

Office of the Attorney General

A GUIDE TO NON-PROFITS



ADAM PAUL LAXALT
ATTORNEY GENERAL

INTRODUCTION

Directors of Nevada nonprofit corporations are responsible for management of the business and affairs of the organization. This does not mean that the directors are responsible for the day-to-day operation of the nonprofit corporation. Rather, directors are responsible for appointing officers to effectively carry out the daily tasks of running the organization. Directors must supervise and direct the officers, and govern the organization's effort to accomplish its charitable or public purpose. In this regard, the law imposes upon directors the fiduciary duties of care, loyalty and obedience to the law. To enable you to meet these obligations, the law affords you certain rights.

Your duties and rights as a director are related to creation of the nonprofit corporation to promote a charitable or public purpose as opposed to obtaining a private benefit. A nonprofit organization is primarily funded by grants, donations, and fund raising activities. The donor or grantor expects that the organization will use the contribution to achieve the particular public benefit. In a conventional sense, the nonprofit corporation does not own the property which it receives from donors. Instead, it holds the property in "trust" for a specific public purpose.

The directors' rights and duties of care, loyalty and obedience to the law protect this public trust from abuse. Misappropriating or wasting contributions violates the public trust which the organization's directors and officers have assumed. The consequences of violating the public trust may be severe for the organization and its individual directors. The nonprofit organization itself, however, may be held liable for negligent or wrongful acts of its employees or agents. In an extreme case, the organization may be dissolved. Under Nevada Revised Statutes (NRS) 41.480, a director may be held

personally liable for injuries caused by the director's intentional misconduct, fraud, or knowing violation of the law. If, on the other hand, the director exercises due care in managing the nonprofit organization, the director is immune from liability.

This guide will discuss your rights and duties, along with some of the applicable Nevada statutes. Chapter 82 of the NRS governs the formation and operation of Nevada nonprofit organizations. Directors should review a current version of this statute. Since the state legislature may amend these statutes, directors should refer to the text of the statutes to learn about any changes affecting their responsibilities since the publication of this edition. This guide is not intended to prescribe the exact manner in which you must act in all situations. For more specific information or advice, you may contact a private attorney or one of the resources available in the nonprofit community.

DUTY OF CARE

Directors of Nevada nonprofit corporations must discharge their duties in good faith and in a manner which the director reasonably believes to be in the best interests of the organization. NRS 82.221(1). **The director is held to a "reasonable person" standard, which means the director must exercise the care an ordinarily prudent person would exercise under similar circumstances. The exercise of due care includes:**

1. Active Participation

- ✓ Actively participate in the management of the nonprofit organization. This includes **attending meetings of the board, evaluating reports, reviewing performance of executive officers,** and setting the executive officer's compensation.
- ✓ Receive information beforehand about matters upon which you will vote in meetings. **Ask questions and use your own judgment.**
- ✓ Beware of the one person show. That is, if one or two directors dominate the board and the organization's activities, do not relax and assume everything is running smoothly. "Nonmanagement" is the quickest route toward trouble. Also, do not allow staff to exercise undue control over the board. **Be aware of, and informed about, every major action taken by the organization. The buck stops with you.**

2. Following the Money

- ✓ **Be involved and informed in all aspects of the finances** of the nonprofit organization.

- ✓ **Make sure a realistic annual budget is developed.** The organization should have an adequate internal accounting system. Require management to produce timely and accurate income and expense statements, balance sheets, and budget status reports.
- ✓ **Obtain confirmation from management that all required filings, (such as tax returns) are submitted** and employee withholding taxes and insurance premiums are paid in a timely manner.
- ✓ **Consider maintaining a standing audit and finance committee.**
- ✓ Adopt an **investment policy** that requires funds to be deposited in federally insured, interest bearing accounts. If the board desires to invest larger sums in securities, select only those securities with a history of stability, growth, and a good payment record. Do not subject public funds to high risk investments.
- ✓ Above all, **make certain the funds are being used for the organization's charitable or public purpose.** Administrative expenses and promotional expenses, including compensation of employees and independent contractors, must be commensurate with the organization's financial resources and capabilities. If an organization raises funds for a charitable purpose but consistently uses virtually all its income for administrative and promotional expenses with little or no distribution to the charitable purpose, the board has failed to exercise due care.

