

Legal Counsel for Churches

October | 2023

Corporate Governance for Churches & Their Leaders

M SMITH | LAW PLLC



Prohibited Activities for Churches

prohibition. Allowing a candidate to use a church's assets or facilities will also violate the prohibition if other candidates are not treated the same.

Churches are automatically considered nonprofit organizations under the Internal Revenue Code. As such, these religious institutions enjoy limited privileges and protections. Church leaders should understand what churches may and may not do. The consequences for making an error could be dire for a ministry.

According to the IRS Publication for nonprofits, certain activities are prohibited or restricted for organizations exempt from federal income tax under Section 501(c)(3). Here is a list of restricted activities that apply to churches.

Refrain From Supporting or Opposing Candidates in Political Campaigns

Churches are prohibited from directly or indirectly participating in, or intervening in, any political campaign on behalf of (or in opposition to) any candidate for elective public office. (Fed, State or local races)

Political campaign intervention includes any and all activities that favor or oppose one or more candidates for public office. Contributions to political campaign funds or public statements of position (verbal or written) made by or on behalf of a church in favor of or in opposition to any candidate for public office clearly violate this rule.

Distributing statements prepared by others that favor or oppose any candidate for public office will also violate the

Churches are permitted to conduct neutral voter education activities (including the presentation of public forums and the publication of voter education guides) if they are carried out in a non-partisan manner.

Ensure That Net Earnings Do Not Inure in Whole or in Part to The Benefit of Insiders

A church should not operate for the sole benefit of private shareholders or individuals. The term "private shareholder or individual" refers to persons who have a personal and private interest in the organization, such as an officer, a director, or a key employee. Any amount of personal benefits may be grounds for loss of tax-exempt status.

Operate for the Primary Purpose of Conducting a Trade or Business that is Unrelated to Exempt Purpose(s)

A prohibited activity is an unrelated trade or business if it is regularly carried on and is not substantially related to furthering the exempt purpose(s) of the church.

The term "trade or business" generally includes any activity conducted for the production of income from selling goods or performing services.

Business activities of an exempt organization ordinarily are considered regularly conducted if they show a frequency and continuity similar to, and are pursued in a manner similar to, comparable commercial activities of nonexempt organizations.



Do Not Devote a Substantial Part of Activities to Influence Legislation

If a substantial part of a church's activities consists of carrying on propaganda or otherwise attempting to influence legislation, the ministry does not qualify for tax exemption.

An organization will be regarded as attempting to influence legislation if it contacts, or urges the public to contact, members or employees of a legislative body for the purpose of proposing, supporting, or opposing legislation, or if the organization advocates the adoption or rejection of legislation.

Church leaders should consult with their legal counsel if an activity appears in doubt. The cost of a mistake here could lead to losing the church's nonprofit status. ■

Forming an Independent Church Auxiliary



Occasionally, leaders decide there is a need to form a new auxiliary or affiliate to the church. The new institution may be created for various purposes.

In some instances, a new institution is launched to serve as an extension of the ministry. In other circumstances, the church seeks to pursue business opportunities to support its charitable works.

When it is decided that a separate corporation is desired, the church should go about starting the entity in an orderly way. This is important to establish independence and control risks. Here are some necessary steps for forming a new corporation.

Church leaders should be very clear about the stated objective. Church management should have specific goals it seeks to attain with the new organization. Having clear intentions in the beginning will help determine important strategic decisions.

Once leadership knows what it wants to achieve, the work begins with choosing *Incorporators* to represent the new corporation until it receives its official documents. The incorporators are the persons who apply for the Articles of Incorporation from the North Carolina Secretary of State.

The incorporators should decide on a name for the new corporation. The name should be one that does not infringe on the intellectual property rights of other companies. The incorporators can conduct a name search at the NC Secretary of State site to make sure the name is available.

The application for the Articles requires deciding who will be the *Registered Agent*. This person is the point of contact to receive official documents for the corporation. The Registered Agent must be 18 years old or older and have a North Carolina address.

After receiving the Articles, the incorporators should approve the initial bylaws and elect the first Board of Directors. The bylaws will describe the purpose of the corporation, the rules of governance, and authority of the officers.

The board of directors has some important decisions to make in the beginning. It should direct that an application be made with the Internal Revenue Service for an *Employer Identification Number*, EIN. This number is akin to the corporation's social security number. This number will be needed for many purposes, regardless of whether the corporation has employees.

The corporation may need a *State Tax Identification* number issued by NC. If the company plans to hire employees in the state, selling taxable goods and services, or may owe excise taxes, the board will want to apply for this Number.

