

Why every church needs a dissolution clause

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It used to be common for constitutions and bylaws of Baptist churches to include a dissolution clause. In the unlikely event the church should close, the clause indicated the church's assets would go to the association or state convention.

Over time, dissolution clauses started disappearing from church bylaws. And that is a significant problem, because ***churches without a dissolution clause could have to pay property and other taxes going all the way back to when they took the dissolution clause out of their documents.***

What is a dissolution clause?

A dissolution clause is a statement explaining what will happen to a nonprofit organization's assets in the event the organization dissolves or otherwise discontinues operating. It might be included in a nonprofit's bylaws, governing document or, if the nonprofit is incorporated, the certificate of formation. Here's one example of a dissolution clause:

Upon discontinuance of this Church by dissolution or otherwise, any assets lawfully available for distribution are to be transferred to one or more organizations qualifying as an exempt organization under Section 501(c)(3) of the Internal Revenue Code, as amended, by a majority of members attending at a duly called business meeting.

Why do churches need a dissolution clause?

In simplest terms: It's the law. The assets of a church aren't distributable to the church's members, regardless of whether the church is incorporated or unincorporated.

[Chapter 22 of the Texas Business Organizations Code](#) governs nonprofit corporations. Section 22.001(5) defines a nonprofit corporation as “a corporation no part of the income of which is distributable to a member, director, or officer of the corporation.” Other than a few exceptions, a church cannot liquidate its assets and distribute the money among the remaining members when it ceases to operate.

Similarly, Chapter 252 of the Texas Business Organizations Code governs unincorporated nonprofit associations. Section 252.009 addresses the distribution of personal property of an inactive nonprofit association. It states, in part, “If a nonprofit association is classified under the Internal Revenue Code as a 501(c)(3) organization or is or holds itself out to be established or operating for a charitable, religious, or educational purpose, as defined by Section 501(c)(3), Internal Revenue Code, then any distribution must be made to another nonprofit association or nonprofit corporation with similar charitable, religious, or educational purposes.”

What is the tax benefit of a dissolution clause?

A dissolution clause is necessary for churches that own property to be exempt from ad valorem taxes as well. In Texas, an ad valorem tax is the tax on tangible personal property and real estate. The amount of this tax is calculated based on a percentage of the value of the property as

determined by local appraisal districts. Under [Section 11.20 of the Texas Tax Code](#), “An organization that qualifies as a religious organization as provided by Subsection (c) is entitled to an exemption from taxation of” real and personal property.

Subsection (c) states that to “qualify as a religious organization for the purposes of this section, an organization (whether operated by an individual, as a corporation, or as an association) must ... by charter, bylaw, or other regulation adopted by the organization to govern its affairs direct that on discontinuance of the organization by dissolution or otherwise the assets are to be transferred to this state, the United States, or a charitable, educational, religious, or other similar organization that is qualified as a charitable organization under Section 501(c)(3), Internal Revenue Code of 1954, as amended.”

In other words, **having a dissolution clause is a requirement for a church to be ad valorem tax exempt with regard to the church’s real and personal property.** In fact, the form a church completes when applying for an ad valorem tax exemption requires the church to affirmatively state it has a dissolution statement adopted by “charter, bylaw, or other regulation adopted by the organization.” Filling out this form incorrectly or later removing the dissolution clause could lead to allegations of fraud and the potential for taxes to be retroactively charged on property previously tax-exempt.

What should churches consider when adopting a dissolution clause?

Know where to put it. For an unincorporated church, the simplest solution is to include the clause as a separate paragraph or section in the church bylaws. An incorporated church may either amend its certificate of formation to include a dissolution clause or include it in the bylaws. I

typically recommend to churches that they place the clause in the church bylaws.

Balance specificity and flexibility. Some churches state that upon dissolution, the property will go to a 501(c)(3) organization. This maximizes flexibility for the church, but it does not ensure the property will go to organizations with similar beliefs or a similar mission as the church.

Other churches name the specific organizations that will receive the property. This has the benefit of ensuring church property will go to like-minded organizations upon dissolution—such as a convention, association, or another church or ministry. The drawback is naming a specific organization does not provide as much flexibility should the circumstances of the church or the entity named in the dissolution clause change.

Review it periodically. One of the reasons I encourage the church to place the clause in its bylaws is because churches—hopefully—engage in periodic reviews of the bylaws. Typically, the certificate of formation is not reviewed. Every church should review its dissolution clause from time to time to make certain the clause is up to date and still reflects the requirements of the law and the wishes of the congregation.

Use the process as a discipleship opportunity. While dissolution clauses are legal in nature, they also demonstrate good stewardship of the assets God has entrusted to the local church. Discussing and adopting a dissolution clause provides a wonderful opportunity for church leadership to teach critical lessons about biblical financial stewardship.

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