

a DISSOLVING NONPROFIT

IN WASHINGTON STATE



WASHINGTON
Secretary of State
Corporations & Charities Division



Nonprofit Association
of Washington



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Introduction

You are starting to think that something is wrong. You are running out of money, you are having a lot of trouble finding board members, or the programs that worked so well long ago aren't working in today's world. You are wondering if it is time to think about dissolving your nonprofit.



Just as there are thousands of nonprofits starting each year, there are many organizations that decide to wrap up their work. It is healthy within our communities to have some organizations dissolve so that time, energy, and money can be focused on other organizations.

“Dissolving a Nonprofit” guides you through the decision-making and actions involved in closing down a nonprofit organization. It gives you guidance on the key compliance steps, as well as information on how to manage communication and community outreach in a way that honors your legacy.

We know that you are probably feeling anxious about the process. Our culture honors those who start projects, not end them. You might perceive that people will think that you have done something wrong. We hope that this resource gives you a chance to make informed, mission-centered decisions. We encourage you to take the time and give yourself the space to plan actions that reflect your best intentions for the people you serve. We hope that you can honor the important work that your organization has done. This resource represents a distillation of knowledge, experience, and research from nonprofit leaders, people who have experience dissolving nonprofits, lawyers and capacity builders.

“Dissolving a Nonprofit” is part of a larger set of toolkits related to nonprofit practice. It is also supported by an information and referral service and pro-bono legal assistance. See the “Nonprofit Navigator” on Page 8 for more information about who is available to help you.

THE FINE PRINT

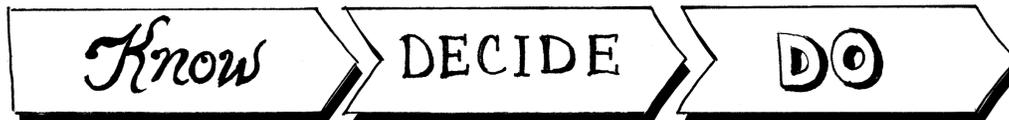
This Toolkit includes high-level information about dissolving a nonprofit. It refers to other resources that go into more depth. It is designed for general use and not for the specific characteristics of an individual organization or person. It contains information about the laws impacting nonprofit organizations in Washington. Legal information is not the same as legal advice. It is always a good idea to consult with an attorney to get advice as to how the law should be interpreted related to the specifics of your organization and situation. Communities Rise is a great place to start if you need legal help: www.communities-rise.org. Also, laws impacting nonprofit organizations change over time. The information contained in this Toolkit may become out of date.

Let's get started!

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There are 3 main chapters to “Dissolving a Nonprofit.”
Look for these icons to help you keep track of your progress:



Part 1	Part 2	Part 3
What you need to KNOW Pages 2–4	What you need to DECIDE Pages 5–6	What you need to DO to dissolve Pages 7–9
<ul style="list-style-type: none"> ▪ Options other than dissolution ▪ People matter ▪ Net assets belong to the public ▪ Dissolution plan ▪ Board’s role 	<ul style="list-style-type: none"> ▪ Where to dissolve ▪ Key questions in how to dissolve 	<ul style="list-style-type: none"> ▪ Three channels <ul style="list-style-type: none"> ○ State ○ Federal ○ Local ▪ Two tracks <ul style="list-style-type: none"> ○ Board ○ Operation

Review: What Is a Nonprofit?

Before we get started, let's remember the definition of "nonprofit." A **nonprofit** is a type of **CORPORATION** that is created to accomplish a **PUBLIC BENEFIT**. It does not have owners other than the **COMMUNITY AT LARGE**. It has no shareholders. It cannot be set up for the purpose of generating an income or profit for the organizers. Some organizations apply for **TAX-EXEMPT STATUS** from the Internal Revenue Service (IRS) so that donations can be tax-deductible to the donor and the organization can avoid federal corporate income tax. There are many classifications of tax-exempt organizations, one of which is 501(c)(3).

