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Honorable Eric Schneiderman
Attorney General of the State of New York
120 Broadway
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Re: Nonprofit Initiative

Dear Attorney General Schneiderman: :

We have read with great interest about your recent announcement in a speech to the Association for a Better New York of a new initiative by your office to revamp New York State laws affecting nonprofits to make them less burdensome. We understand that you are proposing to form a working group of nonprofit, government and labor representatives to develop proposals and recommend reforms.

We heartily congratulate you on this undertaking and would like the opportunity to work with you in this endeavor. The role that nonprofits play in the state has been crucial to New York's economy and its cultural and political importance and this proposal has the promise of lessening the needless burdensome regulation that New York nonprofits currently face.

As a committee of the New York City Bar Association composed of lawyers serving a broad spectrum of nonprofit organizations with extensive experience with nonprofit-related laws, we feel that we can be of great assistance in this process.

We especially would like to note the urgent need to reform the Not-for-Profit Corporation Law (N-PCL). As you are probably aware, the N-PCL imposes needless hurdles related to the formation, operation and dissolution of nonprofits that are not present in the laws of other states. As a result, there is a growing trend among New York nonprofit lawyers to incorporate New York-based nonprofits outside of New York, especially in Delaware (a state where many New York corporate lawyers already incorporate many of their business clients).

As New York lawyers, we would rather form those corporations under New York law. Furthermore, while the Attorney General's office may exercise some degree of authority over nonprofits qualified to conduct activities in New York, its authority over those organizations is far more constrained than it is over organizations incorporated in New York. Accordingly, we feel that it is imperative that the N-PCL be reformed so as to discourage this migration out of state.

For several past legislative sessions a bill has been introduced in the State Legislature to revamp the N-PCL in it entirely. The most recent version of this bill is A-5727/S-4611. The bill had its genesis in a proposal of the New York State Bar Association (State Bar). Our committee studied the bill, and, among other things, held a public forum on November 2, 2009 entitled *Ideas for Change: A Conversation About Reforming New York Nonprofit Law and Regulations*. That session consisted of a two and half hour panel discussion with representatives from the legislature, practitioners, academics and regulators on the bill and administrative issues relating to nonprofits' activities in New York. We conducted a section-by-section analysis of the N-PCL and the State Bar bill and we are currently working with the State Bar with the goal of preparing a draft bill that both bar associations can jointly sponsor. We look forward to educating your office on the status of the proposal.

The N-PCL, based in large part on the existing Business Corporation Law (BCL), was adopted in 1970, over 40 years ago. While certain provisions have changed over the years, it has not been updated as much as the BCL. It is ripe for a full scale review and revision. As we learned in our review of the existing law, many of its provisions are confusing or burdensome (or both). While lawyers who regularly practice in this field are familiar with the sometimes counterintuitive and arcane aspects of the N-PCL, they are often a surprise to lawyers less experienced in this field (including many business lawyers familiar with the BCL); this can lead to errors or unintentional violations of the N-PCL. As you probably know, due to their limited finances many nonprofits rely on the *pro bono* services of these lawyers instead of seeking the counsel of more seasoned nonprofit specialists. It would be helpful for all New York lawyers if the N-PCL was revised for more clarity and to eliminate unnecessary burdens.

These unnecessary burdens arise under the current law in all aspects of a nonprofit's life – its formation, operation and eventual dissolution. These include:

- Delays in the formation stage (and the corresponding process of qualifying out-of-state nonprofit corporations to conduct activities in New York) created by requirements such as the need to determine a nonprofit's "type" (with confusion over the correct "type" often leading to rejection of certificates of incorporation and certificates of authority for foreign corporations) and to obtain pre-formation consents from one or more state agencies, which can be a lengthy process. Until these various requirements are met, the organization cannot commence the groundwork that must be done before it can start operations, including obtaining Internal Revenue Service recognition of its tax exempt status and registering with state agencies to solicit funds.

- Burdens in the operational phase including high vote requirements for certain board actions, cumbersome provisions for determining the number of directors and forming

committees, uncertainty as to whether boards can act by electronic consent and required state agency consents for certain changes.

- Although recently improved, the cumbersome dissolution process.

While many of the unnecessary burdens faced by nonprofit corporations formed in New York arise from the provisions of the N-PCL, some of them are found at the administrative level, where nonprofit corporations frequently experience delays and other costly obstacles to obtaining necessary governmental consents. This combination of statutory and administrative challenges make it more difficult for nonprofit corporations to perform the services for which they were (or hope to be) established and discourage them from forming, and in some cases from operating, in New York.

