NONPROFIT FORMATION ISSUES

Presented by the
American Bar Association
Business Law Section Nonprofit Organizations Committee,
Section of Taxation Exempt Organizations Committee,
Commission on Law and Aging and
Center for Professional Development

Defending Liberty
Pursuing Justice

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This publication accompanies the audio program entitled "Nonprofit Formation Issues" broadcast on January 16, 2013 (event code: CET3NPF).

Table of Contents

Nonprofit Issues for the "Non" Nonprofit Lawyer

A Series of Three Webinars

Session 1: Nonprofits - Getting Started

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Threshold Issues

- What is a nonprofit?
- Difference between nonprofit and tax-exempt
- Differences in types of exemptions
- State versus Federal oversight

Alternatives to Organizing a New Nonprofit

- Already existing entity
- Fiscal sponsorship
- Business entity with charitable purposes
- Business entity with business purposes

Form of Entity

- Trusts
- Unincorporated associations
- Limited liability companies
- Corporations

Types of Nonprofits

- Public benefit
- Mutual benefit
- Religious

Types of Exemptions

- 501(c)(3) – charity
- 501(c)(4) – social welfare
- 501(c)(5) – labor/horticulture
- 501(c)(6) – trade/professional association
- 501(c)(7) – social club

Classifications within 501(c)(3)s

- Private foundations
- Public charities
  - Automatic
  - Public support test
  - Supporting organization

Formation Documents

- Articles/Bylaws
- Trust Agreement
- Certificate of Organization/Operating Agreement

Articles of Incorporation

- Limit provisions in articles to
  - Mandatory
  - Those which should not be easily modified
  - Allowed by State law to limit liability
- Purpose clause
- Irrevocable dedication of assets
- Resolving conflicts between documents

Bylaws

- Overview and Philosophy
- Should contain what needs to be in bylaws, but not more than is necessary
- Contains powers, basic rights, duties, and limitations of rights of the Board and the members, individually and collectively
- For guidance for legal content of bylaws, look at:
  - applicable corporation law
  - charitable solicitation laws
  - tax-exemption requirements, IRS Form 990 questions
  - Sector-specific legal requirements
  - volunteer limitation of liability (Good Samaritan) laws

10

Who Chooses the Directors?

- Membership v. nonmembership
- Delegates
- Appointed directors
- Self-perpetuating directors

Who Controls the Corporation?

- Members v. directors v. officers
- Difference between policy and day-to-day operations
- Overriding authority (*e.g.*, religious authority)
- Resolving disputes

Ancillary Governing Bodies

- Committees of the board
  - Executive Committee
  - Audit and/or Finance Committee
  - Board Development/ Nominating
- Advisory boards
- Duplicate boards (directors, elders, deacons, trustees)

Fiduciary Duties

- Duty of care
- Duty of loyalty
- Reliance and inquiry
- Directors’ versus Officers’ duties

Transactions Involving Insiders

- Legal standards versus organization culture
  - What can you do?
  - Even if you can do it, should you?
- Compensation of directors / officers
- Conflicts of interest policies

Director Protections

- Having good policies and following them
- Liability shields
- Indemnification
- Directors' and officers' insurance

Corporate Housekeeping

- Holding of meetings
- Minutes of meetings
- Policies
- Initial and continuing registrations
  - Annual/biennial filings (State)
  - Filings with Attorney General (State)
  - Tax returns (Federal & State)

Tax Status

- Default: taxable
- Exemption available?
  - Purpose
  - Organization
  - Operation
- IRS Form 1023 v. IRS Form 1024

Requirements for Tax-Exempt Status as a 501(c)(3)

- Exempt purpose(s).
- **Organized** exclusively for exempt purposes.
- **Operated** exclusively for exempt purposes.
- No private inurement.
- No candidate political activity.
- No substantial legislative lobbying.

Conclusion

DO GOOD WELL!

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NONPROFIT GOVERNANCE ISSUES

by

LISA A. RUNQUIST[1]

When you formed your nonprofit, did you actually think about the structure you wanted, or did you copy what someone else did? In the area of nonprofits, there is no such thing as a "one size fits all" structure. What is the best form of entity for your organization? Do you have members? If so, what rights, if any, have you given them? What is the difference between articles and bylaws, and what should be in each document? What is the difference between members, directors and officers? What other decisions should you think about?

What types of nonprofits are available?

Trusts

In the early days of the United States, the only way for a corporation to be formed was by special act of a legislative body. Thus, it was not uncommon for property dedicated to a charitable purpose to be held in trust for that purpose, rather than obtaining a corporate charter through special legislative action. Of course, the formation of a corporation has become a simple process of filing and the trust format for charitable entities has become the exception rather than the rule.

When we refer to a trust today, we are generally referring to an actual "trust" entity that has one or more trustees, trust assets, and a charitable purpose for which the trust was formed. The beneficiaries of a charitable trust are not defined individuals; they may be an undefined group of individuals, but the beneficiary may be a purpose unrelated to an individual, e.g. protection of the environment, etc. where the public good is the ultimate beneficiary. State law applicable to trusts generally also applies to charitable trusts. For example, a trustee may or may not be able to delegate his/her duties to another, depending both on state law and the language of the trust instrument.

1. **Lisa A. Runquist**, has over 35 years of experience representing nonprofit organizations, is the first winner of the Outstanding Lawyer Award, a Nonprofit Lawyers Award presented by ABA Business Law Section, and in 2010 became the first person to win both the Outstanding Lawyer Award and the Vanguard Award. She has authored numerous publications on nonprofit and religious organizations, including "The ABC's of Nonprofits", published by the ABA Business Law Section, and has been active in nonprofit and exempt organization committees of both the American Bar Association and the State Bar of California Association.

A trust may be established as a tax-exempt entity in the same manner as a corporation.

Unincorporated Associations

A nonprofit unincorporated association is another form that is sometimes used. It is not clear whether an unincorporated association is legal entity apart from the members that are involved therein. The Uniform Nonprofit Unincorporated Associations Act, as proposed by NCCUSL and adopted by some states, does regard the association as a separate entity. Further exempt status can be established for an unincorporated association, just as with a trust and a corporation. However, some states have found members of an unincorporated association liable (almost as "partners") in situations where members of a corporation would be exempt from liability. California has gone further than NCCUSL, and has revised its law so that unincorporated associations have many of the rights, and will be entitled to similar liability protections as are available for corporations.

Two essential elements of an unincorporated association appear to be the voluntary joining together, <u>and</u> a joining to serve a common or agreed purpose or objective. This purpose or objective, if the organization is indeed charitable, will not be to benefit any of the individuals involved, but rather is to benefit the charitable purpose for which the organization is formed. Thus, the members are such only because of their concern for the purpose, and not because they are going to achieve anything for themselves. Indeed, if the organization is to be exempt as a 501(c)(3) entity, they <u>cannot</u> receive something for themselves. Using this analysis, an unincorporated association should not be considered to be a partnership entity, but should be considered to be an entity apart from any of the individuals involved. Of course, if the nonprofit unincorporated association is not charitable, which would include most mutual benefits and co-ops, it might be argued that the members function more in the role of partners. However, even here, it is likely that the existence of the organization is not dependent upon the involvement of any particular individuals and that holding the unincorporated association to be an entity is more reasonable.

