WHAT EVERY BOARD MEMBER SHOULD KNOW

A Guidebook for Tennessee Nonprofits
2019 Edition

Dear Tennessee nonprofit board members,

Thank you for your service to the nonprofit sector in our state. Tennessee nonprofits are vital to our citizens, providing important services and opportunities in communities throughout the state. By donating your time and talents to Tennessee's diverse nonprofits, you play an essential role in shaping a brighter future for all of us.

Our offices designed this guidebook to help you become more knowledgeable and successful board members. The 2019 edition includes updated information, as well as completely new sections on board development and data breaches.

We believe the principles and practices in this updated guidebook will strengthen your organization, and we encourage you to share this guidebook with your fellow board members, and other community members.

Sincerely,

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Tennessee Attorney General and Reporter

Tre Hargett
Tennessee Secretary of State

Tari Hughes
President and CEO, Center for Nonprofit Management

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Introduction and Table of Contents

This Guidebook has been prepared as a reference tool for you, the board members of Tennessee nonprofit organizations. It describes some of your rights and duties as well as issues which you may encounter. Your service should be a rewarding experience. This Guidebook attempts to help you prepare for this service. It is not intended to be a complete summary of the laws governing nonprofits in Tennessee or a substitute for legal advice.

Nonprofits in Tennessee can be divided into two general categories: public benefit nonprofit corporations – commonly referred to as charities – which exist to serve public causes, and mutual benefit nonprofit corporations, which exist to serve their members (such as homeowner associations). This Guidebook is directed primarily to board members of public benefit nonprofit corporations. While many of these principles do apply to both types of organizations, some laws may be different.

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KEY: = Best Practices = Examples = Glossary Word

Board Member Duties

Although as a board member you may not manage the day-to-day activities of your nonprofit, you do act as a steward and have certain fiduciary responsibilities under Tennessee law. Specifically, Tennessee law imposes upon you the duties of good faith, loyalty and care.

The **duty of good faith** means that you must act in good faith and be fair in your dealings with your nonprofit. You have a duty to follow your nonprofit's governing documents, carry out its mission, and ensure its funds are used for lawful purposes. You must be upfront and honest in your dealings with the nonprofit, and in fulfilling your other fiduciary obligations.

The **duty of loyalty** means that you must act in a manner you reasonably believe to be in the best interests of your nonprofit organization and that you not seek to benefit personally from the activities or resources of the nonprofit you serve. In the event that you have a conflict of interest between the interests of the nonprofit and your own interests, you must comply with Tennessee law in resolving this conflict. Actions that benefit you at the expense of your nonprofit are a breach of your fiduciary duty.

The **duty of care** means that you must act reasonably, as a prudent person in similar circumstances would, that you are familiar with the nonprofit's activities and financial condition, and that you participate regularly in board meetings. It is the job of the governing board to oversee the work of the chief executive officer of the nonprofit and to make sure that the organization is faithfully carrying out its charitable purpose without extravagance or waste. You should carefully consider whether you have the time to participate as required before agreeing to serve on a board. Failing to honor these obligations can seriously harm your nonprofit organization and undermine its charitable mission. Furthermore, under Tennessee law, you may be personally liable to the nonprofit for the harm it suffers if you breach your fiduciary duties.

Board members also have a duty to disclose material information to the rest of the board. If you are aware of information that you believe could affect or require a board decision, you must share it with your fellow board members, unless you cannot legally do so (e.g., disclosure will violate ethical or confidentiality laws).

Examples:

Duty of *good faith* → being honest with the nonprofit in seeking travel or expense reimbursement

Duty of *loyalty* → offering printing services to the nonprofit at market or below market rates

Duty of *care* → voting against, or tabling, a fundraising contract for which you don't believe the board has been provided information, and then actively seeking more information

Fulfilling Your Fiduciary Duties

In making decisions affecting the nonprofit, directors must act on an informed basis, in good faith, and with the honest belief that the action taken was in the best interests of the nonprofit. Below are some ways you can fulfill your fiduciary duties under Tennessee law by participating actively in the management and operation of the nonprofit:

- Attend board meetings and meetings of committees on which you serve. Make certain that you receive detailed information beforehand about matters that are going to be discussed and voted on at a meeting, especially the financial reports and financial statements of the nonprofit.

- Carefully read all the material you receive, ask questions, and be active in board discussions. It is important to know how the organization is functioning and understand the specific purposes and mission of the nonprofit. Be informed about every major action that the nonprofit takes and be proactive about reviewing materials in a timely manner.

- Use your own judgment in voting and do not simply follow the lead of the chief executive officer, chairperson of the board, or fellow board members. A responsible board member will ask about the reasons for recommending a particular action and the consequences, good and bad, such action will bring.

- Participate in strategic planning activities that assess and plan for the nonprofit's future. Ask about the status of the nonprofit's internal controls and about written policies and procedures that protect the nonprofit from error, fraud and embezzlement.

- Inquire whether the nonprofit has a written conflicts of interest policy, and be familiar with the procedures for how to identify potential conflicts and how to handle them when they arise.

- Inquire whether the nonprofit has a directors and officers liability policy and whether the nonprofit indemnifies its directors, officers, and volunteers from liability.

- Review the nonprofit's charter and bylaws. Make sure such documents are up-to-date and the nonprofit is operating in accordance with such documents.

- Be familiar with federal, state, and local laws relating to nonprofit corporations and charitable solicitations and ensure that the nonprofit is in compliance with all such laws and any required filing o reporting deadlines.

