Product Details

Form a California nonprofit corporation

Tens of thousands of arts groups, educators, social service agencies, environmental groups, and others have used this bestselling book to form their California nonprofit. Your group can, too.

Obtaining 501(c)(3) tax-exempt status is a lot easier now with the IRS Form 1023-EZ streamlined application. Use this book to form your California nonprofit corporation and obtain your federal and state tax exemptions. We provide step-by-step instructions for both the longer IRS Form 1023 and the streamlined IRS Form 1023-EZ application.

How to Form a Nonprofit Corporation in California shows you how to:

choose a name and structure

prepare and file articles of incorporation

qualify as a 501(c)(3) public charity

obtain federal and California state tax-exempt status

create bylaws

set up a corporate records book

prepare minutes of your first board meeting, and

handle post-incorporation filings and tasks.

This new 17th edition is completely updated to cover changes to the law.

Check out Nolo's list of California products. Not a California resident? Use How to Form a Nonprofit Corporation .

IRS, FTB, and AG Forms and Publications

Name Availability Inquiry Letter

Name Reservation Request Form

California Submission of Exemption Request (Form 3500A)

FTB Notice 2008-3: AB 897—Implementation-Issuance of Exempt Acknowledgment Letter

IRS Form 1023: Application for Recognition of Exemption (6/2006)

Instructions for IRS Form 1023

Form SS-4: Application for Employer Identification Number

Instructions for Form SS-4

Form 5768: Election/Revocation of Election by an Eligible Section 501(c)(3) Organization To Make Expenditures To Influence Legislation

Publication 557: Tax-Exempt Status for Your Organization

Publication 4220: Applying for 501(c)(3) Tax-Exempt Status

Publication 4221-PC: Compliance Guide for 501(c)(3) Public Charities

Publication 4221-PF: Compliance Guide for 501(c)(3) Private Foundations

Publication 1828: Tax Guide for Churches and Religious Organizations

IRS Revenue Procedure 75-50

IRC Section 4958: Taxes on Excess Benefit Transactions

IRS Regulations Section 53.4958-0, Table of Contents

Registration/Renewal Fee Report to Attorney General of California (Form RRF-1) (3/2005)

Instructions for Filing Form RRF-1 (3/2005)

California Attorney General’s Guide for Charities (2005)

Guide to Charitable Solicitation (1999)

Assessors’ Handbook, Section 267: “Welfare, Church, and Religious Exemptions”

IRS and Tax Articles

Public Charity or Private Foundation Status Issues under IRC §§ 509(a)(1)−(4), 4942(j)(3), and 507 Disclosure, FOIA and the Privacy Act

Update: The Final Regulations on the Disclosure Requirements for Annual Information ¬Returns and Applications for Exemption

Education, Propaganda, and the Methodology Test

Election Year Issues

Lobbying Issues

Private School Update

UBIT: Current Developments

Intermediate Sanctions (IRC 4958) Update

IRS Revenue Ruling 2007-41: Political Campaign Prohibition Guidance

Internal Revenue Bulletin (IRB 2008-18) with T.D. 9390 Final Regulation changes to Section 4958 regulations

Information and Tear-Out Forms

(\* Asterisks indicate forms available only as Tear-Out in the book—see Appendix A and B.)

California Secretary of State Contact Information

\* Incorporation Checklist

Special Nonprofit Tax-Exempt Organizations

\*Name Availability Inquiry Letter

\*Name Reservation Request Form

\*California Form 3500A, Submission of Exemption Request

\*IRS Package 1023: Application for Recognition of Exemption

\*IRS Form SS-4: Application for Employer Identification Number

\*IRS Form 5768: Election/Revocation of Election by an Eligible Section 501(c)(3) Organization To Make Expenditures To Influence Legislation

Member Register

\*Membership Certificates

About the Author

Anthony Mancuso

Attorney

Anthony Mancuso is a corporations and limited liability company expert, currently working at Google. He graduated from Hastings College of Law in San Francisco, is a member of the California State Bar, writes books and software in the fields of corporate and LLC law, and studied advanced business taxation at Golden Gate University in San Francisco. He is the author of several Nolo books on forming and operating corporations (both profit and nonprofit) and limited liability companies. His titles include Incorporate Your Business, How to Form a Nonprofit Corporation (national and California editions), Form Your Own Limited Liability Company, The Corporate Records Handbook, and LLC or Corporation? His books have shown over 500,000 businesses and organizations how to form a corporation or LLC. He also is a licensed helicopter pilot and a guitarist.

Table of Contents

Table of Contents

 Your Legal Companion for Forming a Nonprofit

Corporation in California

1. Is Nonprofit Incorporation Right for You?

Is Your Group a Nonprofit That Can Use This Book?

Benefits of the Nonprofit Corporation

The Disadvantages of Going Nonprofit

How Nonprofits Raise, Spend, and Make Money

Your Path to Nonprofit Status

Incorporating in Another State—Don’t Fall for It

2. Legal Rights and Duties of Incorporators, Directors,

Officers, Employees, and Members

Incorporators and Their Role as Promoters

Directors

Officers

Employees

Membership Nonprofits

3. Requirements for Section 501(c)(3) Tax Exemption

Section 501(c)(3) Organizational Test

Valid Purposes Under Section 501(c)(3)

Other Requirements for 501(c)(3) Groups

Information for Specific Questions About Your Group’s Activities

4. Public Charities and Private Foundations

The Importance of Public Charity Status

How to Qualify for Public Charity Status

Private Foundations

5. Other Tax Benefits and Requirements

Federal and State Tax Deductions for Contributions

Federal Estate and Gift Tax Exemptions

Federal Unrelated Business Income Tax

California Unrelated Business Income Tax

California Nonprofit Tax Exemption

California Attorney General Reporting Requirements

California Welfare Exemption

Other California Tax Exemptions

State Solicitation Laws and Requirements

6. Choose a Name and File Your Articles of Incorporation

Choose a Corporate Name

Practical Suggestions for Selecting a Name

Check Name Availability

Reserve Your Corporate Name

Perform Your Own Name Search

Prepare Articles of Incorporation

File Your Articles

Appoint Initial Corporate Directors

7. Bylaws

Choose a Membership or Nonmembership Structure

Bylaws for a Public Benefit Corporation

Membership Bylaw Provisions for a Public Benefit Corporation

Bylaws for a Religious Corporation

Membership Bylaw Provisions for a Religious Corporation

8. Apply for Your Federal 501(c)(3) Tax Exemption

Getting Started

Ways to Complete the Tax Exemption application

Preliminary Reeding

Adding Attachment Pages

Public Inspection Rights

Do You Need to File Form 1023?

Prepare Your Tax Exemption Application

Filling Out the Schedules

Assemble and Mail Your Application to the IRS

What to Expect From the IRS

The Federal Determination Letter

9. Final Steps in Organizing Your Nonprofit

Obtain Your State Tax Exemption

Set Up a Corporate Records Book

Prepare Offer to Transfer Assets From an Existing Business or Organization to Your Nonprofit

Prepare Minutes of Your First Board of Directors’ Meeting

Complying With the Bulk Sales Law

Prepare a Bill of Sale for Assets

Prepare Assignments of Leases and Deeds

File Final Papers for the Prior Organization

Notify Others of Your Incorporation

Apply for a Mailing Permit

Apply for Your Property Tax Exemption

File a Domestic Corporation Statement

File an Initial Report With the Attorney General

Issue Membership Certificates

File Your Articles With the County Recorder

Register With the Fair Political Practices Commission

10. After Your Corporation Is Organized

Piercing the Corporate Veil—If You Want to Be Treated Like a Corporation, It’s Best to Act Like One

Federal Corporate Tax Returns

California Corporate Tax Returns and Reports

Federal and State Corporate Employment Taxes

Sales Tax Forms and Exemption From Sales Tax

Licenses and Permits

Workers’ Compensation

Private Insurance Coverage

Dissolving a Nonprofit Corporation

11. Lawyers, Legal Research, and Accountants

Lawyers

Legal Research

Accountants and Tax Advice

Appendixes

A. Using the Downloadable Forms and Other Online Material

Editing RTFs

List of Corporate, IRS, and other Forms and Publications on the Nolo website

B. Forms

Incorporation Checklist

Special Nonprofit Tax-Exempt Organizations

Articles of Incorporation of a Nonprofit Public Benefit Corporation with Mail Submission Cover Sheet

Articles of Incorporation of a Nonprofit Religious Corporatoin with Mail Submission Cover Sheet

Name Availability Inquiry Letter

Name Reservation Request Form

California Form 3500A, Submission of Exemption Request

IRS Form 1023-EZ: Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code

IRS Package 1023: Application for Recognition of Exemption (With Notice 1382)

Member Register

Membership Certificate

Index

Sample Chapter

Chapter 1

Is Nonprofit Incorporation Right for You?

Deciding to form a nonprofit corporation will be a big step for you and the members of your group. It will involve more paperwork and government forms, on both the state and federal level, than anyone will like; and you’ll have to conduct your business within the legal framework of various state and federal laws. Fortunately, there are big payoffs to all this work and attention, including the ability to attract donors and grant funds, obtain real and personal property tax exemptions and special nonprofit mailing rates, avoid corporate income taxes, and shield officers and directors from legal liability. Before starting down the path of nonprofit incorporation, however, you’ll want to learn a little more about who can form a nonprofit and the consequences of doing so. In this chapter, we’ll explain:

• the kinds of groups that can—and can’t—form a nonprofit using this book

• the benefits you’ll enjoy as a nonprofit—and some of the disadvantages to choosing this route

• how nonprofits can raise start-up funds and earn money, should they wish to do so

• the process you’ll go through (following the instructions in this book) to incorporate and obtain your tax-exempt status, and

• for those considering incorporating in another state, considerations to bear in mind before doing so.

Is Your Group a Nonprofit That Can Use This Book?

A for-profit corporation can be formed for any lawful purpose. Nonprofit corporations, however, must be established under California law for one of three broad purposes: (1) for the benefit of the public (a public benefit corporation), (2) for religious purposes (a religious corporation), or (3) for the mutual benefit of the members of the nonprofit (a mutual benefit corporation). It’s easy to form a nonprofit corporation in California: Just prepare articles of incorporation that say you are formed for one of these three broad nonprofit purposes and then file your articles with the California Secretary of State. This creates your legal corporate entity. However, having a nonprofit corporation recognized by the California Secretary of State is only your first hurdle. The next important step is to obtain the necessary state and federal corporate income tax exemptions for your nonprofit corporation. To obtain these exemptions, your nonprofit must be formed for one or more specific purposes described in the income tax statutes.

