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Profitable Solutions for Nonprofits

All charitable deductions aren't created equal

Is board member compensation a good idea?

Make the most of your fundraising by measuring ROI

Newsbits

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All charitable deductions aren't created equal

With the end of the year on the horizon, your supporters may be thinking about making charitable contributions they can deduct on their 2017 federal tax returns. If you want to keep those supporters on your side, though, you need to explain that different types of donations can carry different tax benefits — and some donations aren't deductible at all.

What can — and can't — they deduct?

Generally, donors can deduct contributions of money or property. The amount of the allowable deduction varies based on the type of donation:

Cash. Cash donations are 100% deductible, including donations made by check, credit card or payroll deduction.

Ordinary income property. Donations of this type are generally limited to the donor's tax basis in the property (usually the amount the donor paid for it). Specifically, donors can deduct the property's fair market value less the amount that would be ordinary income or short-term capital gains if they sold the property at fair market value (FMV).

Property is ordinary income property when the donor recognizes ordinary income or short-term capital gains if he or she sold it at FMV on the date of donation. Examples include inventory, donor-created works of art, and capital assets (for example, stocks and bonds) held for one year or less.

Capital gains property. Donors of capital gains property can usually deduct the property's fair market value. Property is considered capital gains property if the donor would have recognized long-term capital gains had he or she sold it at FMV on the donation date. This includes capital assets held more than one year. But there are certain situations where only the donor's tax basis of the property may be deducted, such as when the donation is intellectual property (for instance, a patent or copyright) or, interestingly, "certain taxidermy property."

Tangible personal property. As the name implies, tangible personal property can be seen or touched. Examples include furniture, books, jewelry and paintings. If your nonprofit uses the donated property for its tax-exempt purpose — for example, a museum displays a donated painting — the donor can deduct its fair market value. But if the property is put to an unrelated use — for example, a not-for-profit children's hospital sells the donated painting at its charitable auction — the deduction is limited to the donor's basis in the property.

What other limits apply to charitable deductions?

As you probably know, there's a limit to the amount of charitable deductions a taxpayer can claim in a given year. The taxpayer's total deduction generally can't exceed 50% of his or her adjusted gross income (AGI). (A higher limit applies for certain qualified conservation contributions.) But donations of capital gains property are generally limited to 30% of AGI.

In some cases, the limits are even lower. For example, deductions for contributions to certain private foundations, veterans' organizations, fraternal societies and cemetery organizations are limited to 30% of AGI. And capital gains property contributions to such organizations are limited to 20% of AGI.

Vehicles. Generally, if a vehicle has an FMV greater than $500, the donor can deduct the lesser of the gross proceeds from its sale by the organization or the FMV on the donation date. But if the nonprofit uses the vehicle to carry out its tax-exempt purpose — for instance, an animal welfare organization that uses a donated van to transport rescued dogs and cats — the donor can deduct the FMV. Make sure you provide Form 1098-C, which your donor must attach to his or her tax return to take the deduction.

Use of property. Say a supporter donates a one-week stay at his vacation home for an auction. Unfortunately, he can't take a deduction because generally only donations of the full ownership interest in property are deductible. The right to use property is considered a contribution of less than the donor's entire interest in the property. But there are some situations in which a donor can receive a deduction for a partial-interest donation, such as with a qualified conservation easement.

Donors also might want to claim a deduction for the donation of their services, such as when a hair stylist donates one free haircut and color for your auction, or a graphic designer lays out each issue of your quarterly newsletter for free. These types of donations aren't deductible as contributions, only as normal costs of doing business. But the related out-of-pocket costs, such as supplies and miles driven for charitable purposes (14 cents per mile), are deductible as charitable contributions.

Help donors help you out

Be aware that there are additional limits on charitable deductions. (See "What other limits apply to charitable deductions?" at left.) And proposed tax law changes could affect charitable deductions, though most likely not for 2017. So keep an eye on federal developments in Washington.

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While tax education may seem beyond your responsibility, you can't afford disgruntled donors. Taking the time to make sure your donors understand the tax implications of their gifts can avoid unpleasant surprises down the road, and keep donors on board as long-term supporters. ■

Is board member compensation a good idea?

Overheard in a nonprofit's office: "It's so hard to find good board members. It's going to be really difficult to fill these board openings."

If your organization struggles each time it needs to fill a board vacancy — and doesn't always come up with the candidates it desires — it may be time to consider creating a board compensation program.

Add up the pluses and minuses

Board member compensation comes with several pluses and minuses your nonprofit should consider. Different organizations might assign different weight to each of the factors.

On the plus side, offering compensation could help attract board members with specialized expertise, such as fundraising or a well-regarded community presence. It also could give you an edge when courting potential board members who'd receive generous compensation from for-profit organizations for serving on their boards.