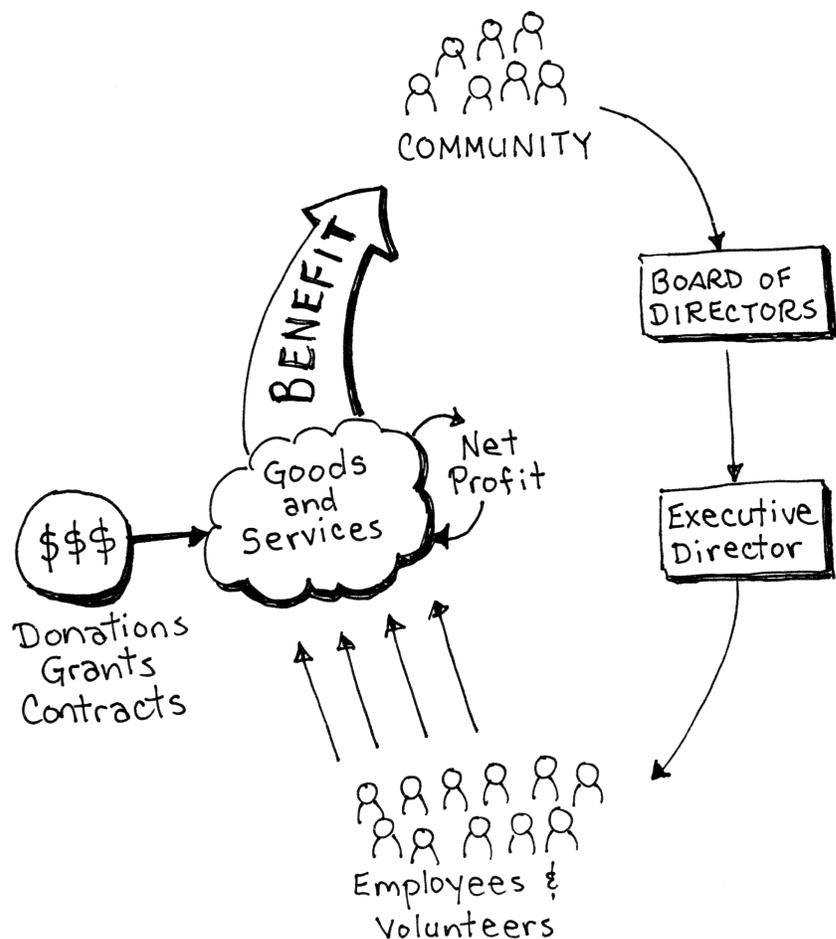
There are several elements of this definition that come into play in dissolving a nonprofit:

Corporation: You are incorporated in the State of Washington. This means that you may have to file Articles of Dissolution in order to no longer formally exist as an entity.

Public benefit: You exist for the public's benefit. The assets you have still belong to the public.

Community at large: Your community has a special interest in your work. They have donated, volunteered, and otherwise supported your work. This means that you need to communicate with the public so that they understand what is going on with your organization. Your partners - or fellow nonprofits working in this space - will want to know since demand for their programs might shift as you shut down operations.

Tax-exempt status: If you are also a tax-exempt charitable organization as defined by the IRS, you should also dissolve at the federal level by filing a final tax return.



This toolkit should help you understand how some of these elements fit together in the dissolution process.



Part 1: What You Need to Know

So you want to dissolve a nonprofit. Before you do, there are five big ideas to know.

1. A nonprofit facing challenges can find solutions in different ways.
2. People matter.
3. Remaining net assets, if any, belong to the public.
4. A dissolution plan will guide you forward.
5. The board makes the decision to dissolve and then oversees the process.

Let's explore these ideas one-by-one:

1. A nonprofit facing challenges can find solutions in different ways.

Perhaps you are feeling the typical warning signs of a nonprofit in trouble. You struggle to meet payroll or to pay other bills, you struggle to find new board members or volunteers, and/or your core supporters have waning energy or have lost interest altogether. What can you do?

There are six main options available to you, not all mutually exclusive:

Engage your community: People have supported your work in the past. They may rally to your aid now if they knew more about your situation. You might consider speaking with funders to share your concerns and see what additional support might be available.

Internal restructure: The challenges you are facing may give you the opening you need to change how the organization is run. It might lead you to restructure your staff—maybe downsize it—to keep your core programs running. Sometimes such a restructuring is needed to garner additional support from funders and others for those core programs.

