diversion of the organization’s assets.” The IRS considers a diversion to be “significant” if the gross value of all diversions exceeds the lesser of \$250,000 or 5% of the organization’s receipts or assets for its tax year or as of the end of the tax year, respectively.<sup>118</sup>

### E. Key Director Liability Cases: *Adelphi* and *United Way*

The following cases—*Adelphi* and *United Way*—illustrate the circumstances in which directors of a not-for-profit can be found liable for breaching their fiduciary duties.

#### *Adelphi*

In *Comm. to Save Adelphi v. Diamandopoulos*,<sup>119</sup> the board of trustees of Adelphi University breached its duty of care in setting the salary and additional compensation of the University President, Dr. George Diamandopoulos, from 1987 to 1995. Specifically, Diamandopoulos received raises of approximately \$30,000 per year starting from \$95,000 in 1985, so that by 1996 his base salary reached \$330,750. In addition to the base salary, Diamandopoulos received a life insurance policy of \$1.25 million, an annual \$60,000 contribution to Diamandopoulos’ pension fund, a contribution to a sabbatical year salary at one sixth of his base salary, which was approximately \$55,000, an option to buy an apartment in New York City for \$905,000 (a 17% discount from the price at which Adelphi acquired it ten months earlier), free rent worth \$36,000 at a house near Adelphi, operating costs for the two residences at approximately \$100,000, and other perks. By 1996, the estimated total compensation when all of these factors were taken into account was \$837,113.

Except for one year, the full board of trustees never reviewed or approved the President’s compensation. Instead, his salary and additional compensation were set by a three-member ad-hoc committee, who approved the compensation package without explanation of Diamandopoulos’ contributions or even an evaluation of how his performance rated against the academic goals of the University. The committee did not consider salaries of presidents at comparable institutions.

In reviewing the decision, the Board of Regents concluded that Diamandopoulos’ salary was not commensurate with the work he performed for Adelphi University as mandated by N-PCL § 202(a)(12). The Board of Regents found that the trustees breached their duty of care by failing to take the necessary steps to inform themselves of the compensation decisions and for awarding Diamandopoulos compensation between 1993 and 1996 that was greater

than the value of the services he performed. Thus, the Regents then removed eighteen of nineteen trustees for breaching their fiduciary duty of care.

In addition, Diamandopoulos and another trustee, Ernesta Procope, were found to have violated their duty of loyalty. Specifically, Procope received personal benefits from certain University insurance contracts. Procope owned and operated E.G. Bowman, Inc., a licensed broker of insurance policies. In 1986, the University's insurer threatened to cancel its coverage. The board of trustees formed a committee, chaired by Procope on account of her expertise in the insurance industry, which was charged with finding a new insurer for Adelphi. Rather than conducting an arms-length search for a new insurer, Procope installed E.G. Bowman as the insurance broker for the University. Diamandopoulos personally authorized the use of Procope's company and explained to the board of trustees that its services were free of charge when, in fact, Diamandopoulos arranged for E.G. Bowman to receive fees of \$1,227,949 in 1987. These terms were never disclosed to the board of trustees and thus the guidelines set forth in N-PCL § 715 for implementation of interested director transactions that were then in effect were not followed. Moreover, this arrangement occurred while Procope was on the committee responsible for setting Diamandopoulos' compensation. Although the arrangement that E.G. Bowman brokered may have been fair, the fact that Procope purposefully used her directorship for personal gain, and did not put the University's needs first by searching for the best available option, created a breach of the duty of loyalty for which she and Diamandopoulos were found liable. Diamandopoulos was also found to have breached his duty of loyalty on account of the other conduct described above.

In the state counterpart to the Board of Regents decision, the Attorney General sued the removed trustees for damages relating to their breaches of the duties of care and loyalty.<sup>120</sup> There was no cooperation between the Attorney General and the Board of Regents in sanctioning the former trustees or the University. However, the New York Supreme Court did incorporate the Board of Regents' investigation, findings, and judgment in its decision. The Attorney General sought damages from the trustees who benefited from the improper payments and interested transactions, as well as from those who allowed the payments. The ousted trustees settled the criminal action by paying \$1.23 million to the University and assuming \$400,000 in legal fees, and Diamandopoulos paid approximately \$750,000 in damages to the University.<sup>121</sup>

#### *United Way*<sup>122</sup>

The *United Way* decision provides a “virtual roadmap for what to avoid in not-for-profit governance.”<sup>123</sup>

William Aramony, the CEO of the United Way of America, and other United Way officials, were found to have engaged in self-dealing and to have breached their fiduciary duties of care and loyalty. Aramony used company funds for chauffeur service, to buy personal gifts, to take vacations and monthly flights to Florida, and to pay his girlfriend a salary despite that fact that she worked only one or two days a month. Aramony arranged these payments through Thomas Merlo, the CFO hired by Aramony, by paying him large bonuses. These bonuses were not based on work performed; rather, they were vehicles through which the executives were able to appropriate company funds for private use. In one instance, Merlo received a bonus of \$300,000, and subsequently allocated \$89,000 to Aramony's girlfriend.<sup>124</sup> In addition, Aramony bought a condominium in Florida with United Way funds for \$125,000, funded through Steven Paulachak, another Aramony appointee in control of a subsidiary of United Way, ostensibly for use for company functions, but which was in fact for personal use.

Merlo purchased annuity funds in the name of United Way and then, using his position as CFO, caused them to be transferred to himself as annuitant. In two such schemes, he defrauded United Way out of approximately \$500,000. The court found that all three officials—Aramony, Merlo, and Paulachak—had violated their duties of care and loyalty.<sup>125</sup> Additionally, the court found that the United Way board of directors breached its fiduciary duty of care by not staying sufficiently apprised of the organization's affairs, noting the following in its decision:

- There were only two board meetings per year and to prepare for those meetings, board members reviewed briefing books created by Aramony that lacked substantial financial or strategic analysis of the organization or of any of its planned initiatives;

- Directors did not seek to investigate the company’s practices or to insist on greater disclosure by management; and
- The board of directors did not investigate whether certain spin-offs were necessary or even financially viable and beneficial.

Concurrent with the convictions above, the board’s conduct became the subject of an investigation by the New York Attorney General and was resolved in an out-of-court settlement pursuant to which the board was required to institute oversight procedures and to become more informed about the workings of the business.<sup>126</sup>

### 5.3 Liability of Directors and Officers to Third Parties

The liabilities of directors and officers to third parties are governed by N-PCL § 720-a.

- *Standard.* Gross negligence or intentional conduct.
  - A person serving without compensation as a director or officer of a not-for-profit entity shall not be liable to persons other than the not-for-profit entity, on the sole basis of the director’s conduct in the execution of his or her office, unless such conduct, with respect to the person asserting liability, constituted gross negligence or was intended to cause the resulting harm to the person asserting such liability.<sup>127</sup>
  - As a result of such a rigorous standard, directors and officers are rarely liable to third parties based on their corporate actions.

## VI. LIABILITIES IMPOSED BY THE IRS: INTERMEDIATE SANCTIONS

### 6.1 Background

I.R.C. § 501(c)(3) proscribes any private inurement or benefit as a condition of tax-exempt status.

- Private inurement and benefit occurs when an officer or director profits financially or receives an improper advantage from the corporation’s actions or existence.<sup>128</sup>

On January 23, 2002, I.R.C. § 4958 was enacted, creating intermediate sanctions, a mechanism short of revocation of exempt status to punish those who benefit or inure at the expense of their organizations. However, the imposition of intermediate sanctions does not preclude a revocation of tax-exempt status if the IRS deems it necessary.<sup>129</sup>

### 6.2 Excess Benefit Transactions

I.R.C. § 4958 classifies certain transactions involving “disqualified persons” as “excess benefit transactions,” imposing a two-tiered excise tax on individuals who profit from those transactions.

- An “excess benefit transaction” is a transaction in which an economic benefit is provided by an applicable tax-exempt organization, directly or indirectly, to a “disqualified person,” where the value of the economic benefit provided exceeds the value of the consideration (including the performance of services) that is received.<sup>130</sup>

The following may be seen as excess benefit transactions:

- Certain sales of property;
- Unreasonable compensation;<sup>131</sup>

- Direct and indirect compensation or enrichment (through a controlled intermediary);<sup>132</sup> and
- Certain gifts by sponsors or other entities in a transaction to directors or officers.

### 6.3 Definition of Disqualified Persons

The I.R.C. definition of “disqualified person[s]” includes:

- A person who was, at any time during the five-year period ending on the date of such transaction, in a position to exercise substantial influence over the affairs of the organization;
- A member of the family of such an individual; and
- A person who controls at least 35% of the transacting or benefiting entity.<sup>133</sup>

Treasury Regulation 53.4958-3(c) defines a “person in a position to exercise substantial influence” to mean:

- Any member of the organization’s governing body, presidents, CEOs, treasurers, CFOs and any other individual regardless of title who either “has ultimate responsibility for implementing the decisions of the governing body or for supervising the management” or “has ultimate responsibility for managing the finances of the organization;”<sup>134</sup> or
- Certain other persons can have “substantial influence,” depending on specific facts and circumstances, such as whether the person is a founder or a significant contributor to the organization.<sup>135</sup>

### 6.4 Taxes on Disqualified Persons and Managers Who Engage in Excess Benefit Transactions

A “disqualified person” who engages in an “excess benefit transaction” is liable for excise taxes under I.R.C. § 4958 as follows:

- An initial tax of 25% of the excess benefit; and
- If the excess benefit is not returned within a reasonable time, then the IRS may levy an additional tax of 200% of the excess benefit on the offending individual.<sup>136</sup>

Additionally, a manager who does not fall within the disqualified person definition can still be taxed, albeit at a lower rate, if that manager is deemed to have knowingly participated in an excess benefit transaction.<sup>137</sup> A manager may be deemed to have “knowingly participated” if the manager had actual knowledge that the transaction would be an excess benefit transaction and either affirmatively approved the transaction or did not oppose the transaction.<sup>138</sup> A manager who knowingly participates in an excess benefit transaction and where such participation was willful and/or not the result of reasonable cause (such as reliance upon a written opinion of counsel) will be taxed at 10% of the excess benefit.<sup>139</sup>

#### *Exceptions to the Disqualified Persons Rule*

- **The “First Bite” Exception.** I.R.C. § 4958 does not apply to payments that are made pursuant to fixed, objective terms specified in a contract before the person was in a position to exercise substantial influence.<sup>140</sup> Once the person has achieved substantial influence, any future payments are reviewable.<sup>141</sup>
- **Reliance on a Professional Opinion Exception.** A manager’s participation in a prohibited transaction will ordinarily not be considered “knowing” if, after “full disclosure of the factual situation to an appropriate professional, the organization manager relies on a reasoned written opinion of that

professional with respect to elements of the transaction within the professional’s expertise.”<sup>142</sup> “Appropriate professionals” include legal counsel (including in-house legal counsel) or certified public accountants or certified public accounting firms with expertise regarding the relevant tax matters.<sup>143</sup>

- **“Safe Harbor” Rebuttable Presumption.** The organization, by taking certain steps, can create a rebuttable presumption that certain compensation agreements or property transfers were reasonable.<sup>144</sup> These steps include approving the compensation in advance through an authorized body, relying upon appropriate data to justify the compensation, and adequately documenting the determination.<sup>145</sup>
- **Advance Decision.** The board or a committee composed entirely of individuals who do not have a conflict of interest with respect to the transaction must make an advance decision regarding the transaction.<sup>146</sup>
- **Comparability Data.** The decision-making body must obtain and rely upon appropriate comparability data in making its decision.<sup>147</sup> Appropriate data may include:<sup>148</sup>
  - Appraisals;
  - Other offers;
  - Availability of similar services in the geographic area of the organization; and
  - Comparable compensation schemes.
- **Disinterested Participation.** Disqualified persons cannot participate in the discussion or the vote, but may be present to answer questions (although they may not be present during any debate or vote).<sup>149</sup>
- **Document the Decision.** The board or committee must document the basis for its decision within 60 days of the action taken or before their next meeting.<sup>150</sup> Documentation must include:
  - Terms of the transaction and date approved;
  - Members of the board or committee present when the transaction was approved, and those who voted on it;
  - Comparability data relied upon and how it was obtained;
  - Actions taken with respect to consideration of the transaction by a board or committee member who has a conflict of interest with respect to the transaction; and
  - The basis for determining the compensation or payment if the board or committee determines that what is reasonable or fair market value is higher or lower than the range of comparable data obtained.<sup>151</sup>

However, if the organization reimburses excise taxes, pays personal expenses, offers to engage in transactions not at fair market value, or pays insurance premiums for excise tax liability for the individual, such payments are generally considered excess benefits unless they are included in the person’s compensation package, which, in turn, is subject to the reasonableness requirement.<sup>152</sup>

## 6.5 Example of Application of Intermediate Sanctions

### *Kamehameha Schools*

The settlement imposed intermediate sanctions of only \$40,000 per trustee even though the IRS had originally sought \$6.5 million.<sup>153</sup> However, contingent on that settlement was the agreement that the organization would pay a \$25 million fine to the state of Hawaii. Additionally, by the terms of the settlement, it was agreed that the implicated trustees would resign and that the organization would follow operational parameters presented in the Closing Agreement in order to retain its exempt status.<sup>154</sup>

## VII. INDEMNIFICATION AND INSURANCE FOR NOT-FOR-PROFIT DIRECTORS AND OFFICERS

### 7.1 Indemnification

N-PCL §§ 721–726 provide the statutory framework for indemnification where a director acts:

- In good faith;
- For a purpose that he or she reasonably believed to be in—or, in the case of service of any other corporation, not opposed to—the best interests of the corporation; and
- In criminal actions or proceedings, with no reasonable cause to believe that his or her conduct was unlawful.<sup>155</sup>

Directors and officers *must* be indemnified if they have succeeded in defending a civil or criminal action or proceeding.<sup>156</sup> The N-PCL allows a not-for-profit corporation to provide indemnification rights and requirements beyond those mandated by statute in the certificate of incorporation or in the bylaws as long as the additional indemnification provisions are not contrary to the indemnification requirements of the N-PCL.<sup>157</sup>

A corporation is prohibited from indemnifying a director where it has been established by an adverse final judgment that his or her acts “were committed in bad faith or were the result of active and deliberate dishonesty and were material to the cause of action so adjudicated, or that he personally gained in fact a financial profit or other advantage to which he was not legally entitled.”<sup>158</sup>

### 7.2 Insurance

Indemnification provisions in the bylaws or certificate of incorporation provide protection only if, and to the extent that, the organization has the financial capability to make indemnification payments. Many organizations purchase indemnity insurance (often called directors and officers insurance) to reassure potential directors that their costs will be covered in case of a claim.<sup>159</sup> According to the N-PCL,<sup>160</sup> a not-for-profit corporation can obtain insurance to:

- Reimburse itself for any indemnification costs;
- Indemnify directors and officers for permissible costs; and
- Indemnify directors and officers for those costs that may not be allowed under the indemnification provisions,<sup>161</sup> provided that such a contract includes the required deductible and co-insurance payments.<sup>162</sup>

## VIII. VOLUNTEER PROTECTION ACT OF 1997

The Volunteer Protection Act<sup>163</sup> is a federal statute that provides liability protection for volunteers of not-for-profit organizations for acts or omission on behalf of the organization if:

- The volunteer was acting within the scope of the volunteer's responsibilities at the time of the act or omission;
- If appropriate or required, the volunteer was properly licensed, certified, or authorized by the appropriate authorities for the activities or practice in the State in which the harm occurred;
- The harm was not caused by willful or criminal misconduct, gross negligence, reckless misconduct, or a conscious, flagrant indifference to the rights or safety of the individual harmed; and
- The harm was not caused by the operating of a vehicle for which the State requires the operator or owner to possess a license or maintain insurance.<sup>164</sup>

This Act preempts state law to the extent that such laws are inconsistent. However, state laws conditioning limited liability for volunteers cannot be inconsistent with this Act. For example, state law may require not-for-profit organizations to adhere to risk management procedures or to maintain insurance or other financially secure financial sources for recovery by individuals who suffer harm as a result of actions taken by a volunteer.

New York has abolished charitable immunity for not-for-profit corporations because it is contrary to the public policy of the state and because insurance made full compensation possible without any significant diminution of a charitable organization's funds.<sup>165</sup> New York does, however, continue to provide certain limited volunteer protection for volunteer fire fighters,<sup>166</sup> volunteers of national ski patrol<sup>167</sup> and the trustees of and certain other people associated with the City University of New York.<sup>168</sup>

ENDNOTES

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<sup>1</sup> References herein to “directors” should be construed as including “trustees” as well.

<sup>2</sup> I.R.C. § 501(c)(3).

<sup>3</sup> N-PCL § 102(a)(5).

<sup>4</sup> N-PCL § 201. There are different types of not-for-profit corporations. Prior to its amendment by the Revitalization Act, which became effective July 1, 2014, the N-PCL divided not-for-profit corporations into Type A, B, C or D. **Type A** classified corporations formed for non-business purposes including, but not limited to: civic, patriotic, political, social, fraternal, athletic, agricultural, horticultural, animal husbandry, and for a professional, commercial, trade or service organization. **Type B** classified corporations formed for non-business purposes including but not limited to: charitable, educational, religious, scientific, literary, cultural or for the prevention of cruelty to children or animals. **Type C** classified corporations formed for a lawful business purpose to achieve a lawful public or quasi-public objective. **Type D** classified corporations formed under other corporate law of the state. Under the Revitalization Act, New York not-for-profit corporations are no longer categorized as letter-type corporations, but are rather classified as charitable or non-charitable corporations. Under the Revitalization Act, “charitable corporation” is defined to mean “any corporation formed, or . . . deemed to be formed, for charitable purposes.” N-PCL § 102(a)(3-a). “Non-charitable corporation” is defined to mean “any [not-for-profit corporation] 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.” N-PCL § 102(a)(9-a). For New York not-for-profit incorporations incorporated before July 1, 2014, Type A not-for-profits are deemed non-charitable, Type B and C not-for-profits are deemed charitable, and Type D corporations are deemed either charitable or non-charitable, depending on the purposes as reflected in their existing charters. *See* N-PCL § 201.

<sup>5</sup> VICTORIA B. BJORKLUND, JAMES J. FISHMAN & DANIEL L. KURTZ, *NEW YORK NONPROFIT LAW AND PRACTICE: WITH TAX ANALYSIS* § 8.07(2) (2d ed. 2013).

<sup>6</sup> *Id.* at § 5.01.

<sup>7</sup> N-PCL § 701(b); BJORKLUND, *supra* note 6, at §6.05.

<sup>8</sup> *Scheuer Fam. Found., Inc. v. 61 Assocs.*, 179 A.D.2d 65, 70 (N.Y. App. Div. 1st Dep’t 1992).

<sup>9</sup> N-PCL § 717(a).

<sup>10</sup> BCL § 717(a).

<sup>11</sup> BJORKLUND, *supra* note 6, at §6.02(5).

<sup>12</sup> *Consumers Union of U.S., Inc. v. State*, 840 N.E.2d 68, 94 n.16 (N.Y. 2005) (Smith, J., dissenting) (quoting NEW YORK STATE ATTORNEY GENERAL, *THE REGULATORY ROLE OF THE ATTORNEY GENERAL’S CHARITIES BUREAU 4* (2003)).

<sup>13</sup> *Id.*

<sup>14</sup> AMERICAN BAR ASSOCIATION, *COMMITTEE ON CORPORATE LAWS, CORPORATE DIRECTOR’S GUIDEBOOK 19* (7th ed. 2020).

<sup>15</sup> *Id.*

<sup>16</sup> BJORKLUND, *supra* note 6, at §6.02(2)(b).

<sup>17</sup> *Id.*

<sup>18</sup> *Hoye v. Meek*, 795 F.2d 893, 896 (10th Cir. 1986).

<sup>19</sup> 3A FLETCHER CYC. L. CORPS. § 1034.70.

<sup>20</sup> MODEL NONPROFIT CORP. ACT § 8.31(a)(2)(4), as amended.

<sup>21</sup> BJORKLUND, *supra* note 6, at §6.02(5).

<sup>22</sup> *In re Comverse Tech., Inc.*, 56 A.D.3d 49, 56 (N.Y. App. Div. 1st Dep’t 2008); *see also Mason-Mahon v. Flint*, 166 A.D.3d 754, 759 (N.Y. App. Div. 2d Dep’t 2018) (“The long-standing rule is that a director does not exempt himself from liability by failing to do more than passively rubber-stamp the decisions of the active managers”) (internal citations and quotations omitted).

<sup>23</sup> N-PCL § 717(b).

<sup>24</sup> N-PCL § 717(b)(1).

<sup>25</sup> N-PCL § 717(b)(2).

<sup>26</sup> N-PCL § 717(b)(3).

<sup>27</sup> N-PCL § 717(b) (Permitting reliance “so long as in so relying they shall be acting in good faith and with that degree of care specified in paragraph (a) of this section” and providing that “Persons shall not be considered to be acting in good faith if they have knowledge concerning the matter in question that would cause such reliance to be unwarranted.”); *see e.g., People by James v. Nat’l Rifle Ass’n of Am., Inc.*, 74 Misc. 3d 998, 1032 (N.Y. Sup. Ct. 2022) (holding that under N-PCL § 717(b) “[p]ersons shall not be considered to be acting in good faith if they have knowledge concerning the matter in question that would cause such reliance to be unwarranted,” and finding that allegations that the NRA’s General Counsel was aware of financial mismanagement concerns raised by whistleblowers and board members and failed to present necessary information to the Audit Committee raised fact questions about whether the officer acted in good faith when signing the NRA’s annual CHAR 500 reports).

<sup>28</sup> BJORKLUND, *supra* note 6, at §6.02(5).

<sup>29</sup> *Id.* (citing *Davidowitz v. Edelman*, 153 Misc. 2d 853, 857 (N.Y. Sup. Ct. 1992).

<sup>30</sup> *See, e.g., People by James v. Roman Catholic Diocese of Albany*, 87 Misc.3d 694, 726 (N.Y. Sup. Ct. 2025) (holding that whether officers and directors of a not-for-profit hospital acted in good faith in administering a pension plan remained a question of fact precluding summary judgment, particularly where they selectively followed actuarial and legal advice).

<sup>31</sup> UPMIFA has been codified in New York at N-PCL §§ 550–558 (“NYPMIFA”). *See also* N-PCL §§ 513–514 regarding investment authority, delegation of investment management and use of restricted funds. For additional information on NYPMIFA, *see A Practical Guide to the New York Prudent Management of Institutional Funds Act*, OFF. OF THE ATT’Y GEN. CHARITIES BUREAU (Mar. 2011), available at <https://ag.ny.gov/sites/default/files/regulatory-documents/mifa-funds.pdf>.

<sup>32</sup> N-PCL § 552(c)(1).

<sup>33</sup> N-PCL § 552(e)(1).

<sup>34</sup> N-PCL § 552(e)(2).

<sup>35</sup> N-PCL § 552(f) (this requirement to have a written investment policy is a requirement of NYPMIFA that is not in the UPMIFA).

<sup>36</sup> N-PCL § 552(c)(2).

<sup>37</sup> N-PCL § 552(e)(4).

<sup>38</sup> N-PCL § 552(e)(4) (this requirement to review decisions to not diversify is a requirement of NYPMIFA that is not in the UPMIFA).

<sup>39</sup> N-PCL § 552(e)(5).

<sup>40</sup> N-PCL §§ 514 and 554 (the requirement that contracts be terminable upon no more than 60 days’ notice is a requirement of NYPMIFA that is not in the UPMIFA).

<sup>41</sup>AMERICAN BAR ASSOCIATION, NONPROFIT ORGANIZATIONS COMMITTEE, GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS 43 (2012) (the “Nonprofit Guidebook”).

<sup>42</sup> *Consumers Union*, 840 N.E.2d at 94 n.16.

<sup>43</sup> *Solash v. Telex Corp.*, 1988 WL 3587, at \*7 (Del. Ch. Jan. 19, 1988).

<sup>44</sup> *Higgins v. New York Stock Exch., Inc.*, 806 N.Y.S.2d 339, 357 (Sup. Ct. 2005) (explaining that directors owe a fiduciary duty of loyalty, which is implicated whenever personal and corporate interests conflict).

<sup>45</sup> See *People v. Vdare Found., Inc.*, 2026 WL 788657 at \*3 (N.Y. Sup. Ct. Mar. 17, 2026) (denying motion to dismiss fiduciary duty claims against foundation directors who used charitable funds to purchase a personal residence, transferred foundation assets to a director-owned for-profit corporation, and failed to file required reports with the Attorney General disclosing self-interested transactions).

<sup>46</sup> See *Matter of People v Trump*, 66 Misc.3d 200, 204 (N.Y. Sup. Ct. 2019) (finding that a foundation director breached his fiduciary duty by allowing his political campaign to orchestrate a charitable fundraiser, direct the distribution of \$2,823,000 in foundation funds, and use both the fundraiser and the distribution of those funds to further his own political campaign).

<sup>47</sup> *Kavanaugh v. Kavanaugh Knitting Co.*, 123 N.E. 148, 151 (N.Y. 1919).

<sup>48</sup> *Id.* at 197; see also *People ex rel. Spitzer v. Grasso*, 50 A.D.3d 535, 546 (N.Y. App. Div. 1st Dep’t 2008) (applying *Kavanaugh*’s good faith standard to hold that a director and compensation committee chair of the New York Stock Exchange had a duty under N-PCL 717(a) to make compensation recommendations in the interest of the corporation, in good faith and with conscientious fairness).

<sup>49</sup> A not-for-profit corporation “shall have power in furtherance of its corporate purposes.” N-PCL § 202(a).

<sup>50</sup> The certificate of incorporation must note “the purpose or purposes for which [the not-for-profit corporation] is formed.” N-PCL § 402(a)(2).

<sup>51</sup> BJORKLUND, *supra* note 6, at §6.04(1).

<sup>52</sup> N-PCL § 511(a)(6) (emphasis added). See also N-PCL §511-a(b)(1), (c).

<sup>53</sup> *Manhattan Eye, Ear & Throat Hospital and Memorial Sloan Kettering Cancer Ctr. v. Spitzer* (“MEETH”), 715 N.Y.S.2d 575, 595 (N.Y. Sup. Ct. 1999).

<sup>54</sup> *Agudist Council of Greater N.Y. v. Imperial Sales Co.*, 158 A.D.2d 683, 684 (N.Y. App. Div. 2d Dep’t 1990).

<sup>55</sup> *51-53 W. 129th St. HDFC v. Att’y Gen.*, 95 A.D.3d 674, 675 (N.Y. App. Div. 1st Dep’t 2012).

<sup>56</sup> *In re Sculpture Ctr., Inc.*, 2001 WL 1568739, at \*4 (N.Y. Sup. Ct. Aug. 24, 2001).

<sup>57</sup> *In re Kenneth Cole Prods., Inc.*, 27 N.Y.3d 268, 274–276 (2016) (explaining the business judgment rule and entire fairness standard).

<sup>58</sup> STEPHEN A. RADIN, THE BUSINESS JUDGMENT RULE: FIDUCIARY DUTIES OF CORPORATE DIRECTORS, 42 (6th Ed., Vol. I 2009). (quoting *In re Walt Disney Co. Derivative Litig.*, 906 A.2d 27, 52 (Del. 2006)).

<sup>59</sup> See *F.D.I.C. v. Stahl*, 89 F.3d 1510, 1517 (11th Cir. 1996).

<sup>60</sup> See *Consumers Union.*, 840 N.E.2d at 87.

<sup>61</sup> *Id.*.

<sup>62</sup> *Higgins*, 806 N.Y.S.2d at 357.

<sup>63</sup> See, e.g., *Comm. to Save Adelphi v. Diamandopoulos* (Bd. of Regents of the Univ. of the State of N.Y. Decision Feb. 5, 1997).

<sup>64</sup> See, e.g., *Alpert v. 28 Williams St. Corp.*, 63 N.Y.2d 557, 570 (1984) (noting that “when there is an inherent conflict of interest, the burden shifts to the interested directors . . . to prove good faith and the entire fairness” of the transaction); *Stavroulakis v. Pelakanos*, 2018 WL 846677, at \* 11 (N.Y. Sup. Ct. Feb. 13, 2018) (“Simply put, where the defendants are either conflicted or have engaged in corporate waste, they have the burden of establishing entire fairness.”); *Spitzer v. Schussel*, 2007 WL 3133222, at \*8 (N.Y. Sup. Ct. Sept. 11, 2007) (“Where, however, there is a showing that a breach of fiduciary duty occurred, including evidence of bad faith and self dealing, or decisions affected by inherent conflicts of interest, judicial inquiry is triggered.”).

<sup>65</sup> *Alpert*, 473 N.E.2d at 26.

<sup>66</sup> *Id.* at 26-27.

<sup>67</sup> *Schussel*, 2007 WL 3133222, at \*8.

<sup>68</sup> *In the Matter of Herbert H. Lehman Coll. Found., Inc. v. Ricardo R. Fernandez et al.* (“*Lehman*”), 292 A.D.2d 227, 228 (N.Y. App. Div. 1st Dep’t 2002) (“[D]irectors of a not-for-profit corporation do not act on behalf of shareholders who control the corporation’s certificate of incorporation, and its board. They act on behalf of beneficiaries who have no direct voice in governing the corporation and must depend on the State to represent and protect their interests.”).

<sup>69</sup> N-PCL § 720(b).

<sup>70</sup> N-PCL § 720(b)

<sup>71</sup> N-PCL § 720(b)(1).

<sup>72</sup> N-PCL § 720(b)(2).

<sup>73</sup> N-PCL § 720(b)(3). In certain cases, a member may bring a derivative suit under N-PCL § 623.

<sup>74</sup> N-PCL § 720(b)(4).

<sup>75</sup> Three major cases in which the Attorney General has taken action as the enforcement agent are: *The People of the State of New York, by Eliot Spitzer v. Richard A. Grasso, Kenneth G. Langone, and the New York Stock Exchange* (“*Grasso*”), 816 N.Y.S.2d 863 (Sup. Ct. 2006) (motion to dismiss four of the six claims denied), *rev’d*, 836 N.Y.S.2d 40 (N.Y. App. Div. 1st Dep’t 2007) (noting that the New York State Attorney General lacked legal authority specifically with respect to non-statutory causes of action); *Vacco v. Diamandopoulos*, 715 N.Y.S.2d 269, 276 (Sup. Ct. 1998) (denying motion to dismiss given the directors’ failure to discharge duties in good faith); and *MEETH*, *supra* note 52, at 597 (denying sale given its failure to promote corporation’s purpose). More recently, the Attorney General succeeded in permanently barring a director of a not-for-profit corporation from serving in any capacity for a charitable entity after the New York supreme court sufficiently found, among other things, that the director had breached his fiduciary duty to a charitable organization under N-PCL § 717, where the director was found to have used charity assets for his personal expenditures. See *Schneiderman ex rel. People v. Lower Esopus River Watch, Inc.*, 975 N.Y.S.2d 369 (Sup. Ct. 2013). Additionally, in 2022, the Attorney General took still-ongoing action against the National Rifle Association of America and four of its officers, seeking to dissolve the organization, recover damages, and remove the officers from NRA employment. See *People by James v. National Rifle Assoc. of America, Inc.*, 165 N.Y.S.3d 234, 246–47 (N.Y. Sup. Ct. 2022).

<sup>76</sup> Elizabeth M. Guggenheimer, *Fiduciary Duties of Directors and Officers of Not-for-Profit Organizations: An Overview for Volunteer Attorneys*, Lawyers Alliance for New York, March 2000, at 14.

<sup>77</sup> *Id.* See also PROCEEDINGS BY ATTORNEY GENERAL, CARMODY-WAIT 2D NEW YORK PRACTICE WITH FORMS § 145:775 (2016).

<sup>78</sup> N-PCL § 804. See *Lehman*, *supra* note 66, at 229 (“By thus diluting the influence of the College and its president on the governance of the Foundation, in effect transforming the Foundation into an independent entity unaccountable to the College, the bylaw amendments changed the Foundation’s powers and purpose as enumerated in its certificate of incorporation. There can be no doubt that any like amendment to the certificate would require judicial approval on notice to the Attorney General.”).

<sup>79</sup> N-PCL §§ 510, 511.

<sup>80</sup> N-PCL § 907.

<sup>81</sup> N-PCL § 1002.

<sup>82</sup> *MEETH*, *supra* note 52, at 143 (citing N-PCL § 511); *see also Villager Capital Advisors, LLC v. Union Settlement Assoc., Inc.*, 2020 WL 4045961, at \*2 (N.Y. Sup. Ct. 2020) (“The sale [of assets] also required approval by both the Attorney General and the Supreme Court.”).

<sup>83</sup> Michael A. Shea, *Closing Agreement Shows IRS Position on the ‘Straight and Narrow’ of Organization Management*, 12 J.TAX’N EXEMPT ORGS. 24 (2000). *See also* I.R.C. § 4958 (imposing an additional tax on “excess benefit transaction[s] benefiting persons with influence over a tax-exempt organization).

<sup>84</sup> *Id.*

<sup>85</sup> *Comm. to Save Adelphi*, *supra* note 61.

<sup>86</sup> N-PCL § 719(a).

<sup>87</sup> N-PCL § 719(a)(1).

<sup>88</sup> N-PCL § 515.

<sup>89</sup> N-PCL § 719(a)(2). *See* N-PCL §§ 502, 504 and 506.

<sup>90</sup> N-PCL § 719(a)(3). *See* N-PCL §§ 504 and 506.

<sup>91</sup> N-PCL § 719(a)(4).

<sup>92</sup> N-PCL § 719(a)(5). *See also* N-PCL § 716.

<sup>93</sup> N-PCL § 719(b).

<sup>94</sup> *Id.*

<sup>95</sup> N-PCL § 719(c).

<sup>96</sup> N-PCL § 716.

<sup>97</sup> *Id.*

<sup>98</sup> *Id.*

<sup>99</sup> *Id.*

<sup>100</sup> A “related party” is defined by the Revitalization Act as: (i) any director, officer, or key person of the corporation or any affiliate of the corporation; (ii) any relative of any individual described in clause (i) of this subparagraph; or (iii) any entity in which any individual described in clause (i) and (ii) of this subparagraph has a 35 percent 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 percent. The Act defines a “related party transaction” as any transaction, agreement, or any other arrangement in which a “related party” has a financial interest and in which the corporation or any of its affiliates is a participant, except that a transaction shall not be a related party transaction if: (i) the transaction or the related party’s financial interest in the transaction is de minimis; (ii) the transaction would not customarily be reviewed by the board or boards of similar organizations in the ordinary course of business and is available to others on the same or similar terms or (iii) the transaction constitutes a benefit provided to a related party solely as a member of a class of beneficiaries that the corporation intends to benefit as part of the accomplishment of its mission which benefit is available to all similarly situated members of the same class on the same terms. *See* N-PCL § 102(a)(19), (23)-(25).

<sup>101</sup> *See* N-PCL § 715(a).

<sup>102</sup> *See* N-PCL § 102(a)(25). A “key person” is defined as any person, other than a director or officer, whether or not an employee of the corporation, who (i) has responsibilities, or exercises powers or influence over the corporation as a whole similar to the responsibilities, powers, or influences of director and officers; (ii) manages the corporation, or a segment of the

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corporation that represents a substantial portion of the activities, assets, income or expenses of the corporation or (iii) alone or with others controls or determines a substantial portion of the corporation's capital expenditures or operating budget.

<sup>103</sup> N-PCL § 715(j).

<sup>104</sup> See N-PCL § 715(h).

<sup>105</sup> N-PCL § 102(a)(24).

<sup>106</sup> See N-PCL § 715(i) and (j). Effective as of May 27, 2017, "in an action by any person or entity other than the attorney general, it shall be a defense to a claim of violation of any provisions of this section that a transaction was fair, reasonable and in the corporation's best interest at the time the corporation approved the transaction" and "in an action by the attorney general with respect to a related party transaction not approved in accordance with paragraphs (a) or (b) of this section at the time it was entered into, whichever is applicable, it shall be a defense to a claim of violation of any provisions of this section that (1) the transaction was fair, reasonable and in the corporation's best interest at the time the corporation approved the transaction and (2) prior to receipt of any request for information by the attorney general regarding the transaction, the board has: (A) ratified the transaction by finding in good faith that it was fair, reasonable and in the corporation's best interest at the time the corporation approved the transaction; and, with respect to any related party transaction involving a charitable corporation and in which a related party has a substantial financial interest, considered alternative transactions to the extent available, approving the transaction by not less than a majority vote of the directors or committee members present at the meeting; (B) documented in writing the nature of the violation and the basis for the board's or committee's ratification of the transaction; and (C) put into place procedures to ensure that the corporation complies with paragraphs (a) and (b) of this section as to related party transactions in the future."

<sup>107</sup> N-PCL § 715-a(a).

<sup>108</sup> N-PCL § 715-a(b)(1).

<sup>109</sup> N-PCL § 715-a(b)(2).

<sup>110</sup> N-PCL § 715-a(b)(3)–(4).

<sup>111</sup> N-PCL § 715-a(b)(6).

<sup>112</sup> N-PCL § 715-a(c).

<sup>113</sup> N-PCL § 715-a(a).

<sup>114</sup> N-PCL § 202(a)(12) (emphasis added).

<sup>115</sup> FRANK WHITE, ISIDORE KANTROWITZ & SOL SLUTSKY, WHITE ON NEW YORK BUSINESS ENTITIES ¶ 202.04 (14th ed. 2014). See *Grasso*, *supra* note 73, at 868 (the Attorney General alleged that a majority of the Board did not effectively vote to approve Grasso's salary and additional compensation, as the Board was presented with allegedly inaccurate and incomplete information).

<sup>116</sup> See N-PCL § 102(a)(25).

<sup>117</sup> Form 990, Return of Organization Exempt from Income Tax, Part VII. See also the discussion relating to excess benefit transactions in Section 6.2.

<sup>118</sup> *Id.* at Part VI, Section A, Line 5 and related instructions. See also Dan Keating & Rebecca Rolfe, *The Most Intriguing Check Box on a Nonprofit's Disclosure Form*, WASH. POST, Oct. 26, 2013.

<sup>119</sup> See *Comm. to Save Adelphi*, *supra* note 61.

<sup>120</sup> *Vacco v. Diamandopoulos*, *supra* note 73.

<sup>121</sup> David M. Halbfinger, *Lawsuits Over Ouster of Adelphi Chief Are Settled*, N.Y. TIMES, Nov. 18, 1998, at B1.

<sup>122</sup> *United States v. Aramony*, 88 F.3d 1369 (4th Cir. 1996); *Aramony v. United Way of Am.*, 28 F. Supp. 2d 147 (S.D.N.Y. 1998), *aff'd in part, rev'd in part sub nom. Aramony v. United Way Replacement Benefit Plan*, 191 F.3d 140 (2d Cir. 1999); *United States v. Aramony*, 166 F.3d 655 (4th Cir. 1999). A large part of this case history revolves around Aramony's efforts to receive several million dollars from a Replacement Benefit Plan that did not contain a "bad boy" clause canceling the payments if Aramony was convicted of a crime. The breaches of his duties and the fines assessed were not at issue in the appeals.

<sup>123</sup> Pamela A. Mann, *Advising Nonprofit Organizations*, PRACTISING LAW INSTITUTE, at 28 (2014).

<sup>124</sup> *United States v. Aramony*, 88 F.3d at 1374.

<sup>125</sup> Mann, *supra* note 121, at 28.

<sup>126</sup> *Vacco v. Aramony*, N.Y.L.J. (N.Y. Sup. Ct. Aug. 7, 1998).

<sup>127</sup> N-PCL § 720-a.

<sup>128</sup> BRUCE R. HOPKINS, *THE LAW OF TAX-EXEMPT ORGANIZATIONS* 485 (8th ed. 2003).

<sup>129</sup> Treas. Reg. § 53.4958-8(a).

<sup>130</sup> I.R.C. § 4958(c)(1)(A).

<sup>131</sup> See Stephanie Strom, *I.R.S. Finds Tax Errors in Reports of Nonprofits*, N.Y. TIMES, Mar. 1, 2007, at A15. Having completed its two-year investigation of executive compensation at nonprofit organizations, the IRS imposed more than \$20 million in penalties on 40 individuals at 25 organizations which substantially overcompensated executives.

<sup>132</sup> Treas. Reg. § 53.4958-4(a)(2).

<sup>133</sup> I.R.C. § 4958(f)(1).

<sup>134</sup> Treas. Reg. § 53.4958-3(c).

<sup>135</sup> Treas. Reg. § 53.4958-3(e)(2), (3). Section 501(c)(3) organizations and certain Section 501(c)(4) organizations are not deemed "disqualified." Treas. Reg. § 53.4958-3(d).

<sup>136</sup> I.R.C. § 4958(a), (b).

<sup>137</sup> I.R.C. § 4958(a)(2).

<sup>138</sup> Treas. Reg. §§ 53.4958-1(d)(4)(iii), 53.4958-1(d)(3).

<sup>139</sup> I.R.C. § 4958(a)(2).

<sup>140</sup> Treas. Reg. § 53.4958-4(a)(3).

<sup>141</sup> Treas. Reg. § 53.4958-4(a)(3)(vii), example 4.

<sup>142</sup> Treas. Reg. § 53.4958-1(d)(4)(iii).

<sup>143</sup> *Id.*

<sup>144</sup> Treas. Reg. § 53.4958-6(a).

<sup>145</sup> *Id.*

<sup>146</sup> Treas. Reg. § 53.4958-6(a)(1).

<sup>147</sup> Treas. Reg. § 53.4958-6(a)(2). See also Strom, *supra* note 129, at A15. Having completed its two-year investigation of executive compensation at nonprofit organizations, the IRS imposed penalties at organizations that failed to use comparable figures or otherwise failed to justify executive pay levels. Mr. Miller, the commissioner in charge of the I.R.S. division

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overseeing tax-exempt entities, noted however “That shouldn’t be read to mean that high compensation wasn’t paid in the other cases...it means that in some cases where we found high compensation – and we did find it – the organization has done a good job of using comparables and establishing a procedure to determine it.”

<sup>148</sup> Treas. Reg. § 53.4958-6(c)(2).

<sup>149</sup> Treas. Reg. § 53.4958-6(c)(1)(ii).

<sup>150</sup> Treas. Reg. § 53.4958-6(c)(3)(ii).

<sup>151</sup> Treas. Reg. § 53.4958-6(c)(3)(i).

<sup>152</sup> Sarah J. Schmidt, *Avoiding the Snares of Intermediate Sanctions*, 14 NONPROFIT WORLD NO. 6, 18 (1996).

<sup>153</sup> Evelyn Brody, *Troubling Lessons from the Bishop Estate Settlement For Administering the New Intermediate Sanctions Regime*, 32 EXEMPT ORG. TAX REV. 431 (2001).

<sup>154</sup> Shea, *supra* note 81, at 19-21.

<sup>155</sup> N-PCL § 722(a).

<sup>156</sup> N-PCL §§ 723. *See* § 722(a).

<sup>157</sup> N-PCL § 721.

<sup>158</sup> N-PCL § 721.

<sup>159</sup> BJORKLUND, *supra* note 6, at §7.03(1).

<sup>160</sup> N-PCL § 726(a).

<sup>161</sup> For instance, fines and penalties where there has been an adverse judgment in a derivative action.

<sup>162</sup> N-PCL § 726(a). An insurance policy issued directly to a director or officer (rather than to a corporation) is not subject to retention and co-insurance requirements.

<sup>163</sup> 42 U.S.C. § 14501 *et seq.*

<sup>164</sup> 42 U.S.C. § 14503.

<sup>165</sup> *Rakaric v. Croatia Cultural Club*, 76 A.D.2d 619, 631 (N.Y. Sup. Ct. 1980) (noting that “the doctrine of charitable immunity is out of tune with the life about us, at variance with modern-day needs and with the concepts of justice and fair dealing” (internal quotation marks omitted)).

<sup>166</sup> *See* N.Y. GEN. MUN. LAW § 205-b.

<sup>167</sup> *See* N.Y. UNCONSOL. LAW § 7310.

<sup>168</sup> *See* N.Y. EDUC. LAW §. 6205. Any member of the board of trustees of the City University of New York, among others, will be indemnified against any claim or suit arising from an act or omission occurring within the scope of his or her duties.

## Not-For-Profit Practice Group

### Annual Reporting Requirements and Public Information Regarding Not-For-Profit Organizations

Board members of not-for-profit organizations should be aware of the reporting obligations that apply to their entity, such as those mandated by the Internal Revenue Service (the “IRS”) and the New York State Attorney General. Board members should also be aware of the publicly available information regarding their organization pursuant to applicable law and regulations. Discussed below is a summary of certain annual reporting requirements and publicly available information regarding not-for-profit organizations. Additional reports and filings may be required, for example, when an organization amends its charter or bylaws. Note that each organization is unique and must determine which reporting or filing obligations are applicable to it.

#### I. CERTAIN ANNUAL REPORTING REQUIREMENTS

The following are descriptions of certain annual reporting requirements for not-for-profit organizations that are incorporated in the State of New York.

##### 1.1 IRS Form 990

Form 990 is an annual reporting return that certain federally tax-exempt organizations must file with the IRS. It provides information on the filing organization’s mission, programs, finances, governance, management and disclosure practices. With some exceptions, organizations that are required to file Form 990 include federally tax-exempt not-for-profit organizations that have gross receipts greater than or equal to \$200,000 or total assets greater than or equal to \$500,000 and all 501(c)(3) private foundations, regardless of income.<sup>1</sup> In general, organizations that are not required to file Form 990 include most faith-based organizations.

Simplified annual reporting forms are available for tax-exempt organizations that do not meet the gross receipts or asset thresholds for filing Form 990. Not-for-profit organizations (other than private foundations) with gross receipts less than \$200,000 and total assets less than \$500,000 are entitled to file Form 990-EZ in lieu of Form 990. An exempt organization (except most 509(a)(3) supporting organizations) whose annual gross receipts are normally \$50,000 or less<sup>2</sup> may instead file Form 990-N (“e-postcard”) which requires disclosure of only the most basic information about the organization.

The IRS maintains a list of exempt organizations, which is available online. The searchable Exempt Organization Select Check is available at <https://www.irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Select-Check>. The searchable database allows users to limit searches to organizations that are eligible to receive tax-deductible charitable contributions, have had their tax-exempt status automatically revoked or have filed Form 990-N (“e-Postcard”). The downloadable “master file” list is available at <http://www.irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Business-Master-File-Extract-EO-BMF>.

Failure to file the applicable version of Form 990 for three consecutive years leads to an automatic revocation of an organization’s Federal tax-exempt status as of the due date of the third unfiled return. See the Instructions for the Form 990 for information on how to complete the Form 990 and what fees and attachments are required, available at <http://www.irs.gov/pub/irs-pdf/i990.pdf>. For more information on Form 990 – see **Tab 9**.

## 1.2 New York State Annual Filing for Charitable Organizations: Form CHAR500

With some exceptions (dependent upon the amount and nature of solicitations), registered charitable or other not-for-profit organizations that have filed a Form CHAR410 (Registration Statement for Charitable Organizations), an online registration available at [https://charitiesnys.com/charities\\_new.html](https://charitiesnys.com/charities_new.html), are required to annually file a Form CHAR500 (Annual Filing for Charitable Organizations), available through the Charities Bureau online portal at <https://ag.ny.gov/resources/organizations/charities-nonprofits-fundraisers/charities-annual-filing-char500>,<sup>3</sup> with the Charities Bureau of the New York State Attorney General. Registration is required of charitable and other not-for-profit organizations that (i) solicit contributions from New York State (including residents, foundations, corporations, government agencies and other entities) (pursuant to Article 7-A of the Executive Law) and/or (ii) are incorporated, are formed or otherwise conduct activity in New York State (pursuant to Section 8-1.4 of the Estates, Powers and Trusts Law). Depending on the organization’s finances during the year, it may be required to submit a filing fee and attachments, such as an IRS Form 990 and an accountant’s audit or review. See the Online Charities Registration User Guide for guidance on how to register charities online, available at <https://ag.ny.gov/sites/default/files/regulatory-documents/online-reg-useguide.pdf>, and the Instructions for the Form CHAR500 for information on how to complete the Form CHAR500 and what fees and attachments are required, available at <https://ag.ny.gov/sites/default/files/regulatory-documents/char500-user-guide.pdf>.

Subsection (9) of Section 172-b of the New York Executive Law requires nonprofit organizations that solicit charitable contributions in New York to file Form CHAR500 with both the Charities Bureau and the New York State Department of State. Along with Form CHAR500, a charitable organization must also submit IRS Form 990 and all applicable financial statements for the most recent tax year.

In addition, certain organizations registered in New York for charitable solicitation purposes must have their financial statements audited or reviewed by an independent certified public accountant, and must file the audit report or review report. The chart below reflects the gross revenue and support thresholds above which a New York not-for-profit will require an independent audit or accountant review:<sup>4</sup>

Gross Revenue & Support Threshold Applicability <sup>5</sup>	
Requirement	Gross Revenue and Support
Audit report	In excess of \$1 million
Review report	\$250,000 to \$1 million

## 1.3 Charitable Solicitation Annual Report

New York not-for-profit organizations annually filing a Form CHAR500 should also be aware that New York, like all states, requires charitable solicitation registration and annual reporting. While the majority of states, including New York, accept the Unified Registration Statement for a not-for-profit organization’s initial filing, annual reports should be submitted by filing a Form CHAR500.

## 1.4 Report to Non-Domiciled States

Not-for-profit organizations incorporated under New York law may need to file reports in states (other than New York) where the organization does business or is registered to do business. This is a case-by-case analysis that New York not-for-profit organizations operating or qualified as a foreign corporation outside of New York should conduct according to the requirements of the relevant state law.

## II. PUBLIC INFORMATION REGARDING NOT-FOR-PROFIT ORGANIZATIONS

There are many organizations and publications which rank or rate not-for-profit organizations based on established standards, criteria or processes. Many of these organizations provide their findings, as well as IRS Form 990s filed by not-for-profit organizations, free-of-charge to the public. Below is a sample list of such organizations and publications.

### 2.1 Organizations

- American Institute of Philanthropy (AIP): AIP is a charity watchdog service whose purpose is to provide information on how efficiently a charity uses donations to fund its supported programs. “CharityWatch exposes nonprofit abuses and advocates for [donor] interests. . .” Its website provides information about the charities which it rates as well as its method for rating charities. <http://www.charitywatch.org>
- Better Business Bureau (BBB) Wise Giving Alliance (WGA): The WGA reports on nationally soliciting charitable organizations that are the subject of donor inquiries. “BBB WGA does not rank charities but rather seeks to assist donors in making informed judgments about those that solicit their support. Evaluations are done without charge to the charity and are posted for free public access on give.org.” <http://www.bbb.org>
- Charity Navigator: Charity Navigator provides information on charities and helps guide intelligent giving by evaluating the financial health, accountability and transparency of these charities. Charity Navigator’s mission is to “make impactful philanthropy easier for all.” <https://www.charitynavigator.org/>
- Candid (f/k/a) Guidestar: Candid gathers and publicizes information about nonprofit organizations. Candid’s mission is to “get[] you the information you need to do good.” <http://www2.guidestar.org>

## ENDNOTES

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<sup>1</sup> Private Foundations file IRS Form 990-PF.

<sup>2</sup> A tax-exempt organization's gross receipts are normally \$50,000 or less if the average gross receipts of the organization for the prior 3 tax years is less than \$50,000. Modified rules apply for organizations that have been in existence for less than 3 years.

<sup>3</sup> New York charitable organizations must submit their CHAR500 annual filings through an online portal on the Bureau's website.

<sup>4</sup> See New York Executive Law § 172-b. See also New York Attorney General's Charities Bureau Guidance Document, "Audit Committee Requirements and Responsibilities under New York's Not-For-Profit Corporation Law as amended through 2017" (September 2018), available at <https://ag.ny.gov/sites/default/files/regulatory-documents/AuditCommittees.pdf>.

<sup>5</sup> This publication has not been updated since 2018.

## Not-For-Profit Practice Group

### Right From The Start: Responsibilities of Directors of Not-For-Profit Corporations (from the NY Charities Bureau website)<sup>1</sup>

Office of the New York State Attorney General  
Charities Bureau  
28 Liberty Street  
New York, NY 10005

(212) 416-8400

[www.charitiesnys.com](http://www.charitiesnys.com)

Guidance Document 2015 - 6, V. 1.0  
Issue date: May 15, 2015

The Charities Bureau of the Office of the New York State Attorney General drafted this guidance to assist current and future boards of directors of not-for-profit corporations and trustees of charitable trusts to understand and carry out their fiduciary responsibilities to the organizations they serve. The information in this booklet reflects changes to the Not-for-Profit Corporation Law that were included in the Nonprofit Revitalization Act of 2013.

Charitable organizations contribute enormously to our society. They educate our children, care for the sick, find cures for disease, preserve our literature, art and music for us and future generations, house the homeless, protect the environment and much more. The fiduciaries of those charitable organizations are responsible for managing and preserving the charitable assets that benefit all of us. Whatever their mission or size, all organizations should have policies and procedures established so that (1) members of their boards understand their fiduciary responsibilities, (2) assets are managed properly and (3) the charitable purposes are carried out. A failure to meet these obligations is a breach of fiduciary duty and can result in financial and other liability for the board of directors.

Please read this booklet carefully. It contains general information to assist current and prospective members of nonprofit boards. It outlines some of the duties of board members and points out questions to ask and information to look for when considering and/or fulfilling the responsibilities of board membership. The Charities Bureau also publishes other guidance containing more detailed information on managing a charitable organization and overseeing its assets. That guidance and other publications of interest to board members are posted at [www.charitiesnys.com](http://www.charitiesnys.com).

This guidance is designed to assist board members by providing them with basic information. It is not a substitute for more detailed information or advice from an attorney, independent certified public accountant or other professional.

## I. WHO MAY JOIN A BOARD?

Board members come from all backgrounds, bringing many different talents to the organizations they serve. Anyone over eighteen is legally qualified to serve on a board.

## II. WHAT SHOULD A PROSPECTIVE BOARD MEMBER KNOW BEFORE JOINING A BOARD?

Anyone thinking about joining a board should consider doing the following *before* joining:

- Read the organization's certificate of incorporation, application for federal income tax exemption, by-laws and board and committee minutes for at least the last year to learn about its purposes, activities and concerns.
- Obtain a current list of board and committee members and find out from the board chair and the organization's chief executive and financial officers what is expected of board members.
- Talk to current and recent former board members to learn about what the board does. In addition, make sure that the board and committee meetings are usually well-attended.
- If you know of any board members who recently left the board, see if you can find out why.
- Review the organization's Internal Revenue Service Form 990, 990EZ or 990 PF and, if it has an outside auditor, its audited financial statements for at least the last two years as well as its current internal financial reports to see how the organization uses its assets and to evaluate its financial health. Ask some questions - Is its auditor's report on its financial statements unqualified? Has the auditor sent the organization a management letter identifying issues of concern? Has the Internal Revenue Service recently audited the organization? If so, what was the result to the audit?
- Obtain an understanding of the internal control structure of the organization and the processes in place to monitor it.
- Find out if the organization is required to register with the Attorney General's Charities Bureau and, if so, whether it has registered and filed all required reports. Find out if it has filed required reports with the IRS and any other government agencies.
- Understand the organization's mission, learn about its programs, read its publications, visit its program sites, look at its website and talk to key staff and major donors. Find out about its reputation in the community.
- Review the organizational chart and understand the accountability structure of the organization. Find out about the employee evaluation and compensation processes and due diligence procedures for entering into material contracts.
- Make sure there is a conflict of interest policy and that it is provided to and signed by new directors and before they join the organization, and annually to directors, officers and employees for review and signature annually. Find out how the organization addresses actual or potential conflicts.
- Find out what committees the board has established and decide which (if any) to join. Make sure the committees appear to be sufficient (audit, investment, budget, finance, compensation, human resources, nominating, governance, etc.). Under New York's Not-for-Profit Corporation Law, corporations required to file an audit with the Attorney General's Charities Bureau must have an audit committee

made up of independent directors or the board must assume that function with only independent members participating. Independent directors are members of the board who are not paid by the organization and neither they nor their family members have any financial relationship with the organization.<sup>2</sup>

- Find out if materials to be considered by the board or its committees are distributed in advance of meetings and whether they provide sufficient information necessary to be part of the stewardship process. Find out how the meetings are structured: by consent agenda or other means.
- Obtain the current year's budget and cash flow projections. Find out how they compare to actual income and expenses and what processes are in place to monitor these comparisons.
- Find out whether the insurance coverage appears to be appropriate, including Directors' and Officers' liability and employee fidelity insurance. The latter is particularly important - it is surprising how often embezzlement is discovered.
- Most important, make sure you are able to devote the time expected of a board member. Understand any responsibilities for fundraising, personal giving commitments and other functions expected of board members. Joining a board without sufficient time to devote to its business is often at the root of troubles faced by boards. A decision to decline an invitation to join a board because you don't have the time to devote to the board should be respected.
- Learn what training (if any) is provided to board members.

### III. WHAT ARE THE DUTIES OF BOARDS OF DIRECTORS?

Most nonprofit organizations are created to achieve a specific purpose or purposes, such as making grants to operating charities, setting up a soup kitchen, teaching children to read, providing health care, supporting cultural institutions, preserving the environment, assisting senior citizens or one of the many thousands of other charitable activities conducted in our state and our country. Those purposes, or the mission of the organization, may be described in its certificate of incorporation, by-laws or other constituent document.

If an organization's purposes are not already clearly included in one of its organizational documents, one of the first activities of the board should be to draft a clear mission statement which should correspond to the purposes described in its certificate of incorporation and application for tax exemption submitted to the Internal Revenue Service. Everyone involved with the organization - directors and officers, employees, volunteers, fundraising professionals and other professionals – should be familiar with and understand its mission. Those individuals plan its future, conduct its programs, raise its funds, make it known to the public, present its financial records to regulatory agencies and others and give it professional advice.

Unless they fully understand why the organization was formed and what it plans to accomplish, board members will not be able to perform their respective tasks appropriately. The mission should be periodically re-assessed and evaluated and amended as needed. Periodic review of an organization's structure, procedures and programs will assist board members in determining what is working well and what practices the organization might want to change in order to be more efficient, effective or responsible.

While the board is not usually involved in the day-to-day activities of the organization, it is responsible for managing the organization and must make decisions crucial to the life and direction of the organization, such as adding or removing board members, hiring and firing key officers and employees, engaging auditors and other professionals and authorizing significant financial transactions and new program initiatives. In carrying out those responsibilities, members of a board of directors must fulfill fiduciary duties to the organization and the public it serves.

Those primary legal duties are commonly referred to as the duties of care, loyalty and obedience. If the organization has affiliates or subsidiaries, the legal duty of impartiality and the duty of fairness to all the charitable interests, may also come into play.

### 3.1 Duty of Care

The duty of care requires a director to be familiar with the organization's finances and activities and to participate regularly in its governance. In carrying out this duty, directors must act in “good faith” using the “degree of diligence, care and skill” which prudent people would use in similar positions and under similar circumstances. In exercising the duty of care, a responsible board of directors should, among other things, do the following:

- The directors as a group, and the officers of the corporation, should exercise their responsibility to undertake reasonable efforts to assure that the organization is operating in compliance with the law. For directors, this means assuring that there is an effective compliance program reporting ultimately to the directors, that there is a policy for protection of whistleblowers which has been communicated to employees, that there are effective internal controls, that there is an effective external audit by an independent auditor, and that allegations of violations of law are investigated and addressed. (Although New York law only requires organizations with over 20 employees and over \$1 million in revenue to have a whistleblower policy, smaller organizations might find it helpful to adopt such a policy as well.)
- Attend board and committee meetings and actively participate in discussions and decision-making, such as setting of policies. Carefully read the material prepared for board and committee meetings prior to the meetings and note any questions they raise. Allow time to meet without senior management present.
- Read the minutes of prior meetings and all reports provided, including financial statements and reports by employees. Do not hesitate to suggest corrections, clarification and additions to the minutes or other formal documents.
- Make sure to get copies of the minutes of any missed committee or board meeting, read them timely and suggest any changes that may be appropriate.
- Make sure there is a clear process for approval of major obligations such as fundraising, professional fees (including auditors), compensation arrangements and construction contracts.
- Make sure that board minutes reflect any dissenting votes in action taken by the board or that any dissenting vote is expressed in writing by letter to the board. Such records are necessary in order for a board member to disclaim responsibility for any particular decision. Absent board members must do this promptly in writing.
- Read literature produced as part of the organization's programs.
- Make sure that monthly financial reports prepared for management are available to the board or finance and audit committees, and that they are clear and communicate the information needed for proper stewardship. Make sure there is an ongoing actual to budget comparison with discrepancies explained.
- Participate in risk assessment and strategic planning discussions for the future of the organization.
- Ensure that the organization has addressed the sufficiency of its written internal financial controls and written policies that safeguard, promote and protect its assets and that they are updated regularly, and has considered an employees', officers' and directors' fidelity bond to protect the organization from embezzlement.

- Assure that the organization has a background check policy for prospective employees.
- Determine whether or not the organization indemnifies its officers and directors from liability and has directors' and officers' liability insurance. If it does, find out what is covered and what is not. If it does not, find out why.
- Encourage diversity among board members. Diversity will help insure a board committed to serve the organization's mission with a range of appropriate skills and interests.
- Be involved in the selection and periodic review of the performance of the organization's Chief Executive Officer, Chief Financial Officer and other key employees responsible for the day-to-day activities of the organization. The board is responsible for ascertaining whether these individuals have the appropriate education, skills and experience to assume a key position; communicating duties, expectations and goals; and then evaluating their performance at least annually, first in an executive session and then with the officer directly.

### 3.2 Duty of Loyalty

Directors are charged with the duty to act in the interest of the corporation. This duty of loyalty requires that any conflict of interest, real or possible, be disclosed in advance of joining a board and when they arise. So that all members are aware of - and avoid - transactions in which the nonprofit's interests are not primary, New York law requires nonprofits to have a written "conflicts of interest" policy. Among the provisions that should be included in such policies are provisions that:

- Define the circumstances that constitute a conflict of interest;
- Set forth procedures for disclosing a conflict of interest to the audit committee or the board;
- Prohibit anyone with a conflict of interest from being present during or participating in the deliberation, voting on the issue that resulted in the conflict or influencing the deliberation or vote on the issue that resulted in the conflict;
- Require the nonprofit to document the existence and resolution of each conflict;
- Require directors to sign annually a statement that identifies entities in which they serve as an officer, director, trustee, member or employee and with which the corporation has a relationship; as well as any transaction of the nonprofit in which the director might have a conflicting interest.

### 3.3 Duty of Obedience

A board has a duty of obedience to ensure that the organization complies with applicable laws and regulations, its mission and its internal governance documents and policies, including:

- Dedicating the organization's resources to its mission.
- Ensuring that the organization carries out its purposes and does not engage in unauthorized activities.
- Complying with all appropriate laws, including registering and filing annual financial reports with the Attorney General's Charities Bureau in New York State, complying with similar laws in other states in which it conducts activities and/or solicits contributions, filing required financial reports with the State Worker's Compensation Board, the State Department of Taxation and Finance and the Internal Revenue Service; and paying all taxes such as Social Security, income tax withholding (federal, state and local) and any unrelated business income tax. Board members may be personally liable for failing to pay

employees' wages and benefits, and for failing to withhold, escrow and pay over to state and federal authorities withholding taxes on employees' wages.

- Providing copies of its applications for tax-exempt status (IRS Form 1023), federal reports (IRS forms 990, 990 PF, 990 EZ) and its financial reports filed with the Attorney General's Charities Bureau to members of the public who request them. Many organizations post their annual reports and other information on the Internet.

#### **IV. MONITOR FUNDRAISING CONDUCTED ON BEHALF OF THE ORGANIZATION**

Many organizations contract with outside organizations or individuals to raise funds on their behalf. Since the fundraiser represents the organization to the public, the selection of a fundraising professional is extremely important. Establishing and following procedures for selection of a fundraiser can avoid future problems. Board members should assess whether management has undertaken reasonable procedures to protect the organization, including:

- Obtaining bids from several fundraising professionals before entering into a contract. Services and fees differ, and comparing bids will aid in the selection of the best contractor for the organization.
- Checking with the Attorney General's Charities Bureau to see if the fundraising professionals being considered are registered and have filed all required contracts and financial reports.
- Asking the Charities Bureau for copies of the fundraising professional's contracts with other charities to determine the services performed for and the fees charged to those charities.
- Asking the fundraising professional for references. Reputable fundraising professionals should be happy to provide a potential client with the contact information for some of its clients.
- Contacting some of the fundraising professional's other clients to see if they were satisfied with the services received.
- Finding out whether the organization's fundraising contracts contain the clauses required by Article 7-A of the Executive Law.
- Reviewing written solicitations and scripts used by the fund raising professional to make sure that solicitations appropriately describe the organization and its activities, include the name of the organization as registered with the Attorney General and advise potential contributors that they may obtain the organization's financial report from the organization itself or from the Attorney General.
- Requiring, as mandated by New York law, that the fundraising professional and any of its representatives ("professional solicitors") disclose the name of the specific professional solicitor and the employing fundraising professional and state that the solicitor is being paid to raise funds.
- When considering engaging a fundraiser to solicit via the telephone, reviewing *Pennies for Charity*, the Attorney General's annual report on telemarketing by professional fundraisers, to see the results of those fundraisers' campaigns.

#### **V. MAKE USE OF AVAILABLE RESOURCES**

In carrying out their responsibilities, board members should realize that they need not do it alone. Board members should consider the need for advice from professionals or experts to assist them in the performance

of their duties, and make appropriate requests for such advice. There are many other resources available to assist nonprofit organizations in fulfilling their fiduciary duties.

Following are some of those resources:

- **The Attorney General's Web site** – [www.charitiesnys.com](http://www.charitiesnys.com) - posts all forms and instructions for registration and annual filing with the Charities Bureau and publications of interest to nonprofit organizations, including guidance on the Nonprofit Revitalization Act of 2013.
- **Contact Us** - If the material on the Attorney General's web site does not answer your particular questions-
  - For questions about nonprofit organizations, contact: [charities.bureau@ag.ny.gov](mailto:charities.bureau@ag.ny.gov) or (212) 416-8401
  - For questions about fundraising professionals, contact: [charities.fundraising@ag.ny.gov](mailto:charities.fundraising@ag.ny.gov) or (518) 776-2160
- **Other Helpful Web Sites** - Many more resources are available on the Internet and in communities around the state. Links to some of those resources are posted on the Attorney General's web site – [www.charitiesnys.com](http://www.charitiesnys.com) Please note that inclusion of any particular entity should not be construed as an endorsement by the Attorney General of that entity or the services it renders.

## ENDNOTES

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<sup>1</sup> This document is a reproduction of the New York State Attorney General Charities Bureau’s published guidance, “Right From The Start: Responsibilities of Directors of Not-For-Profit Corporations” (Guidance Document 2015-6, V. 1.0, dated May 15, 2015). Available at <https://ag.ny.gov/sites/default/files/regulatory-documents/Right-From-the-Start.pdf>. It has not been updated by the Attorney General’s office since its original publication in 2015. The text is reproduced substantially as it appears on the Charities Bureau’s website; any typographical errors in the original have been preserved. *t*

<sup>2</sup> Section 102(a)(21) of the Not-for-Profit Corporation Law sets forth the definition of Independent Director.

## Not-For-Profit Practice Group

### Key ESG Considerations for Not-for-Profit Directors

The pace and scale of recent developments relating to environmental, social and governance (“ESG”) issues can make it difficult for not-for-profit directors to determine what they really need to know to provide effective oversight. Controversy around the term “ESG” and anti-ESG viewpoints have contributed to the volatile environment in which directors fulfill their fiduciary responsibilities. Moving away from ESG as a politicized umbrella concept, directors may focus on the specific E, S and G topics that can contribute to sustainable performance over the long term when setting strategy and providing risk oversight. Adapting to these quickly evolving ESG-related developments requires an agile board, supported by a management team that is appropriately focused on these issues.

