



Washington State (and Federal Tax) Law & Friends of the Library: What Friends Groups Need to Know

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FRIENDS OF THE LIBRARY



Purpose

Friends of the Library (“Friends”) are community-based non-profit groups of citizens who encourage community interest and participation in the Library, promote public knowledge of Library services, resources, facilities and needs, and raise funds to enhance and augment the purposes, programs, services and facilities of their local library (“Library”).

- Branch Friends vs. Library Friends
- Friends vs. Foundation



Relationship to Library

Friends groups are independent nonprofit organizations with their own directors and officers, but have a separate and cooperative working relationship with the Library, its trustees and officers.

- Library/Friends Policy
- Memorandum of Understanding



Organization

- Unincorporated Association
- Nonprofit Corporation (Washington Nonprofit Corporation Act, RCW 24.03)
 - Members? (Usually...)



Organizational Documents

- Articles of Incorporation filed with Washington Secretary of State (\$30 fee; \$50 for on-line expedited filing)
 - Name
 - Period of existence
 - Purpose
 - Registered agent and office
 - Directors
 - Incorporators
 - Dissolution
 - Director liability limitation
 - Indemnification
 - Recommended 501(c)(3) language



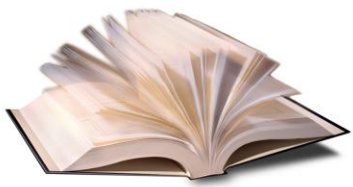
Bylaws

- Member provisions, if any, including qualifications, meeting times and notices, quorum requirements and voting procedures
- Director provisions, including qualifications, meeting times and notices, quorum requirements and voting procedures
- Officer provisions, including qualifications and removal
 - President
 - One or more vice presidents
 - Secretary
 - Treasurer
- Committees, including powers and limitations



Other Organizational Matters

- Business license application for Washington state uniform business identifier (“UBI”) number for tax and employer registration purposes
- Internal Revenue Service (“IRS”) Form SS-4 for federal employer identification number (“FEIN”) for federal tax purposes

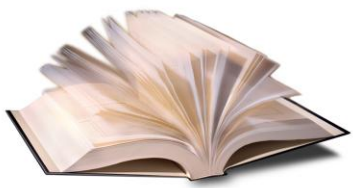


Annual Report

- \$10 fee; \$60 for expedited service
- Failure to file timely results in automatic dissolution of corporation
 - Current registered agent and office
 - Current officers and directors
 - Confirmation of basic information

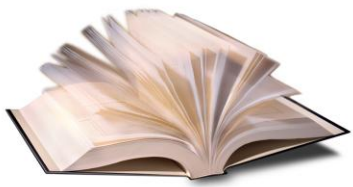


FEDERAL TAX LAW RECOGNITION AS A 501(c)(3) ORGANIZATION



Achieving 501(c)(3) status

- Nonprofit does not mean federally tax-exempt; must apply for and receive recognition as a charitable organization under section 501(c)(3) of the Internal Revenue Code of 1986.
- Successful applications made within 27 months following date of corporate formation relate back to date of formation retroactively.
- No application is required for small public charities as long as gross receipts continue to average less than \$5,000 per year, but application must be submitted within 90 days of the end of the year in which average gross receipts exceed \$5,000 to obtain fully retroactive 501(c)(3) status.



Advantages of 501(c)(3) status

- Contributions are tax-deductible to donors
- Most net income is exempt from federal income tax
- Eligibility for State B&O and sales tax exemptions
- Greater access to private foundation grants
- Qualification for bulk mailing rates



Organizational Requirements

- Organized and operated exclusively for charitable purpose, such as lessening the burdens of government or advancement of education
- No private inurement
- Recommended “magic language” for articles of incorporation (IRS Publication 557)
 - “Said corporation is organized exclusively for charitable, religious, educational, and scientific purposes, including, for such purposes, the making of distributions to organizations that qualify as exempt organizations under section 501(c)(3) of the Internal Revenue Code, or the corresponding section of any future federal tax code.”