Acquisition of programs: You may have important programs serving people that another organization would absorb into its programming. There may even be another organization with an interest in acquiring *all* of your programs. Either way, some or all of your assets will continue to be used within the community. Talk with partners and colleagues working in your cause to see what options might be available to you.

Merger: While unlikely if your organization is facing severe challenges, it is possible that your organization could merge with another organization and keep its key staff and programs in place. Although there are legal differences, the principal practical difference between a merger and an acquisition is one of degree: a merger is more commonly thought of as being more or less between equals, where each organization will contribute to the board and governance of the merged entity (though not necessarily equally), whereas with an acquisition one of the organizations and its management more typically goes away.



Reorganization through bankruptcy: Severe financial challenges might lead you to decide that reorganizing through bankruptcy is your best option. Chapter 11 of the Bankruptcy Code, well known in the corporate world, is available to nonprofits as well. This may help you restructure in ways that allow you to get through these challenges. However, Chapter 11 is an extraordinarily complex and expensive process, not commonly utilized in the nonprofit world.

Dissolution: After considering all of your other options, it may be most appropriate that you close your doors as an organization, either through formal court processes (federal Chapter 7 bankruptcy, state receivership/assignment for the benefit of creditors) or without court intervention. The rest of this toolkit is about how to do this.

2. Community matters in dissolving a nonprofit.

Most nonprofit work comes down to relationships, both within the organization and between the organization and its larger community. These types of people have supported your organization:

- Staff
- Volunteers
- Clients
- Members (membership orgs)
- Past and present board members
- Donors
- Institutional funders (foundations, service organizations, agencies)

They deserve to know about your plans to dissolve your nonprofit. Communication helps to honor the hard work of all who have supported your nonprofit, reduce stress about the future, and guide people through the emotions that come with change.

Celebration is a key part of community. While it may seem like a sad time in the life of your organization, remember that you have a lot to celebrate. You created something that served your community for a period of time. You show that community matters when you celebrate the organization's achievements as a part of your dissolution.

3. Any remaining assets belong to the public.

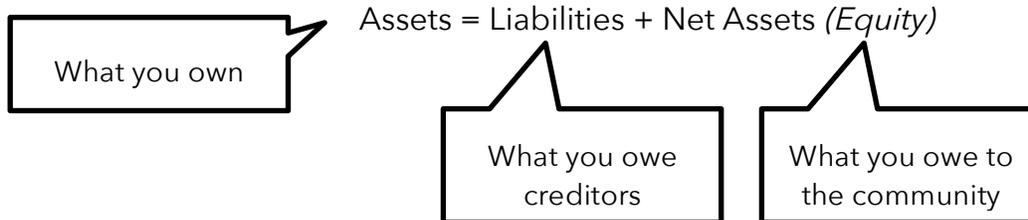
Your organization was granted nonprofit status because it serves a public good. That means that its assets belong to the public. The assets do *not* belong to any one individual nor do they belong to the board.



One way to think about this is in financial terms. The Balance Sheet shows what the organization owns (assets), what it owes (liabilities), and the different between them.

Assets - Liabilities = Net Assets (Equity)

If we rearrange that financial equation, this happens:



A corollary to this equation is more subtle: if liabilities are greater than assets, then there are no net assets. In that situation, the organization does not have any financial obligation to the community, but it is still a nonprofit and still has duties to protect the public interest in its dissolution process.

Your nonprofit may have legal obligations to fulfill before you dissolve. These obligations may include contracts, grant agreements, debts, etc. Taking stock of these legal obligations is an important part of making the decision to dissolve.

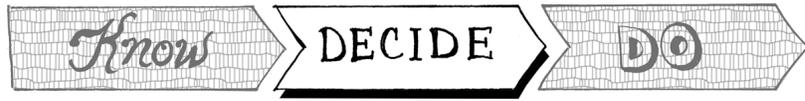
When we think about assets, we often think about money, but you must take into account all assets. Accounts receivable; inventories (whether of equipment, supplies, materials, or other resources); tangible assets such as furniture; real estate; contract rights; and capital investments are all assets that will also belong to creditors or the community.