3. Hiring Professional Fund Raisers

- ✓ When hiring a professional fund raiser, select one who is trustworthy and fiscally responsible. Ask for references

and check with law enforcement agencies and philanthropic resource organizations.

- ✓ Make sure any contract with a professional fund raiser or consultant, especially compensation terms, is fair and reasonable in light of the organization's financial resources and capabilities. Consult with an attorney to review fund raising contracts.
- ✓ Beware of fraudulent "telefunders" and other fraudulent fund raisers seeking to solicit funds on behalf of the nonprofit organization. Fraudulent telefundors obtain large sums of money from individual donors by misleading them into believing they will receive a prize worth more than their donation. Typically, fraudulent telefundors target elderly victims and award prizes worth far less than the donation. The nonprofit organization receives a small percentage of the fraudulently obtained funds. Dealing with fraudulent fund raisers can harm the nonprofit organization's reputation, jeopardize its tax exemption status, and expose it and the directors to potential liability. Telefundors are required to be registered with the Consumer Affairs Division and misrepresentation in soliciting funds is a prohibited deceptive trade practice, subject to civil and/or criminal prosecution.

4. **Records, Records, Records**

- ✓ Be familiar with the contents of the organization's books and records, including the **articles, bylaws, accounting records, and minutes.**
- ✓ **Written minutes should be taken at every board meeting.** Minutes must accurately record the votes cast and identify the names of those in the minority on any question. Minutes should be signed, circulated to the board members for review, and presented for approval.

- ✓ Financial records should be regularly audited by an independent accountant to ensure accuracy.

5. **Forming Committees**

- ✓ Unless otherwise provided in the articles or bylaws, directors may establish committees which exercise the powers of the board in a manner consistent with resolutions or bylaws. At least one director must be a committee member. NRS 82.206.
- ✓ Committees cannot: amend, alter or repeal the articles or bylaws; elect, appoint or remove committee members, directors, or officers; authorize the transfer of all the organization's property or assets; dissolve the organization; adopt a plan for distribution of the assets. Such a committee may not amend, alter, or repeal a board resolution unless permitted to do so by the resolution. NRS 82.206(4)

6. **Conducting Investigations**

- ✓ Investigate warnings or reports of theft or mismanagement by officers or employees of the organization.
- ✓ Where appropriate, consult with an attorney or other professional for assistance.

7. **Knowing your Rights**

- ✓ You have the right to obtain the information necessary to enable you to carry out your responsibilities as a director.
- ✓ You have the right to reasonable access to management.
- ✓ You have the right to inspect the internal information of the organization. Under NRS 82.186, directors are

entitled to inspect the books of account and all financial records during normal business hours. This right may be enforced in court as long as the director has given at least five days written demand to access the information and will use the information for a purpose related to the role as director.

- ✓ Directors are entitled to rely on the reports, opinions, financial records, or other information prepared by directors, officers, employees, committees, attorneys, and accountants as long as the director does not have knowledge which would cause such reliance to be unwarranted. NRS 82.221(2)(c).

DUTY OF LOYALTY

Traditionally, directors have a duty to give their **undivided loyalty to the nonprofit corporation**. This duty requires board members **to use the organization's funds and property to advance the public benefit of the organization rather than private interests**. A potential conflict of interest between the duty of loyalty and a board member's private financial interests may arise if the board member engages in a business transaction with the nonprofit organization. Moreover, a board member's receipt of a financial benefit from the organization creates a negative public perception. **To exercise the duty of loyalty:**

1. **Avoid Detrimental Conflicts of Interest**. A red flag should fly when board members are asked to approve a contract or transaction with a director, a director's family member, or a business in which a director has a financial interest. **Before voting on the transaction, the interested board member should fully disclose his or her financial interest to the entire board**. The board should only approve the transaction if it is clearly in the best interests of the nonprofit organization. As a further precaution, the interested director should abstain from discussion of, and voting on, the matter.

