

For-profit or Nonprofit?

Presented in collaboration with
E-For-All and Groundwork!
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For-profit or Nonprofit?

Primary distinction:

- Where do the profits go?
 - For-profit: to the owners.
 - Nonprofit: back into the organization.

Whether the enterprise “makes a profit” is not relevant!

For-profit or Nonprofit?

Four key questions:

- Who benefits?
- What is its purpose?
- How is it funded?
- Who runs it?

For-profit or Nonprofit?

For any enterprise, begin by analyzing

Who Benefits?

In the for-profit, one or more owners or shareholders benefit because profits are returned to them.

Who Benefits?

- In the nonprofit, the public benefits.
 - Or a large, indefinable subset of the public
- For a charity (so-called 501(c)(3) organization), a “charitable class” must benefit; for example:
 - The needy
 - The elderly
 - The residents of New Bedford
- One person cannot be a charity.

Who Benefits?

- For other tax-exempt organizations, specific groups may benefit; for example:
 - Social Club, whose members benefit from its programs & activities.
 - Trade Association, businesses who are members will benefit.
- Benefits need not be financial; they can be intangible, or property.
- Public benefit leads to public availability of financial reports (IRS Form 990)

What is its Purpose?

For-profit:

- Can have any purpose it chooses.
- Articles of Organization will state its purpose as “all things lawful”.

Nonprofit:

- Must specify an ***exempt purpose***.

What is its Purpose?

Exempt Purpose:

- Purpose specified in statute, case law, or IRS ruling.
- 501(c)(3)
 - Statutory:
 - Charitable, educational, religious, scientific, literary, etc.
 - Other sources of law provide for purposes like museums, and arts and culture, community development.

What is its Purpose?

- Other tax-exempt purposes:
 - Social clubs must have a social purpose—people come together to socialize.
 - Trade associations must serve common business purposes.
 - Advocacy organizations must have a social welfare purpose.

Bottom line: the nonprofit's purpose must fit into statutory or other specific purpose.

What is its Purpose?

The nonprofit's **activities** must be *in furtherance of its exempt purpose*.

- Virtually all (“substantially all”) its activities must be directly related to the exempt purpose.

Example: an activity of a food pantry with a purpose to “feed the needy” might be to deliver groceries to needy peoples’ homes.

What is its Purpose?

- Too much unrelated activity may subject the nonprofit to tax (“unrelated business income tax”) or even loss of tax-exempt status.
- Activities that are “commercial in nature” may be found to be unrelated to exempt purpose.
 - So-called “Commerciality Doctrine”
 - Activities that are too similar to those of business for profit.
 - Operations too similar to commercial business.

How is it funded?

For-profits are funded by:

- The owners, out-of-pocket;
- Investors may provide cash in exchange for an ownership interest; e.g., shareholders;
- Debt financing;
- “Angels”;
- Only limited availability of grants for business, usually governmental.

How is it funded?

Nonprofits:

- Charities are funded (“supported”) by the public; e.g. fundraising, grant-seeking.
- Other tax-exempts are generally funded by their members; e.g., dues payments.
- Some nonprofits are funded by fees for services.
 - Public support + fees for service is allowed.
- “Seed money” and loans are seldom available to nonprofit start-ups.
- Established nonprofits may take on debt.

Who Runs It?

For-profit is run by its owners, or those designated by its owners; for example:

- Owners personally, as in sole proprietorship, partnership.
- Board of Directors (corporation)—but one person—the owner—may be the entire board (in MA).
- Members (LLC) or managers (manager-managed LLC)

