

How to Help Nonprofit Clients

This section of the Web site is intended for law faculty and small business and entrepreneurship programs representing nonprofit corporations. It is intended as a primer for those unfamiliar with nonprofit law. Sample materials are for illustrative purposes only, and are intended to provide a starting point. Faculty and students must consult the specific statutes in the states in which they work and draft their own documents to reflect the case-specific facts and legal requirements in their jurisdictions. Although there are myriad types of nonprofit organizations, most law school programs represent almost exclusively nonprofit corporations. Therefore, this section will be limited primarily to information regarding nonprofit corporations.

Clicking on the hyperlinks will refer the reader to collections of illustrative materials on this Web site. There are many other resource materials related to the formation and operation of all manner of nonprofit entities, including forms, texts, guidebooks, law review articles, and business forms and articles. Students and faculty who wish to pursue these other resources can, of course, use their own law libraries, Westlaw and Lexis accounts, and search engines such as Findlaw.com.

Other source materials contained on this Web site include [Resource Links](#) and [Entrepreneurship Law Scholarship](#).

Some clinics may find it helpful to create an internal document and resource depository, or even a "wiki," which is a type of Web site that permits authorized users to make changes to form documents and other internal resource material, as often forms need to be updated annually.

The following outline is very basic and is intended only as a guide to highlight key issues faculty and students should consider when representing nonprofit corporations. Much more detail can be found in numerous print sources (SEE ATTACHMENT "[NONPROFIT PRINT SOURCES](#)") that have been written, as well as some excellent website resources for nonprofits. (SEE ATTACHMENT "[NONPROFIT WEB RESOURCES](#)") Most law school clinics serving nonprofits will be dealing with the formation and ongoing operations of a charity, and less frequently with mergers and dissolutions. This Roadmap is divided into three main sections: Starting a Nonprofit, Running the Business, and Merger and Dissolution.

STARTING A NONPROFIT

Law students frequently will be involved in starting a charitable corporation. Before beginning, however, it is important that the legal clinic have the following in place:

- Name, address and contact information for appropriate state agencies with jurisdiction over nonprofits (usually the Secretary of State's office is the agency in charge of incorporating nonprofits, and the Attorney General's office is in charge of regulating non profit activity, but check with your state to make sure you have identified the appropriate agencies.)
- Up-to-date information on filing requirements, as well as all necessary formation forms.
- Up-to-date information on state laws and regulations specifically related to regulation of nonprofits and non profit activities.
- Current IRS (state and federal) forms and publications.
- Contact information for trusted accountants with specialized knowledge of non profit accounting and financial procedures
- Contact information for trusted lawyers with special expertise in the area of nonprofit corporation issues, board governance, tax, labor and employment law.

Forming a Nonprofit Corporation

Initial Client Intake

Students in law school clinics representing nonprofit clients should use intake worksheets as a starting point for gathering initial information from clients. This information is extremely important for use in identifying legal issues and in assisting clients through the formation process. (See [FORMATION DOCUMENTS: Nonprofit Clinic Worksheet](#) for more information) In addition, it is helpful for students to have a "checklist" to work from, so that all necessary tasks are completed in a timely manner. (See [FORMATION DOCUMENTS: Checklist for 501\(c\)\(3\) or NonprofLegalCheck - Spanish](#) for more information). Students should also be aware that conflicts can arise when representing nonprofit corporate clients, and performing a conflicts check is an important part of the initial client intake process. (See [FORMATION DOCUMENTS: Conflicts Questionnaire](#) for more information).

Before forming an entity, the lawyer and law student should thoroughly explore with clients two main issues: the purpose of their proposed enterprise and the constituency they intend to serve. It should not be assumed that a tax exempt organization is always the most appropriate vehicle for accomplishing the clients' goals until after the interview takes place and facts are thoroughly reviewed. (See [FORMATION DOCUMENTS: Student Questions Choice of Entity](#) and [Advantages/Disadvantages of Nonprofits](#) for more information). The following considerations should be explored with the client:

1. The purpose and mission of the organization;
2. Whether or not the organization intends to make a profit in whole or part;

3. Sources of funding: E.g., do the clients anticipate obtaining funding from donors, paying clients, government grants, other private sources, and what is the funding plan;
4. Technical expertise: Setting up and operating a nonprofit often requires strict compliance with detailed government tax and funding regulations that a for-profit entity usually does not - does the nonprofit have persons capable of managing, and performing, these tasks;
5. Time considerations: A for-profit venture usually can be set up and operating within a short time period - the application process for federal tax exemption is often long and involved; the urgency of the organization's needs, and what are plans for funding the operation prior to receiving tax-exempt status.
6. As with for-profit entities, not all nonprofits are created equal. There are several types of nonprofit organizations, and each carries with it many implications. As is mentioned above, this Roadmap deals exclusively with nonprofit corporations.

