Summer 2016

Profitable Solutions for Nonprofits

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The nonprofit life cycle

Start-ups face challenges, opportunities

Every organization is different, but most nonprofits follow a somewhat predictable life cycle. And just as they are for a child, the early years for organizations are full of important milestones. A nonprofit's first steps can make the difference between a sustainable organization with the capacity to fulfill its mission and a floundering failure that fades out fast.

Early-stage traits

Nonprofits often begin as an informal group of individuals who see a need for a program or service and feel a personal mandate to help provide it. They boast a high level of motivation, commitment and passion for their vision and usually begin their efforts before they've even considered applying for tax-exempt status or mobilizing support from others. Operations are agile but unstructured. Decision-making is typically done on a consensus basis, perhaps driven by a charismatic leader.

Early-stage nonprofits generally don't have an official board of directors, articles of incorporation or a formal mission statement. Similarly, these organizations generally are without strong internal systems or diverse funding sources.

In fact, there might be some resistance to such formalization. Founders can be reluctant to relinquish their control — or might prefer to focus their energies on their mission of providing programs and services.

The right steps

The incubation period can last for months — or years. But at some point, founders' plans begin to exceed current resources of time, talent and money. Typically, they realize then that, if their organization is to survive and ultimately fulfill its mission, it must take certain steps to formalize governance and develop an infrastructure. This starts with filing articles of incorporation, drafting bylaws, and appointing a board of directors.

The 3 Ws of board development

As nonprofits grow and their boards shift from a collection of passionate early founders focused on operations to a larger, more diverse group tasked with planning and oversight, they should consider using the "3 Ws" approach to board development. The theory calls for selecting board members who possess at least two of these three valuable assets:

Work. Workers can be counted on to reliably and enthusiastically pitch in wherever and whenever needed. They do more than just attend board meetings. They also volunteer, organize events and interact with clients.

Wealth. Those with wealth, or connections to wealth, can generate funds, whether by donating from their own pockets or tapping others.

Wisdom. Wisdom refers to individuals who bring necessary expertise. They may have experience in the nonprofit world or have experienced circumstances similar to those of your constituency. Or they might have expertise in areas that are bound to come up, such as accounting, marketing and the law.

Formulating criteria for continuing programs and services can help create a not-for-profit that's lean and mean, too. As it progresses, your novice organization should begin to track outcomes, with an eye on cutting offerings that aren't working (as painful as that can be). You also might explore collaborative arrangements with other organizations to better serve client needs.

Automation is another key to efficiency. When possible, automate your data management and invest in the technology and equipment to facilitate formalized record keeping and reporting.

Founders or early volunteers are likely to populate the initially small board, and critical decisions should be made by formal votes recorded in written minutes, rather than by casual consensus. As the nonprofit grows, the board will need to move from reacting to events to acting strategically. It should begin to create a formal governance structure, and add members with more diverse backgrounds.

Decisions, decisions

To maximize effectiveness and efficiency, any early-stage organization needs to determine how best to use volunteer help and hire part-time, full-time or contractor staff. Ideally, staffers will be attracted to the job for mission-driven reasons.

Centralized management becomes essential, and you should appoint an executive director. Then craft job descriptions and personnel policies so they're ready to go as your staff expands in coming years. As your organization approaches maturity, it also will need official marketing, fundraising and volunteer management functions.

The financial management priority

Don't underestimate the importance of developing accounting and financial systems. This is particularly true where they're necessary to satisfy compliance requirements. You should institute formal accounting principles and policies, along with adequate internal controls and guidelines for operating reserves.

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Also draw up multiyear budgets (including capital budgets) and development plans that provide for diversified funding streams. If you lack the internal staff to handle such tasks, you can — and should — turn to an outside accounting firm for assistance.

Foundation for success

The ardent, hands-on individuals behind a young nonprofit can sometimes find it hard to work through the seemingly tedious nuts-and-bolts measures associated with establishing a new organization. But taking the time to build a strong foundation will greatly increase your fledgling nonprofit's odds of success. ■

How to score a home run with your board meeting minutes

Minutes of your board's meetings may seem like a mere formality, but they're much more than that. Board meeting minutes reflect on your board of directors and your organization's actions. Savvy nonprofits don't bunt their way through creating these documents — they try to hit them "out of the park."

Here are some best practices for developing minutes that will document your meetings clearly and accurately.

Covering the basics

Meeting minutes should cover such fundamentals as the date and time, whether it was a special or regular meeting, and the names of directors attending as well as names of directors who didn't attend. The minutes should record any board actions (such as motions, votes for and against and resolutions). They also should note whether a quorum was reached, whether any board members left and re-entered the meeting — say, in the case of a possible conflict of interest — and whether there were any abstentions from voting or discussions.