4. A dissolution plan will guide you forward.

Dissolution happens across many levels: state, federal, and local government agencies, as well as the organization's constituents such as funders, creditors, and community partners. It involves board leadership and key operational tasks. Part 3 of this toolkit outlines key steps and considerations to dissolving your nonprofit.

5. The board makes the decision to dissolve and then oversees the process.

It is common for the board to think that its job is done before it really is. The board is the body with the responsibility to see the dissolution through from analysis of options to decision point to distribution of assets and filing of required paperwork. The board holds the responsibility to the community and can leave a powerful legacy of your organization through the distribution of assets. The board only disbands once all of the work has been done, which may take a year or more.



Part 2: Get Ready to Decide

Once you know what is involved in dissolving a nonprofit, you enter a decision-making process. There are two main stages of this decision-making: whether to dissolve, and if you decide to, how to dissolve.

A. To dissolve: Yes or No?

A nonprofit facing challenges has options. As we explained in Part 1, dissolution is just one option among many. Your board must weigh the possibility and pros and cons of each of these options:

- Engage with funders and others
- Internal restructure
- Merger
- Acquisition of key program
- Reorganization through bankruptcy
- Dissolution

Dissolution should be chosen only after the other options are considered and found wanting.

B. Let's dissolve: Key questions

If the board decides to dissolve, there is a second set of decisions to be made:

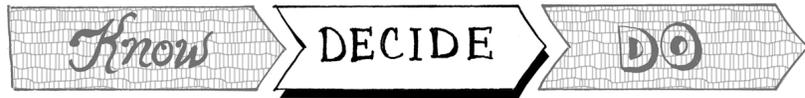
- Which dissolution procedure will be followed?
- What will the guiding values be?
- Who will take the lead in the process?
- How will expertise be engaged?
- When will the community celebrate the life of the organization?

C. How will the dissolution be accomplished?

Recall there are several ways to dissolve an organization: federal bankruptcy (Chapter 7); state receivership/assignment for the benefit of creditors; or out of court dissolution. The appropriate choice may depend on whether or not the organization is insolvent (meaning whether there are net assets). The board should consult with appropriate professionals with experience in this field before making this decision.

IMPORTANT CONSIDERATION

As soon as you start thinking about dissolving your nonprofit, do a calculation of the cost of shutting it down. Consider debts, grants, and lease obligations that may have to be satisfied. Think about the cost of any legal or accounting services you might need. If you can, set these funds aside now so that you avoid unnecessary cost, effort, and heartache later on.



Decision Making: Heart Check

How are you feeling?

Before we move on, let's check in on how you are feeling. Dissolving a nonprofit is an emotional time for many. The emotion around your work is important because it is your heart connection to the cause that you have been advancing and to the people with whom you have been working. In general, emotions are what motivate us to do things. Understanding your emotions will help you to honor them as you move forward.

Here are some typical emotions related to dissolving a nonprofit:

- Fear
- Frustration
- Embarrassment
- Anger
- Sadness
- Confusion
- Exhaustion
- Excitement (to be moving on)

