Leadership Message

Greetings from the Nonprofit Organizations Committee Chair.

My recent travels abroad reminded me how much we have to learn from other countries about nonprofit organizations. Lost in the large North American nonprofit sector, we often forget that the Canadian and U.S. systems for classification, organization, regulation, and taxation of such entities are not the only way that they can be treated. In most of the rest of the world, nonprofits are called "non-governmental organizations" or "NGOs." The name alone lets you know that there is a world of difference in the perception of such organizations in other countries.

In North America, the most outstanding feature is that these organizations, whether charitable or not, is perceived to be that they do not strive to make a distributable profit. The key distinction is thus a way to divide up the private sector between for-profit and non-profit entities. The term "non-governmental organization" may have arisen primarily in the context of international organizations, where nonprofit advocacy groups, many of them non-charitable, have long been recognized as participants in the decision-making process. For-profit entities are not even a part of the calculus as a matter of perception, and the emphasis appears to be more on NGOs as assistants to governments, playing a primary role in social organization.

Nevertheless, private nonprofits or NGOs, particularly charities, play a significant role in many countries, often dating back to the time when religious organizations were the primary providers of the social safety net. Despite different legal systems, NGOs (like North American nonprofits) are a topic of public interest for similar reasons. Headlines abroad indicate that there were concerns with insufficient funds to accomplish worthy missions, misuse of government and donated funds, overly generous executive compensation, inappropriate relationships with donors, maltreatment of staff and beneficiaries.

We have much to learn from the ways that foreign legal systems deal with these issues. For example, Israel is considering a partial tax credit to encourage donations. Several countries are considering different types of curbs or oversight of executive compensation. These issues are of interest directly to North American-based organizations with international operations like foreign-aid charities and international multilevel professional groups. But indirectly, we can learn alternative approaches that work well and those that don't, which is useful when developing our own systems both through formal regulation and through internal self-governance approaches. Historically, the Nonprofit Organizations Committee has hosted several CLE programs on the way different legal systems treat their nonprofit organizations. There have been programs on the laws of Canada, Mexico, and the Far East. In North America, we often re-invent the wheel rather than look outside our own experience for models. While it is often hard with busy caseloads and limited foreign language knowledge to keep up with the treatment nonprofits in foreign lands, the rewards can be significant. The Nonprofit Organizations Committee will continue to search for ways to include this valuable perspective in its programs.

Michael E. Malamut
Chair, Nonprofit Organizations Committee
**Article Writers Wanted**

The Newsletter Editorial Board is seeking articles on nonprofit law subject matter to include in future newsletters. There is no length requirement. If you are interested in submitting an article, please contact:

- Megan Christensen at Christensen@blankrome.com or
- David Levitt at levitt@adlercolvin.com or
- Cari Campbell at cari@campbell-legal.com or
- Matthew Wright at matthew@mgwrightlaw.com

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**Submit Nominations for the 2014 Outstanding Nonprofit Lawyer Awards**

The Committee on Nonprofit Organizations is calling for nominations for the 2014 Outstanding Nonprofit Lawyer Awards. These Awards are given annually in the following categories: Academic, Attorney, Nonprofit In-House Counsel, Young Attorney (under 35 or in practice for less than 10 years) and the Vanguard Award (for lifetime commitment/achievement).

For a nomination form, go to the Nonprofit Lawyer Awards Subcommittee's webpage and look under "Nonprofit Lawyer Awards Documents." You can also find there a list of prior award recipients. **Nominations are due by March 10, 2014.**

The Awards will be announced at the Business Law Section's Spring Meeting in Los Angeles, CA April 10-12.

Send nomination forms by March 10, 2014 to:

William Klimon
Caplin & Drysdale
Suite 1100
One Thomas Circle, NW
Washington, DC 20005
(202) 862-5022
(202) 429-3301 (fax)
wklimon@capdale.com

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**The Nonprofit Committee Needs You!**

The Committee is in search of a person to serve as the Chair of the Trade and Professional Associations Subcommittee. For more information or to volunteer for this position, please contact Michael Malumut (michael@michaelmalamut.com).

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**Two Part Webinar Series for the "Non" Nonprofit Lawyer**

The popular webinar series "Nonprofit Issues for the Non-Nonprofit Lawyer" returns on January 15, 2014. This two webinar series targets lawyers whose practice does not exclusively focus on the representation or formation of nonprofit organizations but who sit on the board of a nonprofit organization or periodically assist public charitable nonprofit entities. It can also be a great refresher course or update course. Both of the live webinars will provide practical drafting advice on essential nonprofit entity documents and provide participants with an opportunity to ask questions. The speakers include experts in the nonprofit area including a representative from the Internal Revenue Service.

