



Colorado  
NONPROFIT  
Association

## STARTING A NONPROFIT ORGANIZATION

Thank you for your inquiry to the Colorado Association of Nonprofit Organizations, a state-wide coalition of over 1,200 charitable nonprofits operating in Colorado. We are happy to share the enclosed materials and resources to help you think through starting a nonprofit organization. Remember, starting a nonprofit is not a decision to take lightly. You may want to research existing nonprofits to see if there is already a group working on the same issue or providing similar programs and services.

This *Nonprofit Start-up Information* was put together by Colorado Nonprofit Association, Metro Volunteers! and the Community Resource Center. It outlines the basic steps in forming a nonprofit and provides guidance on the costs involved and the amount of time needed to complete the process.

### **COLORADO NONPROFIT ASSOCIATION**

455 Sherman St. Suite 207 Denver, CO 80203  
(303) 832-5710

Colorado Nonprofit Association's web site [www.ColoradoNonprofits.org](http://www.ColoradoNonprofits.org) has a section on **Help Desk FAQs** (Frequently Asked Questions). We encourage you to use this section to answer basic questions and find resource links for information on all areas of nonprofit governance and management.

### **The Community Resource Center (CRC)**

655 Broadway, Suite 300, Denver 80203  
(303) 623-1540

The Community Resource Center offers programs to help explore the issues involved in starting a nonprofit. One-on-one consulting and technical assistance is available on a fee basis to guide you through the process. CRC offers other courses of interest to nonprofits and publishes the Colorado Grants Guide.

### **The Colorado Nonprofit Development Center (CNDC)**

4130 Tejon Street, Suite A, Denver 80211

(720) 855-0501 assists emerging charitable groups by providing them with management services and guidance in developing best practices.

### **The Colorado Springs Center for Nonprofit Excellence**

518 North Nevada Avenue, Colorado Springs, CO 80903

(719) 575-4941 provides information for Pikes Peak area nonprofits on the basics of starting a new nonprofit.

They have a complete kit of forms and information available for \$25.00. CSCNE also provides other services including consultations for nonprofits in the area.

### **Metro Volunteers!**

444 Sherman St. Suite 100, Denver 80203

(303) 561-2300 offer many courses on management, direction, and technical skills of use to nonprofits.

We have enclosed membership information about Colorado Nonprofit Association, which is open only to 501(c)(3) nonprofits. Until you obtain your tax-exempt status, you may wish to join Colorado Nonprofit Association's *Business Members* program which is open to individuals and for-profit business, and which gives you all member discounts and a newsletter subscription. We hope you find this information helpful. Please feel free to contact Colorado Nonprofit Association, CRC, CNDC, CSNC or Metro Volunteers! with additional questions or to take advantage of our many programs and products.



## Nonprofit Start Up Information

[501(c)(3) charitable organizations]

*Nonprofit organizations provide a needed service to the community. The IRS recognizes many classifications of nonprofit organizations under the Internal Revenue Code ranging from 501(c)(1) to 501(c)(25). The classification 501(c)(3) is for organizations that provide a charitable service to the community (see "What is a 501(c)(3) Nonprofit Organization" below). The following information is useful to individuals who are considering starting a 501(c)(3) tax-exempt organization in the state of Colorado.*

### What is a 501(c)(3) nonprofit organization?

501(c)(3) organizations must be established and operated for one or more of the following purposes: religious, charitable, scientific, testing or public safety, literary, educational, fostering national or international amateur sports competition, or prevention of cruelty to children or animals. A 501(c)(3) (charitable) nonprofit is a type of organization that qualifies for exemption from federal income tax under section 501(c)(3) of the Internal Revenue Code. In general, no part of the income of a nonprofit organization may be distributed to its members, directors, or officers. Nonprofits are not prohibited from making a profit, only from distributing the net income. Contributions, for which no benefit is received, made to a 501(c)(3) organization, are tax deductible.