Limited Liability Companies

One form of business entity that has recently become popular is the limited liability company. It can be treated either as a corporation or a partnership for tax purposes. If the LLC only has one member, and the LLC does not elect corporate tax treatment, then the LLC will be a disregarded entity for tax purposes, although its structure allows for limited liability for organizational and operational purposes. The question has been raised as to whether a limited liability company could be exempt, and whether this could replace the more common forms currently in use.

It appears that the answer is that a limited liability company can be exempt if it meets certain requirements. However, a limited liability company is not a stand alone entity, but must have member(s). In a discussion by the IRS issued in September of 2000, concerning the tax exempt status of limited liability companies,[2] the IRS has stated that the organization may be a disregarded entity when it has an exempt organization as the sole member. It has also limited its analysis of when a limited liability company may be tax exempt as a separate entity, to those limited liability companies that have memberships composed only of other exempt organizations. It has not addressed the ability of a limited liability company with individual members (such as a congregational church) to be tax exempt.

If the LLC is a disregarded entity, then most attorneys have taken the position that it is not necessary to file a separate exemption application in order for it to be tax exempt.

It is likely that the limited liability company form will be widely used for certain situations that call for potential liability to be split off from the parent organization (such as with the holding of real property). The IRS CPE 2000 text sets forth twelve terms that must be contained in the organization documents before a limited liability company will be found to be exempt.[3] Because of variations in state law,the IRS requires that the first eleven of these conditions be contained both in the articles of organization and the operating agreement. Specifically, the documents must include:

1. A limitation of the LLC's activities to one or more exempt purposes;

2. A statement that the LLC is operated exclusively to further the charitable purposes of its members;

3. A requirement that the LLC's members be section 501(c)(3) organizations or governmental units;

4. A prohibition against the direct or indirect transfer of any membership interest to anyone other than a 501(c)(3) organization or governmental unit;

5. A statement that the LLC, interests in the LLC, or its assets, may be transferred to a nonmember other than a 501(c)(3) organization or governmental unit, only in exchange for fair market value;

6. A dissolution clause requiring the assets to continue to be used for charitable purposes;

7. A requirement that any amendments to either document be consistent with section 501(c)(3);

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[2] See ***Topic B, Limited Liability Companies as Exempt Organizations - Update;* 2000 (for 2001) *Exempt Organizations CPE Technical Instruction Program Textbook.***

[3] If the organization does not meet these conditions, the application must be referred to EO Technical for determination.

8. A statement that prohibits the LLC from merging with or converting into a for-profit entity;

9. A limitation that the LLC not distribute any assets to members that cease to qualify as a 501(c)(3) organization or governmental unit;

10. An "acceptable" contingency plan in the event one or more members cease to qualify as a 501(c)(3) organization or governmental unit; and

11. A statement that the LLC's exempt members will "expeditiously and vigorously enforce all of their rights in the LLC and will pursue all legal and equitable remedies to protect their interests in the LLC." [Question: how can the LLC represent what a separate entity will do?]

In addition, the LLC must represent that all of its organizing document provisions are consistent with state LLC laws, and are enforceable at law and in equity.[4]

There are some other issues with LLC's. The first is that in some states it is still unclear whether an LLC can be formed for nonprofit purposes.

In the states that do not clearly allow an LLC to be a nonprofit, there may be a question of whether property owned by the LLC can be exempt.

If the LLC is a disregarded entity (it has a single member which is exempt, and does not apply separately for exemption, as its finances are aggregated with its exempt member for tax purposes), a question still exists as to whether contributions to the LLC will be considered to be charitable contributions for which a deduction may be taken.

Another item to point out is that, unlike corporations, both LLC's and UA's must have detailed operational rules, as there are no defined rules as there are with corporations. This provides both more flexibility and more issues in setting the organization up. Unlike articles of incorporation, which can be relatively short and simple, the Articles of Organization must be much more detailed.

Nonprofit Corporations

The most common form of nonprofit is the corporation. A principal advantage of a corporation over other possible organizational options, such as an unincorporated association, is that the corporate entity is considered to be its own "person" for legal purposes, distinct from its members, directors and officers. Furthermore, a corporation operates under a clearly defined set of rules of governance and law. The status of an unincorporated association and its members is less clear, particularly if the organization has out-of-state activities. Perhaps most importantly, if a corporation is properly formed

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4 ibid.

and operated, it can offer considerable protection from personal liability to its individual directors, officers, shareholders or members.

The protection from personal liability for persons who act on behalf of corporations is not absolute. For that reason it is generally wise to make sure that the corporation either has substantial assets which can be used to pay such claims or that applicable insurance coverage is in place. Care must also be taken throughout the corporation's existence to observe proper formalities required of doing business in the corporate form, including, without limitation, management by or under the direction of the Board of Directors and the maintenance of minutes and other corporate records.

A business corporation generally exists to make a profit for its shareholders. In contrast, a nonprofit corporation (particularly a charitable organization) exists primarily to advance a purpose or objective, often charitable in nature. Therefore, the goal and focus of the management of charitable organizations should be to advance the entity's stated purposes, rather than the interests of any group of individuals affiliated with the charity.

Allocation of Authority Within the Corporate Structure

In a business corporation, shareholders elect the directors. If a nonprofit has members, the arrangement in nonprofits is similar, substituting members for shareholders. The directors are then collectively responsible for the management of the corporation's affairs. Unless either the statutory law or the corporation's governing documents reserve a particular issue or action for approval by the members, the law provides that the "activities and affairs of a corporation shall be conducted and all corporate powers shall be exercised by or under the direction of the board of directors."

Conflicts Between Documents.

You should look at your articles of incorporation and bylaws. If the articles were drafted recently by someone who regularly represents nonprofits, they will probably be relatively short and will only contain those items that are required to be in the articles of incorporation under state law. If they were drafted earlier (in California prior to 1980), they likely contain a significant amount of material that is no longer necessary under most current laws.

The real issue is when provisions are contained in the articles of incorporation that would normally be in the bylaws. One common problem is when the number of directors are listed in the articles AND in the bylaws; it is subsequently changed in the bylaws, but not in the articles, resulting in a conflict. If the two conflict, the articles will control. However, as most people look to the bylaws to determine the number of directors and their manner of election, there is generally no attention paid to this issue until litigation arises, and it is determined that the number of directors is really the 7 listed in the articles, rather than the 24 listed in the bylaws.

I would leave in the articles those provisions required by state law, any provisions that should not be easily changed (for example, a Statement of Faith for a religious organization), and any provisions allowed by state law to limit the liability of directors and officers. I would remove any other provisions, particularly if there is a similar provision contained in the bylaws.

Who Chooses the Directors?

