

# STARTING A NONPROFIT TOOLKIT



## **Starting a Nonprofit Toolkit**

Welcome to the Starting a Nonprofit Toolkit! This practical toolkit will provide you specific steps you need to start your own nonprofit organization as well as resources and links to help you during this process.

In developing this kit, I compiled resources and tips that I use consulting to many start-up nonprofits.

This toolkit will cover the steps to starting a nonprofit organization in any state including.

- 1. Fiscal Sponsorship**
- 2. Steps to Incorporation**
  - a. Create Business Plan
  - b. Draft Mission Statement
  - c. Recruit Board Members
  - d. Get a Lawyer
  - e. Draft Articles of Incorporation
  - f. Draft Bylaws
  - g. Apply for Business Name
  - h. Apply for Federal EIN#
  - i. File Incorporation with State
  - j. Apply for Federal Tax-Exempt Status
  - k. Apply for Right to Solicit Donations
- 3. Response from the IRS**
  - a. Advanced Ruling
  - b. Public Support Test

Following these steps and utilizing these resources will help you through a smooth incorporation process.

Sincerely,

Heather Carpenter  
M.M. Nonprofit Administration  
heathercarpenter@nonprofitalternatives.org  
<http://www.nonprofitalternatives.org>  
<http://www.nonprofitleadership601.blogspot.com>

Nonprofits are tax exempt under the 501c status of the Internal Revenue Service. There are two types of nonprofits that fall under the 501c3 status--Public Charities and Private Foundations. The majority of people who start their own nonprofit apply for 501c3 tax status which allows their nonprofit to receive tax deductible donations and not pay taxes. There are two options to start your own nonprofit organization. One option is try to find another 501c3 nonprofit to fiscally sponsor your organization or just take the steps to apply for 501c3 status.

## **1. Fiscal Sponsorship**

Fiscal Sponsorship is an option an organization can choose to follow before becoming an official 501c3 nonprofit. Fiscal sponsorship is good for individuals or groups in a hurry to begin operations and accept tax-deductible donations. However, many funding sources-foundation will not fund brand new groups.

Fiscal sponsorship usually involves a contractual agreement between a sponsoring organization and the organization being fiscally sponsored also known as the fiscal project. Fiscal Sponsorship gives the fiscal project's donors an opportunity to receive tax deductions for the donations that they provide for program support. In many cases the fiscal sponsor organization makes specific requirements for an organization to be fiscally sponsored. Some of these requirements involve the fiscal project to engage in strategic planning, fiscal reporting, and accountability activities. There are many ways an organization can be fiscally sponsored, for example one organization can be a project of another organization, or the fiscal project is separate entity with a Board of Directors. "Fiscal Sponsorship: 6 Ways To Do It Right," by Gregory L. Colvin, goes into more details about the different types of fiscal sponsorship.

It is helpful if new organizations that are looking for a fiscal sponsor do a little research before they jump into a fiscal sponsorship relationship. This really helps during the contract negotiation. Since the IRS is really particular about how fiscal sponsor relationships are set up there are a lot of rules about ownership of funds, for example in most cases the new organization doesn't have any control over the money that the donors give to the fiscal sponsor. So, it is challenging when new organizations add clauses in the contract to try to control their funds. It is helpful if new organizations not only learn about the benefits of being fiscally sponsored but also the limitations to being fiscally sponsored. However, once a new organization is fiscally sponsored they can generate donations and funds until they are ready to separate from their fiscal sponsor and apply for 501c3 nonprofit status.

The Foundation Center has a great fiscal sponsorship tutorial for anyone interested in learning more about fiscal sponsorship and the Community Resource Center in Colorado also has a great step-by-step explanation about fiscal sponsorship and the difference between the term "fiscal agent" and "fiscal sponsor." [www.Capaciteria.org](http://www.Capaciteria.org) provides a list of organizations that provide fiscal sponsorship.

