


**Risk relating to
Governing Documents**

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October 3, 2007
2:00 – 3:00 pm EST


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(www.riskinstitute.org)



Key Considerations

- v Governing Documents lay the foundation for your organization's mission and direction – and legal status as a tax exempt organization
- v Exposures
 - What could go wrong? What's the big deal if the governing documents are outdated or inaccurate?
- v How to correct the situation
 - Let's look at what's needed to clean up the mess!


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Overview

- v What are "governing documents"?
- v What can go wrong?
- v What are the risks?
- v How can these documents be changed?
- v What other documents and governance policies are critical to keep updated and keep your nonprofit on track?
- v Strategies for getting your house in order!


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What are “Governing Documents?”

- v Document(s) used to recognize the organization under state law and to guide the organization’s conduct:
 - “Articles of Incorporation” or “Certificate of Incorporation”
 - “Corporate Charter” or “Articles of Association”
- v Bylaws:
 - Drafted upon formation, amended as needed


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Tax Exemption Documents


- v Certificate of Tax Exemption from the State
- v IRS Determination Letter
 - ♣ *All correspondence relating to application for tax exemption*
 - ♣ *Advance Ruling*
 - ♣ *Final Determination Letter*
- v Certificate of exemption for sales and use taxes

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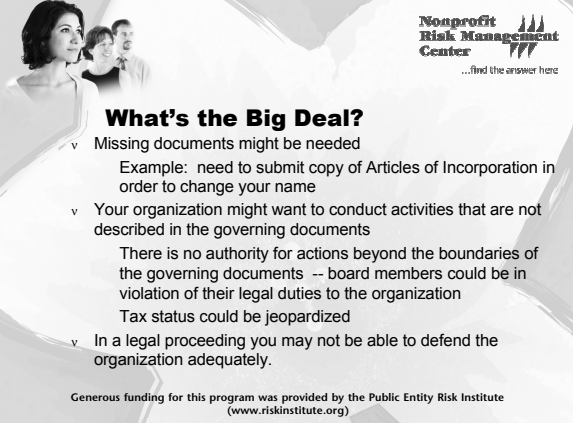


What can go wrong?

- v Lost or missing documents
 - How do you get new copies?
 - ♣ *Contact the State*
 - ♣ *Contact the IRS*
- v Outdated or inaccurate:
 - Organization is not acting the way the documents describe
 - You’ve moved or have a new name
 - ♣ *What do you do? Amend*



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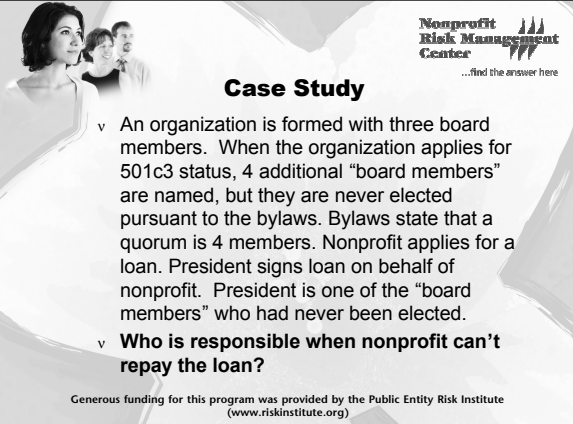


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What's the Big Deal?

- v Missing documents might be needed
Example: need to submit copy of Articles of Incorporation in order to change your name
- v Your organization might want to conduct activities that are not described in the governing documents
There is no authority for actions beyond the boundaries of the governing documents -- board members could be in violation of their legal duties to the organization
Tax status could be jeopardized
- v In a legal proceeding you may not be able to defend the organization adequately.

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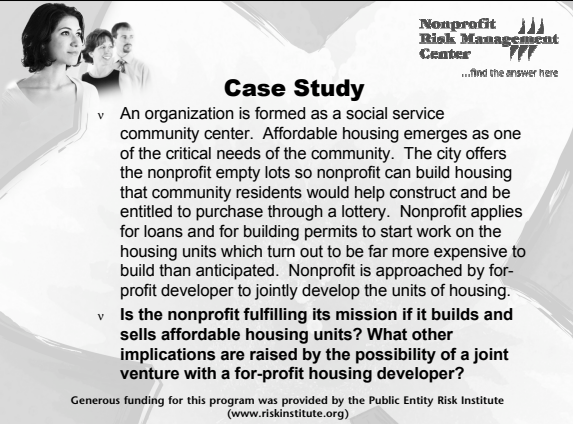


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Case Study

- v An organization is formed with three board members. When the organization applies for 501c3 status, 4 additional "board members" are named, but they are never elected pursuant to the bylaws. Bylaws state that a quorum is 4 members. Nonprofit applies for a loan. President signs loan on behalf of nonprofit. President is one of the "board members" who had never been elected.
- v **Who is responsible when nonprofit can't repay the loan?**