This book has been written specifically for nonprofit corporations that want to qualify for a federal income tax exemption under Section 501(c)(3) of the Internal Revenue Code. This means your nonprofit corporation must be formed for religious, charitable, scientific, literary, and/or educational purposes. If you want to organize as a religious purpose group, we will show you how to form a California religious nonprofit corporation. If you want to organize as a nonprofit to engage in any of the other 501(c)(3) tax-exempt purposes, we will show you how to form a California public benefit corporation. This book is not for groups that want to form a mutual benefit corporation, because mutual benefit nonprofits usually obtain their tax exemption under a subsection of Section 501(c) other than 501(c)(3). It is also not for certain special types of nonprofits (including some public benefit corporations) that do not fall under Section 501(c)(3). See discussion below, “Special Types of California Public Benefit Corporations,” and “Mutual Benefit Corporations.”

When thinking about incorporating your nonprofit, consider which purpose you fall under for Section 501(c)(3). Once you know you fall within one of the 501(c)(3) purposes, you can rest assured that this book can help you through the process. First we’ll help you create your corporate entity in California by showing you how to prepare and file articles of incorporation for a public benefit or religious corporation. Then we’ll show you how to obtain your state and federal nonprofit income tax exemptions for 501(c)(3) status.

Corporation Basics

You don’t have to understand all there is to know about corporations in order to follow this book or form your nonprofit. But there are a few basic concepts you’ll want to have under your belt as you go through the process. Here they are, with special emphasis on any differences between for-profit corporations and nonprofits:

• A corporation is a separate legal entity. A corporation is a legal entity that allows a group of people to pool energy, time, and money for profit or nonprofit activities. It acquires legal existence after its founders comply with their state’s incorporation procedures and formalities. The law treats a corporation as a separate “person,” distinct from the people who own, manage, or operate it. The corporation can enter into contracts, incur debts, and pay taxes. Corporations are either for-profit (business corporations) or nonprofits.

• For-profit, or business, corporations versus nonprofits. Business corporations can be formed for any legal purpose. They can issue shares of stock to investors in return for money or property, or services performed for the corporation. Shareholders receive a return on their investment if dividends are paid or if, upon dissolution of the corporation, any

 corporate assets remain to be divided among the shareholders after payment of all creditors. Nonprofits, on the other hand, generally cannot issue shares of stock or pay dividends under state law (unless they are some type of hybrid such as consumer or producer co-ops). The federal tax code also prohibits 501(c)(3)

tax-exempt nonprofit corporations from paying dividends or profits to their members or other individuals. When a 501(c)(3) tax-­exempt nonprofit corporation dissolves, it must distribute its remaining assets to another tax-exempt nonprofit group.

• In-state and out-of-state corporations. Corporations formed in California are known in California as “domestic” corporations. Corporations formed in other states, even if physically present and engaging in activities in California, are called “foreign” corporations. For example, a corporation formed in California is a domestic corporation as far as California is concerned, but a foreign cor­por­ation when considered by other states. At the end of this chapter, we give you more information on doing business outside California and deciding whether to incorporate in another state.

Public Benefit Corporations

Under state law, public benefit corporations are corporations formed for a “public purpose” or “charitable purpose.” Most groups forming public benefit corporations also want to qualify for Section 501(c)(3) status. These groups usually organize for one of the specified purposes under Section 501(c)(3)—charitable, scientific, literary, or educational. All of these 501(c)(3) purposes are considered “charitable” purposes under California law. For example, a school or educational facility would organize as a California public benefit corporation formed under state law for “charitable” purposes but its 501(c)(3) purposes would be “educational.” The public purpose classification under state law is for groups that want to form civic league or social welfare public benefit corporations (see discussion below on civic league and social welfare groups). Don’t worry—we show you how to fill in your articles so you put in the right purposes under California law and also satisfy the federal and state tax exemption requirements.

Special Types of California Public Benefit Corporations

This book covers the incorporation of California public benefit and religious nonprofits that want to obtain their tax exemption under Section 501(c)(3) of the Internal Revenue Code. There are several other types of California public benefit corporations that obtain tax exemption under other sections of the Internal Revenue Code or that must meet special state law requirements. Below, we list several of the most common types of these special California nonprofit corporations. If you plan to form one of these special non­profits, you’ll need to do your own research or get legal help to form your corporation—this book does not cover the incorporation of these special groups. See “Where to Go for Help for Non-501(c)(3) Nonprofits,” below.

• Civic leagues and social welfare groups. Civic leagues and social welfare groups are formed as California public benefit corporations and seek their exemption from federal corporate income taxation under Section 501(c)(4) of the Internal Revenue Code. Because this book covers only nonprofits exempt under Section 501(c)(3) of the Internal Revenue Code, you won’t be able

 to use this book to incorporate these types of public benefit corporations. (See “Special Nonprofit Tax-Exempt Organizations,” in Appendix B, for a list of organizations that qualify for tax-exempt status under a sub­section of 501(c) other than Subsection 3.)

• Medical or legal service corporations. These are nonprofit corporations operated to assume or defray the cost of medical or legal services. These corporations may be organized as California public benefit corporations or mutual benefit corporations. Special provisions of the California Corporations Code apply (see California Corporations Code §§ 10810–10841).

• Humane societies. A humane society, formed to prevent cruelty to children or animals, can be formed as a Calif­ornia public benefit corporation. The Department of Justice must perform a criminal history check on all incorporators and issue a certificate before the secretary of state will accept the articles of incorporation for filing (California Corporations Code §§ 10400–10406).

Religious Corporations

Just as the name indicates, religious corporations are formed primarily or exclusively for religious purposes. These groups can qualify as religious organizations under both state incorporation law and Section 501(c)(3).

You need not set up a formal church to form a religious nonprofit corporation; these groups can have a general religious purpose. For example, a group organized to promote the study and practice of a particular religion could incorporate as a religious nonprofit corporation. It is unlikely that the California Secretary of State’s office, where you’ll file your articles of incorporation, will question whether your religious activities are genuine. This type of debate is more likely to occur (if it occurs at all) when you apply for your state or federal tax exemptions.

Mutual Benefit Corporations

This book is not intended for mutual benefit corporations. Unlike public benefit corporations and religious corporations, these groups usually qualify for tax-exempt status under a subsection of 501(c) other than 501(c)(3).

Examples of mutual benefit corporations include trade associations, automobile clubs, and social groups, such as tennis clubs. Chambers of commerce, boards of trade, and mechanics’ institutes, which are generally formed to promote trade and commerce, can organize as mutual benefit corporations or as regular, for-profit corporations. Cooperatives, comprising producers or consumers organized for their mutual benefit, can also qualify as mutual benefit nonprofits with special added restrictions applicable to them.

Because these groups do not qualify for tax-exempt status under Section 501(c)(3), they are not entitled to many of the benefits enjoyed by public benefit and religious corporations. For example, contributions to mutual benefit corporations are normally not tax deductible, and other benefits (such as special nonprofit mailing rates and real and personal property tax exemptions) are not available to mutual benefit corporations. Mutual benefit corporations also cannot distribute gains, profits, or dividends to those designated in their articles or bylaws as members, but may provide them with other benefits such as services and facilities. On the other hand, members of a mutual benefit corporation can own part of the corporation. When the corporation dissolves and all its debts and liabilities are paid, the remaining assets, gains, and profits can be distributed to its members.

Do-Good LLCs and Corporations—

The Latest in Limited Liability Entities

A number of states enable the formation of hybrid entities (LLCs and/or corporations) that can make a profit yet also do good. For example, some states (although not California at present) authorize the formation of a low-profit LLC (also called an L3C) that can be formed for an educational or charitable purpose but also can make a profit. States initially created this special type of hybrid entity to allow foundations to more easily distribute funds to a qualified social-purpose organization, but the IRS has not yet formally approved L3Cs for this purpose.

Closer to home, California allows the formation of flexible purpose corporations and benefit corporations, which can be formed to do good works as well as to make money. The advantage of these new California entities is that they can allow the principals to spend time and money trying to do good without having to worry about stakeholders being upset (and suing them) for not spending all their time trying to turn a profit. Because these entities are formed to make money, they do not qualify for a 501(c)(3) corporate income tax exemption.

All of the above hybrid entities are sometimes loosely referred to as B corporations. However, this term really refers to a certification that a socially-responsive corporation, LLC, or other entity can seek, as opposed to a separate type of corporation or other distinct legal entity (see www.bcorporation.net for more information).

Benefits of the Nonprofit Corporation

Now that you understand that this book is intended for nonprofits organized for religious, charitable, scientific, literary, and/or educational purposes that want to qualify for a tax exemption under Section 501(c)(3) of the Internal Revenue Code (and hopefully your nonprofit is among them), let’s look at the benefits you’ll enjoy as a 501(c)(3) tax-exempt nonprofit corporation. The relative importance of each of the following benefits will vary from group to group, but at least one of them should be very significant for your organization.

If you finish this section and conclude that nothing here is very important for your group, you’ll want to consider whether it makes sense to incorporate at all. Many groups accomplish their nonprofit purposes just fine as unincorporated nonprofit associations, without formal organizational paperwork or written operational rules. If you can continue to accomplish your nonprofit purposes and goals informally, you may be happier staying small.

Tax Exemptions

Nonprofit corporations are eligible for state and federal exemptions from payment of corporate income taxes, as well as other tax exemptions and benefits. At federal corporate tax rates of 15% on the first $50,000 of taxable income, 25% on the next $25,000, and 34% and higher on income over $75,000, it goes without saying—at least if you expect to earn a substantial amount of money (from services, exhibits, or performances, for example)—that you’ll want to apply for an exemption. The California corporate income tax exemption is equally attractive, as are county real and personal property tax exemptions. Chapters 3, 4, and 5 cover tax exemptions in detail.

Where to Go for Help for

Non-501(c)(3) Nonprofits

If you want to form a nonprofit for any purpose other than one recognized under Section 501(c)(3) of the Internal Revenue Code, this book is not for you. For example, if you are a civic league or social welfare group that wants nonprofit status, you will want to organize as a public benefit corporation under Section 501(c)(4) of the Internal Revenue Code. Or, if your group is a California mutual benefit corporation, you will seek tax-exempt status under a subsection of 501(c) other than

501(c)(3). This book is not intended for these special types of nonprofits.