- Understand how the organization’s short- and long-term strategy and industry may be impacted by regulatory and other developments relating to specific E, S and G topics, and what the organization is doing to prepare. Assess how the organization’s approach compares to its peers. For example, the Trump Administration has issued several executive orders and made funding and other decisions, and federal agencies have issued memoranda relating to topics that may impact a not-for-profit’s purpose, strategy, funding and/or operations, including relating to the following ESG-related topics:
  - Illegal discrimination and diversity, equity and inclusion (DEI)
  - Religious groups
  - Gender ideology and biological sex
  - Reproductive health care
  - Sports participation
  - Medical research and vaccination
  - University programs
  - Greenhouse gas (GHG) emissions and emissions reduction goals
  - Energy transition and fossil fuels
  - Environmental justice
  - Tariffs
  - Immigration and citizenship
  - Child and forced labor
  - Sanctions and cartels
  - Artificial intelligence
- Keep abreast of ESG-related requirements that may apply to the organization, now or in the future. For example, U.S. entities doing business in California may be required to disclose (a) annual scope 1 and scope 2 GHG emissions (starting in 2026) and annual scope 3 GHG emissions (starting in 2027), verified by an independent auditor (SB 253, as amended by SB 219, applicable to entities with more than \$1 billion annual in total annual revenues), (b) climate-related financial risk and measures adopted to reduce and adapt to such risk (first disclosures due no later than January 1, 2026 and biennially thereafter, with reporting voluntary at the time of writing, while a preliminary junction is in effect) (S.B. 261, as amended by S.B. 219, applicable to entities with more than \$500 million in total annual revenues), and (c) information relating to carbon-neutral and similar claims (effective January 1, 2024) (AB 1305). Similar laws have been proposed in New York, New Jersey and Illinois, among others. The California Air Resources Board has adopted regulations that exempt non-profit or charitable organizations that are tax-exempt under the Internal Revenue Code from SB 253 and SB 261, but these regulations are not yet in effect.

- Identify the methodology and assumptions used by the organization in gathering data relating to ESG topics, review related controls and monitoring/audit processes, and plan for cross-functional information system enhancements as needed. Although an organization may not be required to disclose ESG-related information or comply with particular regulations, they may nevertheless face pressure to provide ESG-related information to suppliers, customers and employees.
- Ensure ESG-related disclosures that the organization makes are aligned across all communications including regulatory filings, organization website, social media and advertisements. Bolster disclaimers to reduce the risk of regulatory and other scrutiny.
- Assess the risk of enforcement and other scrutiny relating to ESG hot button topics, such as “greenwashing,” employee and supplier DEI programs, GHG emissions targets, AI and corporate culture, and implement a crisis preparedness program to help manage issues that arise.
- Understand the anti-ESG landscape of relevance to the organization including restrictions on government contracts with organizations taking various positions on ESG topics and federal agency focus on illegal DEI discrimination and preferences at federal contractors (which may be required to agree to specific provisions incorporated into federal contracts) and in the private sector.
- Determine where responsibility for oversight of various ESG topics should sit within the board and its committees, and ensure ESG-related responsibilities are reflected in committee charters. While all directors should have a baseline competence around ESG issues that relate to the organization, committees with significant ESG-related responsibilities should include committee members with relevant expertise.
- Ensure the organization has an effective compliance program that is fit for purpose, including policies and procedures for employees, directors, volunteers and contractors, resources, training, communications and enforcement.

## Not-for-Profit Practice Group

### Directors' and Officers' Liability Insurance for Non-Profit Organizations

Non-profit organizations and their management teams face significant scrutiny arising from financing operations, making investment and allocation decisions, maintaining a workforce, complying with regulatory requirements, and countless other issues. Particularly at a time of heightened federal government scrutiny of the non-profit sector, it can be critical for entities and their managers to understand the risk mitigation options provided through directors' and officers' liability insurance ("D&O insurance") and the scope of coverage they can expect under current insurance market conditions.

#### I. D&O INSURANCE – WHAT IS IT?

D&O insurance protects organizations' directors and officers against claims alleging they committed wrongful acts in their capacities as directors and officers. Typically this provides that the policy covers "Loss" arising from a "Claim" made during the "Policy Period" against an "Insured" for a "Wrongful Act." As discussed below, each of these terms is governed by the Definitions section of the relevant policy. This type of coverage helps address defense costs, judgments and other liabilities arising from litigation by donors, beneficiaries, vendors, employees, regulators and others. Organizations should ensure that they understand the notification requirements of the policy and provide timely notice to the Insurer of any potential Claim. In the event of a Claim, Insurers appoint defense counsel and pay their fees or reimburse the Insured for its incurred defense costs. As a result, the insurance protects D&Os' personal assets and promotes organizations' missions by helping to attract talented directors and officers to serve.

#### II. POLICY ROADMAP – HOW TO READ A POLICY

First – Declarations Page. This summary of coverage terms identifies the Named Insured (the covered organization to which the policy is issued); the Policy Period (the dates during which Claims may be submitted); and the Limit of Liability (the maximum amount the insurer will pay if coverage applies).

Second - Insuring Agreements. In general, D&O coverage falls into three categories.

Side A: Coverage for D&Os for Claims brought against D&Os for which the organization does not provide indemnity. Examples include scenarios in which an organization is financially unable to indemnify its D&Os, is prohibited by law from using its assets to make indemnity payments, or wrongfully refuses to provide indemnity that is owed to D&Os (in which case the insurer will provide coverage as a Side A claim and then seek recovery from the organization).

Side B: Reimbursement to the organization for amounts spent to indemnify D&Os.

Side C: Coverage for the organization for Claims brought against the organization itself. Examples include criminal prosecutions alleging that an organization participated in wrongfully harboring migrants and "whistleblower" actions under the False Claims Act alleging that the organization wrongfully recovered funds under a state or federal government program (absent restrictive policy phrasing to the contrary).

Third – Definitions. To determine whether an Insuring Agreement is triggered, refer to the policy's Definitions section. While general coverage principles are similar throughout the industry, each insurer defines key terms in a unique way, with potentially significant coverage differences.

- Insured: The entity named as the Named Insured, its subsidiaries, and their D&Os and employees.
- Claim: A third party must initiate an action (including a lawsuit, complaint, or regulatory proceeding) or otherwise make a demand for relief against an Insured.

- **Wrongful Act:** The Claim must allege that an Insured actually committed some wrongdoing in the scope of his/her role as a D&O.
- **Loss:** An Insured must actually incur losses as a result of a Claim. This includes defense costs/attorneys' fees and other monetary liabilities such as judgments and settlements.
- **Policy Period:** The Claim must have been made against the Insured after the policy's inception date and before its expiration date (typically a one-year period).

Fourth – Exclusions. Even if an Insuring Agreement is triggered, an exclusion may preclude coverage for all or part of the submitted Claim (see below).

Fifth – Endorsements. Provisions attached as an addendum to an insurer's standard policy form often significantly change, add or altogether delete coverage terms and conditions.

Sixth - Self-Insured Retention. If a matter is covered, an Insured must pay or incur a certain amount of Loss before the insurer will begin making payments. This is similar to a deductible applicable to other types of insurance. Side A Claims are not subject to a retention.

### III. COMMON D&O INSURANCE CLAIMS FOR NON-PROFIT ENTITIES

Governance liability. Donors may dispute directors' allocation and management decisions, claiming that such decisions were not made in the best interest of the organization and its mission. Claims premised on negligence, misrepresentations and mismanagement are broadly covered.

Indemnification. If an organization must indemnify D&Os for their losses, the Side-B coverage is meant to reimburse the organization for its indemnification payments.

Regulatory investigations and proceedings. D&O insurance often helps offset costs arising from a government investigation or regulatory proceeding, but the scope of coverage depends on a policy's definitions. Policies often do not cover civil or criminal fines or penalties, subject to certain policy-specific exceptions (to the extent insurable by law in a particular jurisdiction). Defense costs associated with a claim seeking to impose fines or penalties might remain covered.

Definitions of "Claim" usually require a demand for monetary or non-monetary relief, and some insurers do not consider demands for documents or testimony as demands for relief against an Insured. When considering whether to buy a policy, it is best to confirm whether the "Claim" definition includes investigations generally or whether a particular type of government allegation must exist to trigger the policy. If the latter restriction applies, a Claim may not exist when a regulator issues a demand for documents or testimony. For example, a federal agency contract audit or investigation might not constitute a "Claim" absent a cognizable demand for relief. Consider also whether options are available for a policy endorsement providing that pre-Claim inquiry costs are covered. Such "inquiry" coverage can help address regulatory action that does not yet constitute a Claim.

Even if a demand for relief is acknowledged, the Claim remains uncovered if the basis for the demand lacks an alleged Wrongful Act. And to trigger coverage, any Wrongful Act must have occurred in a person's capacity as a director or officer. For example, a Claim against a director arising from mismanagement of an employee benefit plan likely would not be made in his/her capacity as a director (see discussion of Fiduciary Liability Insurance below). Consider requesting a policy endorsement providing that certain regulatory notices can trigger coverage for defense costs if they are issued to an insured individual and seek relief without alleging that he/she committed a Wrongful Act.

Employment issues. Depending on a policy’s definitions and exclusions, employment issues including retaliation and discrimination might be covered. Some policies exclude employment-related coverage altogether, with such issues covered only under a separate Employment Practices Liability policy (see discussion below).

#### IV. TYPICAL EXCLUSIONS

Contractual liabilities. Insurance is not provided as a replacement for performing a contractual obligation.

Insured v. Insured Claims. Insurers will avoid covering disputes among multiple directors of the same entity, or between the organization and any of its directors. This exclusion is typically subject to several exceptions. It is best to confirm the scope and impact of the exclusion before engaging directors or accepting a director role.

Fraud, Deliberate Dishonesty & Personal Profit. Insurers will provide coverage for defense costs incurred in connection with allegations of fraud, deliberate dishonesty and gaining of personal profit unless/until a final, non-appealable adjudication establishes that the conduct actually occurred. Once such an adjudication exists, coverage ceases and the insurer is entitled to recover amounts paid in connection with defending against these allegations.

ERISA. Losses arising from violations of the Employee Retirement Income Security Act do not fall within D&O coverage. Refer to a Fiduciary Liability policy instead.

Bodily Injury and Property Damage. Look to a General Liability or similar policy for these types of issues.

Prior Notice. If a Claim is submitted and accepted under one D&O policy, the Claim is generally excluded from coverage under any other D&O policy (including any renewal of the policy under which the Claim was first submitted).

Prior and Pending Litigation. Policies identify a specific “prior and pending” date. There is no coverage for litigation that exists before that date, or for later litigation premised on acts involved in the earlier litigation.

#### V. CONSULT ADVISORS

A D&O policy is a legal agreement governed by jurisdiction-specific rules and industry practices. Discuss the scope and intended operation of any policy with an experienced attorney. Consider legal advice on structuring insurance claims to maximize the likelihood of identifying multiple recovery theories to access several types of policies.

In addition, engage an insurance broker who specializes in D&O coverage. These policies differ significantly from other types of coverage, so relevant experience and industry relationships are key for a broker to be effective. Brokers with D&O expertise (and experience placing policies for non-profit entities in particular) can help assess an organization’s risks, provide benchmarking to identify an appropriate amount of coverage, and arrange for policy phrasing providing the broadest available protection. While brokers can facilitate requests for policy endorsements that broaden the scope of coverage, policies for non-profit organizations tend to be relatively inexpensive and subject to low policy limits, limiting policyholders’ negotiating leverage with insurers.

#### VI. CONSIDER ADDITIONAL TYPES OF INSURANCE

D&O Insurance is separate and distinct from Fiduciary, Professional, Employment Practices and Cyber coverages. If a claim is covered under one type of insurance, it is probably excluded under any other type of insurance.

- Fiduciary Liability Insurance (FLI): Coverage for claims arising from benefit plan management. For example, if individuals involved in an organization's management are also involved in managing employees' benefit plans, FLI will cover employees' allegations of breach of fiduciary duty in managing a plan.
- Professional Liability/Errors and Omissions Insurance (E&O): Coverage for claims arising from performing or failing to perform professional services. If an organization performs services for clients for a fee, claims by clients arising from those services will be excluded under a D&O policy's exclusion for professional services but will likely be addressed under an E&O policy.
- Employment Practices Liability Insurance (EPLI): Coverage for claims arising from an organization's employment-related activities. If a D&O policy generally excludes employment-related issues including claims alleging discrimination, harassment or retaliation, an EPLI policy can provide the necessary coverage.
- Cyber Insurance: Coverage for losses arising from cyber attacks, data breaches, and other network security events. Even if a D&O policy covers allegations that managers failed to adequately protect an organization's networks, cyber insurance would likely cover the costs of actually recovering from a network security event such as data recovery and associated expenses.

## Not-For-Profit Practice Group

### Fundamental Tax Law Considerations for the Not-For-Profit Organization

The following outlines significant tax-law considerations generally relevant to NFP organizations. Given the scope and the nuances of tax law, it is not possible to, and the following is not an attempt to, answer questions that are specific to a particular organization or to a particular set of facts or circumstances. Thus, the following outline should serve merely as a starting point, a resource that can help to educate and alert an NFP board member or executive as to the very significant tax-law considerations that affect every aspect of the organization's conduct.

#### **I. SAFEGUARDING AND SPENDING THE ASSETS OF AN NFP – AN OVERVIEW**

##### **1.1 Not-for-Profit is Not the Same as Tax-Exempt**

1. State Not-For-Profit Corporation Law - The NFP entity is formed under, exists by reason of, and derives its organic legal rights and obligations from state law.
2. Most states have a special statute applicable to NFPs. In some jurisdictions, like Delaware, there is not a separate statutory framework specifically and exclusively applicable to NFPs; rather, general corporate law applies to the NFP corporation.
3. Meaning of “Not-for-Profit” - The defining state law feature of an NFP organization is that there exists no person who can, through ownership or control of the entity, derive a profit from the organization. “Not-for-profit” does not, however, mean that the organization is precluded by state corporate law from conducting an activity that generates a profit, even an activity designed to do so.
4. Meaning of “Tax Exempt” - Classification of an entity as “tax exempt” generally refers to the exclusion it enjoys from paying income and other taxes under US federal, state and local tax statutes. Often (but not always), tax-exempt organizations are those to which donations may be made, subject to limitations, on a tax-deductible basis.
5. Typically, the not-for-profit character of an organization is only one of many requirements for the organization to seek, attain and retain tax-exempt status under the various tax statutes.

##### **1.2 Planning & Supervising NFP Activities & Operations – The NFP Board and Management Must Consider the Organization's Activities Through the Following Prism**

1. Are we “on mission”? The guiding principle of every action (or inaction) taken by an NFP is its “mission” as enunciated in its governing documents.
2. “Mission” is not necessarily what a given board member (or even the entire board) or manager believes to be the organization's goals; rather, “mission” is defined by the organization's governing documents, subject to being amended or updated in accordance with the provisions within those governing documents.
3. What does our certificate of incorporation (charter) say? The organization's conduct must at all times and in every way comport with the guidelines and limitations established under its organic documents.

4. What have we “promised” our donors? Often, if not always, donors to an NFP expect that the funds will be applied in a certain way. Sometimes specific promises are made as part of the fundraising effort, and sometimes no express promise is made other than the implicit assurance that the funds will be applied in accordance with the organizational mission. In many situations, the lines are not clearly drawn. In all cases, the NFP must be ever mindful of valid donor expectations as it deliberates application of organizational assets.
5. What did we tell the IRS when we sought tax exemption? The process by which the NFP seeks tax-exempt status is one in which many representations are made to the IRS (or other taxing authority) regarding virtually (if not actually) every aspect of the organization’s operations. To the extent that, at some later time, the NFP strays from the factual representations made to the taxing authority, it can place its tax-exempt status in jeopardy.
6. Will we jeopardize our exempt status or subject ourselves to tax law penalty? Merely remaining in strict or technical compliance with the representations made to the taxing authorities when first seeking exempt status is no guaranty of anything. Commercial (and other) activities conducted by an NFP can result in the organization losing its exempt status and also can expose both the organization and its members and officers to penalties under the tax law.

### 1.3 NFP Assets Must Be Safeguarded and Properly Spent

1. State Law – Generally under governing state law, the assets of an NFP are held in trust for the public.
  - It’s All About Mission – The NFP’s assets are not in any way the property or domain of the major donor, the founder or the visionary; while these people often are given a say or even a controlling say in the application of NFP assets, those decisions must be guided by the overriding principle that the NFP assets are dedicated to the NFPs mission and held by the NFP in trust for the achievement of that mission.
2. Tax Law – The assets of the tax-exempt NFP must be applied in furtherance of its tax-exempt objectives. The tax law, in its insistence on and enforcement of this principle, provides (at least) three express prohibitions (discussed in greater detail in the succeeding portions of this outline) regarding the use and application of organizational assets:
  - no Private Inurement
  - no Private Benefit
  - no Excess Benefit Transactions
3. When do these tax-law constraints arise? Any act, decision or arrangement that involves the assets of the NFP implicates these tax law constraints. Thus, these constraints arise in just about every deliberation undertaken and every decision made by the NFP board and its management.

## II. THE TAX-EXEMPT NFP – PRIVATE INUREMENT

### 2.1 Private Inurement – Statutory Construct

1. Section 501(c)(3) of the Internal Revenue Code describes an organization “. . . organized and operated exclusively for . . . charitable . . . purposes, . . . *no part of the net earnings of which inures to the benefit of any private shareholder or individual.*”

2. Thus, the tax statute absolutely prohibits so-called “private inurement,” the realization by certain people associated with the organization of any benefit as a result of their association.
3. Private inurement constraint applies to many types of tax-exempt entities, including:
  - Section 501(c)(3) Charities
  - Section 501(c)(4) Social Welfare Organizations
  - Section 501(c)(6) Trade Associations

## 2.2 Private Inurement vs. Private Benefit

1. Aside from the “private inurement” constraint, the tax law also includes an additional prohibition against the NFP affording a “private benefit.”
2. While the proscription against Private Inurement focuses on “insiders,” the proscription against Private Benefit is concerned with anyone (outside the charitable class). Thus, even if someone is not an “insider,” generally the tax-exempt NFP may not provide benefit to that person unless the provision of that benefit is consistent with and in furtherance of its exempt purpose.
  - Private Benefit as a Product of Tax Regulations: The “private benefit” concept grows out of the regulatory interpretation and application of the statutory requirement that the organization be “organized and operated” for exclusively charitable purposes.
  - For purposes of the “private benefit” constraint, the tax law permits a certain level of “incidental” benefit.
3. Practical Difference Between Private Inurement and Private Benefit: Scrutiny and Sympathy – When a tax-exempt NFP provides a benefit to a person outside the charitable class, the taxing authority tends to afford greater latitude if that person is not an “insider.”

## 2.3 Private Inurement – Dealing With Insiders

1. Prohibition Covers Any Asset: Real, personal, tangible, intangible.
2. The Meaning of “Insider”: You know one when you see one.
  - Someone who exercises control and/or has influence
  - Derive Meaning of “Insider” from Excess Benefit Transaction Rules – As discussed below, the tax law contains an entire subset of constraints, the so-called intermediate sanctions, that contain an elaborately defined “insider” concept; to what extent will that definition apply to or inform the meaning of “insider” for purposes of the “private inurement” constraint?
  - The First Contract: One Bite at the Apple – Although a senior executive or executive director, once hired, can be expected to be treated as an “insider” for purposes of this rule, before he/she is hired (assuming no other relationship) there should not be “insider” status. Thus, the first contract with the executive is made with a non-“insider”; watch out, however, when it comes time to amend or renew that first contract!

3. Any Amount of Benefit to “Insider” Prohibited.
  - Practice vs. Theory – Technically, the tax law allows for no benefit, regardless of how little, to be afforded to an “insider.” As a practical matter, however, the taxing authorities are, understandably, reluctant to revoke tax-exempt status from otherwise “good” organizations and, consequently, do not usually enforce this rule in such a stringent manner.

## 2.4 Private Inurement – Value For Value Permitted

1. The private inurement rule prohibits any value or benefit paid or afforded to an “insider.” This constraint, however, does not proscribe the tax-exempt organization from paying or providing value to an “insider” (or any person) if the NFP is getting full value in return.
2. Reasonable Compensation for Services – Thus, the private inurement prohibition does not proscribe compensation so long as it is reasonable and necessary for the services rendered in exchange.
3. Fair Price for Property – Similarly, a tax-exempt NFP may pay value to an insider in exchange for property, so long as the property received by the NFP is (at least) equal in value to the consideration paid.
4. Private Foundations Subject to Greater Constraints: The Self-Dealing Rule – Although tax-exempt organizations generally are permitted to enter into commercially reasonable and fair transactions, whether in a compensatory or other setting, organizations classified under the tax law as “private foundations” are subject to a number of additional, more limiting constraints, including with respect to “self-dealing.” In the case of “private foundations,” the meaning of proscribed “self-dealing” is quite expansive and covers many situations that would otherwise be recognized as reasonable and, at “arm’s-length,” indeed even to certain arrangements clearly favorable for the organization.

## 2.5 Situations Giving Rise to Private Inurement (for “Insiders”) or Potential Inurement

1. The private inurement constraint must be considered in connection with every relationship or interaction between the tax-exempt NFP and any of its directors, officers or other “insiders.”
2. NFP boards and managers often fail to appreciate and focus on the many situations in which the private inurement constraint may apply. The following is an illustrative list of some of the many situations that have the potential to raise the private inurement issue:
  - Excessive Compensation
  - Low-Interest Loans
  - Free Use of Assets
  - Rent-Free Use of Premises
  - “Extra” Bonus, Severance, Reimbursements, Perquisites
  - Payment of Legal Fees
  - Portfolio Management and Other Consultant Fees
  - Fundraising Commissions

- Promoting the Business/Reputation of “Insider”
- Advancing “Insiders” Political/Social Agenda
- “Overly Commercial” Activity
- Commercial Joint Ventures

## 2.6 Avoiding Inurement – Best Practices

1. Board Must Set the “Tone” – Organizational culture and day-to-day conduct of “rank and file” is significantly affected by signals emanating from the Board. The Board should establish a culture of scrupulousness regarding the oversight and application of organizational assets.
2. Monitor Every Use of Organizational Funds/Assets
3. “Test” All Transactions Against Mission/Exempt Purpose
4. Adopt and Follow Written Procedures.
  - Board Guidelines/Policies
  - Conflicts Policy
5. Follow Process for Every Insider Transaction.
  - Obtain Comparables and Perform Diligent Analysis – Assure commercial terms of arrangements are at “arm’s-length” (or better for the NFP)
  - Transaction and all its elements considered, deliberated and approved by an independent committee/body
  - Contemporaneous Minutes – Written memorialization of the processes and deliberations undertaken by the independent committee
  - Documentation – Written agreement incorporating every element of the agreement reached with an “insider”
  - Transparency/Disclosure – Form 990

## III. EXCESS BENEFIT TRANSACTIONS – THE INTERMEDIATE SANCTIONS

### 3.1 Tax Law Imposes Monetary Penalties on “Insiders” and Board Members/Managers Involved in an “Excess Benefit Transaction”

1. Applies to Section 501(c)(3) and Section 501(c)(4) Organizations
2. Organizations treated under the tax law as “private foundations” are not covered by these rules and are instead covered by a different (and long-standing) set of potential excise taxes

### **3.2 The Intermediate Sanctions Target a Specific Abuse: “Excess” Value Provided by the Tax-Exempt Organization to an “Insider”**

1. Too much compensation
2. Too high a price for property (of any sort)
3. Direct or Indirect – These sanctions can apply to situations even where the web of relationships and/or arrangements is complex and fuzzy, if a benefit (even if indirectly) has been provided to an “insider”

### **3.3 These Sanctions Were Enacted in 1996 as a Response to the Inadequacy of the Then Available IRS Tools to Combat Abuses**

1. As noted above, while the Private Inurement rule technically proscribes the tax-exempt NFP from affording any benefit to an “Insider,” for many practical reasons the taxing authority cannot strictly enforce the prohibition and revoke exempt status.
2. The Intermediate Sanctions supplement and overlap with Private Inurement rules.
  - IRS has two weapons: Revocation of exempt status and imposition of Intermediate Sanctions

### **3.4 Excess Benefit Transactions – The Penalties**

1. Penalty Imposed on Recipient “Insider.”
  - Initially 25%, and increasing to 200% of uncured excess benefit
  - Cure and abatement provisions are provided
2. Additional Penalty Imposed on Organization Decisionmaker.
  - 10% of excess benefit up to \$20,000 (per excess benefit transaction)
  - Applies to organization trustees, officers, directors and others
  - Imposed on organization managers who knowingly participated
    - Exception if participation not willful AND reasonable cause
    - “Participation” can be by action or inaction
    - Joint and several liability if more than one participating manager

### **3.5 Excess Benefit Transactions –Who Is an “Insider”?**

1. “Disqualified Person” – “Any person who was in a position to exercise *substantial influence* over the affairs” of the organization.
  - Five-year lookback from date of transaction
2. Board Member, CEO, Managing Director, COO, CFO, Treasurer.

3. Family members; 35% controlled entities.
4. Facts and Circumstances Determination of “Substantial Influence.”
  - Relevant Factors:
    - Founder
    - Substantial contributor
    - Employee entitled to revenue-based compensation
  - Exception for employee below specified amount
    - Exception for New Hire Based on Fixed Compensation – Similar to the “first bite at the apple” described earlier in connection with “private inurement,” the tax law does not apply the “intermediate sanctions” to a first-time arrangement with an executive, even though the executive becomes or may become an “insider” as a result of the new arrangement. This exception is specifically defined, and organizations must beware if the arrangement provides any discretionary compensation, as well as if/when the arrangement is renewed or amended.

### 3.6 Excess Benefit Transactions – Rebuttable Presumption

1. If certain requirements are met, the tax law allows a rebuttable presumption that a contractual arrangement with an “insider” does not run afoul of these rules.
  - Contract terms must be pre-approved by independent committee
  - The decision on contract terms must be based on appropriate data/comparables
  - There must be contemporaneous written documentation of the decision process and the agreement
2. The presumption that the contractual arrangement will not be subject to the intermediate sanctions, where established, is rebuttable by the IRS.

### 3.7 Excess Compensation – Tax Cuts and Jobs Act

1. The 2017 Tax Cuts and Jobs Act added Internal Revenue Code Section 4960, which imposes an excise tax equal to the corporate tax rate (currently 21%) multiplied by the sum of:
  - Remuneration to a “covered employee” in excess of \$1 million, and
  - “Excess parachute payments” to “covered employees.”
2. A “covered employee” means the five highest paid employees, or someone who has been in that category with respect to the organization any time after December 31, 2016.
3. “Excess parachute payments” are generally payments triggered by a change in control of the organization that equal or exceed three times the employee’s average pay for the five-year period preceding the change in control.
4. The excise tax is imposed on the tax-exempt organization.

## **IV. JOINT VENTURES WITH NON-EXEMPT PARTNERS ... WHEN DO THE TAX ISSUES ARISE?**

### **4.1 What Is a “Joint Venture”?**

1. Joint venture includes any arrangement by which the profit from an activity is shared between an exempt organization and a third party.
2. The prototypical case is a partnership or joint venture with third party.

### **4.2 Tax Law Focuses on “Substance”: Even a “Simple” Contract Can Be a “Joint Venture”**

- For example, a “royalty” arrangement pursuant to which the exempt organization shares the profits from an activity with a third party, or
- A compensatory arrangement in which a service provider shares in the profit derived from a given activity

### **4.3 NFP Motivations in Fashioning Profit Sharing Arrangements**

- Attract employees
- Exploit and maximize NFP assets – *e.g.*, intellectual property
- Raise capital to support charitable activity
- Facilitate/enable charitable goals – *e.g.*, medical research

### **4.4 Joint Ventures with Non-Exempt Partners – The Stakes**

1. Tax Exempt Status.
  - Activity Attribution – When an exempt organization has an interest in certain types of entities or businesses, the very activity conducted by the entity or business can be treated, under and for purposes of the tax law, as conducted directly by the exempt organization. Depending on the nature and scope of the activity so attributed, the organization’s exempt status can thereby be placed in jeopardy.
  - Private Benefit – In a context where assets are deployed in a venture and some portion of the venture profit inures to the benefit of a third party, it is possible that the exempt organization will run afoul of the prohibition against private benefit (described above).
2. Unrelated Business Taxable Income (“UBTI”) – The exempt organization’s portion of income or profit derived from a joint venture can be characterized as “unrelated business taxable income” and subject to tax.
3. Private Foundation Excise Taxes – Where a “private foundation” engages in a joint venture, it must also analyze the various prohibitions and excise taxes specifically applicable to it under the tax law, including those regarding:
  - Self-dealing
  - Excess business holdings

- Jeopardy investments

#### 4.5 Joint Ventures with Non-Exempt Partners – Protecting Tax-Exempt Status

1. Trap for Both the Unwary and the Wary? – The tax law relating to joint ventures between an exempt organization and any third party is, in many respects, confused, confusing and unsettled, and can be treacherous. The types of potential arrangements that could, at least in theory and often in practice, be cast as a “joint venture” are many and varied, and not always obvious.
2. Situations to Beware of? – To some extent, it is misleading to attempt to list those commercial/financial/economic arrangements with respect to which an NFP needs to be tax law wary. Any form of partnership, limited liability company or other form of venture with a third party should be considered under these tax law principles. As noted earlier, however, the NFP must remain sensitive to these issues with respect to any other forms of commercial relationship in which there is some element or variation of sharing of profits or success of a venture or activity.
3. If an NFP enters a joint venture relationship, what must it do? –There is no generic answer to this question. As a general proposition, it is useful to appreciate that (at least as things stand today) in situations where an exempt organization has a significant interest in a joint venture that is not conducted inside a taxable corporation, the IRS places critical weight on the stated (and contractually/legally binding) objectives of the venture and on the governance and control over the venture’s conduct.
4. When in Doubt, a Prudent Approach – As noted, often it is unclear whether these tax law principles are implicated. The prudent NFP Board or manager, therefore, is on the lookout for and careful with any profit sharing activity/arrangement. In these situations, often the NFP is well-advised to consider and, perhaps, adhere to the following guidelines:
  - Joint venture organizing documents should establish primary overriding charitable/exempt objective
  - NFP should be provided with overriding control
  - If third party management company is involved, ideally it should be one that is not affiliated with the non-exempt partner
  - All joint venture contracts should be at “arm’s length”/fair

## V. IMPROVING THE WORLD: POLITICS, ADVOCACY, LOBBYING

### 5.1 Participating in Political Campaigns

1. A Section 501(c)(3) organization may not participate or intervene, directly or indirectly, in any political campaign on behalf of or in opposition to any candidate for public office.
2. The prohibition is absolute. Violation of it can result in revocation of exempt status.

### 5.2 Who Is a Candidate for Public Office?

1. A candidate for public office is any individual who has offered himself/herself, or has been proposed by others, as a contestant for an elective public office, whether federal, state or local.

### 5.3 What Activities Constitute Prohibited Participation or Intervention in a Political Campaign?

1. Such prohibited activities include, but are not limited to, the publication or distribution of written statements or the making of oral statements on behalf of or in opposition to a candidate.
2. Whether the activities of an organization or its members or officers have engaged in prohibited political activities depends upon all of the facts and circumstances. Organizations often struggle to find the line between permitted conduct – such as advocacy or education concerning important social issues – and prohibited involvement in political campaigns. There simply is no bright line that tells the NFP how far it may go. The extent to which specific NFP conduct may be found to run afoul of this absolute prohibition can depend, in large measure, on the factual/situational context.

### 5.4 IRS Guidance to Help Distinguish Between Prohibited and Permitted Political Activities

The IRS has issued authoritative guidance describing varying factual scenarios, intended to explain the difference between prohibited and permitted political activities. It is useful to consider these issues as divided into 7 classes of activities:

1. Voter Education and Registration and Get-Out-the-Vote Drives – These activities are permitted if conducted in a non-partisan manner. For example, activities designed to encourage voter registration by all eligible voters regardless of their position on candidates or issues is permitted; on the other hand, activities designed to encourage voter registration only by those likely to vote for a particular candidate would be prohibited.
2. Individual Activities by Leaders – Leaders of Section 501(c)(3) organizations may advocate the election of particular candidates but, may not do so at official functions of the organization or in official publications of the organization. In all cases, care should be taken to make clear that views expressed in an “individual” capacity are not those of, or, in effect, being advanced by, the organization.
3. Candidate Appearances – Inviting political candidates to speak at organizational functions is permitted if all candidates are given an equal opportunity to participate.
4. Candidate Appearances When Speaking as Non-Candidate – Candidates may appear or speak at organization events in a non-candidate capacity. Factors the IRS will take into account in determining whether this test is met include: whether the individual is chosen to speak solely for reasons other than his/her candidacy; whether he/she speaks in a non-candidate capacity; whether mention is made of his/her candidacy or the election; whether any campaign activity occurs in connection with the appearance; whether a nonpartisan atmosphere is maintained; and whether the organization clearly indicates the capacity in which he/she is appearing and does not mention the individual’s candidacy or the upcoming election in communications announcing the appearance. Experience shows that this candidate appearance test is not sufficiently objective to prevent serious disagreements over its application in particular situations.
5. Issue Advocacy – Section 501(c)(3) organizations may take positions on public policy issues, including issues on which candidates for public office disagree. They may not do so, however, in a manner that functions as political campaign intervention, such as by identifying the issue with a particular candidate. This issue, too, can become quite murky.
6. Business Activity – Business activity that could be prohibited intervention in a political campaign includes selling or renting of mailing lists or office space and the acceptance of paid advertising.

Such activities will generally not be treated as prohibited intervention if the good, service or facility is available to candidates on an equal basis and if the fee charged is the organization's normal fee.

7. Web sites – A link on a Section 501(c)(3)'s web site to a candidate's web site or to material on another person's web site that endorses a political candidate may constitute prohibited intervention. Factors to consider include: whether links are provided to the web sites of all candidates for a particular office; and whether there is a non-political reason for a link to another web site that may include, among other material, an endorsement of a particular candidate.

## 5.5 Lobbying For/Against Legislation

1. A Section 501(c)(3) organization may not carry on propaganda or other similar activities, or otherwise attempt to influence legislation *as any substantial part of its activities*. Violation of this prohibition can result in loss of tax exempt status.
2. What is "lobbying"?
  - Contacting or urging the public to contact legislators for the purpose of proposing, supporting or opposing legislation.
  - Advocating the adoption or rejection of legislation.
  - "Legislation" is any bill that has been introduced or a draft bill that may be introduced in any legislative body.
3. What is "substantial"?
  - There are no clear guidelines in the tax law. It is safe to say that "substantial" in this context means something less than the majority of an organization's activities; indeed, it clearly means something considerably less. But how much less is not clear. Consequently, where an exempt organization otherwise restricted from "lobbying" does or expects to do more than an insignificant amount of "lobbying," reliance on this test is risky.

## 5.6 The Expenditure Test – An Objective Guideline For Determining Allowable Lobbying

1. The Section 501(h) Election – Recognizing that many exempt organizations needed greater certainty regarding the amount of "lobbying" they could conduct while still retaining their exempt status, Congress (in 1976) enacted a provision that permits an organization, upon making an election, to undertake "lobbying" activity up to specifically defined dollar thresholds.
2. Section 501(h) permits a Section 501(c)(3) organization to elect an objective "expenditure test" in place of the subjective "substantial part test."
3. May All Section 501(c)(3) Organizations Elect the Expenditure Test? No – The expenditure test election is not available to private foundations or churches, associations of churches or a member of an affiliated group of charities that includes as one of its members a church or association of churches.
4. What Does the Expenditure Test Do? – It lays out specific limits on how much money a charity can spend for lobbying based on its exempt purpose expenditures. The rules distinguish between different forms of lobbying and spell out the amount of expenditures permitted for each type. Under this test, there are no limits on lobbying activities that do not require expenditures, including, for example, unreimbursed activities of volunteers.

5. For purposes of the expenditure test, the meaning of prescribed or limited “lobbying” is set out and excludes certain activity/conduct that otherwise might be thought of as “lobbying.”
6. Penalties for Exceeding Expenditure Test Limits – A Section 501(c)(3) organization that elects the expenditure test will not lose its tax exempt status unless it normally makes lobbying expenditures that are more than 150% of the permitted amount. Exceeding the limits can result in a 25% excess tax on the excess lobbying expenditures.

## 5.7 Reporting Lobbying Expenditures

1. Section 501(c)(3) organizations must report lobbying expenditures to the IRS.
  - The Form 990 (annual tax return) requires details regarding organizational lobbying expenditures
2. More detailed reporting is required of organizations that do not make the Section 501(h) election.

## 5.8 Private Foundations And Lobbying

1. Organizations treated under the tax law as “private foundations” are prohibited from any lobbying and can incur severe tax penalties for doing so.
2. Private foundations may make general support grants to publicly supported charities that lobby so long as the grant is not ear-marked for lobbying.

# VI. THE FORM 990 TAX RETURN – DISCHARGING YOUR RESPONSIBILITY AND ANTICIPATING A SHIFTING LANDSCAPE

## 6.1 Overview of Form 990 – Annual Tax Return

1. Form 990 – In 2008, the IRS meaningfully revamped Form 990, the tax return filed annually by most (but not all) exempt organizations. The revised Form 990 demands considerably greater disclosure as to virtually every aspect of the organization’s activity and conduct than the prior version of the Form 990.
2. Form 990 Demands Significant Disclosure – Due to the broad scope and detailed nature of the information it requires, the Form 990 has often been compared to the Form 10-K, the highly detailed GAAP financial statements or Annual Reports of publicly-traded, for-profit companies.
  - In most cases, the Form 990 demands only disclosure, and does not purport to be changing in any respect the tax law requirements previously and still applicable to exempt organizations.
  - Expanded disclosure does, however, result in greater transparency (and reduced anonymity).

## 6.2 IRS Purposes in Making Revisions to Form 990

1. The IRS has indicated that the old (pre-2008) Form 990 “fail[ed] to meet the Service’s tax compliance interests, or the transparency and accountability needs of the states, the public, and local communities served by the organization.”
  - Thus, the IRS admittedly expanded the scope of the Form to serve non-tax reporting and non-federal purposes

2. New sections of the Form require more disclosure regarding the following areas, considered by the IRS to be “Hot Spots,” in order to curtail abuses:
  - Organizational Governance
  - Compensation
  - Fundraising Activities
  - Related Organizations
3. The goal of the IRS is to strongly encourage, by disclosure, the implementation of “good corporate governance” policies and provide the IRS the ability to better identify abusive transactions.

### 6.3 Form 990 Mandates Enhanced Disclosure Regarding Governance and Compensation – These Sometimes Sensitive and Sometimes Neglected Matters Cannot “Fly Below the Radar”

1. Organizational Governance – Revised Form Asks for Extensive Detail.
  - Organization is required to disclose whether it has policies relating to:
    - Conflicts of Interest
    - Whistleblower
    - Document Retention and Destruction
    - Compensation Review
    - Evaluations of Joint Ventures and Investments in Taxable Entities
  - The organization must disclose whether the board has reviewed the completed Form 990 prior to filing, the process used to have the board review the form, and, if applicable, the process used to make the governing documents, conflict of interest policy, and financial statements available to the public.
  - While adoption of these policies is not mandatory, the decision to adopt some or all of them is a “critical tax compliance consideration” that relates to the private benefit, excess benefit and private inurement prohibitions.
2. Compensation – Enhanced Disclosure Required.
  - Disclosure is required for *all* 501(c) organizations (not just 501(c)(3) organizations) with employees compensated in excess of \$100,000.
  - Detailed information required
    - “Key Employees” is now a separate category from highly paid employees; also, disclosure is required for certain former officers, directors, trustees and key employees.
    - Questionnaire regarding details of compensation and benefits (e.g., first class travel, companion travel, social club dues, compensation based on revenue).

- Compensation Details Required – Base compensation, bonus/incentives, deferred compensation and nontaxable benefits.

#### 6.4 Form 990 Mandates Other Areas of Operational Transparency

1. Fundraising Activities – Enhanced disclosure required for amounts paid to professional fundraisers and amounts received from fundraising events.
2. Foreign Operations – Organizations with revenues or expenses exceeding specified threshold amounts are required to provide information about foreign activities, including a listing of grants to foreign organizations and individuals.
3. Related Parties and Organizations
  - Disclosure of “excess benefit transactions,” loans, grants, and business transactions with “interested persons”
  - All Form 990-filing NFPs, not just 501(c)(3) and (c)(4), must disclose loans, grants and business transactions with “interested persons”
4. High Levels of Financial Transparency – An organization must disclose if its separate or consolidated financial statements for the tax year include a footnote that addresses the organization’s liability for uncertain tax positions under FIN 48 (ASC 740). If so, the substance of the FIN 48 footnotes must be disclosed verbatim.

#### 6.5 Other Significant Changes

1. Political Campaign and Lobbying Activities
  - Political Campaign activity disclosure is required by all 501(c) tax-exempt organizations, not just those exempt under Section 501(c)(3).
  - Disclosure of any funds contributed to other organizations for Section 527 function activities (generally, activities that influence elections).
2. Disclosure of Non-Cash Contributions – IRS focuses on valuation issues.

#### 6.6 Form 990 - Potential Pitfalls and Consequences

1. Many governance practices are not required by federal tax law . . . but:
  - The IRS view is that “good governance and accountability practices provide safeguards that *the organization’s assets will be used consistently with its exempt purposes.*”
  - If issues of private inurement or non-tax-exempt purposes arise, the IRS may use the lack of policies as a factor in reaching a determination and choosing a course of action with respect to the issue.
  - Lack of good corporate governance may lead to increased likelihood of audit
2. Disclosures made on the Form 990 could, in extreme cases, lead to loss of tax-exempt status, for example:

- If new disclosures indicate charitable purpose is not being fulfilled
  - If activities such as lobbying and political contributions go beyond allowable limits
3. Disclosures made on the Form 990 could lead to an increase in actual tax liability. Disclosures create more transparency for UBTI related activities.
  4. Failure to file Form 990, Form 990-EZ, 990-PF or Form 990-N for three consecutive tax years leads to an automatic revocation of Federal tax-exempt status as of the due date of the third unfiled return.

## 6.7 The Form 990 – What NFPs Should Do

1. Review the organization’s by-laws and adopt “good governance procedures.” For example, NFPs should consider adopting written policies regarding:
  - Conflicts of interest
  - Whistleblower
  - Document retention and destruction
  - Compensation
  - Joint Ventures
2. Review Financial and Data Reporting Systems – The Form and Schedules require detailed information; NFPs should confirm that their internal systems can generate the required data.
3. Review Compensation of Executives, Key Employees, and Board Members – Given that substantial information will be disclosed AND available to the public, NFPs should focus on their compensation policies and processes and assure that the required disclosure will not adversely affect them in any of their constituencies. Also, NFPs should recognize and anticipate that the enhanced disclosure may necessitate a significant additional expenditure of time and effort for organizations with complicated compensation arrangements and/or other activities that may give rise to compliance concerns or scrutiny.
4. Re-evaluate Fundraising Activities – If disclosing fundraising costs in greater details would have an adverse effect, an organization may consider changing its fundraising models or policies.
5. Evaluate organization’s adherence with federal and state tax rules in anticipation of the greater transparency for taxing authorities to determine taxable activities.

## VII. NFP GOVERNANCE – WHAT THE IRS WANTS, WHAT THE IRS EXPECTS, AND WHAT THE IRS DEMANDS

### 7.1 IRS Involvement in Governance Issues – Background

- In February 2007, the IRS posted on its web site a discussion draft entitled “Good Governance Practices for 501(c)(3) Organizations,” following which the IRS released a draft new Form 990, which contained a section on governance topics.

- In December 2007, the IRS released its new Form 990, which contained a revised governance section. Following its release, the IRS removed its governance discussion draft from its web site.

## 7.2 Current IRS Position

1. *“Despite the absence of explicit statutory provisions setting forth clear governance standards . . . we are not interlopers trying to regulate an area that is beyond our sphere. . . . The effects of good or bad nonprofit governance cut across virtually everything we see and do in our work. It impacts whether the organization is operated to further exempt purposes and public, rather than private, interests. It dictates whether the organization’s executives are compensated fairly or excessively. It influences whether the organization makes informed and fair decisions regarding its investments or its fund raising practices, or allows others to take unfair advantage. . . . It is no longer a question of whether IRS has a role to play, but what that role will be.”* Steven Miller, Commissioner of the IRS’s Tax-Exempt and Government-Entities Division, speaking at a Georgetown University conference on April 23, 2008.
2. In addition to the Form 990 information, the IRS has a 2008 paper entitled “[Governance and Related Topics – 501\(c\)\(3\) Organizations](#)” on its website.
3. On December 3, 2009, the IRS released a “check sheet” that will be used by examination agents “to capture data about governance practices and the related internal controls of organizations being examined.”
4. IRS View on NFP Mission.
  - The IRS believes a charity should have a mission statement and that it should be reviewed regularly
  - Form 990, Part I, Line 1 requires a description of the mission or most significant activities
5. IRS View Regarding Organizational Documents of NFP.
  - A charity must have organizational documents that provide the framework for its governance and management
  - Copies of a charity’s organizational documents must be submitted to the IRS in connection with its application for tax-exempt status
  - Form 990 requires the organization to report significant changes to its organizational documents
6. IRS View Regarding Governing Body of NFP.
  - The IRS believes that the board of a charity should include individuals who are knowledgeable and informed
  - The IRS believes that a board should include independent members
  - Form 990 asks a fair amount of detailed questions about the board
  - The IRS’s belief as to the desirability of independent board members has not (yet) been incorporated in any regulation or administrative rule

7. IRS View Regarding NFP Governance and Management Policies.
  - The IRS will look to see if a charity has implemented policies relating to executive compensation, conflicts of interest, investments, fundraising, documenting governance decisions, document retention and destruction and whistleblower claims
  - Again, these concepts are not incorporated in any regulation or administrative rule
8. IRS View Regarding Financial Statements and Form 990 Reporting.
  - The IRS encourages the NFP board to ensure that financial resources are used to further charitable purposes and that the organization's funds/assets are appropriately accounted for
9. Transparency and Accountability – The Internal Revenue Code requires a tax-exempt charity to make its Form 1023 (the application for tax-exempt status filed by an organization when first seeking tax-exempt status), Form 990 and Form 990-T available for public inspection.

## Not-For-Profit Practice Group

### IRS Form 990

This memorandum provides a general overview of some of the most important governance, policy and practical issues to address when preparing the Internal Revenue Service (“IRS”) Form 990, as revised in 2025.<sup>1</sup>

Even though specific governance, management, and disclosure policies and procedures generally are not required under the federal tax rules, the IRS considers certain policies and procedures, as well as an active and independent board, important elements of an organization’s governance facilitating or even assuring improved tax compliance and protecting against misuse of organization resources. The IRS has observed that the absence of appropriate policies and procedures may lead to opportunities for excessive compensation, excess benefit transactions, private inurement, operation for non-exempt purposes, or other activities inconsistent with exempt status and thus may indicate to the IRS a need for further inquiry.

Whether a particular policy, procedure, or practice should be adopted by an organization depends on the organization’s particular circumstances, including its size, culture, type, structure, and activities. Accordingly, it is important that each organization consider the governance policies and practices that are most appropriate for that organization in assuring sound operations and compliance with tax law and its exempt purpose.

#### I. GOVERNANCE ACTION ITEMS

Form 990 asks many questions about the filing organization’s policies and practices that were in place at the end of the tax year. In short, the IRS seeks affirmative confirmation that the filing organization has in place each of the policies and practices considered by the IRS to reflect and assure good governance. The IRS uses the information reported on the Form 990 to assess noncompliance and the risk of noncompliance with federal tax law for individual organizations and across the broader exempt sector. It is likely that some negative answers will have no consequence, and some will result in further inquiries from the IRS. So that an organization may answer affirmatively to as many of these questions as is appropriate, the following practices or policies should be considered for implementation by an organization:

1. **Written Record of all Board Actions.** Every meeting and action taken by the board (and its committees that act on behalf of the board), should be documented in writing before the next meeting or within 60 days. Typically the documentation should consist of minutes or written consents in the organization’s minute book, but this requirement may also be satisfied by emails, or similar writings, so long as the documentation clearly specifies the action taken, when it was taken, and who made the decision. (Part VI, Section A, Line 8)
2. **Board Review of Form 990.** An organization must report whether the completed Form 990 was provided to directors prior to filing and must also describe the process for review of the Form 990. Organizations have grappled with the “best” approach to satisfy this IRS request. By way of example, a fairly common approach is for the directors (or a committee thereof) to review and to discuss the Form 990 at a board meeting, with an opportunity to pose questions to management about the information on the Form 990, typically in advance of filing. A copy of the organization’s final Form 990 (including required schedules), should be provided to each director, preferably prior to its filing with the IRS. (Part VI, Section B, Line 11, and Schedule O) Generally, organizations design their return preparation processes in a way that does not put undue responsibility on board members or that places final decision-making authority in the hands of too large a group.

3. ***Conflict of Interest Policy.*** An organization should have a written conflict of interest policy. The policy should define conflicts of interest to include when a person in a position of authority over the organization, such as an officer, director, or manager, may benefit financially from a decision he or she could make in such capacity, including indirect benefits such as to family members or businesses with which the person is closely associated.

The organization's officers, directors, trustees, and key employees should disclose or update annually their interests that could give rise to conflicts of interest, such as substantial business or investment holdings, and other transactions or affiliations with businesses and other organizations and those of family members. (Part VI, Section B, Line 12a-b)

The conflict of interest policy should also include practices for monitoring proposed or ongoing transactions for conflicts of interest and dealing with potential or actual conflicts, whether discovered before or after the transaction has occurred. The conflict of interest policy should specify the committee or other body that determines whether a conflict exists, and the body that reviews actual conflicts. Persons with a conflict should be prohibited from participating in the board's deliberations and other decisions regarding the conflict. (Part VI, Section B, Line 12a-c, and Schedule O)

4. ***Whistleblower Policy.*** Most organizations should have a whistleblower policy that encourages staff and volunteers to come forward with credible information on illegal practices or violations of adopted policies of the organization, specifies that the organization will protect the individual from retaliation, and identifies those staff or board members or outside parties to whom such information can be reported. (Part VI, Section B, Line 13)
5. ***Document Retention Policy.*** Most organizations should have a document retention and destruction policy which identifies the record retention responsibilities of staff, volunteers, board members, and outsiders for maintaining and documenting the storage and destruction of the organization's documents and records. (Part VI, Section B, Line 14)
6. ***Joint Venture Policy.*** Tax-exempt organizations are well-advised to adopt a "joint venture policy," particularly if the organization invested in, contributed assets to, or participated in a joint venture or similar arrangement with a taxable entity during the year. (Part VI, Section B, Line 16a-b)

Ideally, an organization should have in place a process through which planned joint venture<sup>2</sup> activity is brought to the attention of the appropriate organization personnel, is considered through the prism of applicable tax and other legal constraints, and is fashioned and implemented in a manner that comports with the requirements and constraints imposed under law. If the organization invested in, contributed assets to, or otherwise participated in a joint venture or similar arrangement with one or more taxable persons, then the organization should:

- a. adopt a written policy or procedure that requires the organization to negotiate, in its transactions and arrangements with other members of the venture or arrangement, such terms and safeguards as are adequate to ensure that the organization's exempt status is protected, and
- b. take steps to safeguard the organization's exempt status with respect to the venture or arrangement.

Some examples of safeguards include the following:

- Control over the venture or arrangement sufficient to ensure that the venture furthers the exempt purpose of the organization.
  - Requirements that the venture or arrangement give priority to exempt purposes over maximizing profits for the other participants.
  - Prohibitions on the venture or arrangement engaging in or involving activities that would jeopardize the organization's exemption (such as political intervention or substantial lobbying).
  - Requirements that all contracts entered into with the organization be on terms that are at arm's length or more favorable to the organization.
7. **Public Availability of Governing Documents and Financial Statements.** The organization should consider making its Form 1023 (Application for Exemption), Form 990, governing documents, conflict of interest policy, and financial statements (whether or not audited) available to the general public, for example by posting them on a website or providing copies upon request. (Part VI, Section C, Lines 18, 19)
8. **Audit Committee Charter.** Most organizations should have an audit committee with a charter that specifies that the committee has responsibility for overseeing the compilation, review or audit of its financial statements, and selection of an independent accountant or auditor that compiled, reviewed or audited the financial statements. (Part XII, Line 2a-c)

## II. GOVERNANCE, MANAGEMENT AND DISCLOSURE

The IRS has implemented its governance oversight through the revised Form 990 which asks many questions about governance and management. Form 990 requires that organizations disclose the information listed below. Presumably certain types of answers to these questions could trigger further inquiry by the IRS.

1. Whether the organization has an **executive committee** or similar committee with broad authority to act on behalf of the governing body, and if so, its composition and scope. (Part VI, Section A, Line 1a, and Schedule O)
2. The number of **independent<sup>3</sup> directors**. (Part VI, Section A, Line 1b)
3. Whether any of the organization's **officers, directors, trustees, or key employees, had a family relationship or business relationship** with another of the organization's officers, directors, trustees, or key employees. (Part VI, Section A, Line 2, and Schedule O)

To answer the questions on lines 1 and 2 of Part VI (regarding independent directors and business and family relationships among Board members, officers, and key employees) the organization should engage in a reasonable effort to obtain the necessary information to answer these questions. An example of a reasonable effort would be for the organization to distribute a questionnaire annually to each of the organization's officers, directors, trustees, and key employees asking for the information that needs to be reported in response to questions on relationships in lines 1 and 2. The questionnaire could include the name, title, date, and signature of the person reporting information, and contain the Form 990 Glossary definitions of "independent voting member of governing body," "family relationship," "business relationship," and "key employee." The organization may rely on

information it obtains in response to such a questionnaire in answering questions on lines 1 and 2.

4. Whether the organization has **delegated to a management company key management duties** that are customarily performed, or supervised, by officers, directors, or key employees. Such management duties include, but are not limited to, hiring, firing, and supervising personnel, planning or executing budgets or financial operations, or supervising exempt operations or unrelated trades or businesses of the organization. Management duties do not include administrative services (such as payroll processing) that do not involve significant managerial decision-making. Management duties also do not include investment management unless the filing organization conducts investment management services for others. (Part VI, Section A, Line 3, and Schedule O)
5. Significant **changes to its governing documents**. (Part VI, Section A, Line 4, and Schedule O)
6. Any **significant diversion of the organization's assets**. A diversion of assets is any unauthorized or improper use of assets (including embezzlement or theft). Diversion does not include transfers for fair market value. A diversion is considered material if the gross dollar amount exceeds the lesser of \$250,000 or 5% of the organization's gross receipts or total assets. (A diversion of assets may in some cases constitute inurement of the organization's net earnings. In the case of Section 501(c)(3) and Section 501(c)(4) organizations, it also may be an excess benefit transaction taxable under section 4958 of the Internal Revenue Code and reportable on Schedule L). (Part VI, Section A, Line 5, and Schedule O)
7. **Loans or grants to any current or former officer, director**, trustee, key employee, highly compensated employee, or other manager. (Part IV, Lines 26, 27, and Schedule L)
8. Certain types of **fringe benefits** such as first-class or charter travel, travel for companions, tax indemnification and gross-up payments, discretionary spending accounts, housing allowance or payment for business use of personal residence, health or social club dues, bodyguard, chauffeur, financial planner, lawyer, accountant, tax preparer or other personal service providers must be disclosed on Schedule J to the Form 990 regardless of whether the items are reported as compensation on a Form W-2 or 1099. The organization must also indicate whether it followed a written policy regarding payment or reimbursement of such expenses and, if not, it must explain why not. The IRS has stated that the reason for disclosure of these items is to highlight for the IRS potential areas of unreported compensation and arrangements that provide excess benefits to nonprofit executives. An IRS finding of unreported compensation or excess benefit could result in additional taxes and penalties to the executive on the unreported compensation and punitive excise taxes paid by the organization. The Form 990 provides an area for organizations to explain that their use of such benefits is proper and does not result in unreported executive compensation or excess benefits. Additionally, all Section 501(c)(3) and 501(c)(4) organizations must report and explain **compensation contingent** on the revenues or earnings of the organization or any related organization, and **non-fixed payments** (e.g., amounts paid subject to the initial contract exception of the intermediate sanctions provision<sup>4</sup>). (Part IV, Line 23, and Schedule J)
9. The Form 990 Part VI requires **disclosure of additional governance items on Schedule O** (Part VI, Lines 2-9, 11, 12, 15 and 19):
  - a. whether the organization has members and if they elect the directors;
  - b. whether minutes are taken of all board meetings and committees that have board authority;

- c. the process by which the organization reviews its Form 990 and whether it is provided to the board prior to filing;
- d. a description of how the organization monitors and enforces compliance with its conflicts policy, including the process for monitoring proposed or ongoing transactions for conflicts, and the process for dealing with potential or actual conflicts (see instructions for details); and
- e. a description of the process by which the compensation of officers and key employees was determined.

### **III. DISCLOSURE OF DIRECTORS, OFFICERS, AND COMPENSATION AMOUNTS AND PROCEDURES**

The organization must list all of its current officers, directors, and trustees, as those terms are defined in the Form 990 instructions, regardless of whether any compensation was paid to such individuals. Form 990 also requires more disclosure of compensation arrangements and the process used to determine the compensation amounts.

#### **3.1 Disclosure of Compensation**

In addition to current officers, directors, and trustees, the organization must list up to 20 current employees who satisfy the definition of key employee (persons with certain responsibilities and reportable compensation greater than \$150,000 from the organization and related organizations), and its five current highest compensated employees with reportable compensation of at least \$100,000 from the organization and related organizations who are not officers, directors, trustees, or key employees of the organization. The compensation must be reported when it is paid by the organization or from a related organizations (such as, parents, subsidiaries, sibling organizations and other organization that share common control, supporting organizations and supported organizations).

Organizations are required to list the following officers, directors, trustees, and employees of the organization whose reportable compensation from the organization and related organizations exceeded the following thresholds:

<b>Position</b>	<b>Current or former</b>	<b>List on Form 990, Part VII, Section A:</b>	<b>List on Schedule J (Form 990), Part II:</b>
Directors and Trustees	Current	All	If reportable and other compensation > \$150,000 in the aggregate from organization and related organizations (do not report institutional trustees)
	Former	If reportable compensation in capacity as former director or trustee > \$10,000 in the aggregate	If listed on Form 990, Part VII, Section A (do not report institutional trustees)
Officers	Current	All	If reportable and other compensation > \$150,000 in the aggregate from organization and related organizations
	Former	If reportable compensation > \$100,000 in the aggregate	If listed on Form 990, Part VII, Section A

Position	Current or former	List on Form 990, Part VII, Section A:	List on Schedule J (Form 990), Part II:
		from organization and related organizations	
Key employees	Current	All	All
	Former	If reportable compensation > \$100,000 in the aggregate from organization and related organizations	If listed on Form 990, Part VII, Section A
Other Five Highest Compensated Employees	Current	If reportable compensation > \$100,000 in the aggregate from organization and related organizations	If reportable and other compensation > \$150,000 in the aggregate from organization and related organizations
	Former	If reportable compensation > \$100,000 in the aggregate from organization and related organizations	If listed on Form 990, Part VII, Section A

“Reportable compensation” generally means compensation reported in Box 5 of the employee’s Form W-2, Box 1 of a non-employee’s Form 1099-NEC, or Box 7 of a non-employee’s Form 1099-MISC. “Other compensation” generally means compensation that is not reportable compensation, including deferred compensation. The instructions to Part VII explain these terms, and also provide a more detailed table listing various types of compensation and where to report them in Part VII or in Schedule J.

### 3.2 Compensation Amounts

The organization should ensure that no more than *reasonable compensation* is paid. “Reasonable compensation” is the value that would ordinarily be paid for like services by like enterprises under like circumstances. The instructions to Form 990 list several items that count as compensation, all of which are taken into account for determining the value and reasonableness of the compensation. The tax law generally prohibits, and can subject an organization to loss of exempt status as a result of any excessive compensation arrangement. Unreasonable compensation could also result in an *excess benefit transaction*: a transaction in which specified “insiders” and others thought to hold positions of power/authority, including a current or former manager, receives an economic benefit from the organization which exceeds the value of the consideration (such as performance of services) to the organization. An excess benefit transaction also can occur when a manager embezzles from the organization. Recipients of excess benefits and the directors or officers who approve the excess benefits are subject to tax penalties.<sup>5</sup>

### 3.3 Process for Determining Compensation

Form 990 requires disclosure of whether the organization used a process for determining the compensation of the CEO (or executive director, or other person who is the top management official) and of other officers or key employees that included all of the elements listed below for a rebuttable presumption of reasonable compensation (i.e., whether the process for determining compensation of those persons included review and approval by independent persons, comparability data, and contemporaneous substantiation of the deliberation and decision). If the organization did use such a process, then they must describe the process on Schedule O, identify the offices and persons for which the process was used to establish compensation, and state the year in which this process was last used for each such person. (Part VI, Line 15a, b, Schedule J and Schedule O)

### 3.4 Rebuttable Presumption of Reasonable Compensation

Fixed payments (but not discretionary bonuses<sup>6</sup>) under a compensation arrangement are presumed to be reasonable if the following three conditions are met:<sup>7</sup>

1. Review and approval of compensation arrangements by the **disinterested members of the board or the compensation committee** (*i.e.*, persons with conflicts were not involved).
2. **Use of data showing comparable compensation** for similarly qualified persons in functionally comparable positions at similarly situated organizations (both taxable and non-taxable). This may include consulting an independent compensation consultant, reviewing Form 990s of other organizations, compensation surveys, actual written offers from similar organizations competing for the executive's services, or other objective external data to establish comparable values for executive compensation. The use of these items are also disclosed on Schedule J.
3. The board or committee **adequately documents its deliberations and the basis for its determination** that the compensation is reasonable in the minutes of the board or the committee. The minutes should include:
  - a. the terms of the compensation arrangement that were found reasonable;
  - b. the comparability data relied upon by the authorized body and how the data was obtained;
  - c. any member of the board or committee who abstained or voted against the arrangement; and
  - d. whether a member of the board or committee having a conflict of interest was recused or took other action.

In some cases, an organization may find it impossible or impracticable to fully implement each step of the rebuttable presumption process described above. In such cases, most organizations should try to implement as many steps as possible, in whole or in part, in order to substantiate the reasonableness of benefits as timely and as well as possible. These requirements for a "rebuttable presumption," however, may not be appropriate for certain organizations; even so, organizations are well-advised to take any and all steps that *are* reasonable, given their circumstances, to assure proper compensation arrangements. In addition to the steps above, having written documentation of the approved compensation amounts, (*e.g.*, in a written employment agreement, approved budget line item, or board or committee resolution) is helpful to avoid later assertions that a compensation amount is more (or less) than that agreed and that it was determined within the proper framework and procedures.

An important exception to the excess benefit rules and the reasonable compensation requirement is the exception for any fixed payment made pursuant to an initial contract when the contract is both in writing and is with a previously unaffiliated officer or manager.<sup>8</sup> This is an "exception" because (and assuming) there had been no prior relationship between the organization and the other party. In these cases, however, the organization is well-advised to anticipate the application of these rules, and the need to conform with these rules at such later date when the contract is renewed or even materially changed or amended. Renewals and material amendments are often treated under the tax law as new contracts and, consequently, the relationship with the contracting party may, at that subsequent time, have become one that is covered by these excess benefit transaction rules.

#### IV. WHEN TO FILE FORM 990

The Form 990 must be filed within five months and 15 days following the end of the organization's taxable year. For a calendar year organization (where the accounting period ends on December 31st), the due date for Form 990 is May 15th. For an organization with a fiscal year ending September 31, the Form 990 is due February 15th. The due dates may be extended up to six months by filing Form 8868.

*This memorandum is not designed to answer the many questions and issues that arise in connection with the preparation and filing of the Form 990, or otherwise to substitute for the expert advice of a qualified tax return preparer. Please contact your tax return preparer, accountant or an attorney if you have questions about the requirements of Form 990.*

ENDNOTES

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<sup>1</sup> Note that Section 501(c)(3) charities sub-categorized as “private foundations” file the Form 990-PF, and do not file the revised Form 990. In addition, depending on certain asset and/or revenue tests, many organizations will be eligible to file the less burdensome Form 990-EZ or Form 990-N.

<sup>2</sup> Under the tax law, “joint venture” is broadly defined and includes many economic relationships not conventionally or colloquially referred to or thought of as “joint ventures.” A joint venture or similar arrangement means any joint ownership or contractual arrangement through which there is an agreement to jointly undertake a specific business enterprise, investment, or exempt-purpose activity (without regard to (1) whether the organization controls the venture or arrangement, (2) the legal structure of the venture or arrangement, or (3) whether the venture or arrangement is treated as a partnership, association, or corporation for federal income tax purposes). Disregard ventures or arrangements that meet both of the following conditions: (1) 95% or more of the venture’s income for its tax year ending with or within the organization’s tax year is described in Sections 512(b)(1)-(5) of the Internal Revenue Code (generally, passive investment income including unrelated debt-financed income) and (2) the primary purpose of the organization’s contribution to, or investment or participation in, the venture or arrangement is the production of income or appreciation of property.

<sup>3</sup> According to the Form 990 Instructions, a director is considered “independent” only if all three of the following circumstances apply:

- a. The director was not compensated as an officer or other employee of the organization or a related organization.
- b. The director did not receive total compensation or other payments exceeding \$10,000 during the tax year from the organization (or related organizations) other than reimbursement of expenses or reasonable compensation for services as a director. For example, a person who receives reasonable expense reimbursements and reasonable compensation as a director of the organization does not cease to be independent merely because he or she also receives payments of \$7,500 from the organization for other arrangements.
- c. Neither the director, nor any family member of the director, was involved in a loan, grant (*e.g.*, scholarship, award), excess benefit transaction, or certain business transactions involving interested persons, with the organization (whether directly or indirectly through affiliation with another organization) required to be reported on Schedule L. See Form 990 Instructions for transactions required to be reported on Schedule L.

<sup>4</sup> See Schedule J instructions and Treas. Reg. § 53.4958-4(a)(3).

<sup>5</sup> A recipient who receives an excess benefit from unreasonable compensation is liable for a 25% (or 200% if not corrected) tax on the excess benefit. Also, organization managers who participate in an excess benefit transaction knowingly, willfully, and without reasonable cause are liable for a 10% tax on the excess benefit (up to \$20,000). See IRC § 4958.

<sup>6</sup> Nonfixed payments (*e.g.*, a discretionary bonus) may not have a presumption of reasonableness unless there is a specified cap on the amount and the authorized body establishes a rebuttable presumption as to the maximum amount payable under the contract.

<sup>7</sup> See Form 990, Part VI, Line 15. There is a special safe harbor for small organizations. If the organization has gross receipts of less than \$1 million, appropriate comparability data includes data on compensation paid by three comparable organizations in the same or similar communities for similar services.

<sup>8</sup> Treas. Reg. § 53.4958-4(a)(3).

## Not-For-Profit Practice Group

### Issues and Concerns for Directors of Troubled Not-For-Profit Organizations: Recognizing and Facing the Challenges

#### I. FIDUCIARY DUTIES

All directors owe certain fiduciary duties to their organizations, whether the organizations are for-profit or not-for-profit. For example, directors owe a duty of care, which requires them to be informed, attend board meetings, exercise independent judgment, and act in good faith. Directors also owe a duty of loyalty, which requires them to act in the best interests of the corporation by avoiding conflicts of interest, observing confidentiality obligations, and not abusing corporate opportunities for personal gain. In general, the directors of a solvent organization owe their duties to the organization and, in the context of a for-profit corporation, its shareholders, but not to creditors.<sup>1</sup> When an organization is insolvent, however, most courts recognize that fiduciary duties are owed to, or at least can be enforced by, creditors.<sup>2</sup> When an organization is merely in the “zone of insolvency,” a murky area that occurs when the organization cannot generate and/or “obtain enough cash to pay for its projected obligations and fund its business requirements for working capital and capital expenditures with a reasonable cushion to cover the variability of its business needs over time,”<sup>3</sup> the law varies from jurisdiction to jurisdiction as to whether directors’ fiduciary duties expand to creditors.<sup>4</sup>

In the for-profit context, depending on the jurisdiction in which a corporate entity is incorporated, the fact that duties may be owed to creditors upon insolvency typically means that directors should maximize the value of the corporation for its creditors and other parties in interest. In the not-for-profit context, however, a director also has a duty of obedience to the organization’s charitable mission.<sup>5</sup> The challenge for a director of an insolvent (or potentially insolvent) not-for-profit organization in New York is to balance the interests of the organization’s creditors against the interest of preserving and adhering to the organization’s charitable mission.<sup>6</sup> Although many for-profit corporations are able to rely on their own operations to sustain themselves in times of crisis, many not-for-profit corporations rely on donations, which may not be enough to sustain themselves. Directors of not-for-profits need to be mindful of their organization’s commitments and expenses when the organization’s solvency depends on future fundraising and donations.