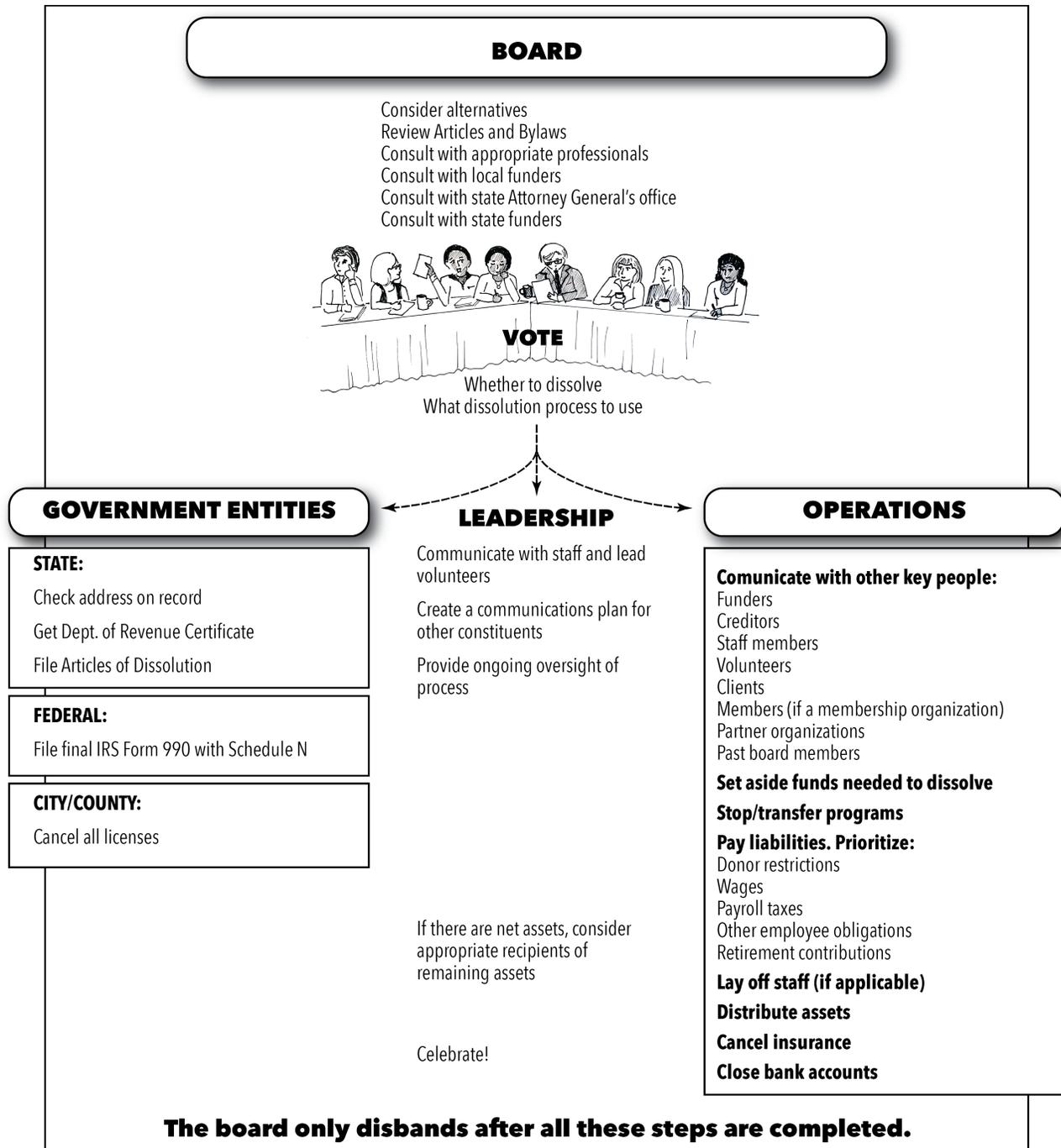
It is normal to feel a loss when something is ending.

- Circle the emotions that you feel most right now.
- Invite your fellow board members/staff members to identify what they are feeling right now.
- Talk about the emotions you are feeling.

By honoring that emotion, you are honoring your heart connection to the cause that most likely brought you into this work. And by recognizing this range of possible emotions, you are better prepared to deal with those emotions exhibited by others involved in the process.

Part 3: Dissolve a Nonprofit

You have decided to dissolve your nonprofit. You have done due diligence in making a decision that you and your community stand behind. Now what? Dissolution happens across several channels: state, federal, and local government agencies, as well as the organization's other constituents. It involves board activities and operational tasks.





Nonprofit Navigator

Here is more information with links to find key forms:

State

- [Check address on record \(https://www.sos.wa.gov/corps/\)](https://www.sos.wa.gov/corps/)
- Get Department of Revenue "Revenue Clearance Certificate" [Read more](#) / [Get application at https://dor.wa.gov/doing-business/my-account/revenue-clearance-certificate.](https://dor.wa.gov/doing-business/my-account/revenue-clearance-certificate)
- File [Articles of Dissolution](https://www.sos.wa.gov/_assets/corps/nonprofitdiss2010v3.pdf) (DOR certificate required from https://www.sos.wa.gov/_assets/corps/nonprofitdiss2010v3.pdf)
- Consult with the Washington Office of the Attorney General, which supervises nonprofits in Washington:
Email: charities@atg.wa.gov
Address: 800 Fifth Avenue, Suite 2000, Seattle, WA 98104
Telephone: (206) 389-2061
- Prepare draft Plan of Dissolution
- Board tentatively approve Plan of Dissolution, subject to AG approval
- Send to Attorney General and request approval
- Upon approval, adopt final Plan of Dissolution