Membership v. Nonmembership Corporation - If the corporation has corporate members, these persons have certain rights. There are clear reasons why a membership corporation might be preferred; however, the trend in most nonprofits is towards a nonmembership corporation (which may use the term "members" for fundraising purposes, but that is a noncorporate, nonvoting position – or should be). If your bylaws provide for members, there should be a method of adding and removing members, the members need to be specifically defined so they can be identified, and members meetings will need to be regularly held.

Delegates – Sometimes, with organizations that have affiliates, there may be delegates who function in some ways as members.

Appointed Directors – Some nonprofits have directors that are appointed by other persons. This again is often the situation when the organization is affiliated with other entities.

Self Perpetuating Directors – In such a case, the board itself is responsible for electing the directors. They may elect themselves or others. Sometimes such a corporation will have a limit to the number of terms a director may serve, without rotating off.

Who Controls the Corporation?

Sometimes members and/or delegates reserve some powers to themselves. However, in most instances, the corporation is ultimately controlled by the directors. The directors set policy, and "direct" what the corporation is to do. However, the directors are not responsible for the day to day operations of the organization. That is normally overseen by the officers.

The officers are normally elected by the board. They are responsible for the day to day operations, carry out the directives of the board, and report back to the board.

The directors may also set up committees of the board. Each committee has the power to exercise board authority over specific areas (e.g the "audit committee" may select the auditor, interface with the auditor, and the like). Committees report back to the board. Although committees of the board may exercise board authority, the board, as a whole, can always override a decision of a committee.

Sometimes an "executive committee" of the board actually controls most of the decision making; this is especially the case in situations with large boards. This is NOT something that should generally be encouraged, as directors, as a whole are responsible for the corporation. In such a situation, it may be that the "executive committee" is actually the board of directors and the rest of the board are really advisors. If this is the case, the bylaws should be amended to make this clear.

Especially with religious organizations, there may be an overriding authority that has the ability to oversee and modify decisions of the board. This should be carefully evaluated to make sure that by providing for this authority, the corporation has not actually transferred the liabilities of the board operations to the overseeing person.

A final issue that is not uncommon is to find that the authority of the board is split between more than one board. In such a situation, the question is: Who is ultimately in control and has the ultimate legal responsibility (i.e. fiduciary duties)? If this is not clarified, it can result in disputes that will need to be resolved by the courts.

What a Director Does/Does Not Do.

Directors are responsible for planning and directing the management of the charity's business and affairs. Directors have no individual power as a director to bind the corporation. Instead, directors take action as a body and those decisions are documented by Board resolutions. Directors who are also officers may be authorized by Board resolution to act on the corporation's behalf <u>in their capacity as officers</u>, but the Board acts as a unit.

Nevertheless, each director is individually accountable to the corporation's members and, in the case of directors of charitable organizations, to the state and federal regulatory authorities (primarily the IRS, the State Franchise Tax Board and the Attorney General) who seek to protect the public's interests in the charity.

The purpose of every act and decision of the director should be to advance the charity's purpose. If the personal aims of the individual are not the same as the aims of the organization, then the individual should not serve as a director. In no event should a director initiate or knowingly support or allow actions that will either exceed or defeat the charity's stated purposes.

Role of Corporate Officers and Agents.

Officers and agents of a nonprofit organization normally implement the decisions and policies established by the Board of Directors. Typically the Chief Executive Officer of a charity (often designated as its "Executive Director") and sometimes the Chief Financial Officer (typically called the "Treasurer") answer directly to the Board. Most other employees, agents and contractors answer to the Executive Director or other senior management duly authorized by the Board.

The Role of Committees In Charitable Corporations.

If a committee is intended to exercise the authority of the Board, non-directors may not serve. Further, committees with Board authority and their members must be designated by resolution adopted by a majority of the total number of directors then in office, at a meeting at which a quorum is present, provided, however, that the Articles or Bylaws of the corporation may modify this rule to require that committees be appointed by a majority vote of a specified number of authorized directors. The concept of "exercising the authority of the board" denotes actions which can bind the corporation without prior authorization from, or later ratification by, the Board.

In addition to committees with responsibility of the Board, corporations can create other committees that have no such authority. Actions of these committees must be ratified by the Board if they are to bind the corporation and their membership may include non-directors. If a committee has non-director members, its scope of authority is similar to that of other corporate agents who are delegated specific responsibilities by the Board, subject to the Board's ultimate direction and control.

Compensation of Directors

Private Inurement Issues. Although tax-exempt charitable organizations are prohibited from being organized to benefit any particular person or narrow group of persons, charities are not prohibited from compensating their directors, officers and employees although in California, 51% of the directors of a public benefit corporation cannot be paid for services other than as a director. However, as discussed below, this is the area in which most nonprofits get into trouble, sometimes losing their exempt status. Excessive compensation (i.e., "inurement") may cause the charity to lose its tax exempt status.

Effect on Liability Protections. It is also important to note that many statutes have been passed which seek to limit the liability of directors of nonprofit corporations so long as the director is serving as an uncompensated volunteer. Accordingly, the payment of compensation beyond a per diem or the reimbursement of a director's out-of-pocket expenses could preclude the director from enjoying these statutory liability protections.

Effect on Funding Opportunities. Finally, when excessive expenditures are made with respect to the Board and its activities, certain types of funding may be jeopardized. The purpose of the organization and the service of its directors should not be to benefit themselves as individuals or to provide "perks" to the Board and senior management. The principal objective should always be to advance the purposes of the charity, itself. Funds spent on Board activities are not available to advance the nonprofit purposes of the organization. Each Board expenditure should be justified in light of the corporation's specified purposes.

Documenting Decisions/Actions of the Directors

Action Should Be Taken At Formal Meetings or By Written Consent. Since directors are merely agents acting on behalf of the corporation, it is very important that their actions be taken in accordance with all legal requirements and that the actions be properly documented. Directors may only take action in one of two ways, namely, at a properly noticed meeting at which a quorum is present or by unanimous written consent (some states allow action by majority written consent).

Although in many states no prior notice is required of regular meetings of the Board when the time and place of such meetings are fixed by the Bylaws or by prior action of the Board, notice of meetings is generally required in all other instances. Notice should be given in the manner required by the corporate Bylaws and/or state law. If a quorum of the Board fails to appear at a meeting, no valid action can be taken, other than to adjourn the meeting.

> The IRS has now actively involved itself in the area of nonprofit governance. Although it has always been important, this intervention by the IRS into what has been a matter of state law, has made it even more imperative that nonprofit leaders take an active role in reviewing, restructuring if necessary, and implementing a corporate governance structure that will allow their organization to thrive in this new environment.

What Policies Does Your Organization Need To Adopt Or Update? What Should Be Included In These Policies? How Will Each Policy Be Implemented?

I have listed the policies referred to in the Form 990 below. At least some of these should be drafted, adopted and implemented by all nonprofit organizations. Many of these your organization may already have in one form or another. But even if you already have them, it is a good idea to periodically review them, to determine what changes might be necessary or appropriate, due to the changes in the legal climate. Of course, there may be some policies that you do not need at this point but may need in the future, and others that you do not need now, and are unlikely to need in the future.

