



BOARD LEADERSHIP: Exempt Organizations Accounting and Tax Issues

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Section 1

Financial Basics

Financial Basics

- Why is this Important?
 - You have a legal duty to care for the best interests of the organization
 - You are accountable to charity regulators
 - You may be personally liable for the conduct of the organization

Financial Basics

Staff Job Descriptions

- Chief Financial Officer (CFO)
 - Top-ranking financial position
 - Links financial affairs with organizational strategy
 - Oversees internal financial staff and systems
 - Typically reports to Chief Executive Officer and the Board

Financial Basics

Staff Job Descriptions

- Controller
- Accountant
- Bookkeeper, Clerk
 - Keep original financial records
 - Collect data, record revenues, make expenditures

Financial Basics

Board Job Descriptions

– Treasurer

- Board Member with overall responsibility for financial affairs
- Manages, with the finance committee, the board's review of and action related to the board's financial responsibilities
- Works with the chief executive and the chief financial officer to ensure that appropriate financial reports are made available to the board on a timely basis.
- May be more hands-on in smaller organizations

Financial Basics

Board Committees

- Finance
 - Oversees budgeting, financing, and investment performance
 - Ensures board receives accurate and complete information
 - Anticipates financial problems
- Audit
 - Manages the yearly audit and conflicts between auditors and financial staff
 - Selects an independent auditor

Financial Basics

Auditor

- Sole responsibility — to offer an objective opinion on the reliability of management's financial record keeping
- May also offer routine financial advice

Financial Basics

Principal financial documents

- Annual audited financial statements
- Monthly/Quarterly unaudited financial statements
- Other ad hoc or unique financial reports

Financial Basics

- Audited Financial Statements
 - Independent Auditor's Report
Opinion Letter
 - Statement of Financial Position
Balance Sheet
 - Statement of Activity and Change in Net Assets
Income Statement
Profit & Loss Statement
 - Statement of Functional Expenses
 - Statement of Cash Flow
 - Notes On The Financial Statements
Footnotes
 - Supplementary Information, if needed

Financial Basics

Monthly/Quarterly Unaudited Financial Statements

- Internally prepared
- Current, Timely delivered
- Frequency and detail may vary based on the needs of the Board

Financial Basics

Other Important Financial Reports

- IRS Form 990
- Annual Budget
- Major Financial Commitments
Loans, Purchases, Acquisitions
- Investment Statements And Policies

Section 2

Financial Management Definitions

Financial Management Definitions

Generally Accepted Accounting Principles (GAAP)

- The body of accounting practices and principles that are commonly accepted in the public, private, and nonprofit sectors

Financial Management Definitions

Financial Accounting Standards Board (FASB)

- The accounting industry group that promulgates accounting “rules” and guidance for practitioners

Financial Management Definitions

Accrual Basis

- The practice of recording revenue when earned and expenses when incurred, regardless of when the associated cash is actually received or spent

Cash Basis

- Records cash as it flows in and out of the organization, similar to a checkbook

Financial Management Definitions

Fund Accounting

- Method of accounting and presentation whereby assets and liabilities are grouped according to the purpose for which they are to be used

Financial Management Definitions

Accounts Receivable

- Bills sent to customers for products or services rendered
- Cash has not yet been received
- Appears as an Asset on Balance Sheet

Financial Management Definitions

Accounts Payable

- Invoices received from vendors for products or services purchased
- Cash has not yet been paid
- Appears as a Liability on Balance Sheet

Financial Management Definitions

Prepaid Expenses

- Amounts paid to vendors for products or services not yet received
- Cash has been paid
- Appears as an Asset on Balance Sheet

Financial Management Definitions

Deferred Revenue

- Amounts received from customers for products or services not yet rendered
- Cash has been paid
- Appears as a Liability on Balance Sheet

Financial Management Definitions

Property, Plant, and Equipment

- Buildings
- Furniture
- Computers
- Automobiles
- Leasehold Improvements

Financial Management Definitions

Depreciation

- General - Reducing the value of a fixed asset each month by a preset amount to reflect the presumed reduction in value of that asset
 - Usage, passage of time, wear and tear, obsolescence, depletion, inadequacy, rot, rust, decay
- Accounting - Allocating the expense of an asset across the span of time when that asset is generating revenue
 - Little or no regard for the market value

