



Get Better at Doing Good: Best Practices

**Presented by:
Andrew J. Knutson
Gunderson, Palmer, Nelson & Ashmore, LLP
Rapid City, South Dakota**

Disclaimer

These seminar materials and Mr. Knutson's presentation are intended to provide the seminar participants with guidance as to best practices for nonprofit corporations. The materials and Mr. Knutson's comments do not constitute, and should not be treated as legal advice regarding the use of any particular technique or the tax consequences associated with any such technique. Although every effort has been made to assure the accuracy of these materials and comments at the seminar, Mr. Knutson and Gunderson, Palmer, Nelson & Ashmore, LLP do not assume responsibility for any individual's reliance on the written or oral information disseminated during or after the seminar. Each seminar participant should independently verify all statements made in the materials and at the seminar before applying them to a particular fact situation, and should independently determine both the tax and nontax consequences of using any particular technique before recommending that technique.

Finally, Mr. Knutson's jokes may be few, unfunny, and/or poorly timed.



What are we talking about?

- **Nonprofit Corporations**
 - Formed and governed under state law
 - Nonprofit corporations may seek tax-exemption under a broad range of IRC sections
- **Tax Exemption**
 - Regardless of federal tax status, nonprofit corporations are subject to the same SD state law
 - Passage of the New Act will not change your corporation's tax exemption



Old and New

- **The South Dakota Nonprofit Corporation Act - 1965**
 - SDCL chapters 47-22 through 47-28



- **South Dakota Model Nonprofit Act**
 - 2016
 - New Act as presently proposed, even if adopted, will still allow existing nonprofit corporations in South Dakota to stick with being governed by the Old Act



Best Practices

Mind your Manners

Manner of Acting

Ordinary Course

Special Circumstances

Avoid and Mitigate

What's Reasonable?



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Management and Control

- Management Responsibility – Oversight
 - Authority to Bind the Corporation
- Number – how many directors should you have?
 - Quorum – p.3
 - New Act
- Director Approval (II(C)(3))
- Mechanics of Acting
 - Notice (New Act): p.3
 - Technology
 - Committees
 - New Act: p.4



Designated Bodies

- New: Designated Bodies. What are they? p.4
- Who can be a member of a Designated Body?
- To the extent delegated, the Board (or the members) are relieved of responsibility and fiduciary duty as to the delegated powers.
- When would this be useful?
 - Can be perpetual
- Committee vs. Advisory Committee vs. Designated Body
- Beware: This is one spot that *could* have a tax exemption issue. Again, this is **not mandatory**. It's not about what the law allows you to do, it what you put in the corp. documents.
- Not relieved of oversight duties



Volunteer Protection

- P. 9-10, Appendix A
- **Federal Law**
- **State Law**
 - Who is protected?
 - What's compensation?
 - Protected Against What?
 - When am I not protected?
- **Transactions with Third Parties**
 - Use the full legal corporate name
 - Always disclose representative capacity
 - Internally and externally
 - Liability, indemnification



Volunteer Protection

- **Corporate Liability**
 - IRS Back taxes, penalties, negligent actions, vicarious liability...
- Board services is typically not covered by professional liability insurance



Liability Insurance

- **Errors and Omissions / Directors and Officers Policies**
 - Sometimes together, sometimes not
 - Purpose: insure the corporation and its agents against negligent acts or omissions committed by directors, officers, and/or employees.
 - Cover agent, corporation, or both?
- **Indemnification** (see II(H))
 - Mandatory (SDCL 47-22-65.2) and permissive. D&O, Emp, Members
 - What do your corporate documents say?
 - What about when the director or officer is not a party to the suit?
 - What about Advancements?
- **General Liability**
 - Protection against claims – it's a business
 - Continuance of organization
 - Adequately compensate those who suffered



Administrative Matters

- **Organizational Documents - State Law**
- **Minutes / Resolutions**
 - Separate Policy / Bylaws should address
 - Contemporaneous
- **Articles**
- **Bylaws**
 - When was the last time they were updated? Check up?
 - If significant revisions are made to the articles or bylaws, those changes are required to be listed in the next year's IRS Form 990
- Policies – part of the Bylaws or not.



