

What every nonprofit board member should know

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Tony Novak, CPA, MBA, MT
PO Box 333
Newport NJ 08345

856-237-9199

tony@SouthJersey.cpa
www.southjersey.cpa

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Foreword

This booklet was inspired by the hope that every nonprofit board regardless of their background could have access to the tools to fast track their journey to effective community leadership. The focus here is on simplest things: understanding core responsibilities, documents, financial statements, prevailing technology, and common terminology encountered when operating a nonprofit organization.

Introduction

Congratulations on being asked to join the Board of Directors of a nonprofit organization! Of course, you want to do a good job. You may have prior experience leading an organization or this might be a brand-new experience. Different nonprofit organizations have vastly different management cultures, organizational structures and procedures. This report is meant to outline some basic knowledge that is common to every nonprofit organization that should be helpful to new board members.

The onboarding process for new board members typically involves gaining an understanding of the legal and structural setup of the organization, its goals, public image and the duties and ethical responsibilities of a board member. It also involves gaining some practical skills in group leadership. Many individuals find that their experience as a nonprofit board member helps expand their self-vision of leadership potential in other areas of life including career and professional settings.



You are not running a child's lemonade stand. Your nonprofit has an important mission and performance expectations.

Getting started

Organizational reading list

The first thing that you likely want to do is read more about your nonprofit organization. Even if you think you already know your organization, now is the time to check your understanding by reading the actual organizational documents. The items you read will vary depending on the type of information and what documents are available, but this list may help to get started. As a practical matter, nonprofit organizations may wish to keep this information together in an online file folder that is assessable to board members.

- Articles of incorporation or association
- Organization's bylaws
- Any amendments to either the articles of incorporation or the bylaws

- Recent board meeting minutes
- A list of the current officers, directors, committees, and their chairpersons
- The IRS tax-exempt determination letter
- Latest tax return
- Most recent financial statements and accountant’s report
- State charities registration filing, if applicable
- Mission statement
- Organization’s web site
- Conflict of interest policies for board members
- Directors’ and officers’ liability insurance policy
- Insurance summary of the organization

If you are not familiar with some of these terms or the importance of the details within the documents, don’t worry about it at this point. The first step is just to read the documents that are available. Other sections of this report cover some topics in more detail and the Resources section gives links to more information.

Board meeting procedures

The second thing you may want to explore is the management style of the board meetings. Some organizations follow a more formal framework and others are more free form and casual. Most nonprofit board loosely follow a discussion format resembling “Roberts Rules of Order”, a short book written 140 years ago to help organizations and groups of people make decisions. The online version and a “cheat sheet” may be useful to new board members help become more familiar with board meeting procedures.

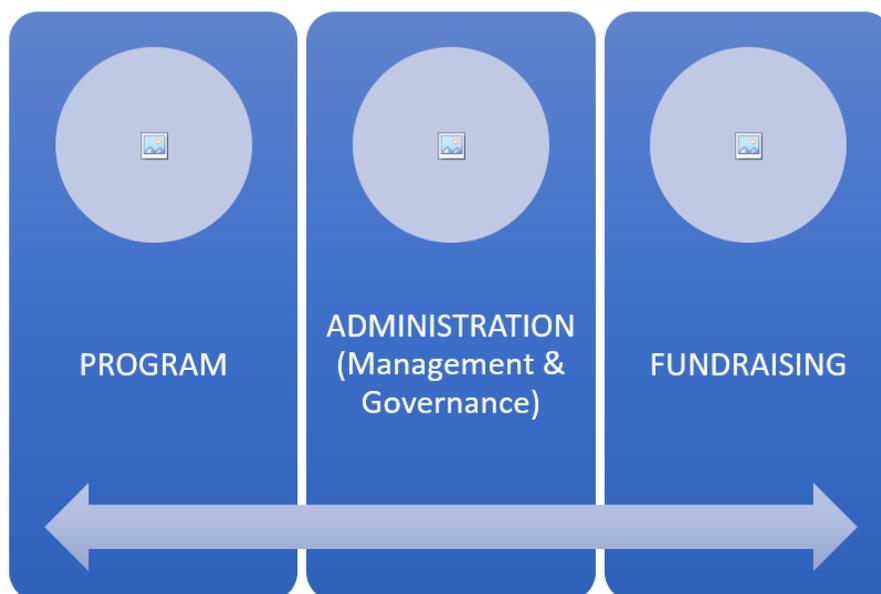


Illustration from Megan Genast Tarnow, The Mobius Group

Legal

Types of organizations

Some nonprofit organizations can be simple informal associations without any documentation, bank account or legal format. A good example is a neighborhood block party committee. Others can be formed as corporations or legally recognized entities licensed to do business or operate charities in various states with billions of dollars like The Nature Conservancy. A director should be familiar with the legal organization and documentation supporting those organizational choices. A common problem with nonprofit organizations is that the actual documentation as it exists does not support the legal format that the founders intended.

Nonprofit organizations can be organized as associations, partnerships, trusts or corporations. An individual's effort is typically not recognized as a nonprofit organization. Most states require at least two persons to organize an unincorporated nonprofit entity.

