
BEST PRACTICES FOR MANAGEMENT OF FRIENDS BOARDS

**Presented for the
Friends of Libraries Section
New York Library Association
March 20, 2018**

**Courtney Darts, Esq.
Legal Director
Pro Bono Partnership**

Please Note

This presentation is provided as a general informational service to clients and friends of Pro Bono Partnership. It should not be construed as, and does not constitute, legal advice on any specific matter, nor does this presentation create an attorney-client relationship. You should seek advice based on your particular circumstances from an independent legal advisor.

The Pro Bono Partnership

- Pro bono legal assistance for nonprofit organizations through the services of staff and volunteer attorneys
- To be eligible, the organization must be:
 - Nonprofit, tax-exempt (or seeking 501(c)(3) status);
 - In our service area (Connecticut, New Jersey, and New York's lower Hudson Valley and Long Island);
 - Serving the poor and disadvantaged; providing health and human services; protecting the environment; or teaching and promoting the arts; and
 - Unable to pay for legal services without significant impairment of program resources.

Our Legal Services

Non-litigation business law matters, in areas such as:

- Corporate structure and governance
- Contracts
- Employment law
- Environmental law
- Intellectual property law
- Mergers, dissolutions, or bankruptcy
- Real estate (including lease reviews)
- Regulatory compliance (e.g., registration, annual reporting, charitable solicitation, lobbying)
- Tax law and tax exempt status

Today's Agenda

1. Nonprofit and tax-exempt overview
2. The role of the board of directors
3. Recent changes to New York laws
4. Tips for a better board
5. Questions and answers

Nonprofit and Tax-Exempt Overview

Incorporation and Tax Exemption

Becoming a tax-exempt nonprofit corporation is a two-step process

- **Step One: Incorporation**
 - Product of state law
 - Achieved by filing a certificate of incorporation or articles of incorporation with the state
- **Step Two: Tax Exemption**
 - Federal designation
 - Corporation applies to the Internal Revenue Service and asks to be recognized as tax-exempt

Pros and Cons of Incorporating

PROS

- Limited liability
- Easier to open a bank account
- May be necessary in order to enter into contractual agreements
- More attractive to funders
- Perpetual existence

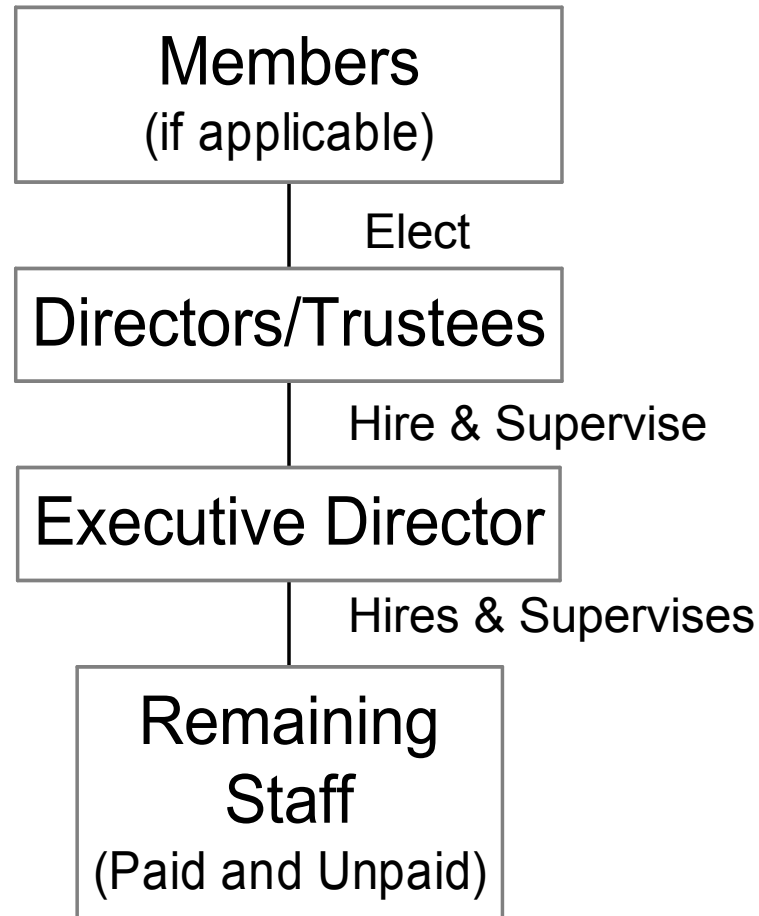
CONS

- State filing requirements
- Observing corporate formalities (board meetings, resolutions, etc.) and maintaining corporate records
- Must recruit and retain people to carry out work
- Perpetual existence

501(c)(3) Tax Exemption

- 501(c)(3) is one type of tax-exempt organization
- Can accept tax-deductible charitable donations
- Doesn't pay income taxes; may be exempt from sales, property and other state and local taxes
- No private benefit or inurement
- Federal and state registration and reporting requirements
- Restrictions on lobbying activities
- Absolute bar on political campaign activities

Organization Chart for Nonprofits



The Role of the Board of Directors

Why Do Nonprofits Have Boards?