If you are a special nonprofit that is not covered by this book, you can find legal forms and tax exemption help online. For sample articles of incorporation for mutual benefit corporations and public benefit civic leagues and social welfare groups, go to the California Secretary of State website (the Business Entities section). If you are seeking tax exemption for a nonprofit under a subsection of 501(c) other than 501(c)(3),

go to the IRS website at www.irs.gov and obtain IRS Package 1024. The IRS 1024 package contains forms and instructions to use to apply for a nonprofit tax exemption under Internal Revenue Code Sections 501(c)(2), (4), (5), (6), (7), (8),

(9), (10), (12), (13), (15), (17), (19), and (25).

The California Franchise Tax Board website at www.ftb.ca.gov has state tax exemption application forms to download and use to apply for your state corporate income tax exemption for these special non-501(c)(3) groups. IRS Publication 557 and IRS Form 1024 also contain information and instructions on forming some of these special purpose nonprofits.

see an expert

Get the help of a competent tax adviser as soon as you decide to incorporate. Make sure you choose someone experienced in the special field of nonprofit bookkeeping. Ask the adviser to help you (especially your treasurer) set up a good record-keeping system. Have the tax helper periodically review the system to be sure that you have met accepted bookkeeping standards and have filed your tax forms on time.

Receiving Public and Private Donations

One of the primary reasons for becoming a 501(c)(3) nonprofit corporation is that it increases your ability to attract and receive public and private grant funds and donations.

• Public sources. Tax-exempt government foundations (like the National Endowment for the Arts or Humanities, the Corporation for Public Broadcasting, or the National Satellite Program Development Fund) as well as private foundations and charities (such as the Ford Foundation, the United Way, or the American Cancer Society) are usually required by their own operating rules and federal tax regulations to donate their funds only to 501(c)(3) tax-exempt organizations.

• Private sources. Individual private donors can

claim personal federal income tax deductions for contributions made to 501(c)(3) tax-exempt groups. At death, a complete federal estate tax exemption is available for bequests made to 501(c)(3) groups.

In short, if you plan to ask people to give you significant amounts of money in furtherance of your nonprofit purpose, you need to demonstrate to your donors that you have 501(c)(3) tax-exempt status.

Protection From Personal Liability

Protecting the members of your group from personal liability is one of the main reasons for forming a corporation (either profit or nonprofit). Once you’re incorporated, in most situations directors or trustees, officers, employees, and members of a corporation won’t be personally liable for corporate debts or liabilities, including unpaid organizational debts and unsatisfied lawsuit judgments against the organization, as they normally would be if they conducted their affairs without incorporating. Creditors can go after only corporate assets to satisfy liabilities incurred by the corporation—not the personal assets (car, home, or bank accounts) of the people who manage, work for, or volunteer to help the nonprofit corporation.

Example: A member of the audience sued a nonprofit symphony orchestra when the patron fell during a concert, claiming that the symphony (which also owned the concert hall) provided an unsafe ramp. The patron won a judgment that exceeded the orchestra’s insurance policy limits. The amount of the judgment in excess of insurance is a debt of the corporation, but not of its individual directors, members, managers, or officers. By contrast, had the orchestra been an unincorporated association of musicians, the principals of the unincorporated group could be held personally liable for the excess judgment amount.

In a few situations, however, people involved with a nonprofit corporation may be personally liable for the corporation’s liabilities. Here are some major areas of potential personal liability:

• Taxes. State and federal governments can hold the corporate employee who is responsible for reporting and paying corporate taxes (usually the treasurer) personally liable for any unpaid taxes, penalties, and interest due for failure to pay taxes or file necessary returns. With proper planning, your nonprofit corporation should be tax exempt, but you may still have to file informational returns and annual reports with the secretary of state, as well as pay employee withholding and other payroll taxes and taxes on income unrelated to your nonprofit purposes. IRS penalties for delinquent tax payments and returns are substantial, so keep this exception to limited liability in mind—particularly if you will be the treasurer.

• Dues. Members of a nonprofit corporation are personally liable for any membership fees and dues they owe the corporation. In most cases, this is a minor obligation since dues are normally set at modest amounts.

• Violations of statutory duties. Corporate directors are legally required to act responsibly (not recklessly) when managing the corporation. They may be held personally financially liable if they fail to act responsibly. Personal liability of this sort is the exception, not the rule. Generally, as long as directors attend meetings and carry out corporate responsibilities conscientiously, they should have little to worry about—the corporate limited liability shield insulates directors from all but the most reckless and irresponsible decisions.

• Intermingling funds or other business dealings. A nonprofit corporation must act so that its separate existence is clear and respected. If it mixes up corporate funds with the personal funds of those in charge, fails to follow legal formalities (such as failing to operate according to bylaws, hold director meetings, or keep minutes of meetings), or risks financial liability without sufficient backup in cash or other assets, a court may disregard the corporate entity and hold the principals responsible for debts and other liabilities of the corporation. In legalese, this is known as “piercing the corporate veil.” Piercing the veil is the exception, not the rule, and only happens when a court decides that it is necessary to prevent a gross injustice or fraud perpetuated by the founders or principals of a corporation.

• Private foundation managers. If the nonprofit corporation is classified as a private foundation, foundation managers can be held personally liable for federal excise taxes associated with certain prohibited transactions. They may also be held personally liable for penalties and interest charged for failing to file certain tax returns or pay required excise taxes. (As explained in Chapter 4, a private foundation is a 501(c)(3)

corporation that does not qualify as a public charity—you’ll see that most 501(c)(3) nonprofits can qualify as public charities and are not subject to the private foundation requirements.)

• Loans. When a nonprofit corporation takes a loan to cover its operating costs or buys property subject to a mortgage, banks and commercial lending institutions sometimes insist on the personal guarantee of its directors or officers. If the directors or officers agree to personally guarantee the loan or mortgage, the protection that they would normally enjoy as a result of their organization’s corporate status goes away. It is somewhat unusual for nonprofit directors or officers to sign a personal guarantee. Obviously, if they do, they will be liable to repay the loan if the corporation cannot do so.

Separate and Perpetual Legal Existence

A corporation is a legal entity that is separate from the people who work in it. Again, one benefit of this separate existence is that corporate liabilities are not the liabilities of the managers, officers, or members of the corporation (known as the corporate characteristic of limited liability). Another benefit is that this corporate legal person is, in a sense, immortal; the nonprofit corporation continues to exist as a legal entity despite changes in management or other corporate personnel caused by the resignation, removal, or death of the people associated with it. It may, of course, be dissolved or drastically affected by the loss of key people, but its inherent perpetual existence makes it more likely that the group’s activities will continue, an attractive feature to the private or public donor who prefers funding activities that are organized to operate over the long term.

Employee Benefits

Another benefit of the nonprofit corporation is that its principals can also be employees and, therefore, eligible for employee fringe benefits not generally available to the workers in unincorporated organizations. These benefits include group term life insurance, reimbursement of medical expenses, and coverage by a qualified corporate employee pension or retirement income plan.

Formality and Structure

The formal corporate documents—the articles, bylaws, minutes of meetings, and board resolutions—that you’ll prepare as a nonprofit will actually be quite useful to your organization. They’ll outline the group’s purposes, embody its operating rules, and provide structure and procedures for decision making and dispute resolution. This is important for any collective activity, but for nonprofit groups it is vital, especially if the board includes members of the community with diverse interests and viewpoints. Without the clear-cut delegation of authority and specific operating rules in the articles and bylaws, running the organization might be a divisive, if not futile, affair.

Miscellaneous Benefits

Additional advantages are available to nonprofits that engage in particular types of activities or operations. These benefits can be helpful, and in some cases are critical, to the success of a nonprofit organization. Here are examples of some of the benefits available to certain types of tax-exempt nonprofits:

• Your nonprofit may qualify for exemptions from county real and personal property taxes.

• 501(c)(3) organizations receive lower postal rates on third-class bulk mailings.

• Many publications offer cheaper classified advertising rates to nonprofit organizations.

• Nonprofits are the exclusive beneficiaries of free radio and television public service announcements (PSAs) provided by local media outlets.

• Many stores offer lower membership rates to nonprofit employees.

• Nonprofit employees are often eligible to participate in job training, student intern, work-study, and other federal, state, and local employment incentive programs (where salaries are paid substantially out of federal and state funds).

• 501(c)(3) performing arts groups are qualified to participate in the performance programs sponsored by federally supported colleges and universities.

• Certain 501(c)(3) educational organizations are eligible for a tax refund for gasoline expenses (for example, in running school buses).

Example: A senior citizens’ botany club began as an informal organization. Initially, six members took a monthly nature walk to study and photograph regional flora. Everyone chipped in to buy gas for whoever drove to the hike’s starting point. Recently, however, membership increased to 15 and the group decided to collect dues from members to pay the increased expenses—gas money, guidebooks, maps, and club T-shirts—associated with more frequent field trips. To avoid mixing club monies with personal funds, a treasurer was designated to open a bank account on behalf of the organization. Several people suggest that it is time to incorporate the club.

Does incorporation make sense at this time? Probably not. There is no new pressing need to adopt the corporate form or to obtain formal recognition as a tax-exempt nonprofit. Most banks will allow an unincorporated group without a federal Employer Identification Number or IRS tax exemption to open up a non–interest-bearing account. However, should the club decide to seek funding and contributions to spearhead a drive to save open space in the community, it might be a good idea to incorporate.

The Disadvantages of Going Nonprofit

If your group has come together for 501(c)(3)

tax-exempt purposes, and if reading about the benefits of becoming a nonprofit above prompted a “Wow! We would really like to be able to do that!   ” then chances are you’ve decided to tackle the rules and forms necessary to establish your status as a legal nonprofit. Before jumping in, however, take a minute to read the following descriptions of some of the hurdles and work you’ll encounter along the way, especially if you have been operating informally (and successfully) without financial or employee record keeping or controls. If any of the following appear insurmountable to you, think again about incorporating.

Official Paperwork

One disadvantage in forming any corporation is the red tape and paperwork. You’ll begin by preparing initial incorporation documents (articles of incorporation, bylaws, and minutes of first meeting of the board of directors), and an IRS income tax exemption application. Although this book will show you how to prepare your own incorporation forms and income tax exemption application with a minimum of time and trouble, the process will still take you a few hours at the very least. You and your compatriots must be prepared for some old-fashioned hard work.

