

SB893

Measure Title: RELATING TO NONPROFIT CORPORATIONS.

Report Title: Nonprofit Corporations

Description: Amend chapter 414D, Hawaii Revised Statutes, to impose a duty of loyalty on directors and officers of nonprofit corporations, to prohibit directors from voting on matters where they have a conflict of interest, to recodify provisions that would allow nonprofit corporations to convert into and out of domestic nonprofit corporations, and to increase the length of time that the Attorney General has to review proposed dissolutions of public benefit corporations.

Companion: [HB1027](#)

Package: Governor

Current Referral: CPH, JDL

Introducer(s): KOUCHI (Introduced by request of another party)



**TESTIMONY OF
THE DEPARTMENT OF THE ATTORNEY GENERAL
TWENTY-NINTH LEGISLATURE, 2017**

ON THE FOLLOWING MEASURE:

S.B. NO. 893, RELATING TO NONPROFIT CORPORATIONS.

BEFORE THE:

SENATE COMMITTEE ON COMMERCE, CONSUMER PROTECTION, AND HEALTH

DATE: Tuesday, February 7, 2017 **TIME:** 9:00 a.m.

LOCATION: State Capitol, Room 229

TESTIFIER(S): Douglas S. Chin, Attorney General, or
Hugh R. Jones, Deputy Attorney General

Chair Baker and Members of the Committee:

The Department of the Attorney General supports this Administration bill. The purposes of this bill are to partially restore a previously existing section of the State's nonprofit corporation law, which allows domestic nonprofit corporations to "convert." This bill, if enacted, would allow, under certain circumstances, a domestic nonprofit corporation to convert to a foreign nonprofit corporation. The bill also makes technical amendments to provisions regarding dissolution of certain nonprofit corporations and makes clarifying amendments to provisions concerning a director's statutory duties and the procedure by which "conflict transactions" are handled by directors of nonprofit corporations.

A. Conversion Provisions.

The Attorney General proposed legislation in 2012 (H.B. No. 2458) repealing section 414D-207, Hawaii Revised Statutes (HRS), which allowed a domestic nonprofit corporation to convert to a foreign corporation "or any other business entity." The reason for repealing section 414D-207, HRS, was that, as written, the statute at the time allowed the diversion of charitable assets for use in for-profit activities in situations where a domestic nonprofit corporation could solicit and receive charitable donations intended for charitable purposes and then convert the entity to a foreign for-profit entity and use those charitable donations for the benefit of shareholders of a corporation or members of a limited liability company. H.B. No. 2458 was signed into law on April 20, 2012 as Act 37. In hindsight Act 37 went too far. When the Legislature repealed

section 414D-207, HRS, it also prevented domestic nonprofit corporations from converting to foreign nonprofit corporations.

This bill, if passed, will restore a portion of repealed section 414D-207, HRS, by: (a) authorizing domestic nonprofit corporations to convert to foreign nonprofit corporations; (b) creating a procedure regarding conversion; and (c) enacting provisions regarding the legal effect of a conversion.

Procedure

A domestic nonprofit corporation may convert into a foreign nonprofit corporation if: (a) the board of directors approves a plan of conversion in the manner prescribed by law; (b) the conversion is permitted and complies with the law of the state or country in which the converted entity will be incorporated; and (c) the corporation has members and the members of the domestic nonprofit corporation become members of the converted entity.

The proposed new section also allows for the abandonment of conversion before the time the conversion becomes effective. In addition, the bill provides for the filing with the State of articles of conversion.

Effect of Conversion

This bill contains provisions regarding the effect of conversion, in that after conversion the converted entity continues to exist and owns all property of the converting entity and its liabilities and obligations. The converted entity remains subject to civil proceedings in Hawaii and must irrevocably appoint an agent for service of process in Hawaii.

B. Director's Statutory Duties.

The duties of directors of nonprofit corporations are set forth in section 414D-149, HRS. At common law, directors of nonprofit corporations (as well as trustees of charitable trusts) have a duty of loyalty. Section 414D-149, HRS, does not presently expressly recognize a duty of loyalty, although a director's duty to act "in good faith" also implies such a duty. Likewise section 414D-150, HRS, implies a duty of loyalty.

This bill amends sections 414D-149 and 414D-150, HRS, to expressly recognize that a director has a duty of loyalty.

C. Conflict Transactions.

At present, a director of a nonprofit corporation may vote on any transaction in which the director has a direct, or indirect conflict of interest as long as the conflict is disclosed and a majority of the board members who are free of any conflict approve the transaction pursuant to section 414D-150. This provision would require the recusal from voting of any director that has a direct, or indirect conflict of interest.

D. Technical Amendments.

The bill amends section 414-233, HRS, to clarify that no assets of a dissolving corporation shall be transferred or conveyed until after twenty business days, rather than just twenty days, after the corporation gives the Attorney General the required notice of intent to dissolve.

The Attorney General respectfully requests that you pass this bill.



ALOHA SOCIETY OF ASSOCIATION EXECUTIVES
ASAE-Hawaii
P.O. Box 282
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February 7, 2017

Testimony To: Senate Committee on Commerce, Consumer Protection, and Health
Senator Rosalyn H. Baker, Chair

Presented By: Tim Lyons, Legislative Chairman
Aloha Society of Association Executives

Subject: S.B. 893 – RELATING TO NONPROFIT CORPORATIONS.

Chair Baker and Members of the Committee:

I am Tim Lyons, Legislative Chairman for the Aloha Society of Association Executives, a trade association composed of individuals who manage professional 501(c) (6) business organizations. We have confined our comments to only two (2) sections of this bill. We do not think that when this bill was drafted, the drafters considered that these amendments would also apply to our type of non-profit organizations. We are not concerned with Section 1, 2 or 3 regarding conversions however Section 4 and 5 prompt us to have some comments.

Section 4 amends Section 414D-149 HRS, a section which we have long questioned inasmuch as it requires a director to discharge his duties not only as a Director but also as a member of a committee in a prescribed manner. We are not quite sure why a Director has a super imposed duty over that of other committee members merely because they happen to serve on a committee. We have no argument with the new language added in subsection 2 requiring a duty of loyalty to the corporation

however, we find that generally a duty of loyalty is considered to be part of a fiduciary responsibility and therefore would already be covered.

Secondly, we also note that in Section 5 of the bill, regarding a prohibition on voting in any transaction in which there is a conflict of interest, we believe that there may be situations where either the vote of the Director is needed or the conflict of interest is so minor as to not require a prohibition but merely a disclosure. Therefore we think there should be language that suggests that the Director could either declare their conflict for Board resolution or require that the Director take it upon himself to declare the conflict or recuse himself from voting. The automatic prohibition may not be appropriate in every single situation.

With those comments we appreciate the opportunity to testify.

Thank you.

TO: Members of the Committee on Commerce, Consumer Protection & Health

FROM: Natalie Iwasa, CPA, CFE
Honolulu, HI 96825
808-395-3233

HEARING: 9 a.m. Tuesday, February 7, 2017

SUBJECT: SB 893 – Charitable Organizations **SUPPORT Deactivation**

Aloha Chair and Committee Members,

Thank you for allowing me the opportunity to provide testimony on SB 893, which makes several changes to the law regarding charitable organizations.

Changes to Section 467B-2.1 would allow organizations to apply for deactivation. I support this and ask you to pass at least this portion of the bill.

Some organizations may change their operations and no longer rely on public contributions. It makes sense to then allow them to deactivate.