Creating a Structure

State law governs the creation and operation of a nonprofit. The first step in creating the nonprofit corporation must be to determine what the state requirements are for creating a legal entity: this can be done by contacting the state agency responsible for registering corporations and nonprofits, such as the Secretary of State's office. Typically such a corporation is formed by filing some type of nonprofit articles of incorporation with the responsible agency. In some states, charities are also required to register with that state's Department of Justice, Attorney General's Office, or Corporations Division. (See [FORMATION DOCUMENTS: Choice of Entity Letter](#) or [TAX DOCUMENTS: Tax Considerations for Illinois Nonprofits](#)). The National Association of State Charity Officials ([NASCO](#)) is an organization of state officials that regulate charitable organizations and fundraising, and has links to state-specific information. Attorneys advising non-profits should also be aware of a new type of limited liability company (LLC) that is called an L3C ([NON PROFIT FORMATION DOCUMENTS: L3C Booklet](#)). To date, only five states have authorized this type of venture, but it definitely bears consideration by the careful advisor, especially for clients who are interested in for-profit activities, and those interested in participating in program-related investments of non-profit foundations

When forming an entity, the following basic elements should be included in a checklist:

Members

Most states recognize both membership and non-membership organizations. If the clients select to create a membership organization, the lawyer must help the client determine whether those members should have voting rights. This

section will not discuss membership organizations, however attorneys should be aware that different requirements apply to membership and non-membership nonprofit corporations. Usually it is much easier for a nonprofit that is just starting out to choose to be a non-membership corporation.

Board Selection and Composition

Increasingly, since Sarbanes-Oxley, the IRS and the courts have given greater scrutiny to the governance of non-profits. Thus, the selection of board members for a start-up organization is one of the most important parts of the entity-formation process. Some things to consider when creating a “start up” board include:

Number: Specific state laws set forth requirements for member and non-member organizations, including the minimum number, composition, and officers on the board. Nonprofits can definitely provide for more than the minimum in the bylaws or articles of incorporation. Organizations should carefully consider factors that will influence the number selected, however, including the amount of work that will be required of members, the number needed to constitute a quorum, and whether the number will be large enough to accomplish the organization’s business but not so large that it is impossible to function efficiently.

Composition: This is arguably the most important element of board selection, and can have the greatest impact upon the organization’s ability to thrive. Once again, a [checklist](#) should be developed to assist clients with ensuring the board is well rounded, contains the appropriate operational and substantive expertise required (such as financial, fund-raising ability, etc.), and reflects the community served.

Officers: Most nonprofit corporations also are required to have officer positions; the most common are equivalent to a secretary and a chair or president. Additional officers can be appointed, and most boards include at least a treasurer (or budget and finance position), and fundraising officer as well. It is always a good idea to set forth in the bylaws the guidelines regarding the roles, rights, and responsibilities of board members and officers. In addition, if the Executive Director is to be an officer or board member, the Director’s duties should also be set out in the bylaws.

Selecting a Name, Obtaining an EIN Number, Filing Articles of Incorporation

Name and EIN Number: Before filing Articles of Incorporation, clients must select a name for their nonprofit. States may have specific regulations that may restrict the types of names that can be used, and it is important to check with the governing state agency to make sure the name complies with such regulations before proceeding to file the Articles. It also is important to perform an online search to protect the entity from claims of infringement. If

an exempt corporation later changes its name, it must notify the IRS. (See [TAX DOCUMENTS: IRS Change of Corporation Name](#) for more information). Once the corporation is formed, you should obtain a state ID number and an EIN (Federal Employer Identification Number) from the IRS. You can then set up a bank account using the EIN - make sure when doing so to designate authorized signers and co-signers.