## **2. Steps to Incorporation**

There are 10 specific steps to create an official 501c3 nonprofit organization. I will explain each of these steps briefly, however I highly recommend reading Nolo Press's book: "How to Form a Nonprofit Corporation" which describes each of these incorporation steps in great detail as well as provides sample forms and templates that nonprofits need for incorporation. Some of these documents and templates can also be found on the National Economic and Development Law Center's website, see Nonprofit Corporation and Formation: [http://www.nedlc.org/Publications/publications\\_legal.htm](http://www.nedlc.org/Publications/publications_legal.htm) as well as the IRS website.

The steps to incorporation.

### **a. Draft Business Plan**

A nonprofit is like any business and requires a good plan to get started. Sample plans can be found on the Small Business Administration's website <http://www.sba.gov>. A good plan includes these components:

- Mission statement
- Description of activities
- Marketing plan
- Need for your nonprofit in the community, evaluation of what is already out there.
- Board and Staff bios showing their capabilities to perform the duties of the nonprofit.
- 3 year budget including realistic income and expenses. Some of these expenses are:
  - Start-Up Costs
  - Pre-incorporation expenses
  - Incorporation & filing fees, board recruitment
  - Office, furniture, equipment, legal, accounting, marketing, logo, technology
  - Initial Operating costs
  - Recruitment & Training, insurance, postage, and utilities

### **b. Draft Mission Statement**

Your mission statement states what you do and why, short and to the point, convey passion. A mission statement is usually accompanied by a vision statement which shows where your organization wants to accomplish in the future.

### **c. Recruit Board Members**

You are required to have a minimum of 3 board members to start. Recruit people you can trust. It is important to be diverse in board member selection. While some board members may be able to give money, others may have expertise in an area that is needed. As an example, if an organization is recruiting 9 board members, it will want to recruit a lawyer, a teacher, an entrepreneur, two constituents (someone who benefits from the

organization's services), a local community leader, a businessperson, a member of the nonprofit community, and a psychologist. The board member resource center is: <http://www.boardsource.org>. Board source also provides affordable how-to guides for board members. The Council on Quality and Leadership also provides a free guide called, "Developing and Supporting a Board of Directors." <http://www.thecouncil.org>.

In some states the Board Chair and the Board Secretary cannot be the same person.

#### **d. Get a Lawyer**

It is not a requirement for nonprofits to use a lawyer during the incorporation process; however it is helpful to receive legal advice from the start. In some cities and states, start-up nonprofits can receive pro-bono legal advice from their local bar association or other legal services organization.

#### **e. Draft Articles of Incorporation**

- Must be a tax-exempt purpose
- No profits can benefit any individual
- Cannot be a political organization
- Upon dissolution, all assets must go to another tax-exempt organization of similar service

#### **f. Draft Bylaws**

The bylaws are a very important document for a new nonprofit. Nonprofits must follow what is stated in their organizational bylaws so it is important to work with trusted board members and advisors when creating the bylaws for your organization. The bylaws describe your organization's corporate rules, behaviors, and actions and include the following sections:

- Powers of the board
- Meetings information
- Directors (numbers, elections, tenure, vacancies, removal, quorum, compensation, voting)
- Officers
- Committees
- Operational Staff
- Fiscal Year
- Conflicts of Interest
- Amendments

#### **g. Apply for Business Name**

Applying for a business name is another important step in the incorporation process. Check on [www.Guidestar.org](http://www.Guidestar.org) to see if name isn't already being used by a nonprofit. Think twice about including Foundation in the name of your organization because many assume foundations already have endowed or existing funds. Names are approved on a state by state basis; however some nonprofits choose to also trademark their name to avoid potential future law

suites. Here are the requirements for applying for a name with the Secretary of State.

- Name must not already be used in the state
- Name availability search with Secretary of State
- Reserve name with Secretary of State

**h. Apply for Federal EIN#**

- National application SS-4 with IRS.
- This is a permanent identity for all government reports and documents.

**i. File Incorporation with State**

Nonprofit status requirements vary from state to state, however many states provide nonprofits with exemption from sales tax. In addition, each state's Attorney General and Secretary of State's website list nonprofit specific filing requirements. It is also helpful to consult a nonprofit attorney to find out the specific state filing requirements.