Abandonment of an organization’s charitable mission should be a last resort.<sup>7</sup> Thus, in evaluating a proposed sale of the assets of a not-for-profit corporation, the Attorney General or a court will consider whether the sale will promote the interests of the organization.<sup>8</sup> For example, if a not-for-profit animal rescue organization proposes to sell its assets to a greyhound racing business, the Attorney General or a court may be unwilling to sanction the sale. Accordingly, directors of a troubled not-for-profit organization should be aware that they must keep the organization’s charitable mission at the forefront of their concerns when making decisions about the organization’s fate.

The consequences of breaching a fiduciary duty owed to a not-for-profit corporation are just as severe as the consequences for breaching a duty owed to a for-profit entity. These consequences can include personal liability, as well as the negative impact the breach could have on employees and on those who rely on the charitable purpose of the organization.

#### II. DEALING WITH CREDITORS

When a not-for-profit organization runs into trouble, often the first parties it will hear from are its creditors. Generally, creditors do not share the same concerns about an organization’s charitable mission and may threaten various remedies to force a not-for-profit organization to pay its debts. As not-for-profit organizations do not always have operations that generate cash, such organizations have limited sources of

funds with which to satisfy their creditors. Borrowing money to repay creditors may not be an option for a troubled not-for-profit and, even if it is, the organization ultimately will have to generate the funds to repay its loans. Moreover, many donations and grants are restricted and cannot be used to repay creditors or to finance general operations. The Attorney General or the courts may impose restrictions on an organization's ability to sell its real estate or substantially all of its assets to pay its creditors if they see such sales as a threat to the organization's charitable mission.<sup>9</sup> Thus, when a not-for-profit organization encounters financial difficulties, developing a restructuring plan acceptable to creditors may be more complicated than it would otherwise be for a regular corporate entity.

## 2.1 Accessing Charitable Donations to Pay Creditors

State law determines whether a not-for-profit organization will be able to access private donations to repay its creditors, regardless of whether it is in bankruptcy.<sup>10</sup> Under New York law, for example, a not-for-profit organization is bound to observe the restrictions donors place on their contributions.<sup>11</sup> Notably, these restrictions also apply to interest and appreciation on donated funds if the gift instrument expressly specifies the donor's intent that the organization may not spend any accrued appreciation.<sup>12</sup>

New York law requires the board of a not-for-profit corporation to cause the corporation to keep accurate accounts of directed donations separate and apart from other accounts.<sup>13</sup> New York law also requires the organization's treasurer to make an annual report to the organization's members (or board, as applicable) regarding the use of restricted assets and the income derived from them.<sup>14</sup> Misuse of restricted funds (or the failure to comply with restrictions) may give rise to personal liability for the directors, officers, or key persons<sup>15</sup> or to an action for an order requiring the return of the funds to the donor.<sup>16</sup>

Organizations may attempt to obtain releases of donor restrictions by (i) obtaining the donor's consent in a record,<sup>17</sup> or (ii) applying to the state supreme court (or the surrogate's court if the gift was by will), if "the restriction has become impracticable or wasteful, it impairs the management or investment of the fund, or if, because of circumstances not anticipated by the donor, a modification of [the] restriction will further the purposes of the fund."<sup>18</sup> In evaluating whether to authorize a release of a donor restriction, a court must determine whether (i) the gift was charitable in nature, (ii) the language of the gift instrument indicates the donor intended a general, rather than specific, charitable intent, and (iii) the purpose for which the gift was created has failed.<sup>19</sup> Even if a restriction is released, however, the released funds must be used for the charitable purposes of the corporation rather than general operating expenses.<sup>20</sup>

Similarly, under New York law, charitable gifts may not be considered property of a bankruptcy estate for distribution to creditors upon dissolution.<sup>21</sup> One New York court rejected the argument that payment of a charitable organization's debts is a proper charitable purpose.<sup>22</sup> In so deciding, the court noted that donors who made general gifts to charitable organizations intended to further "the charitable purpose for which the entity was formed as set forth in its charter. In the case of hospital corporations, such purpose is deemed to be the actual and continued provision of acute patient care services rather than the satisfaction of creditors' claims."<sup>23</sup>

A bankruptcy court in Massachusetts issued a contrary decision allowing not-for-profit debtors to use restricted gifts to repay their creditors.<sup>24</sup> The court went so far as to hold that the debtor, which was liquidating and had permanently discontinued its charitable operations, could still receive bequests intended for charitable purposes and apply them to satisfy the claims of its creditors. On appeal, however, the United States Court of Appeals for the First Circuit noted that it disagreed with the bankruptcy court's extension of the definition of "charitable purposes" to payment of creditors where the organization had discontinued its charitable operations.<sup>25</sup> The First Circuit's decision turned on the timing of the gift.<sup>26</sup> The court found that, because the bequest in question had vested when the hospital was still operating, the hospital could use the proceeds to pay its creditors for debts incurred while the organization was still operating.<sup>27</sup> Accordingly, the court affirmed the bankruptcy court's decision allowing the organization to use the bequest to pay its creditors' claims.

The United States District Court for the District of Columbia affirmed a similar bankruptcy court decision.<sup>28</sup> However, the court's decision was based on the District of Columbia not-for-profit corporation law, which provided that a dissolving not-for-profit corporation must first satisfy its liabilities to creditors before any charitable gifts are returned or distributed to other charitable institutions. Notably, the D.C. statute relied upon has since been superseded.<sup>29</sup> Now, when a not-for-profit is dissolved under D.C. law, "[p]roperty held in trust or otherwise dedicated to a charitable purpose shall not be diverted from its purpose by the dissolution of [the not-for-profit] corporation unless and until the corporation obtains an order of the" court.<sup>30</sup>

## 2.2 Soliciting Additional Donations

As discussed above, troubled organizations may not be able to tap into restricted funds to pay creditors. Troubled organizations, however, may decide to go public with their troubles in an attempt to bring in new donations to pay creditors. Depending upon the organization and the circumstances, public awareness of the organization's financial troubles may stimulate or impede fundraising. If the organization decides to seek additional donations during a period of financial trouble, donors may be more inclined to restrict donations or seek assurances that their contributions will be used for charitable purposes rather than to pay creditors. Because New York courts will not infer that donors intended their gifts to be used to pay creditors, financially troubled New York organizations that solicit donations may want to consider setting up special unrestricted funds or creating a pledge form that explicitly allows the organization to use the gift in support of operations and/or restructuring.

## 2.3 Compelling Donors to Pay Their Pledges

Troubled organizations may also seek to bring in money by enforcing outstanding pledges for charitable contributions. Under New York case law, pledges are generally enforceable.<sup>31</sup> A pledge can create a unilateral contract between the pledgor and pledgee. The pledgor can be compelled to complete performance on the pledge if there was consideration for the pledge, such as the creation of a named scholarship on the pledgor's behalf, or if the pledgee acted in substantial reliance on the pledge. Such reliance may include using a pledge agreement as collateral to obtain the funds necessary to carry out the organization's charitable mission and to honor the promises the organization made to the donor in return for the pledge.

As discussed above, however, if the organization is seeking to compel payment on pledges or bequests for the purpose of paying its creditors, this analysis may change. Moreover, even if an organization may be able to compel payment on pledges, the organization should consider whether doing so would create public relations problems that outweigh the benefits of receiving the pledges.

## 2.4 Member Contributions

Creditors may also seek payment from members of not-for-profit corporations. Such members will only be liable to the extent of (i) any unpaid portion of lawfully imposed initiation fees, membership dues, or assessments and (ii) any other debts the members owe to the organization.<sup>32</sup> Notably, however, a creditor may only bring an action to apply such liability to a debt of the corporation if the corporation is adjudged bankrupt or the creditor obtains a final judgment against the corporation that is unsatisfied.<sup>33</sup>

## 2.5 Accessing Government Grants to Pay Creditors

A number of courts have held that federal grants remain the property of the federal government unless and until expended in accordance with the terms of the grant.<sup>34</sup> These courts arrived at their holdings by evaluating the specific restrictions placed by the government on each organization's use of grant funds.<sup>35</sup> According to one court, where a grant specifically provides that its proceeds may be used to pay a grantee's creditors, then such grant will be considered property of the grantee's bankruptcy estate.<sup>36</sup> But because

many federal grants impose such “pervasive restrictions” on the identity of the grantee and the administration of the funds, the grantee cannot be considered to have a property interest in the grant.<sup>37</sup> Accordingly, such grants generally are not considered property of the bankruptcy estate.<sup>38</sup> Notably, even if an organization is able to treat the proceeds of government grants as property of the estate, the organization may have trouble securing future grants.

## 2.6 Selling Assets to Pay Creditors

Troubled not-for-profit organizations may decide to sell assets in order to repay creditors. Although this seems straightforward, many states require board and/or court approval of significant asset sales. In New York, for example, a not-for-profit organization generally must secure the approval of two-thirds of its board before selling all or substantially all of its assets (or a majority of the board if the corporation has more than 20 board members).<sup>39</sup> In addition, in New York, charitable corporations must seek approval from a court or the Attorney General before selling all or substantially all of their assets.<sup>40</sup> The court or Attorney General may require the assets to be distributed to organizations involved in substantially similar activities.<sup>41</sup> Moreover, because the Bankruptcy Code requires sales of property of a not-for-profit debtor’s estate to be conducted in accordance with applicable nonbankruptcy law, not-for-profit organizations that file for bankruptcy protection will not be able to avoid state law provisions governing the sales.<sup>42</sup> They, however, may be able to substitute what may be a more expeditious bankruptcy court approval for the requirement of obtaining state court approval.

The Bankruptcy Code also may affect sales of donor lists and other personally identifiable information. Section 363(b)(1) of the Bankruptcy Code provides that if the debtor “in connection with offering a product or a service discloses to an individual a policy prohibiting the transfer of personally identifiable information about individuals to persons that are not affiliated with the debtor and if such policy is in effect on the date of the commencement of the case, then the trustee may not sell or lease personally identifiable information to any person unless” the sale is consistent with the privacy policy or a consumer privacy ombudsman is appointed and the court approves the sale.<sup>43</sup> Even though this provision is not explicitly directed at not-for-profit corporations, such organizations should be aware of the potential impact on a not-for-profit debtor’s sale of donor lists where the debtor had previously indicated to its donors that their personally identifiable information would be kept private.

If a not-for-profit enters into any real estate transactions, it should be sure it complies with any special approval requirements imposed by the applicable not-for-profit statute. For example, in New York, a not-for-profit corporation may not purchase or dispose of real property where such property would, upon its purchase, constitute all or substantially all of the assets of the corporation, unless authorized by two-thirds of the entire board of directors (or a majority of the board if the corporation has more than 20 board members).<sup>44</sup>

The statute does not address the consequences of the failure to comply with this provision, although, given the “strong-arm” powers of a debtor in possession or trustee in bankruptcy, lessors and counterparties to real estate transactions may face an attempt to unwind any transaction for which the statutory approval was not obtained. It is also not clear what liability directors and officers could face for failing to comply with this provision.

## III. DIRECTOR AND OFFICER LIABILITY

When an organization runs into trouble, any number of parties may seek to impose liability on the organization’s directors and officers. These parties include (i) employees (*e.g.*, wrongful termination or Anti-Discrimination Act violations), (ii) outsiders (*e.g.*, vendors and other not-for-profits), (iii) the not-for-profit corporation itself (via derivative claims), (iv) other directors (for violation of fiduciary duties), (v) beneficiaries of the organization’s mission, (vi) members, (vii) donors (*e.g.*, misuse of a restricted gift), (viii) state attorneys general, and (ix) other government officials (*e.g.*, the IRS and the Department of

Labor). Directors may be held liable for any number of acts or omissions. Examples of such types of liability are provided below.

### 3.1 Employee Wages

Under New York law, directors and officers may be subject to criminal liability for failing to pay employee salaries as they come due.<sup>45</sup> In addition, directors and officers of an organization can be held personally liable if the organization fails to pay the government withholding taxes (including income tax, social security, and Medicare taxes) deducted from employee wages.<sup>46</sup> Accordingly, if a not-for-profit organization encounters financial difficulties, the board should ensure that employee-related payments are not diverted to pay creditors.

### 3.2 Taxes

Under New York law, directors and officers can also be held personally liable if the organization fails to pay certain taxes. For example, New York law imposes personal liability on directors and officers who are “responsible persons” for collected but unremitted sales and use taxes.<sup>47</sup> Whether an individual qualifies as a “responsible person” is determined from the particular facts and circumstances of each case.<sup>48</sup> Not-for-profit organizations, however, should be aware that directors or officers who exercise sufficient authority or control over financial and tax matters may be held personally liable when a company fails to remit certain taxes owed.

### 3.3 Director Support of Prohibited Actions

Another common basis for imposing liability on not-for-profit directors is director support of actions prohibited by law. Section 719 of the New York Not-For-Profit Corporation Law (the “N-PCL”) makes directors jointly and severally liable for the benefit of creditors, members, or an organization’s ultimate beneficiaries to the extent of any injury caused by the director’s voting for or support of prohibited actions.<sup>49</sup> Examples of such prohibited actions include (i) self-dealing, (ii) redemption or payment of interest on capital certificates, subvention certificates, or bonds contrary to not-for-profit corporation law, and (iii) distribution of assets after dissolution of the corporation (a) in violation of New York’s requirement that a not-for-profit corporation’s assets be distributed to entities engaged in substantially similar activities or (b) without paying or adequately providing for all known liabilities of the corporation (excluding untimely claims). If a director is found to have discharged his or her duties to the organization pursuant to section 717 of the N-PCL, however, the director will not be held liable for supporting the prohibited action.<sup>50</sup> Section 717 requires directors and officers to discharge their duties “in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.”<sup>51</sup> Notably, section 717 allows directors to rely on information or reports prepared by officers or employees of the organization, counsel or other professional advisors, or a committee of the board, provided such directors (i) believe such committee or individuals are competent and reliable, and (ii) do not have knowledge that would make such reliance unwarranted.<sup>52</sup>

### 3.4 Director, Officer, or Key Person Misconduct

Directors, officers, or key persons may be subject to liability for neglect or violation of their duties in managing corporate assets or for knowingly supporting or effecting unlawful conveyances of corporate assets.<sup>53</sup> Specifically, section 720(a) of the N-PCL provides:

- (a) An action may be brought against one or more directors, officers, or key persons of a corporation to procure a judgment for the following relief:
  - (1) To compel the defendant to account for his official conduct in the following cases:

- (A) The neglect of, or failure to perform, or other violation of his duties in the management and disposition of corporate assets committed to his charge.
  - (B) The acquisition by himself, transfer to others, loss or waste of corporate assets due to any neglect of, or failure to perform, or other violation of his duties.
- (2) To set aside an unlawful conveyance, assignment or transfer of corporate assets, where the transferee knew of its unlawfulness.
  - (3) To enjoin a proposed unlawful conveyance, assignment or transfer of corporate assets, where there are reasonable grounds for belief that it will be made.<sup>54</sup>

Section 720 applies to wrongful transfers of corporate assets by not-for-profit directors, officers, or key persons to themselves and unauthorized use of corporate funds for personal expenses.<sup>55</sup>

Actions for misconduct may be brought by the state attorney general, the corporation itself, other directors or officers, a state law receiver, a bankruptcy trustee, judgment creditors, members (as a derivative action), or, if the organization's bylaws permit, by a party who contributed at least \$1,000 to the organization.<sup>56</sup>

### 3.5 Excess Benefits and Compensation

Not-for-profit directors who receive or approve excess benefits are subject to liability under both state and federal law. Under New York law, not-for-profit corporations may elect or appoint officers and fix the reasonable compensation of directors and officers.<sup>57</sup> Although New York law provides little guidance to not-for-profit boards for setting director compensation,<sup>58</sup> section 715(e) generally requires a vote of the majority of the entire board to set officer compensation.<sup>59</sup> In one high profile case, the New York Court of Appeals considered a complaint for excessive compensation against the former chairman of the New York Stock Exchange. One of the counts of the complaint included a claim for violation of section 715(f), which requires approval of the majority of the board to fix an officer's salary if not done in or pursuant to the bylaws.<sup>60</sup> The Court of Appeals dismissed the claim because it found that it would impose liability on directors without any proof that they were at fault. According to the court, this was contrary to the general design of the not-for-profit corporation statute, which provides directors with a "business judgment" defense if they can show that they acted in good faith.<sup>61</sup> The decision suggests that proper authorization procedures may help protect directors against liability, while at the same time, technical violations of the statute will not automatically result in liability where the directors acted in good faith.

In addition to incurring liability for excess compensation under state law, not-for-profit directors may be subject to liability under federal tax law for excess benefits. The IRS may impose "intermediate sanctions" on not-for-profit directors who receive or approve excess benefits. Intermediate sanctions are excise taxes of 25% on the amount of the excess benefit.<sup>62</sup> Even if an offending director pays the 25% tax, failure to return the excess benefit, with interest, may result in the imposition of an additional excise tax of 200% of the benefit.<sup>63</sup>

In determining whether a benefit is excessive, the IRS will look to the market and to the compensation allowed at similar organizations.<sup>64</sup> There is a rebuttable presumption that compensation is not excessive if it satisfies the following test: (i) it was approved in advance by an authorized body—such as a compensation committee—of individuals, none of whom had a conflict of interest with regard to the compensation decision at issue, (ii) the authorizing body relied on comparable data to set compensation (*i.e.*, compensation of similar individuals at comparable organizations), and (iii) the decision was adequately documented.<sup>65</sup> Accordingly, not-for-profit directors should insist that their organizations implement compensation approval systems that will satisfy this test.

### 3.6 Limitations on Liability

Except with respect to director misconduct and director support of prohibited actions as described above and except with respect to actions brought by the Attorney General or a beneficiary of a charitable trust, directors who do not receive compensation for their services cannot be held liable to any entity other than the corporation itself unless such directors were grossly negligent or intended to cause harm.<sup>66</sup>

Under New York law, except as otherwise provided in the applicable gift instrument, a not-for-profit corporation's board may delegate to its committees, officers or employees, the authority to act in place of the governing board in investment or reinvestment of institutional funds.<sup>67</sup> No director (whether for-profit or not) will be held liable for the investment and reinvestment of institutional funds by, and for the other acts or omissions of, persons to whom authority is so delegated or with whom contracts are so made.<sup>68</sup> As such, directors who receive compensation for their services should strongly consider encouraging their boards to reasonably delegate investment authority to investment professionals.

### 3.7 Indemnification

The N-PCL includes detailed indemnification provisions and also provides for contribution from other directors and/or recovery from other parties who knowingly received unauthorized distributions.<sup>69</sup> There are two types of indemnification under the N-PCL: mandatory and permissive. A not-for-profit corporation may extend indemnification beyond the restrictions of mandatory or permissive indemnification by including a provision in the corporation's bylaws or certificate of incorporation, passing a board resolution, or entering into a separate agreement. However, indemnification of a director is not permissible under any circumstance if the director acted in bad faith, was deliberately and materially dishonest, or procured some illegal gain.<sup>70</sup>

1. *Mandatory Indemnification.* Under New York law, not-for-profit corporations are required to indemnify their directors for expenses (including costs and attorney's fees) incurred in successfully defending a civil or criminal proceeding, whether brought by the corporation as a derivative suit or by a third party.<sup>71</sup> Although a director does not have to secure a victory on the merits of the litigation to be eligible for indemnification, mandatory indemnification is not available to a director who settles.<sup>72</sup> If a director is only partially successful in his or her defense, the corporation is still required to indemnify the director proportionately.<sup>73</sup> If a not-for-profit corporation fails to comply with its mandatory indemnification obligations, a director may apply to the court to order such indemnification.<sup>74</sup>
2. *Permissive Indemnification.* New York law also allows not-for-profit corporations to indemnify their directors even if directors (i) are unsuccessful in defending actions against them or (ii) decide to settle.<sup>75</sup> Permissive indemnification is only allowed, however, if a director acted in good faith and reasonably believed that he or she was acting in the best interests of the corporation.<sup>76</sup> Additionally, if a director was involved in a criminal proceeding, he or she must have had no reasonable cause to believe that his or her conduct was unlawful.<sup>77</sup>

Directors may be indemnified for settlement costs and reasonable expenses, including attorney fees and the costs of appeal, in both derivative suits and third-party actions, but directors may not be indemnified for judgments and fines in derivative suits. If a corporation declines to exercise permissive indemnification, but a director has met the conditions allowing permissive indemnification, then the director can petition the court to order the corporation to provide indemnification.<sup>78</sup>

New York law sets forth three alternative procedures for corporations to follow when determining whether to indemnify directors who were unsuccessful in defending against third-party litigation or directors named as defendants in derivative actions.<sup>79</sup> These alternatives also apply to corporate approval of indemnification of ongoing expenses.<sup>80</sup> The alternatives are (i) authorization by a quorum of disinterested directors finding

that the director in question has satisfied the standards for permissive indemnification (*i.e.*, acted in good faith, reasonably believed he or she was acting in the best interests of the corporation, and, in the case of a criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful),<sup>81</sup> (ii) authorization by a quorum of disinterested directors who have relied on the opinion of an independent legal advisor that the director in question has satisfied the standards for permissive indemnification,<sup>82</sup> or (iii) authorization by a quorum of disinterested directors who have based their decision on the approval of the membership of the corporation (if the corporation has members) that the director in question has satisfied the standards for permissive indemnification.<sup>83</sup>

3. *Director and Officer Insurance.* Under New York law, not-for-profit corporations may maintain directors and officers insurance (“D&O Insurance”) to indemnify the corporation or directors and officers as described above.<sup>84</sup> If a court finds that a director has committed acts of deliberate and active dishonesty or the director has personally gained an illegal profit or advantage, the D&O Insurance may not be used to cover indemnification costs, but it may be used to cover defense costs.<sup>85</sup> D&O Insurance may not be used to indemnify parties for punitive damages.

Modern D&O Insurance policies include three different components.<sup>86</sup> “Side A” coverage insures past, present, and future directors and officers in their respective capacities as individual insureds (including defense costs) against any insured loss arising from a claim for any actual or alleged wrongful act. “Side B” coverage insures the corporation for amounts it pays out to indemnify its directors and officers. “Side C” coverage insures the corporation against any loss arising from a claim against it for any actual or alleged wrongful act of the corporation. The causes of action covered by a D&O Insurance policy depend on its terms.

Courts generally engage in fact-intensive inquiries to determine whether the proceeds of an organization’s D&O Insurance policy are property of the debtor organization’s estate and thus subject to bankruptcy’s automatic stay, or whether they belong to directors and officers personally.<sup>87</sup> Courts have not decided the issue uniformly.<sup>88</sup> If such proceeds are found to be property of the estate, a director seeking access to them would have to petition the bankruptcy court to lift the automatic stay.

Many modern D&O Insurance policies contain “insured vs. insured” exclusions. Conceived as a protection against collusive lawsuits, insured vs. insured exclusions prevent recovery against a policy where a lawsuit is brought by, or on behalf of, an insured party (for example, the organization) against another insured party (for example, a director). Most insured vs. insured exclusions, however, do not apply when the lawsuit is being brought derivatively, without the aid or assistance of an insured party.

4. *Removal of Directors.* Generally, directors of not-for-profit corporations may be removed for cause by a vote of members or directors, as long as a quorum of a majority of directors is present at the applicable meeting, and provided that (i) if the organization has cumulative voting, the number of votes cast against removing a director would not be enough to elect the director at an election of the entire board and (ii) in organizations in which directors are elected by classes or groups of an organization (e.g., holders of bonds), then a director so elected may only be removed by vote of such class or group.<sup>89</sup> A director may also be removed for cause upon an action brought by the state attorney general or 10% of the corporation’s members requesting removal for cause.<sup>90</sup> A court may bar from reelection any director so removed.<sup>91</sup> A director may be removed without cause by a vote of an organization’s members if the organization’s certificate of incorporation or bylaws so permit.<sup>92</sup>
5. *Resignation of Directors.* Generally, a director has the right to resign from a board and will not incur additional liability by doing so,<sup>93</sup> but resigning from the board will not absolve the director of liability for prior bad acts.<sup>94</sup> Moreover, after resigning, the former director will retain certain fiduciary duties, such as confidentiality. Notably, however, some courts have held that a director

cannot resign if doing so would harm the corporation or leave the interests of the corporation in jeopardy.<sup>95</sup>

## IV. WHAT TO DO IF YOUR ORGANIZATION ENCOUNTERS DIFFICULTIES

One of the most common problems for any organization that runs into trouble is denial. Not-for-profit organizations are no different, and, in fact, because not-for-profit organizations generally do not have the same onerous public reporting obligations that for-profit corporations do, the realization that an organization may be getting into financial trouble may be even more delayed. Further delay may aggravate the problem. Accordingly, not-for-profit directors who encounter trouble should act quickly to determine what course of action to take. Refer to **Tab 13** for a checklist of items to consider when a not-for-profit organization begins to experience financial difficulties. Among other things, the board of directors should determine whether they have board members with the time and experience necessary to navigate a not-for-profit through financial difficulties, and whether financial, operational, and legal advisors are needed to assist with a restructuring and, if so, retain them.<sup>96</sup>

Boards should also begin to consider whether the trouble is serious enough to warrant a restructuring or going out of business altogether. If an organization decides to restructure, it may be able to effectuate the restructuring out of court. Sometimes, however, the organization will need the protections and powers that a court proceeding affords, whether under state law or under the federal Bankruptcy Code. The not-for-profit organization, with the assistance of its advisors, should review the federal and state law options available to it and determine, in light of all the circumstances, which option best addresses the needs and problems of the organization. Some of the reorganization and liquidation options available to not-for-profit organizations are summarized below. *See also Tab 12.*

### 4.1 Restructuring Options

1. *Out-of-Court Restructuring.* Organizations may renegotiate their debt obligations out of court. Out-of-court restructurings may be accomplished in conjunction with new financing advanced on the basis of the corporation's goodwill and/or the threat of bankruptcy. An out-of-court restructuring may be beneficial because it may help a not-for-profit avoid the stigma of bankruptcy and certain other disadvantages of chapter 11. Out-of-court restructurings also demonstrate creditor confidence and involve fewer parties than bankruptcy cases. On the other hand, negotiating separately with every creditor constituency (as compared to a bankruptcy case in which all creditors are brought into the same forum) may be time-consuming. In an out-of-court restructuring, it is often difficult to demonstrate to creditors that you are treating them fairly and that one creditor is not being treated less favorably than others. In addition, the powers available to a debtor in bankruptcy (e.g., automatic stay, the ability to "cram down" on a dissenting class, and inducements available for postpetition financing) are not available in out-of-court restructurings. Without these powers, there is a potential for hold-outs and there is no guarantee that parties will come to a consensus regarding the restructuring.
2. *Chapter 11 Cases.* Chapter 11 of the Bankruptcy Code typically contemplates the continuation and financial and operational rehabilitation of a debtor's business, but an organization may also sell its assets (either as a going concern or in lots) and/or liquidate under chapter 11. A reorganization under chapter 11 permits an organization to continue its business operations in bankruptcy while a plan of reorganization is negotiated, confirmed, and consummated. The plan of reorganization governs how a debtor's liabilities will be addressed and discharged and lays out the plan for emerging from chapter 11 (typically as a viable enterprise). Among other things, a not-for-profit debtor will have to show that its plan for addressing liabilities is feasible under section 1129 of the Bankruptcy Code, *i.e.*, not likely to be followed by liquidation after emerging from bankruptcy.

Unlike for-profit enterprises that utilize sales history to project future revenue, courts are hesitant to rely on previous donations as evidence of future fundraising ability when determining a plan's feasibility under section 1129.<sup>97</sup> Courts reason that raising funds during or immediately after a bankruptcy case will be more difficult as donors are hesitant to give for the purpose of satisfying creditors.<sup>98</sup>

Although chapter 11 may be a relatively more costly process than other restructuring processes available and will require significant management attention, there are many advantages to reorganizing under chapter 11.<sup>99</sup> Foremost among these advantages is the “fresh start” to which a chapter 11 debtor is entitled. This fresh start results from the discharge of all of the debtor's debts under the Bankruptcy Code.<sup>100</sup> In addition, the bankruptcy court provides a single forum for resolving all issues concerning the debtor. This gives the debtor a certain amount of leverage and, as such, may enable the debtor to obtain better trade terms than it would in an out-of-court restructuring.

One of the major benefits of a chapter 11 filing is the automatic stay that the Bankruptcy Code permits a debtor to stay all actions against the property of the debtor's estate. Although the automatic stay is interpreted broadly and is designed to give a debtor a “breathing spell” from its creditors so it can focus on reorganizing, there are some limitations to the automatic stay.<sup>101</sup> Moreover, even where such limitations are not applicable, creditors may petition the bankruptcy court for relief from the stay. Nonetheless, the automatic stay is a valuable tool for debtors and is not available outside of bankruptcy.

Other tools available in bankruptcy include inducements to prospective financiers to assist debtors in securing financing during the course of their bankruptcy cases,<sup>102</sup> the power to assume, assign, and reject executory contracts and unexpired nonresidential real property leases,<sup>103</sup> and the ability to sell assets free and clear of liens (subject to court approval).<sup>104</sup> Chapter 11 debtors may also resort to “cramdown.” Cramdown involves confirming a chapter 11 plan over the dissent of a class or classes of creditors provided at least one class of creditors that is impaired by the plan accepts the plan and the court finds the plan does not discriminate unfairly and is fair and equitable.<sup>105</sup> Specifically, to meet the criteria for cramdown, a chapter 11 plan may not violate the “absolute priority rule,” which prevents junior interests from receiving distributions before senior interests have been paid in full.<sup>106</sup> In the for-profit context, this means that equity (and other junior classes) may not receive a distribution unless senior interests, *i.e.*, creditors, are paid in full. In the not-for-profit context, on the other hand, there is some question as to whether the absolute priority rule would prevent retention of control by members or controlling entities of the not-for-profit organization if creditors are not paid in full.<sup>107</sup> Courts have found that the absolute priority rule does not extend to members or controlling entities of non-profit organizations who are not receiving distributions.<sup>108</sup>

In spite of all of these tools, a chapter 11 case certainly has its disadvantages. The stigma of bankruptcy may negatively affect operations and impair fundraising (although for some organizations, bankruptcy may have the opposite effect and generate support and donations from the community). Moreover, a bankruptcy filing may give rise to increased scrutiny of the organization. Directors and officers may also be subject to more scrutiny after a bankruptcy filing. In addition, upon request of a party in interest, a bankruptcy court may appoint an examiner to examine the affairs of a debtor.<sup>109</sup> A court may also appoint a trustee to run the debtor's estate in the event of fraud or gross mismanagement, or if the court determines the appointment of a trustee is in the best interests of the debtor's constituents. When a court appoints a trustee, the management of the debtor loses control of the organization. Appointment of a trustee is relatively rare, however, especially in cases without fraud or criminal activity.<sup>110</sup>

Chapter 11 can also be costly. Not only must the debtor retain professionals, but it also pays for the fees and expenses of professionals engaged by any official committee appointed in the chapter 11 cases (usually at least one official committee—the unsecured creditors' committee—appointed in each case). One issue from the not-for-profit debtor's perspective is whether a board member can also act as counsel for the debtor in its chapter 11 case. In this context, two issues arise: (i) whether the board member's engagement as counsel results in a conflict of interest and (ii) whether the services as counsel overlap with the board

member's regular board duties. In one bankruptcy court decision, the court answered both of these questions in the negative and approved the board member's fee application.<sup>111</sup>

The Bankruptcy Code also requires that the use, sale, or lease of estate property must be in accordance with applicable nonbankruptcy law, and such use, sale, or lease may not be inconsistent with any relief granted under certain specified provisions of section 362 of the Bankruptcy Code concerning the applicability of the automatic stay.<sup>112</sup>

In addition, section 541(f) of the Bankruptcy Code provides that any property of a not-for-profit debtor's estate may be transferred to an entity that is not such a corporation, but only under the same conditions that would apply if the debtor was not in bankruptcy. Similarly, section 1129(a)(16) provides that transfers of property under a not-for-profit debtor's chapter 11 plan must be made in accordance with applicable nonbankruptcy law governing transfers of the not-for-profit company property. Most states have laws prohibiting not-for-profits from transferring their property to organizations that are not engaged in substantially similar activities as the debtor. As a result, not-for-profit debtors will not be able to use bankruptcy law to circumvent state law transfer restrictions. To the extent that state law permits such a transfer so long as the not-for-profit organization (typically, on notice to the state attorney general's office) obtains a court order permitting such transfer, bankruptcy court approval may be a more expeditious means of obtaining such relief.

3. *Involuntary Chapter 11 Cases.* Although the Bankruptcy Code does allow creditors of for-profit corporations to commence involuntary chapter 11 proceedings against them, creditors may not commence involuntary bankruptcy proceedings against not-for-profit corporations.<sup>113</sup> In addition, a court may not convert a voluntary chapter 11 case to a chapter 7 (liquidation) case unless the debtor so requests.<sup>114</sup> A court may, however, dismiss the case altogether if cause exists for conversion.<sup>115</sup>
4. *Prepackaged and Prenegotiated Chapter 11 Cases.* In a prepackaged chapter 11 case, the debtor negotiates a plan of reorganization with creditors before filing for bankruptcy. As a result, debtors in prepackaged chapter 11 cases typically emerge from bankruptcy more quickly than debtors in traditional chapter 11 cases. "Prepacks" may offer not-for-profits the best of both worlds. Because they are typically shorter than traditional chapter 11 cases, prepacks resemble out-of-court restructurings but allow debtors the use of many of the tools and advantages of chapter 11.

In addition to their relative speed, prepacks may also be preferable to ordinary chapter 11 cases because a prepack debtor will have obtained a favorable vote on its plan of reorganization before entering chapter 11. As such, a true prepackaged chapter 11 case is often less contentious than ordinary chapter 11 cases.

For a typical not-for-profit organization, however, a prepackaged chapter 11 case may be difficult to accomplish. In a bankruptcy case, entities whose claims are being negatively affected (impaired) by a chapter 11 plan are entitled to vote to accept or reject the plan. The nature and extent of trade claims against a potential debtor can change on a daily basis. Thus, it is virtually impossible to conduct a prepetition solicitation of a class consisting of trade claims, as would be necessary if a prepackaged plan proposed to affect them. As a result, most true prepackaged cases are only used where the debtor wants to use the bankruptcy process to restructure one or more classes of claims (such as bank debt, publicly traded debt, or even tort claims), but might not be able to get the 100% approval that would be required under applicable nonbankruptcy law for such restructuring. The typical prepackaged plan provides for payment in full of trade claims so the debtor does not have to solicit the votes of trade creditors. This makes it difficult for the debtor to use other powers of the Bankruptcy Code, such as the ability to reject contracts and leases, to its full advantage. Thus, where an operational – as opposed to a financial – restructuring is needed, it may not be possible to accomplish a restructuring through the means of a prepackaged plan.

Where a potential debtor does wish to alter rights of general unsecured creditors and has the basic framework of a restructuring agreement that is supported by its major constituencies, it may pursue a “prenegotiated” plan. In this situation, the potential debtor negotiates the terms of the plan with its principal constituents (and, therefore, has a degree of confidence that they ultimately will vote to accept the plan), but the potential debtor has not conducted a formal solicitation of votes on the plan. The debtor commences its chapter 11 case and then follows the same process as in a traditional chapter 11 case. The only real difference is that, having ironed out the terms of its restructuring prior to commencing its chapter 11 case, the debtor is likely to be able to emerge from chapter 11 more quickly than a traditional chapter 11 debtor.

5. *Subchapter V of Chapter 11.* In a subchapter V chapter 11 case, a qualifying small business debtor restructures its debts under a streamlined framework designed to make the chapter 11 process faster and generally less expensive. For eligible not-for-profits, subchapter V may offer an efficient restructuring path that preserves many of the benefits and protections of chapter 11 while minimizing administrative burdens and professional costs.

To qualify, an entity must be “a person engaged in commercial or business activities” with aggregate debts not exceeding a certain limit,<sup>116</sup> of which not less than 50 percent must have arisen from the entity’s commercial or business activities.<sup>117</sup> For not-for-profit organizations, bankruptcy courts have generally held that the “commercial or business activities” requirement does not mandate a profit motive and thus not-for-profit organizations are eligible to seek subchapter V relief.<sup>118</sup>

Subchapter V eliminates certain procedural burdens present in traditional chapter 11 cases, such as the requirement to solicit acceptances of a disclosure statement<sup>119</sup> and the appointment of a creditor’s committee.<sup>120</sup> It also allows the debtor to confirm a plan without acceptance by any impaired classes.<sup>121</sup> Instead, confirmation of a nonconsensual plan requires a commitment of projected disposable income over 3–5 years.<sup>122</sup> Existing equity ownership of a debtor can also continue following a subchapter V case, which does not require compliance with the “absolute priority rule”.<sup>123</sup>

## 4.2 Liquidation or Dissolution<sup>124</sup>

1. *Chapter 7 Cases.* Chapter 7 of the Bankruptcy Code contemplates an expeditious, orderly liquidation of all of the debtor’s property. Under chapter 7, the debtor does not continue as an ongoing business enterprise. Instead, a trustee is appointed to take over the management of the debtor and convert the debtor’s assets and properties to cash. The proceeds are then distributed to creditors in accordance with the priorities established in the Bankruptcy Code. Liquidation under chapter 7 has many advantages over dissolution under state law. For example, chapter 7 cases are generally relatively quick and inexpensive. In addition, many of the tools available in chapter 11 are available to a chapter 7 trustee, such as the automatic stay and the power to sell assets free and clear of liens. The disadvantages of chapter 7 include the appointment of a trustee, who effectively replaces management and the board of directors of the debtor, and additional scrutiny on the organization’s prepetition dealings. In addition, no discharge of prebankruptcy debts is available for a debtor that liquidates, rather than reorganizes.
2. *Non-Judicial State Law Dissolution.* Solvent non-for-profit corporations may also dissolve or liquidate using a non-judicial state law dissolution process. A non-judicial dissolution process is not available under New York law for an insolvent not-for-profit corporation, which must use a judicial state law dissolution or other in court process such as chapter 7.<sup>125</sup> Under New York law, non-judicial dissolution procedures differ depending upon the type of not-for-profit corporation<sup>126</sup> and the amount of assets and liabilities of the corporation.<sup>127</sup>

If the corporation has no assets other than a reserve fund of \$25,000 or less to be used to pay (i) the costs of winding up the organization’s affairs such as attorneys’ and accountants’ fees and (ii) liabilities less than

\$10,000, then the corporation can use a streamlined procedure for dissolution.<sup>128</sup> Under the streamlined procedure:

- (i) the board of directors (or equivalent governing body) adopts a Plan of Dissolution;
- (ii) if the corporation has members entitled to vote, after the board of directors has authorized the Plan of Dissolution, such plan is submitted to the membership for approval;
- (iii) if approval of any governmental body or officer was required for the formation of the corporation, the corporation must get written approval of the dissolution from that governmental body or officer;
- (iv) the corporation then submits the following to the Attorney General: (a) a Petition for Approval of the Certificate of Dissolution, (b) the original Certificate of Dissolution with the original of any governmental consents, if required, and (c) all required financial reports, including a final report;
- (v) the organization must then request a Consent to Dissolution of a Corporation from the New York State Tax Department of Taxation and Finance;
- (vi) next, the corporation sends the original Certificate of Dissolution with the original NYS Department of Taxation and Finance clearance and the original of any required governmental body or officer consents, along with a check for the required filing fee payable to the NYS Department of State; and
- (vii) the corporation sends a copy of the Department of State's receipt to the Attorney General.<sup>129</sup>

If, on the other hand, the corporation has assets and/or liabilities in excess of those described in the previous paragraph, the board must engage in a slightly stricter and more time consuming process.<sup>130</sup> Non-judicial dissolution is generally slower and more complex than liquidation under chapter 7 of the Bankruptcy Code. Pursuant to this process, among other requirements, the organization must seek approval of its Plan of Distribution from the Attorney General or the supreme court.<sup>131</sup>

The Plan of Distribution is the document that sets forth how the dissolving entity's assets will be distributed, first, to its creditors and then to organizations engaged in substantially similar activities. Thus, the Attorney General typically becomes an integral component of the dissolution process.

Note, too, as part of this process, the sale of a dissolving not-for-profit's assets may give rise to personal liability for directors, *e.g.*, if directors approve a distribution without first paying or adequately providing for the corporation's known liabilities in their plan of dissolution.<sup>132</sup> If the corporation is insolvent and lacks sufficient assets to do so, it cannot use a non-judicial dissolution process and should instead liquidate or dissolve using a judicial state law dissolution or other alternative (chapter 11 or chapter 7 bankruptcy proceeding). Accordingly, non-judicial dissolution under state law may not compare favorably to liquidation under the Bankruptcy Code depending on a corporation's circumstances.

3. *Judicial State Law Dissolution.* New York law also provides for judicial dissolution, which is similar to non-judicial dissolution but involves more court oversight over the process.<sup>133</sup> Judicial dissolution may be initiated by the Attorney General in the case of fraud or related misconduct.<sup>134</sup> Generally, however, judicial dissolution in the liquidation context is initiated by an organization's board.<sup>135</sup> In such a situation, a majority of the directors may present a petition for judicial dissolution where the assets of a not-for-profit corporation are insufficient to discharge its liabilities or where dissolution will benefit the corporation's members.<sup>136</sup>
4. *Receivership.* Receivership under state law involves court appointment of a receiver to run the not-for-profit corporation in order to pay off its debts.<sup>137</sup> In some ways a receivership is very similar

to chapter 11, but receivership is typically thought of as a creditor remedy because the debtor loses control of the company. Receiverships may or may not result in the dissolution of the corporation. In New York, receivership law is largely considered obsolete.

5. *Assignment for the Benefit of Creditors.* Another rarely used wind down method under New York law is an assignment for the benefit of creditors. In an assignment for the benefit of creditors, a corporation assigns all of its nonexempt property to an assignee (typically a lawyer) who then liquidates the property (sometimes under court supervision) and distributes the proceeds pro rata to creditors.<sup>138</sup>

ENDNOTES

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<sup>1</sup> See *N. Am. Catholic Educ. Programming Found., Inc. v. Gheewalla, C.A.*, 930 A.2d 92, 99 (Del. 2007).

<sup>2</sup> Under Delaware law, fiduciary duties are not owed directly to the creditors of an insolvent corporation, but creditors of the insolvent corporation are able to enforce the directors' duties to the corporation. The Delaware Supreme Court in *Gheewalla* clarified that while creditors of an insolvent Delaware corporation do not have direct claims against directors for breaches of fiduciary duties, creditors have standing to pursue such breaches derivatively on behalf of the corporation. See *id.* at 101–02. This is because creditors of an insolvent corporation “take the place of the shareholders as the residual beneficiaries of any increase in value,” and “the corporation’s insolvency makes the creditors the principal constituency injured by any fiduciary breaches that diminish the firm’s value.” *Id.* (internal citations omitted).

In contrast, under New York law, it appears fairly well-settled that the directors of an insolvent corporation owe fiduciary duties to creditors. This premise arises from a 1953 New York Court of Appeals case that is still cited as good law. *N.Y. Credit Men’s Adjustment Bureau, Inc. v. Weiss*, 110 N.E.2d 397, 398 (N.Y. 1953) (“If the corporation was insolvent at that time it is clear that defendants, as officers and directors thereof, were to be considered as though trustees of the property for the corporate creditor-beneficiaries.”); see also *Clarkson Co. v. Shaheen*, 660 F.2d 506, 512 (2d Cir. 1981), *cert. denied*, 455 U.S. 990 (1982) (citing *Weiss* in holding that directors of an insolvent New York corporation owe fiduciary duties to creditors, and creditors can sue to enforce those duties); *Hughes v. BCI Int’l Holdings*, 452 F. Supp. 2d 290 (S.D.N.Y. 2006) (holding that creditors had standing to assert a breach of fiduciary claim against the director of an insolvent New York corporation, because even though “[a]n officer or director does not owe a fiduciary duty to the creditors of a solvent corporation, the fact of insolvency causes such a duty to arise.”) (internal citations omitted); *C3 Media & Mktg. Grp., LLC v. Firstgate Internet, Inc.*, 419 F. Supp. 2d 419, 431 (S.D.N.Y. 2005) (same; dismissing claim by creditor against director for fraudulent inducement because the director made the statement prior to the company’s insolvency and did not therefore, at the time he made the statement, owe the creditor a fiduciary duty); *Econ. Dev. Growth Enter. Corp. v. McDermott*, 478 B.R. 123, 128 (N.D.N.Y. 2012) (citing *Hughes* in holding that directors of an insolvent corporation owe a fiduciary duty to preserve the assets of the corporation for the benefit of creditors); *Post-Confirmation Comm. of Unsecured Creditors v. Feld Grp., Inc. (In re I Successor Corp.)*, 321 B.R. 640, 659 (Bankr. S.D.N.Y. 2005) (“Once a corporation becomes insolvent, the fiduciary duties of corporate officers and directors also extend to creditors.”) (internal citations omitted); *Kittay v. Atl. Bank of N.Y. (In re Global Serv. Grp. LLC)*, 316 B.R. 451 (Bankr. S.D.N.Y. 2004) (Under New York law, “[o]nce insolvency enures, the fiduciary duties of corporate officers and directors also extend to creditors. As a result, the officers and directors owe duties to multiple constituencies whose interests may diverge. At this point, they have an obligation to the community of interest that sustained the corporation, to exercise judgment in an informed, good faith effort to maximize the corporation’s long-term wealth creating capacity”) (internal citations omitted); *Secs. Investor Prot. Corp. v. Stratton Oakmont, Inc.*, 234 B.R. 293, 334 n.27 (Bankr. S.D.N.Y. 1999) (“Under the New York law, a director’s fiduciary duty runs to creditors when the corporation becomes insolvent.”); cf. *Brenner v. Philips, Appel & Walden, Inc.*, 1997 WL 33471053, at \*6 (S.D.N.Y. 1997) (“Under New York law, directors of an insolvent corporation have a duty not to divest the corporation of assets without affording creditors an opportunity to present and enforce their claims.”); *In re Mid-State Raceway, Inc.*, 323 B.R. 40, 58 (Bankr. N.D.N.Y. 2005) (“In the bankruptcy context, the directors owe duties not only to the corporation and its shareholders, they also owe a duty of good faith to the creditors.”).

The theory under which directors of insolvent New York corporations are found to have fiduciary duties to creditors is sometimes referred to as the “trust fund” doctrine. See, e.g., *Credit Agricole Indoseuz v. Rossiyskiy Kredit Bank*, 729 N.E.2d 683, 688 (N.Y. 2000) (By virtue of the trust fund doctrine, “the officers and directors of an insolvent corporation are said to hold the remaining corporate assets in trust for the benefit of its creditors.”); *Heimbinder v. Berkovitz*, 175 Misc. 2d 808, 816 (N.Y. Sup. Ct. 1998) (The fiduciary duty that corporate directors and officers owe to creditors derives “from the principle that the corporate assets constitute a trust fund for the benefit of creditors.”); *Roos v. Aloï*, 127 Misc. 2d 864, 868 (N.Y. Sup. Ct. 1985) (“As to the right of creditors, the courts of this state have, under certain circumstances, adopted the ‘trust fund’ theory. Under this theory, the assets of a corporation, in certain situations, constitute a trust fund for the benefit of creditors.”); see also *RSL Commc’ns PLC v. Bildirici*, 649 F. Supp. 2d 184, 202 (S.D.N.Y. 2009), *aff’d*, 412 F. App’x 337 (2d Cir. 2011), *cert. denied*, 132 S. Ct. 97 (2011) (“[T]he duty that directors owe to the creditors of an insolvent corporation under New York law is defined primarily by the ‘trust fund doctrine.’”). Generally, however, “the application of the trust fund doctrine in New York has been for the purpose of imposing liability on corporate directors or transferees for wrongful dissipation of assets of an insolvent corporation, in actions later brought by court-appointed receivers, trustees in bankruptcy or judgment creditors,” rather than as a general source of fiduciary duties. *Credit Agricole*, 729 N.E.2d at 688. Moreover, a creditor’s remedies thereunder are “limited to reaching the asset which would have been available to satisfy his or her judgment if there had been no conveyance.” *Heimbinder*, 175 Misc. 2d at 816. Furthermore, the trust fund doctrine does not automatically create an actual

lien or other equitable interest in corporate assets and may not be used by a general creditor to obtain a preliminary injunction in aid of a money judgment not yet obtained. *Credit Agricole*, 729 N.E.2d at 688.

The recognition by New York courts of broad director duties likely stems from the fact that even outside the context of insolvency, New York statutory law permits directors of a for-profit corporation to consider interests beyond those of the shareholders, including creditors. See N.Y. BUS. CORP. LAW § 717(b) (“In taking action, . . . a director shall be entitled to consider, without limitation (1) both the long-term and the short-term interests of the corporation and its shareholders and (2) the effects that the corporation’s actions may have in the short-term or in the long-term upon any of the following: . . . (iv) the corporation’s customers and creditors.”). Interestingly, the New York Not-for-Profit Corporation Law does not have a completely analogous provision; it only provides that the board, subject to any specific limitations set forth in the applicable gift instrument, must take into account “(A) general economic conditions; (B) the possible effect of inflation or deflation; (C) the expected tax consequences, if any, of investment decisions or strategies; (D) the role that each investment or course of action plays within the overall investment portfolio of the fund; (E) the expected total return from income and the appreciation of investments; (F) other resources of the institution; (G) the needs of the institution and the fund to make distributions and to preserve capital; and (H) an asset’s special relationship or special value, if any, to the purposes of the institution,” when delegating investment management of institutional funds. See N-PCL § 552(e). Although this provision does not explicitly permit consideration of the not-for-profit corporation’s creditors, New York statutory law explicitly allows creditors to sue directors for certain actions that caused harm to the creditors in both the for-profit and not-for-profit spheres. See N.Y. BUS. CORP. LAW § 719(a) (“Directors of a corporation who vote for or concur in any of the following corporate actions shall be jointly and severally liable to the corporation for the benefit of its creditors or shareholders, to the extent of any injury suffered by such persons, respectively, as a result of such action” in various specified circumstances, including in the declaration of dividends, the purchase of shares, dissolution, and the making of loans to directors); N-PCL § 719(a) (“Directors of a corporation who vote for or concur in any of the following corporate actions shall be jointly and severally liable to the corporation for the benefit of its creditors or members or the ultimate beneficiaries of its activities, to the extent of any injury suffered by such persons, respectively, as a result of such action,” in certain specified circumstances, including the unauthorized distribution of the corporation’s cash or property to members, directors or officers, certain redemptions, dissolution, or the making of loans to directors.). Finally, New York statutory law explicitly provides judgment creditors, receivers, and bankruptcy trustees the right to sue a director or officer “in the right of the corporation” for such director’s or officer’s wrongful conduct or violation of general duties. See *id.* § 720; N.Y. BUS. CORP. LAW § 720.

<sup>3</sup> See *Pereira v. Cogan*, 294 B.R. 449, 521 (S.D.N.Y. 2003), *cert. denied*, 126 S. Ct. 2286 (2006) (applying Delaware law), *rev’d on other grounds*, *Pereira v. Farace*, 413 F.3d 330 (2d Cir. 2005).

<sup>4</sup> Specifically, some courts have stated that the fiduciary duties of an organization’s directors expand to creditors even if the organization is not yet insolvent, if it is in the zone of insolvency. See, e.g., *Schnelling v. Crawford (In re James River Coal Co.)*, 360 B.R. 139, 170 (Bankr. E.D. Va. 2007) (applying Virginia law and stating that “[o]nce a corporation enters the zone of insolvency, the fiduciary duties owed by [d]irectors extend also to the corporation’s creditors”). Under Delaware law, however, directors of a corporation in the zone of insolvency do not owe fiduciary duties to creditors, and creditors of such a corporation can even assert claims for breaches of fiduciary duty derivatively. Clearing up confusion from lower court opinions that suggested otherwise, the Delaware Supreme Court held definitively that directors of a solvent Delaware corporation operating in the zone of insolvency do not owe fiduciary duties to creditors and creditors may not assert direct claims for breaches of fiduciary duty against those directors. See *Gheewalla*, 930 A.2d at 101. Although the *Gheewalla* court did not say so explicitly, the thrust of its opinion appears to be that creditors of a corporation operating in the zone of insolvency cannot even bring claims derivatively on behalf of the corporation. *Id.* (“When a solvent corporation is navigating in the zone of insolvency, the focus for Delaware directors does not change: directors must continue to discharge their fiduciary duties to the corporation and its shareholders by exercising their business judgment in the best interests of the corporation *for the benefit of its shareholder owners.*”) (emphasis added).

No New York court has considered whether to adopt the Delaware court’s reasoning in *Gheewalla*, and New York caselaw regarding directors’ duties while an organization is operating in the zone of insolvency is scant. In *RSL Communications*, the United States District Court for the Southern District of New York concluded that “there is no support under New York law” for imposing upon directors an unlimited fiduciary duty of care with respect to the organization’s creditors. *RSL Commc’ns PLC*, 649 F. Supp. 2d 184, 207 (S.D.N.Y. 2009). The *RSL Communications* court declined, however, to decide whether New York law would find that the trust fund doctrine applies while an organization is in the zone of insolvency and noted that the duties imposed by the trust fund doctrine are more “narrow” than a general fiduciary duty of care. *Id.* at 203 n.10. At least one New York court indicated that the trust fund doctrine does apply when a corporation is on the brink of insolvency though not yet technically insolvent. See *Weiss*, 110 N.E.2d at 398 (“If the corporation was then technically solvent but insolvency was approaching and was then only a few days away, defendants, as officers and directors, were, in effect, the trustees by statute

for the creditors by virtue of section 60 of the General Corporation Law which obligated them to protect the trust res for the creditors and to account for waste in not obtaining full value for the res, if there was any waste by reason of their conduct.”). Section 60 of the General Corporation Law, cited in *Weiss*, is the predecessor statute to N.Y. BUS. CORP. LAW § 720. *Purves v. ICM Artists, Ltd.*, 119 B.R. 407, 411 n.7 (S.D.N.Y. 1990). Prior to the *RSL Communications* decision, several federal district courts stated that New York law may impose upon an organization’s directors fiduciary duties to its creditors while in the zone of insolvency. See *Stratton Oakmont, Inc.*, 234 B.R. at 334 n.27 (stating that no New York case holds that a board’s fiduciary duties do not begin to run to creditors as soon as the corporation approaches insolvency); *Hallinan v. Republic Bank & Trust Co.*, 2007 WL 39302, at \*8, n.29 (S.D.N.Y. 2007) (appearing to apply New York law and noting in dicta that “once a corporation enters the zone of insolvency, the directors owe fiduciary duties to the corporations’ [sic] creditors, in addition to its shareholders) (internal citations omitted); *Fed. Nat’l Mortg. Assoc. v. Olympia Mortg. Corp.*, 2006 WL 2802092, at \*6 (E.D.N.Y. 2006) (upholding claim against officers and directors for breach of fiduciary duty based on a theory that when a corporation enters the zone of insolvency, the officers and directors owe fiduciary duties to the corporation’s creditors; the defendants, however, did not dispute that proposition but argued for the claim to be dismissed on other grounds); *Kittay v. Flutie N.Y. Corp. (In re Flutie N.Y. Corp.)*, 310 B.R. 31, 57 (Bankr. S.D.N.Y. 2004) (“Michael Flutie, much as a director of a corporation that is in the zone or vicinity of insolvency, owes a fiduciary duty not only to [the corporation] and any shareholders, but also to its creditors.”) (applying New York law but citing cases applying Delaware law); cf. *Clarkson Co.*, 660 F.2d at 512 (rejecting proposition that directors only owe duties to creditors when “liquidation is imminent and foreseeable” or “it is clear that the corporation is no longer a going concern”) (internal citations omitted). It should be noted that the *Flutie* court’s reliance on pre-*Gheewalla* Delaware cases renders that decision of questionable persuasiveness. The issues of whether and to what extent directors of New York organizations owe fiduciary duties to the organization’s creditors while it is operating in the zone of insolvency thus remain open questions. It is clear, at least, that, as is the case under Delaware law, creditors of New York corporations operating in the zone of insolvency have standing to sue the directors derivatively for breaches of fiduciary duties. See *In re I Successor Corp.*, 321 B.R. at 659 (“[C]laims based on the breach of fiduciary duty to creditors when a company is in the zone of insolvency are derivative of claims of breach of fiduciary duty to the company itself.”).

<sup>5</sup> The rationale for this duty is that donations to nonprofit organizations are made on the assumption and reliance that the charitable purposes of the organization will be fulfilled and the donations will not be used for other purposes. *Trs. of Rutgers Coll. v. Richman*, 125 A.2d 10 (N.J. Ch. 1956).

<sup>6</sup> See *In re HHH Choices Health Plan, LLC*, 554 B.R. 697, 704 (Bankr. S.D.N.Y. 2016) (“But it cannot be the case that the Court is simply paralyzed if both objectives, paying creditors as much as possible and serving the mission of the corporation, cannot be met at the same time. So what weight is to be applied? The best I can discern from the case law is that all of these considerations are supposed to be taken into account and balanced in a reasonable way, and with no other requirement or particular weight to be applied.”).

<sup>7</sup> See, e.g., *Manhattan Eye, Ear & Throat Hosp. v. Spitzer*, 715 N.Y.S.2d 575, 595 (Sup. Ct. 1999) (“Embarkation upon a course of conduct which turns it away from the charity’s central and well-understood mission should be a carefully chosen option of last resort. Otherwise a board facing difficult financial straits might find a sale of assets, and ‘reprioritization’ of its mission, to be an attractive option, rather than taking all reasonable efforts to preserve the mission which has been the object of its stewardship.”); *In re United Healthcare Sys., Inc.*, 1997 WL 176574, at \*5 (D.N.J. Mar. 26, 1997) (when analyzing an articulated business reason for a sale of a charitable institution’s assets, the court must consider the fact that a debtor is a charitable institution and that the board of the non-profit organization has a fiduciary obligation to maintain the acute care facility in question); *In re Brethren Care of S. Bend, Inc.*, 98 B.R. 927, 935 (Bankr. N.D. Ind. 1989) (finding that a sale that would provide continued services to the debtor’s patients/residents was a good business reason for the sale of a charitable institution’s assets). But see *Dennis v. Buffalo Fine Arts Acad.*, 15 Misc. 3d 1106(A) (N.Y. Sup. Ct. Mar. 21, 2007) (limiting the holding in *Manhattan Eye, Ear, & Throat Hospital* to sales of all or substantially all of the entity’s assets, and determining that the same considerations do not apply when a charitable entity disposes of only a small portion of its assets in a way that does not depart from its corporate purposes).

<sup>8</sup> N-PCL §§ 511, 511-a. See also *Rogers Duell ex rel Rogers v. Ying-Jen Chen*, 42 Misc. 3d 1226(A) (N.Y. Sup. Ct. Feb. 11, 2014).

<sup>9</sup> N-PCL §§ 511, 511-a.

<sup>10</sup> *In re Winsted Mem’l Hosp.*, 249 B.R. 588, 594 (Bankr. D. Conn. 2000) (the debtor’s ability to pay creditors out of private donations “depends on whether, in the absence of the bankruptcy filing, the [debtor] would have been permitted to do so”); see also 11 U.S.C. § 363(d) (2010) (“The trustee may use . . . property [of the estate] only in accordance with applicable nonbankruptcy law applicable to the transfer of property by a debtor that is such a corporation or trust . . .”).

<sup>11</sup> N-PCL § 513(b) (With certain exceptions, “the governing board shall apply all assets thus received to the purposes specified in the gift instrument . . . and to the payment of the reasonable and proper expenses of administration of such assets.”).

<sup>12</sup> *Id.* § 553.

<sup>13</sup> *Id.* § 513(b).

<sup>14</sup> *Id.* § 513(b).

<sup>15</sup> *Id.* § 720(a). See, e.g., *Sergeants Benevolent Ass’n Annuity Fund v. Renck*, 796 N.Y.S.2d 77, 80 (1st Dep’t 2005).

<sup>16</sup> Generally, donors of restricted gifts who do not retain a property interest in their gifts do not have standing to sue for return of such gifts in the event donees fail to comply with the restrictions. See, e.g., *Steenek v. Univ. of Bridgeport*, 1994 WL 463629, at \*7 (Conn. Super. Ct. Aug. 18, 1994). Notably, however, one court granted a donor’s request for return of its charitable gift directed toward building a school when the recipient mismanaged the school project and failed to meet the deadlines and other requirements of the gift instrument. *Dickler v. Cigna Prop. & Cas. Co.*, 1998 WL 126938, at \*7 (E.D. Pa. Mar. 19, 1998); see also *Smithers v. St. Luke’s-Roosevelt Hosp. Ctr.*, 723 N.Y.S.2d 426, 434 (1st Dep’t 2001) (court-appointed estate administrator had standing to sue for recovery of allegedly misused restricted assets because she was enforcing her late husband’s rights under his agreement with the hospital through specific performance of that agreement).

<sup>17</sup> N-PCL § 555(a).

<sup>18</sup> *Id.* § 555(b). Section 555(b) also requires the not-for-profit institution to “notify the donor, if available, and the attorney general,” and both parties “must be given an opportunity to be heard.” *Id.* This provision requires that the funds be used to further the not-for-profit corporation’s charitable purposes, rather than its operating expenses. *Id.* § 555(a) (“A release or modification may not allow a fund to be used for a purpose other than a charitable purpose of the institution.”). In addition, section 555(c) permits a court to modify a restriction on the use or purpose of a fund that is or has become “unlawful, impracticable, impossible to achieve, or wasteful” as long as (i) the modification is “consistent with the purposes expressed in the gift instrument,” (ii) the donor, if available, has been given notice of the application, and (iii) the attorney general has been notified and given an opportunity to be heard. *Id.* § 555(c). A not-for-profit corporation would be able to release or modify a restriction on the management, investment or purpose of a fund without court approval (but upon notice to the donor, if available, and 90-day notification to the attorney general) if (i) the restriction is “unlawful, impracticable, impossible to achieve, or wasteful,” (ii) the fund has a total value of less than \$100,000, (iii) the fund is more than 20 years old, and (iv) the not-for-profit corporation “uses the property in a manner consistent with purposes expressed in the gift instrument.” *Id.* § 555(d).

<sup>19</sup> *In re Othmer*, 710 N.Y.S.2d 848, 851 (Sur. Ct. 2000) (stating that courts may free a charitable organization from restrictions and limitations attached to a donation where the following three conditions are satisfied: “(1) the gift or trust must be charitable in nature; (2) the language of the will or trust instrument, when read in the light of all attendant circumstances, must indicate that the donor demonstrated a general, rather than specific, charitable intent; and (3) it must be determined to the court’s satisfaction that the particular purpose for which the gift or trust was created has failed, or has become impossible or impracticable to achieve.”); *In re Trustco Bank*, 954 N.Y.S.2d 411, 418 (Sur. 2012), *aff’d sub nom. In re Lally*, 112 A.D.3d 1099, 976 N.Y.S.2d 701 (2013) (applying the test in *Othmer* to apply the doctrine of *cy pres* to reform the gifts made to a foundation; *In re Edward John Noble Hosp. of Gouveneur*, 39 Misc. 3d 279 (N.Y. Sup. 2013) (applying the test for release of a donor restriction set forth in *Othmer* and modifying the terms of certain trusts to permit the principal of the trusts to be pledged as collateral, or, in the alternative, paid directly to not-for-profit hospital so that it could meet its financial commitments because the court found that the donors had a general charitable intent and the not-for-profit’s financial condition made it impracticable for it to both abide by the donors’ restrictions and satisfy the donors’ charitable intent).

<sup>20</sup> N-PCL § 555(f) (“This chapter shall not limit the application of the doctrines of *cy pres* and deviation.”).

<sup>21</sup> See *In re Kraetzer’s Will*, 462 N.Y.S.2d 1009, 1013 (Sur. Ct. 1983) (holding that a chapter 11 trustee of a bankrupt hospital could not distribute funds from a general gift to the hospital’s creditors because courts have uniformly held that the intention of a testator in making a general gift to a charitable corporation was the furtherance of the charitable purpose for which the entity was formed as set forth in its charter).

<sup>22</sup> *Id.* at 1012 (The termination of a charitable organization’s “benevolent services causes the loss of a charity’s right to receive an absolute disposition or continued income, as the case may be, despite the prior vesting of the bequest or devise. Charitable

gifts by will, being for public purposes, are impressed with a public trust imposed by the charter of each particular entity even if no express trust was created by the donor.”).

<sup>23</sup> *Id.* at 1013 (internal citations omitted).

<sup>24</sup> *Boston Reg'l Med. Ctr., Inc. v. Reynolds (In re Boston Reg'l Med. Ctr., Inc.)*, 298 B.R. 1, 28 (Bankr. D. Mass. 2003) (donors to hospitals “do not contemplate that hospital personnel will apply donated monies directly to patients’ wounds. They understand full well that the hospital will use the funds to pay the employees and other creditors through whom it provides medical care to its patients.”).

<sup>25</sup> *Boston Reg'l Med. Ctr., Inc. v. Reynolds (In re Boston Reg'l Med. Ctr., Inc.)*, 410 F.3d 100, 111 (1st Cir. 2005) (“We decide only that, absent a contrary provision in the will or indenture of trust, a charitable organization that has ceased to perform any charitable work and that is incapable of redirecting new funds for charitable purposes is ineligible to receive a charitable bequest or gift.”).

<sup>26</sup> *Id.* at 114.

<sup>27</sup> *Id.*

<sup>28</sup> *Bierbower v. McCarthy*, 334 B.R. 478 (D.D.C. 2005) *appeal dismissed* 2006 WL 3086921 (D.C. Cir. Oct. 17, 2006); *cf.* N-PCL § 1002-a.

<sup>29</sup> *See* D.C. CODE § 29-412.01 *et seq.*

<sup>30</sup> *Id.* § 29-412.05(c).

<sup>31</sup> *See, e.g., In re 375 Park Ave. Assocs.*, 182 B.R. 690, 694-95 (Bankr. S.D.N.Y. 1995) (citing numerous cases for the proposition that “New York courts have uniformly held that a charitable pledge constitutes a unilateral contract, that, when accepted by the charity by incurring liability in reliance thereon, becomes a binding obligation.”).

<sup>32</sup> N-PCL § 517(b) (“A member shall be liable to the corporation only to the extent of any unpaid portion of the initiation fees, membership dues or assessments which the corporation may have lawfully imposed upon him, or for any other indebtedness owed by him to the corporation.”).

<sup>33</sup> *Id.* § 517(b) (“No action shall be brought by any creditor of the corporation to reach and apply any such liability to any debt of the corporation until after final judgment shall have been rendered against the corporation in favor of the creditor and execution thereon returned unsatisfied, or the corporation shall have been adjudged bankrupt, or a receiver shall have been appointed with power to collect debts, and which receiver, on demand of a creditor to bring suit thereon, has refused to sue for such unpaid amount, or the corporation shall have been dissolved or ceased its activities leaving debts unpaid.”).