### Do I have any other options besides forming a new 501(c)(3)?

A group of individuals may wish to start a nonprofit organization because they have identified a need(s) in the community which is not currently being addressed. It is not always necessary, however, to form an independent 501(c)(3) corporation. Numerous nonprofit organizations already exist across the state (over 13,000 identified in COLORADO NONPROFIT ASSOCIATION's *2000 Directory of Colorado Nonprofits*!). These provide a broad spectrum of programs and services to meet the needs of special populations or constituencies, e.g., elderly, domestic violence, animal rights, etc. One of the best alternatives to the formation of an independent organization is to contact a nonprofit that is currently providing services to the group or groups which your concerns impact. They may be willing to add a program which will provide the service to meet the need(s) you have identified. Likewise, they may already have the service, track-record and philanthropic relationships established which will allow them to obtain funding for that program. Traditionally, newly established 501(c)(3) organizations find that securing the limited available funds is extremely difficult. It's the old chicken before the egg theory...you often can't get funding to operate without having already been in operation and funded.

If you determine that you do need to incorporate your own organization and apply with the IRS for your 501(c)(3), there is an ongoing obligation to keep accurate financial records, file local, state, and IRS forms annually or as required, be a separate employer, and establish a variety of other practices which are necessary to run an organization. It is also essential to develop an accurate financial accounting system as soon as possible after filing your applications.

### What is the tax exempt 501(c)(3) process?

There are two steps in becoming a 501(c)(3) nonprofit corporation: One, incorporating (applying to become a corporation) in the state of Colorado and, two, filing for income tax exemption from the IRS.

#### Step one:

One or more persons may incorporate in the State of Colorado by signing and delivering or mailing articles of

incorporation in duplicate to the Colorado Secretary of State's office located at 1700 Broadway, Suite 200, Denver, CO 80202 or by e-filing them in the Business Center section of their website at [www.sos.state.co.us](http://www.sos.state.co.us). The fee for paper filing your articles is \$125, the fee for e-filing is \$25. If the articles of incorporation conform to the law and all necessary fees have been paid, they will be filed and a certificate of incorporation will be issued. If you take them to the Secretary of State's office, the staff will ensure that the name your organization has chosen is not being used by anyone else. You may also check your name on the web site, [www.sos.state.co.us](http://www.sos.state.co.us)

For an additional fee, you can receive a Certificate of Good Standing and a copy of the Articles of Incorporation if needed. The incorporation takes 7-10 business days and then the information is available on the state's website. Visit the Fees Schedule section of the Business Center on the Secretary of State website.

This incorporation does not make an organization exempt from income tax--that is done by filing for tax-exempt status with the IRS (see step two).

**Note:** It is important that the requirements of both the state and federal government are met in the contents of the articles of incorporation. The federal government requires that additional information not required by the state be included. If this is not done at the time of the original state filing, the articles will have to be amended before filing with the IRS for tax-exempt status.

## Step two:

The second step is filing form I023 (Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code) with the IRS and a variety of other materials such as articles of incorporation, bylaws, and budgets along with the nonrefundable IRS filing fee (see "What expense is involved?").

You can call 800-829-3676 or visit the IRS web site [www.irs.gov](http://www.irs.gov) or go to your local office to get your forms. In Denver the main IRS office is located at 600 17<sup>th</sup> Street at Welton (downtown) in the north Tower building on the 12<sup>th</sup> floor.

**Note:** Bylaws do not have to be filed with the state for purposes of incorporation, but a copy of bylaws as well as articles of incorporation must be filed with the IRS with the application for 501(c)(3) (income tax-exempt) status. They are the internal operating rules of your organization and they set up in advance the rules by which the organization must operate.

You will need the following forms:

- Form SS-4, the form to file for your federal Employer Identification Number (EIN) Fill this form out and fax it to the IRS office in Ogden, Utah at 801-620-7115 along with a letter asking to receive an EIN within five days. Call 801-620-6755 if you don't receive it within the five days. You need this before you can submit your application.
- Form I023, the primary form for applying for 501(c)(3) status. This package should also include Form 872-C which you will need for your application. Fill out the application before you read the guidelines; then refer to them for those questions you find confusing. Prior reading tends to create doubt and confusion about the application.
- Form I023 Guidelines, a packet of instructions that you will use selectively.
- Form 8718, which you will need to determine your application fee.