More “magic language”

- “No part of the net earnings of the corporation shall inure to the benefit of, or be distributable to its members, trustees, officers, or other private persons, except that the corporation shall be authorized and empowered to pay reasonable compensation for services rendered and to make payments and distributions in furtherance of the purposes set forth in Article Third hereof. No substantial part of the activities of the corporation shall be the carrying on of propaganda, or otherwise attempting to influence legislation, and the corporation shall not participate in, or intervene in (including the publishing or distribution of statements) any political campaign on behalf of or in opposition to any candidate for public office. Notwithstanding any other provision of these articles, the corporation shall not carry on any other activities not permitted to be carried on (a) by a corporation exempt from federal income tax under section 501(c)(3) of the Internal Revenue Code, or the corresponding section of any future federal tax code, or (b) by a corporation, contributions to which are deductible under section 170(c)(2) of the Internal Revenue Code, or the corresponding section of any future federal tax code.”

And even more “magic language”

- “Upon the dissolution of the corporation, assets shall be distributed for one or more exempt purposes within the meaning of section 501(c)(3) of the Internal Revenue Code, or the corresponding section of any future federal tax code, or shall be distributed to the federal government, or to a state or local government, for a public purpose. Any such assets not so disposed of shall be disposed of by a Court of Competent Jurisdiction of the county in which the principal office of the corporation is then located, exclusively for such purposes or to such organization or organizations, as said Court shall determine, which are organized and operated exclusively for such purposes.”



Application for Recognition of Exemption

- IRS Form 1023 and separate instructions
 - FEIN is a prerequisite
 - Required documents
 - Articles of incorporation
 - Bylaws
 - Conflict of interest policy (recommended by IRS; sample appears as Appendix A to instructions to Form 1023)

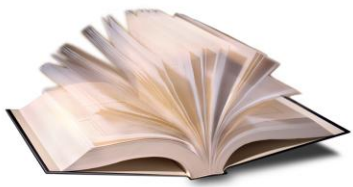


Required Information

- Narrative description of activities and information regarding specific activities, such as influencing legislation (see II.E.2 below)
- Compensation and other financial arrangements with officers, directors and any highly compensated (over \$50,000/year) employees and independent contractors
- Four years of financial data, including historical (if any) and projected revenues and expenses, as well as a balance sheet for most recent year

More required information

- Information related to status as a public charity or private foundation
 - Friends groups will likely be public charities, which must receive either
 - At least one-third of their total financial support from government agencies, contributions from the general public and contributions or grants from other public charities, or
 - At least 10% of their total financial support from government agencies, contributions from the general public and contributions or grants from other public charities, and establish facts and circumstances demonstrating public support
 - Public charity status is a more favorable status



Fees and Timing

- Fees:
 - \$400 if gross receipts are \$10,000 or less during a four-year period;
 - \$850 otherwise
- Timing
 - Depending on completeness and quality of application, determination may take from two to eight months (or more)



Restrictions of Political Activity

- All 501(c)(3) organizations are prohibited from supporting or opposing candidates for public office in any political campaign
- A 501(c)(3) organization, such as a Friends group, may attempt to influence legislation (“lobbying”) by
 - Communicating with any member or employee of a legislative body, or with any government official or employee who may participate in the formulation of the legislation; urging approval of levy and bond propositions is considered such communication (“direct lobbying”)
 - Attempting to affect the opinions of the general public or any segment thereof (“grassroots lobbying”)

Restrictions Cont'd

- Activities to attempt to influence legislation may not constitute a “substantial” portion of the organization’s activities; “substantial portion” is not defined
- Alternatively, a 501(c)(3) organization, may make an election under Section 501(h) by filing IRS Form 5768 to make lobbying expenditures to influence legislation within specific limits:
 - Up to 20% of annual exempt purpose expenditures if the total annual exempt purpose expenditures are not over \$500,000, with a sliding scale above that amount
 - Up to 25% of that amount (i.e., $25\% \times 20\% = 5\%$ of total annual exempt purpose expenditures) can be spent on grassroots lobbying
 - If either of those amounts is exceeded in any tax year, an excise tax of 25% of the excess for the tax year will be imposed



Maintaining 501(c)(3) Status

- Charitable purposes
- No private inurement
- Unrelated business income (“UBI”) resulting from a regularly pursued trade or business that is not substantially related to the organization’s exempt purpose is subject to tax. Exceptions include:
 - A business, such as a used book store operated by a Friends group, where all of the work is undertaken by unpaid volunteers
 - A business of selling merchandise, substantially all of which has been donated, such as used books and other media
 - Dividends, interest income and royalties
 - Rental income from the lease of property that is not debt-financed

