# INCORPORATION OF A CHAPTER

Incorporation is the process of creating a legal entity under authority granted by a state. A corporation is a separate legal entity, with continuing existence independent of its officers, directors, stockholders, or members. An organization, whether incorporated or not, may be either a for-profit entity or a nonprofit organization. For-profit organizations typically are incorporated, issue stock to shareholders, and are taxable on net income. Non-profit organizations have no specific "ownership" as such, but are generally controlled by members, who do not receive stock. Only non-profit organizations can be granted an exemption from federal income tax by the Internal Revenue Service, but incorporation is not required for an organization to be considered tax-exempt by the IRS. The decision of whether a chapter of FMCA should incorporate is influenced by a number of considerations.

The following specific considerations are involved in determining whether or not to incorporate a chapter of FMCA:

**Liability**

One of the primary purposes of incorporation is to protect individual officers or members from personal liability when these individuals are conducting activities on behalf of the chapter. These individuals will generally not be personally liable for damages relating to chapter activities, including personal injury, property damage or contractual liability, if the chapter is incorporated and as long as the individuals are acting reasonably and in good faith. If the chapter is unincorporated, the officers or members may be personally liable for any damages associated with chapter activities. This means that the individual assets of the officers and members could be seized to pay for damages associated with chapter activities if the injured party won a lawsuit. The assets which could be seized would, in most states, include an individual's home and car.

Of course, most chapters will never have a lawsuit brought against them. Yet, accidents do happen. For example, someone could be injured at a chapter rally and claim that the chapter was negligent for failing to provide adequate traffic control.

Even if a chapter is incorporated, an officer or member would still be personally liable in certain situations. For example, personal liability would attach for intentional wrongdoing.

**Insurance**

Whether the chapter is incorporated or unincorporated, it can purchase insurance to cover many types of likely claims against it or its officers or members. For an unincorporated chapter, insurance coverage would help protect the assets of officers and members after a lawsuit. Obtaining insurance, however, is often more difficult for an unincorporated association. In certain circumstances, the insurance company may not be able to determine the precise authority for the organization and its operation. Incorporated organizations usually have better opportunities for obtaining desired insurance.

FMCA does carry a general liability insurance policy on its chapter members which is applicable to incorporated as well as unincorporated chapters. Refer to a description of insurance coverage that is contained within the Risk Management Guide which is available online to all presidents.

**Legal Actions**

A corporation can sue and be sued in its corporate name, while an unincorporated chapter must, in some jurisdictions, appear in court in the name of participating individuals, such as officers or members. This is important from the liability aspect, discussed above, but also from the viewpoint of a chapter having to file a lawsuit. For example, a chapter might wish to sue the owner of a vacant lot who withdrew permission at the last minute for the chapter to hold a rally there. An unincorporated chapter might not be able to file a lawsuit in the name of the chapter. The members or officers would be required to individually file a joint lawsuit against the landlord. Not only is this cumbersome, but individuals are frequently reluctant to have their names associated with lawsuits. An incorporated chapter can use its own name in a legal action and is not required to bring its individuals or officers into a lawsuit as parties.

**Independence**
A corporation has an existence of its own, independent from its members, directors or officers. A corporation is theoretically perpetual, although it can be dissolved. An unincorporated chapter has no separate legal existence. Its actions are only the joint actions of its members. Each time a member enters or leaves the chapter, the entity changes. For this reason, landlords and vendors are sometimes unwilling to enter into contracts with unincorporated associations, because the "entity" they are dealing with are in a constant state of flux.

**State Laws**
A corporation is formed by filing Articles of Incorporation with a state government under the state's corporation laws. These laws give guidance to corporations on organizational structure, voting and other matters. Corporations are governed by a well-established body of statutory and case law. By comparison, unincorporated associations are not subject to any reliable set of rule concerning formation, administration or governance. There is little authority that an unincorporated association can turn to when questions in these areas arise.

State laws frequently offer protection from liability for officers and directors of non-profit corporations whose own actions result in damages - as long as the individuals were acting in good faith. State laws generally do not offer similar protection to officers or directors of unincorporated associations.

**Income Taxes**
Liability of an incorporated association for federal or state income taxes is usually limited to corporate assets. In contrast, the members of an unincorporated association could be personally responsible for income taxes. Especially if the unincorporated association had no assets that the taxing authority could attach, the taxing authority could well attach the assets of the members to obtain payment of income tax due.

Of course, most chapters of FMCA will not incur income tax liability. But, it must be kept in mind that a "tax exempt" organization is not exempt from all taxes. It is only exempt from taxes on receipts from certain membership activities. The rules for determining whether income from a non-membership activity constitutes taxable income are quite complex. Even unintentional failure to pay income taxes would impact personally on the members of an unincorporated chapter.

If a chapter incorporates, it is still eligible to be included in FMCA's group tax exemption. (See separate memo regarding Income Tax Filing for Chapter – IRS form 990).

**Technical Requirements**
A corporation must meet a number of technical requirements to obtain and maintain its corporate status. A corporation must also observe various organizational and operational requirements under state law. Articles of Incorporation must be filed with the state to establish a corporation. In addition, annual meetings must be held, minutes must be kept, and annual reports must be filed by corporations. Incorporation entails some legal costs, such as costs for drafting the Articles of Incorporation and bylaws, and making the required filings. Most of these technical requirements for corporations, however, are relatively straightforward and involve only modest expense.

In the case of each individual chapter, the benefits of incorporation must be weighed against the detriments. The paperwork and expense must be balanced against the protection from liability afforded members, and the other considerations set forth above. The answer will not be the same in all cases. Each chapter should examine its own activities to determine whether problems could possibly arise in one of these areas. The chapter will also want to consider whether the possibility of a problem is real or only very remote. For example, a chapter that does not engage in fund-raising activities, sponsors a minimal number of rallies with good safety precautions in place, does not serve food or alcohol at meetings, and keeps very little money in a bank account, probably has only a remote chance of creating a situation in which members could be liable. More active chapters will have more realistic chances of a problem arising.

Since the impact of whether or not the chapter incorporates falls directly on the members as well as the officers, the officers of the chapter may wish to consult the members and explain the considerations before making a decision.

The FMCA National Office does not have legal counsel on staff to assist you with this. Therefore, if you are further interested in incorporation, you may want to start by contacting your state government. In many states, it would be the Secretary of State. However, this does not hold true for all.

***Disclaimer:*** *Incorporation can be complicated and the application of rules is subject to circumstances unique to each FMCA Chapter. FMCA is not engaged in rendering legal, accounting or other professional services. If legal or other expert assistance is required, the services of a competent professional should be sought by the Area or chapter.*