## What expense is involved?

You may prepare your own articles of incorporation and bylaws, as well as complete form I023, using the information and forms contained in this start-up packet, or through other resources. There are lawyers who can do a good deal of the application process for you, but it will be expensive. You should, however, have all of these documents reviewed

by an attorney and/or public accountant who specializes in nonprofit incorporation, prior to submitting them to either the state or federal government, to ensure that they are in compliance with all state and federal regulations. In addition, it is not always easy to determine whether the proposed purpose and/or activities of the organization will be eligible: you may need to seek the advice of an accountant or attorney who is familiar with nonprofits to determine this.

- \$25 or \$125 fee for state incorporation
- \$150 or \$500 (as of 01/01/00) non refundable IRS filing fee
- Lawyers and/or accountant fees

Total cost averages \$550 to \$5000

The amount of the fee required to file for tax-exempt status with the IRS is based on projected annual gross receipts for the first four years of the organization's existence: if less than \$10,000, the filing fee is \$150; if more than \$10,000, the filing fee is \$500. This fee is not refundable, even if tax-exempt status is denied. In addition, it is recommended that you have a lawyer and/or public accountant review the material prior to submitting it to the appropriate agencies. The cost for an attorney's and/or accountant's services will vary, depending on the amount and accuracy of the paperwork you provide, as well as their individual fee schedules.

## How long does the process take?

Depending on the form of payment of the state incorporation fee, it will take approximately seven to ten days for the Articles of Incorporation to be posted on the state's website. Once form 1023 is filed with the IRS, it can take from 2 to 6 months for you to receive a response and your first response may be to ask for additional information. Always respond as quickly as possible, certainly within the 20 days you are generally given.

**Note:** Remember if you file within 15 months of receiving your state incorporation (27 months with an extension filed) your 501(c)(3) status will be given retroactive to the date of the incorporation.

## What else do I need to know?

First and foremost you need to ensure that your organization will not be perceived as "duplicating service"--that is, offering a service that is already being provided by another nonprofit. Given the number of operating nonprofits, particularly in metropolitan areas, it is likely that an organization is already providing programs which address the concerns you have. Establishing a nonprofit to provide a service that is already provided by an existing organization will be frustrating when it comes to raising funds. Funds for nonprofit organizations are limited and the funding community also prioritizes what it feels are the most critical needs. By the same token, fundraising will also be difficult if the service provided by your organization is not perceived as a critical need by the funders.

Next, be sure that you and others involved with the organization have the time and energy needed to commit to the start-up of a nonprofit. The original Board of Directors must be able to give of their time, money, and expertise. Infant nonprofits are normally staffed by volunteers until such time as funding is secured to compensate employees. In addition, members of nonprofit boards of directors have a legal responsibility to ensure that an organization is not mismanaged.

Obtaining a letter of tax exemption from the IRS entitles your organization to pay no income tax. Exemption from sales tax and property tax is not included and must be obtained separately from the state and city (sales tax) by filing the required paperwork. It is also important to remember that being a tax-exempt organization does not exempt you from filing the appropriate tax returns and there are substantial penalties for failing to do so.

A final note about conflict of interest issues. Nonprofit organizations cannot be established for the private benefit of

any individual. Founders may be employed by the organization as staff members, but the nonprofit must be created for the purpose of improving the public welfare and not as a way to avoid paying taxes or to funnel money to specific people. If you have any doubts about this issue, please consult the attorney with whom you are working. There must also be a clear separation between existing for-profit and nonprofit organizations. When serving in the capacity of directors and officers, individuals' first loyalty should be to the nonprofit organization and its mission.