- Review board or committee minutes to make certain that the meetings and votes were properly recorded. Written minutes should be taken at every board and committee meeting by someone other than the chair. The minutes should accurately reflect board and committee discussions, as well as actions taken at meetings. If there are errors in the minutes, ask for clarifications or changes.

- Review and understand the nonprofit's business records, including financial documents and audit requirements. Ensure that the nonprofit maintains accurate records and books and has sufficient document retention policies in place.

Note: In the Tennessee Nonprofit Corporation Act, board members are referred to as directors; however, nonprofits themselves usually use the term "board members" when referring to members of the nonprofit governing board.

Fulfilling Your Fiduciary Duties *continued*

• Review and understand how the nonprofit's data, including personal and financial information of donors, employees, volunteers and members served by the nonprofit, is maintained, and ensure that adequate protections are in place.

• Investigate warnings or reports of director, officer, or employee theft, mismanagement, and misconduct. The board should adopt procedures to handle reports of inappropriate uses of resources or inaccurate reporting of financial affairs and inappropriate conduct. These procedures should include protections for anyone reporting the possibility of such damaging activities. Where appropriate, a director should consult an attorney or other professional for assistance, and in some instances, the board as a whole may need to seek such advice.

Nonprofit board members vs. nonprofit officers

Under Tennessee law, nonprofit corporations are required to have both **board members** and **board officers**. Generally speaking, board members are responsible for directing the overall vision and mission of the nonprofit corporation. Officers, on the other hand, are responsible for the day-to-day management of the nonprofit. In addition, officers are responsible for reporting to the board. We recommend that when officers are selected from the agency's management, that they not also serve as voting members of the board. In this way, board members can focus on organizational oversight, and officers can focus on organizational operations and management.

Nonprofit officers have similar fiduciary duties to board members. As with board members, officers must act in good faith and in the best interests of the nonprofit organization. Officers must also be loyal to the nonprofit and exercise care in managing its affairs. Like board members, nonprofit officers can be held personally liable for harm to the nonprofit caused by breaching the fiduciary duties of good faith, loyalty, and care. In addition, officers must inform a superior officer or the board of material information about the nonprofit. If, as an officer, you learn about actual or potential violations of the law by the nonprofit, or if you learn that another officer or board member has or will breach a fiduciary duty to the nonprofit, you must notify your supervisor or the board.

Note: In the Tennessee Nonprofit Corporation Act, board members are referred to as directors; however, nonprofits themselves usually use the term "board members" when referring to members of the nonprofit governing board.

Required Board Members and Officers

Tennessee has certain minimum requirements with respect to nonprofit officers and board members. The following checklist will help ensure that you are complying with these requirements:

- Tennessee nonprofit corporations must have at least three board members who are natural persons. We recommend at least seven directors, when possible.

- Tennessee nonprofit corporations must have officers, including a president and secretary, who must be different persons. (See sidebar on page 5 for information about the differences between **board officers** and **board members**.)

- Unless the nonprofit's charter or bylaws provide otherwise, the officers shall be elected or appointed by the board of directors.

- The board of directors or bylaws must designate one officer to be responsible for preparing the minutes of the board.

Board Development

It is important to provide incoming board members with a thorough orientation to the nonprofit, including its organization, mission, and programs. Be sure to inform new board members about the extent of the board service expected and any financial demands that occupy board service. Provide opportunities for new board members to get to know other board members and officers so they can form relationships vital for future years of productive board service. We recommend creating a board member handbook that contains important information such as board policies, biographical and contact information for other board members, legal documents, financial data, meeting dates and minutes, and committee descipions.

Consider creating staggered board terms to ensure that the nonprofit's board is always composed of more experienced, longer-serving board members while welcoming new board members. It might also be helpful to establish mentor/mentee relationships between longer-serving and new board members. In addition, it may be helpful for new board members to have access to specific trainings on the more complicated areas of managing a nonprofit, including financial oversight, audits, and conflicts of interest.

Board Engagement

The board members of a nonprofit must be well-informed, hold regular board and committee meetings, maintain accurate minutes of those meetings, encourage open discussion, and pursue the nonprofit's mission and best interests with determination. One of the responsibilities of a board member is to make certain that the nonprofit operates in a fiscally sound manner, has mechanisms in place to keep it fiscally sound, and is properly using any restricted funds it may have.

Examples of best practices for engagement include:

- Making certain that a realistic annual budget is developed. The budget should be developed early enough so that the entire board can be involved in its review and approval before the beginning of the fiscal year. Expect management to produce timely and accurate income and expense statements, balance sheets and budget status reports. Expect to receive and review these in advance of board meetings.

- Making certain that the required annual federal and state reports and tax returns are properly and timely filed with both the Internal Revenue Service and the Tennessee Department of State. Such examples may include, but are not limited to, IRS Form 990, Annual Report and Charitable Solicitations Registrations.

- Requiring periodic confirmation from management that employee withholding taxes and insurance premiums are being paid when due.

- Paying special attention to where and how the funds of the nonprofit are being held and invested. We recommend creating standing audit and finance committees to regularly review your nonprofit organization's finances and assets. Confirm that restricted funds are being accounted for separately and that they are being used in accordance with the restrictions applying to them.

- Ensuring that fundraising is done honestly and with integrity. Often, an organization will enter into a contract with an individual or organization to solicit funds and raise money on its behalf. While this can provide much needed funding, it is important to carefully review the contracts and literature (brochures, scripts and other related material) of the **professional fundraiser** or **professional fundraising counsel** ("advisor" or "consultant"). It is a good idea to inquire into the track record and activity in other states of fundraisers or consultants you might hire. Finally, check to see if the professional solicitor is registered with the Division of Charitable Solicitations and Gaming and has filed the required notices and related material.

