Organization and Formation

Organization Mission Statement – A well-defined mission statement sets forth the organization’s purpose and cause and serves to provide the overriding theme of operations. The mission statement is also used by the IRS to determine eligibility for exempt status.

Articles of Incorporation – Must state that:
1. The organization is organized exclusively for its exempt purpose. Many well-intentioned organizations fail because they ignore the need to put necessary processes and controls in place to monitor regulatory, financial and legal requirements. Such processes may include policies around conflicts of interest, document retention and destruction, annual state filing requirements, whistleblower procedures, gift acceptance and investment policy, just to name a few. It is critical that these policies be documented, approved at the appropriate levels of management and the board of directors, and if applicable, be reviewed regularly and made available to employees and other stakeholders.

State of Iowa – All tax exempt entities must file organizational documents as required by state law.

Internal Revenue Service (IRS) – In order to be exempt from income tax, an entity must request to be classified as tax exempt from the IRS by filing Form 1023/1023-EZ (501(c)(3) organizations) or 1024 (all other organizations). A determination letter will be granted to those who are approved providing written assurance of the organization’s tax-exempt status.

501(c)(6) – Trade associations, chambers of commerce, real estate boards, and board of trade.

Chapter and Group Exemptions – If your organization is affiliated with a central organization, it may be recognized as a tax exempt entity under a group exemption. A local chapter of a national organization may be under an aggregate exemption, but still needs to file its own tax return if it is organized as a separate legal entity. Check with your national organization to determine if your organization must file a Form 1023 or 990.

Governance

Common Policies Needed – It is extremely important that the board of directors institute a solid governance structure to oversee the operations of the nonprofit entity. Many well-intentioned groups fail because they ignore the need to monitor regulatory, financial and legal requirements. Such processes may include policies around conflicts of interest, document retention and destruction, annual state filing requirements, whistleblower procedures, gift acceptance and investment policy, just to name a few. It is critical that these policies be documented, approved at the appropriate levels of management and the board of directors, and if applicable, be reviewed regularly and made available to employees and other stakeholders.

Board of Directors and Other Resources

Liability – Boards of directors and officers have a fiduciary responsibility to the organization and its constituents that they serve. They are personally responsible for their actions. As a result, each director and officer should clearly understand their role in the organization, and ensure they have adequate time and skills to carry out their role.

Diversity – Many nonprofits are formed because of a common mission or passion among a group of individuals. Oftentimes, this group of individuals come from similar backgrounds and/or has similar traits. Look to include people of diverse backgrounds and skill sets among the board of directors and officers to ensure a broader perspective as you move the organization forward.

Term Limits – Many organizations will limit the length of service by defining a specified period of service (term) and limiting the number of terms a board member or officer may serve.

Relationships of Members, Board and Officers – It is imperative that board members and officers place the interest of the organization before their own personal interest. Therefore, organizations should adopt a conflict of interest policy that will allow the organization to manage any conflicts that may exist or arise.

Professional Members – Many organizations find it beneficial to enlist the skills of professionals such as attorneys, accountants, engineers and business people to complement the skills of other board members. Consider calling local trade associations if you are having trouble locating a needed skill set.

Directors and Officers Insurance – Consider purchasing liability insurance to protect the directors and officers who serve the organization. The cost of the insurance is typically paid by the nonprofit organization.

Recordkeeping, Minutes – It is imperative that the financial and governance records accurately summarize the activity of the organization. As a result, financial records should be designed to facilitate the accurate reporting of revenues and expenses, the presentation of financial reports for internal and external purposes, and for preparation of federal and state tax returns. In addition, adequate safeguards should be in place to allow for the appropriate supervision and oversight of the preparation of financial records. The organization should also ensure that the activity of the board (and committees) is captured in minutes. Minutes should be prepared on a timely basis and approved by the board (or committee) at the following meeting. The minutes should contain sufficient detail to allow for the capture of all pertinent activity during the meeting, including those in attendance and the results of votes with respect to specific actions.

Financial and governance records should be retained in accordance with the organization’s document retention policy, which should be consistent with regulatory, legal and tax requirements.

Budgeting, Committees – All organizations must be financially viable to sustain their activities. To assist in the financial oversight process, many organizations have developed an annual budgeting process that will project anticipated revenues and expenses into the next year or longer. The budget should be approved by the board of directors and it is generally a prudent practice to review budget to actual amounts monthly. This budgeting process may be performed in conjunction with a board committee, such as a finance, audit or budget committee.