After you’ve set up your corporation, you’ll need to file annual information returns with the state (the Franchise Tax Board and the attorney general) as well as the Internal Revenue Service. Also, you will need to regularly prepare minutes of ongoing corporate meetings, and, occasionally, forms for amending articles and bylaws. The annual tax reporting forms will require the implementation of an organized bookkeeping system plus the help of an experienced nonprofit tax adviser, as explained below. Fortunately, keeping minutes of these meetings is not all that difficult to do once someone volunteers for the task (typically the person you appoint as corporate secretary). Sample forms for amending nonprofit articles are available from the California Secretary of State’s website. Go to the Business Entities section and click on “Forms, Samples, and Fees.”

Annual nonprofit informational tax returns do present a challenge to a new group unfamiliar with state tax reporting forms and requirements. Other record-keeping and reporting chores, such as double-entry accounting procedures and payroll tax withholding and reporting, can be equally daunting. At least at the start, most nonprofits rely on the experience of a tax adviser, bookkeeper, or other legal or tax specialist on the board or in the community to help them set up their books and establish a system for preparing tax forms on time. See Chapter 11 for recommendations on finding legal and tax professionals for your nonprofit.

Incorporation Costs and Fees

For nonprofit incorporators unwilling to do the job themselves, a main disadvantage of incorporating a nonprofit organization is the cost of paying an attorney to prepare the incorporation forms and tax exemption applications. Putting some time and effort into understanding the material in this book can help you eliminate this disadvantage, leaving you with only the actual cost of incorporation. Including the typical $400 federal tax exemption application fee, total fees to incorporate are approximately $450 to $500. (Costs are $450 higher for nonprofits that anticipate gross receipts of more than $10,000. These groups pay an $850, rather than a $400, federal tax exemption application fee.)

Time and Energy Needed to Run the Nonprofit

When a group decides to incorporate, the legal decision is often part of a broader decision to increase not just the structure, but the overall scope, scale, and visibility of the nonprofit. With a larger, more accountable organization come a number of new tasks: setting up and balancing books and bank accounts, depositing and reporting payroll taxes, and meeting with an accountant to extract and report year-end figures for annual informational returns. Although these financial, payroll, and tax concerns are not exclusively corporate chores, you’ll find that most unincorporated nonprofits keep a low employment, tax, and financial profile and get by with minimum attention to legal and tax formalities.

Example: A women’s health collective operates as an unincorporated nonprofit organization. It keeps an office open a few days a week where people stop by to read and exchange information on community and women’s health issues. The two founders donate their time and the office space and pay operating costs (such as phone, utilities, and photocopying) that aren’t covered by contributions from visitors. The organization has never made a profit, there is no payroll, and tax returns have never been filed. There is a minimum of paperwork and record keeping.

The founders could decide to continue this way indefinitely. However, the founders want to expand the activities and revenues of the collective. They decide to form a 501(c)(3)

nonprofit corporation in order to be eligible for tax-deductible contributions and grant funds from the city, and to qualify the group to employ student interns and work-study students. This will require them to prepare and file articles of incorporation and a federal corporate income tax exemption application. They must select an initial board of directors and prepare organizational bylaws and formal written minutes of the first board of directors’ meeting.

After incorporation, the group holds regular board meetings documented with written minutes, sets up and uses a double-entry bookkeeping system, implements regular federal and state payroll and tax procedures and controls, files exempt organization tax returns each year, and expands its operations. A full-time staff person is assigned to handle the increased paperwork and bookkeeping chores brought about by the change in structure and increased operations of the organization.

This example highlights what should be one of the first things you consider before you decide to incorporate: Make sure that you and your coworkers can put in the extra time and effort that an incorporated nonprofit organization will require. If the extra work would overwhelm or overtax your current resources, we suggest you hold off on your incorporation until you get the extra help you need to accomplish this task smoothly (or at least more easily).

Restrictions on Paying Directors and Officers

As a matter of state corporation law and the tax exemption requirements, nonprofits are restricted in how they deal with their directors, officers, and members. None of the gains, profits, or dividends of the corporation can go to individuals associated with the corporation, including directors, officers, and those defined as members in the corporation’s articles or bylaws. State self-dealing rules apply as well, regulating action by the board of directors if a director has a financial interest in a transaction. Finally, with respect to California public benefit corporations (if you form a 501(c)(3) tax-exempt nonprofit corporation for nonreligious purposes, you will form a California public benefit corporation), a majority of the board of directors cannot be paid (other than as a director), or related to other persons who are paid, by the corporation. This can represent a significant restriction because it eliminates the close-knit organization many picture when they think of a small, grassroots nonprofit corporation.

Restrictions Upon Dissolution

One of the requirements for the 501(c)(3) tax exemption is that upon dissolution of the corporation, any assets remaining after the corporation’s debts and liabilities are paid must go to another tax-exempt nonprofit, not to members of the former corporation.

Restrictions on Your Political Activities

Section 501(c)(3) of the Internal Revenue Code establishes a number of restrictions and limitations that apply to nonprofits. Here, we discuss a limitation that may be very significant to some groups—the limitation on your political activities. Specifically, your organization may not participate in political campaigns for or against candidates for public office, and cannot substantially engage in legislative or grassroots political activities except as permitted under federal tax regulations.

Example: Society for a Saner World, Inc., has as one of its primary objectives lobbying hard to pass federal and local legislation that seeks to lessen societal dependency on fossil fuels. Since a substantial portion of the group’s efforts will consist of legislative lobbying, the group’s 501(c)(3) tax exemption probably will be denied by the IRS. Instead, the group should seek a tax-exemption under IRC § 501(c)(4) as a social welfare group, which is not limited in the amount of lobbying the group can undertake. Of course, the benefits of 501(c)(4) tax exemption are fewer too—contributions to the group are not tax-deductible and grant funds will be more difficult to obtain—see “Special Nonprofit Tax-Exempt Organizations,” in Appendix B.

Oversight by the Attorney General

The California Attorney General has broad power to oversee the operations of California public benefit corporations, more so than it does with other California nonprofits. (Remember: If you form a nonreligious 501(c)(3) tax-exempt corporation, you will be forming a California public benefit corporation.) The state can even take the corporation to court to make sure it complies with the law.

By contrast, California religious purpose nonprofit corporations have wider flexibility in managing their internal affairs. If a religious corporation does not set up its own operating rules, provisions of the nonprofit law will apply to its operations by default. These are less stringent than those that would apply to a public benefit corporation under similar circumstances.

How Nonprofits Raise, Spend, and Make Money

Most nonprofits need to deal with money—indeed, being able to attract donations is a prime reason for choosing nonprofit status. Nonprofits can also make money. Nonprofit does not literally mean that a nonprofit corporation cannot make a profit. Under federal tax law and state law, as long as your nonprofit is organized and operating for a recognized nonprofit purpose, it can take in more money than it spends in conducting its activities. A nonprofit may use its tax-free profits for its operating expenses (including salaries for officers, directors, and employees) or for the benefit of its organization (to carry out its exempt purposes). It cannot, however, distribute any of the profits for the benefits of its officers, directors, or employees (as dividends, for example).

This section explains how nonprofits raise initial funds and how they make money on an ongoing basis.

Initial Fundraising

A California nonprofit corporation is not legally required to have a specified amount of money in the corporate bank account before commencing operations. This is fortunate, of course, because many beginning nonprofits start out on a shoestring of meager public and private support.

So, where will your seed money come from? As you know, nonprofit corporations cannot issue shares, nor can they provide investment incentives, such as a return on capital through the payment of dividends to investors, benefactors, or participants in the corporation (see “Corporation Basics,” at the beginning of this chapter).

Nonprofits have their own means and methods of obtaining start-up funds. Obviously, the most common method is to obtain revenue in the form of contributions, grants, and dues from the people, organizations, and governmental agencies that support the nonprofit’s purpose and goals. Also, if you are incorporating an existing organization, its assets are usually transferred to the new corporation—these assets may include the cash reserves of an unincorporated group, which can help your corporation begin operations. You can also borrow start-up funds from a bank, although for newly formed corporations a bank will usually require that incorporators secure the loan with their personal assets—a pledge most nonprofit directors are understandably reluctant to make.

Often, of course, nonprofits receive initial and ongoing revenues from services or activities provided in the pursuit of their exempt purposes (ticket sales, payments for art lessons or dance courses, school tuition, or clinic charges).

For information on meeting California’s special fundraising rules, see “State Solicitation Laws and Requirements,” in Chapter 5.

Making Money From Related Activities

Many nonprofits make money while they further the goals of the organization. The nonprofit can use this tax-exempt revenue to pay for operating expenses (including reasonable salaries) and to further its nonprofit purposes. For example, an organization dedicated to the identification and preservation of shore birds might advertise a bird-watching and -counting hike for which they charge a fee; the group could then use the proceeds to fund their bird rescue operations. What it cannot do with the money, however, is distribute it for the benefit of officers, directors, or employees of the corporation (as the payment of a patronage dividend, for example).

Example: Friends of the Library, Inc., is a 501(c)(3) nonprofit organized to encourage literary appreciation in the community and to raise money for the support and improvement of the public library. It makes a profit from its sold-out lecture series featuring famous authors and from its annual sale of donated books. Friends can use this tax-exempt profit for its own operating expenses, including salaries for officers and employees, or to benefit the library.

Making Money From Unrelated Activities (Unrelated Income)

Nonprofits can also make money in ways unrelated to their nonprofit purpose. Often this income is essential to the survival of the nonprofit group. This unrelated income, however, is usually taxed as unrelated business income under state and federal corporate income tax rules. While earning money this way is permissible, it’s best not to let unrelated business activities reach the point where you start to look more like a for-profit business than a nonprofit one. This can happen if the unrelated income-generating activities are absorbing a substantial amount of staff time, requiring additional paid staff, or producing more income than your exempt-purpose activities. If the unrelated revenue or activities of your tax-exempt nonprofit reach a substantial level, the IRS can decide to revoke the group’s 501(c)(3) tax exemption—a result your nonprofit will no doubt wish to avoid.

Example: Many thousands of books are donated to Friends of the Library for its annual book sale, one of its major fundraising events. Although the sale is always highly successful, thousands of books are left over. Friends decides to sell the more valuable books by advertising in the rare and out-of-print books classified sections in various magazines. The response is overwhelming; soon, there are six employees cataloging books. In addition, Friends begins a business purchasing books from other dealers and reselling them to the public. Such a situation could attract attention from the IRS and prompt it to reconsider Friends’ 501(c)(3) tax-exempt status.

Making Money From Passive Sources

Although it’s not typical for the average nonprofit, a nonprofit corporation can make money from passive sources such as rents, royalties, interest, and investments. This income is nontaxable in some cases.