## **Starting Up Without Stalling**

by Marilyn Dickey

The Chronicle of Philanthropy, April 3, 1997, pg. 33-35

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**When Ruth Libby of Scarborough, Me., sent her son to kindergarten, she knew it would be a big moment for him. But she hardly expected that it would transform her into a non-profit entrepreneur. One day after her son brought home a note from his teacher, urging parents to contribute household items to stretch the school's budget for special projects. With that simple request, the seeds for a new group called Ruth's Reusable Resources, or the 3R's, were planted.**

**Ms. Libby started out by giving her son egg cartons, scraps of yarn, empty canisters from 35-millimeter film, and many other items to take to school. She encouraged friends and relatives to do the same.**

**But she didn't stop there. She went to local businesses to solicit donations. The UNUM Corporation, an insurance company in Portland, Me., contributed used binders, paper clips, filing cabinets, and old computers. Falcon Rule in Auburn, Me., furnished cartons of slightly defective rulers. With so many supplies to give away, Ms. Libby soon found herself knee-deep in school supplies and inundated with requests from teachers all over town.**

**UNUM was so pleased that it no longer had to spend time and money seeking ways to send its cast-offs to charity, that a year ago it offered to provide Ms. Libby the money she needed to turn her information project into a charity. So far the company has provided \$19,000 and is now deciding whether to give her more money.**

**Ms. Libby has made many strides toward making her non-profit group more official. She has formed a board of directors, hired one part-time employee, and is ready to apply to the Internal Revenue Service for charity tax status.**

**Working from an abandoned school building, she now has enough donated supplies to fill the gymnasium, cafeteria, four classrooms, and even the restrooms. She estimates that her group has saved the Scarborough school system about \$58,000 this past year.**

**While that success has pleased Ms. Libby, she still has a long way to go. She says she has to spend so much time collecting and distributing goods that she has had few spare moments left over to learn about the ins and outs of becoming a full-fledged non-profit organization.**

**Experts say frustrations like those experienced by Ms. Libby are common among the tens of thousands of groups that get started every year. Following are recommendations on ways to avoid the most common stumbling blocks:**

**Conducting extensive research. The biggest mistake organizers make is failing to figure out whether a new charity is really needed, says Jon Pratt, executive director of the Minnesota Council of Nonprofits. He says it is wise to ask as many people as possible whether the mission proposed new**

**group is already being accomplished-or if it could be carried out by existing charities, by government agencies, or by businesses.**

**For instance, he says, in recent years an increasing number of local groups have formed to help people in a specific country or region abroad. If somebody wanted to form a committee in Cincinnati to help people in Afghanistan, he says, he would urge the organizer to ask, "Are there enough people in the Cincinnati area who are concerned about that topic, and does it make sense?" He says if the answer is No, he would urge the organizer to find a national or international organization that he or she might want to join.**

**Choose an appropriate board. A typical board of directors has 15 to 20 members, says Rick Moyers, communications director at the National Center for Nonprofit Boards, but not all charities need to follow that standard.**

**Mr. Moyers advocates keeping boards as small as possible. "If you have too many people," he says, "it becomes diffused and no one really feels responsible for it. It can be difficult to have a meaningful discussion among a group of 30 people. And if you have a board of 30 or 40 or 50 people, each time it comes together, it's such a different group that it can be hard to maintain continuity."**

**The initial board is almost always formed by people who are most committed to the charity's cause, and is usually a hands-on group, in charge of both governing and administration.**

**Once the charity is established and hires a director and adds staff members, the board's composition will probably change and the members will spend more of their time on oversight and less on administration. That often leads some members to drop out and gives charities an opportunity to figure out what their boards are missing. In many cases, experts say, boards of young charities lack enough members with financial expertise, experience in the charity's program area, or strong ties to local businesses, civic groups, and other organizations.**

**Judy Fox is coordinator of Women in Transition, a program that helps female jail inmates in Rhode Island. The people who were on her advisory committee are the ones who formed the initial board when the group sought official charity status two years ago. "They were leaders in the community, and they had already bought into the program, so I wanted to keep them involved," she said.**

**Having a dedicated board made a crucial difference in helping her group get off the ground, says Ms. Fox, and its members brought with them experience in important areas such as grant-proposal writing. But a year from now, she says, she would like to have some new faces on the board.**

**"We definitely have holes in terms of expertise like accounting," she says, "and we're trying to fill those holes."**

**Create a mission statement. Before an organization takes the legal steps to become a charity, it should craft a mission statement that explains the group's goals. Many groups use those phrases in their articles of incorporation and bylaws-which means that donors, watchdog groups, and government oversight agencies will measure a charity's performance by its ability to prove that it has strived to carry out its mission.**

