

The Governance Structures of Community Foundations – County Report UNITED STATES OF AMERICA

Introduction

Since 1914 when the Cleveland Foundation was established, community foundations in the United States of America have evolved in a variety of legal forms. US tax regulations allow for community foundations to exist in trust form with single or multiple banks; as multiple trusts with an incorporated distribution committee; as a single not-for-profit corporation with no trusts, or as a combination of trusts with a corporation.

The option of choice for the past two decades is the incorporated not-for-profit form and will be the focus of much of this paper. Additional information on other forms is available through links and examples.

In General ([*Legal Compendium for Community Foundations*](#))

A community foundation is a grantmaking publicly supported charity that is basically structured as an amalgamation of grant-making endowed funds. Each fund is usually named after the donor who established it (e.g., The Ed and Betty Smith Fund) or for its charitable objectives (e.g., The Mill Creek Park Endowment Fund). Several community foundations administer only endowment funds, but many others permit grants from principal.

A community foundation carries out the diverse instructions that have been given by its governing body and its donors. Although most grants are made to public charities within a defined geographic area, grants to national charities, and increasingly, international charities are becoming more common.

Federal and State Law Definitions

Community foundations must satisfy both State and Federal legal requirements. To operate in the corporate form, community foundations must be first incorporated as a not-for-profit organization in the State in which it operates. The community foundation must also be recognized by the Internal Revenue Service of the Federal Government as a tax-exempt publicly supported charity, 501(c)(3). Despite these requirements, there is little reference in either federal or state law that specifically defines community foundations. Ironically, much interpretation of the legalities regarding community foundations comes from the fact that they are NOT private foundations, and thus are not subject to some rules specific to these organizations.

Legal Structure Under State Law ([*Legal Compendium for Community Foundations*](#))

Requirements regarding governance structure and rules stem from State laws of incorporation. While regulations vary between States, most minimally require:

- Governing Documents ([By-Laws](#) and [Articles of Incorporation](#), or [Articles of Trust](#)) - describes the organization, purpose and general rules of operation.
- Board of Trustees (Board of Directors) - many States allow a minimum of three (3) persons to form a new not-for-profit corporation. The Governing Documents must identify how Trustees/Directors are selected, how long they may serve, their legal duties, and how they may be removed.
- Officers – Similarly, in many states, not-for-profit corporations are only required to have three officers (President, Secretary, Treasurer). Again, Governing Documents must identify their selection, term, duties and removal.

- Membership – Some states require not-for-profit organizations to elect a separate group of members, who in turn elect the Board of Trustees/Directors. (some States allow the members and Board to be the same group of people).

Incorporation as a not-for-profit allows the community foundation to exist, but it cannot accept tax-deductible contributions or make grants without recognition by the IRS as a 501(c)(3) tax-exempt public charity.

Required Status as a Charitable Organization Under Section 501(c)(3) of Internal Revenue Code: (*Legal Compendium for Community Foundations*)

In addition to being a valid organization under state law, a community foundation must be organized and operated in such a way that it qualifies as a public charity.

Organizational Test – Governing documents (articles of incorporation, articles of association or trust instrument) must state that the community foundation will be operated “exclusively” for charitable purposes and describe the transfer of assets to another public charity in the case of dissolution. Satisfied with these requirements, the IRS will respond with a “[letter of determination](#)” which authorizes the community foundation to operate as a 501(c)(3).

Operational Test – Annual reporting on [IRS Form 990](#) and possible IRS audits will determine whether the organizations actual activities are “primarily” charitable. Allowable non-charitable or for-profit activities must be reported, possibly resulting in some level of taxation.

Community Foundations with multiple-trust agreements must, and not-for-profit incorporated community foundations should satisfy the Single Entity Test.