Your Path to Nonprofit Status

Nonprofit organizations first obtain nonprofit corporate status with the California Secretary of State—a simple formality accomplished by filing articles of incorporation. Then they go on to obtain a corporate income tax exemption with the Internal Revenue Service. California recognizes your federal tax exemption, so you don’t have to prepare a separate state tax exemption application. In sum, your path to nonprofit status is a basic two-step process—first you incorporate with the California Secretary of State, then you apply for tax-exempt recognition from the Internal Revenue Service (you’ll notify the California Franchise Tax Board of your federal income tax exemption). When you’re done with this book, you’ll have completed each of these steps.

State Law Requirements for Nonprofits

The California Secretary of State must officially recognize all California nonprofit corporations. To obtain state recognition, you’ll file articles of incorporation with the secretary of state’s office stating that your organization is entitled to receive nonprofit corporate status. This book covers the basic requirements for obtaining recognition by California’s Secretary of State as a nonprofit corporation. The California Nonprofit Corporation Law (California Corporations Code §§ 5000–9927) governs the organization and operations of California nonprofit corporations.

We focus on public benefit corporations in this book (those formed for public or charitable purposes) because these corporations make up the majority of nonprofit corporations eligible for exemption under Section 501(c)(3) of the Internal Revenue Code. Requirements for religious corporations are noted only if they are different from the requirements for public benefit corporations.

Tax-Exempt Status Under Federal and State Tax Law

Both state and federal tax laws apply to California nonprofit corporations. To obtain tax-exempt status, nonprofits must comply with initial and ongoing requirements under the federal Internal Revenue Code. California tax law parallels the federal law. In most ways, understanding and complying with state and federal tax rules is more important (and more challenging) than fulfilling the state corporate law requirements. This book focuses on nonprofit corporations seeking tax-exempt status under Section 501(c)(3) of the Internal Revenue Code, which are nonprofits organized for religious, charitable, educational, scientific, or literary purposes.

Incorporating in Another State—Don’t Fall for It

Corporations formed in a particular state are known in that state as domestic corporations. When viewed from outside that state, these corporations are considered foreign. A foreign corporation that plans to engage in a regular or repeated pattern of activity in another state must qualify to do business there by obtaining a certificate of authority from the secretary of state. For example, a corporation formed in Nevada that intends to do regular business in California is a foreign corporation here, and must qualify the corporation with our secretary of state.

Incorporators who plan to operate in another state besides California have naturally considered whether it makes sense to incorporate in that other state. Maybe the incorporation fees or corporate taxes are lower than those in California or the nonprofit statutes are more flexible. Then, the reasoning goes, one could qualify the corporation in California as a foreign corporation. As tempting as this end run may appear, it’s not usually worth it. This section explains why, and also advises you of out-of-state activities that you can engage in without worrying about qualifying in another state.

Qualifying as a Foreign Corporation in California Will Cost You More

The process of qualifying a foreign corporation to operate in California takes about as much time and expense as incorporating a domestic corporation. This means that you will pay more to incorporate out-of-state since you must pay the regular California qualification fees plus out-of-state incorporation fees.

Multiple Tax Exemptions

Your corporation will still be subject to taxation in each state in which it earns or derives income or funds. If the state of incorporation imposes a corporate income tax, then the nonprofit corporation will need to qualify for two state corporate tax exemptions—one in California, the state where the corporation will be active, and one for the state of incorporation. Similarly, double sales, property, and other state tax exemptions may often be necessary or appropriate.

Multiple State Laws

Your out-of-state corporation will still be subject to many of the laws that affect corporations in California. Many of California’s corporate statutes that apply to domestic corporations also apply to foreign corporations.

Out-of-State Activities Below the Radar

For the above reasons, most readers who flirt with the idea of incorporating in a state other than California would be well advised to skip it. This doesn’t mean, however, that you’ll have to trim all of your activities to stay within California. Fortunately, there are many things nonprofits can do as a foreign corporation in another state without obtaining a certificate of authority from the secretary of that state. Here are some that are recognized in many (but not all) states:

• maintaining, defending, or settling any legal action or administrative proceeding, including securing or collecting debts, and enforcing property rights

• holding meetings of corporate directors or of the membership and distributing information to members

• maintaining bank accounts and making grants of funds

• making sales through independent contractors and engaging in interstate or foreign commerce

• conducting a so-called isolated transaction that is completed within 30 days and is not one of a series of similar transactions, and

• exercising powers as an executor, administrator, or trustee, so long as none of the activities required of the position amounts to transacting business.

When Out-of-State Incorporation Makes Sense

There may be a few of you for whom incorporation in another state makes sense. If you plan to set up a multistate nonprofit with corporate offices and activities in more than one state (a tristate environmental fund for example), you may want to consider incorporating in the state that offers the greatest legal, tax, and practical advantages. To help you decide where to incorporate, you can refer to the secretary of state’s website for each state where you operate. Type “nonprofit resource libraries” into your browser’s search box—you’ll find a host of online resources at your disposal. An experienced nonprofit lawyer or consultant can also help you determine which state is the most convenient and least costly to use as the legal home for your new nonprofit corporation.

References to IRS Articles and Materials

Throughout the book, there are references to IRS articles and materials that you can download from Nolo’s website (see Appendix A for the link). Some of this material includes articles and information made available by the IRS on its website as part of its Exempt Organizations Continuing Professional Education Technical Instruction Program, which regularly publishes articles for tax-exempt organizations. The IRS has the following statement on its website regarding this material: “These materials were designed specifically for training purposes only. Under no circumstances should the contents be used or cited as authority for setting or sustaining a technical position.”

In other words, use this material to learn about IRS tax issues, but don’t expect to be able to rely on it if you end up in a dispute with the IRS. Nolo includes this material as a convenience to the reader and as an alternative to directing you to the IRS website. This material is taken directly from the IRS website at www.irs.gov (enter “EO Tax Law Training Articles” in the search box at the top of the main website page, then follow the links to “Exempt Organizations Continuing Professional Education Technical Instruction Program” main page, where you’ll find a link to an alphabetical index of the articles, “Exempt Organizations CPE Topical Index”). If you are interested in one of the issues, you should check the IRS website for any updated articles or information on your topic.

We hope you enjoyed this material. The rest of the book is available for purchase.

Product Details

Keep your corporate status—and avoid personal liability

Incorporating your business is an important first step in obtaining limited liability status. To keep that status, you must observe a number of legal formalities, including holding and documenting shareholder and director meetings.

Meeting minutes form the primary paper trail of a corporation’s legal life—and The Corporate Records Handbook provides all the instructions and forms you need to prepare them. Minutes forms include:

Notice of Meeting

Shareholder Proxy

Meeting Summary Sheet

Minutes of Annual Shareholders' Meeting

Minutes of Annual Directors' Meeting

Waiver of Notice of Meeting, and

Written Consent to Action Without Meeting

You'll also find more than 75 additioal resolutions which let you:

elect S corporation tax status

borrow or lend money

adopt pension and profit-sharing plans

authorize bank loans

authorize a corporate line of credit

set up employee benefit plans

purchase or lease a company car

amend articles and bylaws

and more!

The Corporate Records Handbook gives you the forms you need to keep required records.. This edition has been updated to reflect the latest changes in the law.

“This practical guide gives step-by-step instructions plus the legal forms to be filled out and filed to keep corporate status.”-Orange County Register

“Should be part of any serious business library—and any corporate library.”-Bookwatch

ISBN

9781413322590

Number of Pages

600

Included Forms

Notice and Minutes Forms

Meeting Summary Sheet

Call of Meeting

Meeting Participant List

Notice of Meeting

Acknowledgment of Receipt of Notice of Meeting Proxy

Certification of Mailing

Minutes of the Annual Meeting of Shareholders

Minutes of Special Meeting of Shareholders

Minutes of Annual Meeting of Directors

Minutes of Special Meeting of Directors

Waiver of Notice of Meeting

Approval of Corporate Minutes by Directors or Shareholders

Cover Letter for Approval of Minutes of Paper Meeting

Written Consent to Action Without Meeting

Standard Corporate Business Resolutions

Authorization of Treasurer to Open and Use Accounts

Authorization of Treasurer to Open and Use Specific Corporate Account(s)

Authorization of Corporate Account and Designation of Authorized Signers

Authorization of Rental of Safe Deposit Box

Adoption of Assumed Name

Board Approval of Proposed Contract

Approval of Lease

Purchase of Real Property

Authorization of Sale of Real Property

Delegation of Authority to Corporate Employee

Director Ratification of Employee’s Acts

Board Ratification of Contract

Rescission of Authority of Employee

Shareholder Ratification of Decisions or Acts

Certification of Board or Shareholder Action

Affidavit of Corporate Decision Making

Acknowledgment

Corporate Tax Resolutions

S Corporation Tax Election

S Corporation Shareholders’ Agreement

Accumulation of Corporate Earnings

Qualification of Shares Under Internal Revenue Code Section 1244

Approval of Independent Audit of Corporate Financial Records

Approval of Corporate Tax Year

Payment and Deduction of Organizational Expenses

Resolutions to Amend Corporate Articles and Bylaws

Approval of Amendment to Articles of Incorporation

Approval of Restatement of Articles of Incorporation

Amendment of Articles Form

Approval of Amendment of Bylaws

Corporate Hiring and Appointment Resolutions

Approval of Hiring of Corporate Employee

Approval of Bonuses and Salary Increases

Shareholder Ratification of Employee Pay

Approval of Independent Contractor Services

Appointment of Corporate Officers

Authorization of Payment for Attending Meetings

Annual Director or Officer Stipend for Attendance at Meetings

No Compensation for Attending Corporate Meetings

Indemnification and Insurance for Directors and Officers

Director Conflict-of-Interest Resolutions

Board Approval of Transaction Benefiting a Director

Directors’ Written Consent to Transaction Benefiting a Director

Shareholder Approval of Transaction Benefiting a Director

Shareholder Written Consent to Transaction Involving a Director

Resolutions for Loans to the Corporation

Authorization of Loan at Specific Terms

Authorization of Maximum Loan on General Terms

Unlimited Authorization of Loans for Business Needs

Authorization of Line of Credit

Authorization of Line of Credit With Cap on Each Transaction

Authorization of Loan Terms Secured by Corporate Property

Resolution Approving Loan to Corporation

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan) Secured by -Corporate Property

