

Who Owns a Nonprofit Corporation?



Let's be clear about one thing. No one owns a nonprofit corporation.¹

While there is no outright ownership, there is control. One of the fundamental questions I ask when forming a new nonprofit corporation is how board members will be selected. This is a key question because those who hold the power to select board members retain the ultimate authority over the corporation.

The possibilities are limited by the nonprofit corporation statute in the state where the corporation is domiciled. In Arizona, the possibilities include the following:

Self-perpetuating Board. A self-perpetuating board is a board that selects its own members. One advantage of a self-perpetuating board is its simplicity. The directors whose terms are ending elect their successors which may be themselves.

The downside of a self-perpetuating board is the potential for entrenchment. Self-perpetuating boards can lead to an overly chummy board where no one wants to risk hurting anyone's feelings. This can lead to performance problems being overlooked out of politeness and can limit the organization's ability to attract new board members with fresh perspectives and new ideas.

One way to avoid entrenchment is to limit the number of terms that the directors can serve. Another mechanism to avoid entrenchment is to stagger the boards into different groups whose terms end at different times. Staggered boards have the advantage of creating a mechanism to bring in new board members every year.

Member (or Delegate) Elected Board. A board elected by voting members has the benefit of being more democratic in nature. In addition, membership classes can be structured to permit representation of various stakeholder groups.

Voting membership in a nonprofit corporation also confers certain rights and privileges under state law. For example, voting members have statutory rights to certain corporate information and, the ability to bring lawsuits to enforce the corporation's rights. However, these rights can be exploited to permit a group with a strong ideology to assume a leadership role in a nonprofit and radically change the nonprofit corporation's direction. The Sierra Club faced just such a [takeover attempt](#) by ideologically motivated groups in 2004. Accordingly, a voting membership structure should not be created lightly.

Organizations that elect their boards by member vote must also contend with the additional complexity of separately documenting two sets of meetings including notices, waivers, votes, resolutions, delegations, etc.

¹ There are some states that permit nonprofit corporations to issue stock and some relatively rare situations that require stock ownership; however, in the vast majority of cases, no one owns a nonprofit corporation.

A voting member corporation can also have a sole member or a sole corporate member which can result in the tightest control one can exercise over a nonprofit corporation. For this reason, many nonprofit subsidiaries are created with the parent corporation as the sole corporate member of the subsidiary.

Board Appointed by Third-Party. Many states allow the bylaws to specify a third party that is permitted to directly appoint one or more board members. This option can be used to provide board representation to stakeholder groups without the added complexity of a voting membership structure.

Some Combination of the Above. Most nonprofit corporation statutes permit any number of combinations and permutations of the above. These hybrid structures can be further combined with reserved powers, super majority vote requirements, and voting trusts to further refine and balance the interests of various stakeholders.

While it is possible under most state law statutes to create a structure that confers control of a nonprofit corporation that is tantamount to ownership, if the organization is a public charity and the control group represents private interests, expect strong push back from the IRS.

While there is no statutory authority for this position, it is the author's experience that the IRS is suspicious of any charity that is tightly controlled by any one family, business, or related group.