Profitable Solutions For Nonprofits

Passing donor scrutiny with flying colors

New rules affect how your auditor must communicate internal controls issues

Know when to say thanks — and no thanks

Newsbits

PLUS!

Heads up: FASB discussing standards for mergers and acquisitions

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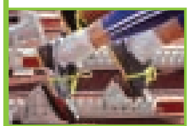
Passing donor scrutiny with flying colors



How do donors view your nonprofit? Do they consider your organization reputable? Do they believe you provide up-to-date and thorough information?

In this day of transparency and accountability, not-for-profits increasingly are providing more details on their funding sources, expenses and financial practices. In fact, this is now the norm for the sector. Let's look at how many not-for-profits are exhibiting their good practices and credibility and see if your organization is making the grade.

Study your nonprofit

Making information available about your finances, operations and governance can be a full-time job that you lack the resources to perform. So you may wonder if your organization is completing tasks in all the right areas. To find out how well donors and the rest of the public think you're doing, take the following test:

1. Is your financial data up to par? To ensure financials are in order and accounting practices are standardized, accountable nonprofits undertake an independent audit annually.

Post pertinent financial information, programs and other key information about your organization and its operations on your Web site.

2. Do you have an audit committee? For many nonprofits, an audit committee is an effective way to oversee financial reporting and internal controls — and, most important, assist the board with the auditing process. Give your audit committee the most current and detailed information by having the appropriate technology in place to track financials, generate financial reports and streamline internal processes. Your financial advisor can help you get started or guide your audit committee to improve processes.

3. Is your staff diligent about accountability? In transparent organizations, every staff member and board member does what's necessary to conduct business transparently and ethically. For example, CFOs file tax

forms and documents on time and provide accurate financial reports, and fund-raisers efficiently maintain donor lists and report funds.

4. Are you a good communicator? Nonprofits should have nothing to hide. Donors and the public will be confident that your organization is trustworthy if you share information and give easy access to it. So post pertinent financial information, programs and other key information about your organization and its operations on your Web site. Also, share information via newsletters, annual reports and press releases.

5. Do you work with watchdog groups? Organizations wanting to promote an honest image regularly provide watchdog groups with information about their not-for-profits. They also respond to all inquiries from rating agencies, such as Charity Navigator, GuideStar and the Better Business Bureau, and the media.

Display your goods with Form 990

Form 990 is a critical accountability tool for your organization. It captures significant information, including your financial status, sources of funding, compensation of staff and board members, and overhead and fund-raising costs. This form, which is required by the IRS, can be requested and viewed by staff members, donors, charity evaluators and the media. So, providing information that's clear, succinct and accurate is essential.

Keep these tips in mind when completing your Form 990:

- Use guidelines to properly classify all expenses as program services, management and general, or fund raising.
- Highlight the mission and work of your nonprofit in the "Statement of Program Service Accomplishments" section.
- Check and double-check for accuracy.
- File on time to avoid penalties.

Your Form 990 may be the best, and only, representative of your organization to the public. Present the information well to help ensure your not-for-profit is viewed positively. You can see for yourself by visiting GuideStar.org — and you can check out other nonprofits there as well.

Research what others are doing

Much of the Sarbanes-Oxley Act (SOX) is not mandatory for nonprofits. But many not-for-profits are consistently adhering to standards set by SOX and have stringently adopted corporate governance reforms, according to *The Impact of Sarbanes-Oxley on Private & Nonprofit Companies*, a survey of 20 nonprofits and 36 for-profit private companies. Other notable findings:

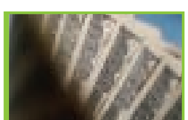
- 84% of respondents said corporate governance reform is "about right," an increase from 78% in 2005.
- Nonprofits continue to self-impose corporate governance standards, but they're strongly influenced by their boards and outside auditors.
- The estimated cost of implementing corporate governance procedures increased 26% — for an average annual price tag of $105,000.

Overall, nonprofits have adopted more aspects of SOX than for-profit companies, implementing or planning to implement whistle-blower procedures, board approval of nonaudit services by auditors and restrictions on executive compensation. One reason for this difference is that not-for-profits typically have more stakeholders they're accountable to than for-profits.

