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## Are Nonprofit Startup Costs Tax-Deductible Donations for the Founder? – Transcript

Jess Birken 00:00:02 Welcome to Charity therapy, the podcast where we explore the ups and downs of the nonprofit sector and answer your burning questions. I'm your host, Jess Birken, owner of Birken Law Office, and I'm excited you're here. Imagine hanging out with me and my super smart, funny, nonprofit expert pals. You get to ask them anything about your nitty gritty nonprofit life and get their wisdom for free. Whether you're a seasoned pro or just strapping on your nonprofit boots, we're here to share stories and remind you you're not alone on this journey. So get ready to join the conversation and bring me the tough questions I ain't scared. Ready to rock? Let's dive in. Hello and welcome to this episode of Charity therapy. I am back with Megan. Hello. I am here with Jess.

Meghan Heitkamp 00:00:50 Since you didn't introduce yourself, why was that delay? Because I really thought you had more to say. And then you didn't. But that's fine. We can just. I don't know, It's bare minimum. It's a day.

Meghan Heitkamp 00:01:03 It's a day. I started this day trading barbs with my teenager Max. And.

Jess Birken 00:01:10 And he called me a chud.

Meghan Heitkamp 00:01:13 Whenever you say that, I just keep thinking it sounds like a slur of some kind. So I keep being like, no. And then it's like, oh, no, it's not actually like. I

mean, it's not a compliment, but you're not saying compliment like worse than dummy or something. I don't.

Jess Birken 00:01:28 Even.

Meghan Heitkamp 00:01:28 Know.

Jess Birken 00:01:29 I honestly, I don't even know because.

Meghan Heitkamp 00:01:31 I'm.

Jess Birken 00:01:32 Of the era that.

Meghan Heitkamp 00:01:33 Judd's.

Jess Birken 00:01:34 Was a horror movie that and.

Meghan Heitkamp 00:01:36 Chud stood.

Jess Birken 00:01:37 For cannibalistic humanoid underground dweller, I think. And it was like a I believe the loose plot of this movie was that, like in the sewers of New York City, there were these creepy things that probably they reach out of the sewers and grab your ankles or something. I don't know, I've never seen the movie, but it's like lore. It's

like law. And so then I'm like, why is my 17 year old using the word chud? Because ain't no way that Max understands.

Meghan Heitkamp 00:02:09 He has no idea. He has no idea. Now I need to go find it and watch this movie. Like, do you have the sense? Obviously you haven't seen it, but is this, like, genuine horror movie or, like, b side terrible horror? That's really funny. So I think.

Jess Birken 00:02:23 Let's take horror in the loosest possible terms, like attack of the Killer Tomatoes level horror.

Meghan Heitkamp 00:02:33 Which also I've never heard of. And that sounds incredible. So. Oh, it's.

Jess Birken 00:02:35 Literally.

Meghan Heitkamp 00:02:36 A.

Jess Birken 00:02:37 Quote unquote horror movie where people are mowed down by giant tomatoes.

Meghan Heitkamp 00:02:44 Great.

Jess Birken 00:02:44 So, you know, I don't think you can be that scared watching a movie where and remember, this is like the 70s.

Meghan Heitkamp 00:02:53 So the special effects, special effects are quite special.

Jess Birken 00:02:57 Just like a trick of the lens with, like, a giant tomato, you know, and probably like a big red piece of cloth, like trying to be shoved inside of a door or something and people being like, no, not the tomatoes.

Jess Birken 00:03:11 Oh, I'm so ready. I need to go watch this. This is such as, like what I used to. Yes. Like, this is what used to be. And we need to go back to that. Yeah. Like there was the attack of the lycanthrope or something, which was like a giant rabbit's giant. Right? So, like, they just film a rabbit, but then they, like, layer on a person in the frame. And because rabbits are a little terrifying, they really only when you see them yawn and you realize what their tastes look like. You're like, oh my God. And I know this courtesy dress of your rabbits when I crush them. And when I used to yawn, I was like, this is horrifying. Like, you are scary. I did not know. So, I mean, I'm just saying we need to go back to that era of horror because the whole, like, gore porn thing, I'm just like, no, that's gross. I want giant tomatoes chasing people.

