

About U.S. Nonprofits

*An Overview of Charitable Organizations
for the Absolute Beginner*

By LaCharla L. Figgs, Founder,
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INTRODUCTION

Welcome to this brief introduction to U.S. charitable nonprofits. I'm LaCharla Figgs, founder of Nonprofit Startup Academy and a 25+-year veteran supporting US nonprofits. I've written this short ebook to share the basic definition and some of the characteristics of U.S. charitable organizations.



This ebook does NOT discuss what some countries outside the U.S. call non-governmental organizations, which are similar to US nonprofits.

And it doesn't discuss *every type* of US nonprofit. A US nonprofit may have a charitable, civic, educational, religious or other purpose.

This ebook looks only at *charitable organizations*—nonprofits created for “good works.” I hope that after you read these few pages, you'll know what a charitable nonprofit is, why it exists, and some of its limitations.

If you're interested in learning more, please visit me at the [Nonprofit Startup Academy](#).

All my best,

LaCharla

LaCharla L. Figgs, Founder
Nonprofit Startup Academy

WHAT IS A NONPROFIT?

A U.S. nonprofit is a special type of organization. Just like a commercial business, a nonprofit is a legal entity created in your state according to the state's Corporations laws.

Instead of being a corporation (or company) that operates in order to earn a profit for its owners, a nonprofit is an organization that operates in order to carry out a charitable, civic, educational, or religious purpose. That purpose—not profit—is the reason it operates.

What's In A Name?

I use the term *nonprofit*, but states use different names for these organizations. For example, California calls them *Public Benefit Corporations*, and Maryland calls them *Nonstock Corporations*. Nevada uses the term *Non-Profit Corporations*, while Ohio uses the slight variation, *Nonprofit Corporations*. And you'll often hear the term not-for profit, too.

The terms differ, but they refer to the same kind of organization—one that exists to serve a mission, rather than to generate profit for its owners and investors.

The term and spelling “*nonprofit*” is the one most often used in the U.S. nonprofit sector, and so I use it in this article and at [Nonprofit Startup Academy](#).

BIRTH OF A NONPROFIT

Create a nonprofit by filing Articles of Incorporation, Articles of Organization, or a similar document required by your state. That document will contain basic information about the organization, including its name, purpose, location and founder(s). After the state approves and records your Articles, the nonprofit is brought to life and the Articles become its birth certificate.

Income Tax Exemption

Once the nonprofit is a legal entity, its founders usually seek exemption from federal income taxes by applying to the Internal Revenue Service (IRS) for what's called "**501c3**" status. That term comes from the section of the IRS regulation covering tax exemption for U.S. nonprofits.

With 501c3 status, nonprofits in some states can apply for exemption from some state and local taxes. These exemptions allow the nonprofit to keep more funds for its programs.

Also, prospective grant makers and donors see 501c3 status as assurance that the organization is a legitimate U.S. charity.

WHAT MAKES IT DIFFERENT?

Three things make a nonprofit different from a for-profit: Its purpose, the fact that it has no owner, and where its money comes from. Let's look at those more closely:

1. The Nonprofit's Purpose

As I've indicated, a nonprofit's main purpose (the *mission*) is NOT to earn money for its founder(s).

Instead, a nonprofit must have a well-defined purpose that the state recognizes as charitable, civic, educational, or religious.

Nonprofit founders are usually concerned about issues and needs that government and business can't or won't solve. These compassionate people get to work creating programs and organizations that answer those needs.

In contrast, the founder of a for-profit creates a business in order to make money. When that business fails to make money, the owner has no reason to keep the doors open.

Nonprofits *often* run programs that are tough to pay for or that lose money. They fight to keep these programs alive because the people they serve have few, if any, other options.