Please note that the only thing worse than not having a written policy on an important matter is having a written policy and not following it. That is a recipe for disaster. Because many organizations are simply adopting policies that have been furnished to them by their accountants or taken off of the internet, without making sure that the policy is appropriate for their organization or can be easily implemented, such a policy is likely to be used against them in any subsequent litigation. Further, there may well be issues that were not considered when a policy is adopted simply so that the organization can check the box saying that they have such a policy; again this can work against the organization when that particular issue arises and is not covered. This practice of adopting a policy without examining all the potential implications may make the defending lawyer happy, but is likely to result in untold aggravation to the organization and its directors and officers. See *The IRS's New Regulation of Nonprofit Governance*, http://www.abanet.org/buslaw/blt/2009-07-08/runquist.shtml

With that said, let us briefly look at the policies:

1. **Mission Statement / Most Significant Activities** -- This is something that many organizations already have. The mission statement should be reviewed regularly, probably on an annual basis, to make sure that remains an adequate description of the purposes/activities of your organization, and that any necessary revisions are made.

What the IRS has ignored, is the fact that the Mission Statement is not the last word on the subject. The place to start in examining the purposes and activities, is the Articles of Incorporation. Generally there is a purpose clause that sets forth what the organization has been formed to accomplish.

Take a look at your Articles. What does the purpose state? Is this in line with what your organization does? If not, I would recommend that the Articles be amended, if possible, to bring them in line with your activities. If the Articles cannot be amended, then the organization needs to change its operations to be consistent with the purpose clause in the Articles, REGARDLESS of what your mission statement might say.

The Mission Statement should be a short, easily understood explanation of the goals and aspirations of the organization. It needs to be consistent with the purpose clause, but may include more specific goals. The Mission Statement can be amended on a regular basis, as the operations expand, contract, or are modified. Generally the Mission Statement is adopted by the board, whereas, if the organization has members, member approval is needed for amendment of the articles of incorporation. Further, amendments to the Articles require filing with the state Secretary of State or other similar governing body; changes to the mission statement can be done by resolution.

2. **Compensation Policy** - The process for determining compensation should include a review and approval by independent persons, comparability data, and contemporaneous substantiation of the deliberation and decision. For the CEO and the CFO, the ultimate determination of the compensation must be done by the board itself.

This policy is necessary to comply with the federal intermediate sanctions law (see http://www.runquist.com/article_intermedsancts.htm for more specific information), as well as some state laws, such as the California Nonprofit Integrity Act.

3. **Reimbursement Policy for Business Travel and Entertainment** (applies to officers, directors, and key employees).

This is an area in which many nonprofits get into trouble. One of the biggest problems I have seen has to do with the use of corporate credit cards. To the extent possible, my advice would be DO NOT HAVE CORPORATE CREDIT CARDS. Instead, have the person make the payment and seek reimbursement, or have the expense in question paid directly by the organization or, if the amount is known, have an advance made, with receipts and an accounting provided. It is understood that this may not be possible; for example, a federally qualified health center may have persons on its board that do not have credit cards. If credit cards are to be used, someone other than the user must match up the receipts to the statements and require reimbursement of any expenses for which receipts are not provided, or are not reimbursable expenses.

Note: I have seen organizations lose their tax exempt status, and officers be convicted of stealing from the corporation and sent to prison, when there have not been appropriate records kept, where there has not been a reimbursement policy in place that was followed, or when there has been inappropriate use of credit cards.

4. **Conflict of Interest Policy**. Questions in the Form 990 have to do with both the adoption and the implementation of a conflict of interest policy. Having a conflict of interest policy is not a new concept, and all nonprofits should have one. However, the Form 990 is now implying that a conflict of interest policy or policies must address not only potential conflicts of officers and directors, but also of key employees.

The conflict of interest form that the IRS prepared several years ago and which is contained in the instructions to Form 990 does NOT address conflicts that may be present for key employees. The organization may find it necessary to have more than one policy, as the potential conflicts of interest involving employees may well differ from the potential conflicts of interest of directors. If the nonprofit has not revised its policy within the past two years, it is likely to need revision.

Some nonprofits put the conflict of interest policy in the bylaws. I do not recommend this. I will insert a basic policy, but put most of the specifics into a separate policy adopted by resolution. One reason for this is to make it easy to revise, as the questions being asked by the IRS change. Take a look at your Bylaws. Does it say anything about conflicts of interest?

5. **Board Member Independence Policy** - Although some state laws require that a majority of the directors not be employees, there is no state or federal requirement that prohibits employees from being directors. In addition, the issue of independence is extremely complex.

The definition of an independent director has been endlessly debated in legal circles, especially with regard to business corporations. This has included significant concern about making sure that any requirements of disclosure specifically exempt disclosure of confidential matters. The body of legal analysis concerning these matters has been totally ignored by the IRS in both defining an independent director and in requiring disclosure. In fact, the IRS has ignored the existence of second issue. And it has developed a definition of independent director that is both simplistic (is there any financial benefit) and at the same time, extremely difficult to determine/implement.

It should be noted that there are many situations where a director might be interested in one particular item, but is otherwise disinterested. However, even if that director is disinterested more than 99% of the time, if he or she is financially interested in one particular item, the IRS has seen fit to classify the director as an interested director for all purposes. For purposes of discussion, let us assume that there are 5 directors, and that 4 of them fall into this category (each interest is different). With regard to those 4 items, the interested director recuses himself/herself, which means that 80% of the voting power is disinterested and voting on each matter. Let us also assume that each of those items has actually resulted in a benefit to the organization (e.g. provision of discounted services, etc.). Yet the required disclosure on the Form 990 will state that there are 5 directors, and that only one of them is independent..

As a result of the IRS having reduced the issue of independence to one of compensation, to avoid having an incorrect view of the governance of the organization reflected on a public document, many organizations have modified the structure of their corporate governance in a manner that may not be beneficial to the organization, to assure that "correct" answers are made to the questions. It should be noted that, contrary to the implications of the form, there are no "correct: answers. The result, however, of this type of modification is that the organization will likely have to forego the benefits that it could have derived from the directors, in order to assure that its directors are "independent" under the IRS definition. This is one of the negative results of the new form.

Has your organization made such changes? If so, was it done via modifications to the articles or bylaws?

Whether the organization decides to redo its governance structure or not (I would not recommend such a restructuring unless and until the organization makes a clear determination of what is ultimately going to be in the best interest of the organization) there needs to be a questionnaire to cover these issues (we normally recommend it be combined with the conflict of interest questionnaire, so that the directors only have one questionnaire to answer) so that the organization is able to appropriately answer the questions, with whatever explanations are necessary or desired. It should be noted that the IRS periodically revisits what it is requiring; therefore, it is appropriate to review the questions each year to make sure that the right questions are still being asked.

