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PubPol 671: Policy & Management in the Nonprofit Sector
Lecture 4: Legal and Regulatory Overview

Neel Hajra
Report from the Field

- Citizens United vs. F.E.C.
  - Bars limits (via PAC rules) on express advocacy and electioneering communications
  - Impact on nonprofit sector?
Report from the Field

- Lee: Replicating the Harlem Children’s Zone
Notes

- First paper assignment will be posted by this weekend (see lecture 2 slides for general options)
Recap of Previous Class

- Economic: Three Failures Theory
- Political Theories
- Re-Valuing the Sector
# Re-Valuing the Sector: Rankings!

<table>
<thead>
<tr>
<th>Group</th>
<th>All</th>
<th>Some</th>
<th>None</th>
</tr>
</thead>
<tbody>
<tr>
<td>4. Social Services</td>
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<td>1</td>
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<tr>
<td>8. Philan. Intermediaries</td>
<td>3</td>
<td>1</td>
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<tr>
<td>9. International</td>
<td>3</td>
<td>1</td>
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<tr>
<td>10. Religion</td>
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<td>1</td>
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<tr>
<td>5. Environment</td>
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<td>2</td>
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<td>6. Housing/Devel</td>
<td>2</td>
<td>1</td>
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<tr>
<td>2. Education / Research</td>
<td>1</td>
<td>3</td>
<td></td>
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<tr>
<td>7. Law / advocacy / politics</td>
<td>1</td>
<td>3</td>
<td></td>
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<tr>
<td>1. Culture/Rec</td>
<td></td>
<td></td>
<td>4</td>
</tr>
<tr>
<td>3. Health</td>
<td>3</td>
<td>1</td>
<td></td>
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<tr>
<td>11. Biz, prof. associations</td>
<td>3</td>
<td>1</td>
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</table>
Re-Valuing the Sector: Reasons!

<table>
<thead>
<tr>
<th>#</th>
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<tbody>
<tr>
<td>16</td>
<td>Market Failure</td>
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<tr>
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<td>Experimentation</td>
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<tr>
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<td>Historical</td>
</tr>
<tr>
<td>14</td>
<td>Diversity / Pluralism / Freedom</td>
</tr>
<tr>
<td>13</td>
<td>Subsidies</td>
</tr>
<tr>
<td>12</td>
<td>Government Failure</td>
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<td>10</td>
<td>Free Riders</td>
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<td>9</td>
<td>Categorical Constraint</td>
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<tr>
<td>7</td>
<td>Consumer Control</td>
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<td>6</td>
<td>Political</td>
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<tr>
<td>5</td>
<td>Solidarity</td>
</tr>
<tr>
<td>1</td>
<td>Voluntary Failure</td>
</tr>
</tbody>
</table>
Knight Foundation Article from last class

- Collapse of “traditional” media, reformation within nonprofit sector
- What does this reveal about the role of the nonprofit sector?
This Class

- Understand the general legal framework for domestic nonprofits
- “Kitchen sink” approach!
Why Important?: Management

- Operating in compliance with law
- Understanding rights and limitations
- Effecting policy reform
Why Important? Enforcement

Just some of the ways around non-distribution…

- Nonprofit Capital
- Partnerships
- Non-Arm’s Length Transactions
- Compensation
- Solicitation

Neel Hajra
Regulatory Pathway

- State: Corporate form
- Federal: Federal tax exempt status – 501(c)(3)
- State: State tax exemptions
- Local: Property tax
- 501(c)(3) nonprofit is a state nonprofit corporation with federal tax exempt status
Corporate Form

Public

- Board of Trustees
- Executive Director
- Staff & Volunteers

corporation
Recap: Benefits of Corporate Form

- Limited liability
- Perpetual existence
- Employee benefits
- Formality and structure
- For state: regulation!
Next: State Regulation
State Corporations Acts

- Nonprofit corporation created under state law
- Variance from state to state, but no major disparities
Articles of Incorporation

- Basic characteristics
- Filed Articles = corporation created
- Standard Articles for Michigan
Articles of Incorporation

- Name
- Mission
- Basis, Assets, Budget, Governance
  - Non-stock vs. Stock
  - Simple assets & budget
  - Directorship vs. Membership
Articles of Incorporation

- Location of Office
- Incorporators
- (extra) Include IRS restrictions
- (extra) Protect board & volunteers

Note –
- indemnity, nonprofits, risk management
Bylaws

- Internal regulation and management
- Adopted at first meeting by the new board
Bylaw requirements and recommendations (for MI)

- **Purpose:** “As stated in the Articles of Incorporation.”

- **Number of Directors:** Must have three. Recommend at least five.

- **Term for Directors:** Must be at least one year. Recommend at least two years and staggered terms.

- **Board Meetings:** Must be at least annual; recommend monthly during first year.
Bylaw requirements and recommendations (for MI)

- **Officers**: Must have President, Secretary, and Treasurer. Recommend Vice-President as well.

- **Quorum**
  - Must have at least a majority when Board is < 7
  - Must have at least 1/3 when Board is seven+
  - Recommend majority
Director Fiduciary Duties

- Loyalty
- Care
- Confidentiality

(much more about this in Lecture 6)
Charitable Solicitation License

- Required by every state
- Based on amount requested, not amount received
- One year licenses
Attorney General

- Main agent for enforcing nonprofit regulatory compliance
- Often lax and/or uncoordinated regulation
Next:
Federal Regulation
Internal Revenue Code

- Section 501c is primary section for nonprofits
- 501(c)(3) is for charitable nonprofits
- Within 501(c)(3):
  - Private foundation
  - Public charity
Organizational Test

- Articles of Incorporation
  - Exempt purpose
  - Assets irrevocably pledged to charitable causes
Operational Test

- Engaged primarily in exempt purpose activities
- Unrelated activities must be “insubstantial”
Unrelated Activity

- “Commercial”
- UBIT
- Exceptions
  - Voluntary work
  - “convenience” businesses
  - Sales of donated goods
  - Etc.
Public Charity Qualification: Four Ways to Qualify

- Automatic
- Publicly Supported Organization
- Public Support Test
- 1/3 Qualified Support
- 1/10 Qualified Public Support + Attraction of Public Support

Very important to be cognizant of this rule, especially for young nonprofits
**Automatic qualification:** Churches, institutional schools, hospitals/medical research organizations, public safety organizations, governmental organizations, supporting organizations
Public charity test 2a

- 1/3 of total support from “qualified support”
- “Qualified support” – includes no more than 2% of total income from any single donation
- Exceptions for large single donations, “unusual grants”, and donations from publicly supported groups
Public charity test 2b

- 1/10 of total support from “qualified support”

- “Attraction of public support” considers number of factors: Continuous solicitation of funds (required), percentage of support, support from representative group, representative governing body, availability of service to public, held accountable by other public funders
Public charity test 3

Normally receive 1/3 of support from combination of:

- Qualified support and
- Gross receipts from activities related to exempt purpose
Reich: “Anything Goes”

- 99% approval rate!
- What does this say about:
  - Standards?
  - Regulation & Oversight?
  - Bureaucracy?
Lobbying

- “Not substantial”
- Issues vs. Legislation
- 501(h) - clear standard!:
  - 20% of the first $500,000
  - + 15% of the next $500,000
  - + 10% of the next $500,000
  - + 5% of the remaining
  - = the overall lobbying limit
Elections

- Bright line prohibition!

- (have you seen violations of this?)