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan) With Balloon Payment

Promissory Note: Periodic Payments of Interest With Lump Sum Principal Payment

Promissory Note: Lump Sum Payment of Principal and Interest at Specified Date

Promissory Note: Lump Sum Payment of Principal and Interest on Demand by Noteholder

Promissory Note: Variable Schedule of Payments of Principal and Interest

Resolutions for Loans by the Corporation to Insiders

Approval of Corporate Loan to Insider

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan) Secured by Property

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan) With Balloon Payment

Promissory Note: Periodic Payments of Interest With Lump Sum Principal Payment

Promissory Note: Lump Sum Payment of Principal and Interest at Specified Date

Promissory Note: Lump Sum Payment of Principal and Interest on Demand by Noteholder

Promissory Note: Variable Schedule of Payments of Principal and Interest

Release of Promissory Note

Employee Fringe Benefits and Business Expense Reimbursement Resolutions

Authorization of Group Health, Accident, or Disability Insurance for Employees

Adoption of Self-Insured Medical Reimbursement Plan

Purchase of Group Term Life Insurance

Authorization of Employee Death Benefit

Agreement Regarding Death Benefits

Purchase or Lease of Company Car

Authorization of Payment of Standard Mileage Allowance to Employees

Business Meal Expense Allotment for Employees

On-Premises Meals and Lodging to Employees

Authorization of Corporate Credit and Charge Cards for Employees

Reimbursement of Actual Travel and Entertainment Expenses to Employees Under Accountable Reimbursement Plan

Reimbursement of Actual Travel and Entertainment Expenses to Employees Under Nonaccountable Reimbursement Plan

Authorization of Per Diem Travel Allowance for Employees

Board Approval of Stock Bonus or Stock Option Plan

Corporate Retirement Plan Resolutions

Board of Directors’ Adoption of Retirement Plan

Board of Directors’ Adoption of Profit-Sharing Plan

Shareholder Ratification of Retirement Plan

Stock Dividend Resolutions

Declaration of Cash Dividend

Authorization of Cash Dividend Payable in Installments

Declaration of Year-End Dividend

Declaration of Regular and Extra Dividend

Declaration of Accumulated Dividend to Preferred Shareholders

Authorization of Property Dividend to Shareholders

Stock Issuance Resolutions

Approval of the Issuance of Shares

Sale and Issuance of Shares for Property

Sale and Issuance of Shares for Indebtedness Canceled

Sale and Issuance of Shares for Services

Sale and Issuance of Capital Stock for Assets and Liabilities of a Business

Bill of Sale and Agreement

Issuance of Shares in Exchange for Assignment of Trademark, Service Mark, Patent, or Copyright Assignment

Issuance of Shares in Return for Cash and Promissory Note

About the Author

Anthony Mancuso

Attorney

Anthony Mancuso is a corporations and limited liability company expert, currently working at Google. He graduated from Hastings College of Law in San Francisco, is a member of the California State Bar, writes books and software in the fields of corporate and LLC law, and studied advanced business taxation at Golden Gate University in San Francisco. He is the author of several Nolo books on forming and operating corporations (both profit and nonprofit) and limited liability companies. His titles include Incorporate Your Business, How to Form a Nonprofit Corporation (national and California editions), Form Your Own Limited Liability Company, The Corporate Records Handbook, and LLC or Corporation? His books have shown over 500,000 businesses and organizations how to form a corporation or LLC. He also is a licensed helicopter pilot and a guitarist.

Table of Contents

Your Legal Companion for The Corporate Records Handbook

1. Corporate Documents and Laws

Organize Your Corporate Records

Your State Corporate Filing Office

Looking Up the Law Yourself

2. Meetings, Minutes, and Written Consents - How to Document Corporate Action

Three Ways to Document Formal Corporate Decisions

Questions and Answers About Meetings, Minutes, andWritten Consents

3. Before You Hold Your Meeting - Prep Work and Notice

Overview of Corporate Meetings

Steps to Hold a Meeting

4. How to Hold a Directors' or Shareholders' Meeting

Step 1. Call and Provide Notice of the Meeting

Step 2. Prepare Your Agenda

Step 3. Prepare Your Resolutions in Advance

Step 4. Gather for Your Meeting

Step 5. Hold a Virtual Meeting

Step 6. Appoint a Chairperson and Secretary

Step 7. Calling the Meeting to Order

Step 8. Do You Have a Quorum?

Step 9. Approve Minutes From Last Meeting

Step 10. Reports by Officers and Committees

Step 11. Introduce and Discuss Specific Proposals

Step 12. Take the Votes of Directors or Shareholders

Step 13. Handle Unfinished Business

Step 14. Adjourn the Meeting

5. Preparing Minutes for Shareholders' Meetings

Preparing Minutes for Annual Shareholders' Meetings

Preparing Minutes for Special Shareholder Meetings

6. Preparing Minutes for Directors' Meetings

Choosing the Correct Minutes Form

Preparing Minutes for Annual Directors' Meetings

Preparing Minutes for Special Directors' Meetings

7. Paper Meetings

When Is It Appropriate to Hold a Paper Meeting?

How to Prepare Minutes for Paper Meetings

8. Action by Written Consent

Step 1. Check Your Bylaws for Your Written Consent Rules

Step 2. Prepare the Written Consent Form

Step 3. Place Signed Consent Forms in Your Corporate Records Book

9. Resolutions for Authorizing Business Transactions

When to Use Business Corporate Resolutions

Bank Account Resolutions

Resolution to Adopt Assumed or Fictitious Business Name

Resolution to Approve a Contract

Real Property Resolutions

Authorization or Ratification of Employee's Authority

Certification, Affidavit, or Acknowledgment of Corporate Decision Making or Document

10. Corporate Tax Resolutions

S Corporation Tax Election

Accumulation of Earnings

Section 1244 Stock Plan

Resolution for Approval of Independent Audit

Selection of Corporate Tax Year

Resolution for Payment and Deduction of Corporate Organizational Cost

11. Resolutions for Amending Articles or Bylaws

Decide Whether to Amend Articles or Bylaws

Amending Your Articles of Incorporation

Amending Your Bylaws

12. Corporate Hiring and Appointment Resolutions

Hiring and Paying Corporate Employees

Using Independent Contractors

Appointing and Paying Corporate Officers

Compensation for Attending Meetings

Approval of Indemnification for Corporate Directors, Officers, and Employees

13. Conflict of Interest Resolutions

Approval of Business Between the Corporation and Its Directors

Resolutions to Approve Director Conflict of Interest Transactions

Resolutions for Shareholder Approval

14. Resolutions for Loans to the Corporation

When to Use Corporate Loan Resolutions

Loans by Banks and Other Lending Institutions

Loans by Shareholders and Other Insiders

Promissory Notes Overview

Sample Promissory Note Forms

15. Resolutions for Loans to Insiders

Insider Loan Restrictions Under State Law

Tax Considerations and Consequences of Insider Loans

Resolution for Approval of Corporate Loan to Insider

Supporting Documentation - Promissory Notes

Release of Promissory Note

16. Fringe Benefit and Reimbursement Resolutions

Introduction to Employee Fringe Benefits

Group Health, Accident, and Disability Insurance

Self-Insured Medical Reimbursement Plans

Resolution Authorizing Group Term Life Insurance

Authorization of Death Benefit Contract

Payment of Employee Automobile Expenses

Payment of Meals and Lodging

Resolution Authorizing Business Expenses With Corporate Credit or Charge Card

Reimbursement of Employee Business Expenses

Resolution Approving Stock Bonus or Stock Option Plan

17. Retirement Plan Resolutions

How to Use This Chapter

Overview of Corporate Retirement Plans

Resolutions to Adopt Retirement Plans

18. Stock Dividend Resolutions

Stock Dividend Rules

Stock Dividend Resolutions

19. Stock Issuance Resolutions

Legal and Tax Issues Affecting Stock Issuance

Stock Issuance Resolutions

20. Lawyers, Tax Specialists, and Legal Research

How to Find the Right Lawyer

Finding the Right Tax Adviser

How to Do Your Own Legal Research

Appendixes

A. Using the Interactive Forms and Other Online Material

Editing RTFs

Forms

B. How to Locate State Corporate Filing Offices and State Laws Online

How to Find Your State's Websites for Corporate Filing and Tax Information

How to Find Your State's Business Corporations Act Online

C. Corporate Minutes Forms

Notice and Minutes Forms

Meeting Summary Sheet

Call of Meeting

Meeting Participant List

Notice of Meeting

Acknowledgment of Receipt of Notice of Meeting

Proxy

Certification of Mailing

Minutes of the Annual Meeting of Shareholders

Minutes of Special Meeting of Shareholders

Minutes of the Annual Meeting of Directors

Minutes of Special Meeting of Directors

Waiver of Notice of Meeting

Approval of Corporate Minutes

Cover Letter for Approval of Minutes of Paper Meeting

Written Consent to Action Without Meeting

Standard Corporate Business Resolutions

Authorization of Treasurer to Open and Use Accounts

Authorization of Treasurer to Open and Use Specific Corporate Account(s)

Authorization of Corporate Account and Designation of Authorized Signers

Authorization of Rental of Safe Deposit Box

Adoption of Assumed Name

Board Approval of Proposed Contract

Approval of Lease

Purchase of Real Property

Authorization of Sale of Real Property

Delegation of Authority to Corporate Employee

Director Ratification of Employee's Acts

Board Ratification of Contract

Rescission of Authority of Employee

Shareholder Ratification of Decisions or Acts

Certification of Board or Shareholder Action

Affidavit of Corporate Decision Making

Acknowledgment

Corporate Tax Resolutions

S Corporation Tax Election

S Corporation Shareholders' Agreement

Accumulation of Corporate Earnings

Qualification of Shares Under Internal Revenue Code Section 1244

Approval of Independent Audit of Corporate Financial Records

Approval of Corporate Tax Year

Payment and Deduction of Organizational Expenses

Resolutions to Amend Corporate Articles and Bylaws

Approval of Amendment to Articles of Incorporation

Approval of Restatement of Articles of Incorporation

Amendment of Articles Form

Approval of Amendment of Bylaws

Corporate Hiring and Appointment Resolutions

Approval of Hiring of Corporate Employee

Approval of Bonuses and Salary Increases

Shareholder Ratification of Employee Pay

Approval of Independent Contractor Services

Appointment of Corporate Officers

Authorization of Payment for Attending Meetings

Annual Director or Officer Stipend for Attendance at Meetings

No Compensation for Attending Corporate Meetings

Indemnification and Insurance for Directors and Officers

Director Conflict of Interest Resolutions

Board Approval of Transaction Benefiting a Director

Directors' Written Consent to Transaction Benefiting a Director

Shareholder Approval of Transaction Benefiting a Director

Shareholder Written Consent to Transaction Involving a Director

Resolutions for Loans to the Corporation

Authorization of Loan at Specific Terms

Authorization of Maximum Loan on General Terms

Unlimited Authorization of Loans for Business Needs

Authorization of Line of Credit

Authorization of Line of Credit With Cap on Each Transaction

Authorization of Loan Terms Secured by Corporate Property

Resolution Approving Loan to Corporation

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

 Secured by Corporate Property

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

 With Balloon Payment

Promissory Note: Periodic Payments of Interest With Lump Sum Principal Payment

Promissory Note: Lump Sum Payment of Principal and Interest at Specified Date

Promissory Note: Lump Sum Payment of Principal and Interest on Demand

 by Noteholder

Promissory Note: Variable Schedule of Payments of Principal and Interest

Resolutions for Loans by the Corporation to Insiders

Approval of Corporate Loan to Insider

Promissory Note: Monthly Installment Payments of Principal and Interest

 (Amortized Loan)

