American-Scottish Foundation, Inc. (“ASF”)
Conflict of Interest Policy
Definitions and Procedures

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1. Introduction

Under New York statutory and Common Law principles, those involved in running a nonprofit, owe it a Duty of Loyalty, to serve in the nonprofit's interests and not in one's own self-interest. This Duty of Loyalty is shared, by a minimum, between Board Members, Officers and Key Employees (someone who can exercise "substantial influence"). This Duty of Loyalty means avoiding and resolving actual or apparent Conflicts of Interest ("COI") and Related Party Transactions ("RPTs").

New York's Not for Profit Corporation Law, mandates that a nonprofit's "independent" Board Members create a COI Policy to guide, at a minimum, the Board Members, Officers and Key Employees, on what constitutes a COI or an RPT, and how to resolve them.[1]

Under New York Law, an Independent Board Member is defined as a Board Member who:

(i) is not, and has not been within the last three years, an employee of the nonprofit or an affiliate of the nonprofit, and does not have a relative who is, or has been within the last three years, a "Key Employee" of the nonprofit or an affiliate of the nonprofit; and

(ii) has not received, and does not have a relative who has received, in any of the last three fiscal years, more than ten thousand dollars in direct compensation from the nonprofit or an affiliate of the nonprofit (other than reimbursement for expenses reasonably incurred as a director or reasonable compensation for service as a director as permitted by paragraph (a) of section 202 (General and special powers)); and

(iii) is not a current employee of or does not have a substantial financial interest in, and does not have a relative who is a current officer of or has a substantial financial interest in, any entity that has made payments to, or received payments from, the nonprofit or an affiliate of the nonprofit for property or services in an amount which, in any of the last three fiscal years, exceeds the lesser of twenty-five thousand dollars or two percent of such entity's consolidated gross revenues. For purposes of this subparagraph, "payment" does not include charitable contributions.

NOTE: These rules are NOT optional but mandatory, and they follow below. You should

[1] §712(c) and §715-a.

observe this Conflict of Interest Policy, because violations of this policy could:

- jeopardize your service as a Board Member, or Officer; and / or
- result in your termination of employment; and / or
- subject you to fines, lawsuits or tax consequences; and / or

• hurt this nonprofit's resources, its ability to serve its cause and its beneficiaries and members, and even threaten its tax exempt status or entire existence.

NOTE: You are expected to have read this policy, be familiar with its provisions and have a responsibility to ask questions about anything you do not understand. Therefore, ignorance of this policy will not be considered an excuse for violations.

Therefore, please take the time to study this COI Policy and take it seriously.

2. A Conflict Of Interest Is A Beginning, Not An End

It is important that you realize a COI, by itself, does not necessarily mean that a decision maker is disqualified from participating in a particular decision or transaction, or that a specific decision or transaction is void or voidable or should be avoided. However, certainly, these are possible outcomes. It is also possible that certain decision makers should recuse themselves, or for the nonprofit to disqualify them, from participating in that particular decision or transaction.

Therefore, a COI or RPT inquiry is simply the beginning of a set of realizations and steps that must be taken to "Review, Resolve and Report" the situation. In any case, the nonprofit must follow the procedures below, any time there is a COI, actual or apparent, as well as RPTs.

3. What Is A Conflict of Interest?

COIs can be thought of as either: (1) "actual" and (2) "apparent" (sometimes called "perceived") or (3) "Related Party Transactions" ("RPTs"). Board Members, Officers and Key Employees must guard against all three types in their actions.

a. Actual Conflict of Interest: This occurs when the nonprofit individual in question has a pervasive familial, financial, or personal interest that affects that individual's ability to be impartial, fully perform their job or role, or if they use company resources or information for their own benefit (personal use also can be a form of RPT, see below). It also could involve gifts, personal favors, loans, or an interest in property with the affected nonprofit individual. The individual or the individual's family do not necessarily need to benefit financially, but their personal interest might be so important that their judgment is compromised. Examples include:

• The nonprofit's "ethics officer" judges the appropriateness of their own actions (how can a person be impartial toward themselves?). Or, the nonprofit's ethics officer judges the appropriateness of the actions of their own manager (the ethics officer would have incentive to find wrongdoing or no wrongdoing depending on whether the ethics officer wanted to curry favor with or remove their own manager). Either way, it is questionable whether the ethics officer should be a judge of proprietary, and someone else should do this function in these cases, if at all possible.