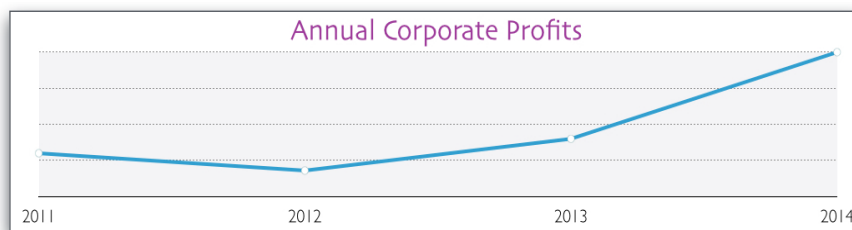
NONPROFIT FOUNDERS: WORKING TO CHANGE THE WORLD

2. No Nonprofit Owner

The second thing that makes a nonprofit different from a for-profit is that by law, no one can own a nonprofit.

In place of an owner, a board of directors or board of trustees assumes legal responsibility for the nonprofit and oversees its affairs in a responsible way.

That creates an important limitation. While an entrepreneur can operate the business and spend her business profits however she wishes (within the law, of course), nonprofit board members *don't own* the nonprofit or its funds. And they're *not* allowed to engineer financial gain for themselves, using their positions as board members.



Here's a fictitious example of inappropriate action by a board member:

A community-based, housing development nonprofit plans to buy 12 properties in a troubled neighborhood over the next 3 years. Their ultimate goal is to eliminate all the tumble-down houses on the block, replace them with new ones, and sell them to neighborhood residents at prices they can afford. (All the residents have modest incomes.)

A board member who is part of this planning process, buys three of those properties at rock-bottom prices before the board is ready to buy, hoping to profit from the sales. This use of insider information makes the board member guilty of abusing her position. She's using her role as a board member for personal financial gain.

And that's NOT legal.

Board Member Compensation

As I said, founders and board members aren't allowed to use the organization's money as if it's their own. In addition, some states—California, for example—allow “*reasonable compensation*” for nonprofit board service, while others allow only reimbursement of board-related expenses.

IRS pays attention to the way boards handle money, too. Board members absolutely *must* avoid misusing funds and other organizational assets, because that can cause the state to strip the organization of its nonprofit status and the federal government to revoke its tax-exemption.

NO ONE allows board members to treat nonprofit assets like their own personal treasure chest.

3. Where Nonprofits Get Money

The last thing that makes a nonprofit organization different from a for-profit business is where its money comes from.

A business earns money by selling products or services in large enough quantities and at high enough prices to create a profit for its owners and investors.

Not so with nonprofits. Nonprofits sometimes charge for products or services that serve the mission, but they don't price them to earn a profit. For example, affordable housing nonprofits charge rents based on income for those with low incomes. Those low rents don't cover the cost of providing those homes.

So nonprofit organizations typically depend on the following sources for survival:

- Financial contributions from individuals and businesses
- Grants from nonprofits, businesses, and governments
- Contracts for services (*Such as for youth programs*)
- Below-market fees for service (*Such as for counseling*)
- Interest earned by endowments
- Bequests

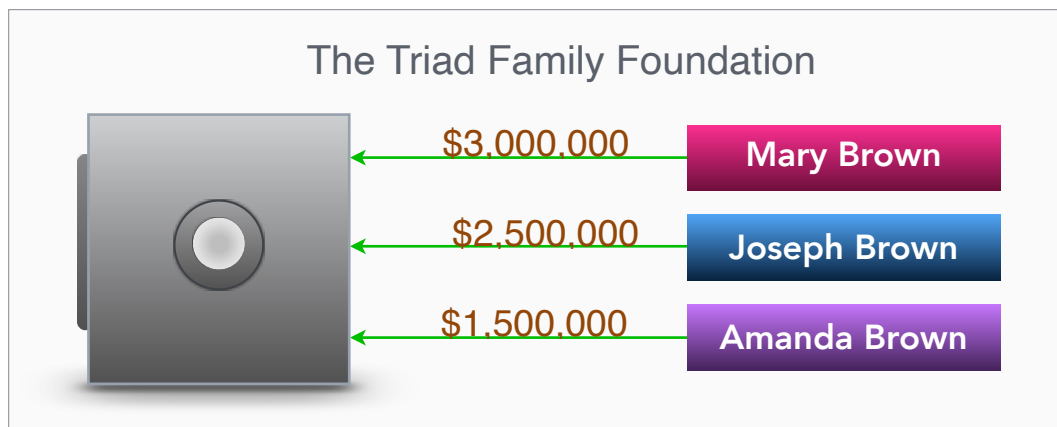


Types of Nonprofits

We have two kinds of nonprofit in the U.S.: [foundations](#) and [public charities](#). IRS classifies nonprofits based in part on where they get most of their funds.