Articles of Incorporation: Every nonprofit corporation must file Articles of Incorporation with the appropriate state agency. Most state agencies have pre-printed forms with explicit directions that must be followed to the letter. The Internal Revenue Service has information [online](#) that can help ensure you insert the correct language. As is noted on the IRS website, to obtain federal tax-exempt status, the Articles must include a statement that the purposes of the organization are exclusively charitable, educational, or scientific within the meaning of Section 501(c)(3), and a section that provides that upon termination or dissolution the organization will transfer assets and liabilities to another 501(c)(3) organization. The corporation will become official once the Articles of Incorporation are filed with the appropriate state agency. Be sure and check with the state agency regarding the specific action it takes that determines the filing process is "complete." (e.g., the mere process of sending the articles, having the documents stamped by the agency, receipt of a formal letter, etc.) Always make sure to check for filing fees and include them with your submission. Only after the Articles of Incorporation have been filed can the organization hold its first meeting.

Bylaws: The bylaws set forth the structure of, and operational procedures for, the nonprofit. (There are different legal procedures for a membership vs. non-membership organization, which will not be addressed here.) Clinics should develop a checklist of items to be contained in bylaws that carefully track the requirements set forth in the appropriate state statutes. Always check with the state agency to make sure you have updated information. This section will not set forth all the items that should be included; many excellent references and checklists discuss these matters in detail. At the very least, bylaws should contain provisions relating to the following: 1) whether or not the entity is a membership organization; 2) the name and purpose of the corporation; 3) board composition (including qualifications, voting, and operation of meetings); 4) board duties (including number and terms of directors, removal from office, vacancies); 5) number and types of committees; 6) officers (board chair, titles and duties, election); 7) if the Executive Director is to be a board member or officer, enumerate the Director's duties; 8) a provision for amendments and 9) a conflict of interest policy that conforms with that recommended by the IRS. (See [Appendix A](#) of the IRS Instructions for a sample; in addition, state law often provides standards for board conduct in the event of potential conflicts of interest).

All clinics should have on hand a copy of the new Governance Section in the IRS Form 990. Although the Form 990 is a tax return and not a form that needs to be filed when applying for exempt status, the form requires specific information regarding nonprofit corporate governance that may need to be addressed in an organization's bylaws. In addition, there are governance-related questions contained in other areas of the Form 990. Therefore, when drafting the bylaws of a new nonprofit corporation, review the latest version of the Form 990 and the instructions. The [Form 990 and instructions](#) are on the IRS Web site, as is [background information and commentary](#) and the [June 2008 ACT report](#).

Bylaws may have to be filed with the state agency where the Articles of Incorporation were filed; practitioners should check specific rules within their states. Nonprofits applying for federal tax-exempt status must file their bylaws with the IRS, however.

(See [BYLAWS NONPROFIT: Bylaws of Unincorporated Association](#); [Bylaws Non-Members Corporation](#); [Bylaws Non-Voting Membership Corporation](#), [Bylaws Voting Members Corporation](#) for more information).

Applying for Tax-Exempt Status

Federal Tax-Exempt Status

Section 501(c)(3) of the federal Internal Revenue Code provides income tax exemptions for charitable, religious, and other groups. The IRS Web site contains valuable information for [charities seeking exempt status](#). This section will highlight just a few important considerations.

It is important to carefully consider the definitions of the purposes that 501(c)(3) recognizes as exempt: charitable, religious, educational, scientific, literary, public safety, amateur sports, prevention of cruelty, and special issues.

The IRS carefully examines Articles and bylaws so it is important that they are complete and accurately state the organization's exempt purpose. Although it is not required, the IRS will also look to see whether the organization has a conflict of interest policy that corresponds with the policy it recommends. (See Appendix A of the [IRS instructions](#) for a Sample Policy).

Section 501(c)(3) groups are classified one of two ways, as private foundations or public charities. Most nonprofit corporations represented by law school legal clinics will fall into the latter category, so private foundations are not discussed here.

Completing the Federal Tax-exempt Application

Nonprofits seeking exemption from federal income taxes must fill out IRS Form 1023. This [form](#), the [instructions](#), and [Publication 557](#) with more detailed information are available from the IRS website at no charge. The process is long, complex, and potentially costly. There also is a charge for filing—be sure to check with the IRS for the most current filing fees, which must be submitted with the application. (See [TAX DOCUMENTS: FORM 1023 USER FEES](#)) If possible, have the form reviewed by a tax attorney who specializes in nonprofit law before submitting it to the IRS.