- A Board Member votes on a measure that would involve the nonprofit in some activity that supports the cause of another nonprofit, of which, that Board Member also sits as a director. For example, if the Board Member belongs to an environmental nonprofit that is about to vote to preserve the habitat of a certain animal that the Board Member's other nonprofit raises money to protect. Even though both are good causes that produce no financial benefit to that Board Member, the Board Member is indirectly securing a benefit for this other cause that is of direct personal interest, in such a way that comprises that Board Member's impartial judgment on that particular vote and, at a minimum, he should disclose the Conflict of Interest and steps should be taken to address it.

- A research specialist for the nonprofit decides to mark certain information as non-confidential so they can pass it along to someone else who will give them perks like free baseball tickets and fancy free trips. Perhaps another individual in the nonprofit should decide which items should be confidential, or do so in conjunction with those dealing with the information, such as the research specialist (this way, an in-house expert can provide professional guidance, but there is a check and balance against RPTs).

- The nonprofit has a regular and substantial donor that wants special coverage for publicity sake, in the nonprofit's quarterly newsletter. The individual that edits the newsletter happens to regularly receive free baseball tickets from that donor. The nonprofit may or may not want to have a "gifts policy" that clarifies what can and can't be accepted. Either way, this could be an actual or apparent Conflict of Interest. The nonprofit may very well want to provide greater publicity to such a valued donor; but the free baseball tickets to the editor of the newsletter create a question as to whether the donor received coverage because of the gift. The Board should review this situation.

B. Apparent Conflict of Interest: This is sometimes known as a "perceived" COI. This occurs when a "reasonable person" might believe the judgment of the individual of the nonprofit *could* be compromised in a given situation, whether or not the individual is really capable or incapable of making an impartial decision (i.e. it *"looks bad."*). Examples include:

- The nonprofit's procurement officer, responsible for selecting vendors, just happens to have a friend that works for one of the several companies responding to the nonprofit's recent request for proposals for services. Although some may argue this is an "actual" COI, unless the procurement officer's friend is directly bidding for the project, the procurement officer *might* feel more inclined toward that company, but also, the procurement officer might not care, since it's not as if their friend will benefit in any substantive way. Nevertheless, the situation *could* seem unfair to a reasonable person, and the procurement officer should at least disclose or document the situation.

- A Board Member of a nonprofit involved in the tech industry, is asked to vote on a measure empowering the nonprofit's CEO to write a letter to a local legislator to change certain tech regulations. The Board Member owns <u>in</u>significant amounts of stocks in some companies, including tech firms. Even though the Board Member barely has any money invested in these companies, and even though it is debatable whether these regulations could increase or decrease the value of these companies, the Board Member's stocks *could* create a *perceived* COI to a "reasonable" outsider. Again, the Board Member, at a minimum should disclose their other involvement, and possibly should recuse themselves from both the deliberations and the vote.

c. Related Party Transaction ("RPT"). RPTs are highly defined by New York statute.[2] They can be thought of us as a form of self-dealing or dealing for the benefit of your relatives, or for the benefit of companies under your control.

Basic Definition: If any Board Member, Officer, or Key Employee is directly involved in a decision for setting compensation, a disposition of property, or other financial transaction of the nonprofit or the nonprofit's affiliate(s) (if any), where that Board Member, Officer or Key Employee has a current financial interest, or had a financial interest in the last five years, that is considered an RPT.[3]

Relatives: The same definition applies also to relatives of the Board Member, Officer or Key Employee in question, where those relatives have a financial interest or within the last five years had a financial interest, with the nonprofit or one of its affiliates (if any).

Controlled Entities: And finally, the above applies to entities "controlled" by the Board Member, Officer, or Key Employee and/or their relatives, if that controlled entity has a financial interest or within the last five years had a financial interest, with the nonprofit or its affiliates (if any).

Relevant defined terms are below:

Affiliate: An "affiliate" is another company, entity or organization, directly or indirectly controlled by or in control of this nonprofit, or otherwise related to this nonprofit through common control or ownership.