Maintaining 501(c)(3) Status Cont'd

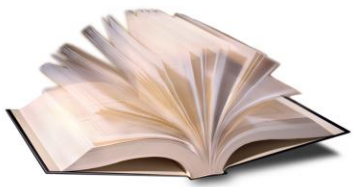
- Annual filing
 - Small 501(c)(3) organizations whose annual gross receipts are normally \$50,000 or less are required to electronically submit IRS Form 990-N, also known as the *e-Postcard*, unless they choose to file a complete IRS Form 990 or 990-EZ instead
 - Larger 501(c)(3) organizations are required to file IRS Form 990 or 990-EZ
 - UBI is reported on IRS Form 990-T
 - Failure to file for three consecutive years will result in loss of 501(c)(3) status

Maintaining 501(c)(3) Status Cont'd

- Disclosure of IRS Forms 1023 and 990
- Receipts for donations of \$250 or more, including a description of any non-cash items and a good faith estimate of value of any goods or services provided



WASHINGTON STATE TAXES



Presumption in favor of taxability

Nonprofit organizations are presumed taxable for purposes of State and local taxes imposed under Washington law, but exemptions may apply



Business & Occupation Tax (RCW 82.04)

- Excise tax on gross receipts imposed for the act or privilege of engaging in business activities, including retail sales and service activities (RCW 82.04.220)
 - State B&O tax
 - Local B&O taxes.
- State exemption for amounts received from fund-raising activities by certain nonprofit organizations (RCW 82.04.3651)
 - 501(c)(3) organizations
 - Nonprofit organizations that meet all of the following criteria: (i) members, stockholders, officers, directors, or trustees of the organization do not receive any part of the organization's gross income, except as payment for services rendered; (ii) compensation received by any person for services rendered to the organization does not exceed an amount reasonable under the circumstances; and (iii) activities of the organization do not include a substantial amount of political activity, including but not limited to influencing legislation and participation in any campaign on behalf of any candidate for political office



Fundraising Activity

- Soliciting or accepting contributions of money or other property or activities involving the anticipated exchange of goods or services for money between the soliciting organization and the organization or person solicited, for the purpose of furthering the goals of the nonprofit organization
- Does not include operation of a regular place of business in which sales are made during regular hours, such as a bookstore, thrift shop, restaurant, or similar business, or the operation of a regular place of business from which services are provided or performed during regular hours, such as the provision of retail, personal, or professional services
- Sale of used books, used videos, used sound recordings, or similar used information products in a library is not the operation of a regular place of business, if the proceeds of the sales are used to support the library

NB: State exemptions may or may not apply at a local level.



Retail sales tax (RCW 82.08)

- Excise tax imposed on the sale of tangible personal property, digital goods and certain services (RCW 82.08.020)
 - State sales tax
 - Local sales taxes
- State exemption for sales made by nonprofit organizations that qualify for fund-raising exemption from State B&O tax (RCW 82.08.02573)

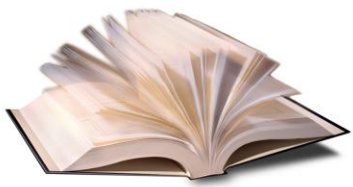


Property taxes (Title 84 RCW)

- Ad valorem taxes levied based on assessed value of real and personal property
- Relevant exemption for real and personal property used by, and for the purposes of, free public libraries (RCW 84.36.040(1)(b)).



WASHINGTON STATE CHARITABLE SOLICITATIONS ACT (RCW 19.09)



Charitable Organization

A “charitable organization” is any entity that solicits or collects contributions from the general public where the contribution is or is purported to be used to support a charitable purpose.

(RCW 19.09.020(2))



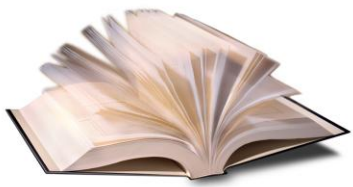
Charitable Purpose

A “charitable purpose” is any religious, charitable, scientific, testing for public safety, literary, or educational purpose or any other purpose that is beneficial to the community, including environmental, humanitarian, patriotic, or civic purposes, the support of national or international amateur sports competition, the prevention of cruelty to children or animals, the advancement of social welfare, or the benefit of law enforcement personnel, firefighters, and other persons who protect public safety. The term "charitable" is used in its generally accepted legal sense and includes relief of the poor, the distressed, or the underprivileged; advancement of religion; advancement of education or science; erecting or maintaining public buildings, monuments, or works; lessening the burdens of government; lessening neighborhood tensions; eliminating prejudice and discrimination; defending human and civil rights secured by law; and combating community deterioration and juvenile delinquency. (RCW 19.09.020(3))