- The organization must be commonly know as a “Community Foundation,” “Community Trust” or “Community Fund”
- All Funds of the community foundation must be subject to a common governing instrument or a master trust or agency agreement.
- The Community Foundation must have a common governing body, which directs all funds exclusively for charitable purposes.
- The Governing Board must have the [variance power](#), the authority to modify any restriction or condition on the distribution of funds for any specified charitable purpose or to any specified organization, and the authority to replace a trustee or investment manager for breach of fiduciary duty or inadequate investment performance.
- The Governing Board must strive for a reasonable [return on investment](#).
- Must prepare appropriate consolidated [financial reports](#).

To retain a tax-exempt status 501(c)(3) with the IRS, community foundations must satisfy the [Public Support Test](#). The Public Support Test is a key feature of all nonprofit tax-exempt organizations in the United States and more specifically community foundations. Briefly, this financial test assures that a community foundation is broadly and publicly supported and not overly dependent on a limited number of donors. Community foundations report this test on the IRS Form 990.

The Governing Bodies of U.S. community foundations

State and Federal laws govern minimal expectations for governing rules, structure and operations of community foundations in the United States. In reality, most community foundations in the United States exceed minimal requirements and have developed governance structures and practices, which exemplify their role as stewards of community resources.

Community foundations organized in the form of corporations are membership organizations. Members are generally considered the “shareholders” of a nonprofit corporation. Memberships range from a few to several hundred individuals and are not used by all Community Foundations. In some cases, members must pay dues and everyone willing to pay such dues may become members. In other cases, membership may be limited to a select few individuals who were founding members.

BOARD OF TRUSTEES

The Board of Trustees (or: Board of Directors) is the key authority of a community foundation. The Board has ultimate legal, fiduciary and moral responsibility for the operations of the organization. The members of the Board serve without compensation. They are appointed 1) by membership, and/or, 2) by the Board, and/or 3) by appointing authorities. In many cases, the Board of Trustees/Directors then in office is empowered to elect their successors and fill vacancies on the Board. In some instances, the Community Foundation may rely on local civic, social, educational or governmental groups to appoint some members to their Board. In all cases, the appointment or election of Boards is regulated by the organizations Governing Documents.

re: Mission

- establishes and regularly reviews the [mission statement](#), [strategic plan](#) and operating principles

re: Policy Development and Implementation

- is responsible for oversight of all financial operations of the organization, including [budgets](#), assets and properties
- approves all grants
- ensures that the community foundation meets all laws and legal requirements
- ensures adequate human and financial resources for foundation operations
- approves policies to prevent perceived, potential or actual [conflicts of interest](#)
- guards against self-dealing
- observes ethical requirements

re: Organizational Structure

- is responsible for the [nomination, selection and recruitment of board members and election of Board officers](#)
- develops a [committee structure](#) consistent with the mission and strategic plan of the organization.
- hires, supervises, evaluates and fires the [President/CEO/ED](#)

PRESIDENT/ CHIEF EXECUTIVE OFFICER (CEO)/ EXECUTIVE DIRECTOR (ED)

The President/CEO/ED, is the lead staff, may or may not be voting member of the Board of Trustees/Directors, and may or may not be paid. In the United States, the President/CEO/ED is generally responsible for the day-to-day operations of the Foundation and may have more authority than in some other countries.

re: Mission

- works with Board to develop overall mission, strategic plan and operating principles

re: Policy Development and Implementation

- recommends operating policies to the board and/or assists the board in the formulation of policies
- has chief administrative responsibility for implementing the strategic plan
- prepares all operating procedures, is accountable for their control and monitors compliance
- prepares all budgets, is accountable for their control, monitors assets and provides required reporting to the Board and legal authorities
- has chief administrative responsibility for grantmaking and asset development
- serves as the chief spokesperson for the Foundation with the community, grantseekers and donors

re: Organizational Structure

- hires, supervises, evaluates and fires additional staff as required by the organization
- serves as primary staff liaison for the Board and Board committees
- assists with or provides orientation for new Board members and ongoing training/education for incumbent members