NONPROFIT LEGAL CURRENTS

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NONPROFIT GOVERNANCE: IT'S NOT ROCKET SCIENCE
PART 2 – ASSURE COMPLIANCE & AVOID GOVERNANCE TRAPS

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Let's start with this basic premise: people join nonprofit boards because of their passion for the mission. No one joins a nonprofit board to spend time and energy on nonprofit governance. Nobody wants to become a governance geek! Because of this basic mindset, nonprofit directors and officers are often surprised when they discover that the only way to protect the organization, its mission and its assets, the only way to fulfill their fiduciary duties under the law, and the only way to protect themselves from personal liability for breach of these fiduciary duties is careful and continuous attention to governance. Bottom line: **as a director or officer of a nonprofit you have no choice but to become a governance geek, both for the good of the organization and for your own good**.

To make matters worse, New York nonprofit law is chock full of requirements, some of them quite demanding, and some of them somewhat counterintuitive. There are no shortcuts to evade these legal requirements, and the only way to comply is to keep governance in the spotlight and to implement governance requirements and procedures with careful attention to detail. Here are some governance requirements that every nonprofit should be sure to follow.

Have An Annual Meeting. New York law requires every nonprofit to have an annual meeting. There are two requirements at the annual meeting: the election of directors and the delivery of the annual financial report. The election of directors is fundamental to nonprofit governance. As one might imagine, deficient or improper election of directors calls into question the board's composition and authority, and can, in turn, undermine the validity of board decisions and actions, with far-reaching negative consequences. The law mandates that certain information be included in the annual financial report. This is set forth in Sections 513 and 519 of the Not-for-Profit Corporation Law. But the mandated financial information is not the end of it. It is often the timeliness requirement for the annual financial report that trips up nonprofits, and this is most certainly a trap for the unwary. The law requires that the financial information provided covers a twelve-month fiscal period *ending not more than six months prior to the date of the annual meeting*. So, if your fiscal year ends December 31, your annual report would need to be delivered before the end of June. Delivery of a complete, compliant and timely annual financial

report is an essential component of New York nonprofit law's model of financial reporting, transparency and governance.

New York Law Does Not Permit Email Voting. Let me repeat that, because it is such a source of confusion for directors and officers. New York law does NOT permit email voting! The board can act in two ways under New York law. One option is action at a meeting (including in-person, phone conference or video conference – depending on what your bylaws provide). The other option is unanimous consent in lieu of a meeting (this can be unanimous written consent or unanimous email consent, again depending on what your bylaws provide). But the key is that **if the board is going to consent without a meeting, the consent must be unanimous**. 19 out of 20 directors consenting is not sufficient. I had this very fact pattern occur with the board of a national organization with 50 directors. 49 directors consented by email. One director did not consent because he was in a coma. The 49 consents were useless (because there was not unanimous consent, and because email voting is not permitted), so the board needed to call a special meeting to take the intended action. These distinctions are anything but insignificant technicalities, because if the consent is not valid, the result is that the action is not authorized, and unauthorized actions can lead to all sorts of entanglements and potential liability, including personal liability for directors.

The law has mandatory requirements in the areas of meeting notice, quorum and voting thresholds. Very often, bylaws are written in a way that violates these mandatory requirements. So, you could be scrupulously following your bylaws, but nonetheless be violating the law. Here too, violations are not harmless technical infractions. Deficiencies in the areas of meeting notice, quorum and voting thresholds can lead to challenges to both the validity of meetings and the authority for the actions that were taken at those meetings, with potential personal liability of directors as an unfortunate consequence.

Committees are another area full of traps for the unwary. There are two types of committees permitted under the law: board committees and committees of the corporation. Each board committee must have at least 3 directors. Non-directors cannot be voting members of board committees. Board committees can possess certain aspects of board authority, which are formally delegated to the committee by the full board. But there are certain aspects of board authority and functioning that the law does not allow to be delegated to a committee. And there are specific statutory provisions that apply to, and govern, certain board committees (principally, the Executive Committee and the Audit Committee). Committees of the corporation, on the other hand, cannot be delegated any board authority, and cannot bind the corporation. Committees of the corporation can play a strictly advisory role. As a result of this more limited role, non-board members (as well as board members) may serve on committees of the corporation, and there is no minimum number of members for a committee of the corporation. In the area of committees, too, missteps can have serious consequences, and can lead to the undermining of decisions and actions, and potential personal liability of directors.

Nothing listed above is rocket science. So then, why do we see governance deficiencies in these areas cited over and over in regulatory actions against nonprofit directors and officers, and also in litigations by private litigants against nonprofit directors and officers? **Careful attention to detail can eliminate these exposures before they happen.** "An ounce of prevention is worth a pound of cure!" Nonprofits owe nothing less to the organization and its mission, to those that they serve, and to the directors and officers whose service is so vital to the advancement of the organization's good and essential work.

About the Author

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