Operations

Filing Requirements – The following forms are applicable to the organization’s annual filing requirement with the IRS:

<table>
<thead>
<tr>
<th>Requirement</th>
<th>Form</th>
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</thead>
<tbody>
<tr>
<td>Gross receipts $200,000 or greater</td>
<td>990</td>
</tr>
<tr>
<td>OR assets greater than $500,000</td>
<td></td>
</tr>
<tr>
<td>Gross receipts between $50,000 - $199,999</td>
<td>990-EZ</td>
</tr>
<tr>
<td>Gross receipts normally less than $50,000</td>
<td>990-N</td>
</tr>
</tbody>
</table>

There is no State of Iowa filing requirements for Form 990, 990-EZ, or 990-N.

Unrelated Business Income Filing Requirement – If your organization receives more than $1,000 in gross income from sources unrelated to your tax exempt purpose, Form 990-T and Iowa Form 1120 are required to be filed and tax payments may be due.

The Nonprofit Organizations Committee of the Iowa Society of Certified Public Accountants (ISCPA) has developed these tips to provide organizations with basic information necessary to organize and maintain their tax exempt status, as well as continue to serve their communities in the years to come. Organizations should seek professional advice whenever forming any corporate venture.
Donor Receipts – A charitable organization must provide a written statement to donors of a quid pro quo contribution in excess of $75. Additionally, donors claiming a deduction of $250 or more are also required to obtain a written statement from the organization. The acknowledgement must provide the value of any goods or services received in exchange for the donation. See IRS Pub. 1771 for additional information.

Lobbying Expenditures – Public charities are subject to annual limits on the amount of lobbying expenditures. Exceeding those limits can cause your exempt status to be denied. Other exempt organizations may be subject to a proxy tax on lobbying expenditures or the deductibility of member dues may be limited.

Sales/Use and Other Taxes – Nonprofit entities are not automatically exempt from paying sales or use tax on goods and taxable services, and certain other taxes, even if they are exempt from state and federal income taxes. Sales and use tax must be paid unless some other general sales or use tax exemption applies.

Sales made by organizations engaged in educational, religious or charitable activities are exempt from collecting sales tax on proceeds expended for qualifying educational, religious or charitable purposes.

Gambling Activities and Sales Tax – Gambling receipts are subject to sales tax, regardless of the ultimate use of the proceeds. Exempt organizations that conduct games of skill or chance, raffles, bingo and other games are required to obtain a gambling license and sales tax permit.

To obtain a gambling license, refer to the “Social and Charitable Gambling” section of the Iowa Department of Inspections and Appeals website. To obtain a sales tax permit, complete the business tax registration form on the Iowa Department of Revenue website.

Employee vs. Independent Contractor – Organizations are responsible for determining if individuals providing services are employees or independent contractors. Exempt organizations must withhold income taxes, withhold and pay Social Security and Medicare taxes, and pay unemployment tax on wages paid to an employee. Exempt organizations generally do not have to withhold or pay any taxes on payments to independent contractors. An exempt organization can be held liable for employment taxes, plus interest and penalties, if a worker is incorrectly classified as an independent contractor.

Excess Benefit Transaction – An excess benefit transaction occurs when an economic benefit is provided by an exempt organization directly or indirectly to, or for the use of a disqualified person, and the value of the economic benefit provided by the organization exceeds the value of the consideration received by the organization. The definition of a disqualified person can be found in IRS Publication 557.

Compensation – Organizations must ensure that compensation paid to the executive director/CEO and other disqualified persons is reasonable and not excessive. Organizations should document the process of how compensation was determined.

Other Considerations and Resources

Iowa Biennial Report – Organizations must submit a report to the Iowa secretary of state no later than April 1 of each odd-numbered calendar year. There is no fee for filing a Nonprofit Corporation Biennial Report.

Out of State Solicitation – Organizations should contact the attorney general of each state in which it solicits donations before solicitation occurs. Additional registration and filing requirements may apply.

Automatic Revocation of Exempt Status – Any organization that fails to file Form 990, 990-EZ, or 990N for three consecutive years will automatically lose their tax exempt status. The IRS has reinstatement provisions available for organizations that lose their tax exempt status.

Recordkeeping – The statute of limitations for examination of a tax return is generally three years. In many instances, it may be significantly longer. The ISCPA Nonprofit Organizations Committee recommends tax returns be saved indefinitely. Consult your CPA to review your situation.

Helpful Website Links –

- Iowa Secretary of State: https://sos.iowa.gov
- Iowa Department of Inspections and Appeals: http://dia.iowa.gov
- Iowa Department of Revenue: https://tax.iowa.gov/iowa-tax-issues-nonprofit-entities
- Internal Revenue Service: www.irs.gov/Charities-Non-Profits
- Larned A. Waterman Iowa Nonprofit Resource Center: http://inrc.law.uiowa.edu/
- Guidestar: www.guidestar.org

Any advice contained in this communication (including any attachments or other accompanying materials) was not intended or written to be used, and cannot be used, by anyone for the purpose of avoiding any penalties that may be imposed by any governmental or taxing authority.

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