



Is NPO* the Way to Go?

*Not for Profit Organization

You are interested in starting a not for profit, but do you know what is required? Do you know if it is the best way to achieve your objectives? Do you know how to obtain income tax exemption? This brochure is intended to help you understand what is required to start a not for profit, both the business requirements and the legal requirements. Think about this information, research, and make informed decisions about accomplishing your dreams.

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What are the significant differences between a not for profit and a for profit business?

| <u>Not for Profit</u> | <u>For Profit</u> |
|---|---|
| Created for educational, charitable, religious, literary or scientific purposes | Created to make a profit; to be independent; to be your own boss |
| Generally a corporation or a trust | May be a sole proprietorship, a partnership, an LLC or a corporation |
| Operated and organized for an exempt purpose, as identified by the Internal Revenue Service (IRS) | Operated to make a profit |
| No one owns it, not even the founder; in addition, the Board of Directors, not the founder, is in control - founder does not make all the decisions | Owned by the individuals who start it; the owners control the business and may sell interests in the business to others |
| The Board of Directors hires the employees; directors should not be employees | The owners hire the employees and may be the employees |
| All income is used to support programs | Increases in income are returned to the owners or shareholders as dividends or invested in the business |
| Assets, cash, equipment or other property do not belong to the founder, directors, or staff | The owners own the assets |
| It is accountable to the public and the Attorney General; it must file annual reports with federal and state authorities and those reports are public documents | Privacy or proprietary information |
| Sources of revenue: donations, grants, earned revenue for services and products related to its exempt purpose, and borrowed funds | Sources of revenue: purchase of shares by investors, earned revenue from sales, services, borrowed funds |
| Does not pay taxes on its net related income | Pays taxes on its net income |



What are the legal steps:

| <u>A Not for Profit</u> | <u>A For Profit</u> |
|---|---|
| Incorporate as a not for profit; must have at least three directors | Choose business form, which may or may not include incorporation; draft necessary documentation |
| Obtain Federal Employer Identification Number | Obtain Federal Employer Identification Number |
| Draft and adopt Bylaws and Conflict of Interest Policy | Draft and adopt Bylaws or other organizing document depending on entity choice |
| Get business license | Get business license |
| Get State business tax ID number | Get State business tax ID number |
| Register with the Illinois Attorney General Charitable Trust Bureau | Begin your business operations |
| Submit application to the IRS for recognition of income tax exemption | |
| Obtain recognition of income tax exemption | |
| Begin your operations | |

Do not start a not for profit to:

- Have a paying job or address your own problems rather than a true public interest
- Do a short term project like paint a mural on a building, provide financial support to someone in need or solve a short term problem
- Hold a block party or provide financial support to a needy individual or family
- Do things your way and not deal with government bureaucracy or “a boss”
- Get large sums of money that you think funders are waiting to give you

Are still interested in starting a Not for Profit? Is a new organization necessary?

It's a great deal of work. If another organization already addresses the issue, think about working with that organization, and becoming a project or a program of the existing organization. It is a great way to find out if the project will get funded, if people need its services, if it is sustainable, and if you enjoy working in the nonprofit sector. Many times, new projects get started with a fiscal sponsor. A fiscal sponsor is an existing charitable organization that agrees to assist the project with different services, including fundraising under the existing organization name and tax exemption. There is more information about fiscal sponsorship at <http://www.thelawproject.org/wp-content/uploads/2010/06/TLP.FiscalSponsorshipFAQ-20071.pdf>.

If you still want to start a nonprofit, make sure you can distinguish your organization from other established organizations and keep reading...

What do you need to prepare for the IRS?

Tax exempt - 501(c)(3) Not for Profit organizations - must be organized and operated for an exempt purpose as established by the Internal Revenue Code. The IRS looks at the organization's legal documents (its Articles of Incorporation and bylaws) to verify that it is organized for an exempt purpose.

The IRS looks at the operations of the organization to see if it will be operated for an exempt purpose. The organization should have a clear and concise description of its operations and a thorough business plan developed before preparing any legal documents.

The organization can only address the legal matter of income tax exemption after its business plan and project ideas are fully developed.

How do you develop a clear and concise description of your operations - a business plan?

You need to think about what the organization will be doing, how it will function, and be able to explain it in detail.

The organization must be able to explain why its programs are needed. Find data to support the organization's position: Start researching the issues and defining what the organization will do in concrete terms. Read everything you can. Learn everything you can. Learn what others have tried. Learn what works and what doesn't. Talk to people who know about the subject; get other people's opinions. Learn how a nonprofit organization operates.

Consider the following questions, and keep in mind that your passion about the issue is not enough:

Issue: Is there an identifiable documented need, cause, issue, or problem the organization will address? If so, how will the program(s) work to reduce the problem?

Goal: What is the organization's goal? How will it accomplish its goal? What steps will be taken to achieve the goal?

Funding: What finances will be needed to get started? How much money will the organization need to stay in business? Will the organization charge for its services? How much? Is it a charge that those it hopes to serve will be able to afford? Are there funders providing money for your cause?

Who will help? Are there other people who support your cause, and who are willing to volunteer and commit their time to see the organization succeed? There must be at least three active participants on the board of directors and they should not be your family members or should not expect to be hired. Do not identify people to be on the board if they are not willing to work hard and commit their time to the organization as volunteers. Do you and the people on your board have the skills necessary to establish and run a not for profit, or do you have access to people who will work with the organization who have fundraising experience, accounting experience, administrative experience, or specific program expertise? The people on the board should not be the same people who work day-to-day for the organization as staff. The people who want to help need to understand their role as either employees or directors on the board.

When you are able to answer each of these questions and have research to support your answers, you need to develop a written business plan. The business plan should address the operations of the organization and include a projected budget for the first two years of the organization. When the organization has a thorough, well thought-out business plan, it is ready to proceed with the legal process of establishing a not for profit corporation and obtaining recognition of income tax exemption from the IRS.

TLP provides regular training for nonprofit start-ups through our [Emerging Nonprofit Certificate of Training](http://www.thelawproject.org/services/certificate/) boot camp. Check the upcoming training dates here: <http://www.thelawproject.org/services/certificate/>.

To learn more about TLP's services watch our video at http://www.illinoislegaladvocate.org/index.cfm?fuseaction=home.dsp_content&contentID=8360

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