

JAN 17 2007

A BILL FOR AN ACT

RELATING TO NONPROFIT CORPORATIONS.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF HAWAII:

1 SECTION 1. Nonprofit corporations are an indispensable
2 part of our society, offering relief from disasters, nurturing
3 our spiritual and creative aspirations, caring for vulnerable
4 people, protecting our natural and cultural heritage, and
5 finding solutions to medical and scientific challenges. These
6 greatly needed missions can only be accomplished by restoring
7 and preserving the trust and confidence of our public donors.

8 In response to the egregious corporate and accounting
9 scandals of Enron, WorldCom, Tyco, and others, The federal
10 American Competitiveness and Corporate Accountability Act of
11 2002, commonly known as the Sarbanes-Oxley Act, was signed into
12 law. Its purpose is to instill investor confidence in the
13 market by raising the standards of corporate transparency and
14 accounting. While this law applies to nearly all publicly
15 traded corporations, only two of its provisions apply to
16 nonprofit corporations.



1 The tragedy of September 11, 2001, brought an outpouring of
2 support for its victims by public charitable donors. However,
3 these donations often did not reach their intended recipients
4 because of delivery problems and management indiscretions. Many
5 new cases of mismanagement and abuse of charitable assets by
6 managers, officers, and directors of nonprofit corporations are
7 surfacing and increasing at an alarming rate.

8 According to the Better Business Bureau's Wise Giving
9 program, eighty per cent of the money received by charities in
10 the United States comes from individual public donors.
11 Recognizing the impact of public confidence on sustaining these
12 necessary nonprofit corporations, several state legislatures
13 have passed or are considering legislation with provisions
14 similar to those in the Sarbanes-Oxley Act that will restore
15 financial integrity and hold nonprofit corporations to clear
16 standards of accountability.

17 The purpose of this Act is to restore the trust and
18 confidence of the public in nonprofit corporations and
19 charitable organizations by establishing good practices
20 standards, providing clearer standards regarding financial
21 oversight, and encouraging nonprofit corporations to strive for
22 greater disclosure and transparency.



1 SECTION 2. Chapter 414D, Hawaii Revised Statutes, is
2 amended by adding a new section to part VIII to be appropriately
3 designated and to read as follows:

4 "§414D- Audit committees. (a) Every nonprofit
5 corporation required to file an annual report and audit with the
6 department director pursuant to this chapter that receives or
7 accrues in any fiscal year gross revenue of one million dollars
8 or more, exclusive of revenue from grants from, and contracts
9 for services with, governmental entities for which the
10 governmental entity requires an accounting of the funds received
11 shall form an audit committee appointed by the board of
12 directors.

13 (b) The audit committee may include persons who are not
14 members of the board of directors, and shall not include any
15 members of the staff, including the president or chief executive
16 officer and the treasurer or chief financial officer.

17 (c) If the corporation has a finance committee, it shall
18 be separate from the audit committee. Members of the finance
19 committee may serve on the audit committee, except that the
20 chairperson of the audit committee shall not be a member of the
21 finance committee and members of the finance committee shall



1 constitute less than one half of the membership of the audit
2 committee.

3 (d) At least one member of the audit committee shall have
4 adequate experience in financial matters to reasonably assess
5 and analyze the financial statements of the corporation and the
6 competency of the auditing firm.

7 (e) Members of the audit committee shall not receive any
8 compensation for their service on the audit committee and shall
9 not have any financial interest in or any other conflict of
10 interest with any entity doing business with the corporation.

11 (f) The audit committee shall ensure that the auditing
12 firm has the requisite skills and experience to carry out the
13 auditing function for the corporation and that its performance
14 is carefully reviewed.

15 (g) The audit committee shall review the annual audit and
16 have full board approval before accepting or rejecting
17 modifications to or finalizing the audited financial statement
18 to be filed pursuant to section 414D-308(f).

19 (h) The audited financial statement shall be available for
20 inspection by the attorney general and by members of the public
21 no later than nine months after the close of the fiscal year to
22 which the statement relates.



1 (i) The audit committee shall ensure that the lead and
2 reviewing partners of the auditing firm shall not participate in
3 the preparation of the audit for more than five consecutive
4 years.