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

 Secured by Property

Promissory Note: Installment Payments of Principal and Interest (Amortized Loan)

 With Balloon Payment

Promissory Note: Periodic Payments of Interest With Lump Sum Principal Payment

Promissory Note: Lump Sum Payment of Principal and Interest at Specified Date

Promissory Note: Lump Sum Payment of Principal and Interest on

 Demand by Noteholder

Promissory Note: Variable Schedule of Payments of Principal and Interest

Release of Promissory Note

Employee Fringe Benefits and Business Expense Reimbursement Resolutions

Authorization of Group Health, Accident, or Disability Insurance for Employees

Adoption of Self-Insured Medical Reimbursement Plan

Purchase of Group Term Life Insurance

Authorization of Employee Death Benefit

Agreement Regarding Death Benefits

Purchase or Lease of Company Car

Authorization of Payment of Standard Mileage Allowance to Employees

Business Meal Expense Allotment for Employees

On-Premises Meals and Lodging for Employees

Authorization of Corporate Credit and Charge Cards for Employees

Reimbursement of Actual Travel and Entertainment Expenses to Employees

 Under Accountable Reimbursement Plan

Reimbursement of Actual Travel and Entertainment Expenses to Employees

 Under Nonaccountable Reimbursement Plan

Authorization of Per Diem Travel Allowance for Employees

Board Approval of Stock Bonus or Stock Option Plan

Corporate Retirement Plan Resolutions

Board of Directors' Adoption of Retirement Plan

Board of Directors' Adoption of Profit-Sharing Plan

Shareholder Ratification of Retirement Plan

Stock Dividend Resolutions

Declaration of Cash Dividend

Authorization of Cash Dividend Payable in Installments

Declaration of Year-End Dividend

Declaration of Regular and Extra Dividend

Declaration of Accumulated Dividend to Preferred Shareholders

Authorization of Property Dividend to Shareholders

Stock Issuance Resolutions

Approval of the Issuance of Shares

Sale and Issuance of Shares for Property

Sale and Issuance of Shares for Indebtedness Canceled

Sale and Issuance of Shares for Services

Sale and Issuance of Capital Stock for Assets and Liabilities of a Business

Bill of Sale and Agreement

Issuance of Shares in Exchange for Assignment of Trademark,

Service Mark, Patent, or Copyright

Assignment

Issuance of Shares in Return for Cash and Promissory Note

Index

Sample Chapter

Chapter 1

Corporate Documents and Laws

Organize Your Corporate Records........................................................... 4

 Articles of Incorporation......................................................................... 4

 Bylaws................................................................................................... 6

 Minutes of Your First Directors’ Meeting............................................... 7

 Records Showing Stock Was Issued.................................................... 7

 Minutes of Meetings and Written Consents........................................... 8

Your State Corporate Filing Office............................................................ 8

Looking Up the Law Yourself.................................................................... 8

 Finding Your State Corporation Laws................................................... 9

 Look Up Relevant Corporate Statutes.................................................. 10

 Checking Other Laws........................................................................... 10

 When to Consult a Professional.......................................................... 10

Calling, providing notice for, holding, and voting at meetings of your directors and shareholders necessarily means becoming familiar with a bucketful of new terminology and procedures. While mastering this material isn’t difficult, it does require atten­tion to detail. In this chapter, we provide legal and practical background information about basic corporate documents and the state corporation laws on which they are based.

If you are well organized and feel you under­stand the purpose of your articles, bylaws, and minutes, much of the material in this chapter may seem like old hat. If so, you may wish to skip ahead to the next chapter where we present an overview of the common methods of corporate decision making, including corporate meetings and written consents.

Organize Your Corporate Records

Anyone who sets up a corporation needs to be able to quickly locate key organizational documents. Because these are really the constitution of your corporation, you’ll refer to them again and again. When using this book to produce corporate minute and consent forms, we will often refer you to these documents.

If you have not already done so, the best approach is to set up a corporate records book that contains the key documents. You can do this on your own with a three-ring binder or by using a customized corporate kit designed for the purpose.

Your corporate records book should contain:

• articles of incorporation

• bylaws

• minutes of the first directors’ meeting

• stock certificate stubs or a stock transfer ledger showing the names and addresses of your shareholders, as well as the number and types of shares owned by each

• minutes of annual and special meetings of directors or shareholders, if any, and

• written consents.

If someone helped you incorporate, such as a lawyer, accountant, paralegal, or financial planner, you probably received copies of these documents in a corporate records book, commonly called a corporate kit. However, some lawyers attempt to hold on to corporate records in the hope that you will have them take care of all ongoing technicalities. If so, you will need to request a copy of all corporate documents in your client file. (This is your property, so don’t take “No” for an answer.)

If you can’t locate a copy of your articles, write your secretary of state’s corporate filing office and request a certified or file-stamped copy of your articles. (See Appendix B for contact information.) It’s a good idea to call first so you can include the correct fee, which should be just a few dollars or so.

Articles of Incorporation

The first key organizing document all small business corporations must have is their articles of incorporation.(While most states use the term articles of incorporation to refer to the basic document creating the corporation, some states, including Connecticut, Delaware, New York, and Oklahoma, use the term certificate of incorporation. Washington calls the document a certificate of formation, and Tennessee calls it a charter.) A corporation comes into existence when its articles of incorporation are filed with the state corporate filing office. The articles normally contain fundamental structural information, such as the name of the corporation, names and addresses of its directors, its registered agent and his or her office address, and the corporation’s capital stock structure.

For the majority of small corporations, there is no other important information in this document. However, larger corporations sometimes adopt articles containing special provisions that impact future decision-making processes of the corporation.

The Importance of Protecting Your Corporate Status

A corporation is a legal entity that is created and regulated by state laws. For legal, practical, and tax purposes, a corporation is legally separate from any of the people who own, control, manage, or operate it. If you want the advantages of having a corporation, you must follow legal requirements for running it. If you don’t abide by the rules, you could find your business stripped of its corporate status—and the benefits of that status, such as:

• Limited liability. Corporate directors, officers, and shareholders usually are not personally liable for the debts of the corporation. This means that if the corporation cannot pay its debts or other financial obligations, creditors cannot usually seize or sell a corporate investor’s home, car, or other personal assets.

• Business taxes and flexibility. A corporation is a separate taxable entity. Business income can be sheltered in the corporation among the owner-employees as they see fit to reduce their overall tax liability.

• Employee fringe benefits. Owner-employees of a corporation are eligible for deductible fringe benefits, such as sick pay, group term life insurance, accident and health insurance, reimbursement of medical expenses, and disability insurance.

• Commercial loans and capital investment. Lending institutions often give the risk-conscious corporate lender special preferences. Corporations can decide to raise substantial amounts of capital by making a public offering of their shares.

• Business credibility. Corporations have an air of reputability about them. In other words, although placing an “Inc.” after your name will not directly increase sales, it forces you to pay serious attention to the structure and organization of your business, something that is likely to improve all aspects of your business.

• Perpetual existence. A corporation has an independent legal existence that continues despite changeovers in management or ownership. Of course, like any business, a corporation can be terminated by the mutual consent of the owners.

• Access to capital. Private and public capital markets prefer the corporate form over all other business forms, giving the corporation enhanced access to private and public capital. Public offerings can be made by means of a traditionally underwritten initial public offering (IPO) or a direct public offering (DPO) of shares by the corporation itself to its client or customer base.

Example:

The Equity Investors Capital Corporation adopts articles that contain a multiclass stock structure consisting of Class A voting shares and Class B nonvoting shares. A special article requires a vote of two-thirds of each class of stock for the approval of amendments (future changes) to the corporation’s articles or bylaws.

resource

Where to get help preparing articles for a new corporation. If you have not yet formed your corporation, you can create and file your articles online through Nolo’s Online Legal Forms at www

.nolo.com. Or, Nolo publishes several state-specific books and software that show you how to prepare and file articles and take other incorporation steps such as issuing stock under state securities laws. If you want to incorporate in California, see How to Form Your Own California Corporation (Nolo). In other states, see Incorporate Your Business (Nolo).You can also check your state’s corporate filing office for samples and instructions for drafting your own articles. Except in South Carolina, you do not need to involve an attorney. (Appendix B has information on how to find the corporate filing office in your state.)

Bylaws

The bylaws of a corporation are its second-most important document. You do not file bylaws with the state—they are an internal document that contains rules for holding corporate meetings and other formalities according to state corporate laws.

Bylaws typically specify the frequency of regular meetings of directors and shareholders and the call, notice, quorum, and voting rules for each type of meeting. They usually contain the rules for setting up and delegating authority to special committees of the board, the rights of directors and shareholders to inspect the corporate records and books, the rights of directors and officers to insurance coverage or indemnification (reimbursement by the corporation for legal fees and judgments) in the event of lawsuits, plus a number of other standard legal provisions.

tip

Use bylaws for common or changeable rules. State law often gives corporations a choice as to whether to place corporate operating rules and procedures in the articles of incorporation or bylaws. If you have a choice, it’s always best to use the bylaws, because you can change them easily without the need for filing changes with the state. For example, many states allow you to place supermajority quorum or voting rules for directors’ or shareholders’ meetings in either document. If you use the bylaws for this purpose, you can more easily change these provisions because less stringent vote requirements normally apply to the amendment of bylaws. In contrast, if you need to change provisions in your articles, a formal amendment to the articles must be filed with your state’s corporate filing office.