<sup>34</sup> *See, e.g., Westmoreland Human Opportunities, Inc. v. Walsh*, 246 F.3d 233, 244 (3d Cir. 2001) (“As we see it, a federal agency’s retention of pervasive restrictions on a grantee’s identity and manner of performance under a HUD-type grant program is inconsistent with the grantee’s assertion of a property interest in the grant relationship.”); *In re Joliet-Will County Cmty. Action Agency*, 847 F.2d 430, 433 (7th Cir. 1988) (“Practical considerations support characterization of these grant moneys as property of the grantors until expended in accordance with the terms of the grants.”); *U.S. Dep’t of Hous. & Urban Dev. v. K. Capolino Constr. Corp.*, No. 01 Civ 390, 2001 WL 487436, \*4 (S.D.N.Y. May 7, 2001) (“In determining whether the United States has an interest in particular funds, that have been disbursed to a grantee, courts have considered whether the funds were dispensed according to conditions, whether the United States retains a reversionary interest in the funds, and whether the United States employs accountability procedures to ensure that the grants are being spent as directed.”); *Cmty Assocs. v. Novak*, 173 B.R. 824, 828 (D. Conn. 1994) (adopting the reasoning of *Joliet-Will*).

<sup>35</sup> *See Westmoreland*, 246 F.3d at 244.

<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.* (“[I]f these controls are sufficiently extensive, *i.e.*, if, under the terms of the arrangement between the grantor federal agency and the grantee, the agency retains strict, pervasive, and minute oversight over the identity of the grant recipient and the manner of that recipient’s performance, the existence of such controls can demonstrate that the federal grantor agency’s

interest in ensuring the effective administration of that program is weighty enough to exclude the grantee's interest from § 541's property definition.").

<sup>39</sup> N-PCL § 510(a)(1)-(2).

<sup>40</sup> *Id.* § 510(a)(3) ("If the corporation is . . . a charitable corporation . . . such sale, lease, exchange or other disposition shall in addition require approval of the attorney general or the supreme court.").

<sup>41</sup> *See, e.g., Manhattan Eye, Ear & Throat Hosp. v. Spitzer*, 715 N.Y.S.2d at 597 (denying authorization to sell a not-for-profit hospital's assets because sale would not promote the hospital's charitable purpose); *In re Multiple Sclerosis Serv. Org. of N.Y., Inc.*, 505 N.Y.S.2d 841, 867 (1986) (standard for determining suitability of proposed recipient of dissolving not-for-profit's assets under nonjudicial dissolution plan was whether the organizations were involved in substantially similar activities, not whether the recipient's activities conformed as nearly as possible to those of the dissolving entity).

<sup>42</sup> 11 U.S.C. § 363(d) ("The trustee may . . . sell, or lease . . . property [of the estate] . . . (1) [i]n the case of a debtor that is a corporation or trust that is not a moneyed business, commercial corporation, or trust, only in accordance with nonbankruptcy law applicable to the transfer of property by a debtor that is such a corporation or trust . . .").

<sup>43</sup> *Id.* § 363(b)(1).

<sup>44</sup> N-PCL § 509. If the property to be purchased or disposed of does not constitute all or substantially all of the corporation's assets, then approval of the majority of the board is sufficient. *Id.* The term "entire board" is generally defined as "the total number of directors entitled to vote which the corporation would have if there were no vacancies." *Id.* § 102.

<sup>45</sup> *See* N.Y. LAB. LAW § 198-a; *Renzler v. D.F. White, Inc.*, 700 N.Y.S.2d 487, 488 (App. Div. 1999) ("Labor Law § 198-a provides a criminal penalty . . . against the officers and directors of a corporation.").

<sup>46</sup> *See, e.g., Carter v. United States*, 717 F. Supp. 188, 193 (S.D.N.Y. 1989) (holding not-for-profit directors and officers personally liable for failing to pay withholding taxes).

<sup>47</sup> *See* N.Y. Tax Law § 1133(a) ("[E]very person required to collect any tax imposed by this article shall be personally liable for the tax imposed, collected or required to be collected under this article."); N.Y. Tax Law § 1131(1) ("Persons required to collect tax' . . . shall also include any officer, director or employee of a corporation or of a dissolved corporation . . . who . . . is under a duty to act . . . in complying with any requirement of this article, or has so acted.").

<sup>48</sup> *See* N.Y. Comp. Codes R. & Regs. tit. 20, § 526.11(b)(2) ("Whether an officer or employee of a corporation is a person required to collect, truthfully account for, or pay over the sales or use tax is to be determined in every case on the particular facts involved. Generally, a person who is authorized to sign a corporation's tax returns or who is responsible for maintaining the corporate books, or who is responsible for the corporation's management, is under a duty to act."); *see also Coppola v. Tax Appeals Tribunal of State of New York*, 37 A.D.3d 901, 902-03 (2007) (explaining that personal liability turns on a fact-specific inquiry considering multiple factors).

<sup>49</sup> N-PCL § 719(a).

<sup>50</sup> *Id.* § 719(e) ("A director or officer shall not be liable under this section if, in the circumstances, he discharged his duty to the corporation under [s]ection 717 (Duty of directors and officers).").

<sup>51</sup> *Id.* § 717(a).

<sup>52</sup> *Id.* § 717(b) ("In discharging their duties, directors and officers, when acting in good faith, may rely on information, opinions, reports or statements including financial statements and other financial data, in each case prepared or presented by: (1) one or more officers or employees of the corporation, whom the director believes to be reliable and competent in the matters presented, (2) counsel, public accountants or other persons as to matters which the directors or officers believe to be within such person's professional or expert competence or (3) a committee of the board upon which they do not serve, duly designated in accordance with a provision of the certificate of incorporation or the by-laws, as to matters within its designated authority, which committee the directors or officers believe to merit confidence, so long as in so relying they shall be acting in good faith and with that degree of care specified in paragraph (a) of this section. Persons shall not be considered to be acting in good faith if they have knowledge concerning the matter in question that would cause such reliance to be unwarranted.").

<sup>53</sup> *Id.* § 720(a).

<sup>54</sup> *Id.*

<sup>55</sup> *See, e.g., United States v. King*, No. 2000 WL 362026, \*10 (W.D.N.Y. Mar. 24, 2000).

<sup>56</sup> N-PCL § 720(b).

<sup>57</sup> *Id.* § 202(a)(12).

<sup>58</sup> *Id.* § 715(d) (“Unless otherwise provided in the certificate of incorporation or the by-laws, the board shall have authority to fix the compensation of directors for services in any capacity.”).

<sup>59</sup> *Id.* § 715(e) (“The fixing of compensation of officers, if not done in or pursuant to the by-laws, shall require the affirmative vote of a majority of the entire board unless a higher proportion is set by the certificate of incorporation or by-laws.”).

<sup>60</sup> *Spitzer v. Grasso*, 11 N.Y.3d 64 (2008), *aff’g* 836 N.Y.S.2d 40 (1st Dep’t 2007), *rev’g Spitzer v. Grasso*, 816 N.Y.S.2d 863 (Sup. Ct. 2006).

<sup>61</sup> *Id.* at 70–71 (“The plain language of these provisions reveals a legislative policy decision to provide officers and directors of not-for-profit corporations with the ‘business judgment’ protections afforded their for-profit counterparts. . . . By contrast, the four nonstatutory causes of action are devoid of any fault-based elements and, as such, are fundamentally inconsistent with the [statute].”). The Supreme Court had denied the motion to dismiss with respect to the Attorney General’s statutory and nonstatutory claims. The Appellate Division reversed and dismissed the nonstatutory claims on the basis that they violated the scheme put in place by the legislature and thus exceeded the power of the Attorney General. The Court of Appeals affirmed. The remaining statutory claims were subsequently dismissed on the grounds that the stock exchange had ceased to be a not-for-profit corporation.

<sup>62</sup> I.R.C. § 4958; Lawrence M. Brauer, et al., *Intermediate Sanctions (IRC 4958) Update*, available at <https://www.irs.gov/pub/irs-tege/eotopice03.pdf>.

<sup>63</sup> Treas. Reg. §§ 53.4958-1(c)(1), 53.4958-1(c)(2).

<sup>64</sup> AM. BAR ASS’N, COMM. ON NONPROFIT CORP., *GUIDEBOOK FOR DIRECTORS OF NONPROFIT CORPORATIONS* 54, 83 (George W. Overton & Jeannie Carmedelle Frey eds., 2d ed. 2002).

<sup>65</sup> Treas. Reg. § 53.4958-6.

<sup>66</sup> N-PCL § 720-a (With certain exceptions, “no person serving without compensation as a director, officer or trustee of a corporation, association, organization or trust described in section 501(c)(3) of the United States internal revenue code shall be liable to any person other than such corporation, association, organization or trust based solely on his or her conduct in the execution of such office unless the conduct of such director, officer or trustee with respect to the person asserting liability constituted gross negligence or was intended to cause the resulting harm to the person asserting such liability.”).

<sup>67</sup> *Id.* § 514(a).

<sup>68</sup> *Id.* § 514(b) (“The governing board shall be relieved of all liability for the investment and reinvestment of institutional funds by, and for the other acts or omissions of, persons to whom authority is so delegated or with whom contracts are so made.”). Section 554 of the N-PCL governs delegation of fund management and investment functions to external investment managers. *Id.* § 554. This section permits a not-for-profit corporation to delegate such functions to an external agent only “to the extent that an institution could prudently delegate under the circumstances” and provides that a not-for-profit corporation “shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances. . . in: (1) selecting, continuing or terminating an agent . . . ; (2) establishing the scope and terms of the delegation, including the payment of compensation . . . ; and (3) monitoring the agent’s performance and compliance with the scope and terms of the delegation.” *Id.* § 554(a). A not-for-profit corporation that complies with these prerequisites is protected from liability for the decisions or actions of the agent. *Id.* § 554(c).

<sup>69</sup> *Id.* §§ 719(d), 721–26.

<sup>70</sup> *Id.* § 721.

<sup>71</sup> *Id.* § 723(a) (“A person who has been successful, on the merits or otherwise, in the defense of a civil or criminal action or proceeding of the character described in section 722 shall be entitled to indemnification as authorized in such section.”).

<sup>72</sup> *Id.* §§ 722(c), 723(a); *cf. Waltuch v. Conticommodity Servs., Inc.*, 88 F.3d 87, 96 (2d Cir. 1996) (under Delaware corporate law, success “on the merits or otherwise” in the indemnification context extends to situations in which a defendant entered into a settlement gratis (*i.e.*, without having to pay anything)); *Hermelin v. K-V Pharm.*, 54 A.3d 1093, 1107 (Del. Ch. 2012) (stating that “where the *outcome* of a proceeding signals that the indemnitee has avoided an adverse result, the indemnitee has succeeded ‘on the merits or otherwise,’ and further inquiry into the ‘how’ and ‘why’ of the result is unnecessary.”) (internal citations omitted).

<sup>73</sup> N-PCL §§ 722(c), 723(a).

<sup>74</sup> *Id.* § 724(a) (“Notwithstanding the failure of a corporation to provide indemnification, and despite any contrary resolution of the board or of the members in the specific case under section 723 (Payment of indemnification other than by court award), indemnification shall be awarded by a court to the extent authorized under section 722 (Authorization for indemnification of directors and officers), and paragraph (a) of section 723.”).

<sup>75</sup> *Id.* § 722(a).

<sup>76</sup> *Id.*

<sup>77</sup> *Id.*

<sup>78</sup> *Id.* § 724(a).

<sup>79</sup> *Id.* § 723.

<sup>80</sup> *Id.* § 723(c).

<sup>81</sup> *Id.* § 723(b)(1).

<sup>82</sup> *Id.* § 723(b)(2)(A).

<sup>83</sup> *Id.* § 723(b)(2)(B).

<sup>84</sup> *Id.* § 726.

<sup>85</sup> *Id.* § 726(b)(1) (“No insurance under paragraph (a) may provide for any payment, other than cost of defense, to or on behalf of any director or officer: (1) if a judgment or other final adjudication adverse to the insured director or officer establishes that his acts of active and deliberate dishonesty were material to the cause of action so adjudicated, or that he personally gained in fact a financial profit or other advantage to which he was not legally entitled.”).

<sup>86</sup> Richard M. Cieri & Michael J. Riela, *Protecting Directors and Officers of Corporations That Are Insolvent or in the Zone or Vicinity of Insolvency: Important Considerations, Practical Solutions*, 2 DEPAUL BUS. & COM. L.J. 295 (2004).

<sup>87</sup> *See, e.g., Gillman v. Cont’l Airlines (In re Cont’l Airlines)*, 203 F.3d 203, 217 (3d Cir. 2000) (“Other courts of appeals have disagreed as to the circumstances under which the proceeds of a D&O policy can be considered property of the estate, but the analysis has been fact-intensive in any event.”).

<sup>88</sup> *Compare Id.* (“One cannot assume too quickly that the proceeds of this policy are property of the estate when the non-debtor D&Os, not the Continental Debtors, are the direct beneficiaries of the policy. We previously have recognized, albeit in a different context, that the proceeds from an insurance policy should be evaluated separately from the debtor’s interest in the policy itself.”) and *In re La. World Exposition, Inc.*, 832 F.2d 1391, 1401 (5th Cir. 1987); *In re Adelpia Commc’ns Corp.*, 298 B.R. 49 (S.D.N.Y. 2003) (“The problem here, however, is that the Bankruptcy Court assumed that the proceeds from the policies were assets of Adelpia’s estate and automatically subject to the stay under § 362(a)(3). As discussed above, that is not the case.”), with *Minoco Grp. of Cos. v. First State Underwriters Agency (In re Minoco Grp. of Cos.)*, 799 F.2d 517, 519 (9th Cir. 1986) (finding that D&O insurance policy was property of the estate because “the estate [wa]s worth more with the policy than without the policy”); and *First Cent. Fin. Corp. v. Lipson (In re First Cent. Fin. Corp.)*, 238 B.R. 9, 16 (Bankr. E.D.N.Y. 1999) (“While a majority of courts consider a D&O policy estate property [citations omitted], there is an increasing view that a distinction should be drawn when considering treatment of proceeds under such policies.”); *In re W.R. Grace &*

Co., 475 B.R. 34, 80-81 (D. Del. 2012) (noting that the treatment of proceeds under an insurance policy depends on whether the proceeds are payable to the debtor or some other claimant).

<sup>89</sup> N-PCL § 706(a), (c).

<sup>90</sup> *Id.* § 706(d) (“An action to procure a judgment removing a director for cause may be brought by the attorney-general or by ten percent of the members whether or not entitled to vote.”).

<sup>91</sup> *Id.*

<sup>92</sup> *Id.* § 706(b) (With certain exceptions, “if the certificate of incorporation or the by-laws so provide, any or all of the directors may be removed without cause by vote of the members.”).

<sup>93</sup> *Frantz Mfg. Co. v. EAC Indus.*, 501 A.2d 401, 408 (Del. 1985) (“Directors are also free to resign.”).

<sup>94</sup> *7th Sense, Inc. v. Liu*, 631 N.Y.S.2d 835, 836 (App. Div. 1995) (lower court “properly determined that the purported resignation of defendant Victor Liu as an officer and director of corporate plaintiff 7th Sense for personal gain did not relieve him of his fiduciary obligations or liability for his acts of misappropriation”); *Dist. 65, UAW v. Harper & Row Publishers*, 576 F. Supp. 1468, 1483–84 (S.D.N.Y. 1983).

<sup>95</sup> *See, e.g., Zeltner v. Henry Zeltner Brewing Co.*, 174 N.Y. 247, 252–53 (1903).

<sup>96</sup> The business judgment rule will protect directors who rely on their restructuring consultants, even if the restructuring consultants ultimately fail to deliver. *See Gottlieb v. Hicks*, 2007 WL 5312635 (C.D. Cal. Jan. 13, 2006).

<sup>97</sup> *In re Save Our Springs Alliance*, 632 F.3d 168, 172 (5th Cir. 2011) (“The bankruptcy court’s conclusion that past donations are not evidence of future fundraising ability is thus appropriate.”).

<sup>98</sup> *Id.*

<sup>99</sup> For more detail regarding chapter 11, see **Tab 12**.

<sup>100</sup> While an individual debtor is not entitled to a discharge of all of his or her prepetition debts, corporations are entitled to a full discharge unless they file plans of liquidation.

<sup>101</sup> *See, e.g., In re Bankr. Appeal of Allegheny Health, Educ. & Research Found.*, 252 B.R. 332 (W.D. Pa. 1999) (automatic stay did not apply to void state court injunction protecting not-for-profit organization’s charitable assets from its creditors because the state court litigation was subject to the police powers exception to the automatic stay; movants could seek injunctive relief pursuant to section 105 of the Bankruptcy Code, but existence of a viable exception to the stay would inform court’s decision of whether to enjoin a proceeding).

<sup>102</sup> *See* 11 U.S.C. § 364.

<sup>103</sup> The Bankruptcy Code also caps the damages claim of a landlord whose lease is rejected to approximately one year of rent. *Id.* § 502(b)(6). This can be very beneficial to debtors with long-term leases.

<sup>104</sup> When assets are sold free and clear of liens, the liens attach to the proceeds of the sale. *See Id.* § 363.

<sup>105</sup> *Id.* § 1129(b).

<sup>106</sup> *In re Wabash Valley Power Ass’n, Inc.*, 72 F.3d 1305, 1313 (7th Cir. 1995), *cert. denied*, 519 U.S. 965 (1996) (the absolute priority rule “provides that, in order for a bankruptcy plan to be approved in the face of the refusal of an unsecured creditor to accept it (a “cramdown”), the holder of any claim or interest junior to that of the dissenter may not ‘receive or retain under the plan on account of such junior claim or interest any property.’”) (internal citation omitted).

<sup>107</sup> *Id.* at 1318-19; *See also In re Gen. Teamsters, Warehousemen & Helpers Union, Loc. 890*, 265 F.3d 869, 872 (9th Cir. 2001) (affirming decision that chapter 11 plan did not violate the absolute priority rule because not-for-profit debtor’s parent did not have an equity interest in the not-for-profit debtor that would entitle it to be treated like a shareholder or equivalent holder of an equity interest in a for-profit corporation).

<sup>108</sup> *In re Wabash Valley Power Ass'n, Inc.*, 72 F.3d at 1318-19 (“The mere fact that the Members of [not-for-profit electric cooperative] are benefited by Wabash’s operation and might be disadvantaged by its demise also does not give them an ‘interest’ cognizable in bankruptcy. Employees, managers and customers, among others, always have an interest, in the broadest sense, in a corporation. The factor which distinguishes these parties from stockholders is not ‘control’ per se (managers, after all, have at least a limited control) but the ability to make use of that control to generate profits or to increase their own share of profits.”).

<sup>109</sup> A bankruptcy court is virtually required to grant an examiner for any reason if the debtor has aggregate debts in excess of \$5 million. *See* 11 U.S.C. § 1104(c). *But See In re Residential Capital, LLC*, 474 B.R. 112, 120–121 (Bankr. S.D.N.Y. 2012) (concluding that a bankruptcy court may deny appointment of an examiner in limited circumstances, even when the debtor has over \$5 million in fixed debts).

<sup>110</sup> *See In re Adelphia Commc’ns. Corp.*, 336 B.R. 610, 655-656 (Bankr. S.D.N.Y. 2006) (“It has been repeatedly held that the appointment of a chapter 11 trustee is an ‘extraordinary remedy’ . . . and “should be the exception, rather than the rule.”) (internal citations omitted).

<sup>111</sup> *In re Am. Hous. Found.*, 2010 WL 3211691, at \*3 (Bankr. N.D. Tex. Aug. 11, 2010).

<sup>112</sup> 11 U.S.C. § 363(d).

<sup>113</sup> *Id.* § 303(a).

<sup>114</sup> *Id.* § 1112(c).

<sup>115</sup> *See, e.g., In re Sheehan Mem’l Hosp.*, 301 B.R. 777 (Bankr. W.D.N.Y. 2003) (because court could not convert case of not-for-profit debtor that defaulted on its ongoing obligations to chapter 7, it dismissed the case altogether).

<sup>116</sup> As of April 1, 2025, the debt limit is \$3,424,000.

<sup>117</sup> *See* § 101(51D); § 104; 90 Fed. Reg. 8941, 8942 (Feb. 4, 2025).

<sup>118</sup> *See In re Guan v. Ellingsworth Residential Community Association, Inc.*, 125 F.4th 1365, 1379-1380 (11th Cir. 2025); *In re RS Air, LLC*, 638 B.R. 403, 405 (B.A.P. 9th Cir. 2022).

<sup>119</sup> *See* 11 U.S.C. § 1181(b) (providing that the disclosure statement requirement in 1125 does not apply in a case under subchapter V unless the court orders otherwise).

<sup>120</sup> *See* 11 U.S.C. § 1181(b) (providing that 1102(a)(1), which requires the court to appoint a committee of creditors, does not apply in a case under subchapter V, unless the court orders otherwise).

<sup>121</sup> *See* 11 U.S.C. § 1191(b) (removing the 1129(a)(10) requirement that there must be at least one accepting impaired class of claims to confirm a chapter 11 plan).

<sup>122</sup> *See* 11 U.S.C. § 1191(c)(2).

<sup>123</sup> *See* 11 U.S.C. § 1181(a).

<sup>124</sup> For a comparison of liquidation under state law or chapter 11 or chapter 7 of the Bankruptcy Code, see **Tab 12**.

<sup>125</sup> *See* N.Y. AG, Voluntary Dissolution of Not-for-Profit Corporations with Assets 3 (2024) (explaining that an insolvent not-for-profit corporation is not eligible for a non-judicial dissolution).

<sup>126</sup> As of July 1, 2014, there are two types of not-for-profit corporations under New York law: charitable and non-charitable corporations. N-PCL § 201(b). Not-for-profit corporations formed prior to July 1, 2014 fell into one of four types: A, B, C, or D. Under the new section 201 of the Not-For-Profit Corporation Law, Type A corporations are deemed non-charitable corporations, while Types B and C corporations are deemed charitable corporations. Type D corporations “formed for charitable purposes” are also deemed charitable corporations, while Type D corporations formed for any other purpose are deemed non-charitable corporations. Charitable corporations are defined as “any corporation formed, or . . . deemed to be formed, for charitable purposes.” *Id.* § 102(a)(3-a). Non-charitable corporations are defined as corporations formed under the N-PCL other than charitable corporations. *Id.* § 102(a)(9-a).

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<sup>127</sup> *Id.* §§ 1001 *et seq.*

<sup>128</sup> *Id.* § 1001(c).

<sup>129</sup> For more details regarding the step-by-step process, *See* <https://ag.ny.gov/sites/default/files/2023-02/dissolution-without-assets.pdf>.

<sup>130</sup> *Id.* §1001(d).

<sup>131</sup> *Id.* § 1002(d)(3).

<sup>132</sup> *Id.* § 719(a)(4) (directors who vote for or concur in a distribution of assets without paying or adequately providing for all known liabilities are jointly and severally liable to the corporation to the extent of any injury suffered therefrom by creditors, members, or the corporation itself).

<sup>133</sup> *Id.* §§1101 *et seq.*

<sup>134</sup> *Id.* § 1101.

<sup>135</sup> *Id.* § 1102(a).

<sup>136</sup> *Id.* § 1102(a)(1)

<sup>137</sup> *See, e.g., Id.* §§ 1201–18.

<sup>138</sup> *See, e.g., Compagnia Distribuzione Calzature, S.R.L. v. PSF Shoes Ltd.*, 613 N.Y.S.2d 931 (App. Div. 1994).

## Not-For-Profit Practice Group

### Warning Signs of Distress for Not-for-Profit Organizations

Not-for-profit directors should keep an eye out for warning signs of distress. Listed below are non-exclusive examples of several warning signs of distress for not-for-profit organizations.

#### I. DECLINING INCOME

As many not-for-profit organizations rely on donations and government/private grants to fund their operations, it is as important to monitor these external income sources as it is to watch operational revenue levels. In addition, relying on any one source of funding or donor for a significant portion of an organization's funding puts the organization's financial viability at risk if funding from that donor or source ceases or decreases. A continuous or precipitous decline in any of the following sources of income, or an excessive concentration of revenue in any one area, can have a negative impact on the financial viability of the organization.

##### Charitable Contributions/Donations

1. Government/Private Grants
2. Member Dues/Fees
3. Corporate Partnerships
4. Operational Revenue
  - a. May be evidenced by excessive receivables outstanding for over 90 days
  - b. May be caused by a major customer's payment default

#### II. INCREASING OR DISPROPORTIONATELY HIGH EXPENSES

An increase in expenses can be a warning sign of distress. Stable or disproportionately high expenses may also be a warning sign if income is decreasing or not increasing proportionately. Although the board may not be able to control income, it usually has more control over (or at least visibility into) expenses. An increase in any of the following sources of expenses can have a negative impact on the financial viability of the organization:

1. Program Expenses
2. Administrative Expenses
3. Fundraising Expenses

#### III. CREDIT PROBLEMS

Not being able to pay debts as they come due is a bad sign and most likely signals entry into the "zone of insolvency." Credit problems may be evidenced by:

1. Excessive payables remaining unpaid for over 90 days

2. Insufficient funds available to make deposits into trust funds such as employee withholding taxes
3. Inability to fulfill long-term debt obligations
4. Creditors not willing to advance credit
5. Vendors seeking payment on COD terms
6. Losing a major supplier that had performed under special credit terms
7. Reduction in existing lines of credit
8. Excessive re-negotiation of broken loan covenants

#### **IV. ACCOUNTING ISSUES**

Poor financial controls and accounting issues are regular themes for organizations in distress. Ensuring that a board of directors has sufficient expertise in accounting matters to oversee a not-for-profit organization appropriately is key to avoiding otherwise foreseeable financial difficulties. Examples of accounting issues that lead to financial distress are:

1. Unplanned auditor turnover
2. Weak financial reporting, e.g., financial statements are untimely, lack important detail or are too voluminous to be useful, external auditors fail to identify major financial issues, account analyses are delinquent, or basic financial controls are lacking
3. Poor record keeping or inadequate financial records
4. Lack of basic controls, such as perpetual inventory record keeping
5. Significant discrepancies between actual and projected results of the prior three years

#### **V. OPERATIONAL INEFFICIENCIES**

A poorly run organization is bound for financial ruin regardless of how its financials look. Signs of operational inefficiencies include:

1. Board micro-management
2. Absentee board members
3. Laissez-faire board attitudes (e.g., no regular meetings and disregard for other formalities) or a stagnant board roster with long-tenured members selected by the CEO
4. Excessive dependence on consultants
5. High administrative overhead costs

#### **VI. OTHER SIGNS OF DISTRESS**

1. Criminal investigations, extraordinary litigation, or other unusual events not ordinarily encountered in the industry

2. Loss of key financial officers or key personnel
3. Although cash management is always a concern, it may be a warning sign if cash management becomes a primary activity at the expense of traditional management functions
4. Self-dealing by directors and/or others, excessive compensation
5. Whistleblower complaints

## Not-For-Profit Practice Group

### Comparison of Liquidation Options

	CHAPTER 11	CHAPTER 7	STATE LAW
<b>Complexity &amp; Control</b>	<ul style="list-style-type: none"> <li>▪ Generally more complex and requires significant time, effort, and resources from the debtor-company.</li> <li>▪ Potentially more streamlined process (i.e., subchapter V of chapter 11) available to companies with liabilities below a certain threshold; still more complex than other options.</li> <li>▪ See <i>Appendix B</i> for more details on subchapter V.</li> <li>▪ Generally, except where “cause” exists (see <i>Possible Loss of Control</i>), the debtor-company, along with its existing management and directors, remains in control of the business as the “debtor in possession.”</li> <li>▪ See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Can be relatively quick.</li> <li>▪ A court-appointed trustee handles the liquidation of the estate. Management and the board of directors do not control the case.</li> </ul>	<ul style="list-style-type: none"> <li>▪ State law processes (including receivership and/or dissolution) can be complex and slow.</li> <li>▪ There is a somewhat streamlined non-judicial dissolution process available to solvent organizations looking to wind down that have assets and liabilities below a certain threshold and few to no creditors. But even this process comes with its own complexities.</li> <li>▪ In a state law dissolution, the board or management retains control of the dissolution.</li> <li>▪ In a state law receivership, there is a complete loss of control by the company.</li> </ul>
<b>Automatic Stay</b>	<ul style="list-style-type: none"> <li>▪ Automatic stay protects debtor-company from actions by any creditor (including, secured lenders, trade creditors, and potential litigants) to enforce remedies or otherwise collect on any debt.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Automatic stay protects debtor-company from actions by any creditor (including, secured lenders, trade creditors, and potential litigants) to enforce remedies or otherwise collect on any debt.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No automatic stay or analog in state law dissolution proceedings.</li> <li>▪ If liquidating in a receivership, the appointment of a receiver functions like the automatic stay in a bankruptcy case, but</li> </ul>

	CHAPTER 11	CHAPTER 7	STATE LAW
	<ul style="list-style-type: none"> <li>See <i>Appendix A</i>.</li> </ul>		<p>only for actions against property in the receivership. Property in the receivership will be liquidated and distributed pursuant to a court-ordered plan.</p>
<b>Contracts &amp; Real Property Leases</b>	<ul style="list-style-type: none"> <li>Debtor-company has the choice to assume (<i>i.e.</i>, cure defaults and continue performance as usual), assume and assign (<i>i.e.</i>, assume and assign to a third party), or reject (<i>i.e.</i>, cease performance and effectively freeze damages) certain contracts and real property leases.</li> <li>Debtor-company can deal with all of its contracts immediately rather than as they come due.</li> <li>Section 502(b) of the Bankruptcy Code caps rejection damages for real property leases and certain other contracts that are rejected.</li> <li>See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>Same choices as chapter 11 but the chapter 7 trustee (not the debtor-company) has the option for each contract and lease.</li> <li>Section 502(b) of the Bankruptcy Code caps rejection damages for real property leases and certain other contracts that are rejected.</li> </ul>	<ul style="list-style-type: none"> <li>State law dissolution does not offer special protections or powers vis-à-vis contracts and leases.</li> <li>In a receivership, contracts and leases are generally maintained until rejected by the receiver (if at all).</li> </ul>
<b>Dealing with Creditors</b>	<ul style="list-style-type: none"> <li>The debtor-company deals with individual creditors as well as statutory committees (such as an unsecured creditors' committee).</li> <li>Because classes of creditors vote on whether to accept a plan in accordance with</li> </ul>	<ul style="list-style-type: none"> <li>The chapter 7 trustee will deal with creditors.</li> <li>There is no voting or plan confirmation. Rather, the Bankruptcy Code outlines strict rules for the distribution of property in accordance</li> </ul>	<ul style="list-style-type: none"> <li>Management deals with creditors in a state law dissolution.</li> <li>If a receivership is established, the receiver deals with creditors who attempt to "prove" their claim in the court that</li> </ul>

	CHAPTER 11	CHAPTER 7	STATE LAW
	<p>consent thresholds established by the Bankruptcy Code, approval of all creditors is not required. Furthermore, classes of creditors that do not approve of the plan may be “crammed down” if a single impaired class of creditors votes in favor of the plan and other requirements of the Bankruptcy Code are satisfied.</p> <ul style="list-style-type: none"> <li>See <i>Appendix A</i>.</li> </ul>	<p>with the prescribed waterfall.</p>	<p>has jurisdiction over the receivership.</p>
<b>Claims</b>	<ul style="list-style-type: none"> <li>Allowed claims are paid pursuant to a confirmed chapter 11 plan.</li> <li>See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>Allowed claims are paid pursuant to the priority of distributions specified in the Bankruptcy Code.</li> <li>Unless claims are subordinated under section 510 of the Bankruptcy Code (<i>i.e.</i>, by agreement or because of a creditor’s inequitable conduct), priority claims and secured claims are paid before unsecured claims. Claims for fines, penalties, or punitive damages and postpetition interest are only payable after all other claims are paid.</li> <li>If (and only if) anything remains in the “pot” after all creditor claims are satisfied in full, equity holders may receive a distribution.</li> </ul>	<ul style="list-style-type: none"> <li>If the company is dissolved under state law, any remaining assets will be distributed as part of a plan of distribution that must be approved by the court (or the attorney general, depending on the type of dissolution). Dissolution cannot be used to evade creditors, and personal liability may attach for inappropriate distribution of assets.</li> <li>In a receivership, claims are paid out by the receiver upon liquidation of the assets.</li> </ul>

	CHAPTER 11	CHAPTER 7	STATE LAW
<b>Sources of Funds</b>	<ul style="list-style-type: none"> <li>▪ A debtor may use the avoidance powers under the Bankruptcy Code to avoid certain prepetition (<i>i.e.</i>, pre-bankruptcy) transfers of property as preferences or fraudulent transfers, even if there was no “fraud” in the literal sense.</li> <li>▪ Under the Bankruptcy Code, assets can be sold free and clear of liens and other encumbrances.</li> <li>▪ The Bankruptcy Code provides incentives to lenders to provide financing to the debtor-company during the course of the bankruptcy case to allow for continued operations.</li> <li>▪ See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>▪ A chapter 7 trustee may use the avoidance powers under the Bankruptcy Code to avoid certain prepetition transfers of property as preferences or fraudulent transfers.</li> <li>▪ Under the Bankruptcy Code, assets can be sold free and clear of liens and other encumbrances.</li> <li>▪ Financing is typically not an issue because a debtor, absent court approval, will not continue to operate.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Certain transfers may be avoided under state fraudulent transfer law, but preferential transfers can only be avoided in bankruptcy and not state law proceedings.</li> <li>▪ Assets can be sold free and clear of liens through specific court action in a receivership.</li> </ul>
<b>Employee Wages</b>	<ul style="list-style-type: none"> <li>▪ Employee wages are generally given payment priority under the Bankruptcy Code.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Employee wages are generally given payment priority under the Bankruptcy Code.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Employees need to be paid before dissolution.</li> <li>▪ In a receivership, the court may give employee wages priority.</li> </ul>
<b>Judicial and Other Oversight</b>	<ul style="list-style-type: none"> <li>▪ The bankruptcy court, statutory committees (such as an unsecured creditors’ committee), and the Office for the United States Trustee (a division of the Department of Justice) oversee the chapter 11 cases.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The bankruptcy court oversees the process along with the chapter 7 trustee, which controls the estate and the direction of the cases.</li> <li>▪ Creditors may elect a creditors’ committee under section 705 of the Bankruptcy Code, but this option is rarely exercised.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The state court, in a judicial dissolution, and the attorney general, in a non-judicial dissolution,<sup>1</sup> oversee dissolution proceedings.</li> <li>▪ The court oversees a receivership (unless the receivership is created by an administrative agency, in which case the agency provides oversight).</li> </ul>

	CHAPTER 11	CHAPTER 7	STATE LAW
<b>Director and Officer Exposure &amp; Protection</b>	<ul style="list-style-type: none"> <li>▪ Chapter 11 plan may provide for limited releases for directors and officers.</li> <li>▪ See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Generally no mechanism for releasing directors and officers.</li> <li>▪ The chapter 7 trustee is entitled to statutory protections.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No additional protection for directors and officers.</li> <li>▪ Personal liability may attach for improper distribution of assets in a state law dissolution.</li> </ul>
<b>Possible Loss of Control</b>	<ul style="list-style-type: none"> <li>▪ For cause shown (<i>e.g.</i>, fraud, dishonesty, incompetence, or gross mismanagement), the bankruptcy court may appoint a trustee to displace management.</li> <li>▪ See <i>Appendix A</i>.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The debtor-company has no control after the chapter 7 trustee is appointed.</li> </ul>	<ul style="list-style-type: none"> <li>▪ If dissolving pursuant to state law, an organization should be able to retain control of the process, but either the court or the attorney general will play a significant role.</li> <li>▪ If liquidating through a receivership, the receiver and the court control the process; organization, board, and management lose control.</li> </ul>

**APPENDIX A**

**ADVANTAGES & DISADVANTAGES OF CHAPTER 11**

	<b>ADVANTAGES</b>	<b>DISADVANTAGES</b>
<b>Automatic Stay</b>	<ul style="list-style-type: none"> <li>▪ Chapter 11 can provide a debtor-company with breathing room to deal with its creditor claims. The debtor-company will no longer have to worry about creditors running to the court to secure judgments against it because the Bankruptcy Code provides for an automatic stay of all actions against a debtor, its property and property in its possession.</li> <li>▪ Generally lasts for the duration of the bankruptcy case.</li> </ul>	<ul style="list-style-type: none"> <li>▪ The automatic stay is subject to certain limitations (<i>e.g.</i>, governmental entities exercising their police and regulatory powers are not subject to the stay) and can be lifted in certain cases (<i>e.g.</i>, where “good cause” exists to allow a creditor to proceed notwithstanding the bankruptcy).</li> </ul>
<b>Contracts &amp; Leases</b>	<ul style="list-style-type: none"> <li>▪ As noted above, contracts and leases may be assumed, assumed and assigned to a third party, or rejected.</li> <li>▪ A chapter 11 case affords a debtor-company the ability to reject executory contracts and unexpired leases that are no longer advantageous. A rejection is treated as a breach of such contract or lease as of the time of the bankruptcy filing and rejection damages are paid as general unsecured claims in accordance with the chapter 11 plan.</li> <li>▪ These chapter 11 tools allow a not-for-profit organization to deal with all of its contracts immediately (or shortly after the filing of the cases) rather than as obligations under the contracts come due. This allows the debtor-company to avoid the continued incurrence of obligations under an agreement. Put another way, chapter 11 can help “stop the bleeding” if the debtor-company is trapped by a disadvantageous contract.</li> <li>▪ Section 502(b)(6) of the Bankruptcy Code caps damages claims arising from the rejection of real property leases.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Parties to contracts and leases that are assumed by the debtor-company are generally entitled to 100% payment of their past-due amounts at the time of assumption. Thus, if the debtor-company needs to keep certain contracts, it will need to have sufficient cash to cover any arrearage at the time of such assumption.</li> <li>▪ Contracts not assignable outside of bankruptcy, such as intellectual property licenses, are also not assignable during bankruptcy (without counterparty consent). In certain jurisdictions, such contracts also may not be assumable.</li> <li>▪ The contract or lease counterparty can demand assumption or rejection before confirmation of the chapter 11 plan.</li> <li>▪ The Bankruptcy Code does not excuse a debtor-company from performing under an agreement once in bankruptcy. In other words, if the debtor-company incurs obligations during the chapter 11 case, it generally (with very few exceptions) must pay those obligations in full as they become due.</li> </ul>

	<b>ADVANTAGES</b>	<b>DISADVANTAGES</b>
<b>Dealing with Creditors</b>	<ul style="list-style-type: none"> <li>▪ Chapter 11 provides a single forum for dealing with all of the debtor-company’s creditors at once.</li> <li>▪ The protections of chapter 11 change the dynamics of negotiations with creditors.</li> <li>▪ The debtor-company will not need unanimous approval from creditors to bind creditors to a chapter 11 plan. In a chapter 11 case, a plan is accepted by a class of creditors if at least 50% in number and two-thirds in amount of the creditors holding allowed claims in that class (who actually vote) vote to accept the plan.</li> <li>▪ Even if a class does not accept the plan, the debtor-company can still confirm a plan over that class’s dissent so long as at least one impaired class of creditors votes to accept its chapter 11 plan. In other words, the debtor-company will have the ability to “cramdown” a class of unsecured creditors, even if that class votes against the plan, as long as one other impaired creditor class votes to accept the plan.</li> </ul>	<ul style="list-style-type: none"> <li>▪ To protect creditors and the debtor-company’s estate, bankruptcy court approval is required for most actions taken by the debtor-company during a bankruptcy case. The bankruptcy court then becomes a forum for creditors to object to the debtor-company’s course of action, and the court will not approve conduct that will inequitably diminish a creditor’s claim. For example, a debtor-company will need to obtain court approval to use cash collateral encumbered by a creditor and will need to obtain court approval to sell any assets outside of the ordinary course of business.</li> </ul>
<b>Claims</b>	<ul style="list-style-type: none"> <li>▪ A chapter 11 filing will bring all claims against the not-for-profit debtor-company to the forefront, thus enabling the company to achieve a true fresh start. Chapter 11 also flushes out contingent claims.</li> <li>▪ Chapter 11 provides a mechanism for treating all creditors equally and minimizes the risk of creditor holdouts seeking better treatment.</li> </ul>	<ul style="list-style-type: none"> <li>▪ May attract and motivate claimants who would have otherwise not pursued claims and claimants with contingent claims thereby increasing the claims pool.</li> </ul>
<b>Sources of Funds</b>	<ul style="list-style-type: none"> <li>▪ A debtor-company may use the avoidance powers under the Bankruptcy Code to recover property by unwinding certain prepetition transfers of property as preferences or fraudulent transfers.</li> </ul>	<ul style="list-style-type: none"> <li>▪ It is unclear whether restricted funds, including endowments, and restricted donations may be available to satisfy creditor claims.</li> <li>▪ Filing for bankruptcy may scare off donors.</li> </ul>

	ADVANTAGES	DISADVANTAGES
	<ul style="list-style-type: none"> <li>A chapter 11 filing could potentially lead to greater contributions from supporters of the not-for-profit organization.</li> <li>The Bankruptcy Code offers incentives for financiers to provide financing during a reorganization.</li> </ul>	
<b>Employee/Retiree Benefits Issues</b>	<ul style="list-style-type: none"> <li>A chapter 11 case can provide a debtor-company with a forum and process for dealing with the termination of retiree benefits.</li> </ul>	<ul style="list-style-type: none"> <li>In certain jurisdictions, a debtor-company may be prohibited from terminating retiree benefits without first complying with the process set forth in the Bankruptcy Code even if the applicable benefits plan authorizes termination at the election of the employer.</li> <li>A chapter 11 filing may cause anxiety among employees.</li> </ul>
<b>Public Relations</b>	<ul style="list-style-type: none"> <li>Ultimately, reorganizing may make the most business sense, despite a negative reaction from the public. A responsible reorganization will leave the reorganized not-for-profit entity more fit to pursue its mission and more deserving of public trust.</li> </ul>	<ul style="list-style-type: none"> <li>A chapter 11 filing will bring the debtor-company's troubles into the public eye. This could potentially impair a not-for-profit organization's ability to fundraise. On the other hand, in some situations, a chapter 11 filing could act as an impetus for donations.</li> </ul>
<b>Director and Officer Exposure</b>	<ul style="list-style-type: none"> <li>Some chapter 11 plans of reorganization contain releases for director and officer actions taken before or during the course of the bankruptcy.</li> </ul>	<ul style="list-style-type: none"> <li>A chapter 11 filing may increase director and officer exposure to lawsuits by creditors, especially if the plan contains no or only limited release provisions.</li> </ul>
<b>Costs of Chapter 11</b>	<ul style="list-style-type: none"> <li>The administrative costs of a chapter 11 case may be high but worthwhile if the company can reorganize and emerge as a leaner, healthier enterprise (rather than liquidate and dissolve).</li> </ul>	<ul style="list-style-type: none"> <li>The administrative costs of a chapter 11 case may be high. For example, the debtor-company is required to pay the creditors' committee's professional fees (lawyers, accountants and/or financial advisors) and quarterly U.S. Trustee fees (fees range from \$250/quarter to \$250,000/quarter depending on the quantum of a debtor-company's disbursements).</li> </ul>

	ADVANTAGES	DISADVANTAGES
<p><b>Possible Loss of Control</b></p>	<ul style="list-style-type: none"> <li>▪ The debtor-company typically remains in control during the pendency of the chapter 11 case.</li> </ul>	<ul style="list-style-type: none"> <li>▪ For cause shown (<i>e.g.</i>, fraud, dishonesty, incompetence or gross mismanagement), the bankruptcy court may appoint a trustee to displace management. The appointment of a trustee is atypical in a chapter 11 case.</li> </ul>

**APPENDIX B**

**SUBCHAPTER V OF CHAPTER 11**

	<b>SUBCHAPTER V</b>	<b>TRADITIONAL CHAPTER 11</b>
<b>Who Qualifies?</b>	<ul style="list-style-type: none"> <li>▪ Debtor must have no more than \$3,424,000 in total fixed debt (excluding insider/affiliate debt).</li> <li>▪ At least 50% of the debt must come from business activities.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No debt limit.</li> </ul>
<b>Filing a Plan</b>	<ul style="list-style-type: none"> <li>▪ Debtor must file a plan within 90 days of commencing case.</li> <li>▪ No disclosure statement required unless ordered by the court.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No fixed deadline to file a plan.</li> <li>▪ Debtor must file and receive court approval of a disclosure statement to solicit votes on plan.</li> </ul>
<b>Confirming a Nonconsensual Plan</b>	<ul style="list-style-type: none"> <li>▪ Debtor must commit projected disposable income for 3–5 years to fund plan.</li> <li>▪ Plan can be confirmed even if no impaired classes vote in favor.</li> <li>▪ Equity holders may retain interests without full payment to unsecured creditors.</li> </ul>	<ul style="list-style-type: none"> <li>▪ No disposable income requirement.</li> <li>▪ Plan cannot be confirmed unless at least one impaired creditor class votes in favor.</li> <li>▪ Equity holders generally may not retain interests without full payment to unsecured creditors.</li> </ul>
<b>Other Key Features</b>	<ul style="list-style-type: none"> <li>▪ No creditors’ committee appointed unless ordered by the court.</li> <li>▪ A trustee is automatically appointed, but only to oversee and facilitate the case; the debtor remains in possession.</li> </ul>	<ul style="list-style-type: none"> <li>▪ An official committee of unsecured creditors is usually appointed to represent unsecured creditor interests.</li> <li>▪ A trustee is not automatically appointed; usually only in cases involving mismanagement or misconduct.</li> </ul>

## ENDNOTES

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<sup>1</sup> Ultimately, court approval of a non-judicial plan of distribution is still required, unless the streamlined procedures for organizations with assets and liabilities below a certain threshold are utilized.

## Not-For-Profit Practice Group

### Checklist for Directors of Distressed Not-For-Profit Organizations

#### I. FINANCIAL MANAGEMENT

- Understand the organization’s liquidity and cash position
  - Ensure that the organization models quarterly (or periodic) cash flows
  - Analyze and assess the ability of the organization to generate enough cash to survive in the short-term
  - Evaluate whether any business areas require short-term capital to maximize long-term profit potential and whether any areas require immediate funding
  - Determine when the organization will have liquidity issues or when liquidity issues started
  - Analyze liquidity and cash constraints:
    - How much cash is restricted? Is the cash donor-restricted or board-restricted?
    - How can the organization free up cash to maximize liquidity (for example, via asset sales or securitization)?
  - Develop a calendar of key dates, including dates of major cash outlays, covenant dates, and cure periods
  - Review receivables to determine if current collection methods are sufficient
  - Review payables to determine which vendors are “critical”
  - Identify alternative financing sources
    - Identify vulnerabilities and determine how to reduce impact of vulnerabilities
    - Formulate and communicate an action/restructuring plan:
  - How are you going to preserve the profitable operations and abort the unprofitable ones?
  - Can you resolve any operational issues outside of bankruptcy with the consent of the creditors/parties involved?
    - Set goals and standards to monitor the organization’s financial situation and to evaluate performance (determine what success looks like for the organization and whether the organization is on track to achieve such success)
    - Reassess the budget and determine whether to cut back operations
    - Reassess loan covenants and determine whether to renegotiate contracts
    - Institute internal control procedures for:

- Handling funds received and expended by the organization
- Appropriate and timely financial reporting for board members and officers
- Auditing the organization's financial statements
- Evaluating staff and benefit programs
- Maintaining inventory records of real and personal property and their whereabouts
- Implementing personnel and conflict of interest policies
- Assuring compliance with requirements regarding restricted funds

## **II. BOARD COMPOSITION**

- Determine whether there are enough board members with adequate finance and/or restructuring backgrounds and, if not, add additional board members with the requisite expertise
- Add management directors to the board
- Establish special committees to address problem areas
- Add independent director if needed (especially when conflicts of interest arise)

## **III. REVIEW AND EVALUATE ADVISORS, CONTRACTS AND LEASES, AND EXPENDITURES**

- Advisors
  - is it time for a new accountant and/or audit firm?
  - Is it time to discuss options with a financial advisor or restructuring attorney?
- Contracts and leases
  - What contracts and leases are necessary for the organization's continued survival?
  - Are there contracts or leases that could be eliminated?
- Capital expenditures
  - Where are the ongoing capital improvement projects?
  - Which capital expenditures are really needed?
- Which capital expenditures can be terminated without incurring significant additional liabilities?
  - Identify Key Creditor Constituencies and Potential Leverage
  - Government Assistance

- Consider whether assistance can or should be sought from state and/or local governmental authorities

#### **IV. EMPLOYEES**

- Determine whether the organization will be able to pay employee salaries in full and on time. (Note: the failure to pay employee salaries may give rise to director liability.)
- Ensure that withholding taxes are paid to the government in full and on time
- Determine whether the organization will have to give notice to employees it terminates (e.g., two weeks or more)

#### **V. DEVELOP A COMMUNICATIONS PROGRAM**

- Consider how to maintain good relationships with donors while not misleading anyone about the organization's financial condition
- Determine whether it makes sense to reach out to the Attorney General's office
- Develop a communications strategy for other key constituents, including employees and donors

## Not-For-Profit Practice Group

### Sample New York Not-For-Profit Certificate of Incorporation

This sample certificate of incorporation may be used as a starting point for developing a certificate of incorporation for a not-for-profit organization incorporated in New York. If the organization has an existing certificate of incorporation, this form may offer a useful comparison against provisions of the not-for-profit's existing certificate of incorporation and offer the opportunity to review whether such certificate of incorporation is in line with the organization's current operations and New York law.

This sample certificate of incorporation incorporates provisions required by the New York Not-for-Profit Corporation Law (the "N-PCL") as amended by the Non-Profit Revitalization Act of 2013, as amended.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]<sup>1</sup>

## Certificate of Incorporation

### Under Section 402 of the New York Not-for-Profit Corporation Law

THE UNDERSIGNED, being a natural person of the age of eighteen (18) or over, acting as the incorporator, and desiring to form a corporation pursuant to the provisions of the New York Not-for-Profit Corporation Law (the “N-PCL”), does hereby certify:

1. The name of the corporation is **[Entity Name, Inc.]** (the “Corporation”).
2. The Corporation is a corporation as defined in subparagraph (a)(5) of Section 102 of the N-PCL.<sup>2</sup>
3. The Corporation is a **[charitable/non-charitable]**<sup>3</sup> corporation pursuant to Section 201 of the N-PCL.
4. The Corporation is formed for the purposes of **[insert purpose(s)]**.<sup>4</sup> In furtherance of these purposes, the Corporation shall:<sup>5</sup>
  - a. **[insert activities]**; and
  - b. conduct any and all lawful activities which may be useful in accomplishing the foregoing purposes.
5. In furtherance of the foregoing purposes, the Corporation shall have all the general powers enumerated in Section 202 of the N-PCL and such other powers as are now or hereafter permitted by law for a corporation organized for the foregoing purposes, including, without limitation, the power to solicit grants and contributions for any corporate purpose and the power to maintain a fund or funds of real and/or personal property in furtherance of such purposes.
6. Notwithstanding any other provision of this Certificate of Incorporation, the Corporation is organized exclusively for **[charitable][insert other, if non-charitable]** purposes, and intends at all times to qualify and remain qualified as exempt from federal income tax under Section 501(c)(3) of the Internal Revenue Code of 1986, as it may be amended (the “Code”) and, in connection therewith:
  - a. **[if no consent or approval of any state official, department, board, agency or other body is required, use this statement:** the Corporation is not formed for any purpose or to engage in any activity requiring consent or approval of any state official, department, board, agency or other body (and no such consent or approval is required), including any of the activities mentioned in subparagraphs (a) - (v) of Section 404 of the N-PCL;]<sup>6</sup>  
**[or, if consent is required and, as a result, must be attached or endorsed thereon, use the following statement:** the Corporation is formed to engage in an activity or for a purpose requiring consent or approval of a state official, department, board, agency or other body, and such consent or approval is attached;]
  - b. the Corporation is not formed for and shall not be conducted nor operated for pecuniary profit or financial gain, and no part of its assets, income or profit shall be distributed to or inure to the benefit of any private individual or individuals, provided that nothing herein shall prevent the Corporation from paying reasonable compensation for services rendered or from making any other payments or distributions in furtherance of the purposes of the Corporation;

- c. no substantial part of the activities of the Corporation shall be devoted to the carrying on of propaganda or otherwise attempting to influence legislation, except to the extent permitted by the Code whether pursuant to an election under Section 501(h) of the Code or otherwise, and no part of the activities of the Corporation shall be devoted to participating or intervening in (including the publication or distribution of statements) any political campaign on behalf of or in opposition to any candidate for public office;
- d. the Corporation shall not engage in or include among its purposes any activities not permitted to be carried on (i) by a corporation exempt from federal income taxation under Section 501(c)(3) of the Code or the corresponding provisions of any subsequent federal tax laws or (ii) by a corporation to which contributions are deductible under Section 170(c)(2) of the Code (or the corresponding provisions of any subsequent federal tax laws); and
- e. in any taxable year in which the Corporation is a private foundation as described in Section 509(a) of the Code, the Corporation shall distribute its income for said period at such time and in such manner as not to subject it to tax under Section 4942 of the Code, and the Corporation shall not (i) engage in any act of self-dealing as defined in Section 4941(d) of the Code, (ii) retain any excess business holdings as defined in Section 4943(c) of the Code, (iii) make any investments in such manner as to subject the Corporation to tax under Section 4944 of the Code or (iv) make any taxable expenditures as defined in Section 4945(d) of the Code or the corresponding provisions of any subsequent federal tax laws.

7. The office of the Corporation shall be located in **[insert applicable New York County]** in the State of New York.

8. The names and addresses of the initial Directors,<sup>7</sup> each of whom is of full age,<sup>8</sup> are as follows:

Name	Address
[Name]	[Address]
[Name]	[Address]
[Name]	[Address]

9. The Secretary of State of the State of New York is hereby designated as agent of the Corporation upon whom process against the Corporation may be served. The post office address to which the Secretary shall mail a copy of any process against the Corporation served upon him or her is **[Address of the Corporation]**.<sup>9</sup>

10. In the event of dissolution, all the remaining assets and property of the Corporation shall, after payment of all necessary expenses thereof, be distributed to organizations that qualify under Section 501(c)(3) of the Code, or the corresponding provisions of any subsequent federal tax laws, or to the federal government or state or local governments for a public purpose, subject to any approvals required by applicable law.<sup>10</sup>

IN WITNESS WHEREOF this certificate has been signed this \_\_\_ day of \_\_\_\_\_, 202\_\_\_

\_\_\_\_\_  
[Name]  
[Address]

## Schedule A

The following not-for-profit corporate purposes require special consents which, generally, must be endorsed thereon or annexed to the Certificate of Incorporation (the “COI”) (*see* the individual provisions of N-PCL § 404 for specific requirements):

1. **Purpose:** Formation of a trade or business association

**Requires Consent From:** NY Attorney General’s Office (N-PCL § 404(a))

**Procedure:** Contact Office of the NY Attorney General, Antitrust Bureau, 28 Liberty Street, New York, NY 10005; tel: (212) 416-8262

2. **Purpose:** Care of destitute, delinquent, abandoned, neglected or dependent children (or the solicitation of contributions for any such purpose(s))

**Requires Consent From:** Commissioner of the Office of Children and Family Services (N-PCL § 404(b)(1))

**Procedure:**

- Send COI to: New York State Office of Children and Family Services, Capital View Office Park, Attention: Legal Department, 52 Washington Street, Rensselaer, New York, 12144; tel: (518) 473-7793
- After reviewing your COI the Office of Children and Family Services should contact you regarding the steps you should take going forward.

3. **Purpose:** Child Day Care Center (defined below)

- “Child Day Care Center”: any program or facility caring for children for more than three hours per day per child in which child day care is provided by a child day care provider except those programs operating as a group family day care home as such term is defined in § 390(d), a family day care home, as such term is defined in § 390(e), and a school-age child care program, as such term is defined in § 390(f) of the New York Social Services Law.
- “Child Day Care”: Care provided for a child on a regular basis, away from the child’s residence for less than twenty-four hours per day by someone other than the parent, step-parent, guardian or relative within the third degree of consanguinity of the parents or step-parents of such child. Child Day Care shall not refer to care provided in: (a) a day camp, as defined in the state sanitary code; (b) an after-school program operated for the purposes of religious education, sports or recreation; (c) a facility providing: (i) day services under an operating certificate issued by the department or (ii) providing day treatment under an operating certificate issued by the office of mental health or office for people with developmental disabilities or (d) a kindergarten, pre-kindergarten or nursery school for children three years of age or older, or after-school program for children operated by a public school district or by a private school or academy which is providing elementary or secondary education or both, in accordance with the compulsory education requirements of the education law, provided that the kindergarten, pre-kindergarten, nursery school or after school program is located on the premises or campus where the elementary or secondary education is provided (§ 390 of the New York Social Services Law).

**Requires Consent From:** Commissioner of the Office of Children and Family Services (N-PCL § 404(b)(2))

**Procedure:**

- *See #2 to this Schedule A;*
- Also, N-PCL § 404(b)(2) requires that a certified copy of the COI, each amendment thereto, and any certificate of merger, consolidation or dissolution involving such a corporation be provided to The Office of Children and Family Services within 30 days after receipt of confirmation of the filing of such certificate, amendment, merger, consolidation or dissolution with the Department of State. This also applies to any foreign corporation filing an application for authority under N-PCL § 1304 and any amendments thereto, and any surrender of authority or termination of authority in New York of such a corporation.

4. **Purpose:** Adult Care Facility (including the establishment or operation of any adult aged care accommodation; adult care facility; enriched housing programs; residences for adults or the solicitation of contributions for any such purpose)

**Requires Consent From:** Commissioner of Health (N-PCL § 404(b)(1))

**Procedure:** Contact the Department of Health, Division of Legal Affairs, Corning Tower, Rm 2482, Empire State Plaza, Albany, NY 12237; (518) 457-2411

5. **Purpose:** Establishment or operation of a residential program for Victims of Domestic Violence (defined below) or the placing out or boarding-out of children; or a home or shelter for unmarried mothers (or the solicitation of contributions for any such purpose) (does not include the establishment or maintenance of a hospital or facility providing Health Related Services (*see #20 of this Schedule A or Article 28 of the New York Public Health Law*) or facilities for which an operating certificate is required by Articles 16, 19, 22 and 31 of the Mental Hygiene Law)

- “Victims of Domestic Violence”: Any person over the age of sixteen, any married person or any parent accompanied by his or her minor child or children in situations in which such person or such person’s child is a victim of an act which would constitute a violation of the penal law, including, but not limited to acts constituting disorderly conduct, harassment, aggravated harassment, sexual misconduct, forcible touching, sexual abuse, stalking, criminal mischief, menacing, reckless endangerment, kidnapping, assault, attempted assault, attempted murder, criminal obstruction of breathing or blood circulation, strangulation, identity theft, grand larceny or coercion and: (a) such acts have resulted in actual physical or emotional injury or have created a substantial risk of physical or emotional harm to such person or such person’s child and (b) such act or acts are or are alleged to have been committed by a family or household member (§ 459-a of the New York Social Services Law).

**Requires Consent From:** Commissioner of the Office of Children and Family Services (N-PCL § 404(b)(1))

**Procedure:** *See #2 to this Schedule A*

6. **Purpose:** Hospital service, health service or a medical/dental expense indemnity plan (as permitted in Article 43 of the Insurance Law)

**Requires Consent From:** The Superintendent of Financial Services *and* the Commissioner of Health (N-PCL § 404(c))

**Procedure:** For the Commissioner of Health: *See* #20 this Schedule A. For information on the Superintendent of Financial Services: *See* <http://www.dfs.ny.gov/>.

7. **Purpose:** The operation of a school; college; university or other entity providing post-secondary education; a library; or a museum or historical society

**Requires Consent From:** The Commissioner of Education or, in the case of a college/university, the Regents of the University of the State of New York. (N-PCL § 404(d)). **Note:** Other corporations, the certificate of incorporation of which include purposes for which a corporation might be chartered by the Regents of the University of the State of New York, shall provide a certified copy of their charter to the Commissioner of Education within 30 business days after the corporation receives confirmation from the Department of State that the COI has been accepted for filing. N-PCL § 404(d).

**Procedure:** Prior to the filing of the COI with the Department of State:

- Submit two copies of the original, executed COI
- Include a completed consent form (available at: [www.counsel.nysed.gov](http://www.counsel.nysed.gov))
- Include personal check or money order in the amount of \$10 and a self-addressed, stamped return envelope
- Direct the application to:
  - A. NYS Education Department, Office of Counsel, State Education Building, 89 Washington Avenue, Room 148, Albany, NY 12234; tel: (518) 474-3852; or
  - B. New York State Education Department, 89 Washington Avenue, Board of Regents, Room 110 EB, Albany, New York 12234; e-mail: [RegentsOffice@nysed.gov](mailto:RegentsOffice@nysed.gov).
- For more information, *see*: <http://www.counsel.nysed.gov/consents>

8. **Purpose:** Cemetery corporation (but not Cemetery Corporations formed under N-PCL § 1503, see note below)

**Requires Consent From:** New York Cemetery Board (N-PCL § 404(e))

**Procedure:** Must complete the requisite form (on file at Weil) and return to: New York State Department – Division of Cemeteries, One Commerce Plaza, 99 Washington Ave, Albany, NY 12231-0001; (518) 474-6226

- Does not include a religious corporation, municipal corporation, cemetery corporation operated/supervised/controlled by a religious corporation, cemetery corporation belonging to/operated/supervised/controlled by a municipal corporation or religious corporation unless such corporation is for-profit (N-PCL § 1503).

9. **Purpose:** Fire corporation

**Requires Consent From:** The proper authority of each village, town, city or fire district in which the corporation proposes to act (N-PCL § 404(f))

**Procedure:** Such authorities shall be: in a city (the mayor); in a village (a majority of the trustees); in a town (a majority of the members of the town board); in a fire district (a majority of the fire commissioners). Refer to N-PCL § 404(f) for specific requirements regarding public hearings, notice, etc. to be provided, which will depend on the type of authority. Consent must be signed and acknowledged.

10. **Purpose:** Prevention of cruelty to animals

**Requires Consent From:** American Society for the Prevention of Cruelty to Animals (N-PCL § 404(g))

**Procedure:** If approval is not given by the society, within 30 days of application, a certified copy of an order of a justice of the supreme court of the judicial district in which the office of the corporation is to be located, dispensing with such approval, granted upon 8 days notice to such society, will suffice.

11. **Purpose:** Young Men’s Christian Association (“YMCA”)

**Requires Consent From:** The chairman of the national board of the YMCA (N-PCL § 404(h))

**Procedure:** Contact local YMCA

12. **Purpose:** Solicit funds for or otherwise benefit the armed forces (of U.S. or foreign country)

**Requires Consent From:** Adjutant general (N-PCL § 404(i))

13. **Purpose:** Organization of wage-earners for their mutual betterment, protection and advancement (e.g., the regulation of hours of labor, working conditions or wages; or the performance, rendition or sale of services as labor consultant, labor management advisor, negotiator, arbitrator or specialist); and includes every COI in which the name of the proposed corporation includes the words: “union,” “labor,” “council” or “industrial organization”

**Requires Consent From:** The Industrial Board of Appeals (N-PCL § 404(j))

**Procedure:**

- Send the COI and any Certificate of Reservation of the corporation’s name (and three copies of each) to the Industrial Board of Appeal’s Albany office (Averell Harriman State Office Campus, Building 12, Room 136, Albany NY 12240; (518) 474-4785) via first class mail; The board will make an inquiry into the purpose(s) of the proposed corporation as it shall deem advisable and shall order a hearing if necessary to determine whether or not such purposes are in all respect consistent with public policy and labor law. Notice of the time and place of hearing shall be given to the applicants and such others the board deems necessary parties.

14. **Purpose:** Savings bank life insurance

**Requires Consent From:** The Superintendent of Financial Services, to use any of the words/abbreviations in N-PCL § 301(a)(5), (N-PCL § 404(k)); for information on the Superintendent of Financial Services, see #6 above

15. **Purpose:** Association of insurance agents, brokers or underwriters

**Requires Consent From:** The Superintendent of Financial Services, to use any of the words/abbreviations in N-PCL § 301(a)(5), (N-PCL § 404(l)); for information on the Superintendent of Financial Services, see #6 above

16. **Purpose:** Foreign corporation which is an independent laboratory engaged in testing for public safety
- Requires Consent From:** The Superintendent of Financial Services to use any of the words/abbreviations in N-PCL § 301(a)(5) (N-PCL § 404(l)); for information on the Superintendent of Financial Services, see #6 above.
17. **Purpose:** Advancement of corporate, governmental and institutional risk and insurance management
- Requires Consent From:** The Superintendent of Financial Services to use any of the words/abbreviations in N-PCL § 301(a)(5), (N-PCL § 404(l)); for information on the Superintendent of Financial Services, see #6 above
18. **Purpose:** Corporation’s proposed name includes name of political party
- Requires Consent From:** The chairman of the county committee of such political party from the county in which the corporation is to be located, (except, such consent is withheld and the Supreme Court finds such withholding was unreasonable) (N-PCL § 404(m))
- Procedure:**
- For a Democratic chairman, please see: <http://www.nydemocrats.org/>
  - For a Republican chairman, please see: <http://www.nygop.org/>
19. **Purpose:** Corporation’s name includes “American Legion”
- Requires Consent From:** The Department of New York American Legion, duly acknowledged by its commander or adjutant (N-PCL § 404(n))
20. **Purpose:** Establishment or maintenance of any Hospital (defined below) (or the solicitation of contributions for any such purpose(s))
- Requires Consent From:** The Public Health Council (N-PCL § 404(o))
- “Hospital”: A facility or institution engaged principally in providing services by or under the supervision of a physician or, in the case of a dental clinic or dental dispensary, of a dentist, for the prevention, diagnosis or treatment of human disease, pain, injury, deformity or physical condition, including, but not limited to, a general hospital, public health center, diagnostic center, treatment center, dental clinic, dental dispensary, rehabilitation center other than a facility used solely for vocational rehabilitation, nursing home, tuberculosis hospital, chronic disease hospital, maternity hospital, lying-in-asylum, out-patient department, out-patient lodge, dispensary and a laboratory or central service facility serving one or more such institutions, but the term “Hospital” shall not include an institution, sanitarium or other facility engaged principally in providing services for the prevention, diagnosis or treatment of mental disability and which is subject to the powers of visitation, examination, inspection and investigation of the department of mental hygiene except for those distinct parts of such facility which provide hospital service, or a facility or to an institution engaged principally in providing services by or under the supervision of the bona fide members and adherents of a recognized religious organization whose teachings include reliance on spiritual means through prayer alone for healing in the practice of the religion of such organization and where services are provided in accordance with those teachings (New York Public Health Law § 2801)

**Procedure:**

- If solely raising funds: Send letter to the New York State Department of Health with a copy of the COI (it will, in turn, send a letter listing the requirements for the organization)
    - The initial letter should be sent to: The New York State Department of Health, Corning Tower, Rm 2482, Empire State Plaza, Albany, NY 12237; tel: (518) 473-3233
  - If operating a Hospital: Send a Certificate of Need Application to The New York State Department of Health (see above for the address)
    - The application is available at:  
<http://www.health.state.ny.us/nysdoh/cons/apps/gen1.pdf>
  - If New York Department of State Incorrectly Requires Public Health Council Approval
    - If an application for approval is returned by the New York Department of State ordering approval of the Public Health Council and it is believed this mandate was erroneous, contact the Bureau of Health Council and request a “No Approval Letter” which should be included with the re-filing of the COI
21. **Purpose:** Soliciting contributions for a Hospital or facility providing health related services
- Requires Consent From:** The Public Health Council (N-PCL § 404(o))
- Procedure:** See #20 of this Schedule A.
- For the definition of “Hospital”: See #20 of this Schedule A.
22. **Purpose:** Certificate of Incorporation of a Medical Corporation (defined below)
- Requires Consent From:** The Commissioner of Health *and* the Public Health Council (N-PCL § 404(p))
- Procedure:** See #20 of this Schedule A
- “Medical Corporation”: A corporation incorporated under § 4401 of the New York Public Health Law that provides a Comprehensive Health Services Plan
  - “Comprehensive Health Services Plan”: A plan through which each member of an enrolled population is entitled to receive Comprehensive Health Services in consideration for a basic advance or periodic charge (New York Public Health Law § 4401(2))
  - “Comprehensive Health Services”: All health services which an enrolled population might require in order to be maintained in good health, and shall include, but shall not be limited to, physician services (including consultant and referral services), in-patient and out-patient hospital services, diagnostic laboratory and therapeutic and diagnostic radiologic services, and emergency and preventive health services. Such term may be further defined by agreement with enrolled populations providing additional benefits necessary, desirable or appropriate to meet their health care needs (New York Public Health Law § 4401(3))
23. **Purpose:** Establishment/Operation of a Mental Health Facility
- Requires Consent From:** The Commissioner of Mental Health (N-PCL § 404(q))

24. **Purpose:** Operating a Health Maintenance Organization (defined below)

**Requires Consent From:** The Commissioner of Health (N-PCL § 404(r))

**Procedure:** *See #20 of this Schedule A*

- “Health Maintenance Organization”: Any person, natural or corporate, or any groups of such persons who enter into an arrangement, agreement or plan or any combination of arrangements or plans which propose to provide or offer, or which do provide or offer, a Comprehensive Health Services plan (*See #22 of this Schedule A for the definition*) (New York Public Health Law § 4401)

25. **Purpose:** Substance/alcohol abuse (if the corporation’s purposes include establishing or operating a substance, alcohol or chemical dependence or abuse program)

**Requires Consent From:** The Commissioner of the Office of Alcoholism and Substance Abuse Services (N-PCL § 404(u))

**Procedure:** Complete application to become a services provider; the application can be obtained at: <https://oasas.ny.gov/providers/program-certification>. Mail completed application and COI to: Bureau of Certification, Office of Alcoholism and Substance, Abuse Services, 1450 Western Avenue, Albany, NY 12203; tel: (518) 473-3460.