Accepting Donations While Waiting for IRS Exempt Status: Fiscal Sponsors

The process of obtaining federal tax-exempt status can take quite some time, and many organizations want to start operating sooner. During this “waiting period” the nonprofit cannot receive tax-exempt donations, and any donations individuals make during this time cannot be deducted as charitable contributions on their tax returns. Therefore, the nonprofit may wish to explore using a “fiscal sponsor” to accept such donations. A fiscal sponsor is another entity that already has federal tax-exempt status, and which arranges to accept donations under its own name, then forward those donations to the nonexempt corporation. These fiscal sponsorship arrangements are extremely complex and if not set up carefully, can result in the “sponsor” losing its exempt status, the nonexempt corporation not receiving its exempt status, and donors not being able to claim a deduction on their tax returns. Thus, it is imperative that a lawyer with expertise in nonprofit law review any such agreement to ensure that the agreement contains provisions giving the sponsor organization a certain amount of control over funds that are passed through to the nonexempt charity. (See [OPERATIONS DOCUMENTS NONPROFIT: Fiscal Sponsor Agreement](#) for more information).

Expediting the Exemption Application

On occasion, the IRS will expedite applications. To have an [application expedited](#), a charitable organization must present a “compelling reason” which the IRS defines as follows:

- A pending grant, where failure to secure the grant will have an adverse impact on the organization's ability to continue operating.
- A newly created organization providing disaster relief to victims of emergencies.
- IRS errors have caused undue delays in issuing a determination letter.

If the client decides to make a request, that request must be in writing, signed by a principal officer, and explain fully the compelling reason, including the following: the name of the organization or individual grantor, the amount of the grant, the date the grant will be forfeited, and a description of the adverse

impact to the organization should the grant not be received. Usually, the IRS does not charge an additional amount for an expedited application, but that decision is solely within its discretion. (See [TAX DOCUMENTS: Expediting a 501\(c\)\(3\) Application](#) for more information).

State Tax Exemptions

Usually a nonprofit that receives federal exemption status will not need to file separate state exemption requests, as long as they comply with all state and local rules. However, check with your state's Department of Revenue to see if you need to formally request a state exempt organization tax number. (See [TAX DOCUMENTS: Request State Tax Number](#) for more information).

OPERATIONS - RUNNING THE BUSINESS

Clients must understand that running a nonprofit is the same as running a business, and often is more complex. Although it is not the lawyer's role to give accounting and payroll advice, the lawyer does need to advise the client that it is imperative to set up effective accounting, recordkeeping and payroll tax systems, and to seek appropriate professional financial advice. In addition, charitable organizations are subject to the same wage and hour, employment, and health and safety laws as for-profit entities, and can be exposed to the same liability as private corporations for violating state and federal law. Many organizations also will be required to apply for business licenses and comply with local and state regulations. For example, a daycare operation will have to comply with local and state laws governing day care; a homeless shelter offering food with food service regulations, etc. When discussing the structure of business operations, the following points should be discussed with the client:

Employees: Policies for Paid Staff and Volunteers

Organizations operate most effectively when the people running them have a clear understanding of their role, and what is expected of them. Personnel policies should be drafted before any staff are hired, and should apply to both paid and volunteer staff. In addition, best practices suggest that the duties and responsibilities of the Executive Director (if the Executive Director is to be a board member or officer) should be spelled out as well. Depending on the organizational structure, you may want to consider separate management-level personnel policies in a separate handbook. Most small nonprofits do not have labor unions, but if the clinic does represent a nonprofit with a union, it is imperative to enlist the help of a lawyer who is a specialist in labor law. Labor law is different from employment law, and there are very specific state and federal regulations relating to unions and an employer's responsibility with regard to workers organizing activity.