Because the corporation laws of all states are subject to change, it’s possible that bylaws that were valid when adopted will later go out of date. Fortunately, major changes to corporate laws happen only every decade or two, when states modernize their corporate statutes. Nonetheless, if your corporation has been in existence for a few years and you plan a major corporate decision such as the issuance of a new class of shares, declaration of a dividend, or purchase of shares from a shareholder, it’s wise to make sure your bylaw provisions are up-to-date by checking your state’s current business corporation act.

resource

Where to get help preparing bylaws. Some corporations may have been formed in a hurry, by filing articles of incorporation only. If that is your case, you need to take the extra step of preparing basic bylaws for your corporation. Again, if your corporation was formed in California, you can use How to Form Your Own California Corporation (Nolo) to prepare state-specific bylaws for your corporation. For any other state, see Incorporate Your Business (Nolo).

Minutes of Your First Directors’ Meeting

When most businesses incorporate, they prepare minutes of the first meeting of the corpo­ration’s board of directors or of the incorpo­rators (the person or persons who signed and filed the articles on behalf of the corporation). This meeting is usually referred to as the organizational meeting of the corporation. Minutes are simply a formal record of the proceedings of a meeting. The organizational meeting is usually held to approve standard items of business necessary for a new corporation to begin doing business.

Look through the minutes of your organizational meeting. These minutes are designed to document the essential organizational actions taken by the board or the incorporators. They typically show:

• the beginning tax elections made by the corporation—for example, the selection of the corporation’s accounting period and tax year

• details of the corporation’s first stock issuance

• approval of stock certificates and a corporate seal, and

• approval of other beginning business of the corporation, such as the opening of a corporate bank account.

Knowing some of this information may be essential to making informed corporate decisions later.

tip

Don’t worry if you don’t have organizational minutes. Some corporations, especially those created in a rush, simply didn’t prepare minutes of the first meeting of the board of directors or incorporators. If you don’t have these minutes, you can recreate them as explained in “Using Paper Meetings to Create Records for Prior Undocumented Meetings,” in Chapter 7.

Records Showing Stock Was Issued

A new corporation almost always issues stock to record the ownership interests of the persons who invest in the corporation. Most smaller corporations issue stock for cash, property, or the performance of services that were rendered in forming the corporation. Many states prohibit the issuance of shares in return for a promise to pay for the shares later (in return for a promissory note) or for a promise to perform future services. If a small existing business is being incorporated, the business owners are normally issued shares in return for the transfer of business assets to the new corporation.

Example:

Just Friends, a partnership, incorporates as Just Friends, Inc. Each of the three prior business owners owned an equal one-third interest in the partnership. After the transfer of the partnership assets to the corporation, each owner is issued one-third of the shares issued by the corporation (3,000 shares are issued, so each owner receives 1,000 shares in the new corporation).

If you haven’t issued stock or didn’t keep written records showing who owns shares, you should do so now. Stock certificates and stock transfer ledgers are available in most office supply stores.

Once you’ve organized your corporate records book, remember that while a corporate records book makes it easy for you to keep all key documents in one place, it won’t work unless you consistently use it.

Minutes of Meetings and Written Consents

If your corporation has been in existence for some time, you may have records of annual and perhaps special corporate meetings. This is especially likely if a lawyer helped you incor­porate. Check your corporate records, or contact your attorney if you don’t have copies. Again, remember that you have a right to these records.

Your State Corporate Filing Office

Each state has a corporate filing office where you pay a fee and file paperwork for creating corporations, changing the corporate structure, and dissolving corporations.

Information on how to find your state corpo­rate filing office is provided in Appen­dix B. The 50 different states use slightly different names for the office where corporate filings are made. Most commonly, corporations are formed with and supervised by the secretary of state or department of state office. The depart­ment within this bureaucracy that handles corporate filings is commonly designated as the corporations division or corporations department.

Corporation filing offices are sometimes further divided into offices that oversee special areas of concern, such as corporate filings (for example, articles of incorporation or amend­ments to articles), corporate name availability, corporate fee information, and corporate legal counsel. Don’t be put off by this seeming structural complexity. If you need information, check your state’s corporate filing office website. Also, you’ll normally find there is one phone number at the corporate filing office devoted to hand­ling corporate inquiries from the public.

Throughout this book, we refer to the office that accepts corporate filings as the state corporate filing office, whether this office is formally designated as the secretary of state office or by some other title.

Your State’s Corporate Filing Office Website

Check your state’s corporate filing office website for sample forms and other useful information about forming or operating a corporation in your state. Most states have sample articles of incorporation and other forms that you can download or, in some cases, fill in and file online. Many of the state websites also contain links to your state’s corporate tax office (for tax forms and information) and state employment, licensing, and other agencies. See Appendix B for information about how to locate your state corporate filing office website.

Looking Up the Law Yourself

In addition to the rules and procedures set out in corporate articles and bylaws, the organization and operation of a corporation are tightly regulated by a good-sized pile of laws adopted by each state. The primary source of laws that apply to your corporation will be found in your state’s corporation laws (statutes), often titled the Business Corporation Act or designated with a similar name. Legal citations to sections of a state’s business corporation laws are often listed in the following form: “Sec. 21.2 of the Business Corporation Act” or “Article 2-12, BCA.”

Some readers may be reluctant to venture into what they see as the musty or mysterious realm of corporate law research. To be sure, legal research of any type may seem daunting or dry, and corporate statutes are not always models of clear, concise (let alone friendly) language. Nonetheless, be reassured: Looking up corporate rules is not akin to doing your own appendectomy. Corporate statutes are organized by subject matter and are well indexed and cross-referenced. For the most part, the statutes themselves state a fairly simple rule or requirement that, despite the inevitable lawyer jargon, can be comprehended by the average reader.

Most small business people can’t afford to pay a lawyer upwards of $400 per hour every time they want access to basic legal information or help handling ongoing legal formalities and procedures. That’s why we explain the importance of locating an experienced small business lawyer who is willing to act more like a legal coach, rather than a legal representative. (See Chapter 20.) For now, it’s important to know that you can often look up the law yourself, without having to consult, and pay handsomely for, outside legal assistance.

Finding Your State Corporation Laws

Many routine state legal rules, such as those for holding and voting at meetings, obtaining director or shareholder written consent to action without a meeting, and conducting ongoing corporate business, are restated in your articles of incorporation and bylaws. Nevertheless, there may be times when you will want more detail on your state’s corporation statutes.

Once you locate your state’s corporate statutes, it usually takes only a minute or two to find a relevant corporate law requirement or procedure, or to satisfy yourself that one does not exist.

The Model Business Corporation Act

The basic corporate statutes of many states contain the same, or quite similar, rules for organizing and operating business corporations. The reason for this uniformity is that a number of states have adopted some, most, or all of the provisions of a standard law: the Model Business Corporation Act. The act undergoes periodic changes, and states are free to enact it in modified form.

The following states have enacted most, or a substantial portion, of the provisions of the Revised Model Business Corporation Act:

Arkansas Mississippi Tennessee

Florida Montana Virginia

Georgia North Carolina Washington

Indiana Oregon Wisconsin

Iowa South Carolina Wyoming

Kentuck

To find your state’s corporation laws, you can use any of these four easy methods:

• Check your state’s corporate filing office website. Many states provide an online version of their business corporation act (or similarly titled corporation laws). Appendix B provides information on how to find your state corporate filing office website.

• Look up your state’s corporations laws using Nolo’s State Law Resources page at www.nolo.com/legal-research/state-law.html (under “Legal Research,” then “State Law Resources”).

• Type “<your state’s name> Corporation Act” or “<your state’s name> corporation laws” into your browser’s search box. This usually leads to a link to your state’s business corporation act.

• Visit a local law library, a law school library that is open to the public, or a large public library with a substantial business collection. Ask the research librarian for help looking up your state’s business corporation act.

Look Up Relevant Corporate Statutes

To start, you can browse through the table of contents at the beginning of your state’s corporation act or the mini table of contents often located at the beginning of each section heading in the act. Each heading covers major areas of corporate operation or procedure (for example, Corporate Formation, Meetings, Stock Issuance, Corporate Officers, Records and Reports, and the like). Major headings are further broken down into subheadings and sections that treat specific matters, such as Articles of Incorporation, Bylaws, and Director and Shareholder Meetings.

Or, you can usually do a search to find the statute you’re interested in by entering a few key terms.

Checking Other Laws

In addition to a state’s Business Corporation Act, other state laws regulate special areas of corporate activity. These include:

Securities Act or Blue Sky Law. These laws contain each state’s rules and procedures for offering, issuing, selling, and transferring shares of corporate stock and other securities. (The term blue sky law was derived from the sometimes underhanded, and often colorful, practices of corporate con artists who, in return for a small investment in their latest get-rich-quick undertaking, would promise the blue sky to unsuspecting investors. The securities laws of each state attempt, through stock offering qualification and disclosure requirements, to tone down the picture painted by stock promoters to a more realistic hue.)

Tax or Revenue Code. If a state imposes a corporate income or franchise tax, the state’s tax or revenue code will typically contain these provisions.

Commercial Code. The state’s commercial code contains the rules for entering into and enforcing commercial contracts, promissory notes, and other standard commercial documents.

Other state and local laws. Various state laws may impact the activities and operations of all businesses, whether or not they are incorporated. For example, state and local building codes, professional and occupation licensing, and other laws and regulations may apply to your business and its operations.

When to Consult a Professional

Holding corporate meetings and preparing standard resolutions and other corporate paperwork are usually routine tasks for corporations. However, if the decision you are facing is complex, you anticipate any complications or objections, or you simply have questions and need more information, consult with a tax or legal specialist before using the forms in this book. A consultation of this sort will be far more cost-effective than making the wrong decision and having to fix it later. Besides, the fees you incur should be relatively low, since you’re not handing all the paperwork to the lawyer or tax person to do for you. For information on choosing and using a legal or tax professional to help you with ongoing corporate decisions and documentation, see Chapter 20.

Forms

This Book Comes With a Website

Nolo’s award-winning website has a page dedicated just to this book, where you can:

DOWNLOAD FORMS - All forms in this book are accessible online. After purchase, you can find a link to the URL in Appendix A.

KEEP UP TO DATE - When there are important changes to the information in this book, we will post updates

And that’s not all. Nolo.com contains thousands of articles on everyday legal and business issues, plus a plain-English law dictionary, all written by Nolo experts and available for free. You’ll also find more useful books, software, online services, and downloadable forms.