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A One-Hour(ish) Crash Course in Legal Compliance for Nonprofits

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The views expressed are my own (for better or for worse).



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Nonprofit Corporate Governance

A One-Hour(ish) Crash Course in Legal Compliance for Nonprofits

HIERARCHY OF RULES

- Internal Revenue Code
- N.C. Nonprofit Corporation Act
- Articles of Incorporation
- Bylaws
- Internal policies and procedures

N.C. NONPROFIT CORPORATION ACT

- Unusual provisions of N.C. law
 - Only one Board member required
 - No annual report
 - Inspection of financial records by the public
 - Voting members of Board committees must Board members

ARTICLES OF INCORPORATION

- Filed with N.C. Secretary of State
- Members vs. self-perpetuating board of directors
- Limitation of liability

ARTICLES OF INCORPORATION

- 501(c)(3) restrictions:
 - Charitable purposes
 - No private inurement
 - Limited lobbying
 - No political activity
 - Dissolution clause

BYLAWS

- Size and composition of board of directors
- Define rights of members
- Selection and term limits for officers and directors
- Quorum
- E-voting provisions
- Amendments
- Indemnification

RECOMMENDED POLICIES

- Conflict of interest policy with annual disclosures
- Whistleblower policy
- Document retention and destruction policy
- Compensation review and approval process
- Policies on chapters and affiliates

MORE RECOMMENDED POLICIES

- Policy on making organizational information available to the public
- Process for review of Form 990
- Gift acceptance policy
- Investment and spending policy
- Committee charters

A FEW TIPS

1. Review your bylaws and articles of incorporation regularly
2. Look for inconsistencies among your governing documents and policies
3. Amend articles of incorporation and bylaws as needed



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BOARD FIDUCIARY DUTIES

- Duty of Care
- Duty of Loyalty
- Duty of Obedience

DUTY OF CARE

- Responsibility to carry out board roles:
 - In good faith;
 - With the care an ordinarily prudent person in a like position would exercise under similar circumstances; and
 - In a manner the director reasonably believes to be in the best interests of the organization.

DUTY OF CARE

Discharging the duty of care:

- Showing up
- Paying attention
- Remaining informed
- Asking questions until reasonably satisfied
- The more consequential the decision, the more diligence required

Protected by the “Business Judgment Rule” but not when there is a conflict of interest or misconduct. Also may reasonably rely on the reports/advice of officers, counsel, professionals, committees.

DUTY OF LOYALTY

- Responsibility to put the interests of the organization above your own
 - Conflicts of Interest:
 - Know what constitutes a conflict and the process to handle it
 - Corporate opportunity doctrine
 - Confidentiality
 - When appointed by an employer

DUTY OF OBEDIENCE

- Responsibility to remain true to mission and governing documents:
 - Charter (Articles of Incorporation)
 - Bylaws
 - Policies
- (sometimes this duty is seen as a subset of the other duties)



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Federal Tax Laws for 501(c)(3) Nonprofits

- Filed to obtain determination of 501(c)(3) and public charity status
- Retroactive exemption if filed within 27 months of incorporation
- Not required of churches, integrated auxiliaries of churches, and organizations with less than \$5,000 in annual revenue

- Option for some small nonprofits
 - Expenses expected to be under \$50,000 for at least three years AND less than \$250,000 in assets
 - Not available to certain types of complex nonprofits
- Concerns about IRS review of 1023-EZ

EXEMPT PURPOSES – SECTION 501(c)(3)

- Religious
- Charitable
- Scientific
- Testing for public safety
- Literary
- Educational
- To foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment)
- For the prevention of cruelty to children or animals



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The Top Four Ways To Get In Trouble With The IRS

Tip #1

Get the most of your support from a single donor!

- Public charities vs. private foundations
- Public support tests

PUBLIC CHARITY STATUS

A charity is presumed to be a private foundation unless:

- Certain per se public charities (churches, schools)
- Charities that receive wide donative support (509(a)(1))
- Charities that have gross receipts from diverse sources (509(a)(2))
- Supporting organizations (509(a)(3))

Tip #2

Pay your board members! (or at least too much)

In Indiana, a Nonprofit Hospital Richly Compensates Its Board Members

Tip #2

Pay your board members!

- Prohibition on private inurement
- Excess benefit transactions
- Private benefit
- (Also may forfeit immunity)

PRIVATE INUREMENT AND BENEFIT

- Inurement: net earnings flowing to or for the benefit of insiders; no inurement permitted
- Private benefit: operating to benefit private interests more than incidentally
 - Benefit can flow to insiders or unrelated third parties.
- No bright lines: All facts and circumstances

INTERMEDIATE SANCTIONS

- Alternative to revocation for violations of private inurement.
- Penalizes transactions that convey greater value to a “disqualified person” than the exempt organization receives in return.
- Penalties are imposed on the disqualified persons and potentially on organizational managers who approve a transaction knowing it conveys excess benefit.



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Tip #3

Don't bother filing your 990!

Ooops... big ooops.

