



Mosherlaw Nonprofit Update

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Disaster Relief Guidelines

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conditions of distress. Following the September 11 terrorist attacks, charitable organizations may now provide broad-based monetary aid for victims' economic and psychological needs, such as aid to a surviving spouse with children, tuition assistance, and housing and transportation payment assistance. Financial aid must be based on objective criteria, demonstrating that the organization is accomplishing its charitable purposes in good faith and is avoiding any prohibited private benefit.

Record-keeping is very important. At a minimum, an organization's records should show that its disaster relief efforts further its charitable purposes and that it has made proper needs-based assessments. For short-term relief, records should show the type of assistance provided, criteria used, dates, places, and estimated numbers of victims assisted. Long-term aid should be documented in greater detail, including personal information about recipients, any relationships between recipients and organizational leaders or donors, and more information about the criteria and selection process for the aid given. Foreign assistance requires proof that recipients are not on a government terrorist list and that the charity maintains sufficient control over funds given to foreign organizations. Some or all of this information may be required on an organization's IRS Form 990 information return, including special schedules that may apply such as for foreign relief or financial aid.

Funds raised specifically for disaster relief should be segregated for accounting purposes, with documentation showing their proper use as intended. In addition, fundraising that involves sales of goods or service must satisfy applicable state sales tax and unrelated business income tax (UBIT) requirements. For example, a church that holds weekly car washes or sell baked goods to help raise relief funds may owe sales taxes and income tax on the money raised, notwithstanding the good cause involved. For more information on sales tax liability, please see our fourth quarter 2009 Mosherlaw newsletter, available at www.mosherlaw.com. Information on UBIT is available as well on our website under "Featured Articles."

For more information on charitable disaster relief, the IRS has a helpful guide available at www.irs.gov. Our firm's attorneys are also available to provide assistance with specific questions. ❖

Building Revenue Through For-Profit Subsidiaries



Does your organization operate a separate business, perhaps for fundraising purposes or to help provide services or goods to the community? For example, some nonprofits have started restaurants to spur community development and increase revenue. Others create media businesses to sell music, artwork, and other creative resources.

Fundraising can be daunting work. Many nonprofits turn to unrelated business activities to supplement traditional revenue from contributions and grants. This is particularly common when a nonprofit's board has members with business savvy and entrepreneurial skills. A for-profit subsidiary can provide an advantageous legal structure for nonprofits regularly conducting such unrelated business activities.

Federal tax law permits tax-exempt organizations to operate one or more for-profit subsidiaries. The tax-exempt parent can utilize most of the business forms available under state law to organize a for-profit subsidiary, such as a limited liability company. The decision to select

one particular legal form over another often hinges on the intended business operations and capitalization plan for the business.

Under the traditional corporate model, the exempt parent will own the equity in the for-profit subsidiary. The exempt parent also may enter into a joint venture arrangement with a for-profit business, within certain constraints beyond the scope of this article. The subsidiary engages in the unrelated business venture and pays federal and state income taxes on any gross profits. The after tax-profits are distributed to the exempt parent in the form of dividends or other passive investment income which, absent special circumstances, is tax-exempt income. The organization then can utilize this additional revenue stream to advance its exempt purposes.

While federal tax law permits an exempt organization to conduct an insubstantial level of unrelated business activity in-house, separating the business venture into a for-profit subsidiary is advantageous for several reasons. First, it protects the tax-exempt status of the nonprofit parent by ensuring that the organization continues to be primarily operated for exempt purposes. Second, it helps shield the nonprofit's assets from exposure to civil liabilities that may arise within the context of the for-profit business. Third, the for-profit subsidiary can be separately managed by a group of individuals that are exclusively devoted to the business, as opposed to the exempt organization's board managing both operations.

When forming and operating a for-profit subsidiary, the nonprofit board must be careful to ensure that charitable assets used to capitalize the business entity are not later used for impermissible private benefit. This is particularly a concern when the exempt organization is not the sole equity-holder in the for-profit entity. For additional information on the benefits of for-profit subsidiaries, please contact an attorney in our office. ❖

In the News



Our firm's attorneys have recently authored chapters in the Illinois Institute of Continuing Legal Education's publication on not-for-profit corporations, providing detailed legal guidance for practitioners. Michael Mosher and Ryan Oberly updated the extensive materials on organizing nonprofit corporations. Sally Wagenmaker wrote a new chapter on property and sales tax exemptions under Illinois law. Our aim is to help the legal community as well as to maintain the trusted legal expertise on which our clients rely.

Our firm's attorneys are also speaking and teaching throughout the Chicago area. Upcoming events and topics include free forums on employment, real estate, and risk management (sponsored by Partners for Sacred Places), Nonprofit Legal Hot Spots (American Camping Association's Mid-States Conference), Basic Legal Issues for Nonprofits (Harper College), Fundraising Rules, and Tax Reporting Responsibilities (both sponsored by CPAs for the Public Interest). For more information, visit our website at www.moshierlaw.com under "Speaking Engagements." ❖

NOTE: The articles in this newsletter contain legal and tax information of a general nature and may not be relied upon for making decisions concerning tax liabilities or legal issues. Consult your attorney or accountant for professional advice.

Who is a Minister?



Does your organization employ ministers or other religious workers? If so, do you know what tax rules apply to their employment? The Establishment and Free Exercise clauses in the First Amendment empower a religious organization to freely bestow the title of “minister” on any person it deems fit.

However, when it comes to granting the multitude of legal and tax benefits afforded to ministers, the government is not required to accept such designation.

