**SOCIAL JUSTICE 102 CREATING NON-PROFITS**

**FROM THE DESK OF THE DEAN**

**CREATING NON-PROFITS**

**TOPIC 2**

When you are deciding if you want to create a non-profit it is paramount for you to understand the 5 common mistakes made.

**1. Not Understanding the Tax Consequences**

Many people think they'll pay less in taxes if they form a particular type of business entity, but this isn't necessarily true. Here are some basics about business entity taxation. It's always a good idea to get advice from a business lawyer or accountant before deciding on a tax structure.

* A sole proprietorship or a general partnership is known as a “disregarded entity" for tax purposes. The owners of these businesses report business income and expenses on their personal tax returns, and pay tax on any profit.
* Corporations can be taxed in two ways. A C corporation pays corporate income tax on its profits. If a C corp pays dividends to its owners (shareholders), they report those dividends on their personal tax returns, and pay tax on them. Many small businesses end up paying more taxes under this “double taxation" system.
* Some corporations can avoid double taxation by being taxed as an S corporation. An S corp. doesn't have to pay corporate income tax. All of its profits “pass through" to the shareholders' personal tax returns, and the shareholders pay personal income tax on them.
* A limited liability company is a chameleon. It is automatically taxed in the same way as a sole proprietor (if there is one owner) or a partnership (if there are multiple owners). But an LLC also can choose to be taxed as a C corporation or an S corporation. Sometimes, corporate tax status allows an LLC's owners to minimize self-employment taxes or to deduct expenses that would not otherwise be deductible.

**2. Thinking You Don't Need a Formal Business Entity**

If your business is a sole proprietorship or general partnership, you and your business are one and the same. That means that your personal assets are at risk if your business is sued or can't pay its debts.

If you form a business entity such as a corporation, LLC, or limited liability partnership (LLP), your business becomes legally separate from you. If there's a judgment against your business, you may lose the money you have invested in it, but you won't lose your house, car, or personal bank account. Not forming a business entity can be a big mistake if you have partners or have a solo business with significant financial obligations or legal exposure.

A limited partnership also offers limited liability for its “limited partners" but does not limit liability for its general partners.

**3. Believing Your Business Entity Protects You Against Risk**

One of the main reasons for forming a business entity is to protect your personal assets in the event that there's a lawsuit or judgment against your business. A business entity does offer important safeguards, but it won't protect you against everything.

A business entity won't protect you if you are sued and accused of being negligent or intentionally doing something wrong. It won't help you if your business suffers because of a fire or storm. That's why it's important to have business insurance in addition to forming a business entity.

**4. Assuming You Should Incorporate in Delaware (or Nevada or Wyoming)**

You might have heard that a lot of big corporations incorporate in Delaware. Or that you'll save on your taxes if you choose Delaware or another popular incorporation state like Nevada or Wyoming.

For a small business, incorporating out-of-state may actually cost you more and create more paperwork than incorporating in your home state. If you incorporate out of state, you'll need to maintain a registered agent in both your incorporation state and your home state, and you'll be responsible for annual reporting and fees in both states.

If you incorporate in your home state, you'll only have one state to deal with. And an out-of-state **incorporation** probably won't help you save on your taxes, since you'll still be liable for taxes in the state where you actually do business.

**5. Forgoing a Formal Agreement With Your Business Partners**

In the early days of a business, the owners tend to get along with each other and assume that, whatever happens, they'll be able to work things out. But it's a mistake to think that things will always be that way. Businesses evolve, and so do their owners' goals, visions, and relationships with one another. Eventually, there will be conflict and, without an agreement between the owners, that conflict can be very expensive and emotionally draining.

A better practice is to set up a business legal structure at the beginning that includes an agreement among the owners. The agreement can include such things as how conflicts will be resolved, how to deal with a departing owner, how to take on new owners, and how profits and losses will be divided.

Depending on the type of business entity, you might have a partnership agreement, an operating agreement, or a buy-sell agreement. It costs some time and money up front to prepare the agreement, but it's far easier and cheaper to agree at the outset than to try to resolve an emotionally charged conflict later.

Is a sole proprietorship right for you? If you're in business for yourself and you haven't created a formal business structure, then chances are, you're already a sole proprietor–so make sure you understand the implications.

You have several choices when creating a non-profit that allows you more flexibility in covering you and your boards liability. Two of those that effect liability, taxes and ability to raise capital are a sole proprietorship and a LLC or Limited Liability Corporation.

LIABILITY

Sole proprietors are personally liable for the debts of their business. If the business is sued, your house, savings, and other personal assets are at risk. Close up of Persons Hand Holding a Pen Filling out Tax Forms Taxes

TAXES

A sole proprietor is responsible to report all business profits as personal income, and pay self-employment tax on those profits, to cover Social Security and Medicare. Close up of Several 100 Dollar Bills Hard to Raise Capital

RAISING CAPITAL

There are no partners, shares, or membership interests in a sole proprietorship so it's generally difficult to attract investors without changing your business structure.

DBA If you're a sole proprietor, the legal name of your business is your own name. In most states, if you want to operate the business under a different name, you'll need to file for a DBA, "doing business as." Learn about DBAs Business Licenses You may need state or local permits and/or licenses to legally operate your business. We can help you figure out the business licenses you need. Learn about business licenses

Limit your Liability As a sole proprietor, you'll be personally liable for your business's debts and other liabilities. You may want to consider operating as a limited liability company (LLC) instead, so you're better protected.

**TOPIC 2**

**DISCUSSION QUESTION 1**

What is the difference between a sole proprietorship and a LLC?

**DISCUSSION QUESTION 2**

Of the 5 common mistakes made working in and with a non-profit what are the top 3 and why?

**DISCUSSION QUESTION 3**

Are you thinking it is easier to join a non-profit or start your own and why? What are the benefits for both?

**DISCUSSION QUESTION 4 with the Dean**

**PLEASE SET UP A PHONE CALL OR ZOOM CALL WITH THE DEAN FOR 15-30 MINUTES.**