26. **Purpose:** Nonprofit property/casualty insurance program. (if the corporation intends to establish/maintain/operate a nonprofit property/casualty insurance Company pursuant to Article 67 of the New York Insurance Law)

**Requires Consent From:** The Superintendent of Financial Services (N-PCL § 404(v)); for information on the Superintendent of Financial Services, see #6 above

## Schedule B -- Procedure for Filing

**Name availability.** An applicant can search the availability of its proposed corporate name prior to submitting the Certificate of Incorporation by:

- Conducting a search of the Charities Bureau Registry Search at [http://www.charitiesnys.com/RegistrySearch/search\\_charities.jsp](http://www.charitiesnys.com/RegistrySearch/search_charities.jsp) (search for “Organization Names” that contain a particular word to see what names may be available)
- Conducting a search of the Corporation & Business Entity Database on the New York State Department of State website at [http://www.dos.ny.gov/corps/bus\\_entity\\_search.html](http://www.dos.ny.gov/corps/bus_entity_search.html) (search for Business Entity Names that contain a certain word or words)
- Writing to the Department of State, Division of Corporations, 41 State Street, Albany, NY 12231 to determine the availability of a corporate name (or names) and list the name (or names) to be searched in the request (Note: there is a \$5 fee for each corporate name to be searched for availability, which must be accompanied by the request)

**Name reservation.** Searching the availability of a corporate name does not reserve the name, but a corporate name can be reserved prior to filing the Certificate of Incorporation (*See* N-PCL § 303(a))

- File an “Application for Reservation of Name” with the New York State Department of State (filing fee is \$10). Expedited processing is available for additional fees.
  - Application reserves the name for 60 days, which may be extended twice for additional 60 day periods (fee for each extension is \$10; the name reservation filing receipt must accompany the extension request) (N-PCL § 303)
- The Application for Reservation of Name and the changes to the fees can be found at [www.dos.ny.gov](http://www.dos.ny.gov).
- The filing receipt issued by the Department of State for the Application must accompany the Certificate of Incorporation when presented to the Department of State for filing (N-PCL § 303(c))

**Filing completed Certificate of Incorporation.** The completed Certificate of Incorporation, the requisite consents/approvals (if any) and the Certificate of Reservation of the corporation’s name (if used) should be sent to the Division of Corporations, State Records and Uniform Commercial Code of the New York State Department of State in Albany along with the following:

- Cover letter stating: (i) the name of the corporation and (ii) to whom the receipt should be sent (delivery of the receipt completes the incorporation process (N-PCL § 104 and § 403))
- Fees
  - Filing cost of \$75 paid in cash, by check or money order payable to the Department of State, or by MasterCard, Visa or American Express (if paying by credit card, the applicant must then complete and sign the Credit Card/Debit Card Authorization Form available at <https://dos.ny.gov/form-corporation-or-business>)
  - \$10 fee for a certified copy of the Certificate of Incorporation, which the corporation will need for federal and other filings (it is *recommended* to order the certified copy when the corporation files)

- Fee for expedited handling (which is recommended because it can speed up the process from six weeks to ten days) which is \$150 for two (2) hour service, \$75 for same day service and \$25 for 24-hour service; note that “Expedited Handling” must be marked on the envelope or fax (For more information see <https://dos.ny.gov/fee-schedules>)

Note that Weil waives attorney fees for approved pro bono clients, but clients must be aware of their responsibility to pay for filing fees, expedited handling fees, IRS filing fees, Charities Bureau registration etc. Please discuss the details of fees with the Pro Bono Department.

ENDNOTES

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<sup>1</sup> Under N-PCL § 301(a)(1), the corporate name does not need to include “incorporated,” “corporation,” “limited,” etc. if organized for a charitable or religious purpose or for purposes for which the approval of the commissioner of social services or the public health and health planning council is required, or as a bar association; in our recent experience with New York State, however, corporations organized for a charitable purpose have nonetheless been required to include such words and their certificates of incorporation have been rejected if they omit such words. In general, the name chosen cannot be the same as or confusingly similar to another corporation’s name. Please see N-PCL § 301 for general guidelines on choosing a corporate name; and § 302 for limited exceptions.

<sup>2</sup> Pursuant to N-PCL § 102(a)(5)(2) no part of the assets, income or profit of the corporation may inure to the benefit of any of its members, directors or officers except to the extent permitted under the N-PCL.

<sup>3</sup> Under the N-PCL, there are two kinds of not-for-profit corporations. The classification is important because it dictates whether or not the organization may choose to *not* have members (*See* N-PCL §§ 601(a) and 201) and whether or not the organization may be eligible to qualify as a 501(c)(3) organization with the IRS.

1) **Charitable:** Formed or deemed to be formed for any purpose(s) that are charitable, educational, religious, scientific, literary, cultural or for the prevention of cruelty to children or animals. *See* N-PCL § 102(a)(3-a)-(3-b).

a) May qualify as a Section 501(c)(3) organization.

b) May have members, *see* N-PCL § 601(a).

2) **Non-charitable:** Any not-for-profit corporation other than a charitable corporation, including but not limited to one formed for any 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. *See* N-PCL § 102(a)(9-a).

a) Unlikely to qualify as a Section 501(c)(3) organization, but could potentially qualify for exemption under another tax-exempt category.

b) Must have members, *see* N-PCL § 601(a).

<sup>4</sup> Certain purposes of a not-for-profit corporation require special consents from state agencies. Examples include: certain educational corporations, child care centers, foster care agencies and drug treatment programs etc. *See* Schedule A and N-PCL § 404. This provision should be tailored to reflect the purposes for which the corporation is formed. Attorney and client should ensure that they work together to carefully craft the purposes clause. If drafted too narrowly, the provision may restrict what the corporation can do in the future. If drafted too broadly, it may jeopardize the corporation’s ability to obtain any necessary consents under N-PCL § 404 or place the organization in a situation where it has to obtain several approvals, which is administratively burdensome.

<sup>5</sup> This provision should describe activities that are envisioned to further the intended purpose of the corporation and should generally mirror the activities and purposes described in the organization’s application for tax exemption. Note that N-PCL § 402 allows, but does not require, the corporation to set forth any activities that it intends to carry out in furtherance of its purposes.

<sup>6</sup> *See* attached Schedule A.

<sup>7</sup> The board of directors of a not-for-profit corporation must have at least three (3) directors. *See* N-PCL § 702(a). The names and addresses of the initial directors are required to be set forth in the certificate of incorporation. *See* N-PCL § 402(a)(4).

<sup>8</sup> N-PCL § 701(a) requires that directors be at least 18 years of age, or if the corporation qualifies under the appropriate category set forth in N-PCL § 701 for youth based organizations, the corporation may have one or more directors between the ages of sixteen (16) and eighteen (18) so long as they don’t exceed half of the total number of directors required for a quorum. Any organization increasing the number of 16-18 year old directors to more than one must amend its certificate of incorporation.

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<sup>9</sup> The Secretary of State shall be the statutory agent for service of process for all not-for-profit corporations and must be so designated in the certificate of incorporation. *See* N-PCL § 304(a).

<sup>10</sup> The N-PCL provides that the approval of the Attorney General and/or the Supreme Court of the State of New York is required in connection with the dissolution of a not-for-profit corporation. In the case of a charitable corporation or a non-charitable corporation which, at the time of dissolution, holds assets legally required to be used for a particular purpose, the Attorney General's approval is required. *See* N-PCL § 1002(d)(1).

## Not-For-Profit Practice Group

### Sample Delaware Not-For-Profit Certificate of Incorporation

This sample certificate of incorporation may be used as a starting point for developing a certificate of incorporation for a not-for-profit organization incorporated in Delaware. If the organization has an existing certificate of incorporation, this sample may offer a useful comparison against provisions of the not-for-profit's existing certificate of incorporation and offer the opportunity to review whether such certificate of incorporation is in line with the organization's current operations and Delaware law.

This sample certificate of incorporation incorporates provisions required by the Delaware General Corporation Law (the "DGCL").

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## CERTIFICATE OF INCORPORATION OF [NAME OF NOT-FOR-PROFIT ORGANIZATION]

THE UNDERSIGNED, being a natural person, for the purpose of organizing a corporation under the General Corporation Law of the State of Delaware, hereby certifies that:

1. FIRST: The name of the corporation is: [name]<sup>1</sup> (the “Corporation”).
2. SECOND: The address of the registered office<sup>2</sup> of the Corporation in the State of Delaware is [1209 N. Orange Street, in the City of Wilmington, County of New Castle, 19801]. The name of the registered agent of the Corporation at such address is [The Corporation Trust Company].<sup>3</sup>
3. THIRD: The Corporation is organized exclusively for religious, charitable, scientific, testing for public safety, literary or educational purposes, or for the prevention of cruelty to children or animals, all within the meaning of section 501(c)(3)<sup>4</sup> of the Internal Revenue Code, as it may be amended (the “Code”).<sup>5</sup> In furtherance of these purposes, the Corporation may:<sup>6</sup>
  - a. receive, hold and administer funds, securities, gifts and bequests and use, disburse or donate the income or principal thereof for exempt purposes within the meaning of the section 501(c)(3) of the Code;
  - b. apply from time to time all or part of the funds of the Corporation for exempt purposes within the meaning of section 501(c)(3) of the Code by such means as may from time to time seem desirable to its directors, including research, publications, conferences and programs, and the establishment and maintenance of charitable activities or institutions;
  - c. [provide assistance in [●] efforts and conduct any other activities intended to ameliorate the harmful impacts of [●];
  - d. advance science and education on issues related to [●], such as their causes, effects and prevention efforts;
  - e. hold educational forums and develop partnerships, networks and coalitions among . . . ;
  - f. provide direct support services to . . . ;
  - g. heighten public awareness of . . . ;
  - h. encourage volunteerism to . . . ;
  - i. conduct fundraising to support the foregoing activities;]
  - j. conduct any and all lawful activities which may be useful in accomplishing the foregoing.
4. FOURTH: Notwithstanding any other provision in this certificate, the Corporation intends at all times to qualify and remain qualified as exempt from federal income tax under section 501(c)(3) of the Code and, in connection therewith:
  - a. Private Inurement Prohibited. The Corporation shall not be operated for pecuniary profit or financial gain, and no part of its assets, income or profit shall be distributed to or inure to the benefit of its members, directors, officers or other private individuals, except that the

Corporation may pay reasonable compensation for services rendered and make payments and distributions in furtherance of the purposes of the Corporation;

- b. Political Limitations. No substantial part of the activities of the Corporation shall be the carrying on of propaganda or otherwise attempting to influence legislation (except to the extent permitted by the Code whether pursuant to an election under section 501(h) of the Code or otherwise), and no part of the activities of the Corporation shall be participating or intervening in (including the publication or distribution of statements) any political campaign on behalf of or in opposition to any candidate for public office;
  - c. Exempt Activities. The Corporation shall not engage in or include among its purposes any activities not permitted to be carried on by a corporation exempt from federal income taxation under section 501(c)(3) of the Code, or by a corporation to which contributions are deductible under section 170(c)(2) of the Code;
  - d. Private Foundation Limitations. In any taxable year in which the Corporation is a private foundation as described in section 509(a) of the Code, the Corporation (1) shall distribute its income for said period at such time and in such manner as not to subject it to tax under section 4942 of the Code; (2) shall not engage in any act of self-dealing as defined in section 4941(d) of the Code; (3) shall not retain any excess business holdings as defined in section 4943(c) of the Code; (4) shall not make any investments in such manner as to subject the Corporation to tax under section 4944 of the Code; and (5) shall not make any taxable expenditures as defined in section 4945(d) of the Code; and
  - e. Dissolution. In the event of dissolution, after payment of all valid debts of the Corporation and necessary expenses thereof, all the remaining assets and property of the Corporation shall be distributed to organizations that qualify as exempt organizations under section 501(c)(3) of the Code, or to the federal government, or to state or local governments, for a public purpose; any such assets not so disposed of by a Court of Competent Jurisdiction of the county in which the principal office of the Corporation is then located, exclusively for such purposes or to such organization or organizations, as said Court shall determine, which are organized and operated exclusively for such purposes.
5. FIFTH: The name and mailing address of the incorporator are: [name], c/o Weil, Gotshal & Manges LLP, [address].<sup>7</sup>
  6. SIXTH: The Corporation shall be a membership corporation, is not organized for profit and shall not have the authority to issue capital stock.<sup>8</sup> The conditions of membership shall be determined in the manner set forth in the bylaws.<sup>9</sup>
  7. SEVENTH: In furtherance and not in limitation of the powers conferred by law, subject to any limitations contained elsewhere in this certificate of incorporation, the Board of Directors is authorized to make, repeal, alter, amend and rescind any or all of the bylaws of the Corporation.<sup>10</sup>
  8. EIGHTH The number of directors constituting the entire board shall be determined in the manner set forth in the bylaws.<sup>11</sup> Elections of directors need not be by written ballot.<sup>12</sup>
  9. NINTH: A director or officer of the Corporation shall not be personally liable<sup>13</sup> either to the Corporation or to any member or director for monetary damages for breach of fiduciary duty as a director or officer, except to the extent such exemption from liability or limitation thereof is not permitted under the General Corporation Law. Neither amendment nor repeal of this Article nor the adoption of any provision of the certificate of incorporation inconsistent with this Article shall eliminate or reduce the effect of this Article in respect of any matter occurring, or any cause of

action, suit or claim that, but for this Article, would accrue or arise, prior to such amendment, repeal or adoption of an inconsistent provision.

10. TENTH: The Corporation shall indemnify, advance expenses and hold harmless, to the fullest extent permitted by applicable law as it presently exists or may hereafter be amended, any person (“Covered Person”) who was or is a party or is threatened to be made a party to, or is otherwise involved in any threatened, pending or completed action, suit or proceeding, (“Proceeding”) whether civil, criminal, administrative or investigative in nature, by reason of the fact that such Covered Person (or his or her testator or intestate) is or was a director or officer of the Corporation, or is or was a director or officer of the Corporation who at the same time is or was also serving at the request of the Corporation as a director, officer, employee or agent of another corporation, partnership, joint venture, employee benefit plan, trust or other enterprise, against all liability and loss suffered and expenses (including attorneys’ fees) reasonably incurred by such person in connection with such Proceeding and any appeals, and the Corporation may adopt bylaws<sup>14</sup> or enter into agreements<sup>15</sup> with any such person for the purpose of providing for such indemnification. Notwithstanding the preceding sentence, except for claims for indemnification (following the final disposition of such Proceeding) or advancement of expenses, the Corporation shall be required to indemnify a Covered Person in connection with a Proceeding (or part thereof) commenced by such Covered Person only if the commencement of such Proceeding (or part thereof) by the Covered Person was authorized in the specific case by the Board of Directors of the Corporation. The payment of expenses incurred by a Covered Person in advance of the final disposition of the Proceeding shall be made only upon receipt of an undertaking by the Covered Person to repay all amounts advanced if it is ultimately determined that the Covered Person is not entitled to be indemnified under this Article or otherwise. Any amendment, repeal or modification of this Article shall not adversely affect any right or protection hereunder of any person in respect of any act or omission occurring prior to the time of such repeal or modification.

IN WITNESS WHEREOF, the undersigned has duly executed this certificate of incorporation on [date].

/s/ [name]<sup>16</sup>

Name: [name]

Title: Sole Incorporator

ENDNOTES

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<sup>1</sup> Must include “association,” “company,” “corporation,” “club,” “foundation,” “fund,” “incorporated,” “institute,” “society,” “union,” “syndicate,” or “limited” (or abbreviations thereof). DGCL § 102(a)(1). The Division of Corporations may waive the requirement that the name of the corporation contain one of the aforementioned terms, so long as the corporation files a certificate stating that its total assets are not less than \$10 million, or, in the sole discretion of the Division of Corporation in the Department of State, if the corporation is both a nonstock corporation and an association of professionals. *See* DGCL § 102(a)(1).

<sup>2</sup> Recent amendments to DGCL § 131 redefine “registered office” to mean the address of the corporation’s registered agent.

<sup>3</sup> Required by DGCL § 102(a)(2). Two commonly used registered agents are Corporation Trust Company (CT Corp) or CSC Global. You should confirm the proper name and address of your registered agent to include here.

<sup>4</sup> Revise as appropriate for Internal Revenue Code (the “Code”) § 501(c)(4) or (c)(6), etc. organizations in consultation with tax counsel.

<sup>5</sup> This broad description of nearly all the 501(c)(3) exempt purposes is permitted by Delaware, and will give the organization maximum flexibility to operate any exempt activities. More detailed purposes/mission/activities can (but need not) be listed below in the “In furtherance” section. Alternatively, this purpose clause may be limited to only specific exempt purposes or use another variation such as for grant-making organizations: “making of distributions to organizations that qualify as exempt organizations under section 501(c)(3) of the Code.” If the organization will have to register in another state, it may wish to exclude purposes which will require it to obtain additional approvals in that state.

<sup>6</sup> This sentence and the following clauses are not required by the DGCL or the Code but can be used to further specify the intended activities and purposes of the corporation, and should generally be consistent with the activities and purposes described in the organization’s application for tax exemption.

<sup>7</sup> This provision is required by DGCL § 102(a)(5). Typically an action of incorporator document will name the directors of the corporation. Alternatively, the powers of the incorporator may terminate on the filing of the certificate of incorporation (“COI”) in which case the COI must then also include the names and mailing addresses of the initial directors. *See* DGCL § 102(a)(6).

<sup>8</sup> “[T]he fact that [nonstock corporations] are not authorized to issue capital stock shall be stated in the certificate of incorporation.” DGCL § 102(a)(4).

<sup>9</sup> Nonstock corporations are required to have members. *See* DGCL § 102(a)(4). “The conditions of membership, or other criteria for identifying members, of nonstock corporations shall likewise be stated in the certificate of incorporation or the bylaws.” DGCL § 102(a)(4). Typically a nonstock corporation will state in its COI or bylaws the conditions of membership and any classes of rights, powers and duties of membership. Organizations that do not have a class of members distinct from the directors should include in their COI or bylaws a provision that the directors serve as members so long as they are directors: “The members of the corporation shall be the directors thereof. If at any time and for any reason any member shall cease to be a director, such person shall simultaneously cease to be a member.” Thus the directors, as members, elect the board of directors annually.

<sup>10</sup> The COI must grant the directors the power to adopt, amend or repeal bylaws. If this provision is not included, only the members hold these powers. *See* DGCL § 109(a).

<sup>11</sup> Typically initial directors are appointed by “action of incorporator,” although an alternative is to provide in the COI, before the reference to the bylaws, that: “The Corporation shall initially have [five] directors. The following persons shall serve as initial directors of the Corporation until the election of their successors:” and then list the individual initial directors with an address (typically the address of the organization, as this will be a public document).

<sup>12</sup> Directors must be elected by written ballot unless the above provision is included in the COI. *See* DGCL § 211(e).

<sup>13</sup> DGCL § 102(b)(7) provides that the COI may contain a provision eliminating or limiting the personal liability of a director or officer to the corporation or its stockholders/members for monetary damages for breach of fiduciary duty. However, the nonstock corporation cannot eliminate or limit the liability of a director or officer for: (i) breach of the duty of loyalty, (ii) acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law or (iii) improper personal

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benefits. In addition, the nonstock corporation cannot limit the liability of a director under DGCL § 174, or an officer for any action by or in the right of the corporation.

<sup>14</sup> Indemnity provisions may be included in the COI or in the bylaws or by separate indemnification agreement or some combination. Be sure there is no inconsistency.

<sup>15</sup> If directors have contractual indemnification rights from other sources, the priority of those rights should be clearly drafted.

<sup>16</sup> Delaware will accept a conformed typed signature (“/s/ Chris Smith”) and does not need an original signature although the original should be kept in the files.

## Not-For-Profit Practice Group

### Sample New York Not-For-Profit By-Laws

These sample by-laws may be used as a starting point for developing by-laws for a not-for-profit organization incorporated in New York. If the organization has existing by-laws, this sample may offer a useful comparison against provisions of the not-for-profit's existing by-laws and offer the opportunity to review whether such by-laws are in line with the organization's current operations and New York law.

These sample by-laws incorporate provisions required by the New York Not-for-Profit Corporation Law (the "N-PCL"), as amended by the Non-Profit Revitalization Act of 2013, as amended.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## By-laws<sup>1</sup>

### I. NAME, PURPOSES, OFFICE

#### 1.1 Name.

The name of the organization is [Entity Name, Inc.]<sup>2</sup> (the “Corporation”). The Corporation is a New York not-for-profit corporation.

#### 1.2 Purposes.

The purposes and powers of the Corporation shall be those set forth in the Corporation’s Certificate of Incorporation, as amended from time to time (the “Certificate of Incorporation”).

#### 1.3 Office.

The principal office of the Corporation shall be located at [Address of Corporation], in the county of [County], in the State of New York.<sup>3</sup> The Corporation may change the location of the principal office or maintain additional offices at such other places both within or without the State of New York as the Board of Directors of the Corporation (the “Board”) may from time to time determine or the business of the Corporation may require.

### II. MEMBERS

The Corporation shall have no members.<sup>4</sup>

### III. BOARD OF DIRECTORS<sup>5</sup>

#### 3.1 Powers and Number.

The Board shall have general power to control and manage the affairs and property of the Corporation subject to applicable law and in accordance with the purposes and limitations set forth in the Certificate of Incorporation and in these By-Laws (the “By-Laws”). The number of directors constituting the Board shall be [a fixed number of three (3) or more persons] [no fewer than three (3) and no more than [insert number] persons, as determined by the Board] (each a “Director” and, together, the “Directors”). Each Director shall have one (1) vote. The number of Directors may be increased or decreased, but no decrease shall shorten the term of any incumbent Director or decrease the number of Directors to fewer than three (3) Directors.<sup>6</sup> As to any matter upon which the Board may vote, the term “Entire Board” means [the total number of Directors that would be entitled to vote on such matter, assuming for this purpose that no vacancies on the Board existed at the time of such vote]<sup>7</sup> [the total number of Directors that would be entitled to vote on such matter 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), assuming for this purpose that no vacancies on the Board existed at the time of such vote]<sup>8,9</sup>

#### 3.2 Election and Term of Office.

The initial Directors shall be the persons named in the Certificate of Incorporation, and such Directors shall serve until the first annual meeting of the Board and until their successors have been elected or appointed and qualified, or until such Director’s death, resignation or removal. To become a Director, a person shall

be nominated by a Director and elected by a majority of the Board. A Director shall hold office for a [one]<sup>10</sup> year term and each shall continue in office for such term and until such Director's successor shall have been elected or appointed and qualified, or until such Director's death, resignation or removal;<sup>11</sup> provided, however, that any Director elected to fill an unexpired term (whether resulting from death, resignation or removal or created by an increase in the number of Directors) shall hold office until the end of the term which the Director was elected or appointed to fill, or for a term to be determined by the Board which ends at the next annual meeting at which the election of Directors is in the regular order of business and until his or her successor has been elected or appointed and qualified.<sup>12</sup> Directors may be elected to any number of consecutive terms [or may serve a maximum of \_\_ consecutive terms].<sup>13</sup>

### 3.3 Resignation.

Any Director may resign from office at any time by delivering a resignation in writing to [the President, Secretary, Executive Director, Chairperson etc.] of the Corporation.<sup>14</sup> Any such resignation shall take effect at the time specified therein, and unless required by its terms, the acceptance of such resignation shall not be necessary to make the resignation effective.

### 3.4 Vacancies and Newly Created Directorships.

Any newly created directorships and any vacancies on the Board, arising at any time, and from any cause, may be filled at any meeting of the Board by a majority vote of the Directors then in office, regardless of their number.<sup>15</sup> Directors so elected shall serve until the end of the term which the Director was elected or appointed to fill, or for a term to be determined by the Board which ends at an annual meeting and until his successor is elected or appointed and qualified.<sup>16</sup> [A vacancy in the Board shall be deemed to exist on the occurrence of any of the following: (a) the death, resignation or removal of any Director from office; (b) an increase in the authorized number of Directors by resolution of the Board; or (c) the failure of the Directors, at any annual or other meeting of Directors at which any one or more Directors are to be elected, to elect the full authorized number of Directors to be voted for at that meeting.]<sup>17</sup>

### 3.5 Removal.

Any Director may be removed for cause, at any time, by a vote of a majority of the Directors then in office, at a regular meeting or special meeting of the Board called for that purpose; provided that there is a quorum of not less than a majority present at such meeting.<sup>18</sup>

### 3.6 Chairperson.

The Chairperson of the Board shall preside at all meetings of the Board. The Chairperson shall perform such other duties and exercise such powers, as from time to time shall be prescribed by these By-Laws or by the Board. The Chairperson of the Board must not be an employee of the Corporation [unless the Board approves such employee serving in such capacity by a two-thirds vote of the Entire Board and contemporaneously documents in writing the basis for such approval; provided, however, that no such employee shall be considered an "independent director" for purposes of the New York Not-for-Profit Corporation Law (the "N-PCL")].<sup>19</sup>

### 3.7 No Compensation of Directors.

[Directors may serve the Corporation in any other capacity and receive reasonable compensation therefor.] Directors shall not be compensated for their services as Directors, except for payment or reimbursement of reasonable expenses incurred in connection with such services such as costs to attend Board or committee meetings.<sup>20</sup>

## **IV. MEETINGS OF DIRECTORS**

### **4.1 Annual, Regular and Special Meetings.**

Meetings of the Board (annual or regular) may be held on any day and place, and at such time and place, as the Board may from time to time fix. An annual meeting shall be held to elect Directors and at such time the Board shall receive an annual report as required by Section 519(c) of the N-PCL.<sup>21</sup> Special meetings of the Board shall be called at any time and may be held at any place by [insert appropriate title]<sup>22</sup>, or by any Director upon written (including by electronic mail) demand of not less than one-fifth of the Entire Board, and in each case at such time and at such place as shall be fixed by the person or persons calling the meeting.<sup>23</sup> Special meetings may also be called if there is a failure to elect a sufficient number of Directors to the Board.<sup>24</sup>

### **4.2 Notice of Meetings.**

Regular meetings may be held without notice of the date, time and place if such meetings are fixed by the Board. Written (including by electronic mail), oral or any other mode of notice of the date, time and place shall be given to the Board for the annual meeting, special meetings and each regular meeting not fixed by the Board, in sufficient time for the convenient assembly of the Directors, unless such notice has been waived and such notice is not otherwise required by law. Notice of any regular or special meeting need not specify the purpose of any such meeting, except as provided in Article XI of these By-Laws.<sup>25</sup> Any requirements of furnishing notice for a meeting shall be waived by any Director who submits a waiver of notice (which may be written or sent by electronic mail) before or after the meeting or who attends the meeting without protesting (either prior to the meeting or at its commencement) the lack of notice to such Director.<sup>26</sup>

### **4.3 Quorum and Action.**

Except as hereinafter provided, a majority of the Entire Board shall constitute a quorum for the transaction of business.<sup>27</sup> If at any meeting of the Board there shall be less than a quorum present, a majority of the Directors present may adjourn the meeting until such a quorum is obtained.<sup>28</sup> Except as otherwise provided by law or by these By-Laws, at any meeting of the Board at which a quorum is present, the vote of a majority of the Directors present at the time of the vote shall be the act of the Board.<sup>29</sup>

### **4.4 Meeting by Conference Telephone.**

Any one or more members of the Board or any committee thereof may participate in a meeting of the Board or such committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication allowing all persons participating in the meeting to speak to and hear each other at the same time. Participation by such means shall constitute presence in person at a meeting.<sup>30</sup>

### **4.5 Action Without a Meeting.**

Any action required or permitted to be taken by the Board or by any committee thereof may be taken without a meeting if all members of the Board or the committee, as the case may be, consent to the adoption of a resolution authorizing the action. Such consent may be written or sent by electronic mail.<sup>31</sup> The resolution and the written consents thereto by the Directors or committee members shall be filed with the minutes of the proceedings of the Board or the committee.

## V. COMMITTEES

### 5.1 Committees of the Board.

Subject to the following sentence, the Board may designate three<sup>32</sup> or more Directors to constitute one or more committees<sup>33</sup> to serve at the pleasure of the Board,<sup>34</sup> each of which, to the extent authorized by the Board, shall have the authority of the Board with the exception of any authority the delegation of which is prohibited by Section 712 of the N-PCL.<sup>35</sup> The Board, by a majority of the Entire Board (or, in the event the Board at any time consists of at least 30 Directors, by the approval of at least three-quarters of the Directors present at a meeting at which a quorum is present) may designate three or more Directors to constitute an Executive Committee (or similar committee however denominated) which, to the extent authorized by the Board, shall have the authority of the Board with the exception of any authority the delegation of which is prohibited by Section 712 of the N-PCL.

### 5.2 Committees of the Corporation.

Committees, other than committees of the Board, shall be committees of the Corporation. Members of such committees of the Corporation may be elected or appointed in the same manner as officers of the Corporation, but no such committee shall have the authority to bind the Board.<sup>36</sup>

### 5.3 Term and Duty.

Each member of a committee shall serve at the pleasure of the Board. The designation of any such committee and the delegation thereto of authority shall not alone relieve any Director of his or her duty to the Corporation under Section 717 of the N-PCL.<sup>37</sup>

### 5.4 Vacancies.

If any vacancy shall occur in a committee of the Board for any reason, including an increase in the number of members thereof, the vacancy may be filled at any meeting of the Board. If any vacancy shall occur in a committee of the Corporation, the vacancy may be filled in the same manner as officers of the Corporation.<sup>38</sup>

### 5.5 Meetings and Notice.

Each committee may hold meetings at such time or at such place as it shall determine from time to time. No notice shall be required for meetings for which the time and place have been fixed by the committee. Written, electronic, oral or any other mode of notice of the time and place shall be given for meetings of each committee that are not fixed in sufficient time for the convenient assembly of the committee, unless such notice has been waived. The notice of any meeting need not specify the purpose of the meeting. Any requirements of furnishing a notice shall be waived by any committee member who submits a waiver of notice (such waiver of notice may be written or electronic), whether submitted before, at commencement or after the meeting, or who attends the meeting without protesting, prior thereto or at its commencement the lack of notice to such committee member. Each committee shall keep a record of its proceedings.

### 5.6 Quorum and Vote.

At all meetings of a committee, the presence in person of members constituting a majority of the membership of such committee, [but in no event less than [Number of members],] shall be necessary and sufficient to constitute a quorum, and except as otherwise provided by law or by these By-Laws, the act of a majority of the members present at any meeting at which there is a quorum present, shall be the act of the committee.

## **VI. OFFICERS**

### **6.1 Officers, Election and Term of Office.**

The initial officers may include a [President] [a Secretary,] and [a Treasurer,] and thereafter the Board may elect or appoint an [Executive Director,][one or more Vice-Presidents] and such other officers and assistant officers as it may determine.<sup>39</sup> One person may hold more than one office in the Corporation except that no one person may hold the offices of both [President] and [Secretary].<sup>40</sup> The officers may, but need not, be members of the Board.<sup>41</sup> The officers shall be elected annually for a [one year] term and each shall continue in office until his or her successor shall have been elected or appointed and qualified, or until his or her death, resignation or removal.<sup>42</sup> The officers shall each have such powers and duties as are set forth herein and as generally pertain to their respective offices and such powers and duties as from time to time may be conferred upon them by the Board.<sup>43</sup>

### **6.2 Employees and Other Agents.**

The Board may from time to time appoint such employees and other agents as it shall deem necessary, each of whom shall hold office at the pleasure of the Board, and shall have such authority, perform such duties and receive such reasonable compensation, if any, as the Board may from time to time determine.

### **6.3 Removal, Resignations and Vacancies.**

Any officer of the Corporation, who was elected or appointed by the Board, may be removed with or without cause by a vote of the majority of the Directors present at a duly organized meeting of the Board.<sup>44</sup> Any officer may resign by giving [insert # of days] written notice to the Board. The resignation shall take effect at the time specified therein, and unless otherwise specified therein, the acceptance of such resignation shall not be necessary to make it effective. In case of any vacancy in any office, a successor to fill the unexpired portion of the term may be elected by the Board.

### **6.4 [President].<sup>45</sup>**

The [President] shall exercise general supervision over the affairs of the Corporation, subject, however, to the control of the Board. The [President] shall keep the Board fully informed about the affairs of the Corporation. The [President] shall perform all duties incident to the office of [President] and such other duties as from time to time may be assigned to him or her by the Board.<sup>46</sup>

### **6.5 [Vice President].<sup>47</sup>**

The most senior [Vice President], if any, shall, in the temporary absence or disability of the [President], act in the place of the [President], or, if there shall be no [Vice President], the [President]'s duties shall be performed by the individual Director designated by the Board, or by the [President]. Each [Vice President], if any, shall also perform such other duties as from time to time may be assigned to him by the Board or the [President], which duties may include powers elsewhere assigned or delegated to other officers.

### **6.6 [Secretary].<sup>48</sup>**

The [Secretary] shall keep the minute books and, if there be one, the seal of the Corporation, serve or cause to be served all notices of the Corporation including notices of meetings of the Board, record the minutes of all meetings of the Board and, in general perform, all duties incident to the office of [Secretary] and such other duties as from time to time may be assigned to him or her by the Board or the [President], which duties may include powers elsewhere assigned or delegated to other officers.

## **6.7 [Treasurer].<sup>49</sup>**

The [Treasurer] shall have responsibility for the custody of all funds, securities and property owned by the Corporation and shall keep full and accurate accounts of all receipts and disbursements of the Corporation. The [Treasurer] shall be responsible for the deposit of all moneys and other valuable effects in the name and to the credit of the Corporation in such depositories as may be designated by the Board. The [Treasurer] shall exhibit to any Director [or officer]<sup>50</sup> at all reasonable times the Corporation's books of account and records.<sup>51</sup> The [Treasurer] shall render a statement of the financial condition of the Corporation at the annual meeting of the Board. The [Treasurer] shall perform all duties incident to the office of [Treasurer] and such other duties as from time to time may be assigned to him or her by the Board or the [President], which duties may include powers elsewhere assigned or delegated to other officers.

## **6.8 Compensation.**

Any officer, employee or agent of the Corporation is authorized to receive a reasonable salary or other reasonable compensation for services rendered to the Corporation when authorized by a majority of the Entire Board.<sup>52</sup>

# **VII. BOOKS, RECORDS, CONTRACTS AND FINANCIAL AUTHORITY**

## **7.1 Books and Records.**

There shall be kept at the office of the Corporation correct and complete books and records of account of the activities and transactions of the Corporation, including a minute book, which shall contain a copy of the Certificate of Incorporation, a copy of these By-Laws and all minutes of meetings of the Board and its committees.<sup>53</sup>

## **7.2 Annual Report.**

There shall be presented to the Board, within six (6) months after the end of the Corporation's fiscal year, a report verified by the [President] and [Treasurer] or by a majority of the Directors, or certified by an independent public or certified public accountant or a firm of such accountants selected by the Board showing in appropriate detail, including as required by Section 519(c) of the N-PCL, the financial condition and results of operations of the Corporation for its preceding fiscal year. The annual report of the Board shall be filed with the records of the Corporation.<sup>54</sup>

## **7.3 Execution of Instruments.**

The Board is authorized to select the banks or depositories it deems proper for the funds of the Corporation. The Board shall determine who shall be authorized from time to time and in what manner on the Corporation's behalf to sign checks, drafts or other orders for the payment of money, acceptances, notes or other evidences of indebtedness, to enter into contracts or to execute and deliver other documents and instruments.<sup>55</sup>

# **VIII. INDEMNIFICATION**

## **8.1 Indemnification.**

The Corporation [shall][may]<sup>56</sup> indemnify any person made or threatened to be made a party to any threatened, pending or completed, action, suit or other proceeding, whether civil, criminal, administrative, or investigative, including an action by or in the right of the Corporation to procure a judgment in its favor, and whether or not the claim asserted against such person is based on matters which antedate the adoption

of or any amendment to this Article VIII, by reason of the fact that such person (or his or her testator or intestate) is or was a Director or officer of the Corporation, or is or was a Director or officer of the Corporation who at the same time is or was also serving another entity or an employee benefit plan in any capacity at the request of the Corporation, against judgments, fines, penalties, excise taxes, amounts paid in settlement and costs, charges and expenses reasonably incurred as a result of such action, suit or proceeding and any appeals (including reasonable attorneys' fees and disbursements) to the fullest extent that directors and officers are permitted to be indemnified by the laws of the State of New York in effect at the time such expenses, judgments, fines and amounts are paid, or at the time the acts or omissions complained of occurred, whichever gives the greater protection. Notwithstanding the foregoing, no indemnification may be made to or on behalf of any such person if in respect of the proceeding for which indemnification is sought a judgment or other final adjudication adverse to him or her establishes that (a) his or her acts were committed in bad faith or (b) his or her acts were the result of his or her active and deliberate dishonesty and were material to the cause of action so adjudicated or (c) they personally gained in fact a financial profit or other advantage to which they were not legally entitled.

## **8.2 Advancement of Expenses.**

The Corporation shall, to the fullest extent permitted by law, pay expenses incurred in defending any pending or threatened action, suit or other proceeding against a current or former Director or officer referred to in Section 8.01 of this Article VIII, including but not limited to reasonable attorneys' fees, in advance of the final disposition of such proceeding upon receipt of an undertaking by the person who may be entitled to such payment to repay such advances if, as and when it shall ultimately be determined by a court of competent jurisdiction that they are not entitled to be indemnified by the Corporation against such expenses.

## **8.3 Employees and Agents.**

The Corporation may also indemnify an employee or agent or any other person who is or was serving at the request of the Corporation in any capacity at another entity, partnership, trust, employee benefit plan or other enterprise on the same basis on which it shall indemnify a Director or officer under Section 8.01 of this Article VIII, such indemnification to be made in a particular instance as approved by the Board or provided by agreement approved by the Board. The Corporation may advance to an employee or agent (other than a Director or officer) expenses of a proceeding in respect of which it may provide indemnity on the same basis on which it shall advance expenses to a Director or officer under Section 8.02 of this Article VIII, such advancement to be made in a particular instance as approved by the Board or provided by an agreement approved by the Board.

## **8.4 Insurance.**

The Corporation shall have the power to purchase and maintain insurance (i) to indemnify itself for any obligation which it incurs as a result of its indemnification under the provisions of this Article VIII, or to indemnify any person in instances in which the person may be indemnified pursuant to the provisions of this Article VIII or, (ii) to the fullest extent such insurance is permitted by the laws of the State of New York, in instances in which the person may not otherwise be indemnified pursuant to the provisions of this Article VIII.<sup>57</sup>

## **IX. CORPORATE SEAL**

The Corporation need not have a corporate seal. If the Corporation desires to have a corporate seal, such seal shall be in such form as the Board shall prescribe.<sup>58</sup>

## **X. FISCAL YEAR**

The fiscal year of the Corporation shall be determined by the Board.

## **XI. AMENDMENTS**

Except as otherwise provided by law, these By-Laws may be altered, amended or repealed by the vote of a majority of the Directors present at any meeting of the Board.<sup>59</sup> Such action is authorized only (1) at a duly called and held meeting of the Board for which notice of such meeting, setting forth the proposed alteration, amendment or repeal, is given in accordance with the notice provisions for special meetings set forth herein, or (2) by action of the Board without a meeting.

## **XII. WHISTLEBLOWER POLICY**

The Corporation shall adopt a whistleblower policy in accordance with applicable law to provide procedures for the reporting of violations or suspected violations of laws or corporate policies, and protect from retaliation persons who report suspected improper conduct.<sup>60</sup>

## **XIII. CONFLICT OF INTEREST POLICY**

The Corporation shall adopt a conflict of interest policy in accordance with applicable law.<sup>61</sup>

## **XIV. PROHIBITION AGAINST LOANS AND DIVIDENDS**

The Corporation is prohibited from making any loan to any Director. The Corporation is also prohibited from declaring a dividend. This provision shall not, however, prohibit or restrict the transfer of funds upon dissolution of the Corporation in accordance with the provisions of the Certificate of Incorporation or the making of grants or donations to any person, including one (1) or more companies that at the time of grant or donation is tax exempt under Code Section 501(c)(3).

## **XV. REFERENCE TO CERTIFICATE OF INCORPORATION**

References in these By-Laws to the Certificate of Incorporation shall include all amendments thereto or changes thereof unless specifically excepted. In the event of a conflict between the Certificate of Incorporation and these By-Laws, the Certificate of Incorporation shall govern.

ENDNOTES

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<sup>1</sup> Under N-PCL § 602(f), “[t]he by-laws may contain any provision relating to the business of the corporation, the conduct of its affairs, its rights or powers or the rights or powers of its members, directors or officers, not inconsistent with [the N-PCL].”

<sup>2</sup> Under N-PCL § 301(a)(1), the corporate name does *not* need to include “incorporated,” “corporation,” “limited,” etc. if the not-for-profit corporation is organized (i) for a charitable or religious purpose or (ii) for purposes for which the approval of the commissioner of social services or the public health and health planning council is required, or (iii) as a bar association. However, in our recent experience with New York State, corporations organized for a charitable purpose have nonetheless been required to include such words, as their certificates of incorporation have been rejected if they omit such words. In general, the name chosen for the not-for-profit corporation cannot be the same as or confusingly similar to another corporation’s name. *See* N-PCL § 301 for general guidelines on choosing a corporate name and N-PCL § 302 for limited exceptions.

<sup>3</sup> N-PCL § 102(a)(11) defines “office of a corporation” as “the office the location of which is stated in the certificate of incorporation of a domestic corporation, or in the application for authority of a foreign corporation or an amendment thereof. Such office need not be a place where activities are conducted by such corporation.”

<sup>4</sup> Note that this is a sample of by-laws for a **non-membership** not-for-profit corporation. Pursuant to the N-PCL, “non-charitable” entities **shall** have members, while “charitable” entities **may or may not** have members. This Article II should be tailored to the organization’s characterization as either charitable or non-charitable. “Charitable” corporations are formed or deemed to be formed for any purpose(s) that are charitable, educational, religious, scientific, literary, cultural or for the prevention of cruelty to children or animals. *See* N-PCL § 102(a)(3-a), (a)(3-b). A “non-charitable” corporation includes any not-for-profit corporation 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. *See* N-PCL § 102(a)(9-a).

<sup>5</sup> Generally, under N-PCL § 701(a), the only qualification for directors is age. Directors must be at least eighteen (18) years of age or, if the corporation is organized primarily for the benefit of individuals below eighteen years of age and qualifies under the appropriate category set forth in N-PCL § 701(a), the corporation may have one or more directors between the ages of sixteen (16) and eighteen (18). Note that N-PCL § 704 authorizes the board, to provide in the certificate of incorporation or a by-law that directors can be divided into up to five classes to serve staggered terms with each class containing as nearly equal a number of directors as possible. Staggered terms are often recommended for not-for-profit corporations because they allow the board to maintain institutional knowledge. Remember to include a provision in the by-laws relating to classified boards, if staggered terms are desired. Furthermore, the N-PCL authorizes the by-laws or the certificate of incorporation to provide for class voting (N-PCL § 616) and/or cumulative voting (N-PCL § 617). This sample does not include provisions with respect to board classification, class voting or cumulative voting.

<sup>6</sup> *See* N-PCL § 702(a).

<sup>7</sup> Please use this formulation where the size of the Board consists of a fixed number of Directors.

<sup>8</sup> Please use this formulation where the size of the Board consists of a range of Directors.

<sup>9</sup> *See* N-PCL § 102(a)(6-a).

<sup>10</sup> N-PCL § 703(b) states that “[t]he term of office of directors...shall not exceed five years.” Also, note that under N-PCL § 703(b) if there is no language fixing the term of office for directors, the term shall be fixed at one (1) year. Furthermore, note that if the organization is to have a classified board as authorized under N-PCL § 704, “such term shall not exceed a number of years equal to the number of classes into which the board is classified.” *See* N-PCL §§ 703(b) and 704.

<sup>11</sup> *See* N-PCL § 703(c).

<sup>12</sup> *See* N-PCL § 705(c).

<sup>13</sup> *See* N-PCL § 703(b), which only limits the term of office to number less than five years but not the number of consecutive terms a director may serve; use the phrase in brackets if the organization desires to limit the number of consecutive terms a director may serve.

<sup>14</sup> Choose the appropriate person(s) to whom the resignation shall be delivered (e.g., the president and the secretary).

<sup>15</sup> Alternatively, some organizations like to use more specific language than “regardless of their number”, such as the following: “...may be filled at any meeting of the Board by the vote of the majority of the Directors then in office, although less than a quorum, or by a sole remaining Director.”

<sup>16</sup> See N-PCL § 705(c), which is qualified by the term limits outlined in N-PCL § 703(b).

<sup>17</sup> The bracketed language can be used, if the organization prefers more specific language than the phrase “any vacancies...” in the first sentence of this Section 3.04.

<sup>18</sup> See N-PCL § 706(a). In a non-membership organization, directors may not be removed without cause. See N-PCL § 706(b). Note that N-PCL § 706(b) allows *membership* organizations to remove any director *without* cause by vote of the members, if provided for in its by-laws or certificate of incorporation, and such vote of the members should comply with the quorum requirements of N-PCL § 608, the voting requirements of N-PCL § 613 and/or the unanimous consent provisions of N-PCL § 614. Also note that the removal of directors under N-PCL § 706(a) is qualified by § 706(c); review N-PCL § 706(c)(1) if the corporation will have cumulative voting; review N-PCL § 706(c)(2) for specific guidelines on removal pursuant to class voting. Furthermore, note that under N-PCL §§ 112(a)(4) and 706(d), the New York State Attorney General (or if the corporation is a membership organization - also by ten percent of members whether or not entitled to vote) may sue to remove directors for cause. The court may bar from reelection any director so removed for a period fixed by the court. See N-PCL § 706(d). Also, some organizations like to include the following language regarding notice of the action in the removal clause, to be inserted after the last sentence of this Section 3.05: “...; provided further that at least one week’s notice of the proposed action shall have been given to the Entire Board then in office.” Further, some organizations include the following sentence in its removal clause, to stress the importance of board meeting attendance on individual directors: “Missing **[insert appropriate number, often three]** consecutive meetings of the Board, unless a majority of Directors has excused such Director from attendance due to extreme circumstance(s), may constitute cause.”

<sup>19</sup> The N-PCL requires that no employee of the corporation shall serve as chairperson of the board or hold any other title with similar responsibilities, unless the board approves an employee serving as chairperson by a two-thirds vote of the entire board and contemporaneously documents in writing the basis for such approval; provided, that in no case shall such person be considered an “independent director.” See N-PCL § 713(f). Consider exclusion of the bracketed language as a best practice for other purposes in the N-PCL.

<sup>20</sup> See N-PCL § 715(d). While it is not typical that directors are compensated for their services as a director of a not-for-profit organization, if appropriate, consider language such as: “Compensation of Directors. Directors may authorize by resolution the payment to a Director of reasonable compensation for services as a Director. The Corporation may pay or reimburse reasonable expenses incurred by Directors in connection with their Director services, such as costs to attend Board or committee meetings.”

<sup>21</sup> See N-PCL § 519. The annual report of directors must be verified (*see* N-PCL § 519(a) for specific verification requirements), detail the assets, liabilities, principal changes in assets and liabilities, revenue, expenses and number of members (if applicable). See N-PCL § 519(a)(1)-(5). Additionally, the report must be filed with the corporation’s records and either a copy or an abstract thereof entered into the meeting minutes. See N-PCL § 519(b).

<sup>22</sup> The organization may choose who should call board meetings, options include: “Secretary upon the request of the President or of any Director”; “upon the request of the President or any two Directors”; or “by the Chairperson of the Board, the Executive Director or any Director upon written demand of not less than three Directors.” See N-PCL § 710(c), which provides that special meetings of the board may be called by the president or other corporate officer as provided by the by-laws or as determined by the board.

<sup>23</sup> See N-PCL § 710(c).

<sup>24</sup> N-PCL § 710(c): “A special meeting may be called at any time by the president or other corporate officer as provided in the by-laws or as determined by the board; and, in the case of a corporation without members, by any director upon written demand of not less than one-fifth of the entire board.”

<sup>25</sup> Alternatively, some organizations prefer that notice for special and regular meetings be accompanied by an agenda outlining the purpose of the meeting (as the organization must provide for in the annual meeting notice, under the N-PCL) by including language such as the following: “notice shall, in the case of each annual [, special and regular] meeting, be accompanied by a written agenda setting forth all matters upon which action is proposed to be taken.” See N-PCL § 711(b).

<sup>26</sup> See N-PCL § 711(c). Note that if written, the waiver must be executed by the director signing such waiver or causing his or her signature to be affixed to such waiver by any reasonable means including but not limited to facsimile signature. If electronic, the transmission of the waiver must be sent by electronic mail and set forth, or be submitted with, information from which it can reasonably be determined that the transmission was authorized by the director.

<sup>27</sup> N-PCL §§ 707 and 709 provide statutory requirements with respect to quorum requirements and allow, with certain limitations, lesser or greater quorum requirements. Although quorum in this sample is set at the majority of the entire board, this provision can be tailored to the organization's needs; for example, quorum can be fixed at less than a majority of the entire board. See N-PCL § 707. However, N-PCL § 707 also requires that a quorum cannot be less than (i) for a board of fifteen (15) members or less, 1/3 of the entire board and (ii) for a board of more than fifteen (15) members, five (5) members plus one (1) additional member for every ten (10) members (or fraction thereof) in excess of fifteen (i.e., quorum is seven (7) for a board of thirty (30) members). In addition, under N-PCL § 709, there is no ceiling on the number of directors needed to constitute a quorum or for voting, but if an organization wishes to add a supermajority quorum requirement, it must be adopted by two-thirds of the entire board in a non-membership corporation and by two-thirds of the voting members in a membership corporation.

<sup>28</sup> See N-PCL § 711(d).

<sup>29</sup> See N-PCL § 708(d). Directors who are present at the meeting but not present at the time of the vote due to a conflict of interest or related party transaction shall be determined to be present at the time of the vote for the purposes of determining if a quorum is present at such time.

<sup>30</sup> Directors and committee members are authorized by law to participate in meetings via communications equipment unless otherwise restricted by the by-laws or certificate of incorporation. Participation by such means shall constitute presence in person at a meeting as long as all persons participating in the meeting can hear each other at the same time and each director can participate in all matters before the board, including, without limitation, the ability to propose, object to, and vote upon a specific action to be taken by the board or committee. See N-PCL § 708(c).

<sup>31</sup> See N-PCL § 708(b). Note that if written, the consent must be executed by the director by signing such consent or causing his or her signature to be affixed to such consent by any reasonable means including, but not limited to, facsimile signature. Additionally, if electronic, the transmission of the consent must be sent by electronic mail or other electronic means and set forth, or be submitted with, information from which it can reasonably be determined that the transmission was authorized by the director. "Unless otherwise restricted by the certificate of incorporation or the by-laws, any action required or permitted to be taken by the board or any committee thereof may be taken without a meeting if all members of the board or the committee consent to the adoption of a resolution authorizing the action. Such consent may be written or electronic. If written, the consent must be executed by the directors by signing such consent or causing their signatures to be affixed to such consent by any reasonable means including, but not limited to, facsimile signature. If electronic, the transmission of the consent must be sent by electronic mail or other electronic means and set forth, or be submitted with, information from which it can reasonably be determined that the transmission was authorized by the director. The resolution and the written consents thereto by the members of the board or committee shall be filed with the minutes of the proceedings of the board or committee."

<sup>32</sup> N-PCL § 712(a) requires authorization in the by-laws, certificate of incorporation or resolutions of the board and election by (i) in the case of most committees, a majority of the board and (ii) in the case of an executive committee or similar committee, a majority of the entire board (or approval of three-quarters of the directors at a meeting at which a quorum is present in the case of a corporation with a board of 30 or more directors), in order to create a committee. In addition, N-PCL § 712(a) specifies that such committees shall each consist of three or more directors. Authority delegated to such committees can be set forth in the by-laws, certificate of incorporation or resolutions of the board. See N-PCL § 712(a).

<sup>33</sup> Examples of committees include audit, compensation, governance, nominating, executive, development, and finance committees. The advantage to having an executive committee and other committees is that they can meet more regularly than the full board or with more ease on an emergency basis. See N-PCL § 712-a regarding audit committee requirements.

<sup>34</sup> See N-PCL § 712(d).

<sup>35</sup> N-PCL § 712(a) prohibits delegating to any committee authority over the following matters: (1) submission to members of any action requiring members' approval, (2) filling of vacancies in the board of directors or any committee, (3) fixing of directors' compensation for serving on the board or any committee, (4) amendment or repeal of the by-laws or adoption of new by-laws, (5) amendment or repeal of any board resolution, which by its terms is not amendable or repealable, (6) the election or removal of officers and directors, (7) the approval of a merger or plan of dissolution, (8) the adoption of a resolution

recommending to the members action on the sale, lease, exchange or other disposition of all or substantially all the assets of a corporation or, if there are no members entitled to vote, the authorization of such transaction, or (9) the approval of amendments to the certificate of incorporation.

<sup>36</sup> See N-PCL § 712(e). Members of such committees of the corporation, who may be non-directors, shall be elected or appointed as set forth in the by-laws, or if unstated, then in the same manner as officers of the corporation. If the organization does not wish for members of committees of the corporation such members to be appointed in the same manner as officers of the corporation, then the organization should outline how such members are elected or appointed in the by-laws.

<sup>37</sup> See N-PCL § 712(d).

<sup>38</sup> See N-PCL § 712(e).

<sup>39</sup> N-PCL § 713(a) specifies that these offices may be designated by such alternative titles as may be provided in the certificate of incorporation or the by-laws. Remember to properly define the title the organization chooses to use since the designation will be used throughout the by-laws.

<sup>40</sup> Although the N-PCL authorizes one person to hold more than one office at a time (excluding holding the offices of president and secretary simultaneously, which is not permitted by N-PCL § 713(a)), some organizations include language that restricts such person(s) from signing instruments in more than one capacity. The following language is a model of such a restriction: “No instrument that is required to be signed by more than one officer may be signed by one person acting in more than one capacity.”

<sup>41</sup> Some organizations require that officers, such as the president, be members of the board. If so, the following phrase can be inserted into the by-laws or certificate of incorporation: “The [President / *other officers*] shall be [an ex-officio member][ex-officio members] of the Board [with][without] voting rights.” See N-PCL § 713(d). N-PCL § 712(a) expressly permits the by-laws to require that directors who hold certain positions in the corporation be ex-officio members of specific committees of the board.

<sup>42</sup> See N-PCL § 713(c). Unless otherwise provided in the by-laws or certificate of incorporation, all officers are elected or appointed annually.

<sup>43</sup> See N-PCL § 713(e).

<sup>44</sup> Some organizations require that a majority of the entire board must remove an officer. See N-PCL § 714 for the different rules for removing officers elected by members in membership corporations. See N-PCL § 714(c) for a discussion of actions brought by the Attorney General, members or any director to procure a judgment to remove an officer for cause.

<sup>45</sup> See note 35, discussing matters that may not be delegated to a committee.

<sup>46</sup> Some organizations include language that grants the president (or the corresponding title) the authority, alone, to sign contracts authorized by the board. The following is a sample provision: “The President has the power to sign and execute alone in the name of the Corporation all contracts authorized either generally or specifically by the Board, unless the Board shall specifically require an additional signature.”

<sup>47</sup> See note 35, discussing matters that may not be delegated to a committee.

<sup>48</sup> See note 35, discussing matters that may not be delegated to a committee.

<sup>49</sup> See note 35, discussing matters that may not be delegated to a committee.

<sup>50</sup> Some organizations choose to allow their officers the right to see the corporation’s books.

<sup>51</sup> Some organizations choose to add the following language: “...upon application during business hours at the office of the Corporation where such books are kept.”

<sup>52</sup> See N-PCL § 715(d), (e). If not set in the by-laws, an affirmative vote of a majority of the entire board is required to fix the compensation of officers.

<sup>53</sup> See N-PCL § 621(a). Note that the books, minutes and records may be kept in written form or in any other form capable of being converted into written form within a reasonable time.

<sup>54</sup> See N-PCL § 519.

<sup>55</sup> Some organizations prefer to have an additional provision on investments in the financial section of the by-laws. The following is a sample provision: “Investments: The funds of the Corporation may be retained in whole or in part in cash or be invested and reinvested from time to time in such property, real, personal or otherwise, including stocks, bonds, or other securities, as the Board may deem desirable.”

<sup>56</sup> Pursuant to N-PCL § 722(a), a not-for-profit organization may provide indemnification if the “director or officer acted, in good faith, for a purpose which he reasonably believed to be in...the best interests of the corporation and, in criminal actions or proceedings, in addition, had no reasonable cause to believe that his conduct was unlawful.” Such indemnification may cover reimbursement for judgments, fines, amounts paid in settlement and reasonable expenses, including attorneys’ fees actually and necessarily incurred as a result of an action or proceeding brought against such individual in his or her capacity as a director or officer of the corporation. Pursuant to N-PCL § 721, a not-for-profit corporation is permitted to provide indemnification rights and requirements beyond those mandated by the statute, by providing so in the certificate of incorporation or in the by-laws. However, N-PCL § 721 prohibits indemnification if (i) “a judgment or other final adjudication adverse to the director or officer establishes that his acts were committed in bad faith or were the result of active and deliberate dishonesty and were material to the cause of action so adjudicated” or (ii) “that he personally gained in fact a financial profit or other advantage to which he was not legally entitled.” Pursuant to N-PCL § 723(a), any director or officer shall be entitled to indemnification of actual and necessary costs outlined in N-PCL § 722 if the person is successful, on the merits or otherwise, in defense of the civil or criminal action or proceeding of the character described in N-PCL § 722(a). An organization may choose to make indemnification mandatory to the extent permitted by the N-PCL (as described above) by deleting “[may]” and the brackets around the word “shall.”

<sup>57</sup> See N-PCL § 726(a).

<sup>58</sup> If the corporation desires to include a provision on a corporate seal the following is an example: “The corporate seal shall have inscribed thereon the name of the Corporation, the year of its organization and the words ‘Corporate Seal, Not-for-Profit, New York’. The seal may be used by causing it or a facsimile thereof to be impressed or affixed or in any manner reproduced.”

<sup>59</sup> See N-PCL § 707 for the number of directors required for a quorum. Note that in the case of a corporation with no members pursuant to N-PCL § 709(c), any amendment to the by-laws (i) which adds a provision as to greater requirement as to quorum and vote of directors, pursuant to N-PCL § 709(a), or (ii) which changes or strikes out such a provision, shall be authorized by two-thirds of the entire board (or such greater proportion as shall have been specifically provided for in the by-laws).

<sup>60</sup> See N-PCL § 715-b for whistleblower policy requirements, which apply to not-for-profit corporations which have or are anticipated to have twenty (20) or more employees and had in the prior fiscal year annual revenue in excess of \$1,000,000.

<sup>61</sup> See N-PCL § 715-a for conflict of interest policy requirements; see N-PCL § 715 for requirements relating to related party transactions.

## Not-For-Profit Practice Group

### Sample Delaware Not-For-Profit Bylaws

These sample bylaws may be used as a starting point for developing bylaws for a not-for-profit organization incorporated in Delaware. If the organization has existing bylaws, this form may offer a useful comparison against provisions of the not-for-profit's existing bylaws and offer the opportunity to review whether such bylaws are in line with the organization's current operations and Delaware law. These sample bylaws incorporate provisions required by the Delaware General Corporation Law (the "DGCL").

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Bylaws

### I. MEMBERS

#### 1.1 Classification of Membership.<sup>1</sup>

[●] (the “Corporation”) shall have one class of membership.<sup>2</sup> The members of the Corporation shall be the directors thereof. If at any time and for any reason any member shall cease to be a director, such person shall simultaneously cease to be a member.<sup>3</sup>

#### 1.2 Annual Meetings.

The annual meeting of members for the election of directors and for the transaction of such other business as may properly come before the meeting shall be held each year at such time and place as the Board of Directors of the Corporation (the “Board”) shall determine.<sup>4</sup>

#### 1.3 Special Meetings.

Special meetings of the members for the transaction of such business as may properly come before the meeting may be called by order of the Board, the Chair of the Board (“Chair”), the [Executive Director]/[CEO]/[President], the Secretary or by a majority of the members, and shall be held at such time and place as may be specified by such order.<sup>5</sup>

#### 1.4 Notice of Meetings or Waiver of Notice.

Written notice of all meetings of the members, stating the place, date and hour of the meeting, the means of remote communications, if any, by which members and proxy holders may be deemed to be present in person and vote at such meeting shall be delivered in any manner permitted by the Delaware General Corporation Law (“DGCL”) to each member not less than 10 nor more than 60 days prior to the meeting, unless the prescribed period for notice shall have been waived. Notice of any special meeting shall state in general terms the purpose or purposes for which the meeting is to be held.<sup>6</sup> Notice need not be given to any member who submits a written waiver of notice signed by him or her, whether before or after the time stated therein. Attendance of a member at a meeting shall constitute a waiver of notice of such meeting, except when the member attends the meeting for the express purpose of objecting, at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened.<sup>7</sup> Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the members need be specified in any written waiver of notice.

#### 1.5 Quorum.

Except as otherwise provided by law, these bylaws or the Corporation’s certificate of incorporation, a quorum for the transaction of business at any meeting of members shall consist of a majority of the members entitled to vote at the meeting, present in person or by proxy. If there is no such quorum, the members entitled to vote at the meeting, present in person or by proxy, may adjourn the meeting from time to time, without further notice, until a quorum shall have been obtained. When a quorum is once present it is not broken by the subsequent withdrawal from the meeting of any member.<sup>8</sup>

## 1.6 Meeting Organization and Voting.

- a. Meetings of members shall be presided over by the Chair, if any, or if none or in the Chair's absence, by a presiding person to be chosen by the members entitled to vote who are present in person or by proxy at the meeting. The Secretary of the Corporation, or in the Secretary's absence an Assistant Secretary, shall act as secretary of every meeting, but if neither the Secretary nor an Assistant Secretary is present, the presiding officer of the meeting shall appoint any person present to act as secretary of the meeting.
- b. At all elections of directors, the voting may but need not be by ballot, and directors shall be elected by a [majority]<sup>9</sup> of the votes of the members present in person or represented by proxy at the meeting and entitled to vote on the election of directors. Except as otherwise required by law, these bylaws or the certificate of incorporation, any other action shall be authorized by the vote of the majority of the members present in person or represented by proxy at the meeting and entitled to vote on the subject matter.

## 1.7 Member Action Without Meetings.<sup>10</sup>

Any action required or permitted to be taken at any meeting of members may, except as otherwise required by law or the certificate of incorporation, be taken without a meeting, without prior notice and without a vote, if a consent in writing, setting forth the action so taken, is signed by the members having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting at which all members entitled to vote thereon were present and voted, and the writing or writings are filed with the permanent records of the Corporation. Any member executing such consent may provide, whether through instructions to an agent or otherwise, that such a consent will be effective at a future time, no later than 60 days after such consent was delivered to the Corporation. Such consent is revocable prior to its becoming effective. Prompt notice of the taking of corporate action without a meeting by less than unanimous written consent shall be given to those members who have not consented in writing.

## II. BOARD OF DIRECTORS

### 2.1 General Powers.<sup>11</sup>

The business, property and affairs of the Corporation shall be managed by, or under the direction of, the Board. The Board may delegate the management of the day-to-day operations of the Corporation to the officers or other persons provided that the business and affairs of the Corporation shall be managed by, and all corporate powers shall be exercised under, the ultimate direction of the Board.

### 2.2 Composition, Qualifications and Chair of the Board.

- a. The number of directors constituting the entire Board shall be [three (3)], or such larger number as may be fixed from time to time by action of the members or the Board.<sup>12</sup> The use of the phrase "entire Board" herein refers to the total number of directors which the Corporation would have if there were no vacancies.
- b. Directors who are elected at an annual meeting of members, and directors who are elected in the interim to fill vacancies and newly created directorships, shall hold office until the next annual meeting of members and until their successors are elected and qualified or until their earlier resignation or removal.
- c. The Board may elect a Chair and a Vice-Chair of the Board ("Vice-Chair") as officers of the [Board/Corporation]. [The Chair and Vice-Chair are not officers of the

Board/Corporation.]<sup>13</sup> The Chair shall preside at all meetings of the Board and shall have such other powers and duties as may from time to time be assigned by the Board. In the absence or disability of the Chair, the Vice-Chair shall exercise the powers and perform the duties of the Chair until a replacement chair is elected or the disability of the Chair is removed.

### **2.3 Places of Meetings.**

Meetings of the Board may be held at any place as may from time to time be fixed by the Chair or by resolution of the Board, or as may be specified in the notice of meeting.

### **2.4 Annual Meeting.**

As soon as practicable following the annual meeting of members, the newly elected Board shall meet for the purpose of the election of officers and the transaction of such other business as may properly come before the meeting.

### **2.5 Regular Meetings.**

Regular meetings of the Board shall be held at such times and places as the Board shall from time to time by resolution determine.

### **2.6 Special Meetings.**

Special meetings of the Board shall be held whenever called by the Chair or by a majority of the directors then in office.

### **2.7 Notice of Meetings or Waiver of Notice.**

A notice of the place, date, time and purpose or purposes of each meeting of the Board shall be given to each director by mail or electronic transmission at least 2 days before the special meeting, or by telephoning or emailing the same or by delivering the same personally not later than the day before the day of the meeting. Notice need not be given of regular meetings of the Board held at times and places fixed by resolution of the Board. Directors may waive notice of any meeting in writing, and the attendance of any director at a meeting shall constitute a waiver of notice of such meeting except when a director attends a meeting for the express purpose of objecting, at the beginning of such meeting, to the transaction of any business because the meeting is not lawfully called or convened.<sup>14</sup>

### **2.8 Quorum and Manner of Acting.**

[A majority]/[One-third]<sup>15</sup> of the directors then in office shall constitute a quorum. A majority of the directors present, whether or not a quorum is present, may adjourn a meeting from time to time to another time and place without notice. The affirmative vote of a majority of the directors present at a meeting at which a quorum is present shall be the act of the Board,<sup>16</sup> except as otherwise provided by law or in these bylaws.

### **2.9 Meeting Organization.**

At all meetings of the Board, the Chair or Vice-Chair, if any, or if none or in the Chair's or Vice-Chair's absence or inability to act the [Executive Director]/[CEO]/[President], if the [Executive Director]/[CEO]/[President] is a member of the Board, or in the [Executive Director]/[CEO]/[President]'s absence or inability to act any Vice-President who is a member of the Board, or in such Vice-President's absence or inability to act a presiding person chosen by the directors, shall preside. The Secretary of the

Corporation shall act as secretary at all meetings of the Board when present, and, in the Secretary's absence, the presiding person may appoint any person to act as secretary of the meeting.