For example, a federal court rejected a Texas seminary’s argument that four ordained employees working in the maintenance department qualified as ministers. This was despite testimonies that the individuals felt called to the positions. So if ordination alone is not enough, what does it take to qualify as a minister? Does an ordained church librarian qualify? What about a Jewish cantor, a youth pastor, or seminary professor?

Religious and other nonprofit organizations must be cognizant of the different requirements under various federal and state laws. Not surprisingly, federal and state laws do

not uniformly define the term “minister.” Thus, for example, the definition of a minister for religious visa purposes is different than most state laws governing the clergy-penitent privilege. Neither of these definitions conform to the federal tax law definition exempting ministers from income tax withholding and granting the parsonage and housing allowances. Failure to properly evaluate each employee’s qualifications could expose the religious organization and the employee to unexpected tax consequences, civil liabilities, and even criminal penalties.

For most federal income tax benefits, the IRS and courts use the following five factors to evaluate an individual’s qualifications as a minister. A “minister” is one who (1) is ordained, licensed, or commissioned; (2) administers sacraments; (3) conducts worship services; (4) performs services in the control, conduct, or maintenance of a religious organization under the authority of a religious denomination; and (5) is considered to be a spiritual leader by his or her religious body. With the exception of the first requirement, not every factor must be present in every case.

Simply because an individual qualifies as a minister for a given legal purpose does not necessarily mean that accepting the designation is the most advantageous option for the individual and/or the religious organization, particularly in regard to federal income taxes. Thus, religious organizations must carefully evaluate each situation. For additional information on federal or state laws affecting ministers, contact an attorney in our office. ❖

Form 990 Reporting Thresholds

Under the IRS’ reporting requirements, all section 501(c)(3) public charities must file a Form 990 information return. The filing requirement thresholds for the 2009 fiscal year are:

Form 990-N: Gross receipts < \$25,000

Form 990-EZ: Gross receipts < \$500,000, and total assets < \$1.25M

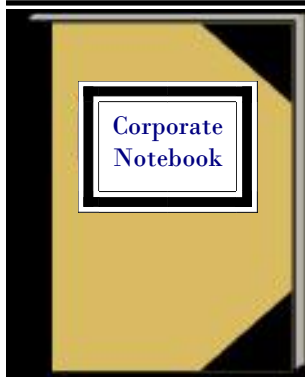
Form 990: Gross receipts > \$500,000, or total assets > \$1.25M

The Form 990 return is due on the fifteenth day of the fifth month after the end of an organization’s fiscal year. For organizations operating on a calendar fiscal year, the filing deadline is May 15. An automatic three-month extension is available if filed prior to the deadline. Late-file Form 990 returns are subject to substantial penalties, and failure to file 990s for three years may result in revocation of tax-exempt status. ❖

Political Activity Prohibition Continues

On January 21, 2010, the U.S. Supreme Court issued a critical free speech ruling in Citizens United v. Federal Election Commission. This decision invalidated federal legislation prohibiting the use of corporate funds for electioneering communications by certain nonprofit organizations *other than* section 501(c)(3) public charities. While significant, the ruling left untouched the federal prohibition on section 501(c)(3) organizations’ involvement in political campaign activities. Consequently, these organizations are still strictly prohibited from engaging in any activities designed to influence the election of political candidates for offices. Such activity may jeopardize a public charity’s tax-exempt status. ❖

Nonprofit Q & A



Q: What is a corporate notebook?

A: A corporate notebook is a repository of an organization's critical documents that are essential to its proper operation.

Q: Of what benefit is a corporate notebook?

A: Organizational leaders can rely on the notebook's information to determine whether their actions are legal and otherwise proper. In addition, the notebook can be used to help monitor deadlines for various filing requirements. The notebook can provide quick access to key information requested by the IRS, other government agencies, or donors. Organizations also can use the notebook as orientation material for new board members, to help them fulfill their fiduciary duty of care to be knowledgeable about the organization.

Q: What documents should be kept in a nonprofit corporate notebook?

A: A nonprofit organization's corporate notebook should contain the following types of documents: (1) organizational documents, such as articles of incorporation and all amendments and current bylaws; (2) tax-exemption documents, such as its IRS determination letter, FEIN information, Form 1023 application, and proof of sales tax exemption; (3) state registrations, such as annual reports filed with the Secretary of State, Department of Revenue registrations, attorney general charitable trust and solicitation registrations, and any assumed name registrations; (4) financials, such as the budget, audited financial statements, revenue/expense statements, and IRS Form 990's; (5) corporate policies such as whistleblower, investment, and document retention policies; (6) asset records such as a list of major assets, insurance policy information, and real estate tax exemption certificates; and (7) corporate records such as recent board minutes, important resolutions, annual conflict of interest disclosure statements, and a list of current directors and officers. In short, a notebook's documents reflect an organization's legal identity.

Q: How should a notebook be maintained?

A: The notebook should be kept by a key corporate officer, in a safe and relatively permanent location. Organizational leaders should be able to access it as needed. It should also be updated periodically.

About mosherlaw.com



Mosherlaw.com is designed to provide useful information for nonprofit organizations including general legal guidance, useful links to other resources, and access to our prior newsletters. Our "Featured Articles" section addresses topics affecting nonprofits including initial considerations for starting a new organization, tax issues such as exemptions and unrelated business income, foreign activities, directors' and officers' responsibilities, legal considerations for religious organizations, and real estate issues. Prior Mosherlaw newsletters are available in the "Archives" section. We hope that mosherlaw.com will be a useful tool for your organization. ❖

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