



# NON PROFIT GPS



HELPING TO KEEP YOU ON THE RIGHT ROAD

## Upgrade and Simplify Your Accounting System

For your calendar or fiscal starting in 2018, there will be changes to your financial reporting that will impact how you report net assets, investment income, and liquidity. The changes to your record-keeping system won't be dramatic but, since there will be changes, this may be an opportunity to look into simplifying your accounting system.

One beneficial change would be to have a separate grouping for your indirect costs (the costs that benefit all of your programs). This will help you analyze the total cost of providing services to make sure you are fully funded. If you receive federal funds this will make it much easier to obtain an appropriate indirect cost rate.

Another useful technique is to reduce the number of accounts you use. Keep in mind most accounting systems allow you to drill down to obtain more detail—so why use multiple accounts to create that detail? As you near year-end look at each of your accounts. Any account that doesn't have a relatively large amount of activity is a good candidate for combining with other accounts. For example, for a small or midsize non-profit, any accounting category that doesn't have \$1,000 of expense in it by the end of the year should be challenged.

More accounts lead to more work, confusion and unnecessarily detailed reports that boards often struggle with. A more concise report is easier to read and make judgments about.

What accounting method should you use? There are a few common choices, including: the accrual basis, the cash basis, the modified cash basis, and—rarely but occasionally—the tax basis.

The accrual basis records revenue as it is earned (including contributions as soon as you have an unconditional commitment) and expenses when you receive the product or service.

The cash basis records income when it is received and payments when they are made. The modified cash basis include some modifications of the cash basis. For example: property and equipment may be recorded as assets.

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The tax basis would use the same method used in preparing your form 990 or 990EZ.

Cash basis reports are the simplest, require the least time, and therefore cost the least to prepare. They are most common with very small nonprofits, but they don't tell the whole story.

Several years ago I had an experience with a nonprofit client that was struggling to make payments. Many bills were being paid late, but since the cash basis of accounting was being used, the financial statements didn't reflect this and the Executive Director wasn't aware of this serious and growing problem.

That's one reason why the American Institute of CPAs recommends the accrual basis. Information and, therefore, decisions are better. Additionally, regulatory requirements may call for the accrual basis. The New York State Charities Bureau requires Generally Accepted Accounting Principles (GAAP) which is the accrual basis.

You can get to the accrual basis by using the cash basis throughout the year and making adjustments at year-end but that won't give you all of the tools that you may need for decision-making.

You might also want to check your bylaws. They may specify the method of accounting you are supposed to follow.

Another benefit of the accrual basis is donated supplies and materials and some donated services are recorded which can provide a better picture of the scope of your operations.

2018 is going to be a year of change for nonprofit financial reporting. Make it work to your advantage by thoughtfully organizing and simplifying your accounting system.

## Related Activities Can Result in Unrelated Business Income

Related activities are not unrelated, right? That's true, however, there is a big exception known as the Commerciality Doctrine which says an activity that is substantially related to your exempt purpose may be treated as unrelated if it is conducted in a commercial fashion. Unfortunately there is no clear definition of this Commerciality Doctrine in the Internal Revenue Code or regulations, and IRS has been somewhat inconsistent in applying it.



Situations where it is most likely to be applied include those where the nonprofit has close ties to a for-profit through its leadership including board members or officers.

**The following factors are likely to be present when IRS asserts the Commerciality Doctrine against a nonprofit:**

- Your organization directly competes with for-profits with comparable pricing;
- the activity is profitable;
- advertising and promotion are used in a manner similar to commercial organizations.

The easiest rebuttal to a Commerciality Doctrine challenge is to demonstrate the organization subsidizes rather than profits from the activity.

Although it is not common, you should be aware of the Commerciality Doctrine to avoid unexpected Unrelated Business Income treatment.

## Form 1099-MISC Filing Reminder

Forms 1099 MISC are due by January 31, 2018. They are required to be prepared and submitted if you pay \$600 or more to individuals or unincorporated businesses during calendar year 2017. Unincorporated businesses would include partnerships and limited liability companies including professional limited liability companies like Heveron & Company CPAs PLLC.

