

Board Training Kits: Articles of Incorporation and Association Bylaws

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Southern Early Childhood Association

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What does it mean to be “Incorporated”?

An association or nonprofit organization that chooses to become an incorporation is “an artificial legal entity composed of individual members but considered to have its own existence apart from its members for purposes of organization, operations, liability, longevity, holding property, and so forth.”

The tax-exempt status of an organization is unrelated to whether or not it is incorporated, as are employment standards, discrimination laws, and requirements regarding employee taxation. An incorporated organization remains incorporated until it is legally “dissolved.”

Source: Jacobs, Jerald A. Association Law Handbook. Third Edition. Washington, DC: American Society of Association Executives, 1996, p. 12.

Advantages and Disadvantages of Incorporation

Advantages:

- Incorporation eliminates the personal liability of members. All debts and obligations are in the name of the corporation, not the managers or board members. The maximum liability of an incorporated association for contract claims and for personal injury or property damage claims generally will be limited to the amount of the assets of the association.
- Incorporation establishes continuity in the face of leadership and staff changes. Corporation status is not affected by changes in personnel, leading to a more stable environment for the organization itself.
- Protection of the association’s name may be easier if the organization is a corporation.
- Courts will tend to adhere to the following hierarchy of laws when examining disputes within or involving an incorporated nonprofit organization: federal laws, state laws, Articles of Incorporation, bylaws, policies, and resolutions.
- Obtaining insurance may be more difficult for an unincorporated association, as it may be more difficult for the insurance underwriter to determine the precise authority for association operation.
- Individuals and firms may be more comfortable working with an incorporated organization, as they may regard that organization as more formally structured, more stable and more businesslike than an unincorporated one.

Disadvantages:

- The process of incorporation may involve moderate expenses for the association, such as legal fees, filing costs, or franchise taxes.
- More specific standards of operation apply to incorporated entities than to non-incorporated ones.
- Dissolution of an incorporated association may be complicated and involve substantial legal expenses.

Sources: www.BoardSource.org, 2005, and Jacobs, Jerald A. *Association Law Handbook*. Third Edition. Washington, DC: American Society of Association Executives, 1996, p. 13-14.

Incorporation Procedures

1. Determine matters such as the association's name, purpose, membership, activities, dues, budget reserves, etc.
2. Define the nature and scope of the organization, what the group will attempt to accomplish, and the means to be used to reach its goals.
3. Identify the location where the association will incorporate (usually the state in which its principal offices are located).
4. Register as a foreign corporation in other states if the association is going to have offices or carry on significant activity in states other than the state of incorporation.
5. Choose Incorporators, or persons who arrange for incorporation for an association and sign the required documents. State law may require that there be a minimum number of them.
6. Draft and file the Articles of incorporation. These are part of the legal grant of corporate status to an association by the state government.
7. Draft and adopt the association's bylaws. Although state laws do not always require them, bylaws are always desirable as they are the main internal rules for association management and governance.
8. Adopt a manual of policies and procedures through a resolution of the board of directors. This document explains, in detail, the managing and governing positions of the association that do not affect the rights and obligations of members, directors, and officers, and thus need not be included in the articles of incorporation or bylaws.
9. Attain state judicial or administrative approval, if necessary. This may be the case for associations that will solicit charitable contributions.

10. Prepare any documentation required by the Internal Revenue Service for determination of federal income tax exempt status.
11. Pay any legal fees, charges for filing the Articles of Incorporation, foreign corporation fees, or any other costs that may be incurred during the incorporation process.
12. Ratify the acts of the incorporators after incorporation.

Articles of Incorporation

An association's Articles of Incorporation are its agreement with the state granting its incorporated status, establishing the basis for that association's separate legal existence. States grant individual legal status to associations in exchange for their commitment to adhere to that state's rules and regulations governing corporations.

What should be included in your Articles of Incorporation?

Your Articles of Incorporation are a binding legal document. The content requirements vary from state to state and, as a general rule, you should include only what the law requires, as complying with state laws for amending the Articles of Incorporation can be a difficult and time-consuming process. Bylaws, which are more easily amended, will handle more detailed policies to govern the organization. Items to include in the Articles of Incorporation:

- Full name of the association
- The association's specific purpose (be brief and broad to allow for future evolution but clearly indicate the organization's tax-exempt focus)
- Duration of the association's existence (often perpetuity)
- Address of the association's principal office and the geographic areas in which the association tends to operate
- Name and address of the legal agent of the association
- Number, names, and addresses of the initial board of directors
- Whether or not the association is a membership organization
- Whether or not there will be association bylaws
- General provisions for conducting the internal affairs of the association
- Dues requirements in general terms
- Procedures for terminating or dissolving the association
- Provisions for distribution of assets when the corporation is dissolved
- Approval by state officials, as required by state law

When completed as required, the Articles of Incorporation are signed by the sponsors, their signatures notarized (in some states), and the document containing the Articles is submitted with the applicable fee to the state government agency or court responsible for approving the granting of corporate status.

When the agency or court has approved the Articles of Incorporation, an official copy is returned to the submitter, and the association should retain several copies of the Articles, showing they have been certified as official by the state government.