  - A professional fundraiser is someone who, for financial or other considerations, asks for and collects donations on behalf of a charitable organization. It may involve phone solicitation, direct mailings, or door-to-door solicitations, among other means. These individuals must register with the Division of Charitable Solicitations and Gaming.

  - A professional fundraising counsel ("advisor" or "consultant") is any person who, for compensation, plans, manages, advises, consults or prepares material for a charitable organization for the solicitation of contributions in Tennessee, but who does not solicit contributions. Fundraising counsels no longer need to register with the Division of Charitable Solicitations and Gaming.

Board Engagement *continued*

• Protecting your brand and keeping current on new fundraising trends. The growth of nonprofits combined with increased technology present both opportunity and challenge. In addition to the traditional forms of fundraising, there are new methods that include online fundraising pages, mobile applications and third parties. The new fundraising platforms create a potential for a nonprofit to be in front of new donors and accept donations in alternative ways. However, these new methods allow individuals or organizations to create online giving platforms without having received prior consent or permission from a nonprofit to raise funds on its behalf. Potential conflicts can develop with branding, messaging, and possible exposure to violations of local, state, and federal laws.

• Be aware of the contracts your organization enters into with a professional fundraiser. In your role, it is important to inquire on an annual basis about the manner in which the logo or brand is being used or leveraged in relation to telemarketing, direct mail, collection receptacles ("donation bins"), social media and online fundraising platforms, or other fundraising practices.

Note: Full-time salaried development or advancement staff are not required to register as professional solicitors or fundraising counsel. However, if someone is hired as an independent contractor, registration may be required based on the contractual agreement.

Board Judgment

In order to carry out your responsibilities as a board member, you must be able to make informed decisions about important matters affecting the daily operation of the nonprofit and how it affects the community it serves. The law permits you to reasonably rely on information from the nonprofit's staff, its lawyer, its accountant, outside advisors, and board committees in making those judgments. If you don't have adequate information, request and obtain it. Management has a duty to provide this information to the board.

You may ask for the following records, which the nonprofit is required to maintain under Tennessee law:

- Minutes for all board meetings;
- Records of board member actions taken without a meeting;
- Records of actions taken by board committees as delegated by the board;
- Appropriate accounting records, including annual financial statements;
- Membership lists, including the names and addresses of each member, in alphabetical order, and showing the number of votes each member is entitled to vote;
- The charter and all amendments currently in effect;
- The bylaws and all amendments currently in effect;
- Board resolutions relating to any class or category of members;
- Minutes of all members' meetings and approvals for the last three years;
- Any written communication to the members for the last three years;
- The names and business or home addresses for current officers and directors; and
- The most recent annual report filed with the secretary of state.

Best practices of the board to stay informed:

- Have a copy of the charter and bylaws of the nonprofit and other documents that may be necessary to understand its operations.
- Inquire about an orientation session for new board members and about a board manual containing the nonprofit's written policies and procedures.
- Request reasonable access to management and reasonable access to internal information about the organization.
- Request reasonable access to the organization's principal advisors, such as its auditors and consultants on executive compensation.
- Engage the services of outside advisors to assist the board with a particular matter.

Selection, Hiring, and Firing the Chief Executive Officer

The chief executive officer (CEO) is the person responsible for day to day management of the nonprofit. The chief executive officer may be sometimes referred to as the executive director. The chief executive officer is also typically the president of the nonprofit.

A major responsibility of the board of directors is the selection of a qualified chief executive officer, the establishment of that person's compensation, review of that person's performance on an annual basis, and offering criticism, where appropriate.

The board is also responsible for removing the chief executive officer. Failing to remove an ineffective chief executive officer can damage a nonprofit organization. It can also be grounds for holding board members liable for breaching their duty of care. Under Tennessee law, the board may remove the chief executive officer, or any other nonprofit officer, at any time, with or without cause. However, this is subject to any contract rights that the officer might have under an employment agreement.

Reviewing Executive Compensation

The public, which supports the nonprofit and uses its services, is interested in knowing how their charitable donations are being used and what compensation levels are being paid. This information is publicly available through the Form 990 your nonprofit may be required to file with the IRS. You may obtain Form 990 for those charities registered with the Department of State's Division of Charitable Solicitations and Gaming by contacting the Division at 615-741-2555 or **charitable.solicitations@tn.gov**. IRS Form 990s are also publicly available at **https://www.nccs.urban.org** or **https://www.guidestar.org**.

In addition, the IRS has established penalties to deal with excessive compensation. Under federal law, board members who knowingly approve excessive compensation and benefits for certain officers could also be subject to penalties. For more information, see the IRS charity website at **https://www.irs.gov/Charities-Non-Profits**. It is also important to know that "compensation" does not just refer to salary, but also includes any retirement benefits, deferred compensation, bonuses, and allowances.

In fulfilling their responsibilities for executive compensation, board members must:

- Know what the chief executive officer is paid, including fringe benefits. (See the following link for guidelines about fringe benefits from the IRS: **https://www.irs.gov/publications/p15b**.) If the board has a formal compensation committee that recommends a specific salary, you are still responsible as a board member for reviewing and approving that salary level and for asking questions about how the salary level was determined. In addition, the IRS asks governing boards to review comparable salary data and specific performance measures to determine appropriate compensation levels.

- Be sensitive to the chief executive's salary in the context of your community. Remember that compensation of the chief executive officer is important to those who donate to the nonprofit, to those who are served by the nonprofit, and to the community at large.