Compensation could be in order, as well, if your board members are expected to invest significant time and effort, or if your nonprofit has a business model that competes with for-profit organizations, such as a nonprofit hospital. In addition, providing compensation can help create an obligation to perform on the board member's part and promote professionalism. This also might:

- Incentivize meeting attendance and accountability,
- Help achieve greater diversity on your board, and
- Make it easier for individuals from different cultures, classes and ages to participate.

Board compensation also comes with several minuses. In general — and this is a big one — *it can look bad*. Donors expect their funds to go to program services, and board compensation represents resources diverted from the organization's mission.

Further, there are IRS and legal implications. The IRS looks carefully at whether any arrangement could create a conflict of interest. And, board members receiving compensation of more than $10,000 aren't independent members of the board by the IRS definition. Reimbursing for expenses under an accountable plan isn't considered compensation for measuring independence. Also, in some states, volunteer board members are protected from legal liability, while compensated members may not be. So you'll need to check on your state's laws.

Launch a compensation program carefully

If you decide to compensate board members, do it correctly. First and foremost, the compensation arrangements must comply with the Internal Revenue Code's private inurement and excess benefit regulations, as well as the IRS rules about "reasonable compensation." Failure to do so can result in steep excise taxes, penalties and even the loss of your organization's tax-exempt status.

Independence is indispensable when setting the amount of, or formula for, board compensation. It should be set by independent directors (who aren't among those to be compensated), or an independent governance or compensation committee, with insight from an independent consultant. The amount should be comparable to that paid by similar nonprofits, as determined

by compensation surveys or other data. Whoever sets the amount should be guided by a formal compensation policy.

The policy should include clear objectives outlining how compensating board members pays off for the organization (for example, by allowing it to attract a member with financial expertise). It should specify which board members are eligible for compensation (the chair, the officers or all members) and how compensation is structured (for instance, flat fee, retainer or per-meeting fee).

The policy also should address expectations for the board members in exchange for their compensation. Expectations can be described, for instance, in terms of number of meetings attended, hours worked or qualifications and experience.

Finally, document, document, document. You'll want written evidence of a formal board vote approving the policy and the compensation amounts, related discussion and copies of the data the board relied on to make the decisions.

Leave no loose ends

Making a shift to a board compensation program is a major change. Your preparation also should include checking to see how other nonprofits with compensation programs handled communicating the change to the public, which can help you develop your own communication plan.

Be sure to seek advice from an attorney who's familiar with laws governing nonprofits in your state. And you may also want to get feedback from supporters and donors before making a final decision. ■

Make the most of your fundraising by measuring ROI

Donors and other stakeholders continue to look for more accountability and transparency from nonprofits, especially regarding fundraising. Not only is the sum of money raised in campaigns meaningful, but how efficiently you're able to raise it, too.

Interested parties look beyond total dollars raised to also consider associated costs in fundraising efforts. *Cost ratios* that present fundraising costs as a percentage of funds raised (also known as *cost-per-dollar*) focus on the expense of fundraising, while *return on investment* (ROI), importantly, focuses on the returns. It makes sense to track both.

Determining ROI vs. cost ratios

The formula for ROI uses the same inputs as the cost ratio but flips them:

ROI = Fundraising revenue / Investment in fundraising (Fundraising expense)

Focusing not only on the big picture but on specific fundraising activities will allow your organization to identify its weaker methods and strategies and improve its overall fundraising performance. Which of your fundraising activities generates the highest return? Once you establish a baseline, you can see where your results are improving and which programs are most effective.

> You must be consistent by measuring your revenues in the same way for each year and campaign.

Some organizations feel it's more meaningful to measure gross revenues raised compared to the fundraising expenses for that effort. However, many follow a more traditional method of measuring ROI using net revenues (revenues minus the related expenses) when comparing to costs. Either way is OK, but you must be consistent by measuring your revenues in the same way for each year and campaign. And remember, these metrics are only meaningful when you compare fundraising activities or trends from one year to prior years.

Calculating the inputs

There are other considerations. How, for instance, do you compute your "fundraising expense"? Although the revenue information is easily available to your development staff, your accounting staff should be recruited to gather data on expenses at the same level of detail by campaign or fundraising effort.

Your fundraising expense should include the direct costs of the initial effort, as well as later efforts. Initial costs might include the investment to create a new donor relationship (for example, online advertising costs or the costs of a phone campaign), while subsequent costs include those associated with maintaining that relationship (for instance, the costs of a renewal mailing).

What about indirect or overhead costs? Be consistent! If you exclude those that you would incur with or without the monitored activity, such as the costs for your website or donor database, make sure they are excluded from every campaign metric. For both costs and revenues, you should use rolling averages that cover three to five years. This will reduce the effect of "one-offs," whether in the form of a significant donation or an economic downturn. You'll also avoid penalizing fundraising activities, such as a major gift campaign, that require some time to show results.

