

# For Profit, Nonprofit and Beyond: Considerations for Media Start-ups

By Heather Franklin

## INTRODUCTION

The last decade has seen an expansion in new journalism start-ups, both for-profit and nonprofit. However, journalists moving from reporting to running an organization face a range of questions from the outset about the kind of newsroom they are trying to build. We are asked regularly by journalists whether they should incorporate as a commercial or a charitable entity. Unfortunately, there is no easy answer.

That's why we created this guide for journalists and media entrepreneurs. This introductory primer is meant to be a brief overview of the issues discussed at greater length in the guide "[Which Legal Structure is Right for My Social Enterprise? A Guide to Establishing a Social Enterprise in the United States](#)," written by Morrison & Foerster LLP for the Thomson Reuters Foundation in 2016. We encourage you to check out that longer piece for more detailed information and longer discussions around issues like financing your venture.

In the sections that follow, we try to arm you with key questions and considerations to take into account as you get your organization off the ground. However, we want to make clear that your tax status is not the same as your business model. Deciding how to structure your organization is only step one, and increasingly nonprofits, for-profits, and hybrid organizations are facing similar revenue challenges and are exploring similar solutions. The tax status and structure of your organization will shape the kind of business you build, but regardless of how you incorporate, you are going to need to develop a diverse revenue mix that truly meets the needs of your community.

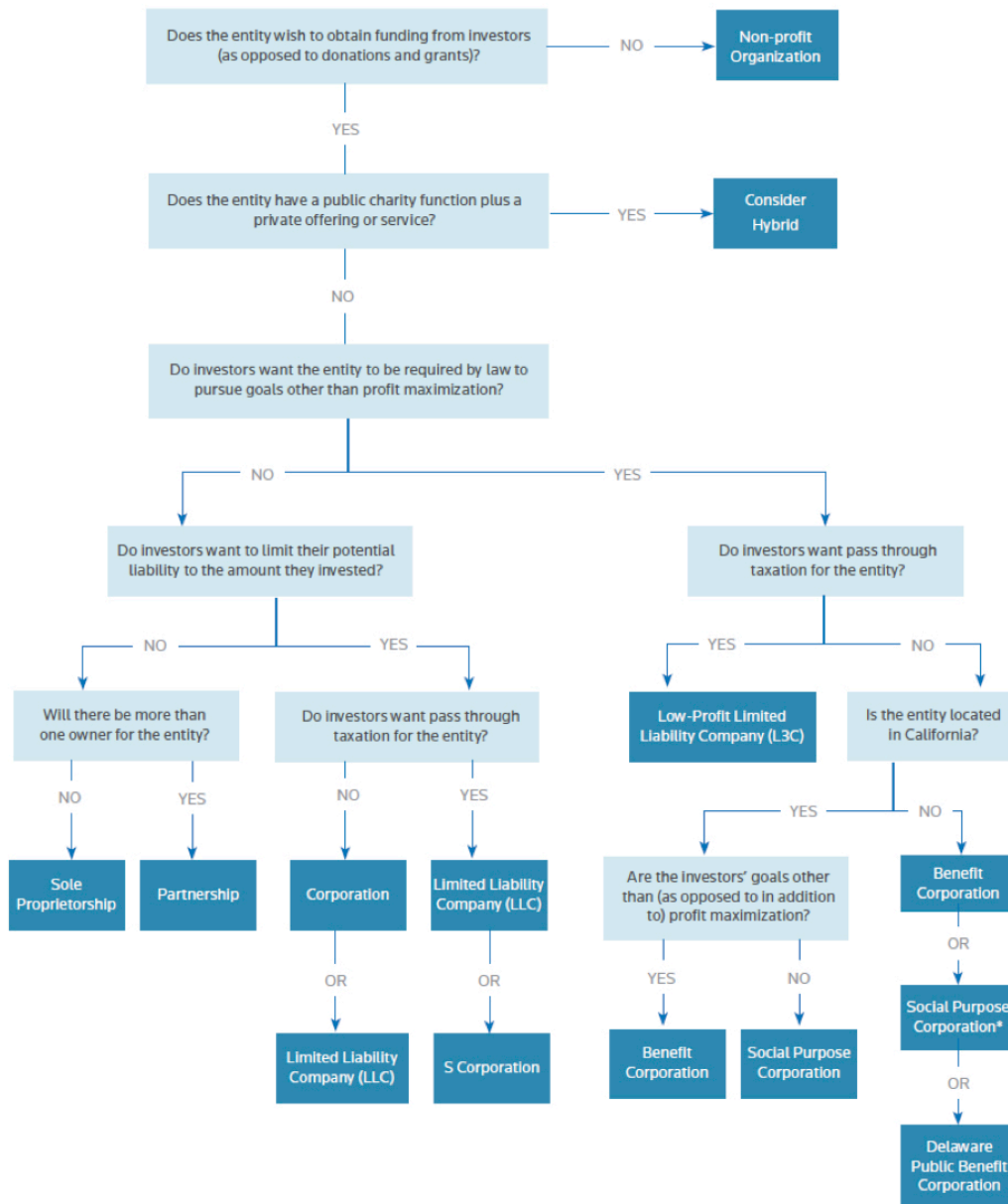
In addition to the key questions and considerations presented in the following sections, we have included a [chart](#) that outlines the relative ease of formation, ownership rules, liability, ease of operation, management structure, tax treatment, and lifespan of the eight business models discussed in this guide.