## **2.10 Action by Written Consent.**

Any action required or permitted to be taken at any meeting of the Board may be taken without a meeting if all the directors consent thereto in writing or by electronic transmission, and the writing or writings or electronic transmissions are filed with the minutes of proceedings of the Board.<sup>17</sup>

## **2.11 Meeting By Telephone or Similar Communications Equipment.**

The members of the Board, or any committee thereof, may participate in any meeting by means of conference telephone or other communications equipment by means of which all meeting participants can hear and be heard by all other participants, and participation in such meeting shall constitute the presence in person by such member at such meeting.<sup>18</sup>

## **2.12 Resignation and Removal.**

Any director may resign at any time upon written notice to the Corporation and such resignation shall take effect upon receipt thereof by the Chair, [Executive Director]/[CEO]/[President] or Secretary, unless otherwise specified in the resignation. Any or all of the directors may be removed, with or without cause, by a majority of the members entitled to vote for the election of directors.<sup>19</sup>

## **2.13 Vacancies.**

Vacancies on the Board, whether caused by resignation, death, disqualification, removal, an increase in the authorized number of directors or otherwise, may be filled by the affirmative vote of a majority of the remaining directors,<sup>20</sup> although less than a quorum, or by a sole remaining director, or by action of the members entitled to vote for the election of directors.

## **2.14 [No Compensation of Directors.**

Directors shall not be compensated for their services as directors, except for payment or reimbursement of reasonable expenses incurred in connection with such services such as costs to attend Board or committee meetings.]<sup>21</sup> Directors may serve the Corporation in any other capacity and receive reasonable compensation therefor.

# **III. COMMITTEES**

## **3.1 Board Committees.**

The Board may, by a resolution adopted by a majority of the directors then in office, designate Board Committees each consisting of one or more directors, and only directors, to serve at the pleasure of the Board.<sup>22</sup> Appointments to any Board Committee shall be by a majority vote of the directors then in office. The Board may designate one or more directors as alternate members of any Board Committee, who may replace any absent or disqualified member at any meeting. Board Committees shall have and may exercise all the powers and authority of the Board in the management of the business and affairs of the Corporation to the extent provided in the resolution of the Board or in the bylaws; but no Board Committee shall have the power or authority in reference to: amending the certificate of incorporation or bylaws, adopting an agreement of merger or consolidation, recommending to the members the sale, lease or exchange of all or substantially all of the Corporation's assets, recommending to the members a dissolution of the Corporation or a revocation of a dissolution, or any other actions which require the approval of the entire Board under

applicable law.<sup>23</sup> Each Board Committee shall keep minutes of its proceedings, and actions taken by a Board Committee shall be reported to the Board.

### **3.2 Advisory Committees.**

The Board may establish one or more Advisory Committees to the Board. Advisory Committees may consist of directors or non-directors and may be appointed as the Board determines. Advisory Committees may not exercise the authority of the Board to make decisions on behalf of the Corporation, but shall be restricted to making recommendations to the Board or Board Committees, and implementing Board or Board Committee decisions and policies under the supervision and control of the Board or Board Committee.

### **3.3 Procedures, Quorum and Manner of Acting.**

Each Board Committee shall fix its own rules of procedure, and shall meet where and as provided by such rules or by resolution of the Board. Except as otherwise provided by law, the presence of a majority of the then appointed members of a Board Committee shall constitute a quorum for the transaction of business by that Board Committee, and in every case where a quorum is present the affirmative vote of a majority of the members of the Board Committee present shall be the act of the Board Committee. In the absence or disqualification of a member of a Board Committee, the member or members present at any meeting and not disqualified from voting, whether or not the member or members constitute a quorum, may unanimously appoint another director to act at the meeting in the place of such absent or disqualified member.

### **3.4 Action by Written Consent.**

Any action required or permitted to be taken at any meeting of any Board Committee may be taken without a meeting if all the members of the Board Committee consent thereto in writing or electronic transmission, and the writing or writings or electronic transmissions are filed with the minutes of proceedings of the Board Committee.<sup>24</sup>

### **3.5 Term and Termination.**

In the event any person shall cease to be a director of the Corporation, such person shall simultaneously therewith cease to be a member of any Board Committee.

## **IV. OFFICERS<sup>25</sup>**

### **4.1 Election and Qualifications.**

The Board shall elect the officers of the Corporation, which shall include a [Chair]<sup>26</sup>, [Vice-Chair], [a/an] [Executive Director]/[CEO]/[President],<sup>27</sup> a [Treasurer] and a [Secretary]. The officers may include, by election or appointment, one or more Vice-Presidents (any one or more of whom may be given an additional designation of rank or function), and such assistant secretaries, such assistant treasurers and such other officers as the Board may from time to time deem proper. Each officer shall have such powers and duties as may be prescribed by these bylaws and as may be assigned by the Board or the [Executive Director]/[CEO]/[President]. Any two or more offices may be held by the same person.

### **4.2 Election and Term.**

All officers shall be elected by the Board and shall serve one year and thereafter until such time as their respective successors are elected and qualified or until their earlier resignation or removal. Any vacancy in any office may be filled for the unexpired portion of the term by the Board.

### **4.3 Resignation and Removal.**

Any officer may resign at any time upon written notice to the Corporation and such resignation shall take effect upon receipt thereof by the [Executive Director]/[CEO]/[President] or Secretary, unless otherwise specified in the resignation. Any officer may be removed from office, with or without cause, at any time by [the Board]/[a vote of a majority of the entire Board.]

### **4.4 The [Executive Director]/[CEO]/[President].**

The [Executive Director]/[CEO]/[President] shall be the chief executive officer of the Corporation, and shall have such duties as customarily pertain to that office. The [Executive Director]/[CEO]/[President] shall have general management and supervision of the property, business and affairs of the Corporation and over its other officers; [may appoint and remove assistant officers and other agents and employees, [other than officers referred to in this Article IV]]; and may execute and deliver in the name of the Corporation contracts and other obligations and instruments.

### **4.5 Vice-President.**

A Vice-President may execute and deliver in the name of the Corporation contracts and other obligations and instruments pertaining to the regular course of the duties of said office, and shall have such other authority as from time to time may be assigned by the Board of Directors or the [Executive Director]/[CEO]/[President].

### **4.6 Treasurer.**

The Treasurer shall in general have all duties incident to the position of Treasurer including custody of all funds and securities of the Corporation, shall be responsible for the receipt and disbursement of all monies of the Corporation, and shall perform such other duties as may be assigned by the Board. The Treasurer shall keep proper books of accounts of such receipts and disbursements and shall prepare financial statements consistent with generally accepted accounting principles in such forms and at such times as may be required by the Board.

### **4.7 Secretary.**

The Secretary shall in general have all duties incident to the position of Secretary including custody of the books, records and documents (other than those maintained by the Treasurer) of the Corporation, shall attest deeds, contracts, leases and other legal instruments and formal documents and shall perform such other duties as may be assigned by the Board or the [Executive Director]/[CEO]/[President].

### **4.8 Assistant Officers.**

Any assistant officer shall have such powers and duties of the officer such assistant officer assists as such officer or the Board shall from time to time prescribe.

### **4.9 Other Officers.**

Other officers may be elected by resolution of the Board and shall have such powers and duties as may be prescribed in such resolution.

### **4.10 Compensation of Officers.**

The [entire Board (other than recused directors)]<sup>28</sup> shall evaluate the performance of the [Executive Director]/[CEO]/[President] annually and determine reasonable compensation, if any, for his or her

services. Any such compensation shall be fixed by a resolution considered at a meeting of the Board in advance of any increase in compensation. [The Board, a committee thereof, or the [Executive Director]/[CEO]/[President]] shall evaluate the performance of all other officers annually and determine reasonable compensation, if any, for their services. All compensation determinations and procedures shall be consistent with applicable law governing tax exempt organizations, these bylaws, and applicable corporate policies, including any conflict of interest policy.

## **V. BOOKS, RECORDS AND REPORTS [AND AUDITS]**

### **5.1 Books and Records.**

The Corporation shall keep correct and complete books and records of account and shall keep minutes of the proceedings of its members, its Board and the Board Committees.

### **5.2 Reports.<sup>29</sup>**

The Corporation shall comply with all Delaware and U.S. federal tax reporting requirements, including filing a Form 990 with the Internal Revenue Service. The Corporation shall publish an annual report. Such report shall include a comprehensive and detailed statement of the Corporation's operations, activities, financial condition and accomplishments for the preceding fiscal year.

### **5.3 [Audits.**

The accounts of the Corporation shall be audited annually, in accordance with generally accepted auditing standards, by independent certified public accountants or independent licensed public accountants certified or licensed by a regulatory authority of a state or other political subdivision of the United States.]

## **VI. MISCELLANEOUS PROVISIONS**

### **6.1 [Conflicts of Interest.**

The Corporation shall adopt a conflict of interest policy.]<sup>30</sup>

### **6.2 Fiscal Year.**

The fiscal year of the Corporation shall be fixed, and shall be subject to change, by the Board.

### **6.3 Indemnification.**

The Corporation shall indemnify, advance expenses to and hold harmless, to the fullest extent permitted by applicable law as it presently exists or may hereafter be amended, any person as provided in the Corporation's certificate of incorporation, and may indemnify, advance expenses to and hold harmless any other person in accordance with applicable law.<sup>31</sup>

### **6.4 Amendments to Bylaws.**

These bylaws may be amended or repealed, and new bylaws may be adopted by the members or by a majority of the directors then in office.<sup>32</sup>

ENDNOTES

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<sup>1</sup> Delaware nonstock corporations must have members in lieu of stockholders. *See* DGCL § 102(a)(4). Typically a nonstock corporation will state in its certificate of incorporation (“COI”) or its bylaws (latter is more flexible) the conditions of membership and any classes of rights, powers and duties of membership. *See* DGCL § 102(a)(4). If a COI or bylaws provide that a Delaware nonstock corporation does not have any members, such a provision is inconsistent with the DGCL although the DGCL provides that “failure to have members shall not affect otherwise valid corporate acts or work a forfeiture or dissolution of the corporation.” DGCL § 102(a)(4).

<sup>2</sup> Delaware nonstock corporations may have multiple classes of members with relative rights, powers and duties. The corporation may also make provisions for future creation of additional classes. *See* DGCL § 102(a)(4).

<sup>3</sup> Organizations that do not have a class of members distinct from the directors should include in their COI or bylaws a provision that the directors serve as members so long as they are directors. Thus the directors, as members, elect the board of directors annually. Unless otherwise provided in the COI or bylaws, each member shall be entitled to one vote on each matter submitted to a vote before the board, however, the COI or the bylaws may specify that only a certain class of members has voting powers. *See* DGCL § 215(b).

<sup>4</sup> DGCL § 211(b) requires an annual meeting of members to elect directors. Under DGCL § 211(b), directors may be elected by written consent in lieu of the annual meeting, however, if such consent is less than unanimous, such action by written consent will only be valid if all of the directorships which are being voted on are vacant at the time of the less than unanimous vote.

<sup>5</sup> The COI or bylaws may also authorize other officers or other persons to call special meetings of the members. *See* DGCL § 211(d).

<sup>6</sup> This provision is permissible pursuant to DGCL § 222(a).

<sup>7</sup> This provision is permissible pursuant to DGCL § 229.

<sup>8</sup> These bylaws define a quorum as a majority of the members entitled to vote. The default for a quorum of members in a Delaware nonstock corporation is one-third of the members entitled to vote at the meeting (DGCL § 215(c)(1)); however, if a separate vote by a class or group or classes or groups is required, a majority of the members of such class or group or classes or groups, present in person or represented by proxy will constitute a quorum entitled to take action with respect to the vote on that matter (DGCL § 215(c)(4)). An increase or decrease in quorum may be made in either the COI or the bylaws. *See* DGCL § 215(c).

<sup>9</sup> Although the default under Delaware law is that members of the governing body shall be elected by a plurality of the votes of the members of the corporation present in person or represented by proxy at the meeting and entitled to vote thereon, unless otherwise specified in the COI or bylaws (DGCL § 215(c) and (c)(3)), it is generally considered governance best practice to have a majority-based voting standard.

<sup>10</sup> This provision is permissible pursuant to DGCL § 228(b).

<sup>11</sup> This provision is permissible pursuant to DGCL § 141(a).

<sup>12</sup> DGCL § 141(b) provides that the board shall consist of one or more members, however, it is generally considered governance best practice to have three or more members.

<sup>13</sup> For non-executive Chairs, use this provision here and provide that the Chair is not an officer of the Board. For executive Chairs, move this provision to the officer section and provide that the Chair is an officer of the Corporation.

<sup>14</sup> This provision is permissible pursuant to DGCL § 229.

<sup>15</sup> DGCL § 141(j) permits nonstock corporations to have a director quorum lower than the 1/3 minimum under DGCL § 141(b). A majority quorum requirement, however, is more common. Large boards that have difficulty meeting quorum can: meet less often and delegate frequently occurring business to an executive committee, or move some directors off the board (e.g., to an advisory board).

<sup>16</sup> DGCL § 141(b) provides that the vote of the majority of the directors present at a meeting at which a quorum is present shall be the act of the board unless the COI or bylaws require a vote of a greater number.

<sup>17</sup> DGCL § 141(f) provides that unless otherwise restricted by the certificate of incorporation or bylaws, any action required or permitted to be taken at any board or board committee meeting may be taken without a meeting if all members of the board or board committee as applicable consent thereto in writing or by electronic transmission.

<sup>18</sup> This provision is permissible pursuant to DGCL § 141(i).

<sup>19</sup> This provision is permissible pursuant to DGCL § 141(k).

<sup>20</sup> Unless otherwise provided in the COI or bylaws, vacancies may be filled by a majority of the directors then in office, although less than a quorum, or by a sole remaining director. *See* DGCL § 223(a)(1).

<sup>21</sup> While it is not typical that directors are compensated for their director services of a nonprofit, if appropriate, consider language such as: “Compensation of Directors. Directors may authorize by resolution the payment to a director of reasonable compensation for services as a director. The Corporation may pay or reimburse reasonable expenses incurred by directors in connection with their director services such as costs to attend Board or committee meetings.”

<sup>22</sup> Note the distinction between board committees and advisory committees, and the requirement that board committees must be made up of directors, and that advisory committees (because they may include non-directors) may only make recommendations to the board rather than take action on behalf of the board. *See generally*, DGCL § 141(c)(2).

<sup>23</sup> The DGCL allows board committees to have the full power of the board except for the above listed actions. *See* DGCL § 141(c)(2).

<sup>24</sup> DGCL § 141(f) provides that unless otherwise restricted by the certificate of incorporation or bylaws, any action required or permitted to be taken at any board or board committee meeting may be taken without a meeting if all members of the board or board committee as applicable consent thereto in writing or by electronic transmission.

<sup>25</sup> DGCL § 142 generally authorizes the board to appoint officers. Different corporations have different titles for officers. This article should be revised to conform with the proper titles and duties of officers. This article sets forth a typical description of the officers’ powers and duties. Instead of describing the roles of the officers, the bylaws may provide that the board will establish the roles of the officers at a later time. For example, “The powers and duties of the officers of the Corporation shall be as provided from time to time by resolution of the Board. In the absence of such resolution, the respective officers shall have the powers and shall discharge the duties customarily and usually held and performed by like officers of corporations similar in organization and business purposes to the Corporation subject to the control of the Board.” Typically, a corporation will have at least a President and Treasurer.

<sup>26</sup> *See* note 13. Chair is not a required officer position but could be an officer if desired. If there is a non-executive Chair, then Chair should not be listed here.

<sup>27</sup> Make consistent throughout the bylaws and other documents.

<sup>28</sup> There is no requirement under DGCL relating to compensation of officers, but consider whether to reserve this for the full board or delegate to the compensation committee. *See* sample compensation committee charter for additional considerations.

<sup>29</sup> This provision is permissible pursuant to DGCL § 502.

<sup>30</sup> The board of a not-for-profit organization should (even if not required to) adopt a conflict of interest policy to assist the directors, officers and others in the organization in identifying, evaluating and resolving conflicts of interest. While not required by federal law or the DGCL, the organization, its directors and officers may be subject to liability, and the organization’s tax-exempt status may be at risk, if the organization enters into transactions that result in improper financial benefit to persons affiliated with the organization.

<sup>31</sup> If not provided in the COI, then provide in the bylaws. *See* sample Delaware not-for-profit COI for indemnification provisions.

<sup>32</sup> The power of the board to amend the bylaws must first be granted in the COI. The organization’s members also have the power to adopt, amend or repeal bylaws. *See* DGCL § 109.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Board Guidelines

The board of a not-for-profit organization may find it useful to set forth governance guidelines it applies in fulfilling its responsibilities, including board leadership, structures, composition, functions and processes, and the organization's expectations of directors. Board guidelines are very specific to the needs and circumstances of the individual not-for-profit organization – one size does not fit all. Governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

The following sample board guidelines are intended to comport with generally accepted practices for not-for-profit organizations. This sample provides only one example for a non-member organization, incorporating elements required by the New York Not-for-Profit Corporation Law (the "N-PCL") including the requirements of the Non-Profit Revitalization Act of 2013, as amended, applicable to New York not-for-profits, as well as elements related to certain disclosure requirements under Internal Revenue Service ("IRS") rules. The guidelines are intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample guidelines should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; they are not intended to establish, by their own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Board Guidelines

#### I. DUTIES AND RESPONSIBILITIES OF THE BOARD

The role of the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) is to manage and direct the affairs of the Organization, and set expectations about the tone and ethical culture of the Organization. In fulfilling their roles on the Board, directors are expected to apply their business judgment and act with due care, in good faith and in accordance with the best interests and purpose of the Organization.

The Board delegates the day-to-day management of the Organization to the [Chief Executive Officer/Executive Director/President] and other senior management of the Organization, and provides guidance to and oversight of management.

The Board fulfills its role (directly or by delegating certain responsibilities to its committees) by:

1. Identifying, reviewing and updating as necessary, the mission and purposes of the Organization in accordance with applicable law;
2. Setting the values and expectations about the ethical culture of the Organization – the “tone at the top” – and reviewing management efforts to instill an appropriate tone and culture throughout the Organization;
3. Providing advice, counsel and support to the [Chief Executive Officer/Executive Director/President] and other senior management;
4. Selecting, regularly evaluating, fixing the compensation of, and, where appropriate, replacing the [Chief Executive Officer/Executive Director/President];
5. Establishing measures of organizational performance and utilizing those measures to ensure senior management accountability;
6. Planning for senior management succession and guiding and overseeing management development;
7. Providing oversight of the Organization’s performance to evaluate whether the business is being appropriately managed in accordance with the Organization’s mission;
8. Reviewing and approving strategic plans and providing guidance to management in formulating the Organization’s strategy;
9. Reviewing and approving the Organization’s annual budget, financial objectives, fundraising plans and major corporate and development activities (including material capital expenditures and transactions outside the ordinary course of business);
10. Reviewing significant changes in the Organization’s auditing and accounting principles and practices;
11. Providing oversight of internal and external audit processes, financial reporting, recordkeeping and disclosure controls and procedures;

12. Reviewing the Organization’s Form 990 prior to filing with the Internal Revenue Service;<sup>1</sup>
13. Providing oversight of risk assessment, management and monitoring processes;
14. Ensuring that compliance systems and processes designed to promote legal and ethical compliance are reasonably effective, and overseeing the Organization’s compliance with relevant laws and regulations;
15. Designing governance structures and practices to position the Board to fulfill its duties effectively and efficiently, and making changes as needed; and
16. Performing such other functions as the Board believes appropriate or necessary, or as otherwise prescribed by law or regulation.

## II. DIRECTOR QUALIFICATION STANDARDS

### Selection of Board Members

[The Board is responsible for selecting the members of the Board.] [The Board has delegated the vetting process to the Nominating and Governance Committee.] The [Board][Nominating and Governance Committee] will review and recommend to the Board, [annually/periodically] the appropriate experience, qualifications, attributes and skills required of directors in the context of the Organization’s current circumstances and the Board’s needs.

The Board expects that all directors will, at a minimum:

1. Have experience or knowledge with respect to at least one area of the Organization’s operations or area of board responsibility, such as [strategic planning, financial management, technology, fundraising and development, public relations or human resources]; and
2. Be committed to the Organization’s mission and programs.

### Director Independence<sup>2</sup>

Directors should be “independent-minded” and be able to exercise objective judgment. The Board should ensure that only “independent” directors are appointed to the Audit Committee, [Compensation Committee and Nominating and Governance Committee, as these committees are responsible for making decisions with respect to issues where management may have a potential conflict].<sup>3</sup>

In determining whether or not a director is “independent,” the Board should consider all relevant facts and circumstances that could affect a director’s ability to exercise objective judgment, including materiality of relationships (business, familial and social) each director may have with the Organization, management, beneficiaries, donors, clients, suppliers and other important constituents. In addition, a director may only be considered “independent” if:<sup>4</sup>

*[For a New York not-for-profit:*

1. The director was not an employee or a key person of the Organization or a related organization or affiliate of the Organization during the past three years;
2. The director does not have a relative who is, or has been within the last three years, a key person of the Organization or an affiliate of the Organization;

3. The director did not receive and does not have a relative who received total direct compensation exceeding \$10,000 in any of the past three tax years from the Organization or related organizations or affiliates of the Organization other than any reasonable compensation for service as a director;
4. The director is not a current employee of and does not have a substantial financial interest in, and does not have a relative who is an officer of or has a substantial financial interest in, any entity that has provided payments, property or services to, or received payments, property or services from, the Organization or an affiliate thereof (not including charitable contributions, dues or fees paid to the Organization for services which the Organization performs as part of its nonprofit purposes, or payments made by the Organization at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the Organization are available to individual members of the public on the same terms, and such services received by the Organization are not available from another source) for property or services in an amount that, in any of the last three fiscal years, has exceeded (a) the lesser of \$10,000 or 2% of such other entity's consolidated gross revenue if such other entity's consolidated gross revenue was less than \$500,000, (b) \$25,000 if such other entity's consolidated gross revenue was \$500,000 or more but less than \$10 million and (c) \$100,000 if such other entity's consolidated gross revenue was \$10 million or more;
5. The director is not, and does not have a relative who is, a current owner (whether whole or partial), director, officer or employee of the Organization's outside auditor, or who has worked on the Organization's audit at any time during the last three years; and
6. Neither the director, nor any relative of the director, was involved in a loan, grant, excess benefit transaction, or a business transaction involving an interested person that is reportable on Schedule L of Form 990, with the Organization (whether directly or indirectly through affiliation with another organization) during the most recent tax year.]

*[For other not-for-profits required to file Form 990:*

1. The director was not compensated as an officer or other employee of the Organization or a related organization during the most recent tax year;
2. The director did not receive total compensation exceeding \$10,000 in the most recent tax year from the Organization or related organizations for services provided in the director's capacity as an advisor, consultant or independent contractor other than any reasonable compensation for service as a director;
3. The director is not, and does not have a relative who is, a current owner (whether whole or partial), director, officer or employee of the Organization's outside auditor, or who has worked on the Organization's audit at any time during the last three years; and
4. Neither the director, nor any relative of the director, was involved in a loan, grant, excess benefit transaction, or a business transaction involving an interested person that is reportable on Schedule L of Form 990, with the Organization (whether directly or indirectly through affiliation with another organization) during the most recent tax year.]

For purposes of these Guidelines:

- An "affiliate" is any entity controlled by, or in control of, the Organization;<sup>5</sup>
- A "key person" is any person, other than a director or officer, whether or not an employee of the Organization who (i) has responsibilities, or exercises powers or influence over the Organization as a whole similar to the responsibilities, powers or influence of directors and

officers; (ii) manages the Organization, or a segment of the Organization that represents a substantial portion of the activities, assets, income or expenses of the Organization; or (iii) alone or with others controls or determines a substantial portion of the Organization's capital expenditures or operating budget;<sup>6</sup>

- A "related organization" includes an organization that controls the Organization, an organization controlled by Organization, and an organization controlled by the same person or persons that control the Organization;<sup>7</sup> and
- A "relative" of a director is that person's (i) spouse or domestic partner; (ii) ancestors, brothers and sisters (whether whole or half-blood), children (whether natural or adopted), grandchildren, great-grandchildren; or (iii) spouse or domestic partner of that person's brothers, sisters, children, grandchildren and great-grandchildren.<sup>8</sup>

### III. BOARD LEADERSHIP

The Board is led by a [non-employee]<sup>9</sup> chair, who is responsible for:

1. Convening and chairing meetings of the Board;
2. Organizing the Board's agenda with input from management and helping to identify the Board's information needs;
3. Leading Board discussions of management performance and compensation in executive sessions; and
4. Encouraging frank but collegial discussions both at the Board level and as between the Board and management.

### IV. DUE CARE AND LOYALTY

Directors are expected to exercise appropriate diligence in providing oversight, and are expected to:

1. Attend and participate actively at all Board and committee meetings;
2. Review meeting materials and agendas in advance;
3. Request other information from management and trustworthy and reliable experts where appropriate before making decisions or taking actions;
4. Be sensitive to indications of potential problems or concerns and make further inquiry until reasonably satisfied that management is dealing with those concerns appropriately;
5. Act with integrity and adhere to all applicable laws, regulations and organizational policies;
6. Keep confidential all non-public information that relates to the Organization's business, unless disclosure and/or use of such information is otherwise authorized; and
7. Advise the Chair of the Nominating and Governance Committee upon a change in the director's professional responsibilities (such as resignation or change of employment) and prior to accepting an invitation to serve on another board of directors.

## V. OTHER EXPECTATIONS

In addition to fulfilling the duties outlined above, the Board is expected to:<sup>10</sup>

1. Meet at least [three] times per year;
2. Meet periodically without members of management present; and
3. Maintain minutes of Board and committee meetings.<sup>11</sup>

[In addition to fulfilling the duties outlined above, each director is expected to:

1. Join and actively participate in at least one committee of the Board;
2. Pay for a ticket to and attend the Organization's annual benefit;
3. Make every reasonable effort to bring financial support to the Organization annually from external sources;
4. Make personally meaningful financial gifts to the Organization at least annually;
5. Leverage personal relationships with others (including corporations, professional service firms, foundations, individuals and government agencies) to assist the staff of the Organization with implementing fundraising strategies, including adding names of potential sources of support to the Organization's mailing list;
6. Act as an ambassador for the Organization with respect to dealings with the general public, donors, government agencies and clients;
7. Act as a mentor to other directors; and
8. Suggest to the Nominating and Governance Committee any potential Board candidates who fulfill the Board's criteria for directors and who could make significant contributions to the Board and the Organization.]<sup>12</sup>

## VI. BOARD COMMITTEES

The Board currently has [seven] committees: [Audit, Compensation, Nominating and Governance, Development, Finance and Investment, Public Relations, Strategic Planning and Executive].<sup>13</sup> Each committee has its own charter, which sets forth the responsibilities of each committee, the qualifications of its members and the procedures of the committee. The Board retains discretion to form new committees, including sub-committees, and can disband committees where appropriate.<sup>14</sup>

## VII. CONFIDENTIALITY

Pursuant to their fiduciary duties of loyalty and care, directors have an obligation to keep confidential all non-public information obtained by a director that relates to the Organization's business and that he or she receives in connection with serving on the Board. Directors may not use such information for personal benefit or the benefit of persons or entities outside the Organization, nor may they disclose this information for any purpose without written authorization of the Board or as may be otherwise required by law or regulation. Confidential information includes, but is not limited to, information regarding the strategy, business, finances, operations and fundraising efforts or plans of the Organization (or any of the Organization's suppliers, customers, donors, volunteers or other constituents), minutes, reports and

materials of the Board and its committees, and other documents identified as confidential by the Organization. The proceedings and deliberations of the Board and its committees are also confidential non-public information and are subject to strict protection.

## **VIII. BOARD INTERACTION WITH THE PUBLIC<sup>15</sup>**

In most situations, the [Chief Executive Officer/Executive Director/President] speaks on behalf of the Organization with donors, employees, clients, suppliers, the media and others. The Chair of the Board is the spokesperson of the Board. Other directors should not communicate with representatives of the media unless duly authorized by the Chair of the Board or the [Chief Executive Officer/Executive Director/President], so as to prevent any inadvertent disclosure of confidential information.

## **IX. DIRECTOR ACCESS TO MANAGEMENT AND ADVISORS**

Directors have access to senior management and to Board and advisors. As the Board's role is one of oversight, with respect to ordinary course matters, directors should use good judgment when communicating with personnel and should coordinate such communications and request of materials through the office of the [Chief Executive Officer/Executive Director/President] or with the Chair of the Board, as necessary or appropriate in the judgment of the directors.

## **X. TENOR OF BOARDROOM DELIBERATIONS**

Achieving an atmosphere in which full and frank discussion can thrive, and consensus can ultimately be reached, is a challenge. It is the responsibility of the Board to act in the best interests of the Organization and disagreements may arise. Within the context of their fiduciary duties, directors should seek to participate and express disagreement in an open and collegial manner, with developing consensus and resolution as the ultimate goal.

## ENDNOTES

<sup>1</sup> IRS Form 990 requires disclosure of whether the organization has provided a complete copy of its Form 990 to all members of the board before filing the form, as well as disclosure of the process, if any, used by the organization to review its Form 990. *See* Form 990, Part VI, Lines 11a-b and related instructions.

<sup>2</sup> IRS Form 990 requires disclosure of the number of voting members of the board who are independent, in accordance with IRS tests. *See* Form 990, Part VI, Line 1b and related instructions.

<sup>3</sup> The N-PCL does not require the compensation committee or the nominating and governance committee to be composed of solely independent directors. However, the N-PCL requires the board or an audit committee comprised solely of “independent directors” (as defined in the N-PCL) to oversee the accounting and financial reporting process and the audit of financial statements of certain New York not-for-profits, with only independent directors permitted to participate in any board or committee deliberations or voting relating to such matters. *See* N-PCL § 712-a. IRS Form 990 also requires disclosure of whether the process for determining compensation of certain key employees included a review and approval by independent persons. *See* Form 990, Part VI, Lines 15a-b and related instructions. In addition, compensation will be presumed reasonable under the relevant tax rules if: (1) the compensation arrangement is approved in advance by disinterested members of the board or the committee; (2) prior to making its determination, the board or committee obtained and relied upon appropriate data as to comparability of compensation such as the compensation paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions, which may include reviewing compensation surveys, actual written offers from similar organizations competing for the person’s services, or other objective external data to establish comparable values for executive compensation (and for small organizations with gross receipts of less than \$1 million, appropriate comparability data includes data on compensation paid by three comparable organizations in the same or similar communities for similar services); and (3) the board or committee adequately and timely documented the basis for its determination that the compensation is reasonable concurrently with making that determination. *See* <https://www.irs.gov/charities-non-profits/charitable-organizations/rebuttable-presumption-intermediate-sanctions>; Internal Revenue Code § 4958 and related regulations.

<sup>4</sup> The bright-line tests for “independence” set forth in IRS rules are different in some respects to the bright-line tests set forth in the N-PCL’s definition of “independent director,” for example, the required “look-back” period is different (the most recent tax year under IRS tests, compared with the past three years under New York tests).

The IRS considers a director to be “‘independent’ only if all four of the following circumstances applied at all times during the organization’s tax year: (1) [t]he member wasn’t compensated as an officer or other employee of the organization or of a related organization...except as provided in the religious exception .... [n]or was the member compensated by an unrelated organization or individual for services provided to the filing organization or to a related organization, if such compensation is required to be reported in Part VII, Section A [of Form 990]; (2) [t]he member didn’t receive total compensation exceeding \$10,000 during the organization’s tax year ... from the organization and related organizations as an independent contractor, other than reasonable compensation for services provided in the capacity as a member of the governing body;... (3) [n]either the member, nor any family member of the member, was involved in a transaction with the organization (whether directly or indirectly through affiliation with another organization) that is required to be reported on Schedule L (Form 990) for the organization’s tax year; (4) [n]either the member, nor any family member of the member, was involved in a transaction with a taxable or tax-exempt related organization (whether directly or indirectly through affiliation with another organization) of a type and amount that would be reportable on Schedule L (Form 990) if required to be filed by the related organization.... A member of the governing body isn’t considered to lack independence merely because of the following circumstances: (1) [t]he member is a donor to the organization, regardless of the amount of the contribution;” (2) the religious exception applies (meaning the member has taken a bona fide vow of poverty and either (a) receives compensation as an agent of a religious order or a section 501(d) religious or apostolic organization, but only under circumstances in which the member doesn’t receive taxable income, or (b) belongs to a religious order that receives sponsorship or payments from the organization or a related organization that do not constitute taxable income to the member); or (3) the member receives financial benefits from the organization solely in the capacity of being a member of the charitable or other class served by the organization in the exercise of its exempt function, so long as the financial benefits comply with the organization’s terms of membership. Instructions to Form 990, Part VI, Line 1b.

The N-PCL defines “independent director” to mean “a director who: (i) is not, and has not been within the last three years, an employee or a key person of the corporation or an affiliate of the corporation, and does not have a relative who is, or has been within the last three years, a key person of the corporation or an affiliate of the corporation; (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 of the corporation; (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 provided payments, property or services to, or received payments, property or services from, the corporation or an affiliate of the corporation if the amount paid by the corporation to the entity or received by the corporation from the entity for such property or services, in any of the last three fiscal years, exceeded the lesser of \$10,000 or 2% of such entity's consolidated gross revenues if the entity's consolidated gross revenue was less than \$500,000; \$25,000 if the entity's consolidated gross revenue was \$500,000 or more but less than \$10 million; \$100,000 if the entity's consolidated gross revenue was \$10 million or more; 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, the terms: 'compensation' does not include reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director...; and '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, or payments made by the corporation at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the corporation are available to individual members of the public on the same terms, and such services received by the corporation are not available from another source." N-PCL § 102(a)(21).

<sup>5</sup> See N-PCL § 102(a)(19).

<sup>6</sup> See N-PCL § 102(a)(25).

<sup>7</sup> See Instructions to Form 990, Glossary.

<sup>8</sup> The definitions of "relative" in the N-PCL and "family member" in the Instructions to Form 990 are substantially the same. See N-PCL § 102(a)(22); Instructions to Form 990, Glossary.

<sup>9</sup> No employee of a New York not-for-profit shall serve as chair of the board or hold any other title with similar responsibilities, unless the board approves such employee serving as the chair by a two-thirds vote of the entire board and contemporaneously documents in writing the basis for approval. See N-PCL § 713(f).

<sup>10</sup> Note that not all actions listed below are required by law, but are best practices. This list should be tailored to the specific needs of the organization.

<sup>11</sup> The N-PCL requires that New York not-for-profits keep complete books and records of account and minutes of the proceedings of the board and any executive committee and keep at its office (or at the office of its transfer agent or registrar in the state), a list or record containing the names and addresses of all members, the class or classes of membership or capital certificates and the number of capital certificates held by each and the dates when they respectively became the holders of record thereof. Any of the foregoing books, minutes and records may be in written form or in any other form capable of being converted into written form within a reasonable time. See N-PCL § 621(a). The N-PCL also requires contemporaneous record-keeping relating to decisions such as approval of certain related party transactions, appropriations for expenditures or accumulations of endowment funds and electing an employee as chair of the board. See, e.g., N-PCL §§ 553, 713(f), 715(b). IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that "[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action." See Form 990, Part VI, Lines 8a-b and related instructions.

<sup>12</sup> Board responsibilities may be tailored to the specific needs of the organization.

<sup>13</sup> Although these Guidelines contemplate the formation of various committees, the Board is not required to form committees, but may do so for administrative ease, especially for larger boards.

<sup>14</sup> The board may also create "committees of the corporation," which may include members who are not directors. Committees of the corporation are not authorized to bind the board. Members of such committees shall be elected or appointed in the manner set forth in the by-laws, or if not set forth in the by-laws, in the same manner as officers of the corporation. See N-PCL § 712(e).

<sup>15</sup> This section should be tailored to the specific circumstances of the organization. Each organization should assess who it wishes to speak publicly on behalf of the organization.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Board Meeting Minutes

This form of meeting minutes may be used as a starting point for the board or a committee of the board to take a record of their meetings.<sup>1</sup> Minutes are a concise summary of the meeting and provide a record of actions taken by the board or committee. There is no one size fits all approach to taking minutes, but this form serves as a foundation for ensuring that the appropriate information is documented after a meeting.

Usually an organization's Secretary is responsible for making sure that minutes are prepared and approved following each meeting. As a best practice, the minutes should be distributed for review in advance of the meeting at which they will be approved. Each meeting generally should begin with the approval of the minutes from the prior meeting, which also allows the members to refresh themselves on the matters covered at the prior meeting and pick up where they left off, as appropriate.

Minutes are not meant to be a verbatim account of the discussions at the meeting. Rather, minutes should provide enough detail to support the actions or determinations made by the board or committee during the meeting, if any, and otherwise remind directors about what occurred during the meeting, so that they do not need to take notes themselves.<sup>2</sup> Accordingly, it may be appropriate to elaborate more on some matters than others. For ordinary course matters, it is generally sufficient to mention the topics discussed, the decisions or determinations that were made during the meeting, if any, as well as any next steps. If the topic of discussion involves important or sensitive matters, then more information regarding the issue, the discussion and resolution, should be included. For example, if during a meeting a board member discloses a potential conflict of interest, the minutes should detail that disclosure, the director's departure from the meeting for discussion and related recusal from related votes and how the conflict was addressed or resolved. Other topics may require more detail including discussions where directors express dissent to the determinations made. Minutes should also detail recusals and related reasons, interim arrivals and departures of directors during the meeting and important strategic determinations for the organization. Formal resolutions (where required) should be drafted in advance and distributed together with other board or committee materials in advance of the meeting. Minutes of executive sessions (i.e., meetings of directors without management present) are typically minimal for general discussions, with formal actions documented by resolutions (but without detail around the discussion).

Minutes should clearly indicate which discussions are subject to privilege, with privileged content redacted in minutes that are approved. Minutes should be treated as confidential within the organization and only accessible on a need-to-know basis by staff. Auditors should not have access to minutes that have not been approved by the board or committee. Organizations should exercise caution if using an AI tool to record the meeting and/or prepare draft minutes, to ensure accuracy and maintenance of confidentiality and privilege.

Various factors unique to an organization (including among others, organization structure, topics being discussed at the meeting and applicable legal requirements) may affect what should be covered. While this sample is generally appropriate for not-for-profit organizations, different and additional elements may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Meeting of the Board of Directors<sup>3</sup> [Date]

A duly called meeting of the Board of Directors of [Organization] (the “Board”) was [held at [location] [with certain participants joining by]] [convened] by video conference during which all participants could hear each other<sup>4</sup> on [day], [date], beginning at [time]. A quorum of Board members [was] present and no Board members objected to the notice calling the meeting.<sup>5</sup> [Name] served as Secretary for the meeting.

#### **I. BOARD MEMBERS PRESENT**

[List names and titles (e.g., Chair, Vice Chair, Treasurer, Secretary)]

#### **II. STAFF PRESENT**

[List names and positions]

#### **III. OTHER ATTENDEES**

[List names and associations, if any, and portions of the meetings attended by such persons]

#### **IV. MATERIALS**

[List materials provided relating to the meeting]

#### **V. PRIOR MEETING MINUTES**

[Name] began the meeting by calling for a motion to approve the minutes from the last Board meeting held on [date], which were previously provided to the Board. The minutes were approved by the Board.

#### **VI. INTRODUCTORY REMARKS AND MEETING PURPOSE**

[Name] summarized the meeting agenda for the Board and began the business of the meeting.

#### **VII. [PRESENTATION[S]] [MATTERS PRESENTED]**

[Summary of items discussed and approved at meeting.]

#### **VIII. CONCLUSION**

[Summary of any concluding remarks or next steps.] [Meeting end time.]<sup>6</sup>

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[Name], Secretary

ENDNOTES

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<sup>1</sup> This template can be used for minutes of the Board or any committee of the Board. The New York Not-for-Profit Corporation Law (“N-PCL”) requires that New York not-for-profits keep minutes of the proceedings of the board and any executive committee. *See* N-PCL § 621(a). The N-PCL also requires contemporaneous record-keeping relating to decisions such as approval of certain related party transactions, appropriations for expenditures or accumulations of endowment funds and electing an employee as chair of the board. *See, e.g.*, N-PCL §§ 553, 713(f), 715(b). IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

<sup>2</sup> The minutes serve as the record of the meeting; for this reason, directors are generally discouraged from taking notes during board and committee meetings. In the event of litigation arising in relation to matters discussed during a Board meeting, contemporaneous notes taken by directors at the meeting could be requested in discovery.

<sup>3</sup> References to “Board” should be updated to “committee,” as appropriate.

<sup>4</sup> N-PCL § 708 provides for methods of participating in meetings of the board and committees.

<sup>5</sup> N-PCL § 707 provides that unless a greater proportion is required by the N-PCL or by the certificate of incorporation or by a by-law adopted by the members (if any), a majority of the entire board shall constitute a quorum, except that the certificate of incorporation or by-laws may fix the quorum at less than a majority of the entire board, provided that in the case of a board of fifteen members or less the quorum shall be at least one-third of the entire number of members and in the case of a board of more than fifteen members, the quorum shall be at least five members plus one additional member for every ten members (or fraction thereof) in excess of fifteen.

<sup>6</sup> Except as otherwise provided in N-PCL § 621, every corporation shall keep, at the office of the corporation, correct and complete books and records of account and minutes of the proceedings of its members, board and executive committee, if any. *See* N-PCL § 621(a). As a best practice, corporations should keep records of minutes of meetings of all committees.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Board and Board Committee Self-Evaluation Form

This questionnaire is intended to assist in obtaining the viewpoints of directors regarding the structure and functioning of the board of directors in order to assist the board in its continuous efforts to improve its and its committees' effectiveness in governing the not-for-profit organization. Board and committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation. The questionnaire can be used in several ways: it can be distributed to directors for them to complete and return (anonymously if need be) to the board chair, a committee of the board or committee chair or other person (such as counsel or other third party adviser) who then collates and reports back to the board; it can be used as a guide for interviews of directors; and/or it can be used to facilitate a discussion by the board. However it is used, evaluation is most effective if the full board has an opportunity for candid and open discussion about any concerns raised or suggestions for areas of improvement.

**Practice Note:** Please note that **completed evaluation forms may be discoverable in litigation.** Therefore, some boards are opting for paperless facilitated board and committee discussions as the means of evaluation. (The questions on the attached form can be used as a guide for such facilitated discussions.) Even when written forms are used, they are typically relied on to collect director viewpoints for an oral report that is given to the board on the results – as an opportunity to engage the full board in a discussion of board performance. A board may wish to consider putting in place a policy that the executed forms not be retained once the information is reviewed. (Document retention policies should be reviewed and limits on routine document destruction in the context of an investigation or institution of a lawsuit considered.) An argument can be made for attorney-client communication protection attaching to the completed evaluation forms if they are designed to provide input to counsel, who is advising the board on efforts to improve governance processes. In such case, consider including a “privileged and confidential; attorney-client communication” legend on each evaluation form, along with a statement to the effect that: “This form is intended for the communication of information to legal counsel, to enable counsel to advise the Board in the Board’s continuous efforts to improve corporate governance.”

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

Please rate the statements that follow on a scale of 1 to 5, with 1 indicating that there is room for improvement and 5 indicating an area of considerable strength for the Board. A score of 3 indicates neutrality, no opinion or no knowledge on the matter.

### I. BOARD SIZE AND COMPOSITION

- |    |  |          |          |          |          |          |
|----|--|----------|----------|----------|----------|----------|
| 1. | The Board has an appropriate number of directors.  | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 2. | The Board's current composition reflects an appropriate mix of skills, experiences and backgrounds in relation to the needs of the Organization. | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 3. | The Board contains an appropriate balance of longer-serving members and newer additions to the Board.  | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 4. | Please circle the three most important skills or attributes that directors should possess:   |          |          |          |          |          |
|    | a. business experience   |          |          |          |          |          |
|    | b. financial acumen  |          |          |          |          |          |
|    | c. ability to think strategically  |          |          |          |          |          |
|    | d. investment experience   |          |          |          |          |          |
|    | e. expertise in relation to governance/ESG   |          |          |          |          |          |
|    | f. fundraising skill and experience  |          |          |          |          |          |
|    | g. access to a network of donors   |          |          |          |          |          |
|    | h. industry experience   |          |          |          |          |          |
|    | i. understanding of ethical issues/human resources   |          |          |          |          |          |
|    | j. understanding of political issues   |          |          |          |          |          |
|    | k. ability to make a financial contribution  |          |          |          |          |          |
|    | l. technology experience   |          |          |          |          |          |
|    | m. other (please specify): _____   |          |          |          |          |          |

**Comments and suggestions:**

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### II. BOARD EFFECTIVENESS AND AGENDA

- |    |  |          |          |          |          |          |
|----|--|----------|----------|----------|----------|----------|
| 1. | Directors are informed, prepared for and appropriately engaged in discussions at meetings. | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 2. | Each director contributes effectively to the work of the Board.                            | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 3. | The Board devotes sufficient attention to:   |          |          |          |          |          |
|    | a. strategic plans and associated risks  | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
|    | b. fundraising and other funding issues  | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
|    | c. whether the Organization is being properly managed                                      | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |

d.	financial statements and processes	1	2	3	4	5
e.	annual operating and capital plans and budget	1	2	3	4	5
f.	the Organization's governance framework and standards of conduct	1	2	3	4	5
g.	periodic review of major projects	1	2	3	4	5
h.	oversight of risk management systems, processes and activities (including vis-à-vis data privacy, cybersecurity and/or insurance, as applicable)	1	2	3	4	5
i.	assessment of the Organization's performance against its strategic goals and plans (including vis-à-vis financial assets and investments, as applicable)	1	2	3	4	5
j.	senior management evaluation and executive compensation decisions	1	2	3	4	5
k.	board and management development and succession	1	2	3	4	5
4.	The Board is well-informed about the Organization's operations and financial condition.	1	2	3	4	5
5.	The Board regularly monitors performance against the Organization's strategic and business plans.	1	2	3	4	5
6.	The Board provides appropriate oversight relating to internal controls and compliance with applicable laws and regulations.	1	2	3	4	5
7.	The Board understands major risks facing the Organization and provides appropriate oversight of risk management.	1	2	3	4	5
8.	The Board is appropriately engaged in evaluating the performance of the [Executive Director/Chief Executive Officer/President] and determining their compensation.	1	2	3	4	5
9.	The Board appropriately communicates its goals, expectations, and concerns to the [Executive Director/Chief Executive Officer/President], and the [Executive Director/Chief Executive Officer/President] is responsive to such communications.	1	2	3	4	5
10.	The Board provides clear and well-understood policy direction to management and employees/volunteers.	1	2	3	4	5
11.	The Board understands and respects that its role is to provide oversight and direction to management and employees/volunteers, and it does not unduly intrude into the day-to-day operations of the Organization.	1	2	3	4	5
12.	Directors have sufficient access to officers and other members of the management team outside of Board meetings.	1	2	3	4	5
13.	The Board has sufficient access to external advisers when needed.	1	2	3	4	5

14.	The Board has adopted appropriate corporate governance and ethics policies and procedures.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
15.	Directors disclose actual and potential conflicts and otherwise comply with the Organization’s Conflicts of Interest and Related Party Transactions Policy.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
16.	The Board effectively oversees the Organization’s (i) Conflicts of Interest and Related Party Transactions Policy, (ii) Whistleblower Policy and (iii) Investment Policy (as applicable).	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
17.	The Board has a positive culture and working environment supported by appropriate meeting processes.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
18.	Each director participates in the Organization’s fundraising activities.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
19.	[The current expectation concerning director personal financial contributions is appropriate.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>

**Comments and suggestions:**

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**III. BOARD INFORMATION, MEETINGS AND LEADERSHIP**

1.	The Board holds an appropriate number of meetings.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
2.	Board meetings are of an appropriate length to cover the business to be conducted and enable directors to meet their responsibilities.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
3.	Directors receive timely and accurate minutes, advance written agendas that are focused on the right issues, meeting notices and other information in sufficient time to allow them to prepare for meetings.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
4.	Directors receive clear, concise and relevant background materials to prepare in advance for meetings.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
5.	Information provided to directors is of an appropriate volume, detailed enough to provide the desired information, and analytic as well as informative.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
6.	Meetings are conducted in a manner that fosters open communication, meaningful participation and timely resolution of issues.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>

7.	Board meeting time is appropriately allocated between Board discussion and management presentations or other speakers.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
8.	Management presentations to the Board are of appropriate quality, length and relevance.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
9.	Directors have sufficient input into shaping the Board’s agenda and priorities.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
10.	The Board’s leadership is effective.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
11.	Executive sessions of the Board (without the [Executive Director/Chief Executive Officer/President] or other employees present) are held periodically.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>

**Comments and suggestions:**

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**IV. BOARD COMMITTEES**

1.	The current Board committee structure, charters, composition and processes assist the Board in the execution of its responsibilities and contribute to its efficiency and effectiveness.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
2.	The Board and relevant committees review (and update as needed) the charter (or other delegation scope/authority) of each committee periodically.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
3.	The Board’s method for determining committee composition and leadership is appropriate.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
4.	The committees effectively communicate their activities, findings and recommendations to the full Board.	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
5.	[The Audit Committee is effective in fulfilling its responsibilities.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
6.	[The Nominating and Governance Committee is effective in fulfilling its responsibilities.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
7.	[The Compensation Committee is effective in fulfilling its responsibilities.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
8.	[The Executive Committee is effective in fulfilling its responsibilities.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>
9.	[The Finance and Investment Committee is effective in fulfilling its responsibilities.]	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>

- |     |   |          |          |          |          |          |
|-----|---|----------|----------|----------|----------|----------|
| 10. | [The Strategic Planning Committee is effective in fulfilling its responsibilities.] | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 11. | [The Development Committee is effective in fulfilling its responsibilities.]        | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 12. | [The Public Relations Committee is effective in fulfilling its responsibilities.]   | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 13. | [The [●] Committee is effective in fulfilling its responsibilities.]                | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 14. | A committee that the Board should consider creating is:<br>_____.                   | <i>1</i> | <i>2</i> | <i>3</i> | <i>4</i> | <i>5</i> |
| 15. | A committee I would like to serve on is: _____.                                     |          |          |          |          |          |

**Comments and suggestions:**

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**V. ADDITIONAL QUESTIONS**

1. What do you consider to be the three most important issues facing the Organization and the Board in the next 12-24 months, and is the Board well-positioned to provide direction on these issues?

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2. Please offer suggestions as to how the Board's organization, performance or effectiveness can be improved.

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## Not-For-Profit Practice Group

### Sample Not-For-Profit Code of Conduct and Ethics

The board of a not-for-profit organization may find it useful to adopt a code of conduct and ethics applicable to the board, management, employees and volunteers of the organization and its affiliates requiring fulfillment of responsibilities in a manner that furthers the purpose and mission of the organization and complies with law, regulations, ethical standards and policies adopted by the organization.

Each not-for-profit organization will need to decide for itself the level of detail required in its code of conduct and ethics. This sample provides only one example incorporating elements that certain New York not-for-profits are required to comply with pursuant to the New York Not-for-Profit Corporation Law (the “N-PCL”). One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

Note that the U.S. Federal Sentencing Guidelines provide for the mitigation of certain penalties depending on a number of factors, including the existence and effectiveness of the organization’s compliance program, one part of which is the code of conduct and ethics, and self-reporting, cooperation or acceptance of responsibility.<sup>1</sup> Although the U.S. Department of Justice has not issued formal guidelines for not-for-profit compliance programs,<sup>2</sup> among the most critical factors in evaluating the effectiveness of such a program is whether it is designed to prevent and detect wrongdoing by employees and enforcement of the program.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Code of Conduct and Ethics

[Consider including a letter from the Chair of the Board or President/CEO/Executive Director. This introductory letter should be aspirational in tone and addressed to employees, volunteers, officers, directors and key persons explaining the purpose of the Code of Conduct and Ethics.]

#### I. YOUR OBLIGATIONS

This Code of Conduct and Ethics (this “Code”) is designed to promote **honest, ethical and lawful conduct** by all employees, volunteers, officers, directors and any other persons who are in a position to exercise substantial influence over the affairs of the Organization (“key persons”) (referred to as “you”) of [\_\_\_\_\_] and all of its affiliates (collectively, the “Organization”). This Code is intended to help you understand the Organization’s standards of ethical business practices and to stimulate awareness of ethical and legal issues that you may encounter in carrying out your responsibilities to the Organization. In addition, independent contractors, consultants and agents who represent the Organization are expected to apply the same high standards while working on Organization business.

The actions of every employee, volunteer, officer, director and key person may affect the **reputation and integrity** of the Organization. Therefore, it is essential that you take the time to review this Code and develop a working knowledge of its provisions. You are required to complete a certificate attesting to compliance with the Code upon becoming an employee, volunteer, officer, director or key person and, thereafter, on an annual basis.

At all times, you are expected to:

- **Avoid conflicts** between personal and professional interests where possible;
- **Comply with the Organization’s Conflicts of Interest and Related Party Transactions Policy**, including by disclosing any conflict to the [Board of Directors of the Organization (the “Board”)]*[[insert name of authorized Board committee, if applicable]* (the “Committee”)]<sup>3</sup> and otherwise pursue the ethical handling of conflicts (whether actual or apparent) when conflicts or the appearance of conflicts are unavoidable;
- **Provide accurate and complete information** in a timely manner in the course of fulfilling your obligations;
- **Provide full, fair, accurate, timely and understandable disclosure** in reports required to be filed by the Organization with regulators and in other public communications made by the Organization;
- **Comply with all applicable laws**, regulations and Organization policies;
- **Seek guidance** where necessary from a responsible supervisor;
- **Promptly report any violations of this Code** to a responsible supervisor, who will in turn report any violations to the [Board][Committee] in accordance with the Organization’s Whistleblower Policy)<sup>4</sup>; and
- **Be personally accountable** for adherence to this Code.

**WHO DO I CONTACT  
FOR GUIDANCE OR TO REPORT CONCERNS?**

If you believe a situation may involve or lead to a violation of this Code, you have an affirmative duty to seek guidance and report such concerns.

- **Seek guidance** from a responsible supervisor or other appropriate internal authority (for example, a Human Resources manager).
- **Disclose concerns or violations** of this Code [in accordance with the Organization’s Whistleblower Policy] to a supervisor, manager, [the Whistleblower Policy Administrator,] the Chair of the [Board][Committee] or the Organization’s legal counsel.

**[BOARD][COMMITTEE] CHAIR:**

[INSERT CONTACT DETAILS]

**[WHISTLEBLOWER POLICY ADMINISTRATOR]:**

[INSERT CONTACT DETAILS]

**[LEGAL COUNSEL]:**

[INSERT CONTACT DETAILS]

**It is the Organization’s policy to encourage the communication of bona fide concerns relating to the lawful and ethical conduct of business, and audit and accounting procedures or related matters. It is also the policy of the Organization to protect those who communicate bona fide concerns from any retaliation for such reporting.**

**Confidential and anonymous mechanisms for reporting concerns are available and are described in this Code. However, anonymous reporting does not serve to satisfy a duty to disclose your own potential involvement in a conflict of interest or in unethical or illegal conduct.**

This Code is part of a broader set of Organization policies and compliance procedures [described in greater detail in the Organization’s employee manuals and distributed memoranda]. This Code is not intended to supersede or materially alter specific Organization policies and procedures already in place and applicable to particular employees as [set forth in the Organization’s employee manuals and distributed memoranda, and] communicated to Organization employees.

No Organization policy can provide definitive answers to all questions. It is difficult to anticipate every decision or action that you may face or consider. **Whenever there is doubt about the right ethical or legal choice to make, or questions regarding any of the standards discussed or policies referenced in this Code, you should fully disclose the circumstances, seek guidance about the right thing to do and keep asking until guidance is obtained.**

**Those who violate the standards in this Code will be subject to disciplinary action. Failure to follow this Code, as well as to comply with federal, state, local and any applicable foreign laws, and the Organization's policies and procedures, may result in termination of board service or of employment with the Organization.**

## II. COMPLIANCE WITH LAWS, RULES AND REGULATIONS

The Organization requires you to comply with all applicable laws, rules and regulations. Violation of laws and regulations may subject you, as well as the Organization, to civil and/or criminal penalties. To assure compliance with applicable laws and regulations, the Organization has established various policies and procedures, including those relating to: [List policies, e.g., Conflicts of Interest and Related Party Transactions Policy, Whistleblower Policy, Document Retention and Destruction Policy]. You have an obligation to comply with these policies and procedures and to promptly alert [a responsible supervisor, the Organization's legal counsel, the Whistleblower Policy Administrator, the Chair of the [Board][Committee], and/or other appropriate internal authority], whose contact information is set forth above, of any deviation from them.

Legal compliance is not always intuitive. To comply with the law, you must learn enough about the national, state and local laws that affect your work at the Organization to spot potential issues and to obtain proper guidance on the right way to proceed. When there is any doubt as to the lawfulness of any proposed activity, you should seek advice from the Organization's legal counsel, whose contact information is set forth above.

Certain legal obligations and policies that are particularly important are summarized below. Further information on any of these matters may be obtained from the Organization's legal counsel, whose contact information is set forth above.

## III. CONFLICTS OF INTEREST AND RELATED PARTY TRANSACTIONS<sup>5</sup>

The Organization expects you to exercise good judgment and the high ethical standards in your activities on behalf of the Organization as well as in your private activities outside the Organization. Particular care should be taken to ensure that no detriment to the interests of the Organization (or appearance of such detriment) may result from a conflict or potential conflict between those interests and any personal or business interests which you may have. In particular, you have an obligation to avoid, and where avoidance is not feasible, to disclose to the appropriate individual (as set forth in the Organization's Conflicts of Interest and Related Party Transactions Policy), any activity, agreement, business investment or interest or other situation that might in fact or in appearance cause you to place your own interests, or those of another, in tension with or above your obligation to the Organization. Care should be taken about the appearance of a conflict since such appearance might impair confidence in, or the reputation of, the Organization even if there is no actual conflict and no wrongdoing.

While it is not possible to describe or anticipate all the circumstances that might involve a conflict of interest, a conflict of interest may arise whenever you take action or have (direct or indirect) interests that may make it difficult to perform your work objectively or effectively or when you (directly or indirectly) receive personal benefits as a result of your position or relationship with respect to the Organization. For

example, a conflict may arise if you have a financial or personal interest in a contract or transaction to which the Organization is a party. In addition, receipt by you or a member of your family of a personal benefit as a result of your position with the Organization may be deemed a conflict of interest. Procedures relating to disclosure and review of conflicts of interest and related party transactions are set forth in the Organization's Conflicts of Interest and Related Party Transactions Policy.

In all instances where the appearance of a conflict exists, you must disclose the nature of the conflict and all material facts related to such conflict to the Chair of the [Board][Committee], who shall communicate that information to the [Board][Committee].<sup>6</sup> We will then work with you to determine what to do next.

#### **IV. COMMUNITY, POLITICAL, CHARITABLE AND OTHER OUTSIDE ACTIVITIES**

The Organization generally encourages participation in community activities outside the Organization. However, employees should avoid any outside personal interest or activity (whether or not for profit) that will interfere with their duties to the Organization. As a guideline, such activities should not encroach on time or attention employees should be devoting to Organization business, adversely affect the quality of their work, compete with the Organization's business, imply Organizational sponsorship or support without express approval by the Organization, and/or adversely affect the reputation of the Organization.

No employee shall publicly utilize any affiliation of the Organization in connection with the promotion of partisan politics, religious matters, or positions on any issue except with written authorization of the Organization.

#### **V. PROTECTION AND PROPER USE OF THE ORGANIZATION'S ASSETS**

You have a personal responsibility to protect the assets of the Organization from misuse or misappropriation. The assets of the Organization include tangible assets, such as products, equipment and facilities, as well as intangible assets, such as intellectual property, trade secrets, reputation and business information (including any non-public information learned as an employee, volunteer, officer, director or key person of the Organization).

##### **5.1 Theft/Misuse of Assets**

The Organization's assets may only be used for business purposes and such other purposes as are approved by the Organization. You must not take, make use of, or knowingly misappropriate the assets of the Organization for personal use, for use by another, or for an improper or illegal purpose. You are not permitted to remove, dispose of, or destroy anything of value belonging to the Organization without the Organization's express prior written consent, including both physical items and electronic information.

##### **5.2 Confidential or Proprietary Information/Privacy**

You must not use or disclose any confidential or proprietary information to any person or entity outside the Organization, either during or after service with the Organization, except with written authorization of the Organization or as may be otherwise required by law or regulation. You may not use confidential or proprietary information for your own personal benefit or the benefit of persons or entities outside the Organization.

Confidential or proprietary information includes all non-public information learned as an employee, volunteer, officer, director or key person of the Organization. It includes, but is not limited to:

- Non-public information that might be (i) of use to suppliers, vendors, joint venture partners or others, (ii) of interest to the press, or (iii) harmful to the Organization or any of its constituents, if disclosed;
- Non-public information relating to the Organization's operations, including financial information, donor lists, mailing lists and any information relating to fundraising (including fundraising efforts, plans, ideas and proposals), minutes, reports and materials of the Board and its committees, and other documents identified as confidential;
- Non-public information about discussions and deliberations, relating to business issues and decisions, between and among employees, volunteers, officers, directors and key persons; and
- Non-public information about employees, directors, officers, volunteers or key persons, or any other individuals about whom the Organization may hold information from time to time.

### 5.3 Outside Communication

The Organization is committed to providing full, fair and accurate disclosure in all public communications and in compliance with all applicable law, regulations and rules. Consistent with this commitment, employees may not answer questions from the media, donors, potential donors or any other members of the public unless specifically authorized to do so by the Organization. If you receive such an inquiry, you must obtain the name of the person and their contact information if possible and immediately notify [the Public Relations Manager or other appropriate person].

As individuals, we all have rights to speak out on issues including in a public forum, whether at your town hall or on a social networking media application or website. However, when you speak as an individual it is critical that you do not give the appearance of speaking or acting on the Organization's behalf. You should be especially aware of the broad reach of social networking media applications and websites, and that such media is increasingly being monitored by donors, customers, competitors, regulators and colleagues. Your comments may be attributed to the Organization, even though you did not intend for your comments to be attributed that way.

Whether or not you identify yourself as an employee of the Organization, you must not engage in any online or social media activities that would violate any of the Organization's policies, including [INSERT NAME OF ANY OTHER POLICIES].

Nothing in this policy intends to, nor should it be interpreted or applied to, in any way limit any employee's rights under applicable federal, state, or local laws, including employees' rights under the National Labor Relations Act to engage in protected concerted activity with other employees to improve terms and conditions of employment, such as (but not limited to) wages and benefits.

### 5.4 Network Use, Integrity & Security

The Organization reserves the right to monitor or review any and all data and information contained on any computer or other electronic device issued by the Organization. In addition, the Organization reserves the right to monitor or review an employee's or officer's use by an employee, volunteer, officer, director or key person of the Internet, Organization Intranet and Organization e-mail or any other electronic communications without prior notice.

Access to Organization systems will be revoked and disciplinary action will be taken in the event that such systems are used to commit illegal acts, or to violate the nondiscrimination, harassment, pornography, solicitation or proprietary information terms of this Code, or any other terms of this Code.

In order to maintain systems integrity and protect the Organization's network, no person is permitted to divulge any passwords used to access any Organization computer or database. Any suspected breach of the Organization's network security systems must be reported to a responsible supervisor or appropriate internal authority immediately.

All employees volunteers, officers, directors and key persons are required to refrain from using or distributing software that may damage or disrupt the Organization's work environment by transmitting a virus or conflicting with Organization systems.

You must not engage in the unauthorized use, copying, distribution or alteration of computer software whether obtained from outside sources or developed internally. All software, including "shareware," contains terms of use that must be adhered to.

## VI. ILLEGAL PAYMENTS

No illegal payments of any kind are to be made to any local, state or Federal Government officials in the United States or to government officials of any other country, territory or municipality at any time or under any circumstances. Moreover, no funds or other assets of the Organization are to be paid, directly or indirectly, to government officials or persons acting on their behalf or to representatives of other businesses for the purpose of influencing decisions or actions with respect to the Organization's activities. Kickbacks to or from any person are prohibited.

**Any question as to whether a gift or payment would be considered improper under the Organization's guidelines or under law must be discussed with the Organization's legal counsel.**

**Under no circumstance is it acceptable for you to offer, give, solicit or receive any form of bribe, kickback, payoff, or inducement.**

You may not use agents, consultants, independent contractors or other representatives to do indirectly what you could not do directly under this Code or under applicable law, rules and regulations.

## VII. MAINTAINING A SAFE, HEALTHY AND AFFIRMATIVE WORKPLACE

The Organization is an equal opportunity employer and bases its recruitment, employment, development and promotion decisions solely on a person's ability and potential in relation to the needs of the job, and complies with local, state and federal employment laws. The Organization makes reasonable job-related accommodations for any qualified employee or officer with a disability when notified by the employee that he/she needs an accommodation.

The Organization is committed to maintaining a workplace that is free from sexual, racial, or other unlawful harassment, and from threats or acts of violence or physical intimidation. Abusive, harassing or other offensive conduct is unacceptable, whether verbal, physical or visual. If you believe that you have been harassed or threatened with or subjected to physical violence in or related to the workplace, you should report the incident to an appropriate supervisor or Human Resources [or the Organization's legal counsel], who will arrange for it to be investigated. All efforts will be made to handle the investigation confidentially.

The Organization prohibits the possession, use or distribution of offensive materials on the Organization's property, or the use of the Organization's personal computers or other equipment to obtain or view such materials. All employees, volunteers, officers, directors and key persons must promptly contact an appropriate supervisor or Human Resources [or the Organization's legal counsel] about the existence of

offensive materials, especially child pornography, on the Organization's systems or premises so that appropriate action may be taken, including notifying the proper authorities if necessary.

The Organization is committed to providing a drug-free work environment. The illegal possession, distribution, or use of any controlled substances on the Organization's premises or at Organization functions is strictly prohibited. Similarly, reporting to work under the influence of any illegal drug or alcohol and the abuse of alcohol or medications in the workplace is not in the Organization's best interest and violates this Code.

All accidents, injuries, or concerns about unsafe equipment, practices, conditions or other potential hazards must be immediately reported to an appropriate supervisor.

### VIII. ACCOUNTING PRACTICES, BOOKS AND RECORDS AND RECORD RETENTION

**Honest and accurate recording and reporting of information is critical to our ability to make responsible business decisions. You have a strict obligation to provide accurate information in the records of the Organization.**

You are expected to support the Organization's efforts in fully and fairly disclosing the financial condition of the Organization in compliance with applicable accounting principles, laws, rules and regulations and making full, fair, accurate timely and understandable disclosure in our reports filed with regulatory agencies and other communications. Our financial statements and the books and records on which they are based must accurately reflect all transactions and conform to all legal and accounting requirements and our system of internal controls.

**All employees, volunteers, officers, directors and key persons – and, in particular, the President/CEO/Executive Director [, the chief financial officer, the controller and the principal accounting officer] – have a responsibility to ensure that the Organization's accounting records do not contain any false or misleading entries. Any known or suspected false or misleading entries must be reported immediately to the [Chair of the Board][Audit Committee].**

The Organization prohibits any misclassification of transactions as to accounts, departments or accounting periods and, in particular:

- All accounting records, as well as reports produced from those records, are to be kept and presented in accordance with law and are to comply with generally accepted accounting principles applicable to the Organization;
- All records are to fairly and accurately reflect the transactions or occurrences to which they relate;
- All records are to fairly and accurately reflect in reasonable detail the Organization's assets, liabilities, revenues and expenses;
- No accounting records are to contain any false or misleading entries;
- All transactions are to be supported by accurate documentation in reasonable detail and recorded in the proper account and in the proper accounting period; and

- The Organization’s system of internal accounting controls, including compensation controls, is required to be followed at all times.

You must always record data in a timely and accurate manner. This protects the Organization’s resources and meets the expectations of the people who rely on the accuracy of the Organization’s records to perform their jobs. Falsifying business records is a serious offense, which may result in criminal prosecution, civil action and/or disciplinary action up to and including termination of employment. If you are authorized to make expenditures or enter into transactions on behalf of the Organization, you must ensure that the applicable records comply with the Organization’s accounting and purchasing policies and that all transactions are recorded properly.