Federal

- Check yes (final return) on either:
[IRS Form 990 \(https://www.irs.gov/pub/irs-pdf/f990.pdf\)](https://www.irs.gov/pub/irs-pdf/f990.pdf) Part IV, line 31
or [IRS Form 990 EZ \(https://www.irs.gov/pub/irs-pdf/f990ez.pdf\)](https://www.irs.gov/pub/irs-pdf/f990ez.pdf) line 36.
- Complete the Liquidation, Termination, Dissolution or Significant Disposition of Assets - [Schedule N \(https://www.irs.gov/pub/irs-access/f990sn_accessible.pdf\)](https://www.irs.gov/pub/irs-access/f990sn_accessible.pdf)

Board

- Review your Articles and Bylaws to know the "rules of the road" about how your organization should proceed with decisions.
- Vote on a [Resolution of Intent to Dissolve \(https://www.centerfornonprofitexcellence.org/sites/default/files/files/Sample Resolution of Intent to Dissolve.doc\)](https://www.centerfornonprofitexcellence.org/sites/default/files/files/Sample%20Resolution%20of%20Intent%20to%20Dissolve.doc). Document the decision in board minutes.
- Create a communications plan, first with your core constituents, then with others
- Vote on the distribution of assets. IRS 990/990EZ Schedule N provides a good chart to follow. Note that this comes after you have paid all of your debt and have settled any contracts or grant agreements you might have.
- Celebrate.



Operations

- Calculate all of the direct and indirect costs of shutting down your organization. Set these funds aside so that you don't fall short later on.
- As soon as you take a vote to dissolve, your organization should stop or transfer programs. If you provide direct services, offer transition information and referrals.
- Communication. The specifics depend on your organization, but communicating with all key people within your organization and with the entire community is an important part of dissolving your organization.
- Pay liabilities.
 - If you have received restricted donations for a specific purpose, you will need to return the funds to the donor.
 - Discontinue leases or service contracts. You may be able to negotiate the amount due.
 - Pay all payroll, payroll taxes, and any other payroll related obligations.
 - This can get quite complicated. You may need help from a CPA or attorney to settle the financial and legal obligations of the organization.
- Layoff staff (if applicable). This includes making sure you issue appropriate tax paperwork to employees and shut down your accounts with the Washington State Employment Security Department and Labor & Industries.
- Distribute assets based on the vote taken by the board. Typically, if there are assets remaining after payment of all liabilities (whether cash, tangible items, or anything else) they are given to another nonprofit organization with a similar mission. The recipient must be approved by the Washington Attorney General's office.
- Cancel insurance.
- Close your bank account.
- Make sure that your organization can continue to receive mail for at least a year. You may want to file an official address change to the home of a board member or your attorney's office if you are vacating your current address.

It is at this point that most organizations have completed the dissolution of their organization. At this point, the board can disband. Time for a celebration with your constituents of all you have accomplished!

Resources

National Council of Nonprofits: <https://www.councilofnonprofits.org/tools-resources/dissolving-nonprofit-corporation>

Washington Nonprofit Handbook: <https://communities-rise.org/resources/washington-nonprofit-handbook/>



Frequently Asked Questions (FAQ)

1. What happens if all of the board members disappear?

If everyone disappears and refuses to do anything, even just to cooperate in a dissolution, there are remedies through the courts. But this is exceedingly rare. There is almost always someone who will step up and do what has to be done to avoid chaos. Board members who simply walk away and refuse to participate in a rational winddown of the organization could well be violating their fiduciary duties as directors.

2. Can we “give away” the organization to an all new board?

Technically yes, but practically not really, at least not without complying with some procedural and legal requirements.

There is nothing wrong with repopulating a board with new blood, although a completely new board is quite uncommon. That means there is no continuity, no institutional memory, and considerable disruption and inefficiency.