Nothing in this guide should be understood as legal advice or counsel. Anyone setting up a new organization should work with a lawyer and tax professional. We are indebted to the [Digital Media Law Project](#) and Morrison & Foerster LLP and the Thomson Reuters Foundation whose earlier work was the foundation of this project.

The guide from Morrison & Foerster LLP and the Thomson Reuters Foundation provides [an invaluable flow chart](#) that walks readers through a series of questions to assist them in narrowing down the right business model for them. The flow chart (below) is a great resource for figuring out what is important to you about your new venture and understanding how your decisions regarding your new venture's guiding principles can guide what business model is best for you. In the sections that follow, we provide more background about the various legal and tax structures you can choose from.

# DECISION MAKING FLOW CHART FROM THE REPORT: "WHICH LEGAL STRUCTURE IS RIGHT FOR MY SOCIAL ENTERPRISE? A GUIDE TO ESTABLISHING A SOCIAL ENTERPRISE IN THE UNITED STATES."

by Thomson Reuters Foundation and Morrison & Foerster. Published, September 2016.



\* Washington and California have adopted "social purpose corporation" legislation (which differs in certain key areas from benefit corporation legislation adopted in many other states).

## COMMERCIAL VENTURES: THE BASICS

In the United States there are three broad categories of business models: traditional for-profits, nonprofit corporations, and non-traditional hybrid models. Within the umbrellas of traditional for-profits and non-traditional hybrid models there are multiple options from which to choose – each offering its own costs and benefits. For more information about each of these business models, click [here](#) to view the chart which endeavors to lay out the basics of each model in more detail.

### Traditional For-Profits

Under the traditional for-profit umbrella there are four different business entities: sole proprietorship, partnership, limited liability company (LLC), and corporation.

- **Sole Proprietorship and Partnership:** Designed for small businesses with a limited number of employees. Neither requires formal incorporation filings with a state government.
- **LLC and Corporation:** Can be used for larger ventures, and therefore come with the benefit of limited liability for the members or shareholders as well as increased formalities around reporting.

### Non-Traditional Hybrids

In addition to the more traditional business models, there are a number of “non-traditional” for-profit models to choose from. The goal of these models is to provide business owners with an alternative to purely profit-driven models. These models are designed to allow business owners to build a social benefit into their mission. They include the worker-owned cooperative, the low-profit limited liability company (L3C), and the benefit corporation.

- **Cooperative:** In a worker-owned cooperative, the workers own the business. Cooperatives are run by democratic principles and are often used by individuals who want to build community wealth by keeping profits within the community that the business is located.
- **L3C and Benefit Corporation:** Both are variations of more traditional business models. The L3C is modeled off of the LLC while the benefit corporation is modeled off of the traditional corporation. Both models operate according to many of the same rules as their more traditional counterparts, but they both have a double bottom line: one focused on turning a profit and the other on creating a public benefit. It’s important to note that the L3C and benefit corporations are not recognized in all 50 states, so you will need to check with your local Secretary of State’s office for more information.

## NONPROFIT VS. FOR-PROFIT: WHICH IS RIGHT FOR YOU?

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### Nonprofit

Before we discuss the challenges and benefits of the nonprofit structure, we should define the core vocabulary involved. (The terms below are often conflated, so it's useful to have clarity about the differences between them.)

- **Nonprofit corporation** is the legal entity most nonprofits use to register with their state government. It is possible to establish a nonprofit organization using another business structure, but a corporation is generally the most appropriate organizational structure.
- **Tax Exemption** is achieved when a nonprofit corporation has filed the necessary paperwork with their state government and the IRS to exempt the organization from paying income taxes. At least on the federal level, nonprofit organizations are not automatically tax exempt, and each state has its own tax code and regulations. To find out more about the rules in your state, consult a tax professional.
- **Tax Deductible** refers to the kinds of gifts (the most common being cash donations) a nonprofit can receive after they successfully apply for tax exempt status. Tax deductible gifts can be written off by individuals and businesses on their tax returns. The ability to receive tax deductible gifts is a benefit granted to some (but not all) 501(c)(3) charities.
- **501(c)(3)** is the section of the U.S. Internal Revenue Code (the “tax code”) that exempts charitable nonprofit organizations from paying federal corporate income taxes.
- **Private foundations and public charities** are the two umbrella classifications of organizations laid out in section 501(c)(3) of the tax code. Anyone looking to start a journalism venture will likely want to be classified as a public charity, as private foundations face a number of additional complex legal rules and restrictions.