6. **Code of Ethics**. Having a code of ethics is probably a good idea. However, even here, an organization should not simply adopt a code of ethics that has been furnished to it, without paying attention to what impact it will have on the organization. Will the code be applicable to the directors? To the officers? To other employees?

7. **Whistle-Blower Policy**. Sarbanes-Oxley applies the whistle-blowing requirements to nonprofits (e.g. you cannot punish someone for reporting a violation of federal law), so having a written policy to prevent an inadvertent violation of this requirement is generally a good idea. It should be noted that SOX does not require that the organization have a policy for this purpose, much less a written policy; therefore, I would recommend that the

organization take its time to make sure that whatever policy is ultimately adopted will be easily followed by the organization. As noted earlier, it is better not to have a policy, than to have a policy that the organization does not implement.

8. **Document Retention/Destruction Policy**. Sarbanes-Oxley also applies the document retention/destruction requirements to nonprofits, so, as with the whistle-blower policy, having a policy is theoretically a good idea. However, this is an extremely difficult policy to both develop and implement.

It should be noted that the traditional concept of such a policy has been to provide the organization with an explanation of why some documents were kept and others were destroyed, and to give the organization the ability to get rid of documents without there being a negative inference that the documents were destroyed to prevent their later discovery. This only works if the organization actually keeps the documents required to be kept by the policy, and destroys the documents required to be destroyed. If the policy is not followed, or does not address a specific type of documents (e.g. email), then the existence of the policy may raise more questions than it answers.

The policy must be drafted only after careful consideration of the issues and options and, upon adoption, must be actually implemented. Otherwise, the organization would be better off without such a written policy.

9. **Document Integrity Policy**. This generally could be combined with a document retention policy.

10. **Endowments/Investments Policy**. Most organizations that have any significant investments generally have an investment policy that defines what types of investments are appropriate, percentages, and the like. This may include a determination not to invest in certain companies that do not operate in accordance with the moral beliefs of the organization. Such a policy should be re-evaluated on a regular basis, especially in light of today's economy.

It is less likely that an organization will have an endowment policy. However, if the organization has or is likely to have endowments, having or not having such a policy may result in even longer term consequences to the organization. For example, if a donor makes a contribution contingent upon a building being named after him or her, what happens if the endowment turns out to be insufficient to maintain the building? What happens then the building is demolished and a new building erected? If the endowment is made for some other specific purpose, how long will the donor and/or his or her family have a voice in determining if that purpose is being carried out, or what will happen to the funds if that purpose is no longer viable? Will funds that are contributed be governed by UPMIFA, or will there be a separate standard to determine when and what portion of the funds can be spent? These and many other questions will be addressed by a well drafted endowment policy.

11. **Financial Statements/ Audit Policy**. Any organization that is required by state law to have a financial audit, should probably have a definition of its audit committees and/or finance committees in its bylaws. Some accountants are now suggesting that the audit committee have a separate charter; as the audit committee is a committee of the board, having the structure and operation set forth in the bylaws should be sufficient. However, is appropriate to review the recommendations of the auditors to determine what else might be done to make sure the organization is adequately governed with regard to oversight of its finances.

12. **Form 990 Review Policy**. The Form 990 is a public document. In completing it, it should be treated as a public relations piece. Further, since it is available for pubic inspection, it is appropriate for those actually overseeing the organization to have reviewed the Form. The IRS wants to know if the final form was made available to the directors before it was filed; it also wants to know the process of actual review. It is appropriate to have a policy setting forth this process.

13. **Policy as to Public Availability/ Disclosure of Documents**. The form 1023, Application for Recognition of Exemption, as well as the forms 990 are required to be made available for inspection. This can be done by making the forms available on-line. Other forms, such as audits, may be required by state law to be made available. However, there is no requirement that most of the other documents that the IRS wants to know about, be made available for public inspection. It is up to the organization to decide on what documents will be made available for inspection, and if so, the terms of such disclosure.

14. **Gift Acceptance Policy** -- A gift acceptance policy, like the endowment policy, may be a very beneficial policy to develop and implement, as it will determine what limitations the organization is willing to have imposed on gifts, and when it is not in the best interests of the organization to accept a particular gift. This, again, should be carefully developed. As it is not possible to envision all situations that may be presented, I would recommend that a method be included by which questionable gifts will be presented to the board or a committee thereof for final determination before acceptance.

15. **Policy as to Contemporaneous Minutes**. In order to fit into the safe harbor of Intermediate Sanctions, one of the requirements is that a decision be reflected in the minutes, and that these minutes be approved by the board no later than their next meeting.

Even apart from that, it is good corporate practice to make sure that all board resolutions are appropriately included in the minutes, that the minutes are furnished to the board in a timely manner so that they can verify that the minutes accurately reflect the decisions of the board, and that the minutes are approved by the board no later than their next meeting.

16. **Fundraising Policy**. Although fundraising is intimately connected with the gift acceptance and endowment policies, the fundraising part of and organization's

operations has many rules and regulations, both state and federal, that need to be followed. Again, as with the other policies described herein, having a fundraising policy is a good idea, but should not be adopted and implemented without making sure that it complies with your state laws (or multiple state laws if you fundraise in more than one state), and that it is appropriate for your organization. For example, if no one on your staff understands a charitable remainder trust or how it functions, then whomever is doing your fundraising should not suggest a to a potential donor that a charitable remainder trust is an appropriate gift giving vehicle.

17. **Joint Venture Policy**. Although the Form 990 asks about a joint venture policy, it is hard to envision a "one size fits all" policy, especially in this area. There are so many types of potential joint ventures, that it is probably best to develop such a policy for each type of joint venture as it arises. If you want a generic joint venture policy it is likely to simply be a policy that the organization will not enter into a joint venture agreement with another organization, without making sure that such an agreement is in compliance with all state and federal laws, and that it does not endanger the exempt status of the organization.

18. **Conservation Easements Policy**. This type of policy is either going to be specifically needed by the organization, or is probably totally unnecessary. Most nonprofits will never be in a position to accept conservation easements. However, a few will want to have a detailed policy in this area.

19. **Policy re Operation of Chapters/Affiliates/Branches**. Except for those organizations that have extended operations through separately organized chapters, affiliates or branches, prior to the issuance of the instructions for the 2009 Form 990, I would have said that such a policy would be unnecessary.

But the instructions now direct the organization to answer yes "if the organization had during its tax year any local chapters, *DISREGARDED ENTITIES*, branches, lodges, units, or similar affiliates ... *AND local units that are not separate legal entities under state law* over which the organization has such authority." Although this nonsensical, as disregarded entities, for tax purposes, are NOT separate entities and are discussed elsewhere in Form 990. And I am not sure what "local units that are not separate legal entities under state law" is referring to. This seems to imply that if an organization controls various charitable remainder trusts, each trust needs to be listed. Or if the organization has divided its operations into three different parts, perhaps it needs to separately define each unit, even though they are all operated under the same corporate umbrella, and are not separate legal entities, even though they are located in different areas, have their own staff, etc. It makes no sense to require an organization to list separate parts of itself. Another example would be a nonprofit incubator that is a fiscal sponsor for a number of nonprofit start-up operations. Does the IRS want EACH of these listed separately here, even though the organization has already described its programs in Part III of Form 990?