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Case Study

- v An organization is formed as a social service community center. Affordable housing emerges as one of the critical needs of the community. The city offers the nonprofit empty lots so nonprofit can build housing that community residents would help construct and be entitled to purchase through a lottery. Nonprofit applies for loans and for building permits to start work on the housing units which turn out to be far more expensive to build than anticipated. Nonprofit is approached by for-profit developer to jointly develop the units of housing.
- v **Is the nonprofit fulfilling its mission if it builds and sells affordable housing units? What other implications are raised by the possibility of a joint venture with a for-profit housing developer?**


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Understanding your exposures


- v If your organization is acting without authority from the state or outside the authority granted to it by the IRS, then the actions of the organization are vulnerable to legal challenge
- v In extreme cases:
 - Tax exempt status can be revoked.
 - The board of directors could be reconstituted by the state attorney general

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How do you Revise Governing Documents?

- v Some require a corporate resolution
- v Some just an amendment filed with the state and IRS
- v Involve the board through a task force
- v Engage a lawyer familiar with nonprofits to conduct a final review



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Amend the nonprofit's Articles of Incorporation

- v Be guided by legal counsel in your state or work closely with the state office that handles business registrations, such as the Secretary of State
- v Requirements:
 - Board approval of the changes
 - Filing fee
 - Generally file in triplicate or duplicate – always keep a copy and request a copy "as filed"

Send the IRS a copy of the amended articles


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Amend Your Bylaws

- v First look at existing bylaws – What are the procedures to amend them?
 - Certain number of votes? By whom? Does the nonprofit have members?
 - ♣ *What notice is required to be given?*
- v Convene a task force of board members
- v Ideally, have a lawyer review the desired changes
- v Send IRS a copy of the amended bylaws with next annual report (Form 990)


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Common Mistakes in Bylaw amendments:


- v No description of how long a board member may serve or how new board members are elected to the board.
- v Elimination of language pertaining to dissolution -- check and make sure the language is in the articles of incorporation, if it is not in the bylaws.
 - IRS requires governing documents to describe what happens to the nonprofit's assets upon dissolution.

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IRS Determination Letter – The Key to the Castle

- v Tells funders whether or not they can donate money to you
- v Permits the organization to be exempt from income taxes at state as well as federal level
- v Must be produced for public review when requested




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IRS Determination Letter (“D”L”)

- v Advance Ruling letter – expires after the first few years – so if that’s all you have, you need a:
- v “Final Ruling” letter
- v Correspondence in connection with application is considered part of DL
- v Should accurately reflect organization’s name and address – Check yours!


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IRS Requires Disclosure of changes to governing documents

Newly revised (proposed) IRS Form 990 asks in Part III whether the nonprofit has revised any of its governing documents in the past year, and if so, to “briefly describe the changes.”


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What other corporate documents are critical to keep up to date?

- v Minutes of board meetings
- v Annual report filed with the state should accurately reflect mailing address and officers, if applicable.
- v Spending policy / check signing authority
 - Any corporate resolution or policy that names an individual by name may be outdated as staff and board transitions occur


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What other corporate policies are key to good housekeeping?

- v Conflict of Interest policy -- disclosure questionnaire
- v Code of Conduct/Confidentiality/Code of Ethics for board and staff
- v Whistleblower Protection policy
- v Document Retention and Destruction policy
 - Newly revised IRS Form 990 asks whether a nonprofit has each of these policies


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Webinar Review

- v Governing documents are primarily the articles of incorporation, bylaws and documents that determine tax-exempt status.
 - They should be reviewed periodically, perhaps every 5-7 years, or more frequently if the nonprofit's activities change.
- v Serious pitfalls can derail a nonprofit that does not have up-to-date governing documents.
- v Governing policies can easily be changed, but it requires board involvement
- v Legal guidance can be helpful in smoothing the process

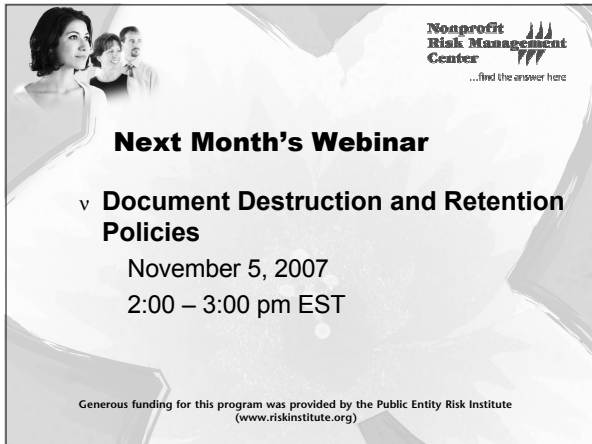
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Thank You!

Contact the Nonprofit Risk Management Center with questions: 202-785-3891
 Jennifer Chandler Hauge, Esq.
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Next Month's Webinar

v **Document Destruction and Retention Policies**

November 5, 2007
2:00 – 3:00 pm EST

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