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Warning: Generally, Tennessee law prohibits payments to any board member or nonprofit officer, except for compensation in reasonable amounts for services rendered, or reimbursement for reasonable expenses incurred on behalf of the nonprofit. *(Tip: We recommend using federal CONUS rates as an appropriate guideline for travel expenses.)* In addition, Tennessee law prohibits loans to board members or nonprofit officers. Examples of prohibited loans include payroll advances, or using corporate credit cards for personal purchases, even if the nonprofit is reimbursed at a later date.

Board Conflict of Interest

Board members owe their nonprofit organizations the **duty of loyalty** (see "Board Member Duties" on page 3), which means acting in the best interests of the nonprofit. Prior to joining a board, you must disclose any personal or business relationship that is in conflict with this duty of undivided loyalty, whether direct or indirect, actual or potential. If a transaction is presented to the board in which you have a direct or indirect personal or business interest, you must disclose that conflict of interest to the board, remove yourself from any board discussion, and not vote on the matter. Board chairs should ask their board members and officers to sign conflict of interest statements at the start of each year in order to document existing or potential conflicts. We recommend that the board adopt a conflict of interest policy and review it at least annually.

If you are asked to vote on a conflict of interest transaction, you must do so with only the best interests of your nonprofit in mind. Before approving a conflict of interest transaction, take great care to ensure that the transaction is fair to the nonprofit, that it is in the best interest of the organization, and that it furthers the nonprofit's mission. Make sure that your reasons for approving the transaction are well documented in the board's minutes. Also be aware that Tennessee law prohibits certain conflict of interest transactions, such as loans to board members.

Finally, you should know that if you vote to approve a conflict of interest transaction, you may be held personally responsible to the nonprofit if the transaction harms the nonprofit or is otherwise unfair. You also have the right as a board member to sue a conflicted party on behalf of your nonprofit organization if the transaction is unfair or harmful.

Note: Conflicts of interest are referred to as "conflicting interest transactions" under the Tennessee Nonprofit Corporation Act.

Charitable Solicitation and Consumer Protection

The **Division of Charitable Solicitations and Gaming** in the **Tennessee Department of State** seeks to protect donors and charitable organizations in regard to charitable solicitation and giving. If your organization solicits contributions, it may be subject to registration requirements set forth in the Tennessee Charitable Solicitations Act, Tenn. Code Ann. §§ 48-101-501, et seq., unless it is exempt (see next page). The Charitable Solicitations Act requires charitable organizations who solicit contributions from, or within, the State to register annually with the Division of Charitable Solicitations and Gaming.

A charitable organization is defined as a "a group which is or holds itself out to be a benevolent, educational, voluntary health, philanthropic, humane, patriotic, religious or eleemosynary organization, or for the benefit of law enforcement personnel, firefighters, or other persons who protect the public safety, or any person who solicits or obtains contributions solicited from the public for charitable purposes."

Due dates of registration:

- **Initial Registration of Charitable Organization**
  Before commencing any solicitation
- **Annual Registration**
  Due on or before 6 months after fiscal year end
- **Professional Solicitors**
  Due each year on or before December 31

Registration involves the submission of an application along with a summary of financial statement and IRS Form 990 (if required to file), list of board members, contracts with professional fundraisers, and an application fee. In addition to charitable organizations, professional solicitors (professional fundraisers) working on behalf or with charitable organization are also required to register. Fundraising counsels (consultants), on the other hand, still operate but are no long er required to register. (See "Board Engagement" for definitions and examples of professional solicitors, and the difference between professional solicitors and fundraising counsels.)

Charitable Solicitation and Consumer Protection, *continued*

Organizations that are exempt from registration:

- Bona fide religious institutions
- Educational institutions and school support organizations
- Cooperative scholarship corporations regulated by title 49, chapter 4, part 1
- Volunteer fire departments, rescue squads or local civil defense organizations
- Community fairs, county fairs, district fairs and division fairs, as defined in§ 43-21-104, that have been qualified by the commissioner of agriculture to receive state aid grants, pursuant to title 43, chapter 21, part 1
- Political parties, candidates for federal or state office, and political action committees required to file financial information with federal or state election commissions
- Hospitals and nursing homes that are subject to regulation by the Tennessee Department of Health
- Any corporation established by an act of congress of the United States that is required by federal law to submit annual reports of its activities to congress containing itemized accounts of all receipts and expenditures after being fully audited by the department of defense

Overall, while the Division assists thousands of organizations annually with registration, the Division also seeks to prevent false, misleading, deceptive or unfair charitable solicitation activity. As stated earlier in this handbook, Tennessee is a generous state and unfortunately, individuals try to take advantage of that charitable spirit. If an individual or organization acts in false, misleading, deceptive or unfair manner, civil penalties of up to $5,000 per violation may be assessed in addition to other possible enforcement actions. It is important that a donor know to whom he or she is giving and if that trust is broken, individuals or organizations must be held accountable.

Protecting Your Nonprofit from Data Breaches

Nonprofits, like their for-profit counterparts, may keep sensitive information about the members and donors they serve as well as employees and volunteers. It is important for a nonprofit organization to have a sound security plan in place to ensure this personal and financial information is protected from hackers and unscrupulous persons who may have access to such information. Data breaches are often crimes of opportunity, meaning that hackers may look for vulnerabilities in businesses of all sizes, even small nonprofits. Your organization, like other nonprofits, may house personal and financial data such as donor information, event registrations, medical information, employee records, and social security numbers. Many nonprofits have not yet adopted robust and current policies to adequately secure their data. If a data breach occurs, the harm extends not only to the individuals whose data was compromised, but to the nonprofit itself, which faces potential liability for the breach as well as reputational harm. Nonprofit board members should lead the organization in conducting a risk assessment of a potential data breach by taking the following steps:

- Identify and take inventory of all data that the nonprofit collects;
- Identify where and how such data is stored and assess the cost versus benefit of maintaining that data according to current practices;
- Identify who within the organization is responsible for keeping the data; and,
- Evaluate the risk for any outside vendors the nonprofit uses which may have relevant data affecting your organization, including accountants, IT services, payroll services, professional fundraisers, cloud storage services, and donation processing services.

