

# Memorandum

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## Enactment of Additional Amendments to the New York Non-Profit Revitalization Act

December 2, 2016

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The New York Non-Profit Revitalization Act of 2013 (the “Act”) was enacted into law on December 18, 2013 and generally took effect as of July 1, 2014.<sup>1</sup> The Act has been previously reformed by both technical and substantive amendments.<sup>2</sup> The most recent amendment (the “Amendment”) was enacted on November 28, 2016 and will generally take effect as of May 27, 2017. The substantive provisions of the Amendment are summarized below.

### **I. Board Governance.**

- *Under the Amendment, two-thirds of the entire board may approve an employee’s service as board chair.*
- The Act originally prohibited an employee of a not-for-profit corporation from serving as the chair of the board or holding any other title with similar responsibilities.
- The Amendment provides an exception to the prohibition and permits an employee of a not-for-profit corporation to serve as the chair of the board or hold another title with similar responsibilities where approved by two-thirds of the entire board, as long as the basis for the approval is contemporaneously documented in writing.
- This provision has an early effective date of January 1, 2017.

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<sup>1</sup> For more information regarding the Act, please see our Memorandum “Enactment of the New York Non-Profit Revitalization Act of 2013,” dated December 30, 2013, available [here](#).

<sup>2</sup> For more information regarding prior amendments to the Act, please see our Memorandum “Enactment of Amendments to the New York Non-Profit Revitalization Act,” dated December 23, 2015, available [here](#).

## II. Related Party Transactions.

- *The Amendment modifies the related party transaction requirements by excluding certain transactions and permitting ratifications of related party transactions entered into without adherence to the requisite approval procedures.*
- The Act introduced the term “related party transaction,” which is defined as a transaction, agreement or other arrangement in which a related party has a financial interest and in which the not-for-profit corporation or charitable trust or an affiliate thereof is a participant.
- The Amendment excludes specified transactions from the definition of “related party transaction.” A transaction will not be considered 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 served by the not-for-profit corporation or charitable trust 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. The Amendment does not provide guidance regarding either when a transaction or financial interest may be considered *de minimis* or the types of transactions that are not customarily subject to board review and approval.
- The Act prohibited entry into any related party transaction unless the transaction was determined by the board to be fair, reasonable and in the best interest of the not-for-profit corporation or charitable trust. Under the Act, enhanced review is required for related party transactions involving a charitable corporation or charitable trust and in which a related party has a substantial financial interest.
- The Amendment clarifies that the related party transaction approval requirements may be satisfied by action of either the board or an authorized committee of the board.
- The Amendment also permits ratification of related party transactions and provides defenses against claims of violations of the related party transaction approval requirements. Under the Amendment, in an action by the attorney general with respect to a related party transaction not approved in accordance with the applicable related party transaction approval requirements at the time it was entered into, it will be a defense that: (i) the transaction was fair, reasonable and in the best interest of the not-for-profit corporation or charitable trust at the time it approved the transaction; and (ii) 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 best interest of the not-for-profit corporation or charitable trust at the time it approved the transaction; and, with respect to any related party transaction involving a charitable corporation or charitable trust 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 trustees 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 not-for-profit corporation or charitable trust complies with the applicable related party transaction approval requirements in the future. In an action by any party other than the attorney general, it will be a defense that a transaction was fair, reasonable and in the best interest of the not-for-profit corporation or charitable trust at the time it approved the transaction.

### III. Independence.

- *The Amendment allows a broader category of directors or trustees to qualify as independent by narrowing the types of payments that will be disqualifying. The Amendment also clarifies that responsibility for administration of the conflict of interest policy and whistleblower policy is not limited to independent directors or independent trustees.*
- The Act introduced the terms “independent director” and “independent trustee” and restricted audit oversight matters with respect to certain not-for-profit corporations and charitable trusts to their purview.
- The Amendment narrows the types of payments that will disqualify a director or trustee from serving as an independent director or independent trustee. Specifically, a director or trustee will be disqualified as an independent director or independent trustee because he or she is a current employee of or has a substantial financial interest in, or has a relative who is a current officer of or has a substantial financial interest in, an entity that has provided payments, property or services to, or received payments, property or services from, the not-for-profit corporation or charitable trust or an affiliate thereof only where the amount paid to or received from the entity for such property or services, in any of the last three fiscal years, exceeded the following: the lesser of ten thousand dollars or two percent of the entity's consolidated gross revenues if the entity's consolidated gross revenue was less than five hundred thousand dollars; twenty-five thousand dollars if the entity's consolidated gross revenue was five hundred thousand dollars or more but less than ten million dollars; one hundred thousand dollars if the entity's consolidated gross revenue was ten million dollars or more. In addition, the Amendment provides that for these purposes, the term “payment” does not include payments made at fixed or non-negotiable rates or amounts for services received, as long as the services are available to the public on the same terms, and any services received are not available from another source.
- The Act provided that the audit committee or another committee comprised solely of independent directors was required to oversee the adoption, implementation of, and compliance with the conflict of interest policy and whistleblower policy, in addition to having audit oversight responsibilities. However, the audit oversight provisions of the Act are not applicable to all not-for-profit corporations and charitable trusts that are required to adopt a conflict of interest policy or a whistleblower policy.
- The Amendment eliminates from the audit oversight provisions the references to oversight of conflict of interest policy and whistleblower policy matters. The Amendment makes clear that disinterested, not

independent, members of the board are responsible for overseeing the adoption, implementation of, and compliance with the conflict of interest policy and the whistleblower policy.