Tax-exempt status

Some nonprofit organizations are registered with federal government as a tax-exempt organization. These may be referred to by reference to the section of the federal tax code that permits their formation. For example, 501(c)(3) describes a charity while 503(c)(7) refers to a social club. Perhaps surprisingly, the motivation for obtaining tax exempt status is not to avoid taxes but to show their tax-exempt status as a qualification for some other purpose. For example, a nonprofit organization may need proof of its tax-exempt registration to be eligible for a grant program. The primary distinction between a tax-exempt nonprofit organization and other nonprofit organizations is the treatment of the assets at dissolution of the entity. Federal law requires the assets of tax-exempt nonprofits to be distributed in a manner that does not enrich the individuals running the organization or other privately owned entities.

State business registrations and ongoing filing requirements

Nonprofit organizations are typically subject to a number of state business registration and licensing requirements. One common request by small nonprofit organizations is a state sales tax exemption certificate. Understand that each of these must be addressed separately by your organization. For example, approval as a tax-exempt entity by IRS may not enable your organization to engage in any specific activity regulated by state law.

Liability

The individual board members may be responsible both individually and collectively for the actions of the non-profit organizations. Let's rephrase and repeat that important point: your action of joining a non-profit board even as a volunteer involves some personal financial risk. Some government agencies require the names

and addresses of all board members, presumably at least partly for this purpose of asserting liability. In some cases, at least anecdotally, government agencies imply individual liability for nonprofit entity obligations even when these may not legally exist. The most common types of liabilities:

- Payroll tax liabilities (for wages of workers of nonprofit organizations)
- Sales and use tax (for activities of a nonprofit organization)
- Registration fees
- Civil liability (for example, injury incurred at a nonprofit organization function)

Nonprofit organizations often protect their officers and directors from these types of liability exposure with insurance designed specifically for this purpose.

Ethics

The basic responsibility of a board member is to be a steward of the nonprofit organization. This is often described as a duty of care, duty of loyalty and duty of obedience. This means managing a balance of self-interests with those of the organization. Some believe that a board member must avoid conflicts of interests. This is not true. Conflicts of interest naturally occur in the normal operation of nonprofit organizations and so the focus should be on managing them, not avoiding them. A simple policy of disclosure and openness goes a long way to this end. Most nonprofit organizations have (or should undertake a project to develop) a written conflict of interest statement for board members.



This graphic on nonprofit governance comes from the National Council of Nonprofits

Finance and accounting

Financial structure

Nonprofit organizations can own financial assets, real estate, take out loans and engage in other transactions common in regular for-profit organizations. Generally, the signature of the Treasurer and at least one other officer is required to conduct larger financial transactions on behalf of the organization.

Accounting

Nonprofit organizations organize their bookkeeping differently than for-profit organizations. Accounting principles require that nonprofit organizations prepare their financial statements intended for public use differently from other types of organizations.

Beginning in years after 2017, nonprofit organizations will report assets under two categories: **Unrestricted** and **Restricted**. For earlier years the assets are reported in three categories: Unrestricted, Temporarily Restricted and Restricted. This format is intended to give the user of the financial report a more useful picture of the organization's finances. In smaller nonprofit organizations where all assets are unrestricted, there is no need to report both types of asset categories.

Foundations of the System

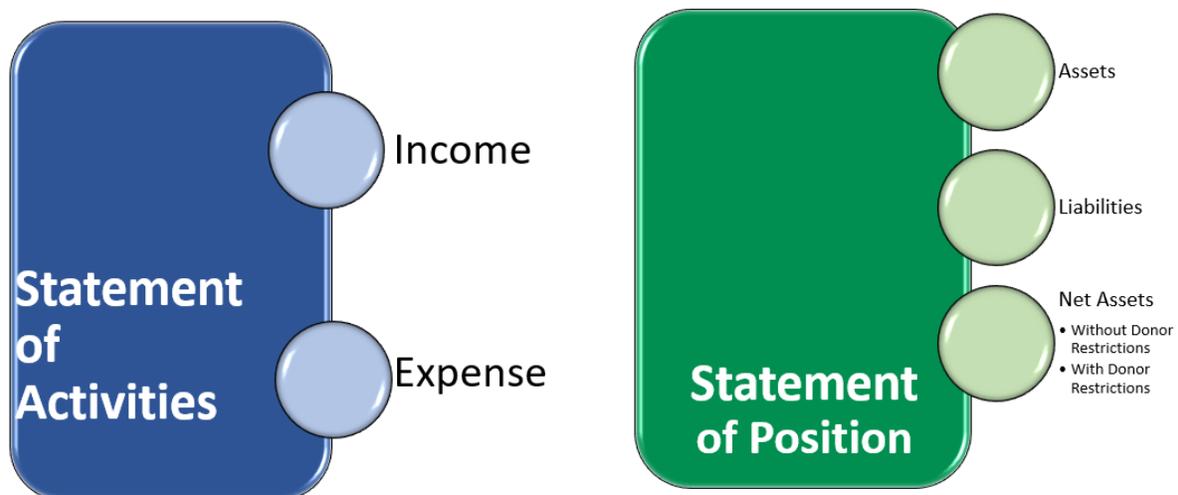


Illustration from Megan Genast Tarnow, The Mobius Group

Taxes and information filings

Nonprofit organizations are usually, but not always, exempt from paying income taxes resulting from ordinary operations. However, nonprofit organizations are subject to other types of taxes and government-imposed fees like payroll taxes, business registration and annual filing costs. In some rare cases the individual board members may be responsible for unpaid taxes of the organization. For that reason, many nonprofit organizations require an annual independent accountant's report.