Financial Management Definitions

Leasehold Improvements

- Construction or improvements for the purpose of preparing the premises for a tenant to conduct business
- Cost is written off over the term of the lease or the period it is expected to be useful

Financial Management Definitions

Liabilities

- Claims against the assets of an organization made by outsiders for services provided and items purchased

Financial Management Definitions

Net Assets

- Resources available for carrying out the organization's objectives after everything else has been paid for
 - Unrestricted
 - Temporarily Restricted
 - Permanently Restricted

Financial Management Definitions

Cost Concept

- The initial value of assets is the sum of the cost of their acquisition
 - Building
 - Land
 - Architect's plans
 - Permits and fees
 - Materials

Financial Management Definitions

Going Concern Principle

- An entity's ability to continue functioning for the foreseeable future
- This assumption is “invisible” — it will only be disclosed when it seems the organization’s existence is threatened

Financial Management Definitions

Materiality

- The importance and significance of an amount, transaction, or discrepancy
- Auditors only address incorrectly recorded items that are above a pre-established level of importance
- FASB has not issued quantitative guidelines

Section 3

The Annual Audit

The Annual Audit

What is an audit?

- A structured examination by an independent, knowledgeable 3rd party
- Performed annually
- Used chiefly by outsiders
 - Funders
 - Lenders
 - Regulators

The Annual Audit

Types of auditor opinions:

- Unqualified (Clean, Unmodified)
- Qualified
- Disclaimed
- Adverse

The Annual Audit

True or False?

- Audits are done to uncover waste, fraud, and abuse
- Auditors review every transaction
- An unqualified opinion means no irregularities have occurred
- Auditors routinely help with accounting for audit clients

The Annual Audit

Who should obtain an audit?

- No requirement for NPO by IRS or SEC
- Public trust and confidence
- State Requirements
- Review
 - Independent analytical review without detailed testing, limited assurance regarding material misstatements and conformity with GAAP
- Compilation
 - The financial statements are the representation of management, no assurance regarding material misstatements and conformity with GAAP

Section 4

Tax Basics

Tax Basics

Tax Exempt Status

- Exemption from Federal Income Tax
- Organized and Operated Exclusively for an Exempt Purpose
- Private Inurement
- Excess Benefits
- Lobbying
- Political Campaign Activities

Tax Basics

Public Charity

- Churches, Schools, Hospitals, Charities supported primarily by donations
- Charities supported primarily by performing program services
- Supporting Organization
- Testing for Public Safety

Private Foundation

Tax Basics

Unrelated Business Income

- Three Part Test
 - Trade or Business
 - Regularly Carried On
 - Unrelated to Exempt Purpose
- Common Exclusions
 - Investment Income
 - Royalties
 - Rental of Real Property

Tax Basics

Examples of Potential UBI

- Advertising
- “Active” Mailing List Rentals
- Debt-Financed Income
 - Rent
 - Investment Income
- Lab Revenue, Pharmacy

Tax Basics

Political Activities

- Must Limit Lobbying to one or two tests
 - Substantial Part
 - Expenditure Test
- Organization Elects which test to use
- Campaign Activities not permitted
- May set-up a related (c)(4) to perform additional lobbying

Tax Basics

Intermediate Sanctions

- Penalty excise taxes on persons who improperly benefited
- Applies only to public charities and social welfare organizations
- Two tiered excise tax
 - Disqualified persons receiving excess benefits
 - Organization managers participating/ approving excess benefit transaction