Additionally, minutes should include summaries of key points from reports to the board and of alternatives considered for important decisions. For instance, describe how the board evaluated bids for outsourcing IT work or chose a particular venue for a fundraising event. Another important component: The minutes should record action items — that is, follow-up work that will be needed — and who'll be responsible. Last, all information in the minutes should be presented clearly and succinctly.

There's no particular requirement about how much detail should be recorded in your minutes. But attorneys often advise their clients to include enough information so that they can be offered as evidence that an action was properly taken and that directors fulfilled their fiduciary duties. When in doubt about the depth of detail to include in your minutes, consult your attorney.

Meeting privately

At times, your board likely will meet "behind closed doors" to discuss particularly sensitive or confidential issues, such as a staff dismissal or key person salaries. Details of these sessions shouldn't be included in the board meeting minutes, although a notation should be made that the board moved to an executive session; the notation should provide the general topic of the conversation. Also be aware of your state's Sunshine Laws that may require open meetings and outline exactly what must be documented.

Details of an executive session can be communicated confidentially in some other form. Nonprofit attorneys sometimes advise their clients *not* to label this communication as "minutes."

Generally, your minutes should be ready for inspection by the next board meeting *or* within 60 days of the date of the original meeting, whichever comes first. IRS Form 990 asks whether there is "contemporaneous," or timely, documentation of the board and board committee meetings in minutes or written actions.

Understanding multiple uses

If your organization is ever audited by the IRS, your meeting minutes likely are among the first documents the agency will request to see. Keep in mind that any attachments, exhibits and reports can be considered part of the minutes.

Meeting minutes also can serve as evidence in court. For example, if someone alleges that the board made a hasty decision in cutting a program, board meeting minutes can be used to present the data that was considered when making that decision.

Considering readability

Many not-for-profits today strive for transparency. But your board isn't being open about its transactions if its meeting minutes are so abbreviated that only the keenest insider can understand the full meaning.

The person assigned to take minutes at your organization's board meetings should produce minutes that are a straightforward and complete report of all actions taken and the basis for any decisions. Simple and unambiguous wording works best.

With that goal in mind, it's a good idea to have a second person review the meeting minutes. That person (as well as the original writer) should ask, "Would this report make sense if I hadn't been at the meeting, and had been unfamiliar with the issues addressed? Would I be able to see at a glance the information provided and decisions made?"

Holding up under inspection

Always keep in mind that the minutes of your board's meetings can be viewed by many sets of eyes. Make sure that they show the real score. ■

When investment income counts as UBI

Dividends, interest, rents, annuities and other investment income are generally excluded when calculating unrelated business income tax (UBIT). But tax law provides *two* exceptions where such income will indeed be deemed taxable. And with IRS scrutiny of unrelated business income intensifying these days, nonprofits need to know about these potential pitfalls.

1. Debt-financed property

When a nonprofit incurs debt to acquire an income-producing asset, the portion of the income or gain that's debt-financed is generally taxable unrelated business income (UBI). Such assets are usually real estate — for example, an apartment building with income from rents not related to the nonprofit's mission. But the assets also could be stocks, tangible personal property or other investments purchased with borrowed funds.

Income-producing property is debt-financed if, at any time during the tax year, it had outstanding "acquisition indebtedness" — debt incurred before, during or shortly after the acquisition (or improvement) of property if the indebtedness wouldn't have been incurred but for the acquisition.

Certain property is exempt from this treatment:

Related to exempt purposes. If 85% or more of the use of the property is substantially related to a not-for-profit's exempt purposes, it's not excluded as debt-financed property. Related use can't be solely to support the organization's need for income or its use of the profits.

Used in an unrelated trade or business. To the extent that income from a property is treated as income from an unrelated trade or business, the property isn't considered debt-financed, as the income is already UBI.

Used in certain excluded activities. Debt-financed property doesn't include property used in a trade or business that's excluded from the definition of "unrelated trade or business" either because it's used in research activities or because the activity has a volunteer workforce, is conducted for the convenience of members, or consists of selling donated merchandise.

Covered by the neighborhood land rule. If a not-for-profit acquires real property intending to use it for exempt purposes within 10 years, the property won't be treated as debt-financed property as long as it's in the neighborhood of other property the organization uses for exempt purposes. The latter exception applies only if the intent to demolish any existing structures and use the land for exempt purposes within 10 years isn't abandoned.

2. Income from controlled organizations

Interest, rents, annuities and other investment income aren't excluded from UBI if they are received from a for-profit subsidiary or controlled nonprofit. The payment is included in the parent organization's taxable UBI to the extent it reduces the subsidiary organization's net taxable income or UBI.