Any workplace policies always should be set forth in an employee handbook. It goes without saying that the handbook should be drafted or reviewed by an

employment lawyer, who can advise the organization with regard to myriad (and often confusingly overlapping) local, state, and federal employment issues. In addition, be aware that in some states, personnel policies or handbooks will be deemed to be a contract between employer and employee, and discrimination laws vary even by locality (e.g., municipal ordinances regarding disparate treatment related to sexual orientation). Each year, these policies should be reviewed by the board and updated as necessary. A [checklist for workplace policies](#) is an important tool to getting started. Some basics that the employer should consider inserting in its personnel policies include:

- Employee evaluation and disciplinary action up to termination;
- Job classifications and job descriptions (including paid and volunteer staff, as well as that of the Executive Director);
- Recruitment, hiring and non discrimination policies;
- Employment conditions, including workers compensation and safety procedures;
- Employee benefits, including leave policies (military, family, jury duty, etc.);
- Intellectual property development (if applicable) and nondisclosure requirements;
- Internet and email use policies, use of other workplace equipment;
- Complaint, grievance and whistleblower processes;
- Additional regulations relating to hours of work and overtime; outside or contract employment.

Clients should be advised to develop specific policies regarding volunteers that closely track the employee policies with regard to recruitment, hiring, screening, placement, supervision, and training. These policies are critical in protecting the organization and its volunteers from liability. You may also want to advise clients to consider using releases with volunteers, as well as obtaining liability insurance.

Wage and Hour Issues

Wage and hour issues (as well as payroll accounting and withholding problems) plague many small non-profits, who frequently run afoul of the law because they have a poor understanding of wage and hour law. Law school legal clinics should have a regularly updated database with the name and contact information for the state wage and hour regulatory agency, and all state and local statutes and regulations regulating wages and hours of work. In addition, most of these state agencies have a wealth of educational material, and provide on-site seminars and technical assistance personnel to help employers. It is important that the clinic have access to the agency's materials and assistance for its clients. All wage and hour policies should be reviewed carefully to ensure compliance with state and federal wage and hour law, and

compliance with statutory “tests” that apply for determining the status of employees. Clients should be discouraged from using “independent contractors,” unless a lawyer has reviewed the contract, as often the law will consider contractors to be employees, regardless of the understanding between the contractor and the nonprofit. Smaller nonprofit corporations may not be subject to federal wage and hour regulations under the Fair Labor Standards Act but they usually always are required to comply with state or local wage and hour and health and safety regulations. The [U.S. Department of Labor](#) has a wealth of information related to federal [wage and hour regulations](#), as well as links to state wage and hour offices.

Creating a Solid Financial Structure: Accounting, Recordkeeping, Audits, Budgets, Income, and Tax Returns

Not only are nonprofit corporations subject to specific and complex regulations regarding payroll and the use of funds, but unfortunately and increasingly, they are vulnerable to financial fraud committed by employees. Thus, it is critical that the nonprofit have a solid financial management structure in place that is reviewed regularly by the budget/finance/audit committee of the board, and is reviewed at least annually by the full board. It is not the lawyer’s role to give specific financial advice, so clients should be encouraged to contact financial experts who can, at a minimum, assist them with preparing: 1) an annual budget with a selected fiscal year that reflects a complete view of all income sources and expenses; 2) a financial policy containing explicit procedures that will protect against fraud and accounting errors; 3) select an appropriate accounting method; 4) establish a payroll system. Payroll issues are extremely complex, and unless the organization is large, or has an experienced payroll specialist on staff, an outside payroll company should be used.

Generating Income: Often exempt organizations do not understand that they are permitted to engage in revenue-generating activities that generate a profit, as long as such activities are substantially related to the purpose of the nonprofit. If, however, these activities have a tenuous relationship to that purpose, the nonprofit can incur substantial liability, and even jeopardize its exempt status. The IRS regulations related to tax liability for “unrelated business income” are extremely complex. Thus, if the clients insist on pursuing such an activity, it is imperative they consult with a CPA experienced in this area. Nonexempt organizations which do operate unrelated businesses must file a Form 990-T (Exempt Organization Business Income Tax Return). [Form 990-T and related instructions](#) are on the IRS Web site.

Investment Income: Any nonprofit that wishes to generate income through investments must not only obtain experienced financial advice before doing so, but must make sure it is authorized to do so in its bylaws. The board should have a committee charged with overseeing these investments, developing a strategy, and which performs regular review. The board may want to consider hiring an outside, independent investment advisor that also advises the board,

or go through an independent funds manager. To allay fears of any potential liability arising out of such activities, the board also may want to consider exploring purchasing D&O insurance.