Jess Birken 00:04:05 It's the sound of like squishing fruit being the scary part. If there's any horror movie buffs listening, please like come at us with some recommendations because I see a bad horror movie marathon in our future, so I love that. Come at us. Okay, what are we actually doing? We're now talking about the. Actually, this one is not even the horrors. This is not the horrors of non-profit life. In fact, today we're talking about good things for the good, which we love. It's a good change of pace sometimes, but today we're talking about a question from a startup, someone who just started a new nonprofit. And before we get into the question, Jess, I wanted to talk to you a little bit about what it looks like to start a nonprofit, because people often reach out and are surprised to hear how much money and time it takes to actually create the nonprofit before they can even start applying for grants and doing all of the things. And so what does it like? How do people pay for this? Like, what does it look like? What do they need to have in place in order to start a nonprofit? I mean, it does kind of depend.

Jess Birken 00:05:19 I mean, there are the people who go to the legal zoom and get some templates filed for them for free, basically for low, low cost of like \$500, you can have the state's free form filed for you at a rip off price. Yeah. But if you're going to do it well and you're going to do it right, and you're going to actually have documents that meet the requirements of the IRS and your state and nonprofit best practices, it probably looks at least like hiring somebody, getting a service from somewhere, and then it's going to cost money. Right. Whether you are legal zooming it or hiring me or somewhere in between, it's not free and I think that's the main things people like. But we're going to be a charity. That's great, but a charity is just a business that has a special income tax status and it's going to need insurance, it needs accounting, it needs legal advice, and fundraising is going to take time and may require some expertise. You need a website. You need all these things.

Jess Birken 00:06:30 Right. And so I think people don't really realize that they're really just they're starting a company. Yeah. Like well, and all of the things that go with that, when I talk to people out front, there's often this sort of like, well, we're gonna fundraise to cover all of the costs, but we need a nonprofit in order to fundraise, or we need to, you know, I have this like Grant, I'm looking at that. We'll be able to cover this, but like, what do we do until then? And there's this sort of chicken and egg problem of like, I need the nonprofit to get the money, but then I need the money to get the non-profit and people get stuck in this problem for a long time before they're actually ready to start anything. Yeah. So that's the thing is, like, you have to spend what's the saying? You got to spend money and make money. Yep. You do have to, like, put some money in before that tax exempt status comes.

Jess Birken 00:07:25 And frequently that is the founder. That is usually our passionate person who wants to do the thing. Yeah. And it looks a little different depending on the entity. Like sometimes it's just an individual person. Sometimes it's a group of people pooling their resources. Sometimes another organization wants to help them out or something like that. You know there's a million ways that this happens. But like you got to get money from somewhere and it's not going to be some big government grant given to you as a lowly individual with an idea, you know, like it's it's going to be smaller and scrappy than that. Okay. So I have a question from just this kind of founder. So, Jess, are you ready to talk about this question? Hit me. In June of 2025, two friends and I created a scrappy little housing placement nonprofit. We all put some of our own money into the bank in June to help make it happen, and we earned our official 501 C3 tax designation from the IRS that September. Does that start up cash? We each contributed count as a

tax deductible charitable donation, even though it happened before our five one C3 status.

Jess Birken 00:08:38 Okay. Great question. First of all, a couple of things. June. September. Right. So there's that some of that chicken and the egg. Right. Because it takes months just to even frankly that's fast. Yeah. Yeah. Exactly. Exactly. I'm guessing that they probably didn't spend a lot of time making bylaws, and they probably did the quick and dirty application. Three months is is not that long, but it is time. And so there, there it is. Case in point, I want to give them props for opening a bank account for the nonprofit and putting the money into the bank. Good job. Sometimes we talk to people who are like, I just have this money and my personal checking like, no, that's not correct. So yeah, good work. So then the question really is, what about the money that you contributed to the nonprofit before you had the income tax exemption? What gives. Is it deductible. What's happening. So there's this nice feature that the IRS knows you have this chicken and egg problem.

Jess Birken 00:09:44 And they also know that they are, shall we say, not the fastest agency that exists in the world under as long as the year. Right. So as long as you apply for income tax exemption within the first two years, technically it's 27 months, but within that first two years of incorporation from the minute you sign up with the state to say we're going to have a non-profit entity, if you seek income tax exemption in that first two year window, the IRS will say, hey, good job getting it to us. Sorry it took us so long. We're going to backdate your income tax exemption all the way to the day you first incorporated. Which basically kind of does like the Spiritus Sancti papal blessing on all of the money that went into the nonprofit's bank account and sort of like retroactively, in a sense, makes that deductible. Now, the wrinkle here, though, is, yeah, you got a two year window, but you're going to be filing your taxes before that. So ideally, if you are getting your income tax exemption, you're not waiting two years because you've already filed your taxes.