To provide oversight

- To ensure that operations, program, staff, finances, internal controls, property, mission, strategic plans are all running smoothly
- To make certain that charitable resources are being used appropriately, in furtherance of the organization's mission
- To help raise financial support and awareness of the organization's work

Fiduciary Duties of Nonprofit Directors

- **Duty of Care:** Performing the director's functions competently; exercising common sense; attending board meetings; reviewing documents; asking questions; making sound and informed decisions
 - NY N-PCL §717(a) - Directors and officers 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.
- **Duty of Loyalty:** Placing the interests of the nonprofit above your own; avoiding conflicts of interest; no self-dealing
- **Duty of Obedience:** Ensuring that the nonprofit is fulfilling its mission and complying with all applicable laws

Fiduciary Duties in Action

General Administration

- **Corporate governance** - hold regular meetings and elections; keep minutes; manage the Board; establish committees; adopt appropriate policies
- **Legal compliance** - timely/proper filings; act in compliance with the organization's mission
- Obtain adequate **insurance**

Fiduciary Duties in Action (cont.)

Finance

- Formulate/approve **operating budget** with Executive Director
- Monitor **income and expenses**
- Review/approve year-end **financial report**
- Ensure adoption of appropriate **internal controls and financial management procedures** (e.g., internal financial reporting requirements, check writing policies, expenditure controls)
- Develop / oversee **fundraising plan and help raise money as needed**
- Ensure the timing filing of **taxes and any related payments**
- **Oversee annual audit**, if organization is required to have one

Fiduciary Duties in Action (cont.)

Personnel

- Hire qualified **Executive Director** and evaluate his/her performance periodically
- Ensure the development and implementation of **personnel policies**
- **Consult with the Executive Director and Director of HR (if any)** and advise as needed re: significant HR matters (e.g., choosing a benefits plan, creating new staff positions, risky terminations, reductions in force in tough times)

Fiduciary Duties in Action (cont.)

- **Program Matters**
 - Determine organizational **mission, philosophy, goals**
 - Ensure regular **evaluation** of program
 - Ensure the organization is operating effectively and efficiently
 - Engage in **strategic planning** as needed

- **Public Relations/Community Relations**
 - **Represent and communicate** the organization's mission, goals and services to the public

Bylaws

- Bylaws are the written rules governing the meetings and actions of the board. Among other things, bylaws should contain provisions for:
- **Directors**
 - Number
 - Qualifications
 - Terms of office
 - Term limits, if any
 - Procedure for election
 - Procedures for resignation/removal
 - Quorum requirement
 - Notices of meetings (regular and special)
 - Participation in meetings
 - Taking action (voting, unanimous written consent)

Bylaws (cont.)

- Among other things, bylaws should contain provisions for (cont.):
 - Officers
 - Committees
 - Executive Director (if organization will have one)
 - Basic financial matters (fiscal year, location of records)
 - Indemnification of directors and officers
 - Procedure for amending

The Nonprofit Revitalization Act: What's Changed for New York's Nonprofits?

Using Tech to Get Board Business Done

- In New York, member and board meeting notices, waivers of notice, and authorizations to act by unanimous written consent may all be sent via fax or e-mail
 - Note the distinction between using e-mail to authorize action unanimously (permitted) and voting over e-mail (not permitted)
- Unless prohibited by a nonprofit's certificate of incorporation or bylaws, directors can participate in meetings via videoconference or conference call. Such participation qualifies as in-person presence at the meeting, allowing director to be counted toward quorum requirement.

Using Committees to Get Board Business Done

- New York law recognizes two types of committees
- **Committees of the board:**
 - Are established by the board and made up only of directors
 - Must have at least three directors serving on them
 - Can act for and bind the board (with a handful of exceptions and within the confines of the resolution or charter establishing the committee)
- **Committees of the corporation:**
 - Can be established by the board or by members, if nonprofit has them
 - Can include non-directors
 - Cannot act for or bind the board

Using Committees (cont.)