FOUNDATIONS

A foundation gets its money from limited sources, such as from an individual, a family or a corporation.



Example of the income sources for a fictitious U.S. foundation.

Examples of U.S. foundations started by individuals or families include [The Ford Foundation](#) and [The Annie E. Casey Foundation](#).

The Ford Foundation

Edsel Ford, whose father Henry founded Ford Motor Company, launched the foundation in 1936 with \$25,000 of his own money. The foundation was intended “for scientific, educational and charitable purposes, all for the public welfare.”

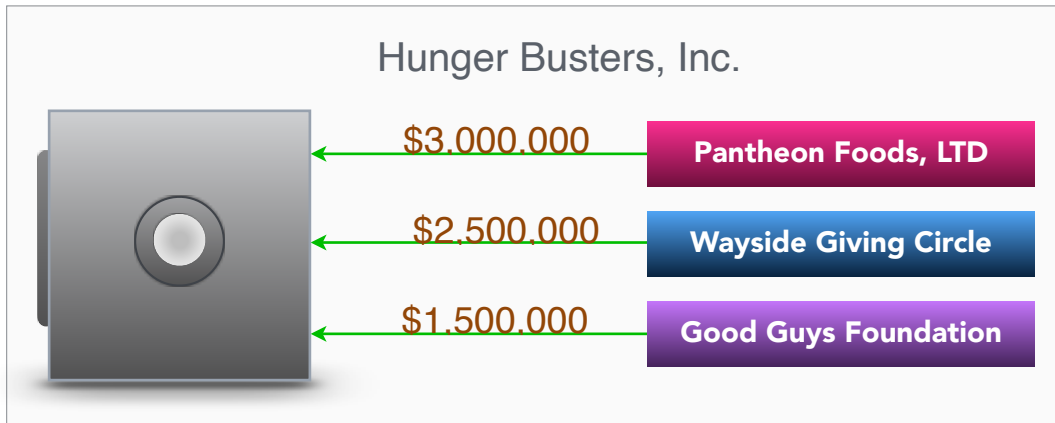
The Annie E. Casey Foundation

This foundation was created by the children of Annie E. Casey to honor the woman who had worked so hard to raise them during difficult times.

Jim Casey, the eldest son, started a messenger service in 1907 to help support his mother and siblings. That company later became UPS.

PUBLIC CHARITIES

A public charity must get funds from a public source—like the state Department of Education—or from a combination of sources, like individuals, government, corporations, foundations, and user fees.



Example of the income sources for a fictitious U.S. public charity.

Common Traits

Foundations and public charities both have board oversight and must limit grant making and programs to charitable, civic, educational, or religious activities.

We tend to think of foundations only as grant makers, but foundations *and* public charities can run programs and make grants.

Foundations that run programs are called operating foundations. In fact, some foundations only make grants. Some only run programs. And others do both.

Most nonprofits that are considered public charities run programs. This is likely the kind of organization you hope to start.

Foundations and public charities follow different federal rules and receive different tax treatment. So, if you're a prospective nonprofit founder you'll need to do your homework and decide which type of nonprofit best suits YOUR vision.

WHAT'S NEXT?

Now you know a U.S. charitable nonprofit is a purpose-driven organization that makes grants, operates programs, or both in order to serve "the public good."

If you're thinking of launching a charitable nonprofit, I'm here to support you. If you visit my website, you'll see the resources and programs I offer to help make it easier for you to reach your goals and bring your Big Vision of serving others to life.

My website is <https://www.nonprofitstartupacademy.com/>. I hope you'll pay me a visit! And if you have questions, feel free to use the Contact form on the site to send them to me.

Supporting your Big Vision,

LaCharla

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