While we support the virtues of a re-write of the N-PCL, we would alternatively support efforts to modify specific provisions of the law pending any total revision. These include:

1. Replacement of pre-formation consent requirements under Section 404 with post-formation notification and approvals to conduct regulated activity.

2. Replacement of "types" under Section 201 with a simpler distinction between "public benefit" and "mutual benefit" type corporations.

3. Replacement of the requirement of approval by a majority (or, in certain instances, two-thirds) of the "entire board"[1] for any real estate transactions (Section 509 – two-thirds for boards of 20 members or less), asset sales (Section 510 – two-thirds for boards of 20 members or less), change in the number of directors (including change by way of amendment of the by-laws) (Section 703), formation and composition of board committees (Section 712) and setting of officer salaries (Section 715) with the approval by a majority (or higher) vote of the board members present at a meeting at which a quorum exists.

4. Revision of the provisions under Sections 605, 614, 708 and 711regarding member and director action to allow electronic communications for notice of meetings and member and director action.

5. Revision of the provisions under Section 702 regarding board size to allow the by-laws of all corporations to provide a range rather than a fixed number (currently, only nonprofits with members who have approved such by-law provision are allowed to use a range but, in fact, the by-laws of many, if not most, nonprofits allow the board to fix the number within a range).

6. Revision of provisions under Section 712 regarding committees to allow the by-laws to set more practical procedures for the appointment of the members (subject to full board

[1] The "entire board" is the number of directors fixed by the by-laws, including vacancies. Since the quorum for board meetings can be set as low as one-third of the entire board, meetings are often validly held without a majority of the entire board being in attendance, meaning these actions cannot take place at that meeting even if everyone in attendance concurs with the proposed action.

oversight) and eliminate the requirement that all committees (excepting the executive committee) consist of at least three members.

7. Simplification of the procedures for (a) asset sales under Section 510, (b) changes of purposes under Section 806, (c) mergers and consolidations under Article 9 and (d) dissolutions under Article 10, and, in some instances, other changes to expedite or simplify such procedures. One idea would be to permit an alternative to the current process of seeking court approval for such transactions on notice to the Charities Bureau, which would allow nonprofits to seek approval from the Attorney General (instead of the courts), using application forms and paperwork established by the Charities Bureau, with the Attorney General's decision being subject to administrative review. This approach, it is hoped, would be simpler, especially for smaller nonprofits without access to nonprofit specialists. The nonprofit would retain the right, as currently set forth in the law, to seek court approval (on notice to the Attorney General), which would avoid the need to take an appeal from an adverse administrative determination under this alternative approach.

8. Elimination of the need under Section 404to give names and addresses of initial directors in the certificate of incorporation, as well as reduction of other rights to obtain such names and addresses under Section 718.

9. Streamlining of corporate filing procedures, including (a) requiring the Department of State to review filings solely on the basis of whether they satisfy the requirements of the N-PCL, such as the requirement that the certificate of incorporation sets forth the purposes for which the corporation is formed, and not, as is currently the case, requiring that the certificate of incorporation describe the activities of the corporation or questioning the appropriateness of a name of the corporation otherwise in compliance with the N-PCL requirements, (b) authorizing (for a fee) the Department of State to "preclear" filings prior to formal submission and (c) allowing the Department of State to make hand corrections to filings to correct minor errors with the consent of the filer.

10. Reformulation of the provisions of the N-PCL to better clarify the role and fiduciary duties of directors and officers. While these provisions do not, we feel, impact on the initial decision of nonprofits to form in New York or elsewhere, the current environment calls for a greater emphasis on good governance practices. We believe that inclusion of all such provisions in one location would also help convince legislators as to why reform of the N-PCL would be wise.

We would appreciate an opportunity to be a part of the process that you envision to modernize New York's nonprofit practices and look forward to the opportunity to work with your office on this worthwhile project.

Sincerely,

David Lowden

cc: Harlan Levy, Esq. First Deputy Attorney General
Jason Lilien, Esq., Bureau Chief of the New York State Attorney General's Charities Bureau
Robert Pigott, Esq., Chair of the Subcommittee on N-PCL Reform

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* did not take part in the consideration or approval of this report