This series follows a three-part series in 2013. This year's webinars will focus on documentation issues. The first 90-minute webinar (http://apps.americanbar.org/cle/programs/t14egd1.html), to be held on January 15 at 1:00 PM (Eastern), will focus on essential nonprofit entity documents - articles of incorporation, bylaws and selected governing policies. The second 90-
minute program (http://apps.americanbar.org/cle/programs/t14eff1.html), to be held on January 22 at 1:00 PM (Eastern), will focus on tax documents, and in particular the application for tax-exempt status (Form 1023) and annual return (Form 990).

The price for Business Law Section members is $125 per webinar.

**Special Offer for Webinar Participants**: Save 20% on Nonprofit Governance Library (Product Code 5070392P) or on each book individually. Visit www.ShopABA.org and enter discount code NONPROFIT14 at checkout to save on nonprofit books published by the ABA Business Law Section.

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Nonprofit Lawyer Profile: Robert Wexler

The Nonprofit Organizations Committee of the Business Law Section and the Exempt Organizations Committee of the Tax Law Section both address issues of importance to attorneys representing nonprofit organizations. Robert Wexler is the recent incoming Chair of the Tax Section Exempt Organizations Committee.

Rob is a principal of Adler & Colvin in San Francisco. His practice focuses on tax and corporate matters for nonprofit organizations and their donors. He has been representing nonprofit organizations for 28 years and enjoys the satisfaction that comes from helping to foster charitable and socially beneficial projects.

In recent years, Rob has developed an interest and expertise in social enterprise, which involves applying business and market-based approaches to solving social problems and pursuing earned revenue strategies to achieve a double- or triple- (financial, social, environmental) bottom line. He advises both nonprofit organizations and social entrepreneurs on developing the most effective legal framework to pursue their proposed social enterprise activities, whether through a nonprofit entity, for-profit vehicle, or some combination of the two.

Rob spent significant time as part of a working group developing legislation to create the flexible purpose corporation in California, which became available in 2012. The objective of the flexible purpose corporation is to facilitate the organization of companies that combine profitability with a broader social or environmental purpose and allow them greater flexibility under the law to pursue these purposes. Rob also helped found the San Francisco chapter of the Social Enterprise Alliance, a membership organization that represents the social enterprise sector.

Rob believes that hybrid entities will continue to evolve and will become increasingly relevant for the young and socially conscious entrepreneurs emerging today.

As chair of the Tax Law Section Exempt Organizations Committee, Rob is open to ideas for how his committee might collaborate with the Nonprofit Organizations Committee to improve the law for nonprofit organizations.

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Feature Article: Nonprofit Revitalization Act Impacts New York Nonprofits and Organizations Registered to Solicit Contributions in the State
By Kimberly A. Lowe, Fredrikson & Byron, P.A. and Matthew Norris, J.D. Candidate, 2014, University of Minnesota Law School

On December 18, 2013, New York’s Governor Andrew Cuomo ushered in a new era of nonprofit governance when he signed into law the Nonprofit Revitalization Act. The Act, which unanimously passed the state’s legislature, is the first major reform to New York's nonprofit laws in forty years.

Nonprofit corporations incorporated under New York law, which include large national organizations such as the American Heart Association and Planned Parenthood, are directly affected by the new law. Some provisions, however, apply to any nonprofit corporation registered in New York to solicit charitable donations.

New York Attorney General Eric Schneiderman says the Act aims to "reduce unnecessary and outdated burdens on nonprofits" while "enhancing nonprofit governance and oversight to prevent fraud and improve public trust." Input from leaders of large and small New York nonprofit corporations, who issued a comprehensive report to the attorney general in 2012, shaped the legislation. Read more...

National Updates

Megan A. Christensen, Blank Rome LLP, Washington, DC

1. IRS Provides Options for Automatically Revoked Organizations to Apply for Reinstatement.

IRS Revenue Procedure 2014-11, issued on January 2, 2014, provides four options for applying for reinstatement of tax-exempt status for those organizations whose exemption has been revoked for failure to file the required annual forms or notices (Form 990 series) for three consecutive years. The four options are described as (a) for organizations eligible to file either Form 990-EZ or Form 990-N and have not previously had tax-exempt status automatically revoked ("Streamlined Retroactive Reinstatement Process"); (b) for organizations not eligible to use the Streamlined Retroactive Reinstatement Process, if it applies not later than 15 months after the later of the Revocation Letter or the date on which the IRS posted the organization's name on the Revocation List ("Retroactive Reinstatement Process (Within 15 Months of Revocation)"); (c) if more than 15 months has passed since the later of the Revocation Letter or posting on the Revocation List, an organization may apply for retroactive reinstatement only under the "Retroactive Reinstatement Process"; or (d) the "Post-Mark Date Process" for any organization, including those eligible for any other reinstatement process. The Revenue Procedure also explains how the new procedures apply to pending and recently approved applications, and modifies and supersedes Notice 2011-44.