After such information has been identified, board members should actively be involved with the development of internal privacy policies to ensure data privacy issues are dealt with consistently and legally. Key people within the nonprofit should be appointed to maintain such policies. Further, the nonprofit should develop an incident response plan that enables it to quickly and effectively respond to a data security incident. The incident response plan should be shared with key people inside the nonprofit's organization, such as its legal, IT, communications, and human resources teams, as well as any key people outside of the organization. It is important for the incident response plan to be kept up-to-date and shared with appropriate staff members during times of employment transition.

In addition, a nonprofit should consider providing cyber security trainings to its board members, officers, and staff, or work with outside consultants who specialize in cyber security best practices. A nonprofit should evaluate any cyber security protections in place with existing insurance policies, such as E&O policies, or consider whether to bear the expense of a separate cyber insurance policy. Finally, a nonprofit should take necessary steps within its budget to ensure that it's software and hardware are up to date, and regularly back up data so that its business operations may remain in place in the event of a cyber security attack.

As board members, it is important to remember that your nonprofit bears a legal and ethical responsibility to handle and protect the personal and/or financial data of donors, employees, and others.

Charitable Trusts and Private Foundations

Your nonprofit may be the beneficiary of a **charitable trust**. Charitable trusts are trusts created for the relief of poverty, the advancement of education or religion, the promotion of health, governmental or municipal purposes, or other purposes the achievement of which is beneficial to the community. Charitable trusts are subject to the provisions of the Tennessee Uniform Trust Code, Tenn. Code Ann. §§ 35-15-101, et seq., and may also be subject to the provisions of the Charitable Beneficiaries Act of 1997, Tenn. Code Ann. §§ 35- 13-101, et seq., the Uniform Prudent Investors Act, Tenn. Code Ann. §§ 35-14-101, et seq., and the Uniform Prudent Management of Institutional Funds Act, Tenn. Code Ann. §§ 35-10-201, et seq. Under the Uniform Trust Code, the Attorney General is given the status of a qualified beneficiary. As such, the Attorney General is required to be a party in any judicial or nonjudicial proceeding involving a charitable trust.

Your nonprofit may also be the beneficiary of a **restricted charitable gift** or donation. A restricted charitable gift is any gift clearly intended for any purpose commonly considered to be charitable or charitable under Tennessee law or the Internal Revenue Code. Restricted charitable gifts may be subject to the Charitable Beneficiaries Act of 1997. Under that Act, the Attorney General is given the statutory duty to represent the interest of charitable beneficiaries, potential charitable beneficiaries and the people of the State of Tennessee in all proceedings involving charitable gifts, and charitable trusts.

The Internal Revenue Service requires **private foundations** to provide copies of Form 990-PFs to state attorneys general. To determine whether your foundation must send a copy of its 990-PF to the Tennessee Attorney General's Office, consult the IRS website at **http://www.irs.gov**. Mail copies of the forms to the following address:

Tennessee Attorney General
Attn: Library
P. O. Box 20207
Nashville, TN 37202-0207

If a private foundation is not conducting any public solicitation, there is not a requirement to register with the Division of Charitable Solicitations. However, if the private foundation solicits contributions from the public, please contact the Division of Charitable Solicitations at (615) 741-2555 or **charitable.solicitations@tn.gov**.

Protecting Charitable Assets

Your duties include protecting the assets of your nonprofit organization. Tennessee law requires nonprofit organizations to use their assets to fulfill their charitable purposes and not for the benefit of private parties. You must ensure that your nonprofit is using its resources as directed in its articles of incorporation and bylaws. If your nonprofit organization sells assets to or purchase assets from a for-profit company, it is important that the sale or purchase price be fair to your organization.

In addition, Tennessee law requires written notice be provided to the Attorney General before certain extraordinary events, including:

- a merger of your nonprofit organization;
- conversion of your nonprofit corporation to a different entity type (e.g., nonprofit corporation to for-profit corporation, nonprofit corporation to limited liability company, nonprofit corporation to partnership, etc.);
- a sale of substantially all of your nonprofit organization's assets; or
- the dissolution of your nonprofit organization (see page 17, "Dissolving and Terminating a Nonprofit Organization").

Tennessee law requires that notice be given to the **Tennessee Attorney General** of these events **at least 45 days prior to the expected close of the extraordinary event**. Generally, officers of the nonprofit are responsible for providing the appropriate notice to the Attorney General. The board of directors should take steps to ensure that the officers have complied with the law. If the officers have not provided notice, then the board must take action to provide the required notice.

The Attorney General's Office will then request information from your nonprofit organization about the transaction. Depending on the size of the transaction, the information request may be brief or extensive. Model information requests are available for review on the Attorney General's website but may be tailored to your specific transaction.

The Attorney General's Office will assess the information provided to make sure that nonprofit assets are being protected consistent with Tennessee law. In particular, the Attorney General's Office will evaluate the transaction to determine if the nonprofit organization is receiving fair market value for its assets.

Protecting Charitable Assets *continued*

In practice, officers and the board should consider taking the following actions before notifying the Attorney General:

- Keep detailed board minutes discussing the transaction. This shows your board is properly fulfilling its fiduciary obligations.

