

NEW WASHINGTON STATE NONPROFIT CORPORATION ACT REVITALIZES LAW GOVERNING NONPROFIT CORPORATIONS

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Effective for most purposes on 1 January 2022, a new state law overhauls and reforms the governance landscape for nonprofit corporations in the state of Washington. Replacing existing Chapter 24.03 RCW (the “Current Act”) in its entirety, the new Washington Nonprofit Corporation Act (the “New Act”) modernizes state law relating to the organization, management, and governance of nonprofit corporations. Loosely based on the American Bar Association’s Model Nonprofit Corporation Act (the “Model Act”), the New Act incorporates certain provisions from the Current Act, includes new provisions either not addressed or incompletely addressed in the Model Act, and deviates from the Model Act in a number of instances.

CHANGES TO EXISTING LAW

Among the many changes included in the New Act are the following:

Default Permission to Deliver Electronic Communications

By default, the New Act allows for the delivery of electronic communications and notices to directors, members, and officers of nonprofit corporations. Though the Current Act allows for individuals to opt in to receive such communications, authorization under the Current Act requires written consent that, in practice, is not always properly documented. If desired, organizations may opt out in their articles or bylaws from using electronic communications.

The New Act also expressly expands the existing default authorization of telephonic meetings to include videoconference meetings. Relatedly, unless otherwise prohibited by an organization’s articles or bylaws, the New Act also expressly allows for consent to board action to be delivered by email.

Additional Requirements as to the Use of Charitable Assets

The New Act clarifies how nonprofit corporations must protect and use charitable assets. Though the Current Act includes certain mechanisms designed to protect charitable assets, the New Act expands upon these requirements and addresses certain situations that the Current Act either omitted or incompletely addressed. In addition, the New Act sets forth supplementary requirements addressing how charitable assets must be treated upon a charitable corporation’s dissolution or in the event of other major transactions. For example, the New Act permits distributions to be made to a charitable corporation’s members that are charitable corporations or government agencies—such distributions are not clearly permitted under the Current Act.

Moreover, the New Act imposes additional rules that differentiate between nonprofit corporations and charitable trusts and confirms the limited circumstances in which the charitable trust chapter (Chapter 11.110 RCW) applies to nonprofit corporations. Via the implementation of more detailed and fulsome standards and requirements, the New Act also provides clarity on restricted and unrestricted charitable assets, and it expands on the ability of nonprofit corporations to modify charitable use requirements established by donors of charitable assets. The New Act also clarifies and refines the role of the Attorney General of the state of Washington (the “Attorney General”) in overseeing the management of charitable assets held by nonprofit corporations.

Of note, the New Act requires that charitable corporations pay a new, annual charitable asset protection fee (the “Fee”) to support the Attorney General's enforcement of the New Act. The Fee will be payable each year upon the filing of a charitable corporation's annual report.

Increased Flexibility Regarding the Use of Charitable Assets

The New Act substantially increases flexibility for nonprofit corporations in their use of charitable assets. The New Act both allows organizations to modify their charitable purposes (unless otherwise prohibited in an organization's articles and bylaws) and provides additional options for organizations seeking to modify or release gift restrictions without first obtaining court approval. Particularly beneficial for nonprofit organizations with onerous gift restrictions, the ability to enter into binding agreements to modify or release gift restrictions will help nonprofit organizations lawfully use charitable assets consistent with an evolution of such organizations' charitable work.

Clarification and Elaboration of Standards for Members of Nonprofit Corporations

The New Act clarifies the rights, obligations, and authority of members of nonprofit corporations and also delimits the circumstances in which members are entitled to statutory rights. Both at present and under the New Act, nonprofit corporations may be structured as membership corporations. However, the Current Act does not clearly delineate which members of nonprofit corporations are deemed “members” for statutory purposes. The New Act clarifies that statutory membership recognition requires that (a) members must be provided for in a nonprofit corporation's articles, and (b) members must have the right to vote for the election of directors or delegates or to vote on at least one type of fundamental transaction. “Fundamental transactions” include amendments to articles or bylaws, mergers, the sale of all or substantially all assets, domestication, conversion, or dissolution of a nonprofit corporation.

The New Act also includes additional guidelines relating to admission of members, the structure of membership rights (including authorization to create multiple classes of memberships with different membership rights), meetings of and actions by members, and other general, member-related governance matters. Of note, the New Act provides additional flexibility in structuring multiple classes of members. Following the implementation of the New Act, nonprofit corporations can more easily be structured to have members with distinct privileges, including with regard to voting rights and other governance matters. As is the case under the Current Act, the New Act does not mandate that nonprofit organizations have members.

Expansion of Requirements Relating to and Obligations of Directors and Officers

The New Act both improves and modifies existing standards relating to the roles, functions, and requirements of directors and officers of nonprofit corporations. In addition to codifying the fiduciary duties of each (consistent with existing corporate law concepts), the New Act provides additional guidance as to board and board committee structure and operation, appointment and removal of directors, impermissible director and officer conduct, board

meetings, and board actions by written consent, among other subjects. In short, the New Act clarifies existing ambiguities in the Current Act by clearly setting forth standards and obligations of conduct of directors and officers.

Several notable revisions directly relate to structural governance requirements. While the Current Act mandates that nonprofit corporations, at minimum, appoint a president and at least one vice president, secretary, and treasurer, the New Act removes the requirement that a vice president be appointed. In addition, the New Act provides that boards of Section 501(c)(3) of the Internal Revenue Code of 1986, as amended, public charities must be comprised of at least three directors. In comparison, both at present and under the New Act, boards of other nonprofit corporations (such as Section 501(c)(3) private foundations) are only required to have one director.

The New Act also imposes a five-year cap on director terms. While overall director tenure is not capped (i.e., a director may be appointed to serve for an unlimited number of terms), this restriction means affirmative board and member action will be needed to ensure director appointments are appropriately documented. Unless otherwise provided for in the organization's articles and bylaws, directors will have standard one-year terms. For organizations formed prior 1 January 2022 that have articles or bylaws providing for director terms longer than five years, the New Act allows for elected directors to continue for the duration of their existing terms (i.e., until the noncompliant term expires), subject to certain limitations. In a helpful addition, the New Act permits the Attorney General to appoint one or more directors if a charitable nonprofit has no remaining directors.

Other Changes to Current Law

Among numerous other changes, the New Act includes new provisions relating to amendments to organizational documents, mergers, domestications, conversions, the disposition of corporate assets, and dissolution. It also expands upon existing reporting and recordkeeping requirements and clarifies certain obligations relating to each. The New Act has no effect on the Nonprofit Miscellaneous and Mutual Corporations Act (Chapter 24.06 RCW).

EFFECT OF THE NEW ACT

The New Act is effective for most purposes on 1 January 2022. The New Act will apply both to all nonprofit corporations incorporated under the Current Act and to all nonprofit corporations incorporated thereafter. In general, the New Act was drafted with the intent of minimizing required updates for existing entities following the New Act's effectiveness. However, Washington nonprofit organizations should carefully review their organizational documents both to ensure compliance with the New Act and to consider whether they need to update their organizational documents to fully take advantage of its new provisions.

The New Act imposes requirements that may impact clients at both structural and operational levels. Please reach out to any member of the nonprofit organizations group at K&L Gates to engage in further discussions. We are happy to provide additional details of the new requirements and the potential impact on your organization.

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