5 (j) The audit committee shall ensure that, while the firm
6 is contracted to perform auditing services, the auditing firm
7 does not provide non-auditing services to the corporation,
8 except for tax preparation that shall be approved in advance.

9 (k) The audit committee shall establish procedures to
10 accept complaints relating to financial matters, including
11 complaints from anonymous sources within the corporation."

12 SECTION 3. Chapter 414D, Hawaii Revised Statutes, is
13 amended by adding a new section to part XV to be appropriately
14 designated and to read as follows:

15 "§414D- Whistleblower protections. (a) Any nonprofit
16 corporation, except those with no paid employees, required to
17 file an annual report pursuant to section 414D-308 shall comply
18 with the requirements of this section.

19 (b) A nonprofit corporation shall not retaliate against
20 any employee of the corporation who has filed a complaint with
21 the governing board, directors or trustees, audit committee, the



1 attorney general, or any other government agency pertaining to
2 the following:

3 (1) Dissipation of the corporation's assets;

4 (2) The mishandling or misuse of restricted funds;

5 (3) Related party transactions;

6 (4) Compliance with state or federal reporting
7 requirements;

8 (5) Overriding or circumventing of the corporation's
9 internal controls;

10 (6) Private inurement; and

11 (7) Fraud.

12 (c) All records pertaining to any complaint that falls
13 under this section and its resolution shall be retained by the
14 corporation for four years from the date the complaint was filed
15 and shall also be made available to the attorney general upon
16 request of the attorney general. These documents shall not
17 constitute public records subject to section 414D- (h) or
18 chapter 92F.

19 (d) If a nonprofit corporation or the responsible officer
20 or agent wilfully retaliates against an employee for a complaint
21 that falls under this section, the attorney general, in addition
22 to any other statutory or common law remedies, may seek:



- 1 (1) Compensation for the employee;
- 2 (2) Back pay for the employee; and
- 3 (3) Any appropriate order prohibiting the reoccurrence of
- 4 the unlawful conduct."

5 SECTION 4. Section 414D-155, Hawaii Revised Statutes, is
6 amended to read as follows:

7 "§414D-155 Standards of conduct for officers. (a) An
8 officer with discretionary authority shall discharge the
9 officer's duties under that authority:

- 10 (1) In good faith;
- 11 (2) With the care an ordinarily prudent person in a like
12 position would exercise under similar circumstances;
- 13 and
- 14 (3) In a manner the officer reasonably believes to be in
15 the best interests of the corporation and its members,
16 if any.

17 (b) In discharging an officer's duties, an officer is
18 entitled to rely on information, opinions, reports, or
19 statements, including financial statements and other financial
20 data, if prepared or presented by:



1 (1) One or more officers or employees of the corporation
2 who the officer reasonably believes to be reliable and
3 competent in the matters presented; or

4 (2) Legal counsel, public accountants, or other persons as
5 to matters the officer reasonably believes are within
6 the person's professional or expert competence.

7 (c) An officer is not acting in good faith if the officer
8 has knowledge concerning the matter in question that makes
9 reliance otherwise permitted by subsection (b) unwarranted.

10 (d) An officer shall fully understand all financial
11 statements and reports. By signing any financial statement or
12 report the officer is ensuring its accuracy and completeness.

13 ~~[(d)]~~ (e) An officer is not liable to the corporation, any
14 member, or other person for any action taken or not taken as an
15 officer, if the officer acted in compliance with this section.

16 ~~[(e)]~~ (f) Any person who serves as an officer to the
17 corporation without remuneration or expectation of remuneration
18 shall not be liable for damage, injury, or loss caused by or
19 resulting from the person's performance of or failure to perform
20 duties of the position to which the person was appointed, unless
21 the person was grossly negligent in the performance of or
22 failure to perform the duties. For purposes of this section,



1 remuneration does not include payment of reasonable expenses and
2 indemnification or insurance for actions as an officer as
3 allowed by sections 414D-159 to 414D-167."

4 SECTION 5. Section 414D-301, Hawaii Revised Statutes, is
5 amended by amending subsection (b) to read as follows:

6 "(b) A corporation shall maintain [~~appropriate~~] complete
7 and accurate accounting records[-] using generally accepted
8 accounting principles."