- Review the Attorney General's model information requests early in the process. Have the staff of your nonprofit begin gathering responsive documents about the transaction so that you can promptly respond to the information request. Failure to respond to the Attorney General's information request in a timely fashion may delay your organization's transaction.

- Depending on the circumstances, seek as many purchasers as possible. While your organization need not automatically sell to the highest bidder, multiple bidders will help show the transaction is fair.

- If there is only a single purchaser, provide independent evidence, such as an independent appraisal, demonstrating the fairness of the transaction.

- Consider contacting the Attorney General's Office more than 45 days prior to the transaction's scheduled closing date. Complex transactions may take significantly more time to evaluate, and the Attorney General's Office can give you an estimate of the time it will take to review the transaction. If the Attorney General's Office does not have enough time to review the transaction before the scheduled closing date, it may seek to delay or block the transaction.

Dissolving and Terminating a Nonprofit Organization

In the course of your service, you may have to make the decision to close a nonprofit organization that, for whatever reason (e.g., lack of funding, fulfillment of purpose, etc.), is no longer able or needed to continue its charitable mission. It is essential that officers and board members continue to fulfill their fiduciary obligations throughout the entire dissolution process. **Dissolution is an extraordinary event that must be reported to the Attorney General before it can be finalized.** After reporting the event, the Attorney General's Office will send your nonprofit an information request packet. If your dissolution is simple, you may only be required to fill out a brief affidavit and provide copies of the nonprofit's organizational documents and recent tax returns (Form 990). If your dissolution is more complex, you will be required to provide more information. A model information request packet and affidavit are available for your review on the Attorney General's website at **https://www.tn.gov/attorneygeneral/working-for-tennessee/reviewing-nonprofits-and-charitable-trusts-gifts.html**.

The Attorney General will need to know the value of your nonprofit's assets and what your organization intends to do with those assets upon dissolution. In general, your nonprofit can only donate its assets to other nonprofits, and some assets may be restricted to a specific purpose. Your nonprofit organization's charter and bylaws may also contain restrictions concerning asset distribution. You are responsible for ensuring that your organization distributes its remaining assets appropriately. You are also responsible for ensuring that such distribution does not take place until the Attorney General's Office completes its review of the dissolution.

Your nonprofit organization will also need to file certain documents with the Tennessee Department of State. Articles of Dissolution and Articles of Termination must be filed with the Division of Business Services and a Notice to Cease Solicitation Activity must be filed with the Division of Charitable Solicitations and Gaming. For more information and forms, please visit **sos.tn.gov/business-services** and **sos.tn.gov/charitable**.

A viable alternative to dissolving a nonprofit corporation may be a merger with another nonprofit corporation. Such an action could continue and even enhance the mission of the organization, while also increasing the ability of the partner agency to serve the community. If a merger is contemplated, it is advisable to involve the board members of each agency on the front end, to create committees to study all aspects of the opportunity, and to lead to votes by the respective boards to move forward.

Public Benefit Hospitals

In 2006 the Tennessee General Assembly passed the "Public Benefit Hospital Sales and Conveyance Act," Tenn. Code Ann. §§ 48-68-201, et seq. Under the new act, any nonprofit or community-owned hospital must provide written notice to the Attorney General **45 days before selling or transferring control of its assets**. The hospital must also certify that each member of its board has been given a copy of the Public Benefit Hospital Sales and Conveyance Act of 2006.

Once the Attorney General receives notice of a proposed hospital sale or transfer of control, the Office of the Attorney General will request additional information from the parties involved in the transaction. In addition, within five days of receipt of notice by the Office of the Attorney General, the hospital must publish notice of the proposed transaction in at least one local, widely read newspaper.

As with other transactions involving nonprofit organizations, sales of public benefit hospitals must be fair to the nonprofit or governmental organizations involved. You should follow the same principles outlined in the section "Protecting Charitable Assets" if your organization is contemplating a hospital sale or transfer of control.

For-Profit Benefit Corporations

In 2015, the Tennessee General Assembly created a new type of corporation: the **for-profit benefit corporation**. The new law took effect on January 1, 2016, and it now enables the creation of a corporation that is both for-profit and also intends to pursue a public benefit or public benefits.

A traditional for-profit corporation is structured in a manner to maximize long term profit for the corporation and its shareholders. However, the key difference of a for-profit benefit corporation is that it must be managed in a way that takes into consideration the public benefit purpose(s) listed in its charter in addition to the financial interests of its shareholders. "Public benefit" means a positive effect or reduction of negative effects on one or more categories of persons, entities, communities, or interests, other than shareholders in their capacities as shareholders, including, but not limited to, an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific, or technological effect.

While both types of for-profit corporations are required to file an annual report each year with the Tennessee Secretary of State Business Services Division, the for-profit benefit corporation also must prepare an Annual Benefit Report and share that report with its shareholders and the public. At this time, there is no special tax exemption for a for-profit benefit corporation; it is taxed the same as a traditional for-profit corporation.

The Office of the Attorney General

The **Tennessee Attorney General** has broad oversight and authority over Tennessee nonprofit organizations. If you have questions concerning the Attorney General's oversight of nonprofits under the Tennessee Nonprofit Corporation Act, please contact the Public Interest Division at (615) 741-5573. Please note that the Attorney General cannot provide legal advice to you or your nonprofit. If your organization requires specific legal advice, the Tennessee Bar Association offers information about obtaining an attorney on their website at **http://www.tba.org/info/find-an-attorney**.