Consistent with the reporting and recordkeeping commitments discussed above, you must accurately and truthfully complete all records used to determine compensation or expense reimbursement. This includes, among other items, reporting of hours worked (including overtime) and reimbursable expenses (including travel and meals).

Compliance with applicable law regarding record retention [and the Organization’s Document Retention and Destruction Policy] is mandatory. Destroying or altering a document with the intent to impair the document’s integrity or availability for use in any potential official proceeding is a crime. *Destruction of records may only take place in compliance with applicable law [and the Organization’s Document Retention and Destruction Policy].* Documents relevant to any pending, threatened, or anticipated litigation, investigation, or audit shall not be destroyed for any reason. If you believe that Organization records are being improperly altered or destroyed, you must report it to a responsible supervisor, the appropriate internal authority or the Organization’s legal counsel.

## IX. RAISING QUESTIONS AND CONCERNS

**Each employee, volunteer, officer, director and key person is responsible for promptly reporting to the Organization any circumstances that such person believes in good faith may constitute a violation of this Code or any other Organization policy, or applicable law, regulations or rules.** If you are in a situation that you believe may involve or lead to a violation of this Code, you have an affirmative duty to disclose to, and seek guidance from, a responsible supervisor, the Organization’s legal counsel, the Chair of the [Board][Committee] or other appropriate internal authority. *See “Who Do I Contact for Guidance or to Report Concerns?” above [and the Whistleblower Policy] for additional details.*

**You are strongly encouraged to report any complaint regarding financial wrongdoing (including circumvention of internal controls or violation of the accounting policies of the Organization), fraud, harassment, or any other illegal, unethical or proscribed conduct (including confidential and anonymous complaints) to the [Organization’s Helpline on [INSERT NUMBER(S)] or to the] policy administrator of the Organization’s Whistleblower Policy, to a supervisor or manager or to the Chair of the [Board][Committee] – see “Who Do I Contact for Guidance or to Report Concerns?” above.**

[The Helpline is a special toll-free line available 24 hours a day, 365 days a year. It is intended to operate in addition to other resources available to you to voice complaints or concerns, such as supervisors, managers and Human Resources staff. The Helpline is monitored by a third party for reporting to the Organization’s [Board][Committee].]

**It is the Organization’s policy to encourage the communication of bona fide concerns relating to the lawful and ethical conduct of business, and audit and accounting procedures or related matters. It is also the policy of the Organization to protect those who communicate bona fide concerns from any retaliation for such reporting.**<sup>7</sup> No retribution against any individual who reports violations of this Code

in good faith will be permitted. Confidential and anonymous mechanisms for reporting concerns are available and are described in this Code [and the Whistleblower Policy]. However, anonymous reporting does not serve to satisfy a duty to disclose your potential involvement in a conflict of interest or in unethical or illegal conduct. Every effort will be made to investigate confidential and anonymous reports within the confines of the limits on information or disclosure such reports entail. While self-reporting a violation will not excuse the violation itself, the extent and promptness of such reporting will be considered in determining any appropriate sanction, including dismissal. The Organization will investigate any matter which is reported and will take any appropriate corrective action.

## **X. VIOLATIONS OF THIS CODE**

Allegations of Code violations will be reviewed and investigated by the Organization's legal counsel, or, in appropriate circumstances by the Organization's [Board][Committee].

**Those who violate the standards in this Code will be subject to disciplinary action. Failure to follow this Code, or to comply with federal, state, local and any applicable foreign laws, and the Organization's policies and procedures may result in, among other actions, suspension of work duties, diminution of responsibilities or demotion, and termination of board service or employment with the Organization.**

**CERTIFICATE OF COMPLIANCE**

I \_\_\_\_\_ hereby certify that I have read, understand  
(Print name)

and am in compliance with the terms of the foregoing Code of Conduct and Ethics.

**Date:** \_\_\_\_\_

**Signature:** \_\_\_\_\_

**Title:** \_\_\_\_\_

*If you have any questions, please contact the Organization's legal counsel:*

[INSERT CONTACT DETAILS]

## ENDNOTES

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<sup>1</sup> See US Federal Sentencing Guidelines, Chapter 8.

<sup>2</sup> See Department of Justice (DOJ) guidance relating to effective compliance programs more generally, including DOJ Criminal Division, Corporate Enforcement and Voluntary Self-Disclosure Policy (March 2026), available at <https://www.justice.gov/dag/media/1430731/dl?inline>; DOJ, Criminal Division, Evaluation of Corporate Compliance Programs (updated September 2024), available at <https://www.justice.gov/criminal/criminal-fraud/page/file/937501/dl>.

<sup>3</sup> The N-PCL requires that the board oversee the adoption, implementation of, and compliance with the conflict of interest policy. Either the board or an authorized committee thereof may review and approve conflicts of interest. See N-PCL § 715-a(a).

<sup>4</sup> The N-PCL requires New York not-for-profits that have 20 or more employees and annual revenue in excess of \$1 million in the prior year to have a whistleblower policy that includes certain provisions. See N-PCL § 715-b.

<sup>5</sup> The N-PCL requires every New York not-for-profit organization (regardless of size) to adopt a conflict of interest policy applicable to directors, officers, and key persons (as defined in the N-PCL) that includes certain provisions. See N-PCL § 715-a. The N-PCL also requires specific procedures to be adhered to with respect to “related party transactions.” See N-PCL § 715(a)-(b).

<sup>6</sup> The N-PCL requires that conflicts of interest, or potential conflicts of interests, be disclosed to the board or to a committee of the board. See N-PCL § 715-a(b)(2).

<sup>7</sup> Whistleblower policies that are required by the N-PCL must “protect from retaliation persons who report suspected improper conduct [and] provide that no director, officer, key person, employee or volunteer of a corporation who in good faith reports any action or suspected action taken by or within the corporation that is illegal, fraudulent or in violation of any adopted policy of the corporation shall suffer intimidation, harassment, discrimination or other retaliation, or in the case of employees, adverse employment consequence.” N-PCL § 715-b(a).

## Not-For-Profit Practice Group

### Sample Not-For-Profit Investment Policy

The board of a not-for-profit organization is responsible for ensuring that the not-for-profit's assets are protected and any investment of its funds is prudent and in the best interest of the organization. The New York Prudent Management of Institutional Funds Act (the "NYPMIFA"), added to the New York Not-for-Profit Corporation Law (the "N-PCL") as Article 5-A (effective September 17 2010) and as amended, governs the management and investment of funds held by New York not-for-profit corporations and other institutions. Under the NYPMIFA, the standard of conduct for each person managing and investing an institutional fund is "comply[] with the duty of loyalty imposed by law" and to "manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances."<sup>1</sup>

The NYPMIFA replaces and updates key provisions of the Uniform Management of Institutional Funds Act, which was adopted in New York in 1978. The NYPMIFA applies to all "institutions" as defined in the N-PCL<sup>2</sup> and covers: (i) the spending of endowment funds, (ii) the standards for the prudent management and investment of institutional funds, (iii) the delegation of management and investment functions to outside advisors and (iv) procedures for lifting or modifying donor-imposed restrictions on the management, expenditure or use of institutional funds (including receiving the donor's written consent or seeking court approval, to release or modify a restriction on the management or investment of an institutional fund).<sup>3</sup>

Not-for-profit organizations defined as "institutions" under the N-PCL, including all New York not-for-profit corporations, corporations formed under the Religious Corporations Law and education corporations as defined in the Education Law § 216-a, are also required to adopt an investment policy setting forth guidelines on investments and delegation of management and investment functions.<sup>4</sup>

The sample investment policy should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

This sample policy is not a "one-size-fits all" but rather provides one example that incorporates elements required under the NYPMIFA. Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms, the extent of financial resources, the type of investments held and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Investment Policy

#### I. PURPOSE

In accordance with the New York Prudent Management of Institutional Funds Act, this investment policy (“Investment Policy”) sets forth guidelines governing the investment and management of the Financial Assets (as hereinafter defined) including the delegation of management and investment functions by [the Board of Directors (the “Board”) of [\_\_\_\_\_] (the “Organization”)] / [[*insert name of authorized Board committee, if applicable*] (the “Committee”) of [\_\_\_\_\_] (the “Organization”), as delegated to the Committee by the Organization’s Board of Directors].<sup>5</sup>

#### II. FINANCIAL ASSETS

The Organization’s financial assets consist of [insert description of the financial assets including, but not limited to, bank accounts, cash, money-market instruments, mutual funds, bonds, stocks] and other stocks, bonds or financial instruments that the Organization may invest from time to time (“Financial Assets”).

#### III. INVESTMENT AND FINANCIAL MANAGEMENT OBJECTIVES

The Organization’s objectives are to monitor and grow its Financial Assets and ensure that they are readily available to the Organization to fulfill its purpose and mission. [*Insert any other relevant objectives or guidelines for the management and investment of Financial Assets for the Organization such as preservation of capital, risk aversion/tolerance, attitude towards future gifts or bequests and any investment restrictions, prohibited assets and prohibited transactions.*]

#### IV. [BOARD][COMMITTEE] RESPONSIBILITIES

In managing the Financial Assets, the [Board][Committee] will act in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances and in the best interests of the Organization.<sup>6</sup> [The Committee will report to the Board, as appropriate, on actions and results, and any other matters the Committee deems appropriate or the Board requests.]

##### A. Investment Allocation and Diversification

The [Board][Committee] shall review (a) from time to time the allocation of the Organization’s investments and determining the appropriate allocations based on the Organization’s [cash-flow] needs, and (b) at least annually, the level of diversification of the Financial Assets.<sup>7</sup> [*Insert any other relevant considerations regarding the allocation of the Financial Assets in light of the N-PCL § 552(e) factors listed below.*]

In making decisions regarding the management and investment of the Financial Assets, the [Board][Committee], in accordance with N-PCL § 552(e), will consider the following factors, if relevant:

1. general economic conditions;
2. the possible effect of inflation or deflation;
3. the expected tax consequences, if any, of investment/management decisions or strategies;
4. the role that each investment or course of action plays within the overall Financial Assets portfolio;

5. the expected total return from income and the appreciation of the Financial Assets;
6. other resources of the Organization;
7. the needs of the Organization to make distributions and to preserve capital; and
8. an asset's special relationship or special value, if any, to the purposes of the Organization.<sup>8</sup>

#### **B. Delegation to External Agent(s)**

The [Board][Committee] may delegate management and investment decisions to an external agent, such as a bank, investment manager or other financial advisor, except where prohibited by the terms of a gift instrument. The [Board][Committee] will establish the scope and terms of the delegation, including the compensation to be paid, and monitor the external agent's performance and compliance with the scope and terms of the delegation.<sup>9</sup>

The Organization will take reasonable measures to assess at least annually the performance of the external agent, including any conflicts of interest it may have.<sup>10</sup> Any actual or potential conflicts of interest involving a member of the Board, officer or key employee of the Organization with respect to the external agent must be disclosed and resolved pursuant to the Organization's Conflicts of Interest and Related Party Transactions Policy. Any contract between the Organization and an external agent involving delegation of investment authority shall be terminable by the Organization at any time, without penalty, upon no more than 60 days' notice.<sup>11</sup>

The [Board][Committee] shall review from time to time the Organization's arrangements with *[insert external agents, such as banks and other financial entities]* with which it maintains the Financial Assets. The [Board][Committee] will review, among other factors, the appropriateness of the costs and fees associated with such *[insert relevant relationship/instruments, such as accounts and any other relevant consideration for whether costs are appropriate and reasonable in relation to the Financial Assets, the purposes of the Organization and the skills available to the Organization]*.

#### **C. Endowment Funds**

The [Board][Committee] will manage the endowment funds of the Organization in accordance with applicable law. An "endowment fund" means an institutional fund, or part thereof, that under the terms of a gift instrument is not wholly expendable by the Organization on a current basis.<sup>12</sup>

Subject to the express intent of the donor, the [Board][Committee] may in good faith appropriate for expenditure so much of the endowment fund as the [Board][Committee] determines is prudent. When deciding whether to use funds from an endowment fund, the [Board][Committee] will consider in the following factors, to the extent relevant, as required by applicable law:

1. the short- and long-term needs of the Organization;
2. duration and preservation of the endowment fund;
3. the purposes of the Organization and the endowment fund;
4. general economic conditions;
5. the possible effect of inflation or deflation;
6. the expected total return from income and the appreciation of investments;

7. other resources of the Organization;
8. where appropriate and circumstances would otherwise warrant, alternatives to spending from the endowment fund, giving due consideration to the effect such alternatives may have on the Organization; and
9. this Investment Policy.<sup>13</sup>

Each time the [Board][Committee] authorizes or approves the use of an endowment fund, the Organization will make a contemporaneous written record describing the factors taken into consideration with respect to such use.<sup>14</sup>

Endowment funds that are subject to similar or identical restrictions may be considered as a group.

The [Board][Committee] will, from time to time as necessary, review the financial needs of the Organization to determine the appropriate investment, expenditure and replenishment of the endowment funds.

To the extent, the [Board][Committee] deems it necessary and appropriate to modify or lift certain donor-imposed restrictions on the management or investment of the Organization's funds, it will do so in accordance with applicable law, for example, by seeking the written consent or approval from the donor or a court with jurisdiction over the matter, or by notifying the Attorney General of the State of New York.<sup>15</sup>

#### **D. Review of Investment Policy**

The [Board][Committee] will review and amend this Investment Policy from time to time as necessary to reflect developments affecting the Organization's finances and activities.<sup>16</sup>

ENDNOTES

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<sup>1</sup> N-PCL § 552(b).

<sup>2</sup> N-PCL § 551(d) defines an “institution” as: “(1) a person, other than an individual, organized and operated exclusively for charitable purposes; (2) a trust that had both charitable and noncharitable interests, after all noncharitable interests have terminated; or (3) any corporation described in subparagraph five of paragraph (a) of section 102 (Definitions).”

<sup>3</sup> The NYPMIFA sets forth procedures whereby certain donor-imposed restrictions on the management or investment of institutional funds may be lifted. A not-for-profit organization “may release or modify, in whole or in part, a restriction contained in a gift instrument on the management, investment, or purpose of an institutional fund” if it receives the donor’s written consent. A release or modification may not allow a fund to be used for a purpose other than a charitable purpose of the institution. *See* N-PCL § 555(a). If the donor is available and withholds such consent, or if the donor is not available, an institution may seek court approval to release or modify a restriction regarding the management or investment of an institutional fund “if the restriction has become impracticable or wasteful, if it impairs the management or investment of the fund, or if, because of circumstances not anticipated by the donor, a modification of a restriction will further the purposes of the fund... To the extent practicable, any modification must be made in accordance with the donor’s probable intention.” N-PCL § 555(b).

A not-for-profit organization may also seek the donor’s written consent or court approval to modify or release a purpose or restriction on the use of an institutional fund if such purpose or restriction becomes “unlawful, impracticable, impossible to achieve, or wasteful.” N-PCL § 555(c). The organization must notify the donor, if available, and the attorney general of the application to the court and the attorney general and such donor must be given an opportunity to be heard. Under the N-PCL, the executors or heirs of a deceased donor are excluded from the definition of “donor” in N-PCL § 551(a-1) and are therefore not entitled to notice.

If an institution determines that a donor-imposed restriction contained in a gift instrument on the management, investment, or purpose of an institutional fund is “unlawful, impracticable, impossible to achieve, or wasteful,” the NYPMIFA provides a procedure for modifying or releasing such a restriction. To implement such a procedure, (i) the fund must be less than \$100,000 in value, (ii) the fund must have been in existence for more than 20 years, (iii) the institution must use the property in a manner consistent with the purposes expressed in the gift instrument and (iv) the institution must notify the attorney general (and, under certain circumstances, the donor, if available) of its determination regarding the donor-imposed restriction. If there has been no notification in response from the attorney general after 90 days, the institution may proceed with the release or modification of such restriction. *See* N-PCL § 555(d).

<sup>4</sup> N-PCL § 552(f).

<sup>5</sup> Although the board is ultimately responsible for the management and investment of the not-for-profit’s assets in accordance with the NYPMIFA, the board may delegate “management and investment functions to its committees, officers, or employees.” *See* N-PCL § 554(f). This sample investment policy contemplates the Board is delegating the management and investment functions to a committee, but any reference in this policy to such committee’s role and responsibilities may be changed to the Board.

<sup>6</sup> The standard of conduct for each person responsible for managing and investing an institutional fund is to “comply[] with the duty of loyalty imposed by law” and to “manage and invest the fund in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstances.” N-PCL § 552(b). To satisfy the standard of prudence, the NYPMIFA sets forth basic requirements, such as a requirement that an institution make a reasonable effort to verify facts relevant to the management and investment of the fund, and that an institution only incur costs that are reasonable and appropriate. N-PCL § 552(c). The NYPMIFA creates “a rebuttable presumption of imprudence” for any endowment gifts made after September 17, 2010, the effective date of the NYPMIFA as follows: “The appropriation for expenditure in any year of an amount greater than seven percent of the fair market value of an endowment fund, calculated on the basis of market values determined at least quarterly and averaged over a period of not less than five years immediately preceding the year in which the appropriation for expenditure is made, creates a rebuttable presumption of imprudence. For an endowment fund in existence for fewer than five years, the fair market value of the endowment fund must be calculated for the period the endowment fund has been in existence. This subsection does not: (1) apply to an appropriation for expenditure permitted under law other than the chapter of the laws of 2010 that enacted this article or by the gift instrument; or (2) create a presumption of prudence for an appropriation for expenditure of an amount less than or equal to seven percent of the fair market value of the endowment fund.” N-PCL § 553(d).

<sup>7</sup> “Except as otherwise provided by a gift instrument... [a]n institution shall diversify the investments of an institutional fund unless the institution prudently determines that, because of special circumstances, the purposes of the fund are better served without diversification. An institution shall review a decision not to diversify as frequently as circumstances require, but at least annually.” N-PCL § 552(e)(4).

<sup>8</sup> When managing and investing an institutional fund, the NYPMIFA provides that, except as otherwise provided by a gift instrument, these factors must be considered, if relevant:

- (A) “general economic conditions;
- (B) the possible effect of inflation or deflation;
- (C) the expected tax consequences, if any, of investment decisions or strategies;
- (D) the role that each investment or course of action plays within the overall investment portfolio of the fund;
- (E) the expected total return from income and the appreciation of investments;
- (F) other resources of the institution;
- (G) the needs of the institution and the fund to make distributions and to preserve capital; and
- (H) an asset’s special relationship or special value, if any, to the purposes of the institution.” N-PCL § 552(e)(1).

<sup>9</sup> The NYPMIFA permits an institution to “delegate to an external agent the management and investment of an institutional fund to the extent that an institution could prudently delegate under the circumstances.” N-PCL § 554(a). An institution must act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances when “(1) selecting, continuing or terminating an agent, including assessing the agent’s independence including any conflicts of interest such agent has or may have; (2) establishing the scope and terms of the delegation, including the payment of compensation, consistent with the purposes of the institution and the institutional fund; and (3) monitoring the agent’s performance and compliance with the scope and terms of the delegation.” N-PCL § 554(a).

When performing a delegated function, an external agent “owes a duty to the institution to exercise reasonable care, skill and caution to comply with the scope and terms of the delegation.” N-PCL § 554(b).

<sup>10</sup> The NYPMIFA requires that the board or a board committee must assess the independence of any external agent – both before and after retaining them to manage and invest institutional funds. The selection of external agents should not be based on any business or personal relationships between the agent and board members or other insiders, but rather the criteria should be the external agent’s competence, experience, past performance and proposed compensation. The board or board committee should consider whether any business or personal relationship with an external agent would reasonably be expected to interfere with the ability of the board or board committee to provide proper oversight. The board or board committee may also refer to the organization’s conflicts of interest policy when considering the external agent’s independence. *See* N-PCL § 554(a)(1).

<sup>11</sup> Any contract delegating the management and investment of an institutional fund to an external agent must “provide that it may be terminated by the institution at any time, without penalty, upon not more than sixty days’ notice.” N-PCL § 554(e).

<sup>12</sup> As defined in the N-PCL, “[e]ndowment fund” means an institutional fund or part thereof that, under the terms of a gift instrument, is not wholly expendable by the institution on a current basis. The term does not include assets that an institution may designate as an endowment fund for its own use, consistent with the terms of the applicable gift instrument.” N-PCL § 551(b).

<sup>13</sup> “Unless stated otherwise in the gift instrument, the assets in an endowment fund are donor-restricted” until the institution determines to appropriate such funds for expenditure by the institution. N-PCL § 553(a). When deciding whether to use funds from an endowment fund, “the institution shall act in good faith, with the care that an ordinarily prudent person in a like position would exercise under similar circumstances” and shall consider, if relevant, the following factors:

- (1) “the duration and preservation of the endowment fund;
- (2) the purposes of the institution and the endowment fund;
- (3) general economic conditions;
- (4) the possible effect of inflation or deflation;
- (5) the expected total return from income and the appreciation of investments;
- (6) other resources of the institution;
- (7) where appropriate and circumstances would otherwise warrant, alternatives to expenditure of the endowment fund, giving due consideration to the effect that such alternatives may have on the institution; and
- (8) the investment policy of the institution.” N-PCL § 553(a).

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<sup>14</sup> “For each determination to appropriate for expenditure, the institution shall keep a contemporaneous record describing the consideration that was given by the governing board to each of the factors enumerated in this paragraph.” N-PCL § 553(a).

<sup>15</sup> The analysis and procedures set forth in N-PCL § 555 to modify or lift donor-imposed restrictions on institutional funds is complex. *See* note 2 above. Please consult with your advisors.

<sup>16</sup> Each institution must “adopt a written investment policy setting forth guidelines on investments and delegation of management and investment functions” pursuant to the NYPMIFA. N-PCL § 552(f).

## Not-For-Profit Practice Group

### Sample Not-For-Profit Conflicts of Interest and Related Party Transactions Policy

#### *Conflicts of Interest*

The board of a not-for-profit organization should as a best practice (even if not required to) adopt a conflicts of interest policy to assist the directors, officers and others in the organization in identifying, evaluating and resolving conflicts of interest.

The organization, its directors and its officers may be subject to liability, and the organization's tax-exempt status may be at risk, if the organization enters into transactions that result in improper financial benefit to persons affiliated with the organization. In addition, since July 1, 2014, the Non-Profit Revitalization Act of 2013 (as amended, the "Revitalization Act") has required that all New York not-for-profits adopt a conflicts of interest policy that meets certain requirements, and that certain review and approval procedures be applied with respect to "related party transactions" as defined in the Revitalization Act. If a corporation had previously adopted a conflicts of interest policy substantially consistent with the provisions of the Revitalization Act, such corporation was deemed to be in compliance with this requirement. The Internal Revenue Service ("IRS") requires tax-exempt organizations to disclose on their Form 990 whether they have a conflicts of interest policy that meets certain requirements. This sample provides only one example for an organization, incorporating elements required by the Revitalization Act, which amended the New York Not-for-Profit Corporation Law (the "N-PCL"), as well as elements related to certain IRS disclosure requirements and is designed to be used in conjunction with a code of conduct and ethics that further describes the policies and values of the organization.

#### *Related Party Transactions*

This sample provides a single set of procedures applicable to all types of conflicts of interest, which include but are not limited to "related party transactions" as defined in the N-PCL. In particular, this sample policy includes additional requirements for "charitable corporations," where a related party has a "substantial financial interest" in a proposed transaction, as recommended best practices applicable to all conflicts. This sample also includes questionnaires relating to conflicts and director independence (for N-PCL audit oversight requirements).

The N-PCL provides that the New York Attorney General may bring an action to enjoin, void or rescind related party transactions or proposed related party transactions that have been entered into, or would be entered into, without complying with applicable procedural requirements and/or that are not reasonable and/or were not in the best interests of the organization at the time of approval, as well as to, among other things, remove directors or officers, order an account of profits, payment for the value of the use of property or assets used in the transaction, or the return of lost assets, payment of double the amount of certain improperly obtained benefits, or seek restitution.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms, and applicable requirements of local, regional or national law) may affect the provisions that should be included. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

It should also be noted that Section 8-1.9 of New York's Estates, Powers and Trusts Law makes applicable to charitable trusts a number of sections of the N-PCL, including the provisions addressing related party transactions and conflicts of interest policies.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Conflicts of Interest and Related Party Transactions Policy<sup>1</sup>

#### I. PURPOSE

All directors, officers and staff owe a duty of loyalty to [●] (the “Organization”) and must act in good faith toward the Organization and in the Organization’s best interests, rather than in their own interests or the interests of another entity or person and must comply with applicable legal requirements. The purpose of this Conflicts of Interest and Related Party Transactions Policy (this “Policy”) is to provide guidance in identifying and handling potential and actual conflicts of interest and related party transactions, as specified in this Policy.

#### II. CONFLICTS OF INTEREST

A conflict of interest arises whenever the interests of the Organization come into conflict with a financial or personal interest of a Covered Person, or otherwise whenever a Covered Person’s personal or financial interest could be reasonably viewed as affecting his or her objectivity or independence in fulfilling their duties to the Organization.

This Policy applies to any person who is a director, officer or key person (as defined below)[, and any other employee, volunteer, independent contractor of or substantial contributor to, the Organization]<sup>2</sup>, (collectively, the “Covered Persons”).

A “key person” is a person, other than a director or officer, whether or not an employee of the Organization who (i) has responsibilities, or exercises powers or influence over the Organization as a whole similar to the responsibilities, powers or influence of directors and officers; (ii) manages the Organization, or a segment of the Organization that represents a substantial portion of the activities, assets, income or expenses of the Organization; or (iii) alone or with others controls or determines a substantial portion of the Organization’s capital expenditures or operating budget.<sup>3</sup>

While it is not possible to describe or anticipate all the circumstances that might involve a conflict of interest, a conflict of interest typically arises whenever a Covered Person has (directly or indirectly) through a relative (as defined below), an entity that such person controls (a “Controlled Entity”), or otherwise has<sup>4</sup>:

1. an interest (financial or otherwise) in a transaction, agreement or any other arrangement in which the Organization participates that may impair such person’s objectivity;
2. a compensatory arrangement or other interest in a transaction with the Organization (other than compensation for service on the Board of Directors (the “Board”) or as a result of being employed by the Organization);
3. a compensatory arrangement or other interest in or affiliation with any entity or individual that: (i) sells goods or services to, or purchases goods or services from, the Organization; (ii) competes with the Organization; or (iii) the Organization has, or is negotiating or contemplating negotiating, any other transaction or arrangement with;
4. the ability to use their position, or confidential information or the assets of the Organization, to their (or a relative’s or Controlled Entity’s) personal advantage or for an improper or illegal purpose;

5. solicited or accepted any gift, entertainment or other favor where such gift might create the appearance of influence on such Covered Person (other than gifts of nominal value, which are clearly tokens of respect and friendship unrelated to any particular transaction);
6. indebtedness to the Organization (other than ordinary business expenses or transactions);<sup>5</sup>
7. acquired any property or other rights in which the Organization has, or the Covered Person knows or has reason to believe at the time of acquisition that the Organization is likely to have, an interest;
8. an opportunity related to the activities of the Organization arises for the Covered Person, unless the [Board] [Audit Committee] has made an informed decision that the Organization will not pursue that opportunity; or
9. any other circumstance that may, in fact or in appearance, make it difficult for the Covered Person to exercise independent, objective judgment or otherwise perform effectively.

Each director, officer and key person is required to disclose in good faith [and in writing]<sup>6</sup> to the [Board] [Audit Committee] at [insert contact information]<sup>7</sup> all material facts related to an actual or potential conflict of interest. [All other Covered Persons should disclose an actual or potential conflict of interest in writing to their supervisor or executive director, as applicable.]<sup>8</sup> Disclosures should be made in advance, before any action is taken on the matter. Conflict identification and analysis can be difficult and, therefore, you are at all times expected to err on the side of caution and disclose all instances where a conflict of interest or the appearance of a conflict exists.

#### *Conflicts of Interest Questionnaire*

Each director [, officer and key person]<sup>9</sup> must submit to the Secretary of the Organization or a designated compliance officer upon joining the Organization and at least once per year thereafter (and updated as appropriate) a questionnaire substantially in the form of the Appendix to this Policy. The Secretary of the Organization or the designated compliance officer shall provide copies of all completed questionnaires to the Chair of the [Board] [Audit Committee].

### **III. RELATED PARTY TRANSACTIONS**

A “Related Party Transaction” is any transaction, agreement or any other arrangement in which a Related Party (defined below) has a financial interest and in which the Organization or any “affiliate” of the Organization (meaning any entity controlled by, or in control of, the Organization) is a participant. A transaction shall not be a Related Party Transaction if: (i) the transaction or the Related Party’s financial interest in the transaction is de minimis, (ii) the transaction would not customarily be reviewed by the Board, or boards of similar organizations, in the ordinary course of business and is available to others on the same or similar terms, or (iii) the transaction constitutes a benefit provided to a Related Party solely as a member of a class of the beneficiaries that the Organization intends to benefit as part of the accomplishment of its mission which benefit is available to all similarly situated members of the same class on the same terms.<sup>10</sup>

A “Related Party” is an individual who is [or was in the last five years]<sup>11</sup> (i) a director, officer or key person of the Organization or any affiliate of the Organization; (ii) any relative of any individual described in the foregoing clause (i); or (iii) any entity in which any individual described in the foregoing clauses (i) and (ii) 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%.<sup>12</sup> A “relative” is a (i) spouse or domestic partner; (ii) ancestor, child (whether natural or adopted), grandchild, great-grandchild, sibling (whether whole- or half-blood); or (iii) spouse or domestic partner of a child (whether natural or adopted), grandchild, great-grandchild or sibling (whether whole- or half-blood).<sup>13</sup>

The Organization shall not enter into any Related Party Transaction unless the transaction is determined by the [Board] [Audit Committee] to be fair, reasonable and in the Organization's best interests at the time of such determination. Any director, officer or key person who has an interest in a Related Party Transaction shall disclose in good faith to the [Board] [Audit Committee] the material facts concerning such interest. In addition, certain Related Party Transactions are required to be disclosed in the notes to the Organization's audited financial statements and its annual federal tax filing on Form 990.

#### **IV. REVIEW, APPROVAL AND RATIFICATION<sup>14</sup>**

The [Board] [Audit Committee] will review all conflicts of interest and Related Party Transactions and determine whether to approve or ratify any such matters. In making its determination, the [Board] [Audit Committee] will consider, without limitation:

1. Alternative or comparable transactions to the extent available;<sup>15</sup>
2. The Organization's mission and resources;
3. The possibility of creating an appearance of impropriety that might impair the confidence in, or the reputation of, the Organization (even if there is no actual conflict or wrongdoing); and
4. Whether the conflict may result in any private inurement, excess benefit transaction or impermissible private benefit under laws applicable to tax-exempt organizations.

Persons with an interest in any matter under review by the [Board] [Audit Committee] are not permitted to be present at or participate in any deliberations or voting by the [Board] [Audit Committee] with respect to the matter giving rise to the potential conflict, and must not attempt to influence improperly the deliberation or voting on such matter. In appropriate circumstances, any such person may be called upon to provide information and answer questions relevant to the determination prior to the commencement of deliberations or voting related thereto.<sup>16</sup> Notwithstanding the foregoing, a director with an interest in a matter under review by the [Board] [Audit Committee] shall be deemed to be present at the meeting for purposes of determining whether a quorum is present.

In the event the Organization and/or a Covered Person in error enters into or otherwise participates in a conflict of interest or Related Party Transaction that requires pre-approval by the [Board] [Audit Committee] pursuant to this Policy, such transaction shall promptly upon discovery of such error be presented to the [Board] [Audit Committee] for its review and the [Board] [Audit Committee] shall in accordance with the procedures prescribed by applicable law consider whether to (i) ratify such transaction; (ii) direct the rescission or modification of the transaction (if possible to do so); (iii) take any disciplinary action; and/or (iv) make changes to the Organization's controls and procedures in connection with such error.<sup>17</sup>

#### **V. RECORDS**

The minutes of the [Board] [Audit Committee] meeting during which a potential or actual conflict of interest, or Related Party Transaction is disclosed or discussed shall be documented contemporaneously with the meeting and reflect the name of the interested Covered Person, the nature of the conflict, and details of the deliberations of the disinterested directors (such as documents reviewed, any alternatives or comparable transactions considered, comparative costs or bids, market value information and other factors considered in deliberations), and the names of the persons who were present for the discussion and votes relating to the transaction or arrangement, and the resolution of the conflict including any ongoing procedures to manage any conflict that was approved.<sup>18</sup> The interested person shall only be informed of the final decision and not of particular directors' positions or how they voted.

## **VI. COMPLIANCE**

If the [Board] [Audit Committee] has reasonable cause to believe that a person covered by this Policy has failed to comply with this Policy, it may make such further investigation as may be warranted in the circumstances and if it determines that such person has failed to comply with this Policy, it shall take appropriate action which may include, in the case of directors and officers, removal from the Board or from office in accordance with the Bylaws or, in the case of key persons or others, termination of employment or other relationship with the Organization or an affiliate.

## **VII. POLICY ADOPTION AND OVERSIGHT<sup>19</sup>**

The Board is responsible for providing oversight of the adoption and implementation of, and compliance with this Policy.<sup>20</sup>

This Conflicts of Interest and Related Party Transactions Policy was adopted by the Board on [month] [day], [year].

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Questionnaire Concerning Conflicts of Interest for Directors [and], Director Nominees, [Officers and Key Persons]<sup>21</sup>

You are required to answer the questions below to the best of your knowledge and belief.

- Please identify any and all entities of which you are an officer, director, trustee, member, owner (either as a sole proprietor or a partner or, if in a partnership or professional corporation, in which you have a 5% ownership interest) or employee and with which \_\_\_\_\_ (the “Organization”) has a relationship:

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- Please identify any and all transactions in which the Organization is a participant and in which you have or might have a financial or other personal interest:

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- Please confirm whether you or any “relative” (as defined in the Conflicts of Interest and Related Party Transactions Policy), have or have engaged in, or whether you know of any other “Covered Person” (as defined in the Conflicts of Interest and Related Party Transactions Policy) that has or has engaged in, any of the following (other than matters already fully disclosed, evaluated and resolved):

	Yes	No
1. a direct or indirect interest (financial or otherwise) in a transaction, agreement or any other arrangement and in which the Organization or any affiliate participates that may impair such person’s objectivity.		
2. a compensation arrangement or other similar interest in a transaction with the Organization (other than, with respect to key persons, your salary as an employee with the Organization or for Board service).		
3. a compensation arrangement or other interest in or affiliation with any entity or individual that: (a) sells goods or services to, or purchases goods or services from, the Organization; (b) competes with the Organization; or (c) the Organization has, or is negotiating, or contemplating negotiating, any other transaction or arrangement with.		
4. used your/their position, or confidential information or the assets of the Organization to your/their (or an affiliated party’s or relative’s) personal advantage or for an improper or illegal purpose.		
5. solicited or accepted any gift, entertainment or other favor where such gift might create the appearance of influence on you/them (other than gifts of nominal value, which are clearly tokens of respect and friendship unrelated to any particular transaction).		

	Yes	No
6. indebtedness to the Organization, other than for amounts due for ordinary travel and expense advances.		
7. acquired any property or other rights in which the Organization has, or you/they know or have reason to believe at the time of acquisition that the Organization is likely to have, an interest.		
8. an opportunity related to the activities of the Organization that is available to the Organization or to you/them, unless the [Board][Audit Committee] has made an informed decision that the Organization will not pursue that opportunity.		
9. any other circumstances that may, in fact or in appearance, make it difficult for you/them to exercise independent, objective judgment or otherwise perform effectively.		

If “yes” to any of the above, please describe the relevant facts (attach a separate sheet if necessary):

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**Certification**

I also acknowledge that I have received a copy of, read and understood the Conflicts of Interest and Related Party Transactions Policy of the Organization and agree that I have adhered and will continue to adhere to such policy.

Additionally, I understand that in order to maintain its federal tax exemption the Organization must engage primarily in activities that accomplish one or more of its tax exempt purposes.

Date: \_\_\_\_\_

Signature: \_\_\_\_\_

Printed  
 Name: \_\_\_\_\_

Questionnaire Concerning Director Independence for Audit Oversight<sup>22</sup>

You are required to answer the questions below to the best of your knowledge and belief.

	Yes	No
1. Have you been an employee or “key person” (as defined in the Conflicts of Interest and Related Party Transactions Policy) of the Organization or an “affiliate” (as defined in the Conflicts of Interest and Related Party Transactions Policy) <sup>23</sup> of the Organization within the last three years?		
2. Do you have a “relative” (as defined in the Conflicts of Interest and Related Party Transactions Policy) who has been a key person of the Organization or an affiliate of the Organization within the last three years?		
3. Have you received and/or do you have a relative who has received more than \$10,000 in direct compensation from the Organization or an affiliate of the Organization in any of the last three fiscal years (not including reimbursement of expenses reasonably incurred as a director or reasonable compensation for services as a director)?		
4. Do you have a financial interest in, and/or are you an employee of, any entity that has provided payments, property or services to or received payments, property or services from, the Organization or an affiliate of the Organization in the last three fiscal years that exceeded: (i) the lesser of \$10,000 or 2% of such entity’s consolidated gross revenues if the entity’s consolidated gross revenue was less than \$500,000; (ii) \$25,000 if the entity’s consolidated gross revenue was \$500,000 or more but less than \$10 million; or (iii) \$100,000 if the entity’s consolidated gross revenue was \$10 million or more? If so, what is or was the nature of your financial interest or relationship?		
5. Do you have a relative who has a financial interest in, and/or who is an officer of, any entity that has provided payments, property or services to or received payments, property or services from, the Organization or an affiliate of the Organization in the last three fiscal years that exceeded: (i) the lesser of \$10,000 or 2% of such entity’s consolidated gross revenues if the entity’s consolidated gross revenue was less than \$500,000; (ii) \$25,000 if the entity’s consolidated gross revenue was \$500,000 or more but less than \$10 million; or (iii) \$100,000 if the entity’s consolidated gross revenue was \$10 million or more? If so, what is or was the nature of your relative’s financial interest or relationship?		
6. Are you a current owner, whether wholly or partially, director, officer or employee of the Organization’s outside auditor or an entity that worked on the Organization’s audit at any time during the past three years?		
7. Do you have a relative who is a current owner, whether wholly or partially, director, officer or employee of the Organization’s outside auditor or an entity that has worked on the Organization’s audit at any time during the past three years?		

If “yes” to any of the above, please describe the relevant facts (attach a separate sheet if necessary):

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Date: \_\_\_\_\_

Signature: \_\_\_\_\_

Printed  
Name: \_\_\_\_\_

## ENDNOTES

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<sup>1</sup> The N-PCL requires every New York not-for-profit corporation (regardless of size) to adopt a conflicts of interest policy applicable to directors, officers and “key person(s)” (as defined in the N-PCL). The N-PCL requires that such policy, among other things: (i) define the circumstances that constitute a conflict of interest; (ii) include procedures for disclosing a conflict of interest or possible conflict of interest to a committee of the board or to the board, and procedures for a committee of the board or the board to determine whether a conflict exists; (iii) require that the person with the conflict not be present at or participate in board or committee deliberation or vote on the matter giving rise to such conflict (although a person with a conflict is allowed to present information and answer questions prior to the commencement of deliberations or voting); (iv) prohibit any attempt by the person with the conflict to influence improperly the deliberation or voting on the matter giving rise to such conflict; (v) require that the existence and resolution of the conflict be documented in the corporation’s records, including in the relevant minutes of meeting; (vi) include procedures for disclosing, addressing and documenting related party transactions; and (vii) require directors to disclose to the corporation (prior to initial election and annually thereafter) any entities with which they are affiliated and with which the corporation has a relationship, and any transactions in which the corporation is a participant and in which the director might have a conflicting interest. If a corporation’s board of directors has adopted a conflict of interest policy that is substantially consistent with the provisions of the N-PCL, such corporation is deemed to be in compliance with the N-PCL’s conflict of interest policy requirements. *See* N-PCL § 715-a. *See also* State of New York Attorney General’s Charities Bureau Guidance Document, “Conflicts of Interest Policies Under the Not-for-Profit Corporation Law” (September 2018), available at [https://ag.ny.gov/sites/default/files/regulatory-documents/Charities\\_Conflict\\_of\\_Interest.pdf](https://ag.ny.gov/sites/default/files/regulatory-documents/Charities_Conflict_of_Interest.pdf).

The N-PCL includes definitions and requires specific procedures to be adhered to with respect to “related party transactions.” A “related party transaction” is defined to mean any transaction, agreement or any other arrangement in which a “related party” (defined below) has a financial interest and in which the corporation or any affiliate of the corporation is a participant, except that a transaction shall not be a related party transaction if: (i) the transaction or the related party’s financial interest in the transaction is de minimis; (ii) the transaction would not customarily be reviewed by the board, or boards of similar organizations, in the ordinary course of business and is available to others on the same or similar terms; or (iii) the transaction constitutes a benefit provided to a related party solely as a member of a class of the beneficiaries that the corporation intends to benefit as part of the accomplishment of its mission which benefit is available to all similarly situated members of the same class on the same terms. *See* N-PCL §102(a)(24). A “related party” is defined to mean (i) any director, officer or key person of the corporation or any affiliate of the corporation; (ii) any relative of any individual described in the foregoing clause (i); or (iii) any entity in which any individual described in the foregoing clauses (i) and (ii) 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%. *See* N-PCL § 102(a)(23). The N-PCL provides that “[n]o corporation shall enter into any related party transaction unless the transaction is determined by the board, or an authorized committee thereof, to be fair, reasonable and in the corporation’s best interest at the time of such determination. Any director, officer or key person who has an interest in a related party transaction shall disclose in good faith to the board, or an authorized committee thereof, the material facts concerning such interest. With respect to any related party transaction involving a charitable corporation and in which a related party has a substantial financial interest, the board of such corporation, or an authorized committee thereof, shall: (1) prior to entering into the transaction, consider alternative transactions to the extent available; (2) approve the transaction by not less than a majority vote of the directors or committee members present at the meeting; and (3) contemporaneously document in writing the basis for the board or authorized committee’s approval, including its consideration of any alternative transactions.” N-PCL § 715(a)-(b).

<sup>2</sup> If the Organization does not have a stand-alone conflicts of interest policy for employees and other relevant persons (such as volunteers, independent contractors or substantial contributors), then consider covering such persons in this policy.

<sup>3</sup> *See* N-PCL § 102(a)(25).

<sup>4</sup> This list should be used as guidance and can be revised pursuant to the rules of the Organization.

<sup>5</sup> The N-PCL prohibits loans (other than through the purchase of bonds, debentures, or similar obligations of the type customarily sold in public offerings, or through ordinary deposit of funds in a bank) by a corporation to its directors, officers or key persons, or to any other corporation, firm, association or other entity in which one or more of its directors, officers or key persons are directors, officers or key persons or hold a substantial financial interest, except a loan by one charitable corporation to another charitable corporation. N-PCL § 716.

<sup>6</sup> The N-PCL does not require written disclosure of conflicts, however, this is recommended as a best practice.

<sup>7</sup> The N-PCL requires that conflicts of interest, or potential conflicts of interests, be disclosed to the board or to a committee of the board, which can then determine whether a conflict does indeed exist. N-PCL § 715-a(b)(2).

<sup>8</sup> The N-PCL does not require disclosure of conflicts by people other than directors, officers and key persons, but the Organization can choose to broaden the disclosure requirement for the particular Organization.

<sup>9</sup> Although N-PCL § 715-a states that the conflicts of interest policy should apply to directors, officers and key persons, the provision requiring the submission of the questionnaire only addresses directors. Consider as a best practice maintaining the more expansive application of the annual disclosure requirement in order to capture conflicts involving directors, officers and key persons.

<sup>10</sup> See N-PCL §102(a)(24).

<sup>11</sup> The N-PCL does not require a 5-year look-back. Under the tax law applicable to public charities, however, the “excess benefit transaction” rule that focuses on related party transactions does have a 5-year look-back in determining who is a “related party.” Since, as a general proposition, private not-for-profit organizations may be subject to even greater tax scrutiny than public charities, they may consider it prudent to adopt the 5-year look-back approach with respect to the scope of their conflict of interest and related party transaction policy. See Section 4958(f) of the Internal Revenue Code.

<sup>12</sup> See N-PCL § 102(a)(23).

<sup>13</sup> See N-PCL § 102(a)(22). “Domestic partner” has the meaning ascribed to such term in Section 2994-a(7) of the New York Public Health Law, where it is defined to mean “a person who, with respect to another person: (a) is formally a party in a domestic partnership or similar relationship with the other person, entered into pursuant to the laws of the United States or of any state, local or foreign jurisdiction, or registered as the domestic partner of the other person with any registry maintained by the employer of either party or any state, municipality or foreign jurisdiction; or (b) is formally recognized as a beneficiary or covered person under the other person’s employment benefits or health insurance; or (c) is dependent or mutually interdependent on the other person for support, as evidenced by the totality of the circumstances indicating a mutual intent to be domestic partners including but not limited to: common ownership or joint leasing of real or personal property; common householding, shared income or shared expenses; children in common; signs of intent to marry or become domestic partners under paragraph (a) or (b) . . . ; or the length of the personal relationship of the persons.” New York Public Health Law § 2994-a(7).

<sup>14</sup> The procedures in Section IV incorporate the additional requirements for “charitable corporations” (as defined by the N-PCL § 102(a)(3-a)), where a related party has a “substantial financial interest” in a proposed transaction, as a best practice. See note 1.

<sup>15</sup> N-PCL § 715(b)(1) only requires the board or a committee to consider alternative transactions to the extent available, however, other criteria suggested are in line with best practices.

<sup>16</sup> See N-PCL § 715-a(b)(3) and § 715(h).

<sup>17</sup> In an action by any person or entity other than the attorney general, it shall be a defense to a claim of violation of any provisions of N-PCL § 715 that a transaction was fair, reasonable and in the corporation’s best interest at the time the corporation approved the transaction. See N-PCL § 715(i).

In an action by the attorney general with respect to a related party transaction not approved in accordance with paragraphs (a) or (b) of N-PCL § 715 at the time it was entered into, whichever is applicable, it shall be a defense to a claim of violation of any provisions of N-PCL § 715 that (1) the transaction was fair, reasonable and in the corporation’s best interest at the time the corporation approved the transaction and (2) prior to receipt of any request for information by the attorney general regarding the transaction, the board has: (A) ratified the transaction by finding in good faith that it was fair, reasonable and in the corporation’s best interest at the time the corporation approved the transaction; and, with respect to any related party transaction involving a charitable corporation and in which a related party has a substantial financial interest, considered alternative transactions to the extent available, approving the transaction by not less than a majority vote of the directors or committee members present at the meeting; (B) documented in writing the nature of the violation and the basis for the board’s or committee’s ratification of the transaction; and (C) put into place procedures to ensure that the corporation complies with paragraphs (a) and (b) of N-PCL § 715 as to related party transactions in the future. See N-PCL § 715(j).

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<sup>18</sup> The N-PCL requires that the existence and resolution of the conflict be documented in the corporation's records, including in the minutes of any meeting at which the conflict was discussed or voted upon. *See* N-PCL § 715-a(b)(5).

<sup>19</sup> IRS Form 990 requires disclosure of whether the organization has a conflicts of interest policy. The federal tax law (and IRS Form 990) does not require that an organization have a conflicts policy; however, the IRS believes that the absence of a conflicts policy is a factor suggesting substandard corporate governance, which (the IRS maintains) may lead to violation of tax law principles applicable to exempt organizations, and therefore warrants heightened scrutiny. *See* IRS Form 990, Part VI, Lines 12a-c and related instructions. Appendix A to the instructions to IRS Form 1023 (Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code) includes a sample conflicts of interest policy; the N-PCL requirements for such a policy are more stringent than those set forth in the IRS sample policy.

<sup>20</sup> The N-PCL requires that the board oversee the adoption, implementation of, and compliance with the conflicts of interest policy to ensure that its directors, officers and key persons act in the corporation's best interest and comply with applicable legal requirements (although committees of the board may help to resolve actual or potential conflicts). *See* N-PCL § 715-a(a).

<sup>21</sup> The N-PCL requires that each director must complete (prior to the director's initial election and annually thereafter), sign and submit to the secretary of the corporation or a designated compliance officer a written statement identifying, to the best of the director's knowledge, any entity of which such director is an officer, director, trustee, member, owner (either as a sole proprietor or a partner) 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. The secretary of the corporation or the designated compliance officer must provide a copy of all completed statements to the chair of the audit committee or, if there is no audit committee, to the chair of the board. *See* N-PCL § 715-a(c). This form suggests that you can send to directors as well as director nominees, officers and key persons, however pursuant to the rule, only directors are required to complete such statement.

<sup>22</sup> *See* N-PCL § 102(a)(21) for the definition of "independent director." Note that certain conflicts of interest and/or related party transactions may impact director independence.

<sup>23</sup> Consider including a list of affiliates in a schedule to the questionnaire.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Whistleblower Policy

The board of a not-for-profit organization should establish a whistleblower policy that encourages individuals to report in good faith violations of law or policies of the organization, specifies that the organization will protect the individual from retaliation and identifies the parties to whom such information can be reported. Each organization must also decide what reporting mechanisms will best balance the organization's valid interests in promoting the internal reporting of concerns about conduct and ethics, achieving efficiency in the use of resources for compliance efforts and preserving attorney-client privilege.

Tax-exempt organizations are required to disclose on their Form 990 whether a whistleblower policy has been adopted, and since July 1, 2014, the Non-Profit Revitalization Act of 2013 (as amended, the "Revitalization Act") applicable to New York not-for-profits has required that certain not-for-profit organizations (those with 20 or more employees and annual revenue above \$1 million) have a whistleblower policy. The New York Not-for-Profit Corporation Law (the "N-PCL"), as amended by the Revitalization Act, requires that the whistleblower policy be adopted and overseen (both in terms of its implementation and compliance therewith) by the not-for-profit corporation's board. Note that an organization that has adopted and possesses a whistleblower policy pursuant to federal, state or local laws that is substantially consistent with the relevant provisions of the N-PCL will be deemed by the N-PCL to be in compliance with this requirement. This sample provides only one example for an organization, incorporating elements required by the N-PCL, as well as elements related to certain disclosure requirements under Internal Revenue Service ("IRS") rules. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

It should also be noted that Section 8-1.9 of New York's Estates, Powers and Trusts Law makes applicable to charitable trusts a number of sections of the N-PCL, including the provisions addressing whistleblower policies.

Also note that New York law requires employers to adopt a written sexual harassment policy including a complaint form and procedures for investigating complaints of sexual harassment.<sup>1</sup> While the sample Whistleblower Policy below includes procedures for reporting and investigating complaints generally, it is not intended as a policy that would satisfy New York's requirement regarding the adoption of sexual harassment policies.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Whistleblower Policy

### I. PURPOSE

\_\_\_\_\_ (the “Organization”) is committed to honest, ethical and lawful conduct, full, fair, accurate, timely and transparent disclosure in all public communications, and compliance with applicable laws, rules and regulations. In furtherance of these commitments, directors, officers, key persons (as defined below), employees, independent contractors, consultants, and volunteers of the Organization (each, a “Covered Person” or “you”) must act in accordance with all applicable laws and regulations, [the Organization’s Code of Business Conduct and Ethics (the “Code”)] and with the policies of the Organization at all times, and assist in ensuring that the Organization conducts its business and affairs accordingly.

A “key person” is a person, other than a director or officer, whether or not an employee of the Organization who (i) has responsibilities, or exercises powers or influence over the Organization as a whole similar to the responsibilities, powers or influence of directors and officers; (ii) manages the Organization, or a segment of the Organization that represents a substantial portion of the activities, assets, income or expenses of the Organization; or (iii) alone or with others controls or determines a substantial portion of the Organization’s capital expenditures or operating budget.<sup>2</sup>

This Whistleblower Policy (this “Policy”) (a) establishes procedures for the reporting and handling of concerns regarding violations or suspected violations of any law, rule, regulation or policy of the Organization, as well as any other matter that could cause serious damage to the Organization’s reputation (each, a “Concern”), and (b) prohibits retaliation against any Covered Person who reports a Concern in good faith.<sup>3</sup>

By appropriately responding to Concerns, we can better support an environment where compliance is valued and ensure that the Organization is meeting its ethical and legal obligations.

### II. WHEN TO RAISE A CONCERN

You are encouraged to disclose to and seek guidance from an appropriate supervisor or manager if you believe any Covered Person or other person associated or doing business with the Organization has engaged, is engaging or may engage in any illegal or unethical behavior or has violated, or may violate any law, rule, regulation or policy of the Organization. Such reportable activity may include, for example, financial wrongdoing (including circumvention of internal controls or violation of the accounting policies of the Organization), fraud, harassment, or any other illegal, unethical or proscribed conduct. While Concerns may be submitted at any time, you should report a Concern as soon as reasonably possible after becoming aware of the matter.

### III. HOW TO RAISE A CONCERN

Concerns may be submitted either in writing or orally. No specific form is required to be filled out in order to submit a Concern, but you are encouraged to provide as much information and detail as possible so that the Concern can be properly investigated. A Concern may be submitted:

- To the administrator of this Policy (the “Policy Administrator,” who is an employee, officer or director of the Organization, as required by law<sup>4</sup>), at [*insert contact information*];

- By discussing it with a supervisor or manager, who will in turn forward the Concern to the Policy Administrator for review where appropriate; or
- In writing (including by e-mail) to the Chair of the [Board of Directors of the Organization (the “Board”) at [*insert contact information*]] [Audit Committee] [*insert contact information, if applicable*]], who will in turn forward the Concern to the Policy Administrator for review where appropriate.<sup>5</sup>

Concerns may be raised anonymously; however, any individual reporting their own violation shall not satisfy their disclosure obligation hereunder with a Concern raised anonymously. Any individual who is the subject of a Concern is prohibited from participating in any Board or Audit Committee deliberations or voting relating to the evaluation of such Concern in accordance with this Policy; provided, that the [Board] [Audit Committee] is not prohibited from requesting that such individual present information as background or answer questions at a meeting of the Board [or of the Audit Committee] prior to the commencement of deliberations or voting relating thereto.<sup>6</sup>

#### **IV. PROCEDURES FOR RECEIVING AND REVIEWING CONCERNS**

Any supervisor, manager or other person receiving a Concern should contact the Policy Administrator who will coordinate further action.

The Policy Administrator will assess each Concern on a preliminary basis to determine to what extent an investigation into the Concern is required, and will direct all aspects of the investigation of any Concern. If the Concern relates to audit, accounting, finance, fraud or similar matters that could implicate the Organization’s financial statements, such Concerns will be promptly forwarded to the Audit Committee for consideration. The Audit Committee may also review and consider other Concerns. The Organization will use its best efforts to conduct the review in a confidential manner, so that information will be disclosed only as needed to facilitate review of the investigation materials or otherwise as required by law. You must cooperate as necessary in connection with any such investigation. Any person who does not cooperate in connection with any such investigation may be subject to disciplinary action, up to and including termination of employment. In the event a Concern involves or implicates the Policy Administrator, the Policy Administrator will promptly recuse themselves from the investigation and inform the [Board] [Audit Committee] in writing. The [Board] [Audit Committee] may investigate such Concern or appoint impartial attorneys to investigate the Concern.

#### **V. RECORDS OF CONCERNS AND INVESTIGATION REPORTS**

The Policy Administrator will maintain a written record of all Concerns, summarizing in reasonable detail for each Concern: (i) the nature of the Concern (including any specific allegations made and the persons involved); (ii) the date of receipt of the Concern; (iii) the current status of any investigation into the Concern and information about such investigation (including the steps taken in the investigation, any factual findings and the recommendations for corrective action); and (iv) any final resolution of the Concern. The Policy Administrator will distribute an update of this record to the Chair of the [Board] [Audit Committee] in advance of each regularly scheduled meeting thereof.

#### **VI. CONFIDENTIALITY**

All Concerns received will be treated confidentially to the extent reasonable and practicable under the circumstances.<sup>7</sup>

## VII. NO RETALIATION

It is the Organization's policy to encourage the communication of bona fide Concerns relating to the lawful and ethical conduct of the Organization's business. It is also the policy of the Organization to protect those who communicate bona fide Concerns from any retaliation for such reporting. **No adverse employment action or other forms of retaliation (including, without limitation, intimidation, harassment, discrimination, coercion or otherwise, whether express or implied) may be taken against any Covered Person based on such person having reported in good faith any Concern or assisted in an investigation of, or the fashioning or implementation of any corrective action or response made in connection with, any Concern.** Any person who violates this prohibition against retaliation will be subject to appropriate disciplinary action, which may include termination of employment or other relationship with the Organization.<sup>8</sup>

## VIII. POLICY DISTRIBUTION

A copy of this Policy shall be distributed to each Covered Person promptly following the adoption of or any amendments to this Policy, and at such time as a person becomes a Covered Person. This distribution requirement may be satisfied by posting a copy of this Policy on the Organization's website or at the Organization's offices in a conspicuous location accessible to employees and volunteers.<sup>9</sup>

## IX. POLICY ADOPTION AND OVERSIGHT<sup>10</sup>

The Board is ultimately responsible for providing oversight of the adoption and implementation of and compliance with, this Policy.<sup>11</sup>

This Whistleblower Policy was adopted by the Board [on / and amended through] [month] [day], [year].

## X. POLICY REVIEW

The [Audit Committee] [Board] will review this Policy periodically.

ENDNOTES

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<sup>1</sup> See Labor Law § 201-g.

<sup>2</sup> See N-PCL § 102(a)(25).

<sup>3</sup> The N-PCL requires New York not-for-profits that have 20 or more employees and annual revenue in excess of \$1 million in the prior year to have a whistleblower policy adopted and overseen by the corporation's board of directors that includes certain provisions and that protects from retaliation persons who report suspected improper conduct. See N-PCL § 715-b(a). See also State of New York Attorney General's Charities Bureau Guidance Document, "Whistleblower Policies Under the Nonprofit Revitalization Act of 2013" (April 2015), available at [https://ag.ny.gov/sites/default/files/regulatory-documents/Charities\\_Whistleblower\\_Guidance.pdf](https://ag.ny.gov/sites/default/files/regulatory-documents/Charities_Whistleblower_Guidance.pdf).

<sup>4</sup> Whistleblower policies that are required by the N-PCL must include "[a] requirement that an employee, officer or director of the corporation be designated to administer the whistleblower policy and to report to the board or an authorized committee thereof, except that directors who are employees may not participate in any board or committee deliberations or voting relating to administration of the whistleblower policy." See N-PCL § 715-b(b)(2).

<sup>5</sup> Whistleblower policies that are required by the N-PCL must include "[p]rocedures for the reporting of violations or suspected violations of laws or corporate policies." N-PCL § 715-b(b)(1).

<sup>6</sup> Whistleblower policies that are required by the N-PCL must require that the person who is the subject of a whistleblower complaint not be present at or participate in board or committee deliberations or vote on the matter relating to such complaint. However, the board or committee may request that the person who is subject to the complaint present information as background or answer questions at a committee or board meeting prior to the commencement of deliberations or voting on the matter. N-PCL § 715-b(b)(3).

<sup>7</sup> Whistleblower policies that are required by the N-PCL must include "procedures for preserving the confidentiality of reported information." N-PCL § 715-b(b)(1).

<sup>8</sup> Whistleblower policies that are required by the N-PCL must "protect from retaliation persons who report suspected improper conduct [and] provide that no director, officer, key person, employee or volunteer of a corporation who in good faith reports any action or suspected action taken by or within the corporation that is illegal, fraudulent or in violation of any adopted policy of the corporation shall suffer intimidation, harassment, discrimination or other retaliation or in the case of employees, adverse employment consequence." N-PCL § 715-b(a).

<sup>9</sup> Whistleblower policies that are required by the N-PCL must include "[a] requirement that a copy of the policy be distributed to all directors, officers, key persons, employees and to volunteers who provide substantial services to the corporation. For purposes of this [requirement], posting the policy on the corporation's website or at the corporation's offices in a conspicuous location accessible to employees and volunteers are among the methods a corporation may use to satisfy the distribution requirement." N-PCL § 715-b(b)(4). It may be administratively more convenient to distribute the policy to all volunteers, not just those providing "substantial services." The policy should also be provided to any persons who are subject to the policy but who may not attend the corporation's offices, such as contractors, consultants and key persons who are not employees, etc.

<sup>10</sup> The federal tax law (and IRS Form 990) does not require that an organization have a whistleblower policy; however, tax-exempt organizations are required to disclose on their Form 990 whether the organization has a written whistleblower policy. See Form 990, Part VI, Line 13. Instructions to Form 990 provide that "[a] whistleblower policy encourages staff and volunteers to come forward with credible information on illegal practices or violations of adopted policies of the organization, specifies that the organization will protect the individual from retaliation, and identifies those staff or board members or outside parties to whom such information can be reported."

<sup>11</sup> The N-PCL requires that the board oversee the adoption and implementation of and compliance with the whistleblower policy to protect from retaliation persons who report suspected improper conduct. See N-PCL § 715-b(a).

## Not-For-Profit Practice Group

### Sample Not-For-Profit Document Retention and Destruction Policy

Not-for-profit organizations should strongly consider implementing a document retention and destruction policy to support legal compliance and the responsible stewardship of information. A well-designed policy helps ensure that required records are maintained for appropriate periods, sensitive information is protected, and unnecessary records are disposed of in a consistent manner. Document retention and destruction policies should be tailored to the organization and the types of documents it regularly uses.

This sample document retention and destruction policy reflects generally accepted practices for not-for-profit organizations. This sample policy addresses requirements of the Sarbanes-Oxley Act of 2002 (which, among other things, prohibits the improper destruction of documents) and certain requirements under Internal Revenue Service (“IRS”) rules. This policy, including a retention schedule setting out the time periods for which certain types of documents should be retained and then destroyed, should be customized in consultation with legal counsel to address the organization’s specific legal obligations and operational needs.

A comprehensive document retention and destruction policy typically identifies key categories of records maintained by the organization, establishes retention periods for these categories of records, and sets out protocols for the timely and secure destruction of records that are no longer required. Necessary documents should be easily located and accessible and securely stored to protect sensitive or personal information. The policy should be clearly communicated to all employees, consistently enforced, and periodically reviewed.

This policy is intended to form part of a greater governance framework regarding data management, data privacy, and record keeping. This sample policy should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization’s certificate of incorporation and by-laws; they are not intended to establish, by their own force, any legally binding obligations.

The various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable sector-specific legal requirements) may affect the provisions that should be addressed in a document retention and destruction policy. Accordingly, organizations should assess their specific circumstances and adapt this policy accordingly.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Document Retention and Destruction Policy

### I. PURPOSES OF THIS POLICY

The purpose of this Records Retention and Destruction Policy (this “Policy”) is to establish requirements for the retention, storage and destruction of Records (as defined below) received or created by \_\_\_\_\_ (the “Organization”) by establishing guidelines, procedures and requirements for the:<sup>1</sup>

1. Retention and maintenance of any Records necessary for the Organization to achieve its mission and comply with applicable law and legal process;
2. Destruction of Records that do not need to be or no longer need to be retained; and
3. Communication of responsibilities concerning Record retention to the Organization’s Board of Directors, officers, members, employees, independent contractors and volunteers, and other parties that may be identified by the Administrator of this Policy (as defined below) from time to time (collectively, the “Constituents”).

Certain federal and state laws require that specific records be kept for defined periods. In certain circumstances, we may have a legal requirement to preserve Records that may be relevant to a pending or anticipated lawsuit, investigation, inquiry, audit or other legal proceeding (a “Legal Proceeding”).<sup>2</sup> There are a variety of consequences, including potential criminal consequences, for failure to retain Records where required by applicable law or legal process. For example, the Sarbanes-Oxley Act of 2002 makes it a crime to change, conceal, falsify or destroy any Record with the intent to impede or obstruct any official or government proceedings.<sup>3</sup>

Many Records may contain information that provides ongoing value to the Organization. Consistent retention pursuant to this Policy and secure disposal help the Organization operate effectively and safeguard information entrusted to it.

The Organization has established a record retention schedule (the “Retention Schedule”) for specific categories of Records. While minimum retention periods are suggested, the retention of Records identified in the Retention Schedule and of Records not included in the categories identified in the Retention Schedule can be determined by directing any inquiries to the Administrator of this Policy.<sup>4</sup>

### II. RECORDS COVERED

**Records:** A “Record” is any type of record, file, document, sample and other form of information created, received or transmitted in the course of the Organization’s operations, regardless of physical format. Records must be maintained pursuant to the Retention Schedule. Records may include, but are not limited to:<sup>5</sup>

1. Contracts and invoices;
2. Electronic files;
3. Emails, letters and other correspondence;
4. Employee, volunteer and director handbooks; or
5. Fundraising and donation records, including donor information.<sup>6</sup>

**Disposable Records:** “Disposable Records” are Records that serve no legitimate purpose, are no longer required for the operation of the Organization, and are not required by law or legal process to be retained by the Organization. Disposable Records may be safely destroyed without violating this Policy. This can include: Records that have been retained for the relevant period prescribed in the Retention Schedule and that are not otherwise required to be retained pursuant to applicable law or legal process; duplicates of original documents that have not been annotated; preliminary drafts, memoranda, reports, worksheets and informal notes that do not represent significant steps or decisions in the preparation of an official record; manuals, training binders and other printed materials obtained from sources outside of the Organization and retained primarily for reference purposes. Disposable Records shall be disposed of in the manner set forth in Section V, below.

**Confidential Information Belonging to Others:** Any confidential or proprietary information belonging to a third party that a Constituent may have obtained from a source outside of the Organization, such as a previous employer or through outside volunteer activities, must not, so long as such information remains confidential and/or proprietary, be disclosed or used by the Organization without the permission of the relevant third party. In the absence of permission, the Organization should generally refuse receipt of this confidential and/or proprietary information, return it to the sender where possible and delete or destroy it, as appropriate.

### III. MANDATORY COMPLIANCE

Each Constituent must comply with this Policy, the Retention Schedule and any communications to preserve evidence in the case of a Legal Proceeding (including as discussed further below in Section V). Failure to comply may subject the Organization and its Constituents to civil and/or criminal liability. If you reasonably suspect that you or someone else may have violated this Policy, you should report the incident immediately to the Administrator.

### IV. ADMINISTRATION

**Administrator:** The [ ]<sup>7</sup> of the Organization or their designee (the “Administrator”) shall administer this Policy. The Administrator’s responsibilities include:

1. Identifying the Records that the Organization must or should retain, consulting with counsel where necessary or appropriate and determining the proper retention period for each Record type, including in accordance with the Retention Schedule;
2. Planning, developing and prescribing Record retention and disposal policies, systems, standards and procedures;
3. Training staff and other Constituents on their obligations under this Policy;
4. Ensuring this Policy and any retention procedures comply with applicable laws (including privacy laws) that may govern the handling of Records concerning the Organization’s Constituents;
5. Periodically reviewing this Policy as needed (including, where necessary or appropriate, in consultation with outside counsel) in order to comply with applicable law, reflect changes in operations and monitor compliance by Constituents or for any other reason the Administrator may determine; and
6. Taking steps designed to ensure that Records created or received by the Organization in connection with a volunteer project are returned to the Organization for retention or destruction, as appropriate, at the end of each volunteer project.

**Constituents:** Constituents shall assist the Administrator, as requested, in the implementation of and compliance with this Policy. Constituents shall return all Records to the Administrator or the Organization upon the end of their employment, project (*i.e.*, for volunteers) or other service with the Organization.

## V. RETAINING, STORING, AND DESTROYING DOCUMENTS

**Retention:** Any Records that are part of any categories listed in the Retention Schedule must be retained for the amount of time set forth in the Retention Schedule. A Record must not be retained beyond the period set forth in the Retention Schedule unless a valid business reason (such as a Litigation Hold or other special situation) calls for its continued retention. If you have any questions about the retention process, please direct any questions to the Administrator in accordance with the “Questions About This Policy” section below.

