

Seed Projects IRS 501(c)3 Compliance Guide

This guide is an overview of what a Seed Project can and cannot do to comply with the tax rules. We do not want to jeopardize our tax-exempt status. You are responsible to follow the current law. This is NOT a complete guide. For further information on 501(c)3 compliance regulations please go to the IRS website at <http://www.irs.gov/pub/irs-pdf/p1771.pdf>.

The IRS changes its rules and guidelines periodically. Be sure to read ALERTS on our web site to remain up to date on IRS requirements.

There are five major rules that must guide all of your Seed Project activities. Violation of any of these rules can result in termination of your non profit status. Be sure to refer to this guide again as you start any new activity and also go to the IRS website mentioned in the preceding paragraph.

Rule #1: NO ECONOMIC BENEFIT TO INSIDERS.

We are prohibited from engaging in activities that directly benefit insiders (Seed Project leaders, officers or board members) with our organization's income or assets.

Examples of activities prohibited by Rule #1

1. A project may purchase a van to serve the purpose of the project; however the van cannot be used by an individual for personal transportation.
2. If an artist is paid by a project to create art, the artist does not own rights to that art and cannot reproduce that art for his/her individual benefit. Everything produced with any contribution from the project is owned fully by the project. A project may reproduce that art work and may market and sell that art with prior approval from the Board. Income from such sales must be used by the project for its work. Members of the project, including any artists, may receive reasonable (fair-market) compensation for their work.
3. A project may contribute some of the funds needed to publish a book if the book serves the mission of the project; however no royalties or income from book sales can be paid to any member or officer, or to any of their family. Any income from any book sales must be received by the project. Members of the project may receive reasonable (fair-market) compensation for their work.

Examples of activities NOT prohibited by Rule #1

1. A project pays the project facilitator a reasonable (fair market) salary as manager of the project and pays two staff members reasonable wages for their work.
2. An artist creates 12 new images for a project's annual calendar sale. The artist is paid reasonable compensation for her work. She does not receive any royalties based on the number of calendars sold or the use of her images. The project decides to use the same art to make some large posters to sell to raise more money. The artist does not receive any additional compensation for this further use of the art she created.

3. A Recycling Project staff member writes a children's book that explains the importance of recycling. The project pays the author a reasonable wage for his work and pays for the publication of the book. The project's sale of the book is so successful that a major publishing firm wants to buy the rights to republish it and distribute it worldwide. The project sells the rights to the publishing firm for \$25,000. The project does not give the author any further compensation. All of the benefit from the success of the book is received by the project.

Rule #2: NO LOBBYING.

We are prohibited from engaging in substantial lobbying, trying to influence legislation. This includes Congress, state legislature, any local council or similar governing body. It does not include actions by executive, judicial or administrative bodies. We cannot contact, or urge the public to contact these bodies. We cannot advocate the adoption or rejection of legislation.

Examples of activities prohibited by Rule #2

1. A project can produce educational commercials about an environmental issue; however it cannot comment on legislation that may impact the environment.
2. A project can support or oppose any act of the government; however it cannot try to influence legislators or participate in demonstrations for or against any particular legislation.
3. The Board specifically prohibits projects from contributing money or other assets to politicians or their staffs. This includes any gifts, meals, entertainment or travel expenses.

Examples of activities NOT prohibited by Rule #2

1. A project staff member makes a personal contribution to a political campaign.
2. Several staff members participate in a political demonstration but do it as individuals, without any reference to the project. (Nothing that identifies them as members of or representatives of the project.)

Rule #3: NO POLITICAL CAMPAIGNING.

We are absolutely prohibited from directly or indirectly participating in, or intervening in, any political campaign on behalf of or in opposition to any candidate for elective office. To ensure this we have adopted a no tolerance attitude towards lobbying or campaigning.

Examples of activities prohibited by Rule #3

1. A project cannot use its facilities to host a campaign event.
2. A candidate may participate in a project event; however the project cannot in any way promote the candidate for election.
3. A project can produce a radio commercial that promotes community funded after school childcare; however a project cannot mention that one candidate is campaigning in favor of this or that another candidate is opposed to this.

Examples of activities NOT prohibited by Rule #3

1. During the election season in which global warming legislation is a hotly contested issue among the candidates, a project hosts an educational fair on global warming. Various booths provide educational materials and sell items to raise money for the project. No booth has any material

promoting or opposing any candidate or any specific legislation. No funds are contributed to any candidate or political group.

2. Legislation is proposed to protect an endangered species in your area. Project staff members visit local politicians, offering them educational materials that describe the ecological impact of protecting endangered species. No reference to the proposed legislation is mentioned in these materials and no staff member comments verbally about the up coming vote. The purpose of the visits is purely educational.