Resource

Tennessee Attorney General's Office:
http://attorneygeneral.tn.gov/nonprofit/nonprofit.html

The Attorney General's website includes Tennessee statutes relevant to nonprofit organizations, model information requests, and information concerning the Attorney General's oversight of nonprofits.

The Tennessee Department of State

As a nonprofit organization, the **Tennessee Department of State** has two Divisions that you need to be aware of as a board member.

Division of Business Services

The Secretary of State's Division of Business Services is responsible for processing documents filed pursuant to the Tennessee Nonprofit Corporation Act. To learn more about the incorporation and filing annual reports, call (615) 741-2286, email **tnsos.corpinfo@tn.gov** or visit **sos.tn.gov-/business-services**.

Division of Charitable Solicitations

The Secretary of State's Division of Charitable Solicitations and Gaming is responsible for administration and enforcement of the Tennessee Charitable Solicitations Act and Tennessee Nonprofit Gaming Law. To inquire about the annual registration of charitable organizations, professional solicitors or annual gaming events, call (615) 741-2555, email **charitable.solicitations@tn.gov** or visit **sos.tn.gov/charitable**.

If your organization is an eligible Internal Revenue Code 501(c)(3) or 501(c)(19) organization, it may apply to hold one annual gaming event pursuant to the Tennessee Nonprofit Gaming Law, Tenn. Code Ann. §§ 3-17-101, et seq. An eligible organization must meet the following requirements:

- Must have IRS Tax Exempt Status as a 501(c)(3) or 501(c)(19) for a minimum of 5 years
- Must have a physical presence in the State of Tennessee for a minimum of 5 years
- Must be registered with the Division of Charitable Solicitations

Additionally, the types of gaming events allowed are raffles, reverse raffles, cakewalks and cake wheels. In order to apply, an eligible organization must submit an application and fee during the open application period beginning July 1 and ending on January 31. Once an application is received by the Division and meets all the requirements, an omnibus list is submitted to both chambers of the Tennessee General Assembly and must be passed by a two-thirds vote. Upon approval, the organization may conduct the annual gaming event on the date it applied for between July 1 and June 30 of the following year.

Capacity-building in the Nonprofit Sector

Four management support organizations in the state provide services for nonprofit organizations. See below for information about the capacity-builder in your region.

CNM
Center for Nonprofit Management

Based in Nashville, the **Center for Nonprofit Management** is a management support organiztion that amplifies the impact of nonprofits and their partners. CNM provides education and consulting to build capacity for community benefit work, and recognizes nonprofit excellence through the annual Salute to Excellence ceremony. Additional information, including board trainings and opportunities specifically for board members, can be found at **www.cnm.org**.

VENTURE FORWARD
Advancing Nonprofits

In Chattanooga, **Venture Forward** inspires and sparks positive momentum for nonprofits and the community, through the sharing of information, providing training and professional development, and encouraging collaboration. Visit **www.ventureforwardnow.org** for more information.

MOMENTUM NONPROFIT PARTNERS

Momentum Nonprofit Partners, located in Memphis, builds the momentum of the nonprofit sector to create equitable, measurable, and lasting change. Their work includes an annual conference, professional development, public policy and research, community collaborations, and more. Visit **momentumnonprofitpartners.org** to learn more.

Alliance for Better Nonprofits

Located in Knoxville, **Alliance for Better Nonprofits** (ABN) is a training, consulting, and resource center for the nonprofits of East Tennessee. ABN provides opportunities for members to learn, grow, and engage in a powerful way. Learn more at **www.betternonprofits.org.**

Other Resources

- **National Association of State Charity Officials**

  http://www.nasconet.org

  The National Association of State Charity Officials (NASCO) is an association of state offices charged with oversight of charitable organizations and charitable solicitations in the U.S. The NASCO website offers news relevant to government regulation of charities, contact information for state charity officials, and other state, federal, and national resources.

- **National Center for Charitable Statistics**

  http://nccs.urban.org

  A project of the Urban Institute and an excellent resource of nonprofit data.

- **Internal Revenue - IRS Tax Information for Charities & Other Non-Profits**

  https://www.irs.gov/Charities-&-Non-Profits

  The Internal Revenue Service's Tax Information for Charities and Other Non-Profits webpage offers information to charitable organizations seeking 501(c)(3) status. The site includes information on the lifecycle of nonprofit organizations, tax guidance, and instructions and training for the new Form 990.

- **Internal Revenue Service – EO (Exempt Organization) Select Check**

  https://www.irs.gov/Charities-&-Non-Profits/Exempt-Organizations-Select-Check

  An online search function to verify if an organization is able to accept tax-deductible contri butions, filed a IRS 990N E-Postcard or had its tax-exempt status revoked and/or reinstated.

- **Giving Matters**

  http://www.givingmatters.com

  An online database of high-quality, comprehensive information about more than 1,400 Middle Tennessee nonprofits.

- **WHEREtoGIVEmidsouth**

  http://www.wheretogivemidsouth.org

  An online directory of nonprofit organizations in the greater Memphis area.

Other Resources *continued*

- **Independent Sector's "Principles for Good Governance and Ethical Practice"**

  https://www.independentsector.org/principles

  A guide outlining 33 principles of sound practice for charitable organizations and foundations related to legal compliance and public disclosure, effective governance, financial oversight, and responsible fundraising.

- **BBB Wise Giving Alliance**

  http://www.give.org

  The BBB Wise Giving Alliance helps donors make informed giving decisions, promotes high standards of conduct among charitable organizations, produces reports about national chari ties, and more.

