Church Incorporation Update 2007

In 2007 the North Carolina Legislature adopted Chapter 59B: Uniform Unincorporated Nonprofit Association Act. It states that a non-profit and/or church can be considered as it is an incorporated entity in cases of litigation. This lifts the importance of incorporation as a risk management factor; however, Dr. Lynn Buzzard has written a statement that explores the impact of Chapter 59B and suggests that incorporation is still a good idea for churches.

Impact of Provisions of NC Gen Stat. 59 on Incorporation of Churches and Nonprofit Ministries

A major factor in considering incorporation of both businesses and nonprofit organizations, including churches, has been to take full advantage of the “limited liability” available through a corporate form. In the development of liability law, a corporate form or legal structure had the substantial advantage that while the corporation was liable for its debts and obligations, the stockholders (owners) of the corporation were not personally liable merely because of their ownership interest. This of course encouraged investment and risk in business ventures. The same advantages developed for nonprofit corporations, so that while the nonprofit corporation remained fully liable for debts and judgments for its acts, the members of those nonprofit organizations were not personally liable. Without this protection from the corporate form, members of many organizations—social, fraternal, benevolent—might find themselves financially at risk if the association they were a member of had some debt exceeding its assets.

The same issues affected churches which in North Carolina were rarely incorporated prior to the 1980s, and thus members were potentially at risk if the church’s debts exceeded their resources. This was a principal factor in the recommendations from legal and church leaders that churches consider moving from an unincorporated association status to incorporation. In North Carolina this was particularly advantageous because the state imposed no annual fees or reporting obligations on such nonprofit incorporations.

In 2007 North Carolina enacted a Uniform Unincorporated Nonprofit Association Act, now Chapter 59, in the General Statutes. This new statutes addressed a range of legal issues and sought to give clarity in regard to matters affecting all kinds of unincorporated associations, including many church and religious unincorporated associations in North Carolina. Of particular relevance to the issue of incorporation is Section 59B-7 which changes some older traditional legal principles, and treats the unincorporated association as a legally separate entity from the members as far as certain rights and duties exist and specifically provides that “A person is not liable for the contract, tort, or other obligations of a nonprofit association merely because the person is a member, is authorized to participate in the management of the affairs of the nonprofit association, or is referred to as a ‘member’ by the nonprofit association.”

The effect of this provisions is to provide the same kind of limited liability to members of an unincorporated nonprofit (such as an unincorporated church), as they would have if the entity were incorporated. This does provide it would seem one of the kinds of protections historically sought by incorporation. And under this statute, the unincorporated association such as a church need take no specific action in order for its members to have the protection from personal liability “merely” because they are members.

NOTE: This new statute does NOT provide absolute immunity from liability – but only provides that there is not any personal liability merely because of membership in the group. If the person, whether a member or not, has engaged in some acts creating liability – even if for and on behalf of the church – they may well be liable – but not because they were a member, but because they personally did some act creating the liability. Thus if a person
who is a member negligently operates a vehicle while acting for the church and injures a person, they may well be liable because they were personally negligent, but not because they were a member.

The same is largely true of immunity and limited liability derived from incorporation provisions.

Now the questions is appropriately asked whether now that 59B-7 provides limited liability similar to incorporation protections, is there any reason any longer for churches and other nonprofit associations or ministries to bother with incorporation.

I believe the answer remains Yes – that it remains advisable and prudent for such unincorporated churches and ministries to carefully review the full advantages of a corporate form, notwithstanding the clear benefits of the new Chapter 59 provisions.

In sum, I believe this is so for several reasons:

1) Chapter 59 is a valued new source of legal protection, but its scope and the application of its provisions is untested, compared to a wealth of clear provisions and cases addresses provisions under the nonprofit corporation provisions.

2) Chapter 59 is less clear and specific about other aspects of limits on liability especially in regard to officers and directors – or in churches we might think of deacons and other church leadership. By contrast, the Nonprofit Corporation Act in Section 55A-8-60 is very clear about certain immunities of directors and officers, AND the conditions under which they are and are not immune. Given the fact the most serious risks for liability are NOT so much extensions of liability to mere members, but arising from acts of the leadership of a church, it is in this area that the greater clarity of the scope of protections provided by the corporate form are clearly preferable. It may be that a court might construe the provisions of Chapter 59 similarly, but that is not so clear.

3) Chapter 59 addresses a relatively small set of issues related to organizational legal identity, and does, as noted, provide some protection for unincorporated bodies, but in no way does it even attempt to provide the much broader provisions of the nonprofit corporation act which are so very key and constructive in clarifying all kinds of issues and aspects of organizational affairs. One of the greatest values of incorporation is not just the limited liability, but the order and breadth of clarity about many other aspects of the structures and procedures of an effective organization. In my experience, carefully crafted Charters and Bylaws developed as an aspect on the process of incorporation have been extraordinarily valuable in clarifying many areas that, because they have not been addressed, have often been the subject of disruptive and divisive conflict in churches.

4) Since North Carolina has long been a friendly state to nonprofit corporations, has no history of intrusive regulations or reporting schemes, has no annual fees, and offers superior and clear protections for both members and leadership, and provides a framework for other broad areas of organizational life, it would in my view be a mistake to rely on one small piece of the puzzle through Chapter 59, and ignore the broader provisions of a nonprofit corporate structure.

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