

COMMON CORPORATE QUESTIONS

There are a number of recurring questions posed to association executives (“AEs”) and officers. The answer to many of these questions lies within the Michigan Nonprofit Corporation Act.

Profit or Nonprofit Corporation?

When AEs and officers are looking for answers to corporate questions, the first thing that needs to be determined is what law governs the association. There is oftentimes confusion on this issue which arises from the loose use of terms. On more than one occasion, members believe that an association is organized on a “for-profit” basis. This leads them and their lawyers to believe that the association is governed by the provisions of the Michigan Business Corporation Act. They are often led down this path based upon their understanding that the association is not tax-exempt.

The issue of whether an association has obtained an exemption under Section 501(c)(6) of the Internal Revenue Code does not address this question of whether the association is organized as a profit or nonprofit corporation under Michigan law. An association of Realtors[®] in Michigan may be organized as a nonprofit corporation but claim no exemption under Internal Revenue Code Section 501(c)(6).

We have checked. Every Realtor[®] association formally incorporated under Michigan law is incorporated as a nonprofit corporation. Thus, corporate governance questions involving any local Realtor[®] association in Michigan will be governed by the Michigan Nonprofit Corporation Act (the “Act”).

Disclosure of Information

On occasion, associations receive requests or demands from members for very detailed information about the financial affairs of the association. These requests can include information as to the salary and benefits of employees of the association, specific expenditures by the association, and account balances of the association. Questions arise as to what information associations are required to provide to members and/or what members are entitled to know about the affairs of the association.

Many members somehow believe that the Michigan Freedom of Information Act (the “FOIA”) applies to a nonprofit corporation. There is absolutely no question that the FOIA has absolutely no application to a Michigan nonprofit corporation. The FOIA only applies to governmental entities.

The amount of information an association may be required to provide its members under the Act used to be very limited. However, under the amendments to the Act which became effective in 2015, members may be entitled to much more information. First, as before, Section 487(1) of the Act provides that upon written request by a member, the association shall mail to the member its balance sheet as of the end of the preceding fiscal year; its statement of income for that fiscal year; and, if prepared by the association, its statement of source and application of funds for that fiscal year.

Second, Section 487(2) now provides that a member may, during regular business hours, inspect for any proper purpose a list of the association’s members “and its other books and records,” if the member gives the corporation a written demand describing with reasonable particularity the purpose of the inspection and the records the member desires to inspect, if the records sought are directly connected with that purpose. This Section defines a “proper purpose”

as a “purpose that is reasonably related to a person’s interest as a . . . member.” The member must deliver the demand to the association’s registered office or principal place of business.

If the association does not permit an inspection required under Section 487(2) within five (5) business days after it receives a written demand from a member, or if the association imposes unreasonable conditions on the inspection, the member may go to the circuit court to seek an order compelling the association to permit the inspection.

If when the member goes to circuit court, he or she is seeking to inspect the books and records of the association beyond just a list of the association’s members, then the burden is on the member to establish that the inspection is for a proper purpose and that the documents sought are directly connected to that purpose. If, on the other hand, the member simply seeks to inspect a list of members of the association, then the association has the burden to establish that the inspection of the member list is for an improper purpose or that the member list is not directly connected with that purpose. The circuit court is granted broad discretion to determine what documents may be reviewed by the member, if any, to prescribe the conditions and limitations on the inspection and to order such other relief as the court deems appropriate.

It should be noted that Section 487(4) also grants a director the right to examine any of the association’s books and records for any purpose reasonably related to his or her position as a director. If the association does not permit the director to review the association’s books and records, then the director may also go to the circuit court, which may exercise its discretion to permit the director to inspect any and all books and records and to prescribe conditions and limitations on that inspection.

Finally, if a member or a director is required to go to court in order to obtain access to the association’s records and if the circuit court orders the inspection of the records demanded by the

member or director, then the court is required to order the association to pay the member's or director's costs, including reasonable attorneys fees, incurred in obtaining the order. The only exception will occur if the association proves that it failed to permit the inspection by the member or director in good faith because it had a reasonable basis to doubt the right of the member or director to inspect the records demanded.

