

THE EFFI BARRY TRAINING INSTITUTE

Legal, Financial, and Governance Fundamentals for New Nonprofits

October 16, 2019

Michael Gellman, CPA, CGMA
Fiscal Strategies "4" Nonprofits, LLC

Benjamin Takis
Takis Nonprofit Law PLLC

HealthHIV DC | HEALTH

This program is funded wholly, or in part, by the Government of the District of Columbia, Department of Health, HIV/AIDS, Hepatitis, STI and TB Administration (HAHSTA).

HealthHIV DC | HEALTH

Learning Objectives

You will:

Part I:

- Describe what it means to be a nonprofit corporation and what it means to be a tax-exempt public charity.
- Examine different approaches to forming and structuring a nonprofit Board of Directors and leadership team.

Part II:

- Identify the key components of accounting systems and safeguarding financial assets.
- Compare the basics of internal and external financial reporting to staff, management, board of directors, and other leadership

HealthHIV DC | HEALTH

The Effi Barry Training Institute

WHAT IS IT?

- Regional trainings
- Individualized technical assistance

- Current & prospective HAHSTA grantees
- Community-based organizations

AUDIENCE

HOW?

- Group-level trainings
- Boot camps
- Community forums
- Individual consultation

- Fee-for-Service business process
- Basic HIV service competencies
- Advanced skills in health care systems
- Data and health informatics
- High-impact prevention programs

TOPICS

HealthHIV DC | HEALTH

The Effi Barry Training Institute

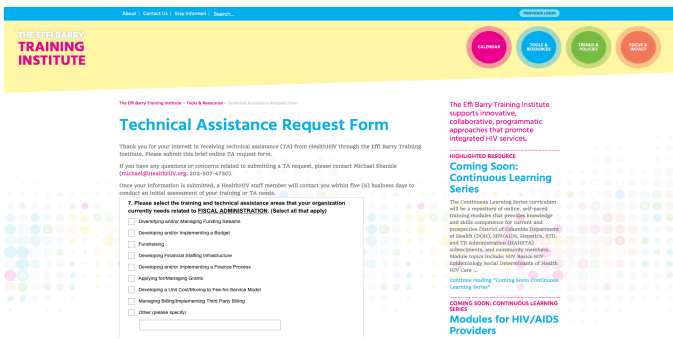


EffiBarryInstitute.org

- Provider Modules & Webinars
- Ryan White HIV/AIDS Program Policies
- Tools & Resources
- Training Calendar



Pulse-Point TA Needs Survey



Technical Assistance Request Form

- Organizational Infrastructure
- Fiscal Administration
- Data Collection, Management, and Reporting
- Service Provision



What is a Nonprofit?

- An entity formed under state law (preferably a corporation)
 - Choosing a state of incorporation: no particular “ideal” state
 - Generally best to incorporate where the organization will be headquartered and operating
 - Changing state of incorporation is a hassle and generally unnecessary
- Does not have owners or shareholders who receive distributions of the “profits”
 - Nonprofits are allowed to make a “profit,” but must use the profits to pursue the mission
- Must comply with the organization’s governing documents
 - Articles of Incorporation
 - Bylaws
 - Policies

HealthHIV DC | HEALTH

What is a Nonprofit?

- Managed by Board of Directors (or Trustees) and Officers, who are subject to fiduciary duties
 - Duty of Care
 - Duty of Loyalty
 - Duty of Obedience
- Directors, Officers, and volunteers are generally protected from personal liability (but not always)
- Subject to certain state reporting and registration rules
- Not necessarily 501 (c) (3) or tax-exempt
 - Many different tax exemptions, e.g. 501(c)(4), 501(c)(6), 501(c)(7)
 - Some nonprofits are taxable

HealthHIV DC | HEALTH

What is a 501(c)(3)?