2. IRS Issues Interim Guidance Regarding Supporting Organizations.

On December 23, 2013, the IRS issued Notice 2014-4 providing interim guidance for organizations described in Section 509(a)(3) that are operated in connection with the public charities they support ("Type III Supporting Organizations"). Type III Supporting Organizations are divided into two categories - those that are "functionally integrated" and those that are not. Notice 2014-4 provides interim guidance for Type III Supporting Organizations that seek to qualify as functionally integrated by supporting a governmental supported organization. Under the Notice, until the earlier of the date final regulations are published under Treasury Regulation Section 1.509(a)-4(i)(4)(iv) or the first day of the organization's third taxable year beginning after 2013, a Type III Supporting Organization will be treated as functionally integrated if it (1) at least one supported organization is a governmental entity to which the Type III Supporting Organization is responsive within the meaning of the...
Treasury Regulations, and (2) engages in activities on behalf of such governmental entity that perform the functions of, or carry out the purposes of such governmental entity and "that, but for the involvement of the supporting organization, would normally be engaged in by the governmental supported organization itself."

On December 10, 2013, Karen Schiller, Acting Director, Exempt Organizations, Rulings and Agreements, issued a memorandum to provide interim administrative guidance regarding the processing and review of exemption applications under Section 501(c)(3) that indicate that the applicant may be involved in political campaign intervention for which additional development is necessary to determine qualification for exemption. The memorandum is directed to the Exempt Organizations Determination Unit and Exempt Organizations Determinations Quality Assurance. The memorandum states that the following activities may suggest the potential for political campaign intervention: voter registration; inaugural and convention host committees; post-election transition teams; voter guides; voter polling; get out the vote drives; events at which candidates speak; communications expressing approval or disapproval of candidates' positions or actions; or other activities that appear to support or oppose candidates for public office.

4. IRS Issues Notices Regarding Charitable Hospitals.
The IRS has issued two Notices related to charitable hospitals regarding the requirements of Section 501(r) of the Internal Revenue Code. Notice 2014-2 confirms that hospital organizations can rely on proposed regulations under section 501(r) of the Internal Revenue Code published on June 26, 2012, and April 5, 2013, pending the publication of final regulations or other applicable guidance. Notice 2014-3 contains a proposed revenue procedure that provides correction and disclosure procedures under which certain failures to meet the requirements of § 501(r) of the Internal Revenue Code will be excused for purposes of § 501(r)(1) (establishing the four requirements for charitable hospitals) and 501(r)(2)(B) (hospital organizations with more than one hospital facility). Notice 2014-3 requests comments regarding the procedures set forth in the proposed revenue procedures.

State Updates

Emily Chan, Adler & Colvin, San Francisco, CA

1. California
On September 6, 2013, Governor Jerry Brown signed into law AB 491. Effective January 1, 2014, AB 491 amends the California Corporations Code to allow California nonprofit and for-profit corporations to take certain actions relating to procedures such as notice and quorum, and adopt special governance provisions in their bylaws for purposes of conducting the corporation's ordinary business in anticipation of or during an emergency. An "emergency" includes events such as a natural catastrophe, a terrorist attack, or a state of emergency proclaimed by a governor or the President.

2. Massachusetts
On December 19, 2013, Attorney General Martha Coakley released a 91-page report "Massachusetts Public Charities CEO Compensation Review" that examines chief executive officer (CEO) compensation of 25 of the largest public charities in Massachusetts. The report also previews a prototype of "Schedule EC," the Attorney General's proposed expanded reporting requirement on CEO compensation to be introduced in early 2014 for certain nonprofit organizations in Massachusetts.

3. New York
On December 18, 2013, Governor Andrew Cuomo signed into law the Nonprofit Revitalization Act of 2013 which is intended to (1) enhance nonprofit governance and oversight to prevent fraud and improve public trust; and (2) reduce unnecessary and outdated burdens on nonprofits. The Nonprofit Revitalization Act is the state’s first overhaul of its not-for-profit corporation law in over 40 years. See the Feature Article of this newsletter above, for more information.
On December 18, 2013, New York’s Governor Andrew Cuomo ushered in a new era of nonprofit governance when he signed into law the Nonprofit Revitalization Act. The Act, which unanimously passed the state’s legislature, is the first major reform to New York’s nonprofit laws in forty years.