Administrative Matters

- **State Filings**
 - Minimal annual report
- Unemployment Insurance
- Worker's Compensation Insurance
- **Policies - p.16**
 - Records – retention and destruction
 - Gift Acceptance
 - Fundraising policy
 - Executive compensation
 - Conflict of interest policy
 - Investment policy
 - Minutes / Resolutions
 - Whistle blower policy
 - Many, many more



Administrative Matters

- **Records**
 - Required
 - Recommended
 - Recommended Permanent
 - Recommended Temporary
 - IRS Compliance Guide, IRS suggested policies
- **What's your policy?** p.5, 17, Appendix
 - Who's responsible for carrying out the policy? (all policies)
 - Suspension of destruction: Audit, Gov't Investigation, Litigation
 - Electronic documents: backup, archive, system check ups...
 - Privacy laws
 - Emergency procedures
 - Document retention schedule



Administrative Matters

Gift Acceptance Policy

- **Who's the audience** (all policies)
 - Guidance for staff and donors. Manage expectations for nonstandard gifts.
- Cash and publically traded securities.
 - Generally accept, okay to ascribe value
- In-kind gifts are great (why?), but...
- **Certain gifts should not be automatically accepted, and a value should not be ascribed without consultation.**
 - Real property, personal property, life insurance, non-liquid securities, Sub-S Stock, retirement assets...
 - Contributions whose sources are not transparent or whose use is restricted in some manner, must be reviewed prior to acceptance due to the special obligations / liabilities.



Administrative Matters

- **Gift Acceptance Policy**
 - When the donor is encouraged to seek professional advice
 - Nonprofit will not provide such professional advice
 - Gift acceptance “committee”
 - What’s not acceptable?
 - Remember the audience



Administrative Matters

- **Gift Substantiation**
 - All donors should get a receipt, but required for \$250+
 - Appraisals.
 - Generally, if the value of the donated property exceeds \$5,000, the donor must get a qualified appraisal for contributions of property (other than money or publicly traded securities).
 - Large Gift = Consultation with donor's tax advisor
- **Gift Annuities and Deferred Gift Annuities**
 - Simple contracts between donor and charity.
 - SDCL 58-1-16
- **Fundraising**
 - Follow state and federal law
 - Website / Brochure
 - Most have a donate now feature, but what about all the options?



Administrative Matters

- How do you want to receive it?
 - Simple Will examples:
 - Specific bequest (not residuary): “I hereby make the following specific bequest: I give and bequeath the sum of Ten Thousand Dollars (\$10,000) to the Humane Society of the Black Hills, current Federal Employer Identification Number 46-0396967, for its general charitable purposes.”
- vs
- Specific bequest (not residuary): “I hereby make the following specific bequest: I give and bequeath the sum of Ten Thousand Dollars (\$10,000) to the Humane Society for its general charitable purposes.”



Administrative Matters

- **Executive Compensation**
 - No real requirements, but should be decided by knowledgeable persons who have no financial interest.
 - Rebuttable presumption test of IRC section 4958.
 - Dilbert.



Administrative Matters

- **Conflict of Interest Policy**
 - Not just for directors and officers.
 - Direct or indirect material personal interest in a transaction? Duty to disclose.
 - Procedures for determining when a conflict exists.
 - Course of action for when a conflict is identified.
 - Instructions to Form 1023 contains a sample policy.
- **State law: New Act.**
 - The New Act contains a section which outlines when a transaction or contract between the corporation and one or more of its directors, officers, or members may be voidable, and when it is not. See section 110 of the New Act.
 - Further, section 111 of the New Act provides a 'safe harbor' for a director to take advantage of a business opportunity that might otherwise have violated the director's duty of loyalty.
 - Essentially, the corporation can disclaim its interest in the opportunity by following certain procedures.