- 501(c)(3) is a *federal* tax status
 - Generally exempt from federal corporate income tax
 - Generally exempt from state corporate income tax
 - Often (but not always) exempt from state property and sales tax
- Must be granted 501(c)(3) status by the IRS based on the organization's mission, activities, and governing documents
 - Includes education, scientific research, "promotion of health," advancement of religion, providing relief to the poor and distressed or underprivileged, and other categories
 - Must use IRS Form 1023 or Form 1023-EZ
 - No 501(c)(3) status until the IRS approves
 - Can be revoked by the IRS
 - State-level applications may be required

HealthHIV DC | HEALTH

What is a 501(c)(3)?

Supported by a
Wide Variety of
Donors

**Public
Charities**

or

**Private
Foundations**

Supported by a
Handful of Donors

HealthHIV DC | HEALTH

What is a 501(c)(3)?

- Specific benefits and burdens
 - Benefits:
 - Net earnings are tax-exempt
 - Donations can qualify for the charitable deduction
 - Eligible for foundation and government grants
 - Burdens:
 - Finances subject to public scrutiny
 - Possible audit requirements
 - Complicated legal and accounting restrictions
 - Maintaining public charity status

HealthHIV DC | HEALTH

Getting and Keeping 501(c)(3) Status

- Explore alternatives first: fiscal sponsorship
- Required provisions in Articles of Incorporation
 - Organized and operated exclusively for 501(c)(3) purposes
 - At least 3 Directors on the Board at all times
 - Distribution of assets upon dissolution
- Watch for conflicts of interest
 - Inurement
 - Intermediate sanctions
- Having a “501(c)(3) purpose”: three key legal principles
 - The “private benefit rule”
 - The “commerciality doctrine”
 - The “unrelated business income tax”

HealthHIV DC | HEALTH

Form 1023 Tips

- Articles of Incorporation must be certified by the state and have all required provisions
- File no later than 27 months after incorporation
- The narrative:
 - Remember it's not a marketing document or grant proposal
 - Aim for 5 paragraphs and include specific examples of "good" activities
 - Know the hot button issues associated with organizations like yours
- Have a qualified, diverse Board of Directors
- Adopt and attach a conflict of interest policy (and follow it)
- Public charity status
 - Mainly donations/grants: probably "509(a)(1) and 170(b)(1)(A)(vi)"
 - Mainly fees for services: probably "509(a)(2)"

HealthHIV DC | HEALTH

Board of Directors

- Board recruitment and involvement is key
 - Diversity in skills, attributes, and perspectives
 - Expertise with your mission
 - Fundraising means or ability
 - Administrative skills
 - Legal and accounting expertise
 - Community stakeholders
 - Independence (watch for family and business relationships)
 - Clarity of roles (balancing oversight and operational duties)
- Common problems
 - Lack of engagement
 - Unclear expectations
 - Micromanagement

HealthHIV DC | HEALTH

Board of Directors

- Term of Board service (Bylaws)
 - Length of term
 - Removal of Board members
 - Consider term limits
 - Staggering terms
- *Keep records of start and end dates for all Board members*
- Different Board roles to explore (Bylaws)
 - Chairperson
 - “Ex Officio”
 - Non-Voting
 - Executive Committee
 - Advisory Committee
 - Other Committees

HealthHIV DC | HEALTH

Officers and Leadership Team

- Required Officers
 - President
 - Secretary
 - Treasurer
- President vs. Executive Director vs. CEO
 - Authority more important than title
- Authority of Officers
 - When to seek Board approval (a surprisingly difficult question)
 - Financial controls
 - Requiring signature/approval of two officers for certain expenditures
 - Requiring signature/approval of Board/Chairperson for certain expenditures
 - Board authority over appointment and compensation of Officers
 - Officer authority over hiring and compensation of other staff

