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# Get By With a Little Legal Help For Your Friends

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Pro Bono Partnership



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# Pro Bono Partnership

- Free business legal services for nonprofit organizations through the services of our staff and corporate and private attorneys
- To be eligible, an organization must be:
  - Nonprofit and tax-exempt (or seeking (501(c)(3) status);
  - Providing services in New York, New Jersey, or Connecticut;
  - Engaging in activities that benefit the poor or disadvantaged or otherwise providing important social services, or arts, educational, or environmental programs;



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# Pro Bono Partnership cont'd.

- Providing programs or services with a demonstrable impact;
  - A group with genuine legal needs that the Partnership can address; and
  - Unable to pay for legal services without significant impairment of program resources.
- To apply to become a client, visit [www.probonopartner.org](http://www.probonopartner.org) and click on “Request Legal Assistance”



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# Available Assistance from PBP

Non-litigation business law matters, such as:

- Corporate governance issues: bylaw reviews, conflict of interest policies
- Employment / HR issues
- Business documents that require legal review or assistance with negotiations, such as forms, contracts or property leases
- Compliance with state and federal regulations re: fundraising



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# WHAT DOES IT MEAN TO BE A NONPROFIT 501(c)(3) ORGANIZATION?



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# Nomenclature

- Charitable organizations have two “classifications”
  - Nonprofit or not-for-profit (function of state law)
    - Formed for a non-pecuniary purpose (for the benefit of their members, for a public good, etc.)
    - Most often are incorporated
    - In New York, not-for-profit corporations governed by the Not-for-Profit Corporation Law
  - Tax exempt under Section 501(c)(3) of the Internal Revenue Code (function of federal law)
    - Organized and operated exclusively for purposes that are charitable, literary, educational, religious, scientific, etc.
    - Governed by Internal Revenue Code



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# How to Form a Not-for-Profit Corporation

- Articulate the mission of the organization
- Identify who will serve as the directors of the corporation (in New York, you must have at least three people over the age of 18)
- File a certificate of incorporation in the state where organization will be incorporated
  - Certificate sets out the charitable purposes for which the organization is formed; in New York, certain purposes require approval of state agencies
- Prepare basic corporate documents – bylaws, conflict of interest policy
- Hold organizational meeting to adopt documents, elect officers, conduct other business



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# How To Be Recognized as Tax-Exempt Under Internal Revenue Code §501(c)(3)

- Tax-exempt status requires formal recognition from IRS (with exceptions)
- Apply on Form 1023, which asks for:
  - Detailed description of organization’s planned activities, leaders, beneficiaries, fundraising plans
  - Multi-year budget
  - Copies of bylaws, certificate of incorporation, conflict of interest policy
- New Form 1023-EZ option for small nonprofits
- IRS issues “determination letter” recognizing organization’s tax-exempt status





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# How to Qualify for State & Local Tax Exemptions

- Apply separately for exemption from:
  - State franchise tax
  - Sales tax (both as consumer and vendor)
  - Local real property tax
- Applications are simpler to complete if organization has already obtained federal tax exemption



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# Should You Incorporate?

## **BENEFITS**

- Limited liability
- Facilitates tax exemption
- Facilitates conduct of activities (entering into contracts, purchasing insurance)
- Perpetual existence

## **OBLIGATIONS**

- State filings
- Federal filings
- Maintaining corporate records
- Observing corporate formalities
- Must recruit and retain people to carry out responsibilities
- Perpetual existence



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# 501(c)(3) Tax Exemption

- Organization can accept tax-deductible charitable donations
- Organization doesn't pay income taxes, and may be exempt from sales, property, and other state and local taxes
- Organization cannot have private benefit or inurement
- Organization must comply with registration and reporting requirements (annual Form 990)
- Restrictions on lobbying activities
- Absolute bar on political campaign activities



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# External Oversight of Tax-Exempt Organizations

- IRS
- State Attorney General
- Other state agencies (e.g., Department of State, Department of Taxation & Finance)
- Grantmakers
- Public
- Media



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# GOOD GOVERNANCE



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# Why Do Nonprofits Have Boards?