In sum, pursuant to Section 487(1), if an association receives a request in writing by a member for the association's balance sheet for the preceding fiscal year or its statement of income for that year or its statement of source and application of funds for that year (assuming that one exists), the association should mail those documents to the member. If an association receives a demand from a member to inspect a list of the members, the association should make the list available for inspection within five (5) business days. Finally, if an association receives a written request for a member to examine other books and records of the association and the association does not want to comply with the request, it is strongly recommended that the association forward the request to its legal counsel to determine if there is a good faith basis for withholding any or all of the requested records. Otherwise, if the member goes to the circuit court and obtains an order requiring inspection of the requested documents, the association could be required to pay the member's costs and reasonable attorneys fees in obtaining the order. Prior to withholding any requested records, the association should have an opinion from its legal counsel that it can refuse the inspection in good faith because it has a reasonable basis to doubt the right of the member to inspect the requested records.

What Records Must Be Maintained?

If members can, upon a minimum of five (5) days written demand, review minutes of member meetings, question then arise as to whether minutes must be maintained for member meetings and what those minutes should look like or contain.

Section 485 of the Act simply requires that a nonprofit corporation keep “books of records of account and minutes of the proceedings of its . . . members, board, and executive committee, if any.” The term “if any” at the end of this sentence in the statute has been informally interpreted by lawyers as meaning “minutes of the proceedings of members, board and executive committee, if any such proceedings have been held.” A conservative interpretation of the statute would result in the conclusion that some form of minutes should be kept for all meetings of the members, board of directors and executive committee, assuming an executive committee exists.

There is absolutely no legal requirement with respect to the composition or content of minutes of a meeting of members, board of directors or executive committee. It has been recommended for some years that the minutes set forth the formal actions and record any abstention or votes if requested by a voting participant.

Who Runs This Association?

Some members have the mistaken belief that Realtor[®] associations are organized as participatory democracies and that all substantial questions should be resolved by a membership vote. The Act does not support this view of the governance of a nonprofit corporation.

Section 501(1) of the Act provides that the business and affairs of a nonprofit corporation shall be managed by, or under the direction of, its board of directors, except as otherwise provided in the Act or in the corporation’s articles of incorporation. The Act goes on in

Section 505(1) to require that a board of directors consist of at least three (3) persons, but that the number of directors shall be specified in the bylaws of the corporation, unless the articles of incorporation fix a number.

Obviously, an association can establish in its bylaws a number of decisions which must be approved or ratified by the members of the association. For example, a number of associations require that the membership approve the sale of any real estate owned by the association. As another example, many associations' bylaws require membership approval for expenditures by the association in excess of a specified amount. All that being said, the bottom line is that the Act places management of the association's affairs squarely on the board of directors.

Removal of a Director

At times, members of a board of directors or members of an association become dissatisfied with the performance of one or more members of the board of directors. They want to know how a member of the board of directors can be summarily dismissed from the board. In reviewing this issue, the first place to look is the bylaws or articles of incorporation of the association. As an example, many associations have a provision calling for the dismissal of members of the board of directors if they are absent without an acceptable excuse for a specific number of meetings.

The provisions in Section 511(1) of the Act governing the removal of a member of the board of directors are fairly straightforward.

First, a member of the board of directors can be removed by a majority vote of the members entitled to vote at an election of directors for any reason or no reason at all.

This provision makes sense, inasmuch as if a member of the board of directors is elected by a

majority vote of the members, he or she can also be removed by a majority vote of the members entitled to vote at an election of directors. The Act as amended in 2015, now provides that an association's articles of incorporation could limit the removal of a director only for cause. The association would need to amend their articles of incorporation to create this limitation.

Second, Section 511(2) also provides that a member of the board of directors may be removed with cause by a vote of the majority of the directors then in office. More than once, this provision has been misconstrued to permit the board of directors of a Realtor® association to vote a member of their board out of office. This provision only applies if a nonprofit corporation is organized upon a directorship basis under the Act. **There are currently no Realtor® associations in Michigan organized upon a directorship basis under the Act** and, therefore, this provision would not apply.