Audits: Audits are essential to maintaining fiscal accountability and transparency, and it is important for the board to retain a reputable CPA firm to perform independent audits on a regularly scheduled basis. Frequently, organizations will have to provide the latest audits when submitting applications for funding. The board also of course should be advised to immediately consult a CPA if the organization receives an audit notice from the IRS or a state agency (such as a payroll audit by the Employment Division).

Fundraising

Several legal issues may arise in connection with fundraising that lawyers should be aware of. Some (but by no means all) important considerations are: 1) whether or not the activities will require a permit from the state agency that oversees charitable activities; 2) compliance with government regulations related to sending money overseas (especially the sending of money overseas since 9/11) (See [OPERATIONS DOCUMENTS NONPROFIT: Sending Funds Abroad](#) for more information); 3) Ensuring that contracts with fundraising firms or independent paid fundraisers contain provisions requiring that their activities comport with all applicable laws (See [BUSINESS CONTRACTS NONPROFIT: Film Production Contract](#), [Graphic Design Agreement](#), [Web site Development Agreement](#) for more information) and; 4) compliance with state and federal consumer and advertising regulations. Compliance with state and federal consumer or advertising laws is becoming an increasingly significant issue with the proliferation of Internet advertising. The National Association of State Charities Officials and the National Association of Attorneys General organized a "Uniform Registration Statement" (URS), which consolidates the requirements of all states' solicitation laws. More information can be found on the [MultiState Filer Project](#) Web site. In addition, clients should be advised that Internet advertising might be subject to the provisions of the federal CAN SPAM Act of 2003. The [Federal Trade Commission](#)'s Web site contains more information on this Act.

Political Activities and Advocacy

Organizations can lose their federal tax-exempt status if they engage in political activity, which is defined by the IRS as "directly or indirectly participating in, or intervening in, any political campaign on behalf of (or in opposition to) any candidate for elective public office." Such exempt organizations may engage in lobbying activities, however, subject to specific limitations. For any organization that intends to engage in any type of elections-related activity or legislative advocacy, it is very important to review the federal IRS regulations pertaining to such activities. There are specific tests related to lobbying activities, as well as rules regarding the types of political

activities that are permissible, such as voter education, candidate forums, and the like. See the [IRS](#) Web site for additional information.

Working with the Board of Directors - Establishing Standards for Good Governance

Although the Federal Sarbanes-Oxley Act does not apply directly to nonprofit corporations, they are subject to increasing scrutiny, most recently for excessive executive pay and lack of transparent fiscal management. Governance policies are critical to avoiding liability, and should be reviewed and updated by the board and legal counsel annually. Obviously, all such policies should be checked for consistency with the organization's bylaws and articles of incorporation. The Panel on the Nonprofit Sector, which was an independent group of exempt organization leaders, drafted "*Principles for Good Governance and Ethical Practice: A Guide for Charities and Foundations.*" This is a new set of principles of ethical conduct for organizations operating in the nonprofit sector, and is a result of the work of a broad cross-section of charities and foundations. Nonprofits can go to [Independent Sector.org](#) to sign on to the principles, and download a copy.

As noted above, it also is prudent to carefully review the Form 990 and its instructions when formulating board governance policy. This Form was changed substantially in 2007, and it now contains a section with numerous questions related to corporate governance. The IRS may pay particular attention to the answers to these questions, so it pays to take extra care in formulating corporate policies. The IRS Web site on [governance](#) can provide some basic information including the new 990 requirements. Idealist.org (www.idealist.org/if/i/en/faq/59-35/3-1) has excellent tips on board governance as well. (See [OPERATIONS DOCUMENTS NONPROFIT: Conflicts of Interest Policy](#) for more information). Some items to consider including in governance policies include:

1. Board member duties regarding financial management, and conflicts of interest;
2. Employee policies, including evaluation of management, grievance procedures, employee whistleblower procedures, and record retention;
3. Annual training for new and ongoing directors that includes elements of good corporate governance;
4. Procedures for regular evaluation of board effectiveness;
5. Process for regular review of all policies: governance policies, all procedures related to compliance with state and federal laws related to tax-exempt status, duties of board members, and fiscal operations.