**The mission statement should clearly articulate the charity's purpose and why it exists. The statement should also elaborate on the values, beliefs, and assumptions of the non-profit organization, as well as on the kinds of people it hopes to serve, lawyers and charity leaders say.**

**However, they say it is not wise to get too explicit about what services and programs a charity will offer, since those often need to be adapted to meet changing needs of the organization and its constituents. Even so, they say, it is wise to periodically review the mission statement and make sure it is up to date.**

**Keep up with the legal paperwork. Groups need to take two separate steps to win legal authority to operate as tax-exempt charities. They must become legally incorporated and they must apply to the Internal Revenue Service for charity status. Until a charity is incorporated, its directors and officers can easily be sued as individuals if something goes wrong. Once a group is incorporated, the organization is more likely to be sued than are the individuals involved in it.**

**Experts say incorporating a charity brings other advantages too: It helps prevent others from using the same name and suggests that a group plans to be around for a long time.**

**However, being incorporated doesn't make an organization exempt from taxation. That requires applying to the I.R.S. "A lot of non-profit groups file articles and just kind of let the rest go," says Anthony Mancuso, a California lawyer who wrote the book *How to form a Nonprofit Corporation*. "then if they're audited, the I.R.S. can look back at all those prior years and say, 'Hey, you weren't exempt' and assess penalties and taxes on all corporate income."**

**The paperwork does not end there. Charities that want to solicit donations are often required to file forms with state and local entities. And after a charity has been operating for a year, it needs to file an informational tax return describing its activities and financing to the I.R.S.**

**Seek low-cost advice. Many founders of non-profits groups find they don't need a lawyer to complete the paperwork entailed in winning charity status. Most forms require just filling in the blanks, much like filing a tax return.**

**If a group is uncomfortable with the red tape but doesn't want to pay a professional to do everything, board members can fill out forms and pass the finished product to a lawyer who will review them and make any necessary changes. Or charities can call the local bar association and ask if a lawyer would be willing to donate his or her time to do the legal work**

**Many management-assistance organizations will provide samples of articles of incorporation and bylaws to use as guidelines.**

**Even organizations that have successfully used low-cost help, however, say that it is not always wise to take that option.**

**Sheldon Mains, head of Minnesota E-Democracy, a project that uses the Internet to get people interested in politics and civic affairs, says when the group decided to formalize its efforts last year, it deliberately shunned offers of low-cost advice and hired a lawyer who was an expert on non-profit issues.**



**E-Democracy was worried that the I.R.S. might not understand that the organization was non-partisan and that it intended to stay away from overt involvement in political campaigns, as required by federal laws governing charities. It decided a lawyer might be better able to make that case and it successfully won an exemption.**

**But the group took the low-cost route after that. When it sought to register E-Democracy as a trademarked name, it obtained pro bono help from a law firm that specialized in telecommunications issues.**

**Draft a sound business plan. Charities are often started by people with a great idea who plunge in without a good business plan, says Jude Kaye, a senior staff consultant at the Support Centers of America, a San Francisco group that runs non-profit management organizations in 14 cities. For example, a social worker who wants to start a counseling program may not be well-versed in management and business issues and might not worry about finances until too late in the process.**

**To work out a reasonable budget, experts advise talking to other organizations that are similar in size, services, and mission. Find out how much of their budgets come from foundations, corporations, and individuals, how much comes from fees and other such earnings, and how much comes from government.**

**“A new organization should have a whole batch of ‘What if?’ budgets,” says Ms. Kaye. That will help avoid a scramble in case a fiscal crisis suddenly erupts, she says.**

**“Non-profits don’t fail because they didn’t have a great idea or they weren’t trying to do good in the world,” says Ms. Kaye. “They fail because they ran out of money to pay the bills or they didn’t file the proper forms.”**