Organizations with the following purposes are able to apply for tax exemption under section 501(c)(3): religious, charitable, scientific, public safety testing, literary, educational, amateur sports, or the prevention of cruelty to children or animals.

You'll notice that journalism is not listed there. The IRS has had a [long](#) and [complicated](#) relationship with journalism which has at times threatened the ability of news organizations to receive tax exempt status. Most journalism nonprofits receive their exemptions as organizations with an educational purpose, but the IRS has specific ideas what educational organizations do. You should review the work of the [Digital Media Law Project's IRS guide](#) before filing for your application for 501(c)(3) status, and definitely consult a tax professional.

Here are some things to consider about setting up as a nonprofit:

- **Administrative Costs:** Nonprofits require significant administrative coordination including required federal and state documents (such as Form 1023 –the application required of nonprofits seeking tax exemption from the IRS), organizational documents (bylaws, board meeting minutes), and ongoing administrative tasks (IRS Form 990, audits, etc.)
- **Foundations and Donations:** Nonprofits are eligible to receive private foundation grants and tax deductible gifts from private individuals. Commercial entities can also receive grants and donations, but donations to for-profit entities are not tax deductible and many foundations often will only make grants to 501(c)(3)s.
- **Nonprofits can make profits:** Within reason, nonprofits are legally allowed to make a profit. Nonprofits are permitted to accumulate a reasonable reserve, but they are not allowed to operate with the goal of accruing profit. Nonprofit organizations that seem to be intentionally overshooting their budgetary goals can have their tax exemption revoked by the IRS. Any profits are required to go back into projects that fulfill the organization’s mission. In addition, 501(c)(3) nonprofits may not be operated for the benefit of any private person or group.
- **Taxation:** 501(c)(3) nonprofits do not pay federal corporate income taxes, and they often are not subject to state income taxes. Depending on your locality, 501(c)(3) nonprofits may be exempt from other forms of taxation. For more information on the specific tax rules in your state and town, consult a tax professional.
- **Advertising:** Within certain constraints nonprofits are allowed to sell advertisements. Many nonprofit journalism sites – including [MinnPost](#), [VTDigger](#), and [Mother Jones](#) – include ads. However, it is important that ad revenue is accounted for correctly so you don’t end up paying too much in unrelated business income tax, which can raise red flags at the IRS and result in the revocation of an organization’s 501(c)(3) status. In granting nonprofit status the IRS examines whether newsrooms are operating differently than commercial outlets, so advertising is best used as a supplement to other revenue streams. For more on nonprofit journalism, advertising, and the IRS see the [Digital Media Law Project](#).
- **Endorsements:** Organizations with tax exemption under section 501(c)(3) are not allowed to endorse or oppose candidates for political office.
- **Lobbying:** Nonprofits are allowed to engage in some lobbying and can engage in advocacy, but there are somewhat complex limitations on both. The resources at [Bolder Advocacy](#) offer good guides for nonprofits looking to engage in lobbying and advocacy.

## For-Profit

While there are reporting obligations and other formalities associated with commercial newsrooms, compared to nonprofits, for-profit news organizations have relatively few rules to take into consideration or abide by.

- **Ownership:** As is outlined in the accompanying [chart](#), ownership and managing powers vary depending on the business model you choose. In a for-profit venture the owners are able to maintain close control of their business in virtually all models (the exceptions being a publicly-traded corporation or a benefit corporation).

- **Revenue Generation:** For-profits have similar options to those of nonprofits except for being eligible for tax deductible donations. However, if a for-profit news venture wants to raise capital from their readership (in a move analogous to nonprofits soliciting individual donations) they can do as [Berkeleyside](#) has done and start a direct public offering (DPO) or other investment mechanism.
- **Professional Compensation:** For-profits are permitted to distribute profits, and high salaries do not raise the same kind of suspicions in for-profit ventures as they do in nonprofits.
- **Taxation:** Depending on the for-profit business model you choose (click [here](#) to see the attached chart for more information), for-profits may be required to pay corporate income taxes. This means that revenue is subject to double taxation –first on the business level and then again when it is distributed as salary to employees.
- **Advertising:** For-profits are allowed to sell as many advertisements as they want with no restrictions on the content, and they can include as many calls to action as they want in their political coverage. In addition, they can endorse political candidates for elected office.