Get top marks

Employing best practices in accountability and transparency can be challenging. But it's necessary to review current procedures and implement new strategies. The payoff can be even greater than getting an A+ from donors and watchdogs: You may be able to better manage your operations and gain greater financial support. ✧

New rules affect how your auditor must communicate internal controls issues



Financial audits can be a complicated process, especially when new auditing standards come down the pike. Last year, the Auditing Standards Board issued Statement on Auditing Standards (SAS) No. 112, *Communicating Internal Control Related Matters Identified in an Audit*, effective for periods ending on or after Dec. 15, 2006. These most recent auditing standards affect how auditors should communicate certain issues related to internal controls over financial reporting that may be identified during a financial statement audit. As a result, you may see an increase in the number of reportable findings during your nonprofit's external financial statement audit.

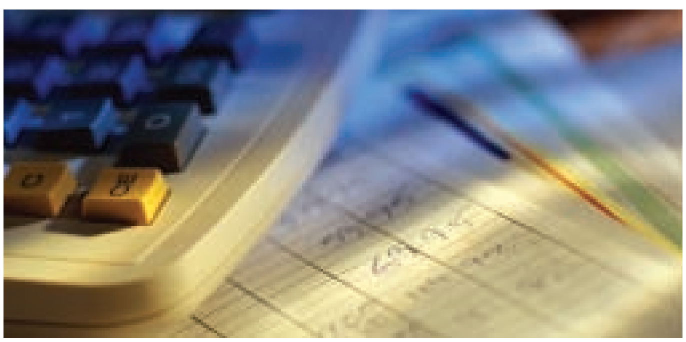
2 types of deficiencies

SAS 112 concentrates on control deficiencies — when the design or operation of a control doesn't allow key staff, in day-to-day operations, to prevent or detect misstatements in a timely manner. Examples of control deficiencies include failing to review and reconcile departmental expenditures, neglecting to obtain proper approval for invoices, depositing cash and reconciling accounts in an untimely manner, and lacking an overdraft funds monitoring system.

There are two types of control deficiencies:

1. Significant deficiency. This is a control deficiency, or combination of control deficiencies, that severely affects your nonprofit's ability to "initiate, authorize, record, process, or report financial data reliably and in accordance with standard accounting principles." These deficiencies prevent you from generating financial data under generally accepted accounting principles to the extent that there's "more than a remote likelihood" that your financial statements will contain a *more-than-inconsequential* misstatement that won't be prevented or detected.

2. Material weakness. This is a significant deficiency, or combination of significant deficiencies, that makes it more than likely that your financial statements will contain a *material* misstatement that won't be prevented or detected.



Where they can occur

SAS 112 provides examples of control deficiencies, significant deficiencies and material weaknesses, which include:

- Inadequate documentation of internal controls components,
- Inadequate design of monitoring controls used to assess the design and operating effectiveness of the entity's internal controls over time, and
- The absence of an internal process to report deficiencies in internal controls to management on a timely basis.

Other instances that SAS 112 considers to be at least significant deficiencies, but that could be material weaknesses, are lack of controls over the period-end financial reporting process, including controls over procedures for the general ledger and adjustments to financial statements, and ineffective oversight of the entity's financial reporting and internal controls by those charged with its governance.

SAS 112 also offers examples of indicators of control deficiencies that typically occur when an auditor finds any restatements of previously issued financial statements that were issued to reflect the correction of a material misstatement or identifies a material misstatement that went previously unidentified by the entity's internal controls. Other indicators are when an auditor learns management, or those charged with governance, has failed to gauge the effect of a previously revealed significant deficiency and to either fix the problem or deem that it will go unfixed.

Assessment

SAS 112 directs auditors on how to evaluate the degree of deficiencies according to:

- Deviations in the design or operation of controls and whether those deviations constitute control deficiencies,
- The severity of control deficiencies based on nature, likelihood and magnitude, and
- Whether misstatements or potential misstatements are more than inconsequential.

If an auditor finds a control deficiency, significant deficiency or material weakness, he or she must notify management or those charged with governance of any significant deficiencies and material weaknesses in writing within 60 days after issuing the audit report.

The effect on your organization

SAS 112 will likely call for additional processing time, more detailed documentation and closer monitoring of your organization's compliance with internal controls, financial reporting and governance — all of which could require time and money. So be sure your key staff and auditing committee are aware of the potential changes.

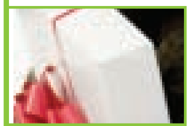
On the other hand, SAS 112 could strengthen your organization's internal systems, and improve its credibility among donors, government agencies, the media and the general public.

Preparing for your next audit

The recent standards changes redefine the audit process because it now requires you and your auditor to anticipate challenges, rather than simply react to those that occur. Although your auditor must remain objective throughout the auditing process, he or she can certainly help you become more familiar with the requirements of SAS 112 and its effect on your nonprofit's financial statement audits. ✧

Know when to say thanks — and no thanks

A gift acceptance policy helps you determine which gifts to accept



If you run a nonprofit, the age-old saying "don't look a gift horse in the mouth" may not be the best policy. Some gifts have restrictions or costs that can bring problems for your organization.