Rule #4: PRIOR APPROVAL IS NECESSARY FOR MOST INCOME PRODUCING ACTIVITIES.

The Board of Directors must be informed of plans for income producing activities other than grants and direct donations. The Board must determine if the activity is allowed PRIOR to your project engaging in the activity. All activities that produce income must have Board approval whether they are related or unrelated to the purpose of the project, unless it is a onetime activity or a grant or a donation.

A project does not need the board's permission for annual fundraising activities. Annual events do not require board approval even if they involve selling products or services. However any activity (such as offering a service or selling a product) which repeats more than once during a year and produces income must receive prior approval from the board. If a repeated activity is not substantially related to the project's exempt purpose, the IRS considers that an unrelated business activity. The Seeds Project generally chooses to disallow all unrelated business activities.

INCOME ACTIVITIES THAT ARE ALLOWED: Services or product sales performed entirely by volunteers, or the selling donated property, or activities that are specifically related to a project's nonprofit purpose are allowed. The board will review any activities that are planned and determine if they are permitted.

INCOME ACTIVITIES THAT ARE NOT ALLOWED: Other than for a one time fundraising event, selling products or services is not allowed unless providing the products or services is part of the nonprofit purpose of the project or unless all the work is done by volunteers. The board will review any activities that are planned and determine if they are permitted.

Examples of activities requiring Board approval under Rule #4

1. A project will publish a book with the intent of selling it to raise money to fund project activities. This involves selling a product and is not a onetime event. Therefore it requires prior approval from the board. The activity will be examined to be sure the project understands how to handle any royalties or subsequent rights to the material. If the purpose of the project is to produce books on a particular topic to further its nonprofit mission then this can also be an ongoing source of income for the project. If not then it can be a onetime source of income and all sales must be done by volunteers.
2. A project will operate a nonprofit organic farm and sell produce to fund the farm. This will be a repeated income activity and therefore requires prior approval from the board. This activity relates to the nonprofit purpose of the project but it will be examined to verify that all sales will be done by volunteers.

3. A project will charge admission to the project-owned botanical garden. Proceeds from the admission sales will be used to fund the garden. This will be a repeated income activity and therefore requires prior approval from the board. The activity relates to the nonprofit purpose of the project but it will be examined to verify that all ticket sales will be done by volunteers.
4. A recycling project sells hot dogs and drinks at an annual community fair to raise money for the project. This is an unrelated business activity but it does NOT require prior approval from the board because it is not a repeated activity. Annual fundraising events do not require board approval.
5. A nonprofit day care project receives income for its services. The parents pay less than the average fee charged by other day care centers in the same area. This will be a repeated, fee for service activity. Therefore it requires prior approval from the board. This activity will be approved because it is income related to the purpose of the project. It is important that the fee is less than what for profit businesses charge, showing that the project is serving the community by providing day care for lower income families.
6. A project is maintaining a garden to protect endangered native plants. They sell native plants to raise money for the project. This activity will be regularly selling products and therefore requires prior approval from the board. This will be approved because the products are specifically related to the nonprofit purpose of the project.

RULE #5: THERE ARE SPECIAL DISCLOSURE RULES FOR CONTRIBUTIONS IN EXCHANGE FOR GOODS OR SERVICES.

A contribution made by a donor in exchange for goods or services is known as a quid pro quo contribution. These contributions require us to disclose to the donor the value of the good or service received and the amount of donation. Failure to do this in a written disclosure can cost us our tax-exempt status. See IRS Publication 1771, Charitable Contributions—Substantiation and Disclosure Requirements at <http://www.irs.gov/pub/irs-pdf/p1771.pdf> for the complete guidelines.

Examples of proper disclosure under Rule #5 are based on estimated “fair market value” of the goods or services. That means the cost of comparable goods or services in your area.

1. A project raises funds by offering a “Spa Day” that includes professional manicures and facials and a light lunch. The staff of a local spa is donating their services which would normally cost \$75. The lunch is donated by project members. They estimate the value of the lunch at \$5, so the total fair market value of the goods and services is \$80. They charge \$150 for each “Spa Day” ticket and include a clear disclosure on each ticket - in the same type size as the price – stating that “The value of this event is estimated to be \$80 and the amount of contribution that may be deducted from your taxes is limited to a maximum of \$70.”
2. A project sells \$100 tickets for a fund raising dinner. These tickets have a clear disclosure - in the same type size as the price – stating that “The value of this dinner is estimated to be \$40 and the amount of contribution that may be deducted from your taxes is limited to a maximum of \$60”.
3. A project sells a set of music CDs for \$75 as a fundraiser. Each printed receipt has a clear disclosure stating that “The value of this CD is estimated to be \$25 and the amount of contribution that may be deducted from your taxes is limited to a maximum of \$50.”