Tax Basics

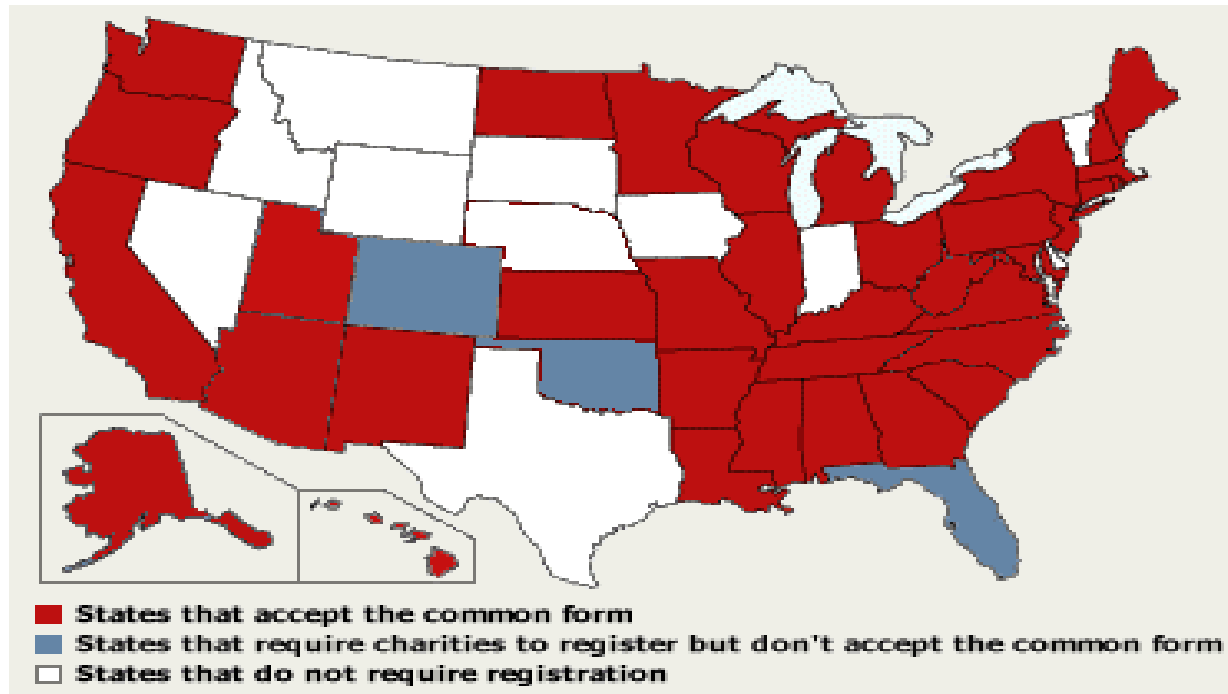
Documented Policies

- Conflicts of Interest Policy
- Presumption of Reasonableness
 - Approved by independent members of Board
 - Reliance on appropriate comparability data
 - Documentation and written substantiation
- Revenue Sharing Transactions
- Whistleblower Protection
- Document Retention and Destruction

Tax Basics

Soliciting

- State Registration



Tax Basics

Soliciting

- Internet Solicitations
 - Charleston Principles
 - Personal jurisdiction
 - Entity specifically targets persons within the state
 - Entity receives repeated, ongoing contributions
 - Email treated the same as direct mail
 - Guidance, not law

Tax Basics

Public Disclosure

- Required
 - Form 1023
 - Previous 3 years Form 990
 - Previous 3 years Form 990-T (501(c)(3) only)
 - Free, or reasonable copy and postage fee
 - “Widely Available” Exception
- Optional
 - Governing Documents
 - Conflict of Interest Policy
 - Financial Statements

Tax Basics

Other Taxes

- State Income/Franchise
- Property
- Payroll
- Unclaimed Property
- Sales and Use
- Withholdings on Raffles

Section 5

Case Study: Children First, Inc.

Case Study

Agenda

- Expansion of Services to Loudon Co.
- Annual Budget Approval
- Committee Reports

Case Study

Mission and Programs

- Consistent with 1023
- Reflected on 990
- Identify new activities
- Identify discontinued activities

Case Study

Income

- Government
- Foundations
- Fee for Service
- Publication Sales
- Fundraising Events
- Annual Community Appeal
- Interest

Case Study

Expenses

- Executive Director
- Consultants (Audit)
- Mortgage
- Equipment
- Travel



DC Cares' Board Leadership Exempt Organizations Accounting and Tax Issues

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