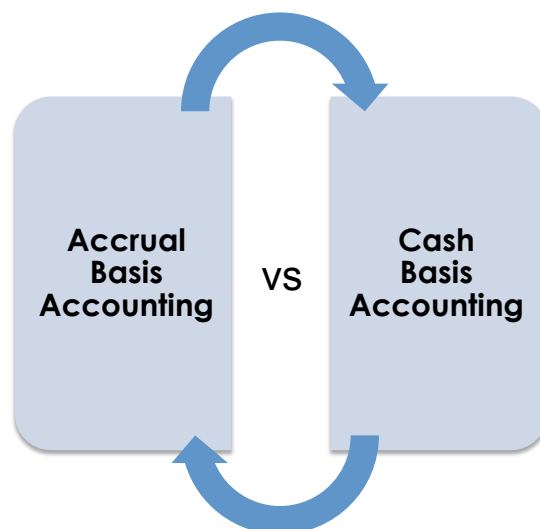
HealthHIV DC | HEALTH

Officers and Leadership Team

- Board members vs. non-Board members as Officers
 - One Model:
 - Board President, Board Secretary, Board Treasurer
 - Executive Director or CEO reports to President; CFO reports to Treasurer
 - Another Model:
 - Board led by Chairperson
 - Non-Board members as President/ED/CEO, Secretary, and Treasurer
- Term of Officer service
 - Interaction with Board terms
 - Interaction with contract rights
- The “outsourced” Executive Director
 - Independent contractor vs. employee
 - Be careful when the Executive Director is an “Officer” under Bylaws

HealthHIV DC | HEALTH

Basic Financial Management



HealthHIV DC | HEALTH

Basic Financial Management

Components of Accounting System and Financial Statements

Assets
Liabilities
Net Assets

Revenue
Expenses

HealthHIV DC | **HEALTH**

Assets

Current Assets

- Cash
- Cash Equivalents
- Investments
- Accounts Receivable
- Pledges Receivable
- Other Receivables
- Prepaid Expenses
- Inventory

Non-Current Assets

- Fixed Assets
- Deposits
- Other Assets

HealthHIV DC | **HEALTH**

Liabilities

Current Liabilities

- Accounts Payable
- Accrued Expenses
- Deferred Income
- Deferred Liabilities
- Grants Payable
- Debt

Non-Current Liabilities

- Accrued Expenses
- Deferred Income
- Deferred Liabilities
- Grants Payable
- Debt

Net Assets

How Different from For-Profits?

- Three Classes – Two Groupings
 - Without Donor Restrictions
 - Unrestricted
 - Undesignated/Designated
 - With Donor Restrictions
 - Temporarily Restricted
 - Permanently Restricted
 - Endowments

Support and Revenue

Support

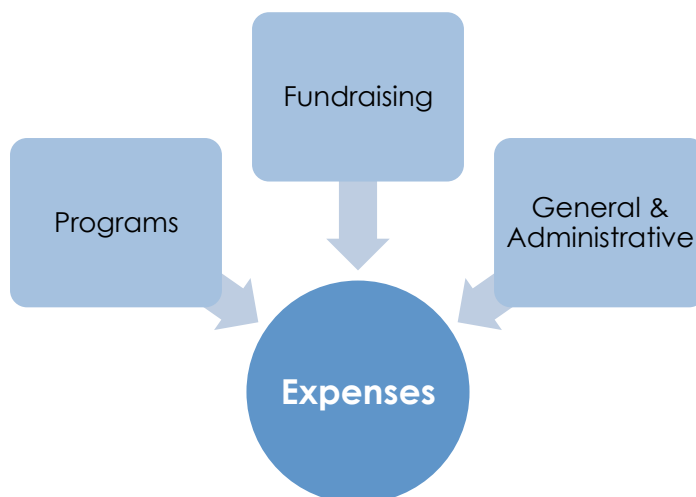
- Contributions
- Grants

Revenue

- Memberships Dues
- Registrations
- Fees for Service
- Publication Sales
- Interest Income
- Miscellaneous

HealthHIV DC | HEALTH

Expenses



HealthHIV DC | HEALTH

Basic Financial Statements

- Statement of **Financial Position**
 - Balance Sheet
 - Point in Time
 - Assets
 - Liabilities
 - Net Assets
 - Reserves

HealthHIV DC | **HEALTH**

Basic Financial Statements

- Statement of **Activity**
 - Income Statement
 - Period of Time (1 to 12 Months)
 - Revenue
 - Expenses
 - Net Assets
 - Net Income
 - » Surplus or Deficit