## FINDING A THIRD WAY

While the for-profit versus nonprofit choice has long defined the conversation around business options in the United States, there have been moves to create alternatives. These models strive to strike a balance between making a profit and benefiting the public – or take advantage of the best of both worlds. These third way arrangements include models like worker-owned cooperatives, low-profit limited liability companies, benefit corporations, and nonprofit/commercial partnerships.

- **Nonprofit/Commercial Partnership:** This would involve setting up two organizations with different tax statuses. The organizations would serve as partners and work together to meet different but aligned missions while taking advantage of different benefits and subsidies. In a partner-subsidiary relationship, the nonprofit has to be run independently of the for-profit and must operate primarily in the service of its charitable mission. An example of what this might look like is a nonprofit investigative journalism organization partnering with a for-profit publishing company.
- **Cooperative:** There are [5 kinds](#) of cooperatives to choose from. Cooperatives are operated by democratic principles and are generally committed to the communities they operate in. [Bristol Cable](#) in the U.K. and [Haverhill Matters](#), a project of the [Banyan Project](#), are examples of this model. [The Devil Strip](#) in Akron, Ohio, is also pursuing a cooperative model.
- **Benefit corporation:** Benefit corporations are a mutation of the traditional corporation that provides a double bottom line: one focused on profit and the other on creating social benefit. It's important to note that benefit corporation legislation has not been adopted by all 50 states. This is not to be confused with B Corp certification, which is a third party standard that companies can measure themselves against. B Corp certification is similar to the Good Housekeeping Seal or Fair Trade Certification. Companies are not required to be incorporated as a benefit corporation to become B Corp certified. In addition to offering a DPO, [Berkeleyside](#) was a benefit corporation (as of 2019 they converted to nonprofit).

- **Low-Profit Limited Liability Company (L3C):** Like the benefit corporation, L3Cs are based on a for-profit counterpart. Legislation establishing the L3C has only been passed in a handful of states, and we have been unable to find examples of journalism organizations utilizing this business model.

## CONCLUSION

Deciding on a business model is not easy, but we hope this primer helps you understand the nuances to the decision and allows you to start a deeper conversation about what option is right for you. If you want to read more about what was discussed in this brief primer, feel free to read [the longer guide](#) written by Morrison & Foerster for the Thomson Reuters Foundation.

Before you finalize any decisions we highly encourage you to seek out the advice of a lawyer and tax professional. While switching your tax status is possible, it is financially and logistically burdensome. Nonprofits looking to go for-profit will have to determine what to do with any assets, as charitable funds are required to remain in the charitable sector, and it is possible that past revenues could be taxed at a penalty if the IRS decides that the organization's nonprofit existence was a sham to support the launch of a for-profit entity. Any for-profit seeking to transition to a nonprofit will be required to restructure and will face heightened scrutiny by the IRS to ensure that the venture is not too commercial to be a nonprofit. Therefore, it is important to consider all of your options carefully and with as much information as possible. We hope that this primer offers you a foundation to build upon as you move forward in the process of designing your venture.

## APPENDIX 1: ADDITIONAL RESOURCES

- [Types of Business Models for New Journalism Ventures](#) – Heather Franklin
- [Which Legal Structure is Right for My Social Enterprise?: A Guide to Establishing a Social Enterprise in the United States](#) – Thomson Reuters Foundation and Morrison & Foerster, LLP
- [How to lose your 501\(c\)\(3\) tax-exempt status \(\*without really trying\*\)](#) – IRS
- [Establishing Your Organization](#) – Bolder Advocacy
- [Types of Organizations](#) – Bolder Advocacy
- [Navigate the Rules](#) – Bolder Advocacy
- [Forming a Business and Getting Online](#) – Digital Media Law Project
- [Launching a Nonprofit News Site](#) – J Lab
- [Law for Media Startups](#) – Tow-Knight Center for Entrepreneurial Journalism
- [Tax-Exempt Journalism and the IRS](#) – Digital Media Law Project
- [Planning a Nonprofit News Organization](#) – Institute for Nonprofit News
- [Other Resources for Forming a Nonprofit News Organization](#) – Reporters Committee For Freedom of the Press



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## **ABOUT US**

Created by eBay founder and philanthropist Pierre Omidyar, Democracy Fund is a foundation helping to ensure that our political system can withstand new challenges and deliver on its promise to the American people. Democracy Fund has invested more than \$125 million in support of a healthy, resilient, and diverse democracy with a particular focus on modern elections, effective governance, and a vibrant public square. For more information, please visit [www.democracyfund.org](http://www.democracyfund.org).

## **ABOUT THE AUTHOR**

Heather Franklin was a graduate intern for Democracy Fund when she wrote this report, and is currently a Digital Campaigner and C. Edwin Baker Fellow at Free Press.