- **Nonprofit related news and periodicals**

  - **Board Source**

    https://www.boardsource.org/eweb

  - **Chronicle for Philanthropy**

    https://philanthropy.com

  - **Nonprofit Quarterly**

    https://nonprofitquarterly.org

  - **Nonprofit Times**

    http://www.thenonprofittimes.com

  - **Center for Nonprofit Management's 2013 Nonprofit Economic Impact Study**

    http://www.cnm.org/getattachment/Resources/Links/The-Nonprofit-Sector-in-the-Nashville-MSA/CNM-Final-Report.pdf

APPENDIX

Glossary

Board directors: board members are referred to as directors in the Tennessee Nonprofit Corporation Act; however, nonprofits themselves usually use the term "board members." (See "Fulfilling Your Fiduciary Duties." Also see glossary definition of "board members" and "nonprofit officers.")

Board members: responsible for directing the overall vision and mission of the nonprofit corporation. (See "Fulfilling Your Fiduciary Duties." Also see glossary definitions of "board directors" and "nonprofit officers.")

Charitable trust: a trust that is not tax exempt, all of the unexpired interests of which are devoted to one or more charitable purposes, and for which a charitable contribu¬tion deduction was allowed under a specific sec¬tion of the Internal Revenue Code; a charitable trust is treated as a private foundation unless it meets the requirements for one of the exclu¬sions that classifies it as a public charity. *IRS definition.* (See "Charitable Trusts and Private Foundations.")

Division of Business Services: a division of the Tennessee Department of State responsible for processing documents filed pursuant to the Tennessee Nonprofit Corporation Act. (See "The Tennessee Department of State.")

Division of Charitable Solicitations and Gaming: a division of the Tennessee Department of State responsible for administration and enforcement of the Tennessee Charitable Solicitations Act and Tennessee Nonprofit Gaming Law. (For more, see "Charitable Solicitation and Consumer Protection" and "The Tennessee Department of State.")

Donor-advised fund: a separately identified fund or account composed of contributions made by individual donors who retain advisory privileges with respect to the distribution of funds and the investment of assets in the account, but maintained and operated by a nonprofit. *IRS definition.*

For-profit benefit corporations: a new type of corporation in Tennessee as of January 1, 2016 for corporations intending to pursue public benefit. (See "For-Profit Benefit Corporations.")

Nonprofit officers: responsible for the day-to-day management of the nonprofit. (See "Fulfilling Your Fiduciary Duties." Also see glossary definitions of "board directors" and "board members.")

APPENDIX

Glossary *continued*

Private foundations: a nongovernmental, nonprofit organization having a principal fund managed by its own trustees or directors. It differs from a 501(c)3 charity because public charities generally derive their funding primarily from the general public whereas private foundations usually derive principal fund from a single source. *Definition from* ***grantspace.org***. (See "Charitable Trusts and Private Foundations.")

Professional solicitor: a person or entity who, for financial or other considerations, solicits on behalf of a charitable organization. (See "Board Engagement.")

Professional fundraising counsel: any person or entity who, for compensation, plans, manages, advises, consults or prepares material for a charitable organization for the solicitation of contributions. (See "Board Engagement.")

Restricted charitable gift: any gift clearly intended for any purpose commonly considered to be charitable under Tennessee law or the Internal Revenue Code. (See "Charitable Trusts and Private Foundations.")

Tennessee Attorney General: a state office with broad oversight and authority over Tennessee nonprofits. Nonprofit board members can contact this office with any questions about the Tennessee Nonprofit Corporation Act. (See "Protecting Charitable Assets" and "The Office of the Attorney General.")

Tennessee Department of State: includes the Division of Business Services and the Division of Charitable Solicitations. (See "Charitable Solicitation and Consumer Protection" and "The Tennessee Department of State.")

APPENDIX

Top Ways to Get Investigated by the Office of the Attorney General

1. Improper conflicting interest transactions

2. Unreasonable executive compensation

3. Failure to follow mission of nonprofit

4. Breach of fiduciary duties

5. Failure to resolve festering disputes among board members, or between board members and staff, or between the nonprofit and donors or volunteers

6. Failure to use restricted gifts in accordance with donor's intent and/or misuse or charitable assets

7. Lending money to directors or officers in violation of the Nonprofit Corporation Act (loans include salary advances, personal use of corporate credit cards, etc.)

8. Unnecessarily complex transactions or organizational structure

9. Failure to adopt and/or follow policies governing financial matters, human resources, conflicting interest transactions

10. Sale of your organization's assets or dissolve without notifying the Attorney General's office in advance/improper dissolution or termination of a nonprofit

11. Failure to keep adequate records and failure to make records available to directors, members, and AG

APPENDIX

Seven Tips from the Division of Charitable Solicitations and Gaming

1. Check to see if your organization is registered with the Division of Charitable Solicitations and Gaming or is exempt from annual registration.

2. If you raise money outside of Tennessee, you may be required to submit and register your charitable organization in other states. For more information, visit the National Association of State Charity Officials at **www.nasconet.org**.

3. If your nonprofit hires a company or individual to raise money via direct mail, special events, telemarketing, online, or by providing consultation services, they will need to register as a professional solicitor.

4. Protect your brand. Individuals, organizations and online platforms may be raising funds or seeking support without your consent or knowledge.

5. Verify that your organization is current with its annual corporate filings in the Division of Business Services.

6. To verity or inquire about tax exempt status with the Internal Revenue Service (IRS), visit **https://www.irs.gov/Charities-&-Non-Profits** or call (888) 829-5500.

7. If you are aware of unfair, false, misleading, or deceptive activity regarding charitable fundraising in your community, contact the Division at (615) 741-2555 or **charitable.solicitations@tn.gov**.

This guidebook was prepared by the offices of:

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