As the answer to these questions is unclear, my inclination would be to follow the language of the question rather than the confusing instruction and, if necessary for completeness, add an explanatory note explaining where information concerning disregarded entities can be found.

The responsibilities and duties of directors, trustees and managers is not new, even if the government oversight has expanded. Although state law may differ, much of the law is the same throughout the various states.

What Is Meant By "Fiduciary Duty"?

General Definition. Modern usage of the concept of a fiduciary includes any person who has a duty to act primarily for the benefit of others in matters connected with the undertaking. The cases speak of a "special confidence reposed in one who, in equity and good conscience, is bound to act good faith and with due regard to the interests of the person who has reposed that confidence." The type of persons who are commonly referred to as fiduciaries include trustees, attorneys and corporate directors.

The Strict Trustee Standard of Duty. Cases involving strict fiduciary relationships, such as cases involving claims against trustees, also impose the rule that the fiduciary cannot exert pressure or influence on the party the fiduciary is serving or take any selfish advantage of his or her trust. Trustee-fiduciaries are also prohibited from dealing with the subject matter of the trust in a way which benefits the interests of the trustee or prejudices the beneficiary, unless the fiduciary is acting in the utmost good faith and with the full knowledge and consent of the beneficiary.

The Standard Applied to Directors of Nonprofit Corporations. The directors of both business and nonprofit corporations have been described in numerous cases as owing a fiduciary duty to their shareholders or members, as well as to the corporation. However, it is well established that a strict trustee standard of duty, which would prohibit any self-dealing with the corporation, regardless of the benefit conferred, is generally not what is intended or required (at least not in California). "A trustee is uniformly held to a high standard of care and will be held liable for simple negligence, while a director must have committed 'gross negligence' or otherwise be guilty of more than mere mistakes in judgment." (Stern v. Lucy Webb Hayes School, 1974, 381 F.Supp. 1033.) There was substantial concern among the drafters of California's Nonprofit Corporation Law that, if too strict a standard was imposed on directors by the Corporations Code, it would be difficult, if not impossible, to get qualified individuals to serve. There was also concern that application of the strict trustee standard would require charities to decline to participate in transactions in which the organization's directors were willing to provide goods or services at below market rates. (See H. Oleck, Nonprofit Organizations' Problems (1980).) California's statutory resolution of these issues reflects these concerns.

Statutory Definition of the Directors' Standard of Conduct (The "Duty of Care").

The standard of conduct prescribed for directors of nonprofit corporations is essentially the same standard that is imposed on business corporations. That standard is generally referred to as the directors' "duty of care." The basic rule reads as follows:

> A director shall perform the duties of a director, including duties as the member of any committee of the board, . . . in good faith, in a manner the director believes to be in the best interests of the corporation, and with such care, including reasonable inquiry, as is appropriate under the circumstances."

Directors are authorized to rely on information, opinions, reports or statements, including financial statements, prepared or presented by:

(a) One or more officers or employees of the corporation whom the director believes to be reliable and competent in the matters presented;

(b) Counsel, independent accountants and other persons as to matters which the director believes to be within such person's professional or expert competence; or

(c) A committee of the Board upon which the director does not serve as to matters within the committee's designated authority.

and for religious corporations,

(d) Religious authorities and ministers, priests, rabbis or other persons whose position in the religious organization the director believes justify reliance.

In relying on the opinions or reports of others, the director must, of course, act in good faith and conduct reasonable inquiry when the need for such inquiry is indicated by the circumstances. The director must also be free of any knowledge which would cause reliance on data received from others to be unwarranted.

The Directors' Duty of Loyalty

Generally. The admonition that a director must act in a manner that the director believes to be in the best interests of the corporation has often been termed the "duty of loyalty." The duty of loyalty has generally been construed as an obligation of the corporate directors to act in the best interests of the corporation and all of its members, including the members of minority factions, and to administer their corporate powers for the common benefit. See Remillard Brick Co. v Remillard-Dandini Co. (1952) 109 Cal.App.2d 405. This is in keeping with the fundamental nature of a nonprofit, to advance and achieve the corporate purpose, rather than to benefit the interests of any private individuals. Directors are to champion the best interests of their organization (which may include their constituents), rather than personal or selfish interests.

The Corporate Opportunity Doctrine. A common law component of the director's duty of loyalty is referred to as the "corporate opportunity doctrine". Under this doctrine, if a director becomes aware of an opportunity or transaction that would be of interest or benefit to the corporation he or she serves, the director is bound to disclose the opportunity to the corporation and permit it to take advantage of the opportunity if it so desires. If a full disclosure of the opportunity is made and the corporation declines to act, the director is then free to pursue the transaction for his or her own advantage. The basis for the doctrine is the "unfairness on the particular facts" of the director taking personal advantage of an opportunity that should rightfully accrue to the corporation. See Industrial Indemnity v. Golden State Company (1953) 117 Cal.App.2d 519.

Statutory Regulation of Self-Dealing Transactions. In speaking of a director's duty of loyalty, the common thought is that a director should avoid participating in, or seeking to influence, any transaction involving the corporation where the director has a conflict of interest. Most nonprofit corporation law contain no such bright line rule, although the Attorney General's representatives argued in favor of a complete ban on any self-dealing by nonprofit directors. Instead, there is often a complicated statutory scheme for approval of "self dealing transactions", which is generally any transaction to which the corporation is a party, and in which one or more of its directors has a material financial interest. Failure to follow proper procedures can result in strict sanctions on directors of public benefit and religious corporations, and to some degree mutual benefit corporations who engage in self-dealing transactions.

Generally, a self-dealing transaction, itself, is not void, voidable or invalid. Instead, the focus is on making the interested director disgorge his or her profits in the matter and making the organization whole. The Court can order the director to make an accounting and pay the profits to the corporation, require the interested director to reimburse the corporation for the value of any corporate property used in the transaction, or require the interested director to return or replace corporate property lost in the transaction or to account to the corporation for the proceeds of any property sold and to pay those proceeds, plus interest, to the corporation.

Absence of Personal Liability (The "Business Judgment Rule"). With the exception of liability for "self-dealing transactions", if a director performs his or her duties in accordance with the specified standard of care, the director shall have no liability based upon any alleged failure to discharge the his or her duties as a director. This exemption, which is commonly referred to as the "business judgment rule," applies even when the director's actions or omissions exceed or defeat the corporation's purpose.

The business judgment rule is rooted in the idea that directors should be entitled to (and in order to properly manage an enterprise must) exercise a broad range of discretion in issues of corporate management and should not be subjected to hindsight assessments of their decisions by the courts. The rule originated in the context of business corporations where shareholders often expect management to take risks in order to maximize profits. Although profit seeking is generally absent from the nonprofit, the justifications for the rule is no less compelling for directors of nonprofit corporations since the element of risk taking and the need for the organization to operate in a "business-like fashion" in order to continue in operation continue to be present; therefore, the concept that directors' decisions should not be second guessed without a substantial basis for doing so remains relevant to nonprofits. Frequently, it will not be obvious which of several alternative decisions will turn out to best carry out the corporation's mission.