Most tax-exempt organizations other than religious organizations submit an annual information filing with the Internal Revenue Service. This is called a **Form 990** or **Form 990PF**. Smaller nonprofit organizations file a Form 990N or Form 990 E-Z. The filing must be made online, not on paper. Unlike tax returns, these

documents are open to public inspection. The annual filing contains a summary of the organization's finances, its activities and the identities of its officers and board members.

The most common IRS problems are failure to file and informational return and late filing of informational returns. Either one can be costly or damaging to the nonprofit organization. Failure to file for three years triggers a revocation of the tax-free status.

The IRS provides free interactive online training to help officers, board members, and volunteers maintain your organization's tax-exempt status at StayExempt.irs.gov. The [Maintaining 501\(c\)\(3\) Tax-Exempt Status course](#) discusses what responsibilities your organization has and what activities can jeopardize your organization's 501(c)(3) status. The [Tax-Exempt Organization Workshop](#) provides additional information on the benefits, limitations and expectations of tax-exempt organizations.

State registered charities must file separate reports with their state of domicile. Those filings are not covered in this publication.

Financial reports

Nonprofit boards are typically presented with an informal financial statement from the organization's Treasurer when they meet. Some non-profit organizations have an independent accountant prepare or compile a periodic financial statement. Because nonprofit organizations handle their accounting differently than for-profit organizations, the financial statements presented to board members and other entities are likely to look different than the statements of other types of organizations. If you have any trouble understanding the statements of your organization, do not be shy about asking for further explanation.

Financial control procedures

Nonprofit organizations should adapt and follow procedures designed to ensure that cash and financial transactions are properly handled. The most basic of these involve procedures for handling cash and checks. The second most important is to have an independent confirmation that the bank's records agree with the financial records presented to the board. Nobody likes to think about the possibility of fraud in nonprofit organizations, but data shows that small nonprofit organizations are at high risk for mismanagement of finances.

Recordkeeping technology

The adaption of hosted accounting technologies helps nonprofit organizations disseminate information and control finances. The majority of nonprofit organizations that use computerized recordkeeping use QuickBooks accounting platform. This is not an endorsement of QuickBooks but rather just an acknowledgement that most nonprofit organizations use this software. The accounting program is used as a starting point or basic technology platform for many of the organization's other computerized activities. Hosted recordkeeping services allow the organization to specify the data that officers, board members staff and other stakeholders. The board may decide to make some information like annual financial statements, viewable by members or the public. Other data like employee records can be restricted or kept private on a "need to know" basis. A wide range of nonprofit management software ties into the accounting system to help bring operating efficiencies.

Almost every month new technologies emerge that have the potential to save time and money, improve internal controls, improve communication and make management and board members' tasks easier. Managing these technologies should be taken with the same care as other board responsibilities. Expect that more frequent reviews, pivots and updates will be required in the future as technology accelerates.

The Keys of Financial Management



Illustration from Megan Genast Tarnow, The Mobius Group

Environmental, Social and Governance

Monitoring an organization's effectiveness in attaining stated core strategic objectives in environmental, social and governance principles has become a major focus of activist nonprofit boards in recent years. While many organizations formally adopt or at least informally embrace these concepts, fewer have active programs for measurement and accountability. As a nonprofit director, you can expect to face an increasing number of these issues over time both from within and from outside your organization.

State considerations

This booklet is meant for broad general purposes and does not address state-specific issues of managing a nonprofit organization. Most of the government requirements for the operation of a nonprofit organization are set at the state level. That means that this booklet omits much important operational information. Please

consider that nonprofit boards, especially for charities, may be required to obtain additional knowledge about state-specific issues and requirements.

Resources

990 Finder <http://foundationcenter.org/find-funding/990-finder>

Guidestar.org

[Maintaining 501\(c\)\(3\) Tax-Exempt Status course](#)

[The Tax-Exempt Organization](#)

National Council of Nonprofits <https://www.councilofnonprofits.org/>

Roberts Rules of Order, online version <http://www.rulesonline.com/>

Ten Basic Responsibilities of Nonprofit Boards (Print), by Richard T. Ingram

Types of tax-exempt organizations <https://www.irs.gov/charities-non-profits/types-of-tax-exempt-organizations>

About the author

Tony Novak CPA, MBA, MT lives in rural southern New Jersey and serves small businesses and nonprofit organizations in the Philadelphia / Delaware Valley region including religious organizations, community associations, funding organizations, trade associations and environmental organizations. He welcomes opportunities for speaking engagements or webinars focused on raising the performance of non-profit leaders. He can be reached through the contact information posted at SouthJersey.CPA.