- To provide oversight
- To ensure that operations, program, staff, finances, internal controls, property, mission, strategic plans are all running smoothly
- To make certain that charitable resources are being used appropriately, in furtherance of the organization's mission
- To help raise financial support and awareness of the organization's work



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# Directors' Fiduciary Duties

- **Duty of Care:** Performing the director's functions with competence; being diligent and attentive; making sound and informed decisions
  - NY N-PCL §717(a): “Directors ... shall discharge the duties of their respective positions in good faith and with that degree of diligence, care and skill which ordinarily prudent men would exercise under similar circumstances in like positions.”
- **Duty of Loyalty:** Pursuing the interests of the organization above one's own; avoiding conflicts of interest; no self-dealing
- **Duty of Obedience:** Ensuring that the organization fulfills its stated purpose



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# Focus on Governance & Accountability

- State and federal regulators are increasingly concerned about governance practices in the nonprofit sector
  - Sarbanes-Oxley (2002)
  - Panel on the Nonprofit Sector (2005)
  - IRS releases new Form 990 (2008)
  - New York enacts Nonprofit Revitalization Act (2013)
- But what constitutes “good governance” will differ for each organization – policies should be tailored appropriately





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# NEW YORK NONPROFIT REVITALIZATION ACT OF 2013



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# Governance for the 21<sup>st</sup> Century

- Meeting notices, waivers of notice, and authorizations to act by unanimous written consent may all be sent via fax or e-mail
  - This applies to both members and directors
- A member may use e-mail to authorize another person to act as his/her proxy (remember, directors cannot appoint proxies)
- Unless restricted by the nonprofit's certificate of incorporation or bylaws, directors can participate in meetings via videoconference or conference call. Such participation qualifies as in-person presence at the meeting, allowing director to be counted toward quorum requirement.



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# Committees

- Act eliminates the designations “standing” and “special” committees
- Committees of the board:
  - Are made up only of directors
  - Must have at least three directors serving on them
  - Can act for and bind the board (with a handful of exceptions and within the confines of the resolution or charter establishing the committee)
  - Common examples: Executive Committee, Finance Committee, Audit Committee
- Committees of the corporation
  - May be established by the board or by members
  - Can include non-directors
  - Cannot act for or bind the board



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# Conflict of Interest Policy Required

- Every NY nonprofit corporation must have a written conflict of interest policy that complies with new statutory requirements
- Policy must:
  - Cover directors, officers, and key employees
    - “Key employee” means any employee able to exercise substantial influence over the nonprofit’s affairs, as defined in IRC §4958 (excess benefit rules)
  - Define the circumstances that constitute a conflict of interest
  - Set out procedures for disclosing a conflict of interest to the audit committee or board
  - Prohibit the person with the conflict of interest from being present at or participating in board or committee deliberations and/or vote regarding the matter that gives rise to the conflict
  - Prohibit the person with the conflict of interest from trying to improperly influence the deliberations or vote on the matter



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# Conflict of Interest Policy cont'd.

- Policy must (cont'd):
  - Require that the existence and resolution of the conflict be documented
  - Set out procedures for disclosing, addressing and documenting related party transactions
  - Require every director, prior to his/her election, and annually thereafter, to complete, sign and submit an annual disclosure identifying:
    - Any entity of which the director is an officer, director, trustee, member, owner, or employee and with which the nonprofit has a relationship
    - Any transaction in which the nonprofit is a participant and in which the director might have a conflict of interest



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# Conflict of Interest Policy cont'd.

- The secretary must provide a copy of all disclosure statements to the chair of the audit committee or board chair
- A nonprofit that has adopted a conflict of interest policy pursuant to federal, state or local law that is substantially consistent with these requirements will be deemed compliant.



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# Related Party Transactions

- What is a related party transaction (“RPT”)?
  - It’s a transaction or agreement involving the nonprofit (or one of its affiliates, if any) in which a related party has a financial interest
- Who is a related party?
  - The directors, officers, and key employees of the nonprofit (and its affiliates, if any) and their relatives
    - Relatives include an individual’s spouse; domestic partner; ancestors; siblings and their spouses, children and their spouses; grandchildren and their spouses; and great-grandchildren and their spouses.
  - Any entity in which one of the individuals described above has at least a 35% ownership interest (or, in the case of a partnership or professional corporation, an ownership interest of more than 5%)



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# Related Party Transactions cont'd.

- A nonprofit may not enter into a RPT unless the board determines the RPT is fair, reasonable and in the nonprofit's best interest.
- Any director, officer or key employee who has an interest in a RPT must disclose the material facts concerning such interest to the board or an authorized committee of the board prior to their deliberations and vote.
- No related party may participate in deliberations or voting regarding the RPT, but the board or committee may request that the person present background information or answer questions prior to the commencement of deliberations or voting.





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# Related Party Transactions cont'd.

- If the nonprofit is a charitable corporation (as defined in the Not-for-Profit Corporation Law) and the related party has a “substantial” financial interest, the board or authorized committee must also:
  - Consider alternative transactions to the extent available;
  - Approve the RPT by at least a majority vote of the directors or committee members present at the meeting; and
  - Document in writing the basis for the board or committee’s approval, including its consideration of the alternatives.
- The Attorney General may bring an action to enjoin, void or rescind any RPT or proposed RPT that is not reasonable or in the best interests of the nonprofit. He/she can also seek restitution, financial penalties, and/or the removal of directors and officers.