Exception for Tortious Conduct.

Even if all of this is done correctly, at least in California, liability of directors and officers may be found to exist. See *Frances T. v. Village Green Owners Assn.*[5]

The California Supreme Court held in *Frances T.* that the business judgment rule is not a bar to individual director liability if a director participates in tortious conduct, *even if the director is acting in his or her official capacity.* Specifically:

> Directors are liable to persons injured by their own tortious conduct regardless of whether they acted on behalf of the corporation and regardless of whether the corporation is also liable.... Directors owe a duty of care, independent of the corporation's own duty, to refrain from acting in a manner which creates an unreasonable risk of personal injury to third parties.... A distinction must [also] be made between the director's fiduciary duty to the corporation (and its beneficiaries) and the director's ordinary duty of care not to injure third parties. The former duty is defined by statute [i.e., Corporations Code Section 7231], the latter by common law tort principles.

The California Supreme Court specifically noted that individual directors named in a personal injury suit have a defense against personal liability if their conduct was not clearly unreasonable under the circumstances or if they reasonably relied on expert advice or the decision of a subordinate who was in a better position to act. In light of the court's specific rejection of the business judgment rule as a shield from personal liability, this confirmation that directors have a defense to personal liability if they can prove that they reasonably followed expert advice or reasonably delegated decisions to a subordinate or committee seems inconsistent, yet beneficial. The *Francis T.* court also held that any director who did not vote in favor of the action which caused the injury would have a defense to personal liability.[6]

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[5] 42 Cal. 3d 490, 229 Cal. Rptr. 456, 457-459 (1986)

[6] See *Frances T. v. Village Green Owner Assn.*, supra, at 509-511. See also

Following publication of the *Frances T.* case, the California Legislature enacted and amended various code sections extending some measure of protection to directors of nonprofit corporations. These inconsistently worded liability protection statutes, with curious categories of included and excluded organizations, is indicative of hastily negotiated compromises reached by lobbyists for various segments of the nonprofit community.

Statutory Indemnification Rights of Directors and Officers.

In addition to the limited statutory protections against personal liability afforded by the general standard of care, state corporate laws generally permit corporations to indemnify directors and officers under a very strict and technical provisions. Even when such rights of indemnity are available, they are only as good as the financial strength of the corporation.

Seagate Technology v. A. J. Kogyo Co., 219 Cal. App. 3d 696, 702 (1990) and *Taylor-Rush v. Multitech Corp.*, 217 Cal. App. 3d 103, 112 (1990).

3

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QUICK GUIDE TO DRAFTING MINUTES OF MEETINGS

A corporation's minute books are its permanent, formal record of all corporate actions. They are open to inspection by the directors at any time, and by members, if any, for purposes related to their interests as a member. They will also be one of the first documents requested in the unfortunate event of any litigation against the organization, or any audit or investigation of the corporation by the Internal Revenue Service or the Attorney General. Therefore, it is important to keep the minute books complete and current. We also strongly advise you to maintain a duplicate minute book at another location, to protect against any loss or destruction of the original.

Minutes of meetings of the Board, each Board Committee, and the membership (if any) should include:[1]

- Affirmation that proper notice was either given or appropriately waived
- The date, time, and place of the meeting
- The name of each director in attendance, and the name of each absent director (or committee member or member of the corporation, as applicable)
- The names of any guests present at the request of the Board (such as lawyers, accountants, or staff members)
- A statement of the time at which the meeting was called to order
- The acknowledgment of the presence of a quorum for the transaction of business
- Approval of the minutes of the prior meeting
- A brief narrative description of the course of the meeting, with decisions and actions taken by the Board, Committee, or membership (if any) in the form of resolutions clearly highlighted, including a record of how each director/committee member/member voted (or that the vote was unanimous), and the names of any directors/committee members/members who abstained from voting, or who recused themselves for any reason

[1] This guidance is largely based on good corporate practice rather than statutory law. Note that if a meeting is required to follow Roberts' Rules of Order or other parliamentary authority, specific formats and additional information may be required.

  - Verbatim or highly detailed minutes are neither necessary nor desirable

  - Board and Committee meeting minutes should support the director's exercise of their fiduciary duties. The amount of time spent in discussions prior to making major decisions, and any follow-up information or investigation requested by the Board, are important to record for this purpose

  - Minutes should clearly address whether and how any conflicts of interest involving directors were addressed at a meeting

  - Minutes should clearly flag any meeting or portion of a meeting intended to be treated as a confidential and privileged attorney-client communication

  - Minutes should clearly flag any meeting or portion of a meeting denoted as an "executive session" and state whether staff or non-directors were excluded from that session. Minutes of executive sessions may be limited to a brief description of the topic discussed, and any resolutions passed, but should be included in the minute book.

  - If the Board relied on advice of counsel or other qualified experts in reaching a decision, that should be clearly stated in the minutes

- Attachments of any documents referred to in resolutions as approved or adopted

- If the meeting is an annual meeting, a record of the election and term of office of any directors or officers of the corporation whose terms expire in that year[2]

- Confirmation or arrangements for scheduling of the next meeting (if applicable)

- A statement of the time at which the meeting was adjourned

Each set of minutes should be submitted by the corporate Secretary for review and approval by the Board, the committee in question, or the membership (if any) at its next meeting. Then, after any amendments made at the subsequent meeting have been incorporated, the original minutes should be signed by the corporate Secretary, and filed in the minute book.

In addition to acting at a meeting, the Board or any Board committee may act by unanimous written consent. This takes the form of a document setting forth the actions to be taken, signed by each Board member or member of the committee, as the case may be. Signed

[2] If the directors are designated by one or more Designators instead of being elected, the Designators' letters notifying the corporation of each designation or other instrument of designation should be filed in the minute book, and no election of directors will occur.

originals of these consents should also be filed permanently in the corporate minute books. The membership may act by written ballot, as described in the corporation's bylaws and the applicable corporate law. Written ballots and tallies should also be filed permanently in the coporate minute books.

Any tax advice contained in this memorandum was not intended to be used, and cannot be used, for the purpose of avoiding penalties that may be imposed under federal tax law. A taxpayer may rely on our advice to avoid penalties only if the advice is reflected in a more formal tax opinion that conforms to IRS standards.

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FORMING A NEW CHARITY: AN OVERVIEW OF THE PROCESS

While no two situations are identical, especially since corporate and state tax law requirements and procedures vary from state to state, and so many variations and alternatives are possible for each step described below, a typical formation process for a new charity might look like this:

Step 1: Form a nonprofit public benefit corporation under applicable state law

- Decide in what state to incorporate the new charity (we often handle incorporations in Delaware and Nevada, in addition to California, and occasionally handle incorporation in other states, particularly Washington State and the District of Columbia).