There are some exceptions for certain types of payments. Feel free to contact us if you have questions. You can also review instructions for these forms which can be found on page 24 of the general instructions for forms 1099.

Go to [IRS.gov](https://www.irs.gov) and do a search for general instructions for forms 1099s.

## What IRS Has in Store for Nonprofits During 2018

The IRS thinks it's better to be a cop car on the side of the road slowing down a bunch of cars than spend their energy ticketing only one driver. They prefer to readily share their upcoming plans with nonprofits.

Their workplan for 2018 will include checks of payroll reporting and unemployment for charities that are subject. They will also be looking for certain types of unrelated business income. They will also review early retirement incentive plans and look at W-2 and 1099 forms to see if those are properly reported on your form 990.

Additionally, proper reporting of federal unemployment tax in situations where charities are associated with non-charitable nonprofits and backup withholding (federal tax withholding which is required from certain gaming winnings and when contractors do not provide their tax ID) will also be under review.

Their strategy for identifying nonprofits they will target includes analysis of filed 990s, 990PFs, and 990EZs to determine which are most likely to have a noncompliance. They will also select cases based on referrals from inside and outside the IRS. They will be selecting some on a purely random basis (Is that a cop car behind that road sign?).

The IRS will focus on organizations that support other charities and file form 990N, charities that were previously for-profit entities, and organizations which have indicators of potential inappropriate benefits to individuals or non-charitable entities.

Additionally, they will examine some entities that received their exemption by filing form 1023EZ, and those that use the full 1023 to apply for exempt status, but were approved through a streamlined review.

## No More Housing Allowance for Clergy?

Many clergy have recently read that the tax court struck down the clergy housing allowance exclusion because it violates the first amendment. This ruling not only affects active clergy but also retired clergy.

This started with a special interest group called the Freedom from Religion Foundation, and the decision came from a judge who issued a similar ruling in 2013. The judge stated, "The allowance violates the establishment clause because it does not

have a secular purpose or effect and because a reasonable observer would view the statute as an endorsement of religion."

The good news is this didn't occur in our tax district, so at this point it doesn't apply to clergy in New York. The bad news is IRS could conceivably start applying this ruling universally—although experts say that is unlikely.

We will report important developments in future issues, and on our NFPnet.org website.



## How Good Is Your Charity's Reputation?

This is an important question because it can affect the funding you receive and even the future of your organization. The AICPA not-for-profit section has recently provided a list of ways you can monitor your reputation.

### Their recommendations include:

- Google your organization's name and look at the top 10-25 items that come up. Are they what you expected? Are they what you wanted?
- Look at your own website objectively. Is it easy to navigate? Is contact information easy to find? Is your financial and other information current and transparent?
- Consider your risk management, including whether you have proper insurance coverage, whether there are claims against your organization, whether you are complying with laws and regulations and whether you have proper human resource practices.
- Review your social media strategy and policies about what is and isn't acceptable.
- Provide opportunities for your members, clients, volunteers, employees and donors to give feedback to your organization.
- Look at how you are presented by third-party websites like the Better Business Bureau Wise Giving Alliance and Guidestar.
- Set up a news feed service that allows you to monitor the Internet for content about your organization.

An employee or board member can periodically monitor these and other important criteria you have identified. You should have procedures to follow up on any concerns that are disclosed.

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## This month's WebStar Winner is: National Network of Fiscal Sponsors

[www.fiscalsponsors.org](http://www.fiscalsponsors.org)

Although we haven't historically been fans of fiscal sponsorship because of the requirements and risks it poses for the sponsoring organization, we must acknowledge this technique is becoming more common. This means there is a need for proper practices.

Enter the National Network of Fiscal Sponsors (NNFS) to help. This organization grew out of a study of issues and challenges with providing fiscal sponsorship.



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NNFS provides useful information such as best practices for fiscal sponsorship including guidelines for fiscal sponsorship.

Some potential funders are attracted to fiscal sponsorship projects because it allows them to test innovative funding solutions.

This organization addresses the needs of potential funders, too, including a list of 10 questions they should ask grantees who use fiscal sponsors.

They also provide a helpful database of fiscal sponsors by geographic area and service area.