California requires nonprofits to fill out form 3500 Franchise Tax Exemption application. Additional documents required with this application are:

- Financial Statements/Budget
- Articles of incorporation
- Bylaws
- Supporting Documents including statement of activities

**j. Apply for Federal Tax-Exempt Status**

- Form 1023
- You will also need to include the minutes of first board meeting
- Most nonprofits can also apply for sales tax exemption; however this is not the case in the state of California.

**k. Apply for Right to Solicit Donations**

This is done with your state's Attorney General's office and is an annual filing requirement.

## **Response from the IRS**

Once you submit all your paperwork to the IRS it generally takes between 8-12 months to receive a response. While your application is pending, you may start receiving tax-deductible donations, however nonprofits be cautious because if their application is not approved then they are required to return the money from their donors.

## **Public Support Test**

In order to be considered a 501c3 public charity, nonprofits must prove they are a public charity by following a public support test. This means over a five year period more than 2/3rds of their funds must come from a variety of sources. Generally nonprofits that have been fiscally sponsored can pass the public support test, however new organizations that don't have very much funding or funding from just two sources may not be granted permanent 501c3 status. The public support test information is included in the 1023 IRS exemption application.

## **Advanced Ruling**

For those organizations that cannot pass the public support may be awarded an advance ruling period. This is a five-year period gives nonprofit an opportunity to get donations from a variety of sources. For more information about the advanced ruling period check out information on the IRS's website. Nonprofits should carefully track their funding during this advanced ruling period and work to receive donations from a variety of public sources.

<http://www.irs.gov/charities/charitable/article/0,,id=123155,00.html>

## **About the Author**

Heather has served as Operations Manager, Consultant, Speaker and Trainer to nonprofit organizations in California and Illinois for over 6 years. She earned her Masters of Management in Nonprofit Administration from North Park University in Chicago, Illinois. Heather is currently pursuing her PhD in Leadership at the University of San Diego. Heather is creator and author of the Nonprofit Management and Operations blog and was interviewed by the national women's blogging website —Blogger; quoted as being a, “Nonprofit Operations Guru.” Heather is currently blogging about Nonprofit Leadership at her Nonprofit Leadership 601 blog.

## **Disclaimer**

Heather is not getting paid by the particular companies or consultants to provide recommendations. The resources listed in the toolkit Heather has found helpful in starting a nonprofit organization. This information is provided strictly for educational purposes.

Many of these resources will be helpful to you and others may not be helpful. Feedback is always appreciated, so any suggestions or comments on how to make this toolkit more helpful to future clients would be much appreciated.

This document is Creative Commons Attribution-Noncommercial-Share Alike 2.5 License.

Are you are really passionate about an issue and thinking about starting your own nonprofit--but don't know where to begin? This toolkit provides a simple overview as well as practical resources for starting your own nonprofit organization. The toolkit is broken into three key areas that are important to know before starting any nonprofit organization. These areas include: fiscal sponsorship, key steps to 501c3 nonprofit incorporation, and handling responses from the IRS.

The toolkit also includes information about the IRS's Five-Year Advance Ruling Period and steps you can take during that period to insure your nonprofit's public charity status.

This practical information will help you through a smooth incorporation process.



Heather is passionate about your nonprofit's operations!! She has served as an Assistant Director, Operations Manager, Consultant, Speaker and Trainer to nonprofit organizations in California and Illinois for over 6 years. She earned her Masters of Management in Nonprofit Administration from North Park University in Chicago, Illinois and is currently pursuing her PhD in Leadership at the University of San Diego. Heather is creator and author of the Nonprofit Management and Operations blog and was interviewed by the national women's Blogging website—Blogger which quoted her as being a "Nonprofit Operations Guru." Heather currently blogs about Nonprofit Leadership at her Nonprofit Leadership 601 on Blogspot.com.

[www.nonprofitalternatives.org](http://www.nonprofitalternatives.org)  
<http://nonprofitleadership601.blogspot.com>