- Make sure the chosen name is available and reserve it.

- Draft the corporate governing documents (typically articles of incorporation and bylaws).

- Client signs the articles of incorporation as the incorporator; we file them with the applicable Secretary of State's office (which starts the new entity's legal existence).

- Obtain a Federal tax ID number for the new entity from the IRS.

- Draft a corporate action document through which the incorporator adopts the bylaws and puts in place the initial Board of Directors and corporate officers.

- The Board should then hold the first Board meeting to complete the formation of the corporation.

The articles and bylaws set forth the governance structure for the corporation, specifying how the Board operates, what officers the corporation will have, etc. Perhaps most importantly, the articles and bylaws explain how the Board of Directors is chosen: by Board vote, by designation by an individual or entity, by a membership, or through some combination of these. We typically discuss these options with the founders, including the advantages and disadvantages of each, to help founders achieve their desired results within a charitable framework.

Once the entity exists as a legal person, it has the power to enter into contracts. It can open bank accounts and write or deposit checks as soon as it has a tax ID number and officers.

Once founders decide to proceed with incorporation, Step 1 can take as little as a week to 10 days in urgent circumstances in most states, but typically takes a few weeks to a few months, depending on how quickly the founders can make all the decisions required, and how complex the governance structure will be. To simply draft and file basic articles of incorporation, obtain a tax ID number, and name officers – the minimum required for the corporation to exist and start doing business – typically takes a few days in most states.

Step 2: Apply for tax-exempt status to the IRS and, if required, applicable state agency

Having a nonprofit corporation is not the same as being tax-exempt. Organizations that are exempt under Section 501(c)(3) of the Internal Revenue Code can offer a charitable contribution deduction to their donors and receive more favorable consideration for many government and foundation grants. To obtain 501(c)(3) status (and equivalent exemption at the state level, if required), the new entity must apply to the IRS and, if required, the applicable state taxing authority, on Form 1023 and the state equivalent.

- To complete the IRS form, we gather from the client extensive information about the people who will control the corporation, including directors and officers, and about the organization's plans and proposed activities.

- We advise founders as individuals, and/or the new entity, on tax law issues raised in the exemption application, such as private inurement, private benefit, conflicts of interest, compensation, fundraising, public support tests, lobbying activities, political activities, etc.

- We provide the complete IRS exemption application package for the client's review and signature.

- Once reviewed and signed by the client, we file the exemption application with the IRS.

- Together with the client, we respond as needed to IRS inquiries about the organization.

- Depending on state tax law, either at the same time as the IRS application, or after the IRS issues its determination letter recognizing the organization as exempt under 501(c)(3), we prepare and file forms if needed to obtain state exemption, generally attaching the IRS letter.

This process to the point of filing an exemption application with the IRS typically takes from a few weeks to a few months, depending on how quickly the client supplies the necessary information, the complexity of the client's plans and applicable tax law, and general attorney workflow considerations. It can start at the same time as Step 1, or later.

Once filed, the IRS will typically acknowledge receipt in approximately two weeks. Thereafter, the IRS screens applications, and those that it finds raise no issues of fact or law are processed within a few weeks to a few months. However, if the IRS has any issues or concerns, it assigns the application to a reviewer. The IRS informs the public, in general terms, of current processing times on its website at http://www.irs.gov/charities/article/0,,id=156733,00.html. For example, as of January 2013, the IRS was assigning for review applications received in March 2012. Once a file has been assigned, we expect to hear from the reviewer with follow-up questions within a few weeks. Sometimes, several rounds of questions may be required to address the reviewer's concerns fully. Assuming a favorable result is eventually reached, it could take from several weeks to several months from when the IRS assigns an application to a reviewer, to issuance of a determination letter.

It is sometimes possible to speed up the review process, especially with evidence that a grant is pending and will be lost unless the new charity can provide the funder with an IRS determination letter by a specified date.

Clients often ask when the new entity can begin accepting tax-deductible contributions. The answer is that, if the entity files its application within 27 months of formation, the IRS's determination of exemption will be retroactive to the date of incorporation. This assumes, of course, that the eventual IRS outcome is favorable. Until the IRS determination letter is issued, new entities should explain to potential donors that an application for tax-exempt status is pending. Donors who claim a charitable contribution deduction for their gifts before then take the risk of an adverse IRS decision. New charities with applications pending may also wish to arrange for a fiscal sponsorship to facilitate donations until they receive a determination letter from the IRS.

Step 3: Other initial filings

- Prepare and file any applicable initial filings with the state Secretary of State's office.

- Prepare and file the initial registration with the state's charity regulator, typically in the office of the state Attorney General.

- Depending on the new charity's proposed operations, various other initial filings at the state and local may be required, such as those relating to business licenses, employees, and charitable solicitation. We assist with these on request.

Step 4: Legal maintenance manual and corporate minute book

Founders of new charities may be quite experienced, or brand new to the requirements and duties of properly operating a nonprofit corporation within Section 501(c)(3)'s requirements. To encourage good corporate housekeeping, we typically provide new entities with an official corporate minute book for the corporation's permanent records, including the initial governing documents, exemption applications, and initial corporate actions. We include a memo for officers and directors covering a range of legal issues relating to operating the new entity in compliance with its tax-exempt and nonprofit corporate status, including:

- If the organization is a public charity, basics of federal tax law governing 501(c)(3) public charities and how to maintain public charity (rather than private foundation) status

- If the organization is a private foundation, basics of federal tax law governing 501(c)(3) private foundations

- Periodic reporting obligations and public information disclosure requirements

- Overview of charitable donation and solicitation rules

- For public charities, an introduction to holding and managing donor-advised funds

- Primer on corporate governance requirements and procedures

- Guidance on directors' fiduciary duties and governance responsibilities

- Guidance on keeping the corporate minute book

- Information on recommended internal policies such as records retention and whistleblower protections

- Suggested resources for further information

Such a memorandum can be an important risk management tool for the new charity's Board and officers, giving them all the basic information they need on the legal obligations they have assumed in creating a new charity.

In addition to the basic package of formation and exemption services, new charities or their founders often need additional help that we are happy to provide, such as:

- deciding whether a charity is the right vehicle in light of goals and founders interests, as opposed to operating as a for-profit, a fiscally-sponsored project, or under some other tax-exempt status than 501(c)(3)

- advising on membership structures or other complex governance arrangements

- interfacing as needed with regulatory agencies after applications have been filed, including drafting supplemental responses to IRS questions on the application

- preparing grant agreements and grant administration forms

- drafting agreements such as corporate name licenses or cost-sharing contracts with affiliated entities

- preparing or reviewing fiscal sponsorship arrangements while IRS determination is pending

- assisting with corporate governance beyond the basics, such as drafting meeting minutes or resolutions needed for client-specific situations

Any tax advice contained in this handout was not intended to be used, and cannot be used, for the purpose of avoiding penalties that may be imposed under federal tax law. A taxpayer may rely on our advice to avoid penalties only if the advice is reflected in a more formal tax opinion that conforms to IRS standards.

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