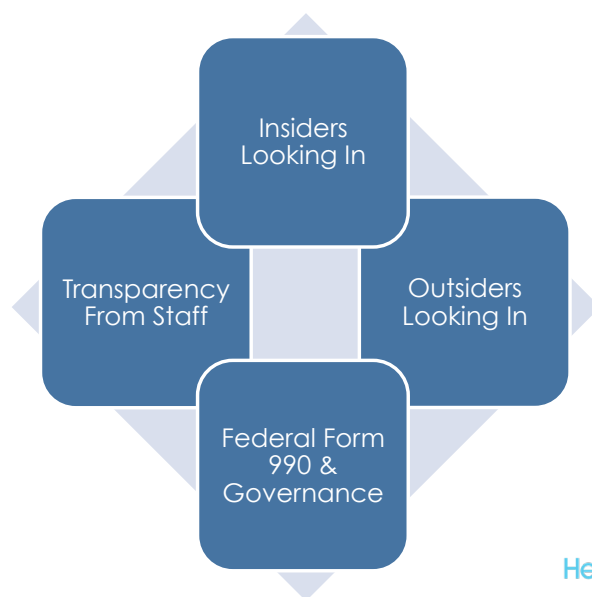
HealthHIV DC | **HEALTH**

Basic Financial Statements

- Statement of **Cash Flows**
 - Period of Time (1 to 12 Months)
 - Require by GAAP
 - Describes Sources and Uses of Cash
 - Operations
 - Investing Activities
 - Financing Activities

HealthHIV DC | **HEALTH**

Financial Accountability



HealthHIV DC | **HEALTH**

First Base: Outsiders Looking In

- Follow Best Practices
- Let Sarbanes-Oxley (SOX) be your Guide
- Do Not Cut Corners
- Transparency

HealthHIV DC | **HEALTH**

First Base: Outsiders Looking In

Five Sarbanes-Oxley (SOX) Guidelines to Consider:

- Create an Audit Committee
 - Whistle Blower Policy
- Publicly Attest to Accuracy of Financial Statements
- Adopt a Code of Ethics
 - Conflict of Interest Policy
- Non-Audit Work by Outside Auditors
- Insider Transactions

HealthHIV DC | **HEALTH**

Second Base: Insiders Looking In

Consider Performing an Annual Financial Check-Up for Board Review:

- Improves Confidence
- Provides for Periodic Oversight
- Enables Fiduciaries to Feel Empowered
- Meets Best Practices
- The Healthy Thing to Do

HealthHIV DC | HEALTH

Second Base: Insiders Looking In

Nonprofit Organization – Financial “Check-Up”

- Related Parties and Other Sensitive Areas
 - Transactions with Related Parties
 - Key Management Compensation
 - Board Approval of Sensitive Transactions
- Internal Controls and Risks
 - Is there a Healthy Attitude about Internal Controls
 - Do we have Adequate Written Financial Policies and Procedures
 - What are the Major Internal Controls in place to Safeguard Cash, Investments and Other Assets
 - Are Assets Protected Against Theft
 - Has the Auditor made Recommendations for Improvements in Internal Controls and have they been Implemented

HealthHIV DC | HEALTH

Second Base: Insiders Looking In

Nonprofit Organization – Financial “Check-Up”

- Internal Controls and Risks (continued)
 - Is at the End of Each Monthly Accounting Period a Budget to Actual Comparison Made and Significant Variances Investigated
 - Are Projections Prepared to Make Sure the Organization is on the Right Course
 - Has Computer Security and Back-up been Reviewed
 - Has Someone Knowledgeable About Nonprofit Taxes Reviewed for Possible Exposure to:
 - UBIT (unrelated business income tax)
 - Private inurement
 - Excess Lobbying/Political Activity
 - Issues Related to Exempt Status
 - Employee vs. Independent Contractor Status

HealthHIV DC | HEALTH

Second Base: Insiders Looking In

Nonprofit Organization – Financial “Check-Up”

- Government Grants and Awards
 - Are you Following OMB Circulars A-110 and A-122
 - Do you have Adequate Time Records
 - Are Adequate Procedures and Controls in Place
 - Have all Reports been Filed Timely
 - Financial Reporting and Audits
 - Have you Arranged to have an Independent Audit
 - Have you Received Clean