- Standing committees vs. ad hoc committees
- Best practices for committees
 - Formally document the vote creating the committee and clearly define the scope of the committee's authority – for standing committees, this may be done through a committee charter or your bylaws
 - Keep minutes of committee meetings – very important for board committees, good idea for any committee
 - Make regular reports to the board
 - Disband when no longer needed

Conflicts of Interest & Related Party Transactions

- Every NY nonprofit corporation must have a written conflict of interest policy that complies with certain statutory requirements
- Policy must:
 - Cover directors, officers, and key persons (individuals who manage or control all or a substantial portion of the nonprofit's activities, programs, and/or budget)
 - Define the circumstances that constitute a conflict of interest
 - Set out procedures for disclosing a conflict of interest to the board or an authorized committee of the board
 - Prohibit the person with the conflict of interest from being present at or participating in the board or committee deliberations and/or vote regarding the matter that gives rise to the conflict

Conflicts of Interest (cont.)

- Policy must (cont.):
 - Prohibit the person with the conflict of interest from trying to improperly influence the deliberations or vote on the matter
 - Require that the existence and resolution of the conflict be documented
 - Set out procedures for disclosing, addressing and documenting related party transactions
 - Require every director, prior to election, and annually thereafter, to complete, sign and submit an annual disclosure identifying:
 - Any entity of which the director is an officer, director, trustee, member, owner, or employee and with which the nonprofit has a relationship
 - Any transaction in which the nonprofit is a participant and in which the director might have a conflict of interest

Related Party Transactions

- What is a related party transaction (“RPT”)?
 - A transaction or agreement involving the nonprofit (or one of its affiliates, if any) in which a related party has a financial interest
- Who is a related party?
 - Directors, officers, and key persons in the nonprofit (and its affiliates, if any) and their relatives
 - Relatives include an individual’s spouse or domestic partner; ancestors; siblings and their spouses; children and their spouses/domestic partners; grandchildren and their spouses/domestic partners; and great-grandchildren and their spouses/domestic partners.
 - Any entity in which one of the individuals described above has at least a 35% ownership interest (or, in the case of a partnership or professional corporation, an ownership interest of more than 5%)

Related Party Transactions (cont.)

- A nonprofit may not enter into a RPT unless the board determines the RPT is fair, reasonable and in the nonprofit's best interest.
- Any director, officer or key person who has an interest in a RPT must disclose the material facts concerning such interest to the board or an authorized committee of the board prior to their deliberations and vote.
- No related party may participate in deliberations or voting regarding the RPT, but the board or committee may request that the person present background information or answer questions prior to the commencement of deliberations or voting.

Related Party Transactions (cont.)

- If the nonprofit is a charitable corporation (as defined in the Not-for-Profit Corporation Law) and the related party has a “substantial” financial interest, the board or authorized committee must also:
 - Consider alternative transactions to the extent available;
 - Approve the RPT by at least a majority vote of the directors or committee members present at the meeting; and
 - Document in writing the basis for the board or committee’s approval, including its consideration of the alternatives.

Related Party Transactions (cont.)

- What isn't a RPT?
 - Transactions that are *de minimis* or of limited monetary value
 - Transactions that wouldn't ordinarily be reviewed by the board and are available to the public on the same or similar terms
 - Transactions that would benefit a related party solely because the related party is a member of the charitable class of people normally served by the nonprofit as part of its mission, provided that the benefit is available to other people in the same class on the same terms

Charitable Registration

- Charitable nonprofits that are formed, operating, and/or soliciting donations in New York State are required to register and file annual financial reports with the Charities Bureau of the NYS Attorney General's office
- There are two relevant laws
 - Article 7A of the NY Executive Law applies to charitable nonprofits that solicit contributions in NY
 - Section 8-1.4 of the Estates, Powers and Trusts Law (“EPTL”) applies to charitable nonprofits that hold and administer property in New York for charitable purposes
- Most NY charitable nonprofits are required to register under both of these laws and are called “Dual Registrants”
- For information about initial and annual filing requirements, visit www.charitiesnys.com

Changes to Financial Reporting Thresholds

- Charitable nonprofits must file a financial report as part of their annual charitable registration. An organization's annual revenue determines what type of financial report it must file.
- The Revitalization Act raised the filing thresholds over the next several years:

Effective Date	Unreviewed Financials Required	Independent CPA Review Required	Independent Audit Required
Prior to July 1, 2014	Less than \$100K	\$100K - \$250K	More than \$250K
July 1, 2014	Less than \$250K	\$250K - \$500K	More than \$500K
July 1, 2017	Less than \$250K	\$250K - \$750K	More than \$750K
July 1, 2021	Less than \$250K	\$250K - \$1 million	More than \$1 million

Requirements for Managing an Audit

- For nonprofits required to submit audited financials to the AG, there are new requirements regarding the board's oversight of the nonprofit's accounting and financial reporting processes and the annual audit.
- All of the board, or a designed audit committee of the board made up solely of independent directors, must:
 - Annually retain or renew the retention of an independent auditor to conduct the audit; and
 - Upon completion of the audit, review the results and any related management letter with the auditor.
- Only independent directors may participate in any board or committee deliberations or voting related to the items listed here.