Sometimes major changes in the organization's status, activities, or structure force you to amend the Articles and to file an updated copy. Such changes include:

- changing the organization's name or address
- substantially changing the organization's mission
- altering the provision for the disposition of assets if the organization is dissolved
- changing the way board members are elected (formal membership structure vs. self-perpetuating board or vice versa)

Sources: www.BoardSource.org, 2005, and Jacobs, Jerald A. *Association Law Handbook*. Third Edition. Washington, DC: American Society of Association Executives, 1996, p. 19-22.

Bylaws

Bylaws: rules adopted and maintained by an association to define and direct its internal structure and management

Legal Characteristics of Bylaws

In terms of the legal hierarchy, Articles of Incorporation are the primary laws of an association and bylaws are subordinate, yet complementary, to an association's Articles of Incorporation.

Bylaws may be viewed as constituting the terms of an agreement between an association and its members, describing the relationships, rights, and obligations for the members, directors, officers and staff of the association. While not required for incorporation in most states, bylaws can be invaluable in resolving differences within the association, and will normally be honored and enforced in a court of law.

The Internal Revenue Service often requires that an organization maintain an internal governing document to attain tax-exempt status, making bylaws especially helpful in such cases.

Formation and Revision of Bylaws

- Usually the authority to adopt or amend bylaws rests with the membership, though some states permit delegation of this authority to a representative body, such as the board of directors.
- Bylaws should be reviewed periodically to ensure that they conform to and reflect current management rules followed by the association, but amendments should be made only when necessary.
- Regarding issues in which changes can be anticipated over the life of the association – such as dues structure, number of directors, etc – the bylaws should give only general guidance or set minimal requirements.
- Up-to-date copies of the bylaws should be made available to all members.

Content of Association Bylaws

Bylaws should be simple, concise, and easily understandable in order to foster members' awareness of bylaw provisions. Well-written bylaws present an image of the association as professional and well-managed, and therefore can serve as recruiting documents for new members and donors. Bylaws of an association may contain the following types of information:

- Purposes of the association expressed in greater detail than in the Articles of Incorporation
- Membership qualifications, admission procedures, and expulsion or resignation procedures
- Officers' qualifications, titles, terms of office, time and manner of election, meetings, powers, and duties
- Filling of vacancies in officers' or directors' positions
- Voting procedures for members and directors
- Notices, times, places, agendas, and minutes of meetings
- Property holding and transfer
- Indemnification of directors and officers
- Number and use of standing committees
- Delegation of authority to directors or officers
- Relationships with other associations, including affiliations and federations

- Adoption and use of an association seal or logo
- Fiscal year, audits, and financial reports
- Location of principal and other offices
- Amendment procedures
- Dissolution procedures
- Use of funds and disposition of surplus assets at dissolution
- Legal compliance, including antitrust policy

Source: Jacobs, Jerald A. *Association Law Handbook*. Third Edition. Washington, DC: American Society of Association Executives, 1996, p. 23-26.

What is a Dissolution Statement?

The Articles of Incorporation should include a statement of dissolution. Its purpose is to define the fate of your organizational assets if the organization ceases to exist. The statement must make it clear that none of the remaining assets will benefit a private person, but instead will be distributed to another tax-exempt nonprofit.

Sample statement: "In the event of dissolution of the Early Childhood Association, the board of directors shall, after paying and making provisions for the payment of all liabilities, distribute all the assets of the corporation over to an organization dedicated to charitable and/or educational purposes and which has been recognized as a 501(c)(3) organization by the Internal Revenue Service."

Source: www.BoardSource.org 2005



Questions for Discussion

1. How do the advantages and disadvantages of incorporation discussed in this presentation apply to your organization? Make a chart outlining the advantages and disadvantages of incorporated status for your association.
2. If your association is already incorporated, were any of the incorporation procedures discussed in the presentation omitted from your association's own incorporation process? If so, what can be done to address them now? If your association is not yet incorporated, how could you manage the incorporation procedure?
3. If your association has already filed its Articles of Incorporation, examine them closely and determine whether or not all of the necessary information is included in them. If anything is missing from your association's Articles, how might you amend the Articles to address that oversight? If your association has yet to devise its Articles of Incorporation, write a sample document, based on the guidelines presented in the discussion.
4. Who in your organization is in charge of writing, maintaining and revising your association bylaws? What is the process by which your association bylaws are revised? Be very specific in outlining this process.
5. Examine your association's bylaws carefully and determine whether or not all of the necessary information is included in them. If your association does not maintain its own set of bylaws, write a sample document, based on the guidelines presented in this discussion.
6. If your organization has non-profit tax-exempt status, how are your organizational assets to be distributed if the organization ceases to exist? If you do not already have a Dissolution Statement for your organization, write a sample document based on the guidelines presented in this presentation.

Sources

Jon Wiley & Sons. Nonprofit Organizations' Business Forms. New York: John Wiley & Sons, 1995.

Oleck & Stewart. Non-Profit Corporations, Organizations & Associations. Englewood Cliffs, NJ: Prentice-Hall, 1994.

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