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# CHARITABLE REGISTRATION AND FUNDRAISING



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# NYS Charitable Registration & Reporting

- Approximately 39 states/jurisdictions (including New York) require charities to register if they are soliciting funds within that state
- Article 7-A of the Executive Law applies to charities that solicit contributions in NY
  - Must register prior to solicitation
  - Several exemptions from initial registration under Article 7-A, including an exemption for organizations that receive less than \$25K per year and do not use professional fundraisers or fundraising counsel
- Article 8-1.4 of the Estates, Powers and Trusts Law (EPTL) applies to charities that are incorporated, formed or conducting activity in NYS
  - There are also several exemptions from the EPTL registration requirement
  - Registered charities administering less than \$25K in the aggregate may seek exemption from filing, but must do so annually
- Dual Registrants are charities that are required to register under both 7-A and EPTL



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# NYS Charitable Registration and Reporting cont'd.

- Initial registration includes Form CHAR 410, filing fee (if applicable), and copies of the charity's certificate of incorporation, bylaws, Form 1023, and determination letter
  - Organizations claiming exemption from registration attach Schedule E
- Annual filings include Form CHAR 500, filing fee that is determined by charity's finances, and copies of financial documents (Form 990, reviewed or audited financial statements if required)
- Visit [www.charitiesnys.com](http://www.charitiesnys.com) for copies of all these forms and instructions



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# NYS Charitable Registration and Reporting cont'd.

- A nonprofit's annual revenue determines what type of financial information it must provide the Charities Bureau as part of its annual report
- Filing thresholds will be changing over the next several years:

Effective Date	Unreviewed Financials Required	Independent CPA Review Required	Independent Audit Required
July 1, 2014	Less than \$250K	\$250K - \$500K	More than \$500K
July 1, 2017	Less than \$250K	\$250K - \$750K	More than \$750K
July 1, 2021	Less than \$250K	\$250K - \$1 million	More than \$1 million



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# NYS Charitable Registration and Reporting cont'd.

- Article 7-A and Dual Registrants must include a statement on any written solicitations that a copy of the charity's most recent annual report may be obtained, upon request, from the charity or from the Office of the Attorney General, Charities Bureau, 120 Broadway, New York, New York 10271
- Charities Bureau maintains a searchable online registry of charities required to register in New York. See [www.charitiesnys.com](http://www.charitiesnys.com).



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# Documenting Cash Contributions

- To deduct a cash donation of any amount, a donor must have either his/her own bank record or a written statement from charity
- If the donation is \$250 or more, deduction requires that the donor obtain a written acknowledgement from the charity
- Charity must also provide a written disclosure if a donor contributed more than \$75 and received some goods or services from the charity in return (called “quid pro quo” contribution)
- For administrative ease and for good donor relations, most charities issue a written acknowledgment for cash gifts of any amount
- Acknowledgment can be sent in hard copy or electronically (e.g., an e-mail to the donor)



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# Documenting Cash Contributions cont'd.

Charity's acknowledgement should be contemporaneous and say:

- Name of charity
- Amount of contribution
- Date contribution was received
- A statement as to whether the charity gave the donor anything in exchange for the contribution
- A description and good faith estimate of the value of any goods or services provided by the charity in exchange for the contribution
- If a quid pro quo payment was more than \$75, a statement that the donor can deduct only the amount by which the contribution exceeds the value of any goods or services received (unless the donor received an item of insubstantial value – e.g., a coffee mug, a keychain)





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# Documenting Non-Cash Contributions

- Generally, the amount of a contribution of property is the fair market value of the property at the time of the contribution, and it is the donor's responsibility to estimate the fair market value of the property, not the charity's
- For property valued at less than \$250, to claim a deduction, a donor must have a receipt from the charity showing the charity's name, date and location of the contribution, and a reasonably detailed description of the property (unless obtaining such a receipt is impractical)
- For property valued at more than \$250, the charity must provide written acknowledgment to the donor and include a statement as to whether the donor received any goods or services in connection with the contribution



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# New York State Sales Tax: Exemption from Tax on Purchases Made By Organization

- To claim exemption from purchases made on behalf of an exempt organization, first file Form ST-119.2, *Application for an Exempt Organization Certificate*
- If organization is granted sales tax exemption, state will issue Form ST-119, *Sales Tax Exempt Organization Certificate* and Form ST-119.1, *Exempt Purchase Certificate*
- To make an exempt purchase, complete Form ST-119.1 and present the completed form to the store at the time of purchase. Payment must be made using cash or a check or debit / credit card in the organization's name – cannot use a personal check or personal debit / credit card to make tax-exempt purchases on behalf of the organization, even if purchaser will be reimbursed



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# New York State Sales Tax: Exemption from Tax on Book Sales