Controlled Entities: This means 5% or more of ownership in a partnership or professional corporation, or 35% of more ownership of another type of entity (such as C Corp).[4]

Financial Interest: The term "financial interest" would include, but is not necessarily limited to: (i) a loan or ownership of property used by this nonprofit (ii) purchasing goods, property or services from this nonprofit (iii) selling goods, property, or services to

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[2] N-PCL, §715; <u>also</u> <u>see</u> 26 <u>USC</u> §4958(f)(1)(A) and further specified in 26 <u>CFR</u> §53.4958-3(c), (d) and (e).
[3] N-PCL, §102.
[4] N-PCL, §102.

this nonprofit (iv) employment in this nonprofit or employment of anyone who worked in this nonprofit (v) some kind of conflict or competition with this nonprofit for property, or sales of goods or services, or some other economic benefit (vi) a lawsuit in which the nonprofit is involved (vii) use of confidential information obtained from this nonprofit to your economic benefit. All these meanings also apply to the nonprofit's affiliates.

Key Employees are people who can exercise substantial influence in the nonprofit.[5] A Key Employee might be someone required to be named in IRS form 990 due to their compensation, if they share authority to control or determine a substantial portion of the organization's capital expenditures, operating budget, or compensation for employees, or if they manage a discrete segment or activity of the organization that represents a substantial portion of the activities, assets, income, or expenses of the organization.

Officers generally are the President, Secretary, Treasurer, Vice Presidents, but may have different titles under the certificate of incorporation or the by-laws.[6]

Relatives are (i) spouses, ancestors, brothers and sisters (whether whole or half blood), children (whether natural or adopted), grandchildren, great-grandchildren, and spouses of brothers, sisters, children, grandchildren, and great-grandchildren; or (ii) a domestic partner as defined in section twenty-nine hundred ninety-four-a of the public health law.[7]

<u>Related Party Transactions Examples</u>

- A Board Member is president of a company that provides vital supplies that the nonprofit needs. The Board Member is willing to ensure that the company sells these supplies at a highly discounted value so that the nonprofit can acquire them cheaply. This is still an RPT and also a potential COI, even if the nonprofit gains a benefit from it and the Board Member's company breaks even or even loses money on the transaction. It might still be possible to conduct this beneficial transaction for the nonprofit, but proper steps have to be taken to legitimize this.

- The nonprofit's procurement officer decides to purchase supplies from a company significantly (35% or more) owned by the procurement officer's sister's spouse. Spouses of family members are counted as "Related Parties" and therefore this is an RPT. Again, this COI must be disclosed. Proper steps will need to be taken before anything further can proceed with this transaction.

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[5] NYS Attorney General, Conflict of Interest Policy, Guidance Document 2015 - 4, V. 1.0, Issue date: April 13, 2015, Page 2. https://www.charitiesnys.com/pdfs/Charities_Conflict_of_Interest.pdf
[6] N-PCL, §713.
[7] N-PCL, §102.

• The nonprofit issued a request for proposals to various companies to provide services, which will be reviewed by a committee of the nonprofit's employees. However, one of these committee members just happened previously to work (four years ago) for one of the companies applying to provide services. Although it's been four years since that nonprofit employee worked for the applying company, this qualifies as an RPT. Why? It's been less than five years that the nonprofit employee worked at the bidding company. The idea is that somehow the nonprofit employee still has loyalty to their old company, and that loyalty could compromise that employee's impartial judgment. Although this situation is probably harmless, the same steps must be followed as for above. The affected employee may have to recuse themselves from this committee, or the Board may decide to let them stay there after disclosing their history.

4. COIs and RPTs Prohibited Unless Fair, Reasonable and In Best Interest

The ASF will not set any compensation, dispose of any property, or permit a transaction, where a Board Member, Officer or Key Employee of the nonprofit, has an actual or apparent COI, or an RPT, as defined above in this COI Policy, unless the Board of Directors, through the procedures described below, determines that the compensation, disposition or transaction is fair, reasonable, and in the nonprofit's best interest at the time of the determination.[8] Any other actual or apparent COI or RPTs for Board Members, Officers and Key Employees, shall be resolved in the same manner (such as where their objectivity might be compromised).