FORM 990

- Every nonprofit must file a Form 990, 990-EZ, or 990-N with the IRS every year
 - Automatic revocation for non-filing for three consecutive years
 - Due date
 - Available to the public
 - Review by board

FORM 990 FILING THRESHOLDS

Form	Gross Receipts	Total Assets
990	\$200,000+	\$500,000+
990-EZ	<\$200,000	<\$500,000
990-N	<\$50,000	N/A

FORM 990 E-FILING

- New law in 2019 – Most nonprofits must file Form 990 or 990-EZ electronically
 - Effective for fiscal years beginning July 2, 2019 or later
 - IRS may delay implementation for small nonprofits for two years
 - Annual gross receipts under \$200,000 and total assets under \$500,000
 - IRS must give notice after failure to file 990s for two years

Tip #4

Be partisan!

- Lobbying is legal for 501(c)(3) nonprofits
- But partisan political intervention is impermissible
- Nonpartisan election-related activities are allowed

LOBBYING SYNOPSIS

1. What is lobbying?

- Influencing legislation at the federal, state or local level

2. It's permissible for 501(c)(3) nonprofits!

How much lobbying can you do?

(as a 501(c)(3) nonprofit)

Two answers:

1. An “insubstantial” amount
2. 501(h) election – expenditure test

ELECTIONEERING

- Provision in Section 501(c)(3)
 - Charitable nonprofits, foundations, and churches cannot:
 - Support or oppose candidates for office
 - Make campaign contributions
 - Coordinate activities with political campaigns

UNRELATED BUSINESS INCOME TAX

- What is UBIT?
 1. Trade or Business
 2. Regularly carried on by a nonprofit
 3. Unrelated to a nonprofit's mission

UNRELATED BUSINESS INCOME TAX

Certain passive investments excluded:

- Dividends, interest, royalties, rents from real property
- Substantially all of the activities conducted by volunteers; also, thrift shops
- Activities conducted for convenience of members, students, patients, and employees

SILO-ING OF UBIT

- General principle – nonprofits pay UBIT on the *net* income from their unrelated business activities
- New IRC Section 512(a)(6)
 - Nonprofits must calculate net UBIT for each “separate” “trade or business”
 - Concerns are undefined terms and the “silo-ing” of expenses into each unrelated business activity

SILO-ING OF UBIT

- New IRS Regulations
 - Nonprofits should use two-digit NAICS codes to group together their business activities
 - No de minimis exemption from silo-ing of UBIT for organizations with relatively small amounts of unrelated business income
 - Unrelated business income from investment activities (e.g. a nonprofit owning interest in a business entity) can be grouped together as long as the nonprofit either:
 1. Owns less than 2% of the profits and capital interest of the entity; or
 2. Owns less than 20% of the capital interest and can't directly control the entity



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Charitable Solicitation and Donor Acknowledgment

Filing Requirements

- License required for most nonprofits
- Exemption for nonprofits that:
 - Less than \$25,000 in grants and contributions per year;
and
 - Do not compensate officers, directors, or professional fundraisers
 - Note: Legislation would increase this to \$50,000
- File with N.C. Secretary of State

Statutory Requirements

- Religious institutions
- Private schools
- Hospitals
- CCRCs
- YMCAs/YWCAs
- Volunteer fire departments, rescue squads and EMS

Filing requirements for individuals

- Fund-raising consultants
- Solicitors
- Contracts must be filed with Secretary of State
- Burden is on nonprofit to check that contractors are licensed

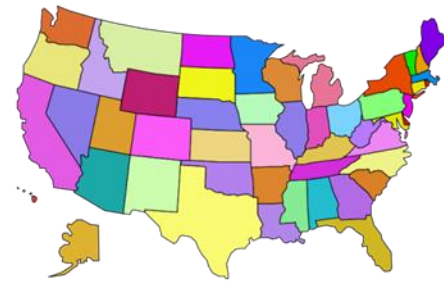
Question: Do you need to register in other states?

Answer:



CHARITABLE SOLICITATION

- *Does a nonprofit need to register in other states?*
- **Charleston Principles (NASCO)**
 - Non-binding
 - Not followed by all state charity regulators
 - Developed in 2001



Possible future development for multi-state filing

- NASCO is looking into a single portal for multi-state filing
 - Probably a long process
- Clarity and consistency in statutes in different states
 - Donate buttons on websites
 - Challenge – coordination and agreement of state legislatures

SOLICITATION DISCLOSURES

- Name of organization
- Address of organization
- Purposes for which contributions will be used
- Disclosures required on gift acknowledgments, website and other solicitations

DONOR ACKNOWLEDGMENT

- Acknowledgment *required**:
 - for all gifts of \$250+, and
 - receive gifts of \$75+ for which you provide valuable goods or services
- Note: Donors who give certain noncash gifts may be required to file a Form 8283 and get an appraisal

*The burden is actually on the donor to have this written acknowledgment, so technically a nonprofit is not required to provide it. Having said that, if you want your donors to continue to make contributions, you should strongly consider providing written acknowledgment letters. Furthermore, if you can read this footnote, you are straining your eyes too much!

OTHER CONSIDERATIONS

- UPMIFA
- Mergers, Transfers, Dissolutions
- Activities in other states
- Foreign Activities

QUESTIONS?

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