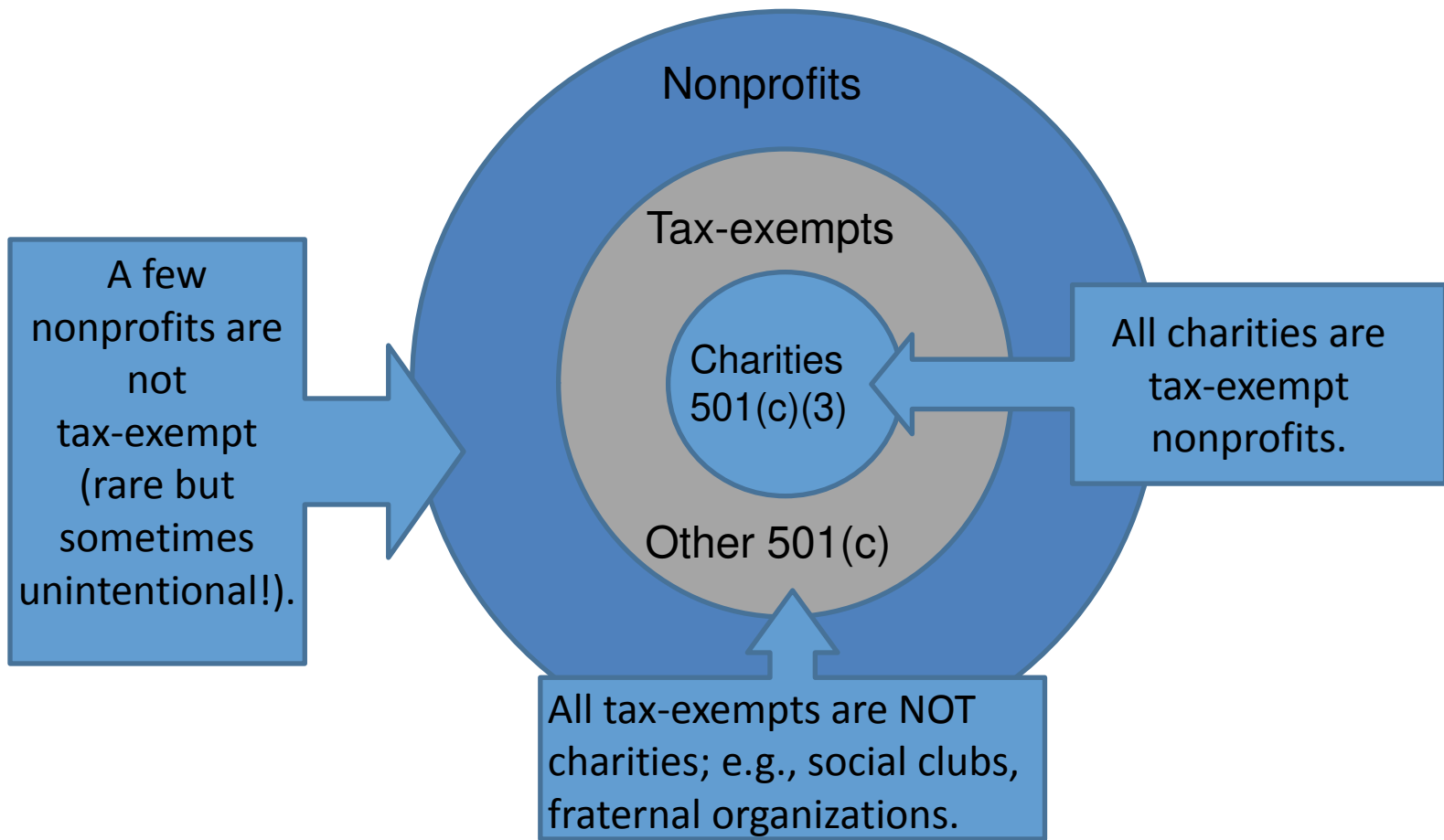
Who Runs It?

Nonprofits are always run by a board of directors. The board has complete authority over the nonprofit.

- To be recognized as tax-exempt, the nonprofit must have a board of several people.
- No one person may control the nonprofit.
- Directors are generally uncompensated volunteers.

Who Runs It?

- Boards may delegate some of their authority to staff—in larger organizations, typically day-to-day operations;
- They may not delegate away all of their authority.
- The board is always ultimately responsible for all activities of the nonprofit.



The Nonprofit Sector

Contact Us!

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