Jess Birken 00:11:07 You can't really claim it as a deduction because that there was no C3 status. So you do want to try and hurry up. Hurry up and get it done basically so that you can if you qualify for a deduction, which is a whole other thing, whether it actually counts for you or not is a thing between you and your CPA. But as long as you've got that income tax exemption before April 15th, everything that happened over the past

year is good. Golden. It all counts because of that IRS backdating. And I just want to bring up because I hear about this from founders in a couple of ways. Like this is one major way that founders choose to fund the beginning of the nonprofit is I'm just going to put my own money into it, and I will take a, you know, deduction on my taxes if it makes sense. But I am just donating my money basically to to get this up and running. We also sometimes see founders who ask the board to vote and have the nonprofit pay them back, basically.

Jess Birken 00:12:16 So even though the nonprofit didn't exist with funds at this time, the board votes and says, hey, like you fronted the nonprofit this cash, we are going to reimburse you and take it on as an expense of the nonprofit and not your individual costs. But that also depends on the nonprofit having the money to do that. Right, right. Because the board has to decide that it's in the best interests of the organization to reimburse those expenses that whoever the founder, one of the initial board members incurred. Nine times out of ten, I don't know why it wouldn't be. So that's going to be fine. But you do have to have a board vote at a board meeting and say here, here are the expenses. I'd like to be reimbursed. And you cannot like in year one. I said this was a donation and now I took a deduction. And now in year two, now that we got our status, well, now I would like to be reimbursed. No, that's that's that's called table dropping people.

Jess Birken 00:13:16 Yes. So you need to decide what you're going to do, at least before your tax filing is coming up, because you can't go back later if you already claimed it as a deduction, as a gift, as a contribution. There's no take backs, as we would say in the 80s. Yeah, exactly. Exactly. So I mean good news for this person. Like yes. The answer is yes. Like your contributions count and you can work with your own tax professional about what that looks like for you. But the IRS would consider that donation to be, you know, to a tax exempt, you know, charity that you can take a deduction for. Okay. I have a couple of takeaways here for us in this conversation. So first, I think the big one is that nonprofits are businesses and all businesses have startup costs. so it will cost money to start a non-profit and likely money out of your own pocket. Despite the fact that you can fundraise and raise money for non-profits down the line, it's a little unlikely you're going to get a lot of money in the door just to do the, like, initial filings.

Jess Birken 00:14:25 So if you are a hopeful nonprofit founder, keep that in mind and remember that you're going to need a chunk of change to work with before you can even get started on being a fully tax exempt nonprofit. Secondly, when you do apply for tax exempt status, if you do it within a certain window of 27 months, the IRS, when they approve your application, will also backdate your tax exempt status to the day you started the nonprofit, the day you incorporated it. So anything that did happen in that mean time is considered an add a tax exempt entity. And that is how, you know, you can donate your money for those startup costs. And then finally. Nope, there's not a third one. That was it. I was really confident that was the third one. Just the two. That's all I got. I think the finally is no double dipping. You can't take a deduction one year and get paid back the next year. So just keep that in mind. Yes. All right, folks, if you enjoyed this episode, do me a favor.

Jess Birken 00:15:33 Share it with a friend. Rate review. Subscribe. If you know a founder who thinks they're going to start a nonprofit and then need a little reality check, you can share this one with them. If you've got a question or a story to share, please get at us. We would love to hear from you. Send us a note online at Charity Therapy Show. And as always, thanks for listening.

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## About the Author



**Hi, I'm Jess Birken**

I'm the owner of Birken Law Office, I help nonprofits solve problems so they can quit worrying and get back to what matters most – The Mission. I'm not like most attorneys, I actually have an outgoing personality, and – like you – I like to think outside the box. Most of my clients are passionate and have an entrepreneurial spirit. I'm like that too. My goal is to help you crush it. Getting bogged down in the minutia sucks the joy out of the important stuff. My clients want to do the work – not the paperwork.

**Let's connect!**

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