**Storage:** Records must be stored in a safe, secure and accessible manner. The Organization should review the terms of third-party vendors that it utilizes in connection with data handling and storage (such as cloud storage providers, HR software providers, donor management software providers, etc.) to ensure that its agreements with third-party vendors include appropriate representations regarding the security of their systems. Records may be stored through electronic or paper copies, as appropriate, and in third-party vendor repositories (*e.g.*, third party payroll systems for employee-related HR information) if originally generated within such repositories or are otherwise most appropriately stored in such repositories given the nature of the Records. If you have any questions about the storage process, please direct any questions to the Administrator in accordance with the “Questions About this Policy” section below.

**Destruction:** The Administrator is responsible for the continuing process of identifying Records that have met their required retention period and supervising the destruction process. The Administrator shall take steps designed to ensure the return, deletion or destruction of the Record in accordance with this Policy, such as by prescribing or requiring third party vendors to prescribe appropriate automatic deletion periods in data repositories. Disposable Records may be discarded or deleted at the discretion of the user no later than thirty (30) days after they have served their purpose. Physical Records should be shredded or destroyed to prevent unauthorized access, while electronic Records should be permanently deleted using secure deletion methods.

**Legal Proceedings and Other Special Situations:** In the case of actual, pending or reasonably anticipated Legal Proceedings, the Administrator shall issue evidence preservation instructions (a “Litigation Hold”). If you believe or the Administrator informs you that the Organization’s Records are under a Litigation Hold you must preserve and not delete, dispose, destroy or change those Records, including emails, until the Administrator determines those Records are no longer needed. If you believe a Litigation Hold may apply or have any questions regarding whether it may apply, please contact the Administrator.<sup>8</sup>

**Exceptions:** Exceptions to this Policy may be granted only by the Administrator.

**Questions About This Policy:** Refer any questions about this Policy to the Administrator ([phone number], [email address]), who is in charge of administering this Policy.<sup>9</sup>

### Retention Schedule<sup>10</sup>

[A retention schedule should be prepared with legal counsel to identify the types of documents that the organization maintains and the periods of time that such documents are required to be retained before they are destroyed. This is typically a simple table listing the type of record in one column and the retention period in another. This schedule should be tailored to your organization’s needs and the applicable legal requirements in consultation with counsel.]

## ENDNOTES

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<sup>1</sup> IRS Form 990 asks whether the organization has a written document retention and destruction policy. *See* Form 990, Part VI, line 14 and related instructions. *See also* IRS Publication 583 (Starting a Business and Keeping Records).

<sup>2</sup> Organizations should confirm applicable federal and state requirements based on their jurisdiction of operation, including but not limited to, federal and state tax laws, federal and state employment and labor law, state data privacy laws and the Sarbanes-Oxley Act of 2002.

<sup>3</sup> “Whoever knowingly alters, destroys, mutilates, conceals, covers up, falsifies, or makes a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States or any case filed under title 11, or in relation to or contemplation of any such matter or case, shall be fined under this title, imprisoned not more than 20 years, or both.” 18 U.S.C. Section 1519.

<sup>4</sup> In general, an organization’s records should be kept for as long as they are needed for the administration of any provision of the Internal Revenue Code. *See* IRS Form 990 Instructions, Requirements for a Properly Completed Form 990 (Recordkeeping). Generally, this means the organization must keep records that support an item of income or deduction on a return until the statute of limitations for that return runs. The statute of limitations has run when the organization can no longer amend its return and the IRS can no longer assess additional tax. IRS Compliance Guide for 501(c)(3) Public Charities.

<sup>5</sup> A record retention schedule describes commonly kept records, but organizations should include additional documents that they commonly use to document their activities and financials. IRS Compliance Guide for 501(c)(3) Public Charities (“A charity can choose any recordkeeping system, suited to its activities, that clearly shows the organization’s income and expenses. The types of activities a public charity conducts determines the type of records that should be kept for federal tax purposes.”)

<sup>6</sup> An IRS Section 501(c) organization that is eligible to receive tax-deductible contributions under IRS Section 170(c) must keep sample copies of its fundraising materials, such as: dues statements, fundraising solicitations, tickets, receipts, or other evidence of payments received in connection with fundraising activities. *See* IRS Form 990 Instructions, Appendix J. Contributions.

<sup>7</sup> Organizations should clearly identify who will oversee and administer the policy. Most commonly this would be the responsibility of the legal or operations function.

<sup>8</sup> Under the Sarbanes-Oxley Act, it is a crime to knowingly destroy a document with the intent to obstruct or influence “the investigation or proper administration of any matter within the jurisdiction of any department or agency of the United States . . . or in relation to or contemplation of any such matter or case.” 18 U.S.C. Section 1519.

<sup>9</sup> If possible, consider including a generic mailbox accessible by the Administrator (so that there is consistency when there are personnel changes) – e.g., OrganizationName\_Administrator@...

<sup>10</sup> All books and records must be maintained so long as they remain material in the computation of any tax. Materiality Rule under Treas. Reg. 1.6001-1.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Data Collection Guidelines

A not-for-profit organization may find it useful to establish data collection guidelines for the organization's collection, use, and potential dissemination of data. Responsible data practices are crucial to building trust with constituents, ensuring legal compliance, and protecting against the inadvertent compromise of sensitive information. These data collection guidelines should be tailored to needs and circumstances of the organization. Organizations should be mindful of their collection of personal data and only do so for legitimate business purposes, while striving for transparency and accountability.

The following sample data collection guidelines are intended to reflect generally accepted practices for not-for-profit organizations. The guidelines are intended to be a component of a comprehensive approach to data privacy, records retention and data stewardship, and should be read in conjunction with the organization's other policies, including the Document Retention and Destruction Policy, as well as applicable law. An organization's data collection practices are governed by a variety of laws including federal, state, and sector-specific regulations, such as those that apply to organizations that deal with health data or the data of children, for example. State-specific data privacy or consumer protections laws may also apply. Organizations should also ensure that any collection of data for use with artificial intelligence tools complies with applicable law. The guidelines should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; they are not intended to establish, by their own force, any legally binding obligations.

The various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable sector-specific legal requirements) may affect the provisions that should be addressed in data collection guidelines. Accordingly, organizations should assess their specific circumstances and adapt this policy accordingly.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Data Collection Guidelines

### I. PURPOSE

The purpose of these Data Collection Guidelines (these “Guidelines”) is to provide guidelines for \_\_\_\_\_ (the “Organization”) with respect to the collection of personal information of its directors, employees, volunteers, clients and donors. As a general rule, the Organization aims to limit the amount of personal information collected to the minimum amount necessary in the context in furtherance of its mission.

### II. DEFINITIONS

- “Personal information” means any information that identifies, could be used to identify or is otherwise related to an individual person. Note that “personal information” may be defined differently under different laws or contracts but is generally any information that can be used to identify an individual. Personal information may include information like name, date of birth, address, phone number, financial information (*e.g.*, credit card numbers), health records, criminal records, employment details, IP addresses and demographic details (*e.g.*, gender, race, religion, etc.).
- “Privacy law” means any law, legal requirement or binding guideline or standard relating to the receipt, collection, use, sharing, transfer or other processing of personal information. Note that non-profits are exempt from certain privacy laws. However, certain privacy laws can apply to non-profits, such as those applying to marketing communications, the personal information of children or students, health-related information and more. Therefore, it is important for the Organization to maintain an ongoing practice of assessing what laws may apply to its activities.

### III. EMPLOYEES & VOLUNTEERS

- With respect to any individuals that assist the Organization in its mission as a director, employee, volunteer, independent contractor or otherwise (such individuals, “Employees & Volunteers”), the Organization should only collect and store the personal information necessary to conduct its business and administer services (*e.g.*, managing pay dispersal, organizing community members, coordinating campaigns, planning cultural and community-building programming and providing social services).
- The Organization should ensure that it retains and destroys any records of Employees & Volunteers in accordance with the Organization Records Retention and Destruction Policy. The Organization should store all Employee and Volunteer information (whether retained temporarily or kept permanently) in a safe, secure and organized manner.

### IV. CLIENTS

- With respect to any individuals to whom the Organization provides services or support (“Clients”), the Organization should only collect personal information that is necessary to provide the services or support (*e.g.*, providing requested social services, managing participation in and hosting campaigns and cultural and community-building events, etc.).
- If the Organization collects any sensitive categories of personal information from or about Clients (*e.g.*, citizenship status, government identifiers, etc.), the Organization should practice additional care and caution when collecting such sensitive personal information to protect the security of such information.

Additionally, the Organization should only collect sensitive personal information where absolutely necessary to provide its services or support to Clients.

- With respect to any Client personal information that the Organization must store to provide its services or support, the Organization should (a) take steps to ensure that the personal information is stored securely (*e.g.*, limiting access to such personal information, storing the personal information on an encrypted drive), and (b) unless otherwise required by applicable law (including any privacy law) or legal process, dispose of the personal information as soon as possible after providing the services or support (but no later than 30 days after the Organization completes providing the services or support) and in accordance with the Organization’s Records Retention and Destruction Policy.
- The Organization should not publish or otherwise share any personal information received from any Client, unless the Organization has notified and obtained the written consent of the Client or as otherwise required by applicable law (including any privacy law) or legal process.

## V. DONORS

- With respect to any individuals that contribute funds to the Organization (“Donors”), the Organization should only collect personal information that is necessary to receive the funds and conduct any appropriate background checks as to source of funds.
- The Organization should ensure that all financial transactions are handled through a third-party service provider. Certain laws and regulations govern the handling, collection and other processing of financial information (*e.g.*, credit card or banking information). The Organization should avoid directly handling or collecting any financial information from Donors.
- The Organization should not use Donor personal information for any purposes other than processing the donation and maintaining its relationship with the Donor.
- The Organization should not publish or otherwise share any personal information received from any Donor, unless the Organization has notified and obtained the written consent of the Donor or as otherwise required by applicable law (including any privacy law) or legal process.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Audit Committee Charter

The board of a not-for-profit organization is responsible for ensuring the integrity of the organization's accounting and financial reporting systems and processes. The board may wish to establish an audit committee comprised of independent directors to assist it in fulfilling this responsibility although it is not required by law to do so.

Tax-exempt organizations are required to disclose on their Form 990 whether they have a committee with responsibility for (i) overseeing the compilation, review or audit of its financial statements, and (ii) selecting an independent accountant to compile, review or audit the financial statements.<sup>1</sup> The New York Not-for-Profit Corporation Law (the "N-PCL"), as amended by the Non-Profit Revitalization Act of 2013, requires that, in the case of New York not-for-profits required to file an independent certified public accountant's audit report with the New York Attorney General because such organization's annual gross revenue exceeds certain thresholds (see "Gross Revenue & Support Thresholds for Independent Audit or Review" below), either the audit committee (which, for this purpose, must be comprised entirely of "independent"<sup>2</sup> directors) or the full board of directors (with only "independent" directors participating in the deliberations or voting), is required to oversee the accounting and financial reporting of the organization and the audit of the organization's financial statements, annually retain the independent auditor to conduct the audit and review the results of the audit and any related management letter with the independent auditor.

The audit committee or full board (with only "independent" directors participating in the deliberations or voting) of a New York not-for-profit with annual revenues in excess of \$1 million must comply with additional enhanced audit oversight requirements.

Whether a not-for-profit organization finds it valuable to establish an audit committee will depend on the financial resources and complexity of the organization (including the size and composition of its board) and its accounting and reporting systems. "One size does not fit all" – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization. For example, a not-for-profit organization with significant financial resources or complex financial arrangements may benefit significantly by establishing an audit committee comprised of independent directors who are financially literate, responsible for retaining and compensating the organization's independent auditor (if any) and providing oversight of internal controls and related processes designed to assure that reported financial data is reliable. In contrast, a small not-for-profit organization with simple financial structures may decide that it would be more efficient and effective to entrust responsibility for ensuring the integrity of financial reporting to the entire board. (In either case, it is important that some members of the board be independent and financially literate, and at least one director should be sophisticated concerning financial reporting and accounting).

This sample charter is intended to comport with generally accepted practices for audit committees of not-for-profit organizations. This sample provides only one example for an organization, incorporating elements required by the N-PCL, as well as elements related to certain disclosure requirements under Internal Revenue Service ("IRS") rules. This sample includes, in addition to generally applicable provisions: (i) provisions relating to independent audit oversight that may be removed for organizations that are not required to file audit reports; (ii) provisions relating to enhanced oversight that may be removed for organizations with revenues below \$1 million; and (iii) provisions relating to an internal audit function which is led by a member of management, which may be removed or modified as appropriate. It is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample audit committee charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

It should also be noted that Section 8-1.9 of New York's Estates, Powers and Trusts Law makes a number of sections of the N-PCL applicable to charitable trusts, including the provisions addressing audit oversight.

#### Gross Revenue & Support Thresholds for Independent Audit or Review

Organizations registered in New York for charitable solicitation purposes may need (i) their financial statements to be audited or reviewed by an independent certified public accountant and (ii) to file with the Attorney General the resulting audited or reviewed financial report and related financial statements. The chart below reflects the annual gross revenue and support thresholds above which such a New York not-for-profit will require an independent audit or accountant review:<sup>3</sup>

<u>Requirement</u>	<u>As of July 1, 2021</u>
Audit report	In excess of \$1 million
Review report	\$250,000 to \$1 million

## [NAME OF NOT-FOR-PROFIT-ORGANIZATION]

### Audit Committee Charter

#### I. PURPOSES

The Audit Committee (the “Committee”)<sup>4</sup> is appointed by the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) to fulfill its responsibilities to provide oversight of: (i) the Organization’s accounting and financial reporting processes, and systems of internal controls and risk management; (ii) the integrity of the Organization’s financial statements and the audit of the Organization’s financial statements; (iii) the Organization’s compliance with legal and regulatory requirements and ethical standards; and (iv) the engagement, independence and performance of the Organization’s independent auditor.<sup>5</sup>

#### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>6</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time. Committee members shall have a basic understanding of finance, accounting and fundamental financial statements. At least one member of the Committee shall have a sophisticated understanding of financial reporting and accounting as determined by the Board.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

**Independence.** Each member of the Committee shall be an “independent”<sup>7</sup> director as required by applicable law [and determined in accordance with the Organization’s Board Guidelines]. Any action duly taken by the Committee shall be valid and effective, whether or not the members of the Committee at the time of such action are later determined not to have satisfied the requirements for membership provided herein.

#### III. AUTHORITY

The Committee’s role is one of oversight. The Organization’s management is responsible for preparing the Organization’s financial statements and the independent auditor is responsible for auditing those financial statements. The Committee recognizes that management, including [the internal audit function,] and the independent auditor have more time, knowledge and detailed information about the Organization than do the Committee members. Consequently, in carrying out its oversight responsibilities, the Committee is not providing any expert or special assurance as to the Organization’s financial statements or any professional certification as to the independent auditor’s work.

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes. The Committee shall have the sole discretion to retain or obtain advice from, oversee and

terminate any independent or other auditor, accountant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

Nothing herein shall preclude the Committee from (i) seeking advice from individuals with expertise in accounting and financial matters who are not members of the Board or the Committee, provided that participation in formal deliberations and voting shall be limited to Committee members or (ii) providing honorific designations to such persons; provided, that members of current management who are responsible for developing and maintaining financial controls should not also be involved in the Committee's performance of its duties as set forth herein and under applicable law.<sup>8</sup>

#### **IV. COMMITTEE MEETINGS**

The Committee shall meet on a regularly scheduled basis, at least [four] times per year and additionally as circumstances dictate. The Committee shall meet at least [twice] each year with the [head of internal audit and with the] independent auditor in separate executive sessions to provide the opportunity for full and frank discussion without members of senior management present.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting, and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

#### **V. KEY RESPONSIBILITIES**

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

##### **5.1 Independent Auditor Retention and Oversight**

1. Annually retain or renew the retention of the independent auditor;<sup>9</sup>
2. Annually evaluate the qualification and performance of the independent auditor, who shall report directly to the Committee;<sup>10</sup>
3. Annually assess the independence of the independent auditor by obtaining and reviewing a report from the independent auditor delineating all relationships between the independent auditor and the Organization and discussing with the independent auditor any such disclosed relationships and their impact on the independent auditor's independence, and by obtaining the independent auditor's assertion of independence in accordance with professional standards;<sup>11</sup>
4. Pre-approve any audit-related and non-audit services to be provided by the independent auditor to the Organization; and

5. At least annually, review a report from the independent auditor describing the auditing firm's internal quality-control procedures and any material issues raised by the most recent quality-control review of the firm, or by any inquiry or investigation by governmental or professional authorities within the preceding five years, with respect to one or more independent audits carried out by the firm and any steps taken to deal with any such issues.

## 5.2 Audit Oversight, Accounting and Financial Reporting<sup>12</sup>

1. Prior to the commencement of the audit, review with the independent auditor the scope and planning of the audit;<sup>13</sup>
2. Upon completion of the audit and as otherwise appropriate, review and discuss with the independent auditor:
  - a. the results of the audit and any problems the independent auditor has encountered performing the audit, any management letter provided and the Organization's response to that letter;<sup>14</sup>
  - b. any significant disagreements between the independent auditor and management,<sup>15</sup> and any other matters that the independent auditor is required by applicable professional standards or otherwise to communicate to the Committee;
  - c. significant accounting and reporting issues, including recent professional and regulatory pronouncements, in order to understand their impact on the financial statements and ensure that all such issues have been considered in the preparation of the financial statements;
3. Review and discuss with management[, the internal auditor] and the independent auditor:
  - a. any significant findings during the year, any restrictions on the scope of the independent auditor's activities or access to requested information,<sup>16</sup> any changes required in the scope of the audit plan, the audit budget and staffing and coordination of audit efforts;
  - b. critical accounting policies and practices used by the Organization and any significant changes in the Organization's accounting policies;
4. Review with management the annual financial statements, the annual audit report and recommendations of the independent auditor, including any audit problems or difficulties and management's response;
5. Review with management and the independent auditor any complex or unusual transactions or other significant matters or events not in the ordinary course of business.

## 5.3 [Internal Audit<sup>17</sup>

1. Review the risk assessment that drives the internal audit plan and annually approve the plan;
2. Review the activities and evaluate the performance of the internal audit function;
3. Review significant adverse internal audit findings and management's response; and
4. Review the effectiveness of the internal audit function, including staffing.]

#### 5.4 Internal Control and Risk Oversight

1. Review and discuss with management and the independent auditor the adequacy and effectiveness of, and any material risks and weaknesses in, the Organization's internal controls and accounting and financial reporting processes;<sup>18</sup>
2. Review and assess with management and the independent auditor the Organization's major financial and other material risks or any significant exposures, the Organization's policies with respect to risk and the steps management has taken to minimize such exposures;
3. Oversight of Legal and Ethical Compliance;
4. Review periodically with the Organization's legal counsel the scope and effectiveness of the Organization's legal and regulatory compliance policies and programs, and ethical standards and policies;
5. [Review and, if appropriate, approve or ratify related party transactions and conflicts of interest, in accordance with applicable Organization policies;]<sup>19</sup> and
6. Oversee legal and regulatory compliance and compliance with the Organization's ethical standards and policies, including the Organization's Whistleblower Policy.

#### 5.5 Other Responsibilities

1. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>20</sup>
2. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests,<sup>21</sup> and maintain minutes or other records of Committee meetings and activities;<sup>22</sup> and
3. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> See Form 990, Part XII, Line 2c and related instructions.

<sup>2</sup> The N-PCL defines “independent director” to mean “a director who: (i) is not, and has not been within the last three years, an employee or a key person of the corporation or an affiliate of the corporation, and does not have a relative who is, or has been within the last three years, a key person of the corporation or an affiliate of the corporation; (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 of the corporation; (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 provided payments, property or services to, or received payments, property or services from, the corporation or an affiliate of the corporation if the amount paid by the corporation to the entity or received by the corporation from the entity for such property or services, in any of the last three fiscal years, exceeded the lesser of \$10,000 or 2% of such entity’s consolidated gross revenues if the entity’s consolidated gross revenue was less than \$500,000; \$25,000 if the entity’s consolidated gross revenue was \$500,000 or more but less than \$10 million; \$100,000 if the entity’s consolidated gross revenue was \$10 million or more; 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, the terms: ‘compensation’ does not include reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director . . .; and ‘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, or payments made by the corporation at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the corporation are available to individual members of the public on the same terms, and such services received by the corporation are not available from another source.” N-PCL § 102(a)(21). An “affiliate” of a corporation is “any entity controlled by or in control of such corporation.” N-PCL § 102(a)(19). A “relative” of a person is that person’s spouse, domestic partner, ancestors, brothers and sisters (whether whole or half-blood), children (whether natural or adopted), grandchildren, great-grandchildren or the spouse or domestic partner of his or her brothers, sisters, children, grandchildren and great-grandchildren. See N-PCL § 102(a)(22). A “key person” is a person, other than a director or officer, whether or not an employee of the corporation, who: (i) has responsibilities, or exercises powers or influence over the corporation as a whole similar to the responsibilities, powers or influence of directors and officers; (ii) manages the corporation, or a segment of the corporation that represents a substantial portion of the activities, assets, income or expenses of the corporation; or (iii) alone or with others controls or determines a substantial portion of the corporation’s capital expenditures or operating budget. See N-PCL § 102(a)(25).

<sup>3</sup> See New York Executive Law § 172-b. See also New York Attorney General’s Charities Bureau Guidance Document, “Audit Committee Requirements and Responsibilities Under New York’s Not-for-Profit Corporation Law As Amended Through 2017” (September 2018), available at <https://ag.ny.gov/sites/default/files/regulatory-documents/AuditCommittees.pdf>.

<sup>4</sup> Unless the board performs such governance activities, the N-PCL requires New York not-for-profits to form an audit committee comprised of “independent directors” (as defined in the N-PCL), or identify independent directors to oversee the audit (if any). Only independent directors of New York not-for-profits will be permitted to participate in any board or committee deliberations or voting relating to such matters. See N-PCL § 712-a.

<sup>5</sup> The N-PCL requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. See N-PCL § 712(a).

<sup>6</sup> The N-PCL requires committees designated by the board to consist of three or more directors. See N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. See DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>7</sup> See note 2 above for definition of “independent director” under the N-PCL.

<sup>8</sup> See New York Attorney General’s Charities Bureau Guidance Document, “Audit Committee Requirements and Responsibilities Under New York’s Not-for-Profit Corporation Law As Amended Through 2017” (September 2018), available at <https://ag.ny.gov/sites/default/files/regulatory-documents/AuditCommittees.pdf>.

<sup>9</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant’s audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1), the board or a designated audit committee of the board comprised solely of independent directors shall oversee the accounting and financial reporting processes

of the corporation and the audit of the corporation's financial statements, and shall annually retain or renew the retention of an independent auditor to conduct the audit and, upon completion thereof, review the results of the audit and any related management letter with the independent auditor. *See* N-PCL § 712-a(a). The N-PCL defines "independent auditor" to mean any certified public accountant performing the audit of the financial statements of a corporation required by Section 172-b(1) of the New York Executive Law. *See* N-PCL § 102(a)(20).

<sup>10</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must annually consider the performance of the independent auditor. *See* N-PCL § 712-a(b)(3).

<sup>11</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must annually consider the independence of the independent auditor. *See* N-PCL § 712-a(b)(3).

<sup>12</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1), the board or a designated audit committee of the board comprised solely of independent directors shall oversee the accounting and financial reporting processes of the corporation and the audit of the corporation's financial statements. *See* N-PCL § 712-a(a).

<sup>13</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must, prior to the commencement of the audit, review with the independent auditor the scope and planning of the audit. *See* N-PCL § 712-a(b)(1).

<sup>14</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1), the board or a designated audit committee of the board comprised solely of independent directors shall upon completion of the audit, review the results of the audit and any related management letter with the independent auditor. *See* N-PCL § 712-a(a).

<sup>15</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must, upon completion of the audit, review and discuss with the independent auditor any significant disagreements between the auditor and management. *See* N-PCL § 712-a(b)(2)(C).

<sup>16</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must, upon completion of the audit, review and discuss with the independent auditor any restrictions on the scope of the auditor's activities or access to requested information. *See* N-PCL § 712-a(b)(2)(B).

<sup>17</sup> This is only needed if the Organization has an internal audit function. Not-for-profit organizations other than those operating at a large scale may not have this function.

<sup>18</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1), the board or a designated audit committee of the board comprised solely of independent directors shall oversee the accounting and financial reporting processes of the corporation. *See* N-PCL § 712-a(a). In addition, the N-PCL requires that for not-for-profits that are required to file an independent certified public accountant's audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, the board or a designated audit committee of the board comprised solely of independent directors must, upon completion of the audit, review and discuss with the independent auditor (a) any material risks and weaknesses in internal controls identified by the auditor, and (b) the adequacy of the corporation's accounting and financial reporting processes. *See*

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N-PCL § 712-a(b)(2)(A), (D). *See also* State of New York Attorney General’s Charities Bureau Guidance Document, “Internal Controls and Financial Accountability for Not-for-Profit Boards” (April 2015), *available at* [https://ag.ny.gov/sites/default/files/regulatory-documents/Charities\\_Internal\\_Controls.pdf](https://ag.ny.gov/sites/default/files/regulatory-documents/Charities_Internal_Controls.pdf).

<sup>19</sup> The board may delegate to the audit committee responsibility for reviewing and approving related party transactions and conflicts of interest. The N-PCL requires every New York not-for-profit corporation (regardless of size) to adopt a conflicts of interest policy applicable to directors, officers and “key person(s)” (as defined in the N-PCL). The N-PCL requires that such policy, among other things, include procedures for disclosing a conflict of interest or possible conflict of interest to a committee of the board or to the board, and procedures for a committee of the board or the board to determine whether a conflict exists. The N-PCL also provides that “[n]o corporation shall enter into any related party transaction unless the transaction is determined by the board, or an authorized committee thereof, to be fair, reasonable and in the corporation’s best interest at the time of such determination....” *See* N-PCL §§ 715, 715-a.

<sup>20</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>21</sup> The N-PCL requires that for not-for-profits that are required to file an independent certified public accountant’s audit report with the New York Attorney General pursuant to New York Executive Law § 172-b(1) and that had in the prior fiscal year, or reasonably expect to have in the upcoming year, annual gross revenue in excess of \$1 million, if the audit oversight duties set forth in N-PCL § 712-a are performed by an audit committee, the committee must report to the board on the committee’s activities. *See* N-PCL § 712-a(b)(4).

<sup>22</sup> IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Nominating and Governance Committee Charter

The board of a not-for-profit organization is typically responsible for nominating candidates to the board, for ensuring that the size, leadership and composition of the board are appropriate and for overseeing governance structure and policies, including the structure of the board committees and the organization's by-laws. The board may wish to establish a nominating and governance committee in order to assist with such responsibilities, however, it is not required by law to do so.

Nominating and governance committees may represent best practice for certain not-for-profit organizations. Whether it would be valuable for a not-for-profit organization to establish a nominating and governance committee will depend on the size and complexity of the particular organization. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

The following sample nominating and governance committee charter is intended to comport with generally accepted practices for nominating and governance committees of not-for-profit organizations. This sample provides only one example for a non-member organization, incorporating elements required by the New York Not-for-Profit Corporation Law (the "N-PCL") including the requirements of the Non-Profit Revitalization Act of 2013, as amended, applicable to New York not-for-profits. It is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample nominating and governance committee charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Nominating and Governance Committee Charter

### I. PURPOSES

The Nominating and Governance Committee (“Committee”) is appointed by the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) to: (1) develop and provide oversight of (a) implementation of policies and procedures regarding Board size, leadership and composition, and (b) Board Guidelines; (2) determine qualifications and characteristics required to become a director; (3) identify and screen individuals who are qualified to serve as directors; (4) recommend to the Board candidates for nomination and election or appointment to the Board, and its committees, or to fill Board vacancies; (5) assist in director orientation and continuing education programs; (6) coordinate and oversee self-evaluations of the Board and its committees; and (7) review on a regular basis the overall governance of the Organization and recommend amendments for approval by the Board where appropriate.<sup>1</sup>

### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>2</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

**[Independence.** Each member of the Committee shall be an “independent” director as determined in accordance with the Organization’s Board Guidelines. Any action duly taken by the Committee shall be valid and effective, whether or not the members of the Committee at the time of such action are later determined not to have satisfied the requirements for membership provided herein.]<sup>3</sup>

### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any director search or recruitment consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

#### **IV. COMMITTEE MEETINGS**

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting, and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

#### **V. KEY RESPONSIBILITIES**

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Oversee the process of selection and nomination of directors, including ensuring that director nominees meet the qualifications required by the certificate of incorporation, by-laws, and Board Guidelines, as applicable, and establish other criteria that are desirable for directors;
2. Identify and screen director candidates (including incumbent directors for potential renomination) consistent with criteria approved by the Board, and recommend to the Board for approval candidates for: (a) nomination for election or re-election to the Board and (b) any Board vacancies that are to be filled;
3. Review annually the relationships between directors, the Organization and members of management and recommend to the Board whether each director qualifies as "independent" under the definition of "independence" set forth in the Board Guidelines and applicable law;
4. Review annually the size, composition and leadership of the Board as a whole, its committees, and any advisory bodies including whether the Board, its committees and any advisory bodies reflect the appropriate balance of independence, sound judgment, business specialization, technical skills, fundraising and development ability, geographic representation, and other desired qualities, and recommend any appropriate changes to the Board;
5. [Coordinate and oversee a periodic self-evaluation of the role and performance of the Board, its committees, and any advisory bodies in the governance of the Organization;]<sup>4</sup>
6. Develop and recommend to the Board, review the effectiveness of, and recommend modifications as appropriate to, the Organization's committee structure and organizational documents, including the certificate of incorporation, by-laws and Board Guidelines;<sup>5</sup>
7. Coordinate with management to develop an appropriate director orientation and continuing education program, including identification of experienced directors as appropriate mentors of new directors;

8. Review emerging corporate governance issues and practices and make appropriate recommendations to the Board;
9. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>6</sup>
10. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>7</sup> and
11. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

<sup>1</sup> The N-PCL requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a). It is considered best practice for not-for-profit boards to delegate responsibility for director nominations and governance matters such as those set forth in this sample charter to a nominating and governance committee, but such a delegation is not required by law.

<sup>2</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>3</sup> It is considered a best practice for independent directors to be responsible for director nominations and governance matters, but independence is not required by law and is not always possible for organizations of small size. The bright-line tests for “independence” set forth in Internal Revenue Service (“IRS”) rules are different in some respects to the bright-line tests set forth in the N-PCL’s definition of “independent director,” for example, the required “look-back” period is different (the most recent tax year under IRS tests, compared with the past three years under New York tests).

The IRS considers a director to be “‘independent’ only if all four of the following circumstances applied at all times during the organization’s tax year: (1) [t]he member wasn’t compensated as an officer or other employee of the organization or of a related organization...except as provided in the religious exception .... [n]or was the member compensated by an unrelated organization or individual for services provided to the filing organization or to a related organization, if such compensation is required to be reported in Part VII, Section A [of Form 990]; (2) [t]he member didn’t receive total compensation exceeding \$10,000 during the organization’s tax year ... from the organization and related organizations as an independent contractor, other than reasonable compensation for services provided in the capacity as a member of the governing body;... (3) [n]either the member, nor any family member of the member, was involved in a transaction with the organization (whether directly or indirectly through affiliation with another organization) that is required to be reported on Schedule L (Form 990) for the organization’s tax year; (4) [n]either the member, nor any family member of the member, was involved in a transaction with a taxable or tax-exempt related organization (whether directly or indirectly through affiliation with another organization) of a type and amount that would be reportable on Schedule L (Form 990) if required to be filed by the related organization.... A member of the governing body isn’t considered to lack independence merely because of the following circumstances: (1) [t]he member is a donor to the organization, regardless of the amount of the contribution;” (2) the religious exception applies (meaning the member has taken a bona fide vow of poverty and either (a) receives compensation as an agent of a religious order or a section 501(d) religious or apostolic organization, but only under circumstances in which the member doesn’t receive taxable income, or (b) belongs to a religious order that receives sponsorship or payments from the organization or a related organization that do not constitute taxable income to the member); or (3) the member receives financial benefits from the organization solely in the capacity of being a member of the charitable or other class served by the organization in the exercise of its exempt function, so long as the financial benefits comply with the organization’s terms of membership. Instructions to Form 990, Part VI, Line 1b.

The N-PCL defines “independent director” to mean “a director who: (i) is not, and has not been within the last three years, an employee or a key person of the corporation or an affiliate of the corporation, and does not have a relative who is, or has been within the last three years, a key person of the corporation or an affiliate of the corporation; (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 of the corporation; (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 provided payments, property or services to, or received payments, property or services from, the corporation or an affiliate of the corporation if the amount paid by the corporation to the entity or received by the corporation from the entity for such property or services, in any of the last three fiscal years, exceeded the lesser of \$10,000 or 2% of such entity’s consolidated gross revenues if the entity’s consolidated gross revenue was less than \$500,000; \$25,000 if the entity’s consolidated gross revenue was \$500,000 or more but less than \$10 million; \$100,000 if the entity’s consolidated gross revenue was \$10 million or more; 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, the terms: ‘compensation’ does not include reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director...; and ‘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, or payments made by the corporation at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the

corporation are available to individual members of the public on the same terms, and such services received by the corporation are not available from another source.” N-PCL § 102(a)(21).

The N-PCL defines an “affiliate” of a corporation as “any entity controlled by, or in control of, such corporation.” N-PCL § 102(a)(19). The Instructions to Form 990 define a “related organization” to include, among others, “an organization that controls the filing organization,” “an organization controlled by the filing organization,” and “an organization controlled by the same person or persons that control the filing organization.” Instructions to Form 990, Glossary.

The definitions of “relative” in the N-PCL and “family member” in the Instructions to Form 990 are substantially the same. A “relative” or “family member” of a director is that person’s spouse, domestic partner, ancestors, brothers and sisters (whether whole or half-blood), children (whether natural or adopted), grandchildren, great-grandchildren and spouses or domestic partners of brothers, sisters, children, grandchildren and great-grandchildren. *See* N-PCL § 102(a)(22); Instructions to Form 990, Glossary.

A “key person” is defined in the N-PCL as any person, other than a director or officer, whether or not an employee of the corporation who (i) has responsibilities, or exercises powers or influence over the corporation as a whole similar to the responsibilities, powers, or influence of directors and officers; (ii) manages the corporation, or a segment of the corporation that represents a substantial portion of the activities, assets, income or expenses of the corporation; or (iii) alone or with others controls or determines a substantial portion of the corporation’s capital expenditures or operating budget. *See* N-PCL § 102(a)(25).

<sup>4</sup> Board and committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the board and its committees.

<sup>5</sup> This charter should be modified as appropriate if this committee (instead of the audit committee) has responsibility for approval of certain transactions and/or oversight of the conflicts of interest policy and/or whistleblower policy. *See* N-PCL §§ 715, 715-a, 715-b.

<sup>6</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>7</sup> IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Compensation Committee Charter

The board of a not-for-profit organization is responsible for determining and reviewing the compensation of the chief executive officer/executive director/president, other senior managers and “disqualified persons” (as defined in the Internal Revenue Code (the “IRC”)) and for ensuring that such compensation is reasonable. Compensation decisions of tax-exempt organizations are presumed reasonable if they are based on objective, documented and comparable information. The board may wish to establish a compensation committee in order to assist with such responsibilities, although it is not required by law to do so.

Tax-exempt organizations are required to disclose on their Form 990 whether, among other things, the process for determining compensation of certain key employees included review and approval by independent persons, comparability data and contemporaneous substantiation of the deliberation and decision.<sup>1</sup> The New York Not-for-Profit Corporation Law (the “N-PCL”), as amended by the Non-Profit Revitalization Act of 2013, applicable to New York not-for-profits, limits the extent to which a person can participate in any board or committee deliberations or vote with respect to such person’s compensation, and includes certain requirements with respect to the review and approval by disinterested directors of “related party transactions” such as compensation arrangements with officers and key persons.

Compensation committees may represent best practice for certain not-for-profit organizations, but one size does not fit all. Whether it would be valuable for a not-for-profit organization to establish a compensation committee will depend on the size of the particular organization and the complexity of its compensation policies. Governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

The following sample compensation committee charter is intended to comport with generally accepted practices for compensation committees of not-for-profit organizations. This sample provides only one example for a non-member organization, incorporating elements required by the N-PCL, as well as elements related to certain disclosure and other requirements under Internal Revenue Service (“IRS”) rules. It is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample compensation committee charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization’s certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Compensation Committee Charter

#### I. PURPOSES

The Compensation Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) to assist the Board in fulfilling its oversight of the Organization’s executive compensation policies and practices, including: (1) making recommendations to the independent directors with respect to the reasonable compensation of the Organization’s [Executive Director/Chief Executive Officer/President] (“[Executive Director/CEO/President]”); and (2) reviewing and approving the reasonable compensation of the Organization’s other managers, employees and any other persons who are in a position to exercise substantial influence over the affairs of the Organization (“key persons”).<sup>2</sup>

#### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>3</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

**[Independence.** Each member of the Committee shall be an “independent” director as required by applicable law and determined in accordance with the Organization’s Board Guidelines.<sup>4 5</sup> Any action duly taken by the Committee shall be valid and effective, whether or not the members of the Committee at the time of such action are later determined not to have satisfied the requirements for membership provided herein.]

#### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any compensation consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

#### IV. COMMITTEE MEETINGS

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate. The Committee shall meet at least [annually] with the [Executive Director/CEO/President] and any other officers or key persons the Committee or the Board deem appropriate to discuss and review the performance criteria and compensation levels of officers and key persons.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting, and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. Members of the Committee who have a financial or other interest in or otherwise have a conflict of interest with respect to any compensation arrangement to be voted on by the Committee (including with respect to such member's compensation or otherwise) are disqualified from deliberations and voting on such matter, but shall be determined to be present to constitute a quorum. The Committee shall otherwise establish its own rules of procedure.

#### V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Establish and review the Organization's overall management compensation philosophy and policy;
2. Review and approve the Organization's goals and objectives relevant to the compensation of the Organization's key executives, including annual performance goals and objectives;
3. Oversee compliance with the compensation policies and procedures and the terms of employment contracts;
4. Review [and approve]<sup>6</sup> any employment, compensation, benefit or severance agreement with officers and key persons;
5. Evaluate at least annually the performance of the key executives against the Organization's relevant goals and objectives, including the annual performance goals and objectives and, based on this evaluation, determine and approve (or recommend to the Board for approval in the case of the [Executive Director/CEO/President], to be voted on by the independent directors) the compensation level (including any incentive awards and any material perquisites) for officers and key persons, reviewing as appropriate, any agreement or understanding relating to their employment, incentive compensation or other benefits based on this evaluation;
6. Determine and approve the compensation level (including any incentive awards and any material perquisites) for other employees as the Committee or the Board may from time to time determine to be appropriate;

7. Ensure that compensation paid to the Organization’s employees is “reasonable,” such that it would ordinarily be paid for like services by similar organizations under similar circumstances. In determining if compensation is reasonable, the Committee will, where appropriate and available, obtain data (such as compensation surveys, third party offer letters or other objective data) as to comparability of compensation such as the compensation paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions;<sup>7</sup>
8. Review on a periodic basis the Organization’s management compensation programs, including any management incentive compensation plans as well as plans and policies pertaining to perquisites or other benefits, to determine whether they are reasonable and appropriate, properly coordinated and achieve their intended purpose(s), and recommend to the Board any appropriate modifications or new plans or programs;
9. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>8</sup>
10. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities (which should, among other things, document the basis for the Committee’s determination that compensation is reasonable);<sup>9</sup> and
11. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> See Form 990, Part VI, Lines 15a-b and related instructions. Disclosure is required regarding the process for determining compensation of the chief executive officer, executive director or top management official, and other officers or key employees of the organization. The Instructions to Form 990 define a “key employee” to mean an employee who meets all three of the following tests: (i) \$150,000 Test: Receives reportable compensation from the organization and all related organizations in excess of \$150,000 for the calendar year ending with or within the organization’s tax year. (ii) Responsibility Test: At any time during the calendar year ending with or within the organization’s tax year: (a) Has responsibilities, powers, or influence over the organization as a whole that is similar to those of officers, directors, or trustees; (b) Manages a discrete segment or activity of the organization that represents 10% or more of the activities, assets, income, or expenses of the organization, as compared to the organization as a whole; or (c) Has or shares authority to control or determine 10% or more of the organization’s capital expenditures, operating budget, or compensation for employees. (iii) Top 20 Test: Is one of the 20 employees other than officers, directors, and trustees who satisfy the \$150,000 Test and Responsibility Test with the highest reportable compensation from the organization and related organizations for the calendar year ending with or within the organization’s tax year. The Instructions to Form 990 define a “related organization” to include, among others, “an organization that controls the filing organization,” “an organization controlled by the filing organization,” and “an organization controlled by the same person or persons that control the filing organization.” Instructions to Form 990, Glossary.

<sup>2</sup> A “key person” is defined in the N-PCL as any person, other than a director or officer, whether or not an employee of the corporation, who (i) has responsibilities, or exercises powers or influence over the corporation as a whole similar to the responsibilities, powers, or influence of directors and officers; (ii) manages the corporation, or a segment of the corporation that represents a substantial portion of the activities, assets, income or expenses of the corporation; or (iii) alone or with others controls or determines a substantial portion of the corporation’s capital expenditures or operating budget. See N-PCL § 102(a)(25); IRC § 4958 and related regulations.

<sup>3</sup> The N-PCL requires committees designated by the board to consist of three or more directors. See N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. See DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>4</sup> A compensation arrangement between a New York not-for-profit organization and a director, officer or key person (each of whom would qualify as a “related party” pursuant to the N-PCL) would constitute a “related party transaction” requiring review and approval by disinterested directors pursuant to the N-PCL. See N-PCL §§ 102(a)(23)-(24), 715). The N-PCL requires that any director, officer or key person 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 his or her interest in the transaction. See N-PCL § 715(a). In addition, when a related party has a “substantial financial interest” in a related party transaction, the board or authorized board committee must, among other things, “consider alternative transactions to the extent available.” See N-PCL § 715(b). The N-PCL also prohibits any person from being present at or otherwise participating in any board or committee deliberation or vote concerning such person’s compensation, although such person may present background information or answer questions prior to the commencement of the relevant deliberations or voting. See N-PCL § 515(b). Similarly, related parties are not permitted to participate in deliberations or voting relating to relevant related party transactions; however, they may be requested to present background information or answer questions concerning such transaction prior to the commencement of deliberations or voting relating thereto. See N-PCL § 715(h).

<sup>5</sup> The N-PCL does not require a compensation committee of independent directors. However, Form 990 requires disclosure of whether the process for determining compensation of certain key employees included review and approval by independent persons. See note 1 above. The bright-line tests for “independence” set forth in IRS rules are different in some respects to the bright-line tests set forth in the N-PCL’s definition of “independent director,” for example, the required “look-back” period is different (the most recent tax year under IRS tests, compared with the past three years under New York tests).

The IRS considers a director to be “‘independent’ only if all four of the following circumstances applied at all times during the organization’s tax year: (1) [t]he member wasn’t compensated as an officer or other employee of the organization or of a related organization...except as provided in the religious exception .... [n]or was the member compensated by an unrelated organization or individual for services provided to the filing organization or to a related organization, if such compensation is required to be reported in Part VII, Section A [of Form 990]; (2) [t]he member didn’t receive total compensation exceeding \$10,000 during the organization’s tax year ... from the organization and related organizations as an independent contractor, other than reasonable compensation for services provided in the capacity as a member of the governing body...; (3) [n]either

the member, nor any family member of the member, was involved in a transaction with the organization (whether directly or indirectly through affiliation with another organization) that is required to be reported on Schedule L (Form 990) for the organization's tax year; (4) [n]either the member, nor any family member of the member, was involved in a transaction with a taxable or tax-exempt related organization (whether directly or indirectly through affiliation with another organization) of a type and amount that would be reportable on Schedule L (Form 990) if required to be filed by the related organization.... A member of the governing body isn't considered to lack independence merely because of the following circumstances: (1) [t]he member is a donor to the organization, regardless of the amount of the contribution;" (2) the religious exception applies (meaning the member has taken a bona fide vow of poverty and either (a) receives compensation as an agent of a religious order or a section 501(d) religious or apostolic organization, but only under circumstances in which the member doesn't receive taxable income, or (b) belongs to a religious order that receives sponsorship or payments from the organization or a related organization that do not constitute taxable income to the member); or (3) "the member receives financial benefits from the organization solely in the capacity of being a member of the charitable or other class served by the organization in the exercise of its exempt function, so long as the financial benefits comply with the organization's terms of membership." Instructions to Form 990, Part VI, Line 1b.

The N-PCL defines "independent director" to mean "a director who: (i) is not, and has not been within the last three years, an employee or a key person of the corporation or an affiliate of the corporation, and does not have a relative who is, or has been within the last three years, a key person of the corporation or an affiliate of the corporation; (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 of the corporation; (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 provided payments, property or services to, or received payments, property or services from, the corporation or an affiliate of the corporation if the amount paid by the corporation to the entity or received by the corporation from the entity for such property or services, in any of the last three fiscal years, exceeded the lesser of \$10,000 or 2% of such entity's consolidated gross revenues if the entity's consolidated gross revenue was less than \$500,000; \$25,000 if the entity's consolidated gross revenue was \$500,000 or more but less than \$10 million; \$100,000 if the entity's consolidated gross revenue was \$10 million or more; 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, the terms: 'compensation' does not include reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director...; and '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, or payments made by the corporation at fixed or non-negotiable rates or amounts for services received, provided that such services by and to the corporation are available to individual members of the public on the same terms, and such services received by the corporation are not available from another source." N-PCL § 102(a)(21).

The N-PCL defines an "affiliate" of a corporation as "any entity controlled by, or in control of, such corporation." N-PCL § 102(a)(19). The Instructions to Form 990 define a "related organization" to include, among others, "an organization that controls the filing organization," "an organization controlled by the filing organization," and "an organization controlled by the same person or persons that control the filing organization." Instructions to Form 990, Glossary.

The definitions of "relative" in the N-PCL and "family member" in the Instructions to Form 990 are substantially the same. A "relative" or "family member" of a director is that person's spouse, domestic partner, ancestors, brothers and sisters (whether whole or half-blood), children (whether natural or adopted), grandchildren, great-grandchildren and spouses or domestic partners of brothers, sisters, children, grandchildren and great-grandchildren. *See* N-PCL § 102(a)(22); Instructions to Form 990, Glossary.

<sup>6</sup> Consider whether the Compensation Committee should have the full authority for determining officers' compensation or if such authority should be reserved for the full Board (voted on by the independent directors). For example, it may be most appropriate for some organizations for the full Board (voted on by the independent directors) to approve compensation of the Director/CEO/President and the committee to approve compensation of all other officers and key persons.

<sup>7</sup> Compensation will be presumed reasonable under the relevant tax rules if: (1) the compensation arrangement is approved in advance by disinterested members of the board or the committee; (2) prior to making its determination, the board or committee obtained and relied upon appropriate data as to comparability of compensation such as the compensation paid by similarly situated organizations, both taxable and tax-exempt, for functionally comparable positions, which may include reviewing compensation surveys, actual written offers from similar organizations competing for the person's services, or other objective external data to establish comparable values for executive compensation (and for small organizations with gross receipts of less than \$1 million, appropriate comparability data includes data on compensation paid by three comparable organizations in

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the same or similar communities for similar services); and (3) the board or committee adequately and timely documented the basis for its determination that the compensation is reasonable concurrently with making that determination. See <https://www.irs.gov/charities-non-profits/charitable-organizations/rebuttable-presumption-intermediate-sanctions>; IRC § 4958 and related regulations; Form 990, Part VI, Lines 15a-b and related instructions. The N-PCL provides that a New York not-for-profit “may pay compensation in a reasonable amount to members, directors, or officers, for services rendered” and that related party transactions must be determined by the board to be “fair, reasonable and in the corporation’s best interest at the time of such determination.” N-PCL §§ 515(b), 715(a).

<sup>8</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>9</sup> The N-PCL requires that New York not-for-profits contemporaneously document in writing the basis for the board or authorized board committee’s approval of certain specified related party transactions, including the consideration of any alternative transactions. See N-PCL § 715(b). IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” See Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Executive Committee Charter

The board of a not-for-profit organization directs the affairs of the organization and is ultimately accountable for the organization's performance. The responsibilities of the board are wide-ranging and require the board to make decisions, ideally on a consensus basis. The boards of some not-for-profits may find that their size or structure makes it difficult for the board to make decisions efficiently and in a timely manner. Such boards may benefit by establishing an executive committee to make decisions on behalf of the board if required, provided it is appropriate to do so. However, one size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization.

Tax-exempt organizations are required to disclose to the Internal Revenue Service (the "IRS") on Form 990 whether the board has delegated broad authority to act on behalf of the board to an executive committee or similar committee, and to describe the committee's composition and authority.

This sample executive committee charter is intended to comport with generally accepted practices for executive committees of not-for-profit organizations. This sample provides only one example for a non-member organization, incorporating elements required by the New York Not-for-Profit Corporation Law (the "N-PCL") including the requirements of the Non-Profit Revitalization Act of 2013, as amended, applicable to New York not-for-profits, as well as elements related to certain disclosure requirements under IRS rules. It is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Executive Committee Charter

### I. PURPOSES

The Executive Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of [\_\_\_\_\_] (the “Organization”) to exercise the powers of the Board in relation to matters that arise between regularly scheduled Board meetings or when it is not practical or feasible for the Board to meet. The Committee is delegated the authority to act as the full Board when exercising the powers and authority under this charter, subject to the limitations listed below and applicable law.<sup>1</sup>

### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board<sup>2</sup> and shall include [the chair of each of the standing committees of the Board and any additional directors selected by the Board].<sup>3</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

### IV. COMMITTEE MEETINGS

The Committee shall meet as circumstances dictate. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee,

including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting, and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

## V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Act on behalf of the Board on matters that arise between scheduled Board meetings or when it is not practical or feasible for the Board to meet, to the extent permitted by applicable law and regulations, the certificate of incorporation and the by-laws. However, the Committee shall not have the power or authority to act on behalf of the Board with respect to the following matters:
  - a. Adopting, amending or repealing any provision of the Organization's certificate of incorporation or by-laws;
  - b. Amending the Organization's mission;
  - c. Filling Board vacancies;
  - d. Changing the membership of, or filling vacancies in, any committee of the Board;
  - e. Adopting an agreement of merger or consolidation;
  - f. Authorizing the sale, lease or exchange of all or substantially all of the Organization's assets;
  - g. Authorizing the dissolution of the Organization or the revocation of a dissolution;
  - h. Fixing compensation of directors for service on the Board or any committee;
  - i. Electing or removing officers and directors; and
  - j. Amending or repealing any resolution of the Board, which by its terms shall not be so amendable or repealable.<sup>4</sup>

[Consider whether other functions should be specifically reserved to the Executive Committee];

2. Call special meetings of the Board when required;
3. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>5</sup>
4. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>6</sup> and
5. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> The N-PCL requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a).

<sup>2</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>3</sup> The N-PCL requires the appointment of executive committee members by a majority of the entire board, provided that in the case of a board of thirty members or more, the appointment shall be made by at least three-quarters of the directors present at the time of the vote, if a quorum is present at that time. *See* N-PCL § 712(a).

<sup>4</sup> Certain duties are not able to be delegated to committees. *See, e.g.*, N-PCL § 712(a). For a Delaware nonstock corporation, *see* DGCL § 141(c)(2) for the actions which are not delegable to a committee and conform this document accordingly.

<sup>5</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>6</sup> The N-PCL requires that New York not-for-profits keep minutes of the proceedings of the board and any executive committee. *See* N-PCL § 621(a). Additionally, for appropriations for expenditures or accumulations of endowment funds, the N-PCL requires that the committee keep a contemporaneous record describing the consideration given to various factors enumerated in N-PCL § 553(a) and keep a record of the action taken. *See* N-PCL § 553. IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Finance and Investment Committee Charter

The board of a not-for-profit organization is typically responsible for the fiscal management of the organization, including the oversight of its finances and its planning and review of its finance and investment objectives. The board may wish to establish a finance and investment committee in order to assist with such responsibilities; however, it is not required by law to do so. The board may also wish to delegate to such finance and investment committee the responsibility of overseeing and implementing the investment policy required under the New York Prudent Management of Institutional Funds Act, added to the New York Not-for-Profit Corporation Law (the “N-PCL”) as Article 5-A in 2010.<sup>1</sup> Please see **Tab 22** for a sample investment policy.

Whether a not-for-profit organization would find it valuable to establish a finance and investment committee will depend on the financial resources and complexity of the organization. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization. The sample finance and investment committee charter is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization’s certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

## [NAME OF NOT-FOR-PROFIT ORGANIZATION]

### Finance and Investment Committee Charter

#### I. PURPOSES

The Finance and Investment Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of [\_\_\_\_\_] (the “Organization”) to assist the Board in fulfilling its oversight responsibilities relating to fiscal management by: (1) overseeing the management of financial assets; (2) reviewing investment policies and strategies; (3) reviewing financial results; (4) ensuring the maintenance of an appropriate capital structure; and (5) reviewing and recommending an annual operating budget for approval by the Board.<sup>2</sup>

Additionally, in order to assist the Organization in the proper and prudent management of its financial resources, the Committee will ensure that the Organization retains personnel, systems and investment managers capable of providing timely and accurate financial information to key decision-makers.

#### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>3</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

**Financial Literacy.** Committee members shall have a basic understanding of finance, accounting, investment management and fundamental financial statements.<sup>4</sup>

#### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any investment manager, consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.<sup>5</sup>

#### IV. COMMITTEE MEETINGS

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting, and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

#### V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Understand the Board's investment goals, risk tolerance level and spending plans in order to develop an investment strategy to meet these goals;
2. Oversee the implementation of and compliance with, periodically review and revise, as appropriate, the Organization's Investment Policy<sup>6</sup> including but not limited to:
  - a. hiring and terminating investment managers;
  - b. regularly reviewing investment performance results;
  - c. setting investment objectives;
  - d. establishing performance objectives and benchmarks;
  - e. devising the asset allocation strategy;
  - f. rebalancing the portfolio of the Organization, as necessary; and
  - g. restricting investments, as necessary;
3. Oversee the prudent management of the Organization's funds in compliance with applicable law, and specifically shall:
  - a. incur only investment fees and costs that are appropriate and reasonable in relation to the assets, the purposes of the Organization and the skills available to the Organization;<sup>7</sup>
  - b. consider the following factors when managing and investing the Organization's funds: general economic conditions; inflation or deflation; tax consequences; expected total return from income and appreciation of investments; other resources of the Organization; the

- needs of the Organization to make distributions and to preserve capital; an asset's special relationship or special value, if any, to the charitable purposes of the Organization; the role that each investment or course of action plays within the overall investment portfolio of the Organization;<sup>8</sup>
- c. make individual management and investment decisions about an individual asset not in isolation but rather in the context of the entire portfolio and as a part of an overall investment strategy having risk and return objectives reasonably suited to the Organization;<sup>9</sup>
  - d. diversify the Organization's investment portfolio, unless the Committee reasonably and prudently determines that, because of special circumstances, the Organization's purposes are better served without diversification (in which case the Committee shall review the decision not to diversify as frequently as circumstances require, but at least annually);<sup>10</sup> and
  - e. promptly upon receiving property, make and carry out decisions concerning the retention or disposition of the property, or to rebalance a portfolio, in order to bring the portfolio into compliance with the Organization's purposes, investment policy, distribution requirements and legal requirements;<sup>11</sup>
4. Review and advise investment managers on a regular basis regarding the form, content and frequency of financial information necessary for the Organization to fulfill its responsibilities;
  5. Direct management and investment managers, where necessary, to undertake longer-term financial planning to evaluate future financial needs;
  6. Receive and review on a quarterly basis investment performance statements and financial statements (statement of financial position, income statement and operating statement) relating to the then current year-to-date as well as key financial benchmarks the Committee deems relevant from time to time. These investment performance statements and financial statements may be accompanied by a narrative highlighting any financial issues and, where necessary, actions related thereto;
  7. Review annually an operating budget proposal by management for the next fiscal year to be approved by the Board;
  8. Approve the financing of capital projects and submit to the Board for approval, where material or otherwise appropriate;
  9. Review, approve and generally oversee the Organization's participation in any joint ventures or similar arrangements. If the Organization does propose to enter into a joint venture, the Committee will approve a joint venture policy and maintain the proper documentation establishing the overriding exempt purpose of the joint venture;
  10. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>12</sup>
  11. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>13</sup>

12. Coordinate with the Audit Committee, as necessary and appropriate; and
13. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> The New York Prudent Management of Institutional Funds Act governs the management and investment of funds held by New York not-for-profit corporations and certain other institutions.

<sup>2</sup> The N-PCL requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a). The N-PCL also provides that an organization may delegate management and investment functions to its committees, officers or employees; provided that the board acts in good faith with the care that a similarly situated person would exercise in selecting such persons to whom these functions are delegated. *See* N-PCL §§ 514, 554(f), 717.

<sup>3</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>4</sup> The N-PCL requires that members of the investment committee with special skills or expertise have a duty to use those skills or expertise in managing and investing the organization’s funds. *See* N-PCL § 552(e)(6).

<sup>5</sup> The N-PCL requires that in managing and investing an institutional fund, an organization may incur only costs that are appropriate and reasonable in relation to the assets, the purposes of the organization and the skills available to the organization. *See* N-PCL § 552(c)(1). An organization may delegate to an external agent the management and investment of an institutional fund to the extent that an organization could prudently delegate under the circumstances. *See* N-PCL § 554(a).

<sup>6</sup> The N-PCL requires each organization to adopt a written investment policy setting forth guidelines on investments and delegation of management and investment functions in accord with the standards of Article 5-A of the N-PCL. *See* N-PCL § 552(f).

<sup>7</sup> The N-PCL requires that an organization may incur only costs that are appropriate and reasonable in relation to the assets, the purposes of the organization and the skills available to the organization. *See* N-PCL § 552(c)(1).

<sup>8</sup> The N-PCL requires that in managing and investing an institutional fund, the following factors, if relevant, must be considered: (A) general economic conditions; (B) the possible effect of inflation or deflation; (C) the expected tax consequences, if any, of investment decisions or strategies; (D) the role that each investment or course of action plays within the overall investment portfolio of the fund; (E) the expected total return from income and the appreciation of investments; (F) other resources of the organization; (G) the needs of the organization and the fund to make distributions and to preserve capital; and (H) an asset’s special relationship or special value, if any, to the purposes of the organization. *See* N-PCL § 552(e)(1).

<sup>9</sup> The N-PCL requires that management and investment decisions about an individual asset must be made not in isolation, but rather in the context of the organization’s portfolio of investments as a whole and as a part of an overall investment strategy having risk and return objectives reasonably suited to the fund and to the organization. *See* N-PCL § 552(e)(2).

<sup>10</sup> The N-PCL requires that an organization diversify its investments unless the organization prudently determines that, because of special circumstances, the purposes of the organization are better served without diversification. An organization is required to review a decision not to diversify as frequently as circumstances require, but at least annually. *See* N-PCL § 552(e)(4).

<sup>11</sup> The N-PCL requires that, within a reasonable time after receiving property, an organization shall make and carry out decisions concerning the retention or disposition of the property or to rebalance a portfolio, in order to bring the organization’s investments into compliance with the purposes, terms and distribution requirements of the organization as necessary to meet other circumstances of the organization and the requirements of Article 5-A of the N-PCL. *See* N-PCL § 552(e)(5).

<sup>12</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>13</sup> For appropriations for expenditures or accumulations of endowment funds, the N-PCL requires that the committee keep a contemporaneous record describing the consideration given to various factors enumerated in N-PCL § 553(a) and keep a record of the action taken. *See* N-PCL § 553. IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any

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committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” See Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Strategic Planning Committee Charter

The board of a not-for-profit organization may wish to establish a strategic planning committee to periodically assess the performance of its mission and strategic plan; however, it is not required by law to do so.

Whether a not-for-profit organization would find it valuable to establish a strategic planning committee will depend on the financial resources and complexity of the organization. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization. The sample strategic planning committee charter is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT-ORGANIZATION]

## Strategic Planning Committee Charter

### I. PURPOSES

The Strategic Planning Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) to develop and monitor performance against the Organization’s mission and strategic plan.<sup>1</sup>

### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of [the chair of each of the committees of the Board] and any additional directors selected by the Board.<sup>2</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until his or her earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

### IV. COMMITTEE MEETINGS

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to and hear each other at the same time and each member can participate in all matters before the Committee,

including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

## V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Assess annually the Organization's success in achieving long-term funding and any program-related goals, as articulated in the Organization's mission and strategic plan adopted by the Board;
2. Review the mission and recommend to the Board amendments as the Committee deems appropriate;
3. Review the strategic plan and recommend to the Board modifications as the Committee deems appropriate, prior to the budget being developed for the next fiscal year;
4. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>3</sup>
5. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>4</sup> and
6. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> The New York Not-for-Profit Corporation Law (the “N-PCL”) requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a).

<sup>2</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>3</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>4</sup> IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Development Committee Charter

The board of a not-for-profit organization may wish to establish a development committee to assist with its fundraising and recruitment efforts; however, it is not required by law to do so.

Whether a not-for-profit organization would find it valuable to establish a development committee will depend on the financial resources and complexity of the organization. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization. The sample development committee charter is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT-ORGANIZATION]

## Development Committee Charter

### I. PURPOSES

The Development Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of \_\_\_\_\_ (the “Organization”) to raise financial and other resources for the Organization by: (1) assisting Board members in their own fundraising efforts; (2) recruiting potential donors; and (3) assisting staff in planning fundraising events.<sup>1</sup>

### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>2</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

### IV. COMMITTEE MEETINGS

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to

and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

## V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Assist and encourage Board members to reach out to potential donors [and make personally meaningful contributions of their own]<sup>3</sup>;
2. Endeavor to recruit new institutional donors;
3. Assist staff in planning and developing fundraising-related events, including benefits and other events designed to maintain existing donors and recruit new donors;
4. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>4</sup>
5. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>5</sup> and
6. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> The New York Not-for-Profit Corporation Law (the “N-PCL”) requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a).

<sup>2</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>3</sup> A personal giving expectation for Board members is not required by law, but is considered a best practice to promote Board engagement and demonstrate commitment to the Organization’s mission.

<sup>4</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>5</sup> IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email, or similar writings that explain the action taken, when it was taken, and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.

## Not-For-Profit Practice Group

### Sample Not-For-Profit Public Relations Committee Charter

The board of a not-for-profit organization may wish to establish a public relations committee to assist with the development and realization of its communications strategies; however, it is not required by law to do so.

Whether a not-for-profit organization would find it valuable to establish a public relations committee will depend on the financial resources and complexity of the organization. One size does not fit all – governance structures and processes should reflect and be tailored to meet the needs and circumstances of the particular organization. The sample public relations committee charter is intended to be a component of the flexible governance framework within which the board, assisted by its committees, directs the affairs of the organization. The sample charter should be interpreted in the context of all applicable laws and regulations, as well as in the context of the organization's certificate of incorporation and by-laws; it is not intended to establish, by its own force, any legally binding obligations.

Please note that various factors unique to a not-for-profit organization (including, among others, organizational structure, activities, life-cycle stage, funding mechanisms and applicable requirements of local, regional or national law) may affect the provisions that should be addressed. Accordingly, while this sample includes standards and provisions that may be generally appropriate for some not-for-profit organizations, different and additional provisions may be appropriate in particular circumstances.

# [NAME OF NOT-FOR-PROFIT ORGANIZATION]

## Public Relations Committee Charter

### I. PURPOSES

The Public Relations Committee (the “Committee”) is appointed by the Board of Directors (the “Board”) of [\_\_\_\_\_] (the “Organization”) to increase the profile of and awareness about the activities of the Organization towards target audiences such as potential donors and volunteers, and in the community generally.<sup>1</sup>

### II. COMMITTEE MEMBERSHIP

**Composition.** The Committee shall consist of three or more members of the Board.<sup>2</sup> Except as otherwise directed by the Board, a director selected as a Committee member shall continue to be a member for as long as such member remains a director or until such member’s earlier resignation or removal from the Committee. Any member may be removed from the Committee by the Board, with or without cause, at any time.

**Chair.** The Chair of the Committee shall be appointed from among the Committee members by, and serve at the pleasure of, the Board, shall preside at meetings of the Committee and shall have authority to convene meetings, set agendas for meetings and determine the Committee’s information needs, except as otherwise provided by the Board or the Committee. In the absence of the Chair at a duly convened meeting, the Committee shall select a temporary substitute from among its members to serve as chair of the meeting.

### III. AUTHORITY

In discharging its role, the Committee is empowered to inquire into any matter it considers appropriate to carry out its responsibilities, with access to all books, records, facilities and personnel of the Organization and, subject to the direction of the Board, the Committee is authorized and delegated the authority to act on behalf of the Board with respect to any matter necessary or appropriate to the accomplishment of its purposes.

The Committee shall have the sole discretion to retain or obtain advice from, oversee and terminate any consultant, legal counsel or other adviser to the Committee and be directly responsible for the appointment, compensation and oversight of any work of such adviser retained by the Committee, and the Organization will provide appropriate funding (as determined by the Committee) for the payment of reasonable compensation to any such adviser.

### IV. COMMITTEE MEETINGS

The Committee shall meet on a regularly scheduled basis, at least [two] times per year and additionally as circumstances dictate.

The Committee shall establish its own schedule of meetings. The Committee may also act by unanimous written consent of its members.

Notice of meetings shall be given to all Committee members, or may be waived, in the same manner as required for meetings of the Board. Any one or more members of the Committee may participate in a meeting of the Committee by means of a conference telephone (or similar communications equipment) or by electronic video screen communication, as long as all persons participating in the meeting can speak to

and hear each other at the same time and each member can participate in all matters before the Committee, including, without limitation, the ability to propose, object to and vote upon a specific action to be taken by the Committee. Participation by such means shall constitute presence in person at a meeting. A majority of the members of the Committee shall constitute a quorum for a meeting and the affirmative vote of a majority of members present at a meeting at which a quorum is present shall constitute the action of the Committee. The Committee shall otherwise establish its own rules of procedure.

## V. KEY RESPONSIBILITIES

The following responsibilities are set forth as a guide for fulfilling the Committee's purposes in such manner as the Committee determines is appropriate:

1. Develop relationships with organizations and individuals external to the Organization, including media outlets, public relations firms and advertising agencies where appropriate, to increase awareness of the Organization, especially in donor and volunteer communities;
2. [Conduct a periodic self-evaluation of the performance of the Committee, including its effectiveness and compliance with this charter, and recommend to the Board such amendments of this charter as the Committee deems appropriate;]<sup>3</sup>
3. Report regularly to the Board on Committee findings, recommendations and any other matters the Committee deems appropriate or the Board requests, and maintain minutes or other records of Committee meetings and activities;<sup>4</sup> and
4. Undertake such other responsibilities as the Board may delegate or assign to the Committee from time to time.

ENDNOTES

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<sup>1</sup> The New York Not-for-Profit Corporation Law (the “N-PCL”) requires that authority delegated to committees of the board be set forth in the certificate of incorporation, by-laws or resolutions of the board. *See* N-PCL § 712(a).

<sup>2</sup> The N-PCL requires committees designated by the board to consist of three or more directors. *See* N-PCL § 712(a). The Delaware General Corporation Law (the “DGCL”) only requires that committees consist of one or more directors. *See* DGCL § 141(c)(2). While there is no specific requirement with respect to the size of this committee, having at least three members is a best practice.

<sup>3</sup> Committee evaluations are not required by law, but are considered a best practice to confirm the appropriate composition and operation of the Committee.

<sup>4</sup> IRS Form 990 requires disclosure of whether the organization contemporaneously documents, by any means permitted by state law, the meetings held or written actions undertaken by the board and any committee authorized to act on behalf of the board. The related instructions provide that “[d]ocumentation permitted by state law can include approved minutes, email or similar writings that explain the action taken, when it was taken and who made the decision. For this purpose, *contemporaneous* means by the later of (1) the next meeting of the governing body or committee (such as approving the minutes of the prior meeting), or (2) 60 days after the date of the meeting or written action.” *See* Form 990, Part VI, Lines 8a-b and related instructions.