Solicitation

A “solicitation” is any oral or written request for a contribution, including the solicitor's offer or attempt to sell any property, rights, services, or other thing in connection with which: (i) any appeal is made for any charitable purpose; (ii) the name of any charitable organization is used as an inducement for consummating the sale; or (iii) any statement is made that implies that the whole or any part of the proceeds from the sale will be applied toward any charitable purpose or donated to any charitable organization; but does not include bingo activities, raffles, and amusement games conducted under chapter 9.46 RCW and applicable rules of the Washington state gambling commission. (RCW 19.09.020(19))



Registration and Renewal

- Charitable organizations must register with the Secretary of State prior to conducting solicitations (\$60 fee; \$50 for expedited service).
- Registration must be renewed annually (\$40 renewal fee; \$50 if late)
- Registration and renewal applications require a report of all solicitation activity in the preceding accounting year.
- Exemption for any charitable organization raising less than \$50,000 in any accounting year when all the activities of the organization, including all fund-raising activities, are carried on by persons who are unpaid for their services and no part of the charitable organization's assets or income inures to the benefit of or is paid to any officer, director, member, or trustee of the organization, other than as part of a charitable class benefited by the charitable organization.



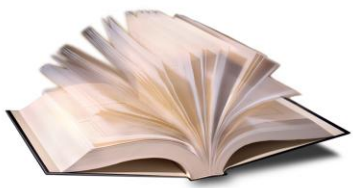
Solicitation Requirements: Disclosures

- Name of individual making solicitation.
- Name of charitable organization and city of principal place of business.
- If charitable organization is registered and if requested by solicited person, the Secretary of State's toll-free phone number (1-800-332-GIVE) and website ([charities@ sos.wa.gov](mailto:charities@sos.wa.gov)) for additional financial and other information on file.
- If the charitable organization is associated with, or has a name that is similar to, any unit of government the entity soliciting contributions must disclose to each person solicited whether the charitable organization is or is not part of any unit of government and the true nature of its relationship to the unit of government.
- Additional disclosures required under specific circumstances.



Solicitation Requirements: Timing

If solicitation is by telephone, disclosures must be made during the solicitation but before asking for a commitment of a contribution, and in writing to any solicited person that makes a pledge within five working days of the pledge. If the solicitor sends any written material before the contribution is received, disclosures must be made in that written material.



Relevant Prohibited Activities

- Representing that a contribution will be tax-deductible unless the charitable organization is a 501(c)(3) organization.
- Representing that the person making the solicitation is a volunteer, member, staff member or employee of the charitable organization if that is not the case.
- Any false, misleading or deceptive statement.
- Telephone solicitations before 8 am or after 9 pm, Pacific time.
- Conduct the natural consequence of which is to harass, intimidate, or torment any person.



Solicitation Requirements: Recordkeeping

Registered charitable organizations must keep accurate, current and readily available books and records (including, at a minimum, documentation supporting the information contained in the annual solicitation report and any statutorily required written authorizations) at their usual business locations until at least three years have elapsed following the effective period to which they relate.



OTHER MATTERS

- Fundraising involving gambling
- Alcoholic beverages at fundraising events
- Financial audits

Questions?

Resources

- Friends Groups generally
 - Washington Library Friends, Foundations, Trustees and Advocates (WLFFTA) <http://wlffta.wla.org/>
 - Association of Library Trustees, Advocates, Friends and Foundations (ALTAFF) <http://www.ala.org/altaff/>
- Nonprofit Corporations
 - Washington Secretary of State <http://sos.wa.gov/>
 - Washington Attorneys Assisting Community Organizations (WAACO) <http://www.waaco.org/>
- 501(c)(3) Organizations
 - Internal Revenue Service <http://www.irs.gov/charities/>

More Resources

- Washington State Taxes
 - Washington Department of Revenue
<http://dor.wa.gov/Content/Home/Default.aspx>
- Washington Charitable Solicitations Act
 - Washington Secretary of State <http://sos.wa.gov/>
- Washington State Gambling Commission
<http://www.wsgc.wa.gov/>
- Washington State Liquor Control Board
<http://www.liq.wa.gov/>



THE END

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