That's why assessing gifts is important. Consider a gift acceptance policy that will help ensure gifts fit with your not-for-profit's mission and values, avoid potential conflicts of interest and are strategically sound and practical.

Deciding what's right for your organization

A gift acceptance policy benefits your organization in a couple of ways. First, it helps you decide which assets and gift forms are appropriate for your nonprofit. For example, a gift that involves additional expenses and maintenance — such as the insurance, docking and storage fees of a boat — could reduce the gift's value significantly and create negative cash flow for your organization. This doesn't include the time and energy this kind of asset requires or the effect, if any, on your reputation. Second, a gift acceptance policy serves as a reminder to your staff and board that gifts can raise financial, tax, publicity and legal issues.

A gift acceptance policy serves as a reminder to your staff and board that gifts can raise financial, tax, publicity and legal issues.

To determine whether you should accept or decline a gift, you must evaluate the appropriateness of the donation and evaluate its potential uses and drawbacks. Many organizations employ a checklist, which includes questions such as:

- Is the gift in line with our principles and values?
- Could the gift create legal problems or threaten our credibility?
- Is the gift financially sound?
- Do the costs of selling or maintaining the gift exceed its potential value?
- Is the gift free from unreasonable and unethical restrictions?

You'll also want your policy to specify review guidelines for each of the different types of gifts you may be offered. After all, a gift of interests in a limited partnership will likely have tax issues that need to be addressed, while a donated painting might require special care and storage that your nonprofit isn't accustomed to. Don't forget an "out" clause. It allows you to decline a gift should a conflict of interest, public relations issue or legal matter occur.

A team effort

Developing and managing your gift acceptance policy is a team effort. It should involve your executive director, planned giving and development directors, accountant and lawyer.

Even if you already have a policy, your organization should have a committee to review gifts, make recommendations to your board and consult with experts — such as valuators and real estate appraisers — as needed. Such a committee is typically made up of board members and staffers who are most familiar with the organization's mission and operations.

Be clear about which fees donors will be responsible for paying when completing gifts.

It's also important to have your board of directors approve your policy and review it annually. Revisiting the policy helps to keep its terms front of mind and allows for changes, such as including or excluding a particular asset or amending the evaluation process.

Helping donors

A gift acceptance policy can be beneficial to donors as well. It leaves no confusion about the kind of assets that you'll accept and that are appropriate for your organization. Be clear about which fees, such as legal and appraisal, donors will be responsible for paying when completing gifts.

Also, recommend that donors meet with a tax advisor before making a gift to determine its compatibility to the organization and the tax impact. And remind them to file the gift with the IRS.

Be informed

If your nonprofit has been operating for years without a gift acceptance policy, you may wonder why you need one now. Developing such a policy can help your organization make an informed decision about the gifts it chooses to accept or decline. More important, it can save you time and money and protect your reputation. ✧

Heads up: FASB discussing standards for mergers and acquisitions

For several years, the Financial Accounting Standards Board (FASB) has been working on changes that will significantly affect how nonprofits treat mergers and acquisitions, including the reporting of goodwill and other intangible assets, such as copyrights, patents and trademarks.

The first exposure draft, *Not-for-Profit Organizations: Mergers and Acquisitions*, intends to improve the accounting and reporting standards for nonprofit mergers and acquisitions by eliminating the use of the pooling-of-interests method of accounting. This method records assets and liabilities at "carryover" amounts, which are the amounts recorded by the acquired organization.

Under the proposal, not-for-profits instead would use the acquisition method, which requires recognizing the assets acquired and liabilities assumed and measuring them at fair value at the acquisition date. Also, organizations would need to identify goodwill as a residual based on the value of the merger's or acquisition's assets or liabilities and provide details so users of the financial statements can evaluate the nature and financial effects of the merger or acquisition.

The other exposure draft, *Not-for-Profit Organizations: Goodwill and Other Intangible Assets Acquired in a Merger or Acquisition*, focuses on the treatment of goodwill and intangible assets recognized as the result of a merger or acquisition.

Financial statements for periods following the combination of two nonprofits would need to provide "consistent and comparable information" about intangible assets and events resulting in impairments of goodwill. The goal is to more accurately reflect the initial and continuing underlying economic value of intangible assets and to provide enhanced disclosures about changes in asset value over time.

Stay tuned for final statements to be issued by FASB.