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The IRS generally considers a corporation to be "controlled" if the other organization owns more than 50% of the "beneficial interest" — either stock in a for-profit or voting board positions in a nonprofit. For example, if a for-profit leases space from an organization that owns more than 50% of its stock, the lease payments are valid deductions from taxable income. But when these lease payments are received by the controlling nonprofit, they aren't excluded from UBI.

Proceed with caution

Failing to pay UBIT on debt-financed property or income from controlled organizations could have negative consequences, ranging from taxes, penalties and interest to, in extreme cases, the loss of tax-exempt status. Your CPA can help you stay on the right side of the UBIT law. ■

NEWSBITS

Microsoft offers nonprofits free cloud services

Microsoft's philanthropic arm has announced that it'll donate $1 billion in cloud computing resources over the next three years to nonprofits and nongovernmental organizations worldwide. The donation is part of an initiative that includes providing a suite of Microsoft cloud services, expanding access to cloud resources for 900 faculty researchers at universities and reaching 20 underserved communities in 15 countries with broadband connectivity and cloud services.

Microsoft's goal is to serve 70,000 nonprofits through one or more of the offerings in its cloud services suite by the end of 2017. The company will focus on increasing that number in subsequent years. Nonprofits must work through TechSoup (Microsoft's partner in the donation program) to satisfy a variety of eligibility requirements to participate. To determine if your organization is eligible, visit Microsoft's home page and search for "eligibility" to reach the "Microsoft Product Donations" link. ■

Report details volunteerism efforts

According to the annual "Volunteering and Civic Life in America" report issued by the Corporation for National and Community Service and the National Conference on Citizenship, approximately one in four Americans, or 25.3%, volunteered with an organization in 2014 — which has remained relatively constant since the increase reflected after 9/11.

In addition, 62.5% of Americans engaged in informal volunteering in their communities, helping neighbors with tasks such as watching each other's children, shopping or house sitting. Notably, the research also found that volunteers are almost twice as likely to donate to charity as nonvolunteers. Almost 80% of volunteers donated, compared with 40% of nonvolunteers.

Your organization can use information in this report to help fine-tune your volunteer program. To keep your numbers healthy, you also can find out more about your volunteers' skills and interests, and assign them to tasks accordingly. And you can offer incentives for volunteering, such as greater recognition and free admittance to your events. ■

Nonprofits warned about email scam

According to published reports, more than two dozen Virginia organizations, as well as organizations around the country, received emails from an individual in England, unknown to the organizations, offering an approximately $30,000 donation.

Here's how the check-kiting scheme works: After receiving the original email, the nonprofit gets a check for $40,000. Another email arrives concurrently, saying that the overpayment is the result of a clerical error and asking the nonprofit to return the excess payment. A victim nonprofit might deposit the check and not know for several days that it bounced, during which time it might send a $10,000 "refund," money that will never be seen again. ■

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Marketing Your Nonprofit Through Form 990

Are you looking for a creative and free way to market your nonprofit organization, to spread the word about its mission and overall performance? Look no further than your Form 990.

Most nonprofit organizations know the public has access to their 990s. Fewer fully exploit the potential of this form, in which they can share their mission, charitable efforts, and accomplishments, along with other aspects of day-to-day operations. When you carefully and thoughtfully respond to the following parts of the Form 990, your basic annual compliance requirement can be transformed into a far-reaching marketing tool.

Is your organization's mission fully understood by the general public?

Part 1, Line 1 allows you to provide a concise overview of the organization's mission. Because this field is limited, you must be succinct while still encouraging readers to learn more in Part III.

Part III, Line 1 provides you the opportunity to present your mission more fully, communicating its core purpose and focus.

Have you highlighted your organization's efforts and accomplishments?

Part III, Line 4 allows you to brag about your organization's performance by describing its objectives and presenting its measurable accomplishments. In this section, you are required to provide a detailed description of your top three program services by order of expense total, but you may choose to present a narrative for each of your programs in Schedule O.

Who are the key players in your organization?

Part V-A and Part V-B offer opportunities to provide insight into the leadership structure of your organization. Here your readers can learn more about the experience your board brings to the nonprofit's mission. You will also report financial information on board members' compensation, or lack of compensation, which can demonstrate the fiscal responsibility of the nonprofit or its commitment to altruism, depending on the circumstances.

Your Form 990 is an unsung tool that is available for marketing your nonprofit and demonstrating its transparency. For more information on completing Form 990 or our other services to nonprofits, contact LaPorte CPAs & Business Advisors Senior Manager Sean O'Neill at soneill@laporte.com.