There is nothing wrong with merging the organization into another nonprofit, which in some respects is “giving away” the organization to the other. Keep in mind that a merger is a legal transaction that requires significant preparation and documentation, best accomplished with legal help and with the knowledge and consent of the Attorney General’s office. It is usually quite difficult to find another nonprofit to engage in a merger if your organization is insolvent - they would be absorbing all the liabilities without getting an equivalent amount of assets. In that situation, you should be considering the various kinds of dissolution noted above.

Finally, there is nothing wrong with identifying another nonprofit to be the recipient of the net assets of the organization after satisfaction of liabilities. Transferring the assets requires the consent of the Attorney General’s office. See above.

3. What if we don’t have money to pay our creditors?

There are several ways to accomplish a formal dissolution of an insolvent organization, whether for profit or nonprofit, including federal bankruptcy chapter 7; federal bankruptcy chapter 11 (very rare for nonprofits, but possible); state court receivership; state court assignment for the benefit of creditors. In some circumstances, organizations can go out of business without a formal process. How best to do that is a complicated question that should be addressed with the help of consultants, lawyers, or other professionals.



4. What is the board liable for?

There are several ways in which board members could become personally liable for the debts of a nonprofit, but such liability is really quite rare. Creditors of nonprofits are almost always sensitive to the unfairness (and the terrible public perception) of going after individuals who have been trying to help the community through service on a nonprofit board, and almost never assert such claims, even when grounds exist. Having said that, board members should be aware of a risk of personal liability when:

- They guarantee a debt owed by the organization. This is the one claim creditors are most comfortable pursuing against nonprofit directors.
- There are employees whose wages are not paid. Washington law allows such employees or the Department of Labor to assert personal liability on the part of officers and directors who were making decisions regarding who got paid and who did not get paid.
- There are withholding taxes that are not paid, whether employment related withholding taxes or sales taxes and the like. Both federal and state law provide for liability for such amounts, on the part of those who were making decisions regarding who got paid and who did not get paid. These individuals could include board members, the executive director, the financial officer (CFO), and accountant.
- There have been breaches of fiduciary duties on the part of the individual board members. Such claims are rarely asserted for breach of the duty of care owed by a director (that is, the obligation to make reasonable decisions based on reasonable input and effort), but they can and more often are brought when the director has breached the duty of loyalty (that is, has personally benefited from a transfer or a decision).

Many nonprofits have director and officer (D&O) insurance policies covering potential liabilities (although such insurance would not help with any guaranty claims). Such insurance is not expensive for nonprofits, in large part because such claims are quite uncommon.

5. This cash flow issue may be only a temporary problem. Instead of something drastic like dissolution, can I just ask the creditors to be patient and we'll catch them up as soon as we can?

You can ask; and some creditors will often be reasonable, particularly those who appreciate the work you are doing. But do not ask your employees to accept anything less than what they are owed, and do not think you can get away with not paying withholding taxes for a while. Not paying salaries or wages would be a violation of state labor laws, even if an employee agrees. Those are the areas where individual directors and officers may suffer personal liability as a



result of those unpaid bills. See the previous FAQ. (And remember - most nonprofit employees are already underpaid compared to what they could get elsewhere. It is unfair to ask them to take even more financial risk. Do not even think about going there.)

6. What do we do with restricted assets such as endowment funds and grant moneys?

Again, this is not a simple analysis, and it should be performed with assistance of lawyers or other consultants. Having said that, there are a couple of basic rules:

- Some funders will, if approached, release the restrictions and allow the funds to be used to pay creditors or go to another nonprofit without the restrictions.
- Others will insist on continued maintenance of the restrictions (or cannot be contacted), in which case the restricted assets must continue to be used in accordance with the restrictions. The Attorney General's office should be consulted in order to ensure the assets remain dedicated to the public benefit for which they were intended.

7. Do I really need a lawyer for this? Lawyers are expensive.

Many of the issues surrounding the dissolution decision, and the dissolution process, are complex. A lawyer may not be necessary, but you really should be consulting with someone who has been through the process before and can show you the ropes.

In any event, while paying lawyers ordinary rates for this kind of advice can indeed be quite expensive, there are resources available that can help identify lawyers and others who are willing to help at no or greatly reduced cost. Wayfind can provide free legal services for dissolution to qualifying nonprofits or may be able to refer you to an attorney