Administrative Matters

- **Investment policy**
 - **Addressing conflicting goals:**
 - (1) protecting (and growing) the investment,
 - (2) earning a reasonable interest rate, and
 - (3) maintaining access to the invested cash when needed.
 - **Hiring Professionals**
 - Reduce, if not nearly eliminate, liability by following prudent practices.
 - Don't delegate authority, delegate liability...
 - Investment committee members – authority and legal responsibility.
 - Investment Advisor – Advice, plan - wealth managers, financial advisors, trust officers, financial consultants, investment consultants, and financial planners.
 - Investment Manager – Who makes investment decisions, and selects the individual securities (stocks and bonds) to implement a specific investment direction.



Administrative Matters

- **Whistle blower / Anti-retaliation policy**
 - Federal law prohibits all corporations, including nonprofits, from retaliating against employees who “blow the whistle” on their employer’s financial management and accounting practices.
 - How will the corporation correct an identified problem?
 - Also various state laws against retaliation.
- **Ethics Policy**
 - What behavior to encourage / discourage



Accounting & Selecting an Accountant

- **Accounting**
 - Work with CPA to establish and observe customary accounting practices
 - Books / financials – what column?
- **Selecting an Accountant**
 - Education and Licenses
 - Experience
 - Independence
 - The Firm
 - Location
 - Personality
 - Proposal
 - How to request a proposal



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Audits!

- **Audits**
 - **State Law**
 - Not required
 - **Federal Law**
 - Required under certain circumstances.
 - Federal law generally requires a “Single Audit” of the corporation (greater than a regular independent audit) in any year that the nonprofit expended over \$750,000 of “federal funds”. (Threshold was \$500,000 through the year 2014)
- **Other Reasons to “audit”**
 - Prudent to have an audit, or smaller version of one, periodically.
 - Protects from liability
 - Discover waste, missing, or misinformation
 - May be required by bank, certain Grants, the members, or employee benefit plan.



Form 990

Return of Organization Exempt From Income Tax

- **2008**
 - Form 990, after 2008, became a good test to determine if your nonprofit has adopted and updated its policies, and whether your nonprofit is following what the IRS considers to be the best practices. IRS has provided guidance as to best practices for 501(c)(3) organizations.
- Does your Board look at the 990 annually?
- **Mission Statement**
 - 2 places in 990 to describe mission, and it's all public and easily accessible.
 - Have reviewed after 2008?
- **Establish a Narrative; 990 = Marketing**
 - No content or character limit



Directors and Officers

- **Individual Responsibilities**
 - Knowledge of Mission
 - Have you read the Mission Statement recently?
 - Focus of the corporation – Scope
 - Knowledge of the Bylaws
 - Have you read the Bylaws recently?
- **Fiduciary Duties**
 - What does “good faith” and “best interests” mean?
 - How does a reasonable person act?
 - Under the New Act, focus is on the manner of acting, not the correctness of decisions.



Directors and Officers

- Analyze
 - Information flow –sufficient information getting to the Board?
 - Info + examination + time
- Attend
- Review Bylaws
- Proper Notice
- Review Materials In Advance
- Read
- Question
- Investigate Rumors



Directors and Officers

- **Communicate** (more than one staff member)
- **Ensure Accuracy**
 - New Act – positions
- **Abide by Policies**
 - E.g., conflict of interest policy
- **Oversight**
- **Seek Advice and Rely on Experts**
 - New Act. This reliance on experts was also part of the Old Act. The New Act, however, expands and clarifies when a director or officer can rely on certain persons, not just experts. This is set forth in sections 87 (for directors) and 92 (for officers) of the not-yet-codified New Act.



Thank You

Please feel free to email me at:
aknutson@gpna.com, or
call 605-342-1078.



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