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Starting a Nonprofit Business

If you have a passion for a cause, starting a nonprofit could be for you.

By Carol Tice

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Making a Difference

Catherine Rohr was a 27-year-old UC Berkeley graduate with a thriving career in venture capital when, at a reception in 2004, she heard an ex-convict speak about the successful construction business he started after leaving prison.

For Rohr, it was a life-changing moment. She realized former drug dealers and gang leaders had entrepreneurial skills: They knew how to manage people, make a profit and handle competition. Using her finance-world connections, she could recruit CEOs to teach ex-convicts to use those skills to start legitimate businesses.

That same year, Rohr started Prison Entrepreneurship Program, and today, it has a \$700,000 budget funded primarily with donations from CEOs and foundations. Nearly 100 percent of the 250 convicts that have participated in PEP are employed on release. Less than 5 percent of participants have returned to prison.

Rohr hopes to eventually see her program expand to prisons nationwide. "This is the hardest I've ever worked in my life," she says. "But I can't imagine going back to having my goal just be to make money. This is the most rewarding thing ever. I have a passion that won't die for these guys."

Most entrepreneurs strive to create for-profit businesses, hoping to make a fortune. Entrepreneurs like Rohr have a different goal: to make a difference.

Nonprofit professionals say young businesspeople at all stages are increasingly drawn to the emotional rewards of nonprofit work. Business-school students frequently approach Jeffrey Schwartz, a consultant in Chevy Chase, Maryland, for advice on starting nonprofits. "They say, 'We don't really want to work in business, because it's soul-stifling instead of soul-stirring,'" he says.

The nonprofit sector may be personally fulfilling, but it's not a snap to succeed in. The attrition rate for nonprofit startups is as steep as it is for businesses. There are already nearly 1 million nonprofits nationwide, and tens of thousands are launched annually. Many eventually go bust.

"In my experience, 50 percent of the nonprofits being created are redundant," says Elizabeth Heath, founder and executive director of The Nonprofit Center of South Puget Sound in Tacoma, Washington. "It's easy to start one, but there is not a clear understanding of what it takes to sustain one."

Lofty goals or not, successful nonprofits employ business basics just like their for-profit counterparts. If the idea of creating a nonprofit appeals to you, consider these pointers to launch one successfully.

Nonprofit defined: A crucial difference between starting a nonprofit vs. a for-profit is that you're creating an asset you will never own, Heath notes. A nonprofit essentially belongs to the community, so you will never be able to sell it. If it goes bust, its assets will be distributed to other nonprofits. "That ownership concept is a struggle for many businesspeople to let go of," she says.

Under the IRS rules that govern nonprofits, no individual can benefit from a nonprofit's activities in any way except through his or her salary. But that doesn't mean you don't have to make a profit. "The truth is, you can't be sustainable unless you raise more than you spend," Heath says. "You need reserves for rainy days and for growth."

The business of charity: Behind every successful nonprofit is a well-thought-out business plan. First, make sure there isn't already a nonprofit with a similar program in your region. Efficiency is crucial.

Before launching their urban, college prep boarding school, The SEED School, in Washington, DC, co-founders Eric Adler, 42, and Rajiv Vinnakota, 35, applied their experience from major management-consulting firms to concoct numerous financial plans, which they then bounced off experts. Even then, the pair had to regroup when expenses outstripped their forecast

A former private-school teacher, Adler was frustrated with the way scholarship students from tough neighborhoods often floundered. His idea: board students, providing a safe, quiet place to study and mentors to keep students focused on college.

Started in 1998, SEED has since seen two similar concepts on the East Coast fail. Key to SEED's success is a model that requires only modest ongoing fundraising--about \$400,000 of its nearly \$11 million annual budget. Most of their finances come from state and federal charter-school funds.

Buoyed by graduation rates substantially higher than the district average, the pair hopes to open two more schools in the area within three years.

Finding Funding, Getting Paid and More

Finding funding: Although many nonprofits collect fees for services of some kind, most rely at least in part on funds raised from private donors, foundations or government grants.

"A common pitfall is that founders don't regard fundraising as one of their principal obligations to the people they serve," says Schwartz.

As a startup nonprofit with no track record, fundraising can be tough, says Adler. Most funders require documentation on how well the nonprofit is meeting its goals--data startups lack. But it can be done--SEED raised \$2 million in initial funds and \$26 million to build its campus. Adler had the most success with individual philanthropists in the DC area with personal knowledge of the district's problems, rather than national foundations. "You have to make them believe you need their gift now and you're going to succeed," he says. "You've got to knock on door after door until you meet the people who can introduce you to the people who are willing to fund it."

Social entrepreneurs: Instead of relying on fundraising, some nonprofit entrepreneurs create a nonprofit business that generates the needed revenue. Though this model has been around for years, it's blossomed in the past seven years into a major movement nonprofit managers call "social entrepreneurialism."