Nonprofit corporations incorporated under New York law, which include large national organizations such as the American Heart Association and Planned Parenthood, are directly affected by the new law. Some provisions, however, apply to any nonprofit corporation registered in New York to solicit charitable donations.

New York Attorney General Eric Schneiderman says the Act aims to “reduc[e] unnecessary and outdated burdens on nonprofits” while “enhancing nonprofit governance and oversight to prevent fraud and improve public trust.” Input from leaders of large and small New York nonprofit corporations, who issued a comprehensive report to the attorney general in 2012, shaped the legislation.

The Act will take effect July 1, 2014. Key provisions of the Act include:

**Provisions Applicable to Both New York Nonprofit Corporations and Any Nonprofit Corporation Registered to Solicit Contributions in New York.**

- **New Audit Requirements and Thresholds:** The Act raises the annual gross revenue threshold triggering an audit by an independent certified public accountant from $250,000 to $500,000 and the threshold amount that triggers a review by an independent certified public accountant from $100,000 to $250,000. The audit thresholds will increase to $750,000 in 2017 and $1 million in 2021. The Act grants the attorney general authority to require an organization with gross revenue in excess of $250,000 to obtain an audit by a certified public accountant within 120 days of the attorney general’s request.

- **Audit Oversight Obligations:** For nonprofit corporations required to submit an annual independent CPA audit, the board, or an audit committee comprised of only independent directors, shall (1) oversee the accounting and financial reporting process and the audit, (2) annually retain or renew the retention of an independent auditor, and (3) review the results of the audit and any related management letter with the independent auditor. Additional requirements apply to organizations with annual revenue above $1 million. If the full board of directors remains responsible for audit oversight, only independent directors may participate in any deliberations relating to the audit.

- **Defines “Independent Director”:** To be an independent director, the Act states that a director must not (1) be an employee or have been an employee of the nonprofit corporation or an affiliate of the nonprofit corporation within the last three years; (2) have a relative who is, or has been within the last three years, a key employee of the nonprofit corporation or an affiliate; (3) receive, or have a relative who has received, over $10,000 in direct compensation from the nonprofit corporation or an affiliate in any of the last three fiscal years—exempting reimbursement for expenses reasonably incurred and reasonable compensation for services as a director; (4) be a current employee or have a substantial financial interest in any entity that has made payments to or received payments from the nonprofit corporation that exceed the lesser of $25,000 or 2 percent of the entity’s consolidated gross revenues—not including charitable contributions but including membership dues—in any of the last three fiscal years; (5) have a relative who is a current officer of or has a substantial financial interest in any entity that has made payments to or received payments from the nonprofit that exceed the lesser of $25,000 or 2 percent of the entity’s consolidated gross revenues—not including charitable contributions—in any of the last three fiscal years. It is important to note that these revised statutory provisions apply to both
nonprofit corporations incorporated under New York law and organizations formed under the laws of another jurisdiction that are registered to solicit charitable contributions in New York.

Provisions Applicable to Any New York Nonprofit Corporation

- **Allows Electronic Meeting Notices and Participation:** The Act now allows membership meeting notices, waivers of notice, and votes requiring unanimous written consent to be conducted by fax or electronic transmission, such as email. Board members may also now participate in meetings via videoconference, Skype, and other technology allowing all people participating in the meeting to hear each other at the same time. These electronic communication methods are not permitted if expressly prohibited by a nonprofit corporation’s bylaws.

- **Prohibits Individuals from Deliberating or Voting on Their Own Compensation:** The Act prohibits any person from voting on or being present at or otherwise participating in any board or committee deliberation regarding their own compensation, and the nonprofit corporations must prepare meeting minutes reflecting such an abstention and recusal. The Act does allow these individuals to provide background information or answer questions at a meeting prior to deliberations and voting.

- **Prohibits Employees from Serving as Board Chair:** The Act prohibits employees of the nonprofit corporation to serve as board chair or hold any other title with similar responsibilities.