#### IV. Key Persons.

- *The Amendment clarifies that the related party transaction and conflicts of interest provisions, as well as the independence disqualifications, apply to individuals with specified power or influence, regardless of whether they are employees.*
- The Act, as amended, defined a “key employee” as a person in a position to exercise substantial influence over the affairs of the not-for-profit corporation or charitable trust, within the meaning of section 4958(f) of the Internal Revenue Code of 1986, as amended (the “Code”) and the Treasury Regulations thereunder.
- Rather than relying on references to the Code and Treasury Regulations, the Amendment replaces the term “key employee” with the term “key person.” The Amendment defines a “key person” as any person, other than a director, trustee or officer, whether or not an employee who: (i) has responsibilities, or exercises powers or influence over the not-for-profit corporation or charitable trust as a whole similar to the responsibilities, powers, or influence of directors or trustees and officers; (ii) manages the not-for-profit corporation or charitable trust, or a segment of it that represents a substantial portion of the activities, assets, income or expenses of the not-for-profit corporation or charitable trust; or (iii) alone or with others controls or determines a substantial portion of the capital expenditures or operating budget of the not-for-profit corporation or charitable trust.
- Under the Amendment, the terms “related party,” “independent director” and “independent trustee” refer to key persons in lieu of key employees. In addition, provisions related to the jurisdiction of the supreme court also apply to key persons. As a result, the Amendment clarifies that the related party transaction provisions, the conflict of interest policy provisions, and the independence disqualifications apply to individuals with specified power or influence, regardless of whether they are employees.

#### V. Committees of the Board.

- *The Amendment eliminates procedural burdens in forming and populating committees of the board.*
- Under the Act (and prior law), a committee of the board may be designated, where authorized under a not-for-profit corporation’s certificate of incorporation or by-laws, only by action of a majority of the entire board.
- Under the Amendment, committees of the board may be created by the certificate of incorporation, the by-laws or action of the board (*i.e.*, a majority of the directors present at a meeting at which there is a quorum).
- Under the Amendment, members of most committees of the board may also be appointed by action of the board. However, the appointment of members of an executive (or similar) committee continues to require

action by a majority of the entire board, except in the case of a board of at least thirty members, where action by at least three-quarters of a quorum is sufficient. In addition, ex-officio members of specific committees may be designated in the by-laws.

- The Amendment clarifies that in addition to the existing prohibitions on: (i) submitting to members any action requiring the members' approval; (ii) filling vacancies on the board or any committee; (iii) fixing compensation of the directors for serving on the board or any committee; (iv) amending, repealing or adopting by-laws; and (v) amending or repealing any resolution of the board that is not by its terms subject to such amendment or repeal, committees may not have the power to: (1) elect or remove officers; (2) approve a merger or plan of dissolution; (3) adopt resolutions recommending to the members action on the sale, lease, exchange or other disposition of all or substantially all of the assets or, if there are no members entitled to vote, approve such transaction; or (4) approve amendments to the certificate of incorporation.
- The Amendment eliminates the statement that provisions of the New York Not-for-Profit Corporation Law (including the Act) applicable to officers generally apply to members of committees of the corporation.

## VI. Other.

- *Conflict of Interest Policies.* The Amendment adds a requirement that each conflict of interest policy include procedures for disclosing possible conflicts of interest in addition to conflicts of interest. In addition, it must include procedures for the board or a committee of the board to determine whether a conflict of interest exists.
- *Whistleblower Policies.* The Amendment adds a requirement that each whistleblower policy provide that the person who is the subject of a whistleblower complaint not be present at or participate in board or committee deliberations or voting related to the complaint, except, upon request of the board or committee, to present background information or answer questions in advance of deliberations or voting. The Amendment also requires that no employee of the not-for-profit corporation or charitable trust participate in any board or committee deliberations or voting relating to administration of the whistleblower policy.<sup>3</sup>

The Amendment can be found at

<https://www.nysenate.gov/legislation/bills/2015/a10365/amendment/b>

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<sup>3</sup> Although there is no express private right of action, it should be noted that the whistleblower policy provisions of the Act were recently found to include an implied private right of action. *See Pietra v. Poly Prep Country Day Sch.*, Index No. 506586/2015 (Sup. Ct. Kings. Cnty. Oct. 24, 2016).

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