In sum, if members of a board of directors or members of an association wish to remove a member of the board of directors, they should look to the association's bylaws and articles of incorporation. The Act only permits the removal of a member of the board of directors through the election process.

The Officer is Not Doing Her Job

Members sometimes complain that an officer of an association is not properly carrying out his or her duties as an officer of the association. Members want to know what a specific officer is required to do under Michigan law. A description of the duties of a president, secretary or treasurer are not to be found under the Act.

Section 531(1) of the Act specifies that the officers of a nonprofit corporation shall consist of a president, secretary, treasurer and, if desired, a chairperson of the board, one or more vice presidents, and such other officers as are described in the bylaws or determined by the board

of directors of the association. Further, two or more offices may be held by the same person, although that officer cannot execute, acknowledge or verify an instrument of the association in more than one capacity.

Section 531(4) addresses the duties of officers of a nonprofit corporation. This statute specifies that an officer, as between that officer, other officers and the nonprofit corporation, has the authority and shall perform those duties in the management of the corporation “as may be provided in the bylaws or determined in accordance with a resolution of the board that is not inconsistent with the bylaws.”

Section 541 of the Act does require that a director and officer discharge the duties of that position in good faith and with the degree of care that an ordinarily prudent person in a like position would exercise under similar circumstances.

There are safe harbors for officers and members of the board of directors when considering complex information or rendering decisions on difficult issues. Section 541 provides that in discharging his or her duties, an officer or director is entitled to rely upon information, opinions, reports or statements, including financial statements and other financial data, if prepared or presented by any of the following:

1. One or more directors, officers or employees of the nonprofit corporation whom the director or officer reasonably believes to be reliable and competent in the matters presented;
2. Legal counsel, public accountants, engineers or other persons as to matters the director or officer reasonably believes are within the person’s professional or expert competence; or
3. A committee of the board of which he or she is not a member if the director or officer reasonably believes that the committee merits confidence.

It should be noted that the above three safe harbors for an officer or director do not apply if an officer or director has knowledge concerning the matter in question that would make reliance otherwise permitted to be unwarranted. For example, if a financial matter is before the board of directors and a member of the board of directors was a CPA with expertise in the matter before the board, that board member may not be able to rely upon an opinion offered by the association's outside accounting firm.

Who Gets to Attend the Meeting?

There are times when it is discovered that a member intends to attend a board of directors meeting and there is concern that the member may either bring up an inappropriate topic or behave inappropriately. The question arises as to whether the member must be permitted to attend the meeting. Some AEs have expressed concern that the Michigan Open Meetings Act (the "MOMA") requires that the member be permitted to attend the board of directors meeting.

First, the MOMA has absolutely no application to any meetings held by an association of Realtors[®]. The MOMA only applies to publicly incorporated bodies, *e.g.*, a township board of trustees or a city council.

Second, the Act does not require that a nonprofit corporation make its board of directors meetings, committee meetings, or any meeting other than a general membership meeting open to the members of the nonprofit corporation. The Act is simply silent on this issue.

Finally, if an association of Realtors[®] wishes to have a policy on permitting or not permitting members to attend board of directors meetings or other committee meetings, it may do so by addressing the subject in its bylaws. If an association of Realtors[®] wishes to control its agenda and prohibit general discussions of unknown topics by members who attend board of directors meetings, the association may wish to consider adopting a bylaw which permits a

member to notify the association in advance of their desire to attend the board of directors meeting and the subject upon which he or she wishes to address the board of directors. If it is determined that the subject matter is appropriate, then the member would be permitted to attend only that portion of the meeting at which he or she would be allowed to address the board.

Conclusion

Under the Act, a nonprofit corporation is run by its board of directors. The Act generally allows each association to establish its own rules of governance in its bylaws. In 2015, the requirements for providing information to members were significantly broadened. The possible risks in denying information to members have increased as well.

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