A prime example is Athena Partners, a Seattle-based, nonprofit bottled-water company founded by former marketing executive Trish May. After surviving a bout of breast cancer, she spent six years investigating how to help fund a cure. Her answer: bottled water adorned with the pink breast cancer-awareness ribbon. Founded in 2003, Athena has since made a deal with food-distribution giant Sysco that will take Athena nationwide next year. Sales this year were \$1 million, and May projects \$2.5 million for 2007. May, 52, says being a nonprofit allowed Athena to tap volunteers who'd been touched by cancer, and it brought free advertising. For instance, Alaska Airlines provided the necessary funds to put giant pictures of Athena's bottle on the Athena delivery trucks.

Nonprofit status also opened many doors in the highly competitive world of bottled-water retailing. When May landed Safeway as her first big account, the grocery chain waived the promotional fees Athena would otherwise have paid for shelf space. Other chains followed suit. "Companies want to partner with you because they want to do the right thing," she says. "They also appreciate the business value of aligning with a cause."

Operating in the nude: Another difference between for-profits and nonprofits is that nonprofits' tax forms are public records. Small, privately held businesses can keep operating details secret, but anyone can read a nonprofit's tax form, known as Form 990, online, learning salaries, revenue, expenditures and more. "Get prepared to get naked because of those 990s," says Mark Grimes, a nonprofits consultant in Portland, Oregon. "You better be real comfortable with people knowing how much you make."

Getting paid: Salaries in the nonprofit sector vary widely. But with many nonprofit heads overseeing large and complex organizations, salaries can be quite substantial. A 2005 Chronicle of Philanthropy study of more than 200 large nonprofit groups found the median salary for nonprofit CEOs was nearly \$320,000.

At nonprofit startups, salaries tend to be lower. Because of her dedication to the cause, May chose not to take a salary. Rohr takes a salary she says is "one-fourth of what I used to make."

SEED founders Adler and Vinnakota worked for free for the first 18 months, living off savings while they got their school off the ground, but they eventually drew salaries that started around \$45,000 and rose each year. Recently, the SEED board upped their salaries to \$150,000 apiece to reflect their blistering workloads and the growing size of the organization.

Soul satisfied: At the end of the day, nonprofit entrepreneurs say they're hooked on the satisfaction that comes from knowing their efforts improve the world. "I loved my [previous] job," says May. "But here, I'm helping affect lives, and [hoping] to save lives, ultimately."

It's just so rewarding."

Paperwork ABCs

Ensure your organization is recognized as a nonprofit by the IRS and conforms to state laws with help from Anthony Mancuso, attorney and author of *How to Form a Nonprofit Corporation*.

1. Register with the state. Nonprofits must register with their state to legally do business as a nonprofit corporation. You'll need to create articles of incorporation--states usually offer examples to work from--and file them with your registration. See your secretary of state or department of licensing office for forms.

2. Apply to the IRS for nonprofit status. This is crucial because without the IRS' nod, donors won't be able to use their contributions as a tax deduction. Most nonprofits seek what's known as 501(c) 3 status, which allows tax write-offs for donors. Over its initial five-year operating period, a charity must demonstrate to the IRS that it has broad-based public support.

Nonprofit applications have been under greater IRS scrutiny in recent years, so Mancuso recommends being scrupulously honest in describing what your charity will do. One other tip: Request an advance ruling that will allow you to operate as a 501(c)3 sooner.

3. Register to raise money. If your nonprofit intends to solicit the public for donations, the organization must register as a charitable solicitor in many states. Obtain forms from the attorney general, secretary of state or other appropriate agency.

4. Convene a board. To qualify as a nonprofit, a board of community stakeholders must be created to help the nonprofit raise money, hire staff, shape group direction and meet goals. The board should not consist of personal friends or people with whom the charity does business.

5. Write bylaws. The bylaws describe your nonprofit's operating procedures. Again, standard forms are available from your secretary of state or state corporations office as a starting point.

Though many people hire a CPA or attorney to help manage the paperwork, you can do it yourself with the help of basic how-to books such as Mancuso's. Otherwise, you can start by trying out your idea as a program or project of an existing nonprofit, which can handle your accounting chores until your group is ready to spin off.

Nonprofit Organization Help Station

Books, organizations and websites to help you get started

- *How to Form a Nonprofit Corporation* by Anthony Mancuso
- *Starting and Running a Non-Profit Made Easy* by David H. Bangs
- [Association of Fundraising Professionals](#): Ethical standards, training and resources for nonprofit fundraisers.
- [BoardSource](#): Resources to strengthen nonprofit boards
- [Foundation Center](#): Information and viewable tax forms of grant-making foundations
- [GuideStar](#): Comprehensive database of nonprofits, with viewable tax forms
- [The Idealist](#): Extensive online resources for those starting and operating nonprofits
- [IRS](#): Tax information for charitable organizations.

Carol Tice is Entrepreneur's "Tax Talk" columnist.