2. **Establish a Written Policy.** The board should establish a written policy for dealing with conflicts of interest. The policy should address disclosure of financial interests and withdrawal from discussion and voting by the interested director. Due to the sensitivity of conflicts of interest, the board may want to require that transactions benefiting a director may be approved only by a greater than majority vote or prohibit such transaction all together. Also, requiring an **annual disclosure** by all board members of their business involvement with the nonprofit organization is recommended.

3. **Misuse of Corporate Information.** Directors cannot use information, documents, records or other data obtained from the nonprofit organization for a purpose unrelated to the organization's interest. For example, a director breaches the duty of loyalty by selling the organization's donor list for personal gain. **A misappropriation of corporate information may subject the director to criminal liability** under NRS 82.186(3).

DUTY OF OBEDIENCE

Board members have a duty to obey the governing documents of the nonprofit organization and comply with state and federal laws. **To exercise the duty of obedience:**

1. **Obey State and Federal Statutes.** Directors should be familiar with state and federal laws relating to nonprofit organizations, charitable solicitations, sales and use taxes, FICA and income tax withholdings, and workers' compensation obligations. Detailed information of Nevada's law governing charitable solicitations and lotteries follows this section. Directors should also be aware of the requirements of the Internal Revenue Service to **protect the organization's tax exemption status.**

2. **Meet Filing Requirements.** Comply with the deadlines for filing tax returns, paying income tax withholdings, making social security payments, registering with the Secretary of State's Office, and so on.
3. **Comply with Governing Documents.** Know and adhere to the provisions in the organization's articles of incorporation and bylaws. Make sure the board is regularly holding meetings, receiving proper notice of the meeting, and following the procedures for voting on matters.
4. **Seek Outside Help.** To ensure compliance with the law, board members should obtain the assistance of legal counsel, accountants or other qualified people.

CHARITABLE SOLICITATION

Charitable Solicitation Act in Nevada

Between 1993 and 1995 the Federal Government and many of the states' Attorneys General engaged in several initiatives aimed at fraudulent telemarketers. It was during this campaign against telemarketing fraud that it became apparent that some legitimate charitable nonprofit organizations had unwittingly contracted with fraudulent telemarketers to raise funds for them. The Attorney General then sponsored legislation to address the fraudulent practices these illegitimate telemarketers were employing. And in 1997, the Nevada Legislature enacted the Charitable Solicitation Act (NRS 598.1305) which prohibits certain conduct by a charitable organization.

1. **Application of the Law.** The Charitable Solicitation Act applies to any charitable organization which directly or indirectly solicits contributions. "Charitable organization" means any person or organization which:
 - ✓ Is tax exempt pursuant to the provisions of section 501(c)(3) of the Internal Revenue Code; or
 - ✓ Is, or holds himself out to be, established for a charitable purpose.

The term does not include organizations which solicits for bona fide religious purposes.

"Solicitation" means any request for a contribution to a charitable organization, made from Nevada or from outside Nevada to Nevada residents, by:

- ✓ Mail;
- ✓ Commercial carrier;
- ✓ Telephone, facsimile or other electronic device; or
- ✓ A face-to-face meeting.

2. **Prohibited acts.** It is illegal for a person, in planning, conducting or executing a solicitation for or on behalf of a charitable organization to:

- ✓ Make any statement or representation concerning a contribution which directly, or by implication, **deceives or misleads** a person acting reasonably under the circumstances; or
- ✓ Make any statement or representation which **omits any material fact**, if the omission has the tendency or effect of deceiving or misleading a person acting reasonably under the circumstances.

3. **Liability.** The scope of liability for nonprofit corporations, its directors and officers is contained in NRS 41.480 and 41.485.

- ✓ A nonprofit corporation liable for injuries or damages caused by the negligent or wrongful acts of the nonprofit organization through:
 1. Its agents;
 2. Its employees; or
 3. Its volunteers.
acting within the scope of their agency or employment.

- ✓ “Agent” means an:
 1. Officer;
 2. Director;
 3. Trustee;
 4. Employee; or
 5. Volunteer.
whether compensated or not .