Managing the Audit (cont.)

- If the nonprofit had annual revenue of more than \$1 million in its prior fiscal year, or reasonably expects to have revenue of more than \$1 million in this fiscal year, the board or audit committee has some additional duties.
- If oversight of the audit is performed by an audit committee, the committee must report their activities to the board.

Who Is an “Independent Director”?

- “Independent director” means a director who within each of the last three years:
 - Has not been an employee or a key person of the nonprofit or any of its affiliates;
 - Has had no relatives who have been key persons of the nonprofit or any of its affiliates;
 - Who has not received, and does not have a relative who has received, more than \$10,000 compensation from the nonprofit or any of its affiliates (other than reimbursement for reasonable expenses); and
 - Has neither been employed by, nor has had a substantial financial interest in, any entity that has either paid or received payments, property, or services from the nonprofit in amounts that exceed certain financial limits.

Definition of “Independent Director” (cont.)

- “Payment” excludes charitable contributions; dues or fees paid to the organization for services that the organization performs as part of its nonprofit purposes; and payments made by the nonprofit at fixed or non-negotiable rates or amounts for services rendered, provided such services are available to the general public on the same terms and are not available from another source.
- “Relative” means a director’s spouse or domestic partner; ancestors; siblings and their spouses/domestic partners; children and their spouses/domestic partners; grandchildren and their spouses/domestic partners; and great-grandchildren and their spouses/domestic partners.
- Again, “key person” means any individual who manages or controls all or a substantial portion of the nonprofit’s activities, programs, and/or budget

Hiring Professional Fundraisers or Fundraising Counsel

- In New York, professional fundraisers (hired on a contract basis to raise funds directly for a charity) and fundraising counsel (hired on a contract basis to advise or assist a charity with its own fundraising program) must be registered with the NYS Attorney General.
- A charity that hires a professional fundraiser or fundraising counsel must make sure the consultant is registered and must have a written contract with the consultant, a copy of which must be filed with the Attorney General.
- The definition of “fund raising counsel” has been changed to exclude grantwriters (an individual engaged solely to draft applications for funding from a governmental agency or an entity exempt from taxation pursuant to Section 501(c)(3) of the Internal Revenue Code)

Tips for a Better Board

Self-Assessment: Looking at the Board You Have Today

- Size?
- Structure?
- Do your board members bring a variety of skill sets?
- Do board members understand their roles and responsibilities? What's your training process?
- Do you orient new board members well? Do you have a board book? A development committee / buddy system?
- Is the board's relationship with the executive director working well? (Either a paid staff person or a volunteer doing the work of an executive director)
- Are your meetings efficient and productive?

How to be a Prudent Board Member

- **Evaluate** information and make decisions based on that information
- **Participate** by reading minutes and all information sent before meetings and attending and speaking at board and committee meetings
- **Delegate** to the Executive Director and those with necessary expertise (accountants, attorneys, etc.) but exercise appropriate oversight
- Be **educated** about the organization; have a comprehensive **board book** for each director

How to be a Prudent Board Member

- Keep adequate **records**
- Comply with **corporate formalities**, all applicable laws
- Have sound **employment practices**
- Make sure your vote is recorded when you **disagree** with board action
- **Resign** from the Board when interest or participation wanes - consider term limits?
- **Be active!**

For More Information

- The New York State Charities Bureau has several useful guides relevant to today's topic. Go to www.charitiesnys.com and click on "Guides & Publications" to find these and many other resources:
 - *Right from the Start: Responsibilities of Directors of Not-for-Profit Corporations*
 - *Internal Controls and Financial Accountability for Nonprofit Boards*
 - *Hiring a Professional Fundraiser: What Charities Need to Know*

Contact Us

Connecticut (except Fairfield County)

280 Trumbull Street
28th Floor
Hartford, CT 06103
Phone: 860-541-4951

Hudson Valley, New York & Fairfield County, Connecticut

237 Mamaroneck Avenue
Suite 300
White Plains, NY 10605
Phone: 914-328-0674

New Jersey

300 Lanidex Plaza
Suite 3203
Parsippany, NJ 07054
Phone: 973-240-6955

Long Island, New York

Touro Public Advocacy Center
225 Eastview Drive
Central Islip, NY 11722
Phone: 631-650-2312



www.facebook.com/PBPartnership



www.twitter.com/PBPartnership



www.linkedin.com/company/pro-bono-partnership