### **How to Apply to the IRS for Charity Certification**

- **Thousands of groups apply to the Internal revenue Service each year to obtain charity status. In 1995, more than 67,000 groups applied. Only 619 of those applications were denied, while an additional 16,000 were held over for consideration in 1996.**
- **To qualify as a charity under Section 501(c)(3) of the Internal Revenue Code, an organization must prove to the service that it operates exclusively for religious, educational, scientific, or similar purposes. Donors to such groups may take charitable-contribution deductions from their taxes, which they cannot do with contributions to other kinds of non-profit organizations.**
- **Following are the basic steps involved in seeking charity status:**
- **Draw up the rules that will govern the charity. Those will become the**
- **Organization’s bylaws, which must be submitted to the I.R.S.**
- **Obtain status as an incorporated charity; organizations that are not**
- **incorporated cannot obtain status as a charity.**

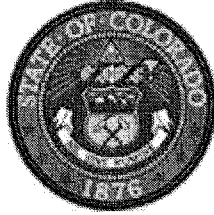
**Collect financial statements showing receipts and expenditures for the current year and the three preceding years to submit along with the application for charity status. Organizations that have been in existence for four years or less only have to provide such information for every year they have operated.**

**Be prepared to submit the organization's publications and copies of leases, contracts, or other legally binding agreements. The service does not require those materials to be submitted, but it has the option of asking for them.**

**The Exempt Organizations Division of the L.R.S. has publications that explain how to apply for non-profit status. Contact the L.R.S. to get Publication 557, Tax-Exempt Status for Your Organization, which outlines the basic procedures for winning charity status and maintaining it. Also ask for Form 1023 (to file for 501(c)(3) status), Form 8718 (to calculate the fee for filing the exemption), and Form SS-4 (to apply for an employer identification number). Forms are available from the service's headquarters at 1111 Constitution Avenue, N.W., CP:E:EO, Room 6411, Washington 20224; (202) 622-8100; fax (202) 622-5088. They may also be obtained from any local L.R.S. office or by calling (800) 829-3676.**

**Publication 557 also can be found on the revenue service's World-Wide Web site at [http://www.irs.ustreas.gov/plain/forms\\_pubs/pubs.html](http://www.irs.ustreas.gov/plain/forms_pubs/pubs.html).**

**Marilyn Dickey**



## The Who, What, When, Where, and Why of COLORADO'S CHARITABLE SOLICITATIONS LAW

As you may have heard, Colorado has a new law updating the state's Charitable Solicitations Act. With this law, Colorado joins forty other states in requiring charities and their paid solicitors to register and provide basic financial information to the state. Here are answers to some common questions charities may have about the new law.

### **WHO IS REQUIRED TO REGISTER?**

If you are a charitable organization intending to solicit contributions in Colorado, you'll register with the Secretary of State under the new law unless your organization falls within one of the law's three stated exemptions:

- You are exempt from filing a federal Form 990 annual information return because you are a religious organization or an organization that engages in exclusively religious activities
- You are a political party, candidate for federal or state office, or a political action committee and you are already required to file with federal or state election commissions
- You do not receive more than \$25,000 in gross revenue per year (excluding grants), or you do not receive contributions from more than 10 people in a fiscal year

### **WHAT DO I NEED TO FILE?**

You'll file a brief, online registration form asking for basic information about your organization and either an electronic copy of your most recent Form 990 or an alternate electronic financial form. Colorado will require much less information from charities than do other states with similar laws.

Charities will only register once, but will have to annually advise the Secretary of State of any changes to their registration. Charities will be required to file a Form 990 or equivalent financial report every year.

### **WHEN DO I REGISTER?**

The registration requirements of the new law take effect on May 9, 2002, at which time charitable organizations will need to register with the state before soliciting contributions.

### **WHERE DO I REGISTER?**

After the online registration system is created, charities will go to the Secretary of State's web site at [www.sos.state.co.us](http://www.sos.state.co.us). Colorado will be the first state in the country to have an electronic-only filing system for charitable solicitations.

### **WHY DO WE HAVE A NEW LAW?**

This law allows donors to make educated choices regarding which charitable causes to support and discourages unscrupulous solicitors from operating in Colorado. We believe it will result in increased donations as donors become more confident about their giving.