Any COI involving employees, not Key Employees, may be resolved by similar steps, as those listed below, taken by the nonprofit's President, in consultation with the nonprofit's Ethics Officer or Human Resources Director, if any, whereby the President, after receiving all relevant material information in a reasonably timely fashion, must make a determination that the COI is reasonable, fair and in the nonprofit's interest at the time of determination. The President shall ensure that their reasoning, including any factors and alternatives considered, is properly recorded for the nonprofit's records and files.

5. Review, Resolve & Report[9]

1. Determine if an actual or apparent COI, or RPT exists, within the guidelines established above. This should be determined prospectively, or as they occur, but it is possible to make a retroactive discovery that should be addressed here.

2. Anyone, especially the affected Board Member, Officer, or Key Employee, who has any relevant information about the inquiry shall, in good faith, disclose material relevant facts to the Board, reasonably prior to any deliberations or vote, to enable a proper review and analysis of such information. Exigencies may help determine what constitutes a reasonable time prior to deliberations and voting.

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[8] N-PCL, §715.

[9] N-PCL, §715 sets many of these standards, which cannot be lowered or dispensed with, but only for "Related Party Transactions" (not necessarily other types of conflicts of interests).

3. The Board reasonably shall determine whether the compensation, disposition or transaction is **fair, reasonable and in the best interest** of the ASF, considering (a) the case particulars (b) industry standards and standards within the nonprofit (c) current situational factors (d) issues of timing (e) the overall best interests of the nonprofit (f) how the particulars appear to outside parties (including donors, the press, regulators and watchdog groups) even if the particulars are considered actually fair (g) and whether anyone would be improperly or unlawfully enriched. [10]

4. Prior to making a final decision, the ASF's Board should consider alternative compensation, dispositions, and transactions to the extent available or possible, or other individuals or ways to accomplish intended goals (i.e. consider substituting a Key Employee who has a COI, with an alternative qualified employee without a COI, etc.).

5. The Board thoroughly should discuss the COI or RPT before voting.

However: **A Board Member, Officer or Key Employee with an actual or potential COI or RPT, may not participate in deliberations or the vote to approve these particulars. Nor, should they attempt to improperly influence (coercing, manipulating, misleading, or fraudulently influencing)[11] the deliberations or vote.**

Exception: **A Board Member, Officer, or Key Employee, even with an actual or potential COI or RPT, may, at the request of the Board, present information, prior to the commencement of deliberation or voting.**

6. When the Board is ready, it should take a valid vote, according to its proper procedures, and determine an appropriate course of action by at least a majority vote of the Board Members. If a particular compensation, disposition or transaction (or other decision) that involves a COI or RPT, is not approved or otherwise addressed by at least a majority of the Board, then that compensation, disposition, transaction or decision cannot be approved and may not go forward.

6a. If the Board cannot satisfactorily resolve the situation at the current time, then the Board is free to deliberate and vote again at another time, especially if new information comes to light, but affected Board Members, Officers and Key Employees, still may not seek to influence improperly the deliberation or vote.

7. The Board, contemporaneously with its official deliberation and vote, shall document, in writing, the basis for the decision (including alternatives discussed) of the Board Members.

Dissent, Absent: A Board Member, absent from a Board Meeting that approved an actual

[10] 26 USC §4958(c)(1)(A) ("Excess Benefit Transactions): any transaction in which an economic benefit is provided by an applicable tax-exempt organization directly or indirectly to or for the use of any disqualified person if the value of the economic benefit provided exceeds the value of the consideration of such benefit.

[11] NYS Attorney General, Conflicts of Interest Policies under the Revitalization Act of 2013, Guidance Document 2015 - 4, V. 1.0 (April 13, 2015). https://www.charitiesnys.com/pdfs/Charities_Conflict_of_Interest.pdf

or apparent COI or an RPT, who does <u>not</u> agree with such a vote, shall ensure their dissent is recorded in the minutes (which may help protect that dissenting Board Member from future potential liability with respect to that vote).[12]

<u>Dissent, Present</u>**: Any Board Member, present at a Board Meeting, that approves an actual or apparent COI or a RPT, who does <u>not</u> agree with such a vote, shall ensure their dissent is recorded in the minutes (which may help protect them from future potential liability with respect to that vote).**[13]

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[12] N-PCL, §719(b).
[13] N-PCL, §719(b).