9 SECTION 6. Section 414D-308, Hawaii Revised Statutes, is
10 amended to read as follows:

11 "**§414D-308 Annual report.** (a) Each domestic corporation,
12 and each foreign corporation authorized to transact business in
13 the State, shall deliver to the department director [~~an~~]
14 complete and accurate annual [~~report~~] reports on a form
15 prescribed and furnished by the department director that sets
16 forth:

17 (1) The name of the corporation and the state or country
18 under whose law it is incorporated;

19 (2) The mailing address of its principal office, the
20 address of its registered office in this State, and
21 the name of its registered agent at its registered
22 office in the State;



1 (3) The names and addresses of its directors and officers;
2 and

3 (4) A brief description of the nature of its activities.

4 (b) The annual report shall be filed within the time
5 periods prescribed in subsections (c) and (d).

6 (c) Notwithstanding any of the provisions of this chapter
7 to the contrary, annual reports reflecting the period from
8 January 1, 2002, through December 31, 2002, that would otherwise
9 be required, may be voluntarily filed with the department
10 director if the annual report complies with the requirements of
11 this section.

12 (d) Effective January 1, 2003, for a domestic or foreign
13 corporation whose date of incorporation or registration in this
14 State falls between:

15 (1) January 1 and March 31, an annual report shall be
16 filed on or before March 31 of each year and shall
17 reflect the state of the corporation's affairs as of
18 January 1 of the year when filed;

19 (2) April 1 and June 30, an annual report shall be filed
20 on or before June 30 of each year and shall reflect
21 the state of the corporation's affairs as of April 1
22 of the year when filed;



1 (3) July 1 and September 30, an annual report shall be
2 filed on or before September 30 of each year and shall
3 reflect the state of the corporation's affairs as of
4 July 1 of the year when filed; and

5 (4) October 1 and December 31, an annual report shall be
6 filed on or before December 31 of each year and shall
7 reflect the state of the corporation's affairs as of
8 October 1 of the year when filed;

9 provided that if a domestic or foreign corporation is
10 incorporated or registered in the same year in which the annual
11 report is due, the domestic or foreign corporation shall not be
12 required to file an annual report for that year. Thereafter,
13 the domestic or foreign corporation shall comply with the
14 requirements of this section.

15 (e) If, in good faith, an annual report does not contain
16 the information required by this section, the department
17 director shall promptly notify the reporting domestic or foreign
18 corporation in writing and return the report to it for
19 correction. If the report is corrected to contain the
20 information required by this section and delivered to the
21 department director within thirty days after the effective date
22 of notice, it shall be deemed to have been timely filed.



1 (f) Every nonprofit corporation required to file an annual
 2 report with the department director pursuant to this chapter
 3 that receives or accrues in any fiscal year gross revenue of one
 4 million dollars or more, exclusive of revenue from grants from,
 5 and contracts for services with, governmental entities for which
 6 the governmental entity requires an accounting of the funds
 7 received shall file with each annual report a complete audited
 8 financial report that is audited by an independent certified
 9 public accountant in conformity with generally accepted auditing
 10 standards.

11 (g) Wilful or persistent failure of a corporation to file
 12 a complete and accurate report or audit report as required by
 13 law shall constitute a breach of the directors' and officers'
 14 duty to the corporation and shall subject the corporation or its
 15 directors, at the suit of the attorney general, to an action or
 16 special proceeding for injunctive relief."

17 SECTION 7. Statutory material to be repealed is bracketed
 18 and stricken. New statutory material is underscored.

19 SECTION 8. This Act shall take effect upon its approval.

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INTRODUCED BY:

[Handwritten signatures and initials]
 Rosalyn H Baker
 S. T. ...
 Jim ...
 Anil ...
 Ron ...
 Carol ...



Report Title:

Nonprofit Corporations; Audit Committees; Fraud Protections

Description:

Requires nonprofit corporations with annual gross revenues of \$1 million or greater to implement federal Sarbanes-Oxley Act-type provisions by forming an audit committee with independent members and using generally accepted accounting principles. Establishes whistleblower protections.