Newsbits

Are nonprofits living in the technological dark ages?

Electronic payment processing services, such as PayPal, FirePay and NETELLER, provide a means for donors to make charitable donations online. But many nonprofits aren't taking advantage of this benefit because they don't have adequate technology in place. This is according to *Online Technology for Social Change: From Struggle to Strategy*, a 2006 report from dotOrganize that discusses how not-for-profits are using online tools.

DotOrganize, an online technology resource, gathered information from qualitative interviews with 20 organizations, online organizing tools and resources, and a survey, which garnered 378 responses from nonprofits (referred to as "social change groups" in the survey). The report shows that:

- 59% are frustrated or struggling with their current technology, with some being unable to implement basic online tools,
- 39% don't use e-mail newsletters,
- 55% don't keep e-mail lists — and those that do report that their lists have fewer than 1,000 donors,
- 47% don't accept donations online, but
- 95% feel that technology is important.

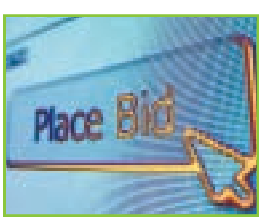
Money, time and lack of staff were cited as obstacles to being able to fully use online tools. To view the report, which recommends how nonprofits can integrate technology, visit www.dotorganize.net. ✧

Employer policy could go up in smoke

Employers that have instituted on-the-job smoking bans are attempting to extend the boundaries beyond the workplace by adopting policies that dictate the behavior of employees when they're off the clock. Armed with at-will employment policies, employers are implementing strategies to control or eliminate workers' use of tobacco — some going as far as to tell staff members they'll be fired if they don't quit smoking. These tactics are being driven by various factors, including increasing health care costs and the desire to improve productivity.

Despite at-will employment policies, some employer attempts at extending smoking bans, beyond what individual states have mandated, are being thwarted by federal and state antidiscrimination statutes. To avoid these problems, take care when implementing nonsmoking policies. For example, be consistent when monitoring staff compliance and investigating complaints of policy violations. It's also key to clearly outline the consequences for policy violations and consistently enforce them — otherwise, your organization may be hit with discrimination claims, or charges of violating federal or state law. ✧

Web site auctions benefit nonprofits



Are you in the market for a 42" LCD television? How about tickets to the World Series? You may bid on these or other items listed at BiddingForGood.com — the proceeds of which benefit the nonprofit hosting the auction. Organizations involved with this fund-raising approach range from elementary schools to the Alzheimer's Association. BiddingforGood.com also provides nonprofits with an online network to share information about their causes with consumers and other not-for-profits. ✧

Link, Murrel & Company

Helping nonprofits fulfill their missions

As a nonprofit executive, you know that operating your organization successfully today is a challenge, to say the least.

You not only have to deal with more intense competition for limited support, you also have to use your resources as efficiently as possible to stay in the black. And of course you have to make sure your organization complies with increasingly complex reporting requirements and regulations — and achieve your goals, too.

This is where Link, Murrel & Company can help. We specialize in helping nonprofits with a full range of accounting, audit, tax, consulting and compliance services.

Our nonprofit clients include a wide range of organizations in the greater Orange County area. Our emphasis on developing proactive, personal and value-added relationships with our clients has helped us build a strong reputation for quality, reliability and performance that exceeds expectations.

Link, Murrel & Company is a proud sponsor of the Volunteer Center of Orange County and supports their mission of being an "essential partner in improving the quality of life in Orange County by connecting community resources, increasing volunteerism, and building professional capacity in nonprofit organizations." The Volunteer Center of Orange County strives to encourage people to become personally involved in making the community a good and welcoming place to live, work, and raise a family. They have developed ways for people to best use their valuable time and talents to help others.

The Volunteer Center of Orange County recently hosted the Inaugural Conference of the Center for Social Enterprise, which provided nonprofit executives, board members and social investors with information about the concept of social enterprises and attempted to increase their awareness and willingness to consider social enterprise strategies for sustainability. The Volunteer Center is dedicated to helping nonprofit organizations generate earned income in support of each organization's mission.

Please visit their website at www.volunteercenter.org.

We hope you enjoy this issue of Profitable Solutions for Nonprofits and that it provides you useful information. Recommendations contained in this newsletter may not be appropriate in certain situations. Before implementing any of the ideas suggested, please contact our office for further inquiry.

We invite you to call Wm. Gary Crouch at (949) 261-1120 to answer any questions you might have about various nonprofit issues or to discuss how we can help your organization meet the challenges facing not-for-profit organizations today.

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