Filling Out Tax Returns

In general, tax-exempt organizations must file tax returns they also are required to pay taxes such as Social Security, Medicare (FICA), and state

unemployment and payroll taxes. The Federal forms are Form 990 or 990 EZ and Form 990 Schedule A. There also may be some state tax returns and some county or local government property tax returns; check with your state taxing authority. Clients should be advised to download new forms each year from the IRS, as the forms are changed annually. The IRS keeps an updated Web site with information on the appropriate [forms and instructions with regard to the 990](#), as well as general [filing requirements](#) for nonprofits.

As is noted above, pay special attention to the Form 990 questions related to corporate governance. Since these questions are not only found in the Corporate Governance Section, but elsewhere in the Form 990, the Form should be reviewed as a whole, rather than just a section at a time. In addition, it is prudent to begin this review early each year so that any changes can be brought before the board before the return is filed. Penalties are assessed for each day the forms are filed late, so it is critical to make sure these are filled out, reviewed, and filed on time.

The IRS does not mandate a particular accounting method for charities, but the method selected must be the same each year. If the organization wishes to change accounting methods, it must obtain written permission from the IRS. Any organization wishing to change its accounting methods should consult first with an accountant, as there are a variety of tax rules that apply depending upon the method selected.

MERGER AND DISSOLUTION

Most law school clinics rarely take on the merger and acquisition or dissolution of nonprofits, as these are infrequent occurrences and also very complicated, so they will not be discussed in detail. Any law school clinic that wants to handle these types of matters should first check with the IRS, including reading the specific [publication](#) dealing with mergers and dissolutions, [TAX DOCUMENTS: Facts About Terminating Or Merging Your Exempt Organization](#), the [termination](#) of a nonexempt corporation, and [dissolution](#) under state law.

Merger

Mergers can include one nonprofit absorbing another, or two organizations merging to create a brand new organization. Regardless of the reason for the merger, these transactions are extremely complex, often involving several parties, including financial institutions. Thus, it is very important to review the particular state law related to them, and perhaps even consult with an attorney expert in these types of transactions. Often, there are restrictions placed upon the types of organizations that can merge, and additional conditions placed on those mergers. Mergers become even more complex when they are between organizations residing in different states, since there are potentially federal, state and local tax issues involved.

Any legal clinic undertaking a merger should work from a detailed checklist to ensure all necessary steps are completed. One important step is a detailed plan for merger, which should include at the very least specific goals and outcomes for the client, and which spells out specific tasks that must be performed, which party will be responsible for such tasks, and deadlines. Perhaps one of the most important parts of process is undertaking thorough and complete due diligence that at the very least reviews all operational aspects of the other entity or entities, including the financials. At some point, the parties will need to sign a memorandum of understanding which spells out each party's intent and responsibilities. Once the parties have completed due diligence and other tasks outlined in the memorandum of understanding, the organization must inform the IRS and usually must file the merger plan with the appropriate state agency.

Dissolution

A nonprofit corporation can be dissolved voluntarily or involuntarily for a variety of reasons. It is important that the practitioner be aware that board members of a dissolved corporation may be held personally liable for any number of issues if a nonprofit is dissolved inappropriately, including unpaid debts, unpaid payroll taxes, and unpaid wages or contracts. Therefore, before undertaking a dissolution, the attorney should set up a formal plan, and carefully review the following to ensure full compliance with each: Articles of Incorporation, bylaws, all relevant policy manuals, and federal, state, and local regulations relating to reporting and filing of taxes. Most importantly, if there are any remaining assets, those must be distributed for an exempt purpose as defined by the IRS, and the IRS must be notified of the dissolution.

OTHER LEGAL ISSUES

It is important to note that each of the sections above just touches upon major issues that should be considered when forming or representing a nonprofit corporation. The practitioner should take care to consult with local regulatory authorities, as well as practitioners experienced in this area of law to further explore the substance of these issues. There are numerous other specialized subjects that are beyond the scope of this particular section, including (but not limited to) formation and operation of other types of nonprofit entities such as membership corporations, religious corporations, trusts, civic and business leagues, co-operatives, and associations; the formation of other types of for-profit business organizations with nonprofit components, such as general partnerships, limited partnerships, and limited liability companies; intellectual property issues; employment laws; lobbying and political activity by tax-exempt organizations; funding and planned giving; tax issues; marketing and advertising; contracting with vendors and service providers; disbursement of funds (such as sending funds abroad); and publicly-supported organizations and fee-supported organizations.

"How To" guide current as of March 5, 2010.