- **Revises Requirements for Related Party Transactions:** The Act prohibits related party transactions unless the board determines the transaction is “fair, reasonable and in the [nonprofit] corporation’s best interest at the time of such determination.” Directors, officers, or key employees who have any interest in a related party transaction must disclose in good faith to the board the material facts concerning such interest. If the related party transaction involves a charitable corporation in which a related party has a substantial financial interest, the board must (1) consider alternative transactions to the extent available prior to entering into the transaction, (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 the basis for approval including any alternative transactions considered. Additional restrictions or procedures may be included in the nonprofit corporation’s bylaws. Related parties are prohibited from participating in deliberations or voting. The attorney general may bring action to enjoin, void, or rescind any related party transaction or proposed transaction that violates these provisions or is otherwise not reasonable or in the nonprofit corporation’s best interests and may seek restitution and removal of the directors or officers.

- **Requires Conflict of Interest Policy:** The Act requires all nonprofit corporations to adopt a conflict of interest policy applying to directors, officers, and key employees. The Act contains several provisions the policy must include. Every director must sign the policy after election, and annually after that, provide a statement disclosing any potential conflicts.

- **Simplifies Corporate “Types”:** The Act eliminates New York’s A, B, C, and D nonprofit corporation types and creates only two categories for nonprofit corporations—“charitable corporations” and “non-charitable corporations.” If a nonprofit corporation is formed for both charitable and non-charitable purposes, it is considered a charitable corporation. Existing nonprofit corporations will be grandfathered into the new classification system, so there is no need to file revised organizational documents. Type B and C corporations will be deemed charitable corporations for all purposes. Type A corporations will be deemed non-charitable corporations. Type D corporations formed for charitable purposes will be deemed charitable corporations, and any other Type D corporations will be deemed non-charitable corporations.

- **Modifies Board Voting Requirements for Non-Substantial Real Estate Transactions:** Non-substantial real estate transactions (transactions not involving all, or substantially all, of the corporation’s assets) no longer require a two-thirds vote of the entire board. Instead, the transaction can be approved by a majority of the nonprofit corporation’s board or a committee. If approved by a committee, the committee must promptly notify the board no later than the next regularly scheduled board meeting.
- **Allows One-Step Approval to Sell, Lease, Exchange, or Dispose of All or Substantially All Assets**: The Act eliminates in most circumstances the need to obtain court approval when a nonprofit corporation seeks to sell, lease, exchange, or dispose of all, or substantially all, assets. The nonprofit corporation may seek one-step approval from the attorney general alone unless:

  1. the nonprofit corporation is insolvent or would become insolvent as a result of the transaction,
  2. the attorney general concludes a court should review the petition and make a determination.

- **Permits One-Step Approval of Mergers and Expands the Types of Nonprofits that Can Merge**: The Act eliminates court approval of merger or consolidation plans in most circumstances. Instead, the attorney general can provide one-step approval. The Act also expands the types of nonprofit corporations that can enter into merger transactions to include educational and religious nonprofit corporations.

- **Allows the Attorney General to Approve Dissolutions**: The attorney general may now approve a nonprofit corporation’s petition for dissolution, but the attorney general may refer the petition to a court if he or she determines court review is appropriate.

- **Defines “Entire Board”**: The Act adds a definition for “entire board” as it relates to voting provisions. “Entire board’ means the total number of directors entitled to vote which the [nonprofit] corporation would have if there were no vacancies.” For voting purposes, if the nonprofit corporation’s bylaws provide for a fixed number of board members, that fixed number is used as the basis. If the bylaws provide a range of directors, the basis is the number of directors within that range elected as of the most recently held election of directors.

- **Clarifies That There Is No Need To Specify Activities in Articles of Incorporation**: A nonprofit corporation only needs to specify whether its purpose is charitable or non-charitable in its articles of incorporation. It need not set forth any activities it intends to carry out to further its purpose.

- **Clarifies Incorporation Requirements for Educational Organizations**: The Act clarifies that only schools, colleges, universities, and organizations providing postsecondary education require the State Education Department’s consent before incorporation. Other entities, such as libraries, museums, and historical societies, may notify the State Education Department of their formation after incorporation.

- **Prohibits Solicitation Before Required Administrative Agency Approval**: The Act prohibits nonprofit corporations required to seek administrative agency approval before incorporating from soliciting funds until approval is obtained.

- **Applies Certain Provisions to Charitable Trusts**: The Act imposes new requirements concerning audits, related party transactions, conflict of interest policies, and whistleblower policies on charitable trusts.

**Whistleblower Policy**

**Requires Whistleblower Policy**: All New York nonprofit corporations with 20 or more employees and more than $1 million in annual revenue in the prior fiscal year must adopt a whistleblower policy to protect from retaliation individuals who report suspected improper conduct. The policy must prohibit intimidation, harassment, discrimination, adverse employment consequences, or other retaliation against whistleblowers. In addition, the Act contains several other provisions that a nonprofit corporation’s policy must include.