- As a starting point, organization must have been granted sales tax exemption by NYS and have received a Form ST-119, *Exempt Organization Certificate*
- “Retail sales of tangible personal property made by a shop or store” are subject to sales tax
- What is a “shop or store”?
  - Any place where goods are sold from display “with a degree of regularity, frequency, and continuity” and
  - Any place where sales are made through a temporary shop or store located on the same premises as persons required to collect sales tax
- To claim exemption from sales tax, the FOL will need to establish that books were not sold at a shop or store and that purchases could not be made on a regular basis by remote means (i.e., through the Internet)



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# New York State Sales Tax: Exemption from Tax on Book Sales

- Each FOL needs to analyze how it sells books in order to determine whether it needs to collect sales tax.
- Generally speaking, the more frequent your sales, the more likely it is you will need to collect sales tax. Few bright-line rules in this area, but we have some guidance from the Dept of Taxation and Finance:
  - FOL regularly operates a book sale in the library where patrons can purchase books during normal library hours = must collect sales tax
  - FOL operates a booth at a flea market where there are other vendors required to collect sales tax = must collect sales tax
  - FOL regularly sells used books through an online website = must collect sales tax
  - FOL operates a book sale one weekend each year = probably not required to collect sales tax
- Can request an opinion from NYS Dept. of Taxation and Finance by submitting Form AD-1.8 or calling (518) 485-2889



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# MANAGING VOLUNTEERS



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# Volunteers

- Individuals who volunteer or donate their services, usually on a part-time basis, for public service, religious or charitable purposes, without contemplation of pay
- Volunteers are not permitted in the for-profit sector



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# NY State Requirements

Volunteers cannot:

- Replace or augment paid staff or do the work of paid staff
- Do anything but tasks traditionally reserved for volunteers
- Be disciplined like an employee for seeking flexibility in hours
- Be required to perform duties involuntarily
- Be under contract to hire by any other business (express or implied)
- Be paid for their services (except expenses)



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# Best Practices: Position Descriptions

- Create position descriptions for each volunteer role
  - Key tasks
  - Relevant expectations (e.g., schedule)
  - Any educational requirements, special skills, licenses or other qualifications
  - Reporting relationship





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# Best Practices: Application and Screening

- Consider having an application form and an interview
- Evaluate your screening process
  - Screen the position, not the person, and follow the same screening process for all volunteers doing the same work
  - Identify the characteristics that will act as disqualifiers for the position



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# Application & Screening cont'd.

- General guideline: The more vulnerable the client(s), and the greater the opportunity for violations of trust, the more intensive the screening process should be
- Backgrounds checks – should you do them? What kind of checks (i.e., criminal, DMV, credit, others)? are relevant for each volunteer position? Who will pay for the checks?



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# Best Practices: Handbook and Orientation

- Consider having a volunteer handbook
  - Scope of responsibilities – what volunteers can and cannot / should not do
  - Safety policies, if any
  - Procedure for volunteers to report problems or concerns
  - Acknowledgment and waiver forms
- Have an orientation process



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# Best Practices: Supervision

- Who manages your volunteers?
- Consistently apply your organization's disciplinary procedures concerning volunteers – are volunteers subject to appropriate discipline, up to and including removal, for violations of your organization's policies?
- Address problems / concerns as they emerge!

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# Liability Concerns

- An organization may be liable if it puts a dangerous person in a position to harm others. Liability will depend partly on adequacy of organization's pre-retention investigation into volunteer's background and partly on organization's supervision. Did organization act reasonably?
  - What's reasonable? It depends:
    - Nature and responsibilities of the position
    - Severity of the potential risk of harm
    - Access to information – cost, delays
    - Resources of the organization
    - Adherence to organization's own policies
- Organization may also be vicariously liable for acts of volunteers performed within the scope of their service on behalf of the organization



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# Insurance

- Does your organization have adequate insurance and appropriate coverage? Some types of policies to consider:
  - General liability
  - Directors and officers liability (D & O )
  - Special events
  - Automobile insurance
  - Other policies as needed
- Check your policies – do they cover volunteers? Harm to a volunteer? Harm caused by a volunteer?
- Talk to an insurance professional

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# Other Resources

“Right from the Start – Guidelines for Non-For-Profit Board Members”

<http://www.charitiesnys.com/pdfs/Right%20From%20the%20Start%20Final.pdf>

“Internal Controls and Financial Accountability for Not-for-Profit Boards”

<http://www.charitiesnys.com/pdfs/Internal%20Controls%20-%20Final%20-%20Small%20Type.pdf>

IRS Stay Exempt: Tax Basics for Exempt Organizations:  
<http://www.stayexempt.irs.gov/>

Nonprofit Risk Management Center: <http://www.nonprofitrisk.org/>



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