



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

ON THE FOLLOWING MEASURE:

S.B. NO. 893, S.D. 1, RELATING TO NONPROFIT CORPORATIONS.

BEFORE THE:

SENATE COMMITTEE ON JUDICIARY AND LABOR

DATE: Monday, February 27, 2017 **TIME:** 10:00 a.m.

LOCATION: State Capitol, Room 016

TESTIFIER(S): WRITTEN TESTIMONY ONLY. For more information, call
Deborah Day Emerson, Deputy Attorney General 586-1471

Chair Keith-Agaran 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 a domestic nonprofit corporation to convert to a foreign nonprofit corporation under certain circumstances, to clarify provisions concerning a director's statutory duties, to clarify the optional, "safe harbor" procedure by which conflict of interest transactions may be handled by directors of nonprofit corporations, and to make technical amendments to provisions regarding dissolution of certain 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 When the Legislature repealed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This bill, if passed, will restore a portion of repealed section 414D-207, HRS, by: (a) authorizing domestic nonprofit corporations to convert to foreign nonprofit corporations; (b) creating a procedure regarding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-155, HRS, implies a duty of loyalty.

This bill amends sections 414D-149 and 414D-155, HRS, to expressly recognize that a director has a duty of loyalty. The express duty of loyalty will help to educate directors of their duty of loyalty and to better protect the nonprofit corporation.

C. Conflict Transactions.

At present, a conflict of interest transaction may be approved under an optional, “safe harbor” procedure where 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. To comply with industry best practices, this provision would require as a part of the safe harbor procedure the recusal from voting of any director who has a direct or indirect conflict of interest. The recusal from voting would not affect any quorum requirements. If for any reason the director does not wish to recuse him or herself from voting on the conflict of interest transaction, the transaction may nevertheless be valid under section 414D-150 if the transaction was fair at the time it was entered into.

D. Technical Amendments.

The bill amends section 414D-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 with an amended effective date of upon the bill’s approval.



ALOHA SOCIETY OF ASSOCIATION EXECUTIVES
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February 27, 2017

Testimony To: Senate Committee on Judiciary and Labor
Senator Gilbert S.C. Keith-Agaran, Chair

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

Subject: S.B. 893, SD 1 – RELATING TO NONPROFIT CORPORATIONS.

Chair Keith-Agaran 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 one (1) section 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.

We think the amendments to Section 3 should be deleted. It is much clearer in the current law without the amendment and this is best accomplished with a Conflict of Interest Policy an organization should adopt.

The language and interpretations are entirely too convoluted and confusing to be generally understood by the average administrator without the benefit of counsel who generally is not in attendance at most meetings except by special request.

We support S.B. 893, SD 1 without Section 3.

Thank you.