Calculating these metrics will help you make better decisions when it comes to allocating your fundraising resources. But keep in mind that ROIs can vary greatly by activity, and a lower ROI doesn't necessarily mean you should cut the activity. One fundraising expert suggests striking a balance between high-cost, high-potential long-term activities and low-cost, short-term activities.

A win-win scenario

Going to the effort of computing the cost ratios *and* ROIs is a win-win. With this information in hand, you can make more informed decisions *and* satisfy your stakeholders. Your CPA can help you in these efforts. ■

NEWSBITS

Study shows digital revenue on the rise

Online nonprofit revenue in 2016 grew by 14%, and email revenue grew by 15%, according to a new study by nonprofit consultants M+R. Based on input from 133 nonprofits, "Benchmarks 2017" found that Web traffic, email list size, Facebook fans, and Twitter and Instagram followers were all on the rise in 2016, while most individual email metrics were down. For example, the emails opened per number delivered fell 7% overall, for an average just under 15%.

For fundraising messages, the response rate was only 0.05%, an 8% drop from 2015. In other words, a nonprofit had to deliver 2,000 fundraising emails to generate a single donation. For every 1,000 fundraising emails delivered, nonprofits raised $36.

M+R also found that respondents invested more in digital ads last year, increasing their spending — including paid search, display and social media advertising spending — by 69%. Visit the Benchmarks section on mrss.com to see full study results. ■

New positions popping up at NFPs?

Three "top jobs" that nonprofits will need to fulfill their missions in the future have been identified by business magazine *Fast Company*: 1) chief culture officer (CCO), 2) data scientist and 3) user experience (UX) designer.

A CCO manages an organization's relationship with the community, implements internal wellness and health initiatives and devises policies to combat employee burnout, according to the magazine. Data scientists help nonprofits identify trends and critical information that can guide their program and service decisions. And UX designers improve the on- and offline processes that clients use (or don't use) to access a nonprofit's programs and services. ■

Employee retention examined

Recognition, trust and support — both monetary and otherwise — are among the critical factors that make nonprofit employees happy and, thus, create a superior nonprofit employer, according to *The NonProfit Times* "2017 Best Nonprofits To Work For" report. The report ranked DonorsChoose.org as the No. 1 organization.

Among the eight categories considered, the largest disparity overall between organizations that made the "Best Nonprofits" list and those that didn't was found within "pay and benefits" (an 18-point differential) and "leadership and planning" (a 16-point differential). Across the 50 not-for-profits recognized, the key drivers for employees included confidence and trust in the organization's leadership and overall satisfaction with the organization's benefits package.

Another statement where the "Best Nonprofits" diverged from others was "This organization gives enough recognition for work that is well done." About 84% of respondents at the recognized organizations responded positively to that statement, compared to only 66% for nonprofits that didn't make the list. ■

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Historic Preservation Tax Credit Programs

Historic preservation tax credits have encouraged economic development in both Louisiana and Texas. Here is a brief overview of how historic tax credits work and how nonprofits can take advantage of them.

Tax credit options

Both the Louisiana and Texas legislatures have created 25 percent historic preservation tax credit programs as a way to encourage the renovation of historic buildings in designated districts. Combined with the federal 20 percent Historic Rehabilitation Tax Credit Program, these two credits offer economic motivation to restore historic properties for income-generating purposes.

How can these programs help nonprofits?

Nonprofit organizations can get a dollar-for-dollar reduction of federal tax liability for 20 percent of the costs of certified rehabilitation activities to certified historic structures through the Federal Rehabilitation Investment Tax Credit Program. Nonprofits simply need to form a limited liability company (LLC) that would operate the property for a minimum five-year period.

As a nonprofit, you can maintain full control and ownership rights through the LLC. However, you will need to find an investor who has federal tax liability and would participate in the LLC. The tax credits are discounted by approximately 10 percent to attract investors to the project. Your investor basically purchases the tax credits from your organization.

Considerations

If you are considering using these credits for a property you currently own, there are certain restrictions that you will need to review and understand. In thinking about historic preservation tax credits, you should know that projects should generally have a minimum cost of at least $1 million, as it is easier to find tax credit buyers for larger than for smaller projects.

Note to Louisiana nonprofits: The Louisiana 25% historical preservation tax credit program sunsets December 31, 2021. The credit will equal 25 percent of eligible costs and expenses incurred through December 31, 2017; the credit will drop to 20 percent effective January 1, 2018, regardless of the year in which the property is placed in service.

If you are a nonprofit interested in taking advantage of these money-saving programs, contact LaPorte Director Sarah Franatovich, CPA, at sfranatovich@laporte.com for more information on how to qualify for historic preservation credits.