- ✓ “Volunteer” means a person who performs services without compensation, other than reimbursement for actual and necessary expenses on behalf of or to benefit a charitable organization, including its:
 1. Officers;
 2. Directors;
 3. Trustees; or
 4. Other persons working for the organization without compensation.

- ✓ A non-volunteer officer, trustee, or director of a nonprofit organization is personally liable for act or omissions arising from failure in his official capacity to exercise due care regarding the management or operation of the entity where the act or omission involves:
 1. Intentional misconduct;
 2. Fraud; or
 3. A knowing violation of the law.

- ✓ A volunteer officer, trustee, or director is not liability for civil damages as a result of an act or omission:
 1. Of an agent of the charitable organization; or
 2. For services he performs for the charitable organization that are:
 - a. Not supervisory in nature;
 - b. Not part of any duties or responsibilities he may have as an officer, director or trustee of the charitable organization;unless his act is intentional, willful, wanton or malicious.

5. **Jurisdiction.** The Attorney General has the primary jurisdiction to investigate and prosecute violations of NRS 598.1305 as deceptive trade practice.

6. **Penalties.** Violation of the Charitable Solicitation Act carries both civil and criminal penalties. NRS 598.0999.
 - ✓ Civil Penalties may include:
 1. A civil penalty not to exceed \$2,500 for each violation.
 2. If an elderly or disabled person is the victim, an additional penalty of up to \$10,000 for each violation (NRS 598.0973).
 3. Reasonable attorneys fees and costs; and
 4. Other relief or reimbursement as the court deems proper.

 - ✓ Criminal Penalties include:
 1. For the first offense, a misdemeanor.
 2. For the second offense, a gross misdemeanor.
 3. For the third and all subsequent offenses, a category D felony

This law was enacted to protect donors and legitimate charitable nonprofit organizations from unscrupulous fund raising practices.

CHARITABLE LOTTERIES

Since the passage of the Nevada Constitution in 1864, lotteries have been generally prohibited in Nevada. Nevada Gaming Commission Regulation 4A and Nevada Revised Statutes Chapter 462 continues in this historic prohibition against lotteries, but now makes an **exception for charitable lotteries.**

A lottery is usually defined as any promotional scheme comprised of the common elements of prize, consideration and chance. NRS 462.105 defines a lottery as follows:

... 'Lottery' means any scheme for the disposal or distribution of property, by chance, among persons who have paid or promised to pay any valuable consideration for the chance of obtaining that property, or a portion of it, or for any share or interest in that property upon any agreement, understanding or expectation that it is to be distributed or disposed of by lot or chance, whether called a **lottery, raffle or gift enterprise,** or by whatever name it may be known.

CHARITABLE LOTTERY REGULATION

In 1989, the Nevada Legislature authorized the amendment of the Nevada Constitution to permit charitable lotteries, by way of a ballot measure. In 1990, the voters passed the amendment to the Constitution and in 1991, the Legislature authorized **limited** charitable lotteries.

The Charitable Lottery program is governed by the Enforcement Division of the Office of the **State Gaming Control Board.** The Enforcement Division can provide specific guidance as to the current law. However, there are some restrictions to the current law and we have outlined them for your reference:

- 1) A charitable lottery must be conducted by a bona fide charitable or nonprofit organization.
- 2) The registration or approval requirements with the Gaming Control Board are different depending on the size of the lotteries. The maximum total value during the same calendar year cannot exceed \$500,000. Generally speaking, the requirements become less rigorous as the value of the prizes in a calendar year become smaller.
- 3) Lottery tickets may only be sold in the primary county in which the charity is located and the counties that border the primary county.
- 4) The law also contains limitations on the amount of compensation that can be expended for prizes, supplies and payment for services to those operating the lottery.
- 5) The net proceeds of the lottery must be utilized for the nonprofit or charitable activities in this state.

Questions regarding the approval process or copies of the necessary forms can be obtained from:

Office of the State Gaming Control Board
Enforcement Division
555 E. Washington, Suite 2600
Las Vegas, Nevada 89101
(702) 486-2020