The board of directors should open a separate financial institution account. It is important to avoid commingling funds with the church. The board should appoint a person to manage the financial affairs.

If the corporation is a nonprofit, it may wish to apply for recognition as a *501(c)(3)* organization. This application is made with the Internal Revenue Service. This can be

a rather demanding process, so the board should choose a qualified person to do this.

If the new corporation will be seeking charitable donations, the board should apply for a *Charitable Solicitation License* from the NC Secretary of State. It is unlawful to seek donations in NC without a license.

The new organization will need to focus on how it will be represented to the public. This may involve the creation of a website, letterhead, email account, and marketing materials. Protecting the organization's brand may lead to seeking a *Trademark* or *Service Mark* to ward off imposters.

The board should decide if it needs certain insurance coverages for the organization and its officers. Types of insurance includes a *Fidelity Bond* to protect the institution from the bad acts of its insiders. *Liability insurance* protects the officers from the risks of their decisions. *Property insurance* protects the physical assets. Other special insurance may be necessary depending on the circumstances.

All along, the board should have been talking about the *Strategic Direction* of the organization. Strategy involves setting benchmarks and aligning resources to accomplish its aims. This discussion includes putting policies in place to guide future decisions. Effective corporate governance habits must be practiced.

These are a few of the tasks necessary to get a new organization off the ground. It will be up to church leaders to set the foundation for helping the endeavor be a big success. ■

The Feeling

of achieving a successful legal result.

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Churches Can Be A Lab for Leaders

There is a saying that leaders are not born but are made. This is to suggest that leadership is a trait that can be taught. If this is so, individuals seeking a leadership post should study leadership traits.

The development of new leaders is an important fiduciary duty of church officials. This is often called succession planning. The process of identifying individuals who can step into a leadership role is critical.

Church officials have a unique opportunity to grow its next generation of leaders. Astute leaders understand that transitions will occur in every ministry. No position is held by the same person forever. Preparing for the time when a change will occur is a prudent step.

Churches intent of growing emerging leaders do so for the ministry and the community. Some young people may wonder how to make their way in their chosen professions. But for many, leadership posts can feel elusive at time. For these individuals, the church offers a place where leadership can be developed and nurtured.

Leadership skills include hard and soft skills. The hard skills include the knowledge and abilities to perform in one's chosen discipline. One must master the technical

aspects of the position. In some instances, hard skills are recognized with certifications, licenses, and industry achievements. The proficiency of hard skills is not necessarily an indication of leadership success.

Often overlooked is the necessity of leaders to master soft or interpersonal skills. The importance of so-called soft skills should not be overlooked. Effective leaders understand the importance of being well-rounded in their capability to lead their teams.

The church is referred to as a laboratory because it offers its members opportunities to learn and practice the interpersonal skills needed for leadership elsewhere. Leadership training can be created by encouraging emerging leaders to take the lead in church ministries. These young participants can be invited to contribute thought-leadership on critical issues. The intent is to build one's ability to exercise interpersonal skills.

Many young people must wait for the precious opportunity to practice leadership. This is because advancement opportunity on their jobs can be a scarcity. The challenge for emerging leaders is how one may gain leadership skills before entering an arena where leadership proficiency is needed.

This is one of the value propositions churches offer young members. Members learn the interpersonal skills needed to amplify their technical abilities. These soft skills include social decorum, communication know-how, emotional intelligence, time management, and professional presence.

Emerging leaders should be invited to hone their presentation skills at church. The church audiences can use their life experiences to encourage and coach young members through peer reviews. Members of churches can collaborate with others to build resumes, pick up new experiences, and explore novel ways of thinking about various industries.

The church as a lab can be a full spectrum experience that readies its members for leadership advancement. This is a critical value for the church where new talent is constantly needed for an evolving landscape.

Church members take the skills learned in the various ministries, and departments to advance their careers in the world. This is what a lab does in a controlled environment. Church members are given a platform on which to fine tune their talents.

Young people should think of their church as an extension of their talent development journey. The lessons learned can be some of the same curriculum found in a professional seminar that costs thousands of dollars.

Churches as leadership labs can fulfill a two-fold purpose. Emerging leaders gain valuable skills. Additionally, church leaders meet their needs for succession planning. ■

Legal Counsel for Churches is a service provided by M Smith Law, PLLC for members of the religious community. This periodical is intended to help churches and their officials become better prepared to address important legal and governance issues. We hope you find *Legal Counsel for Churches* a valuable resource. For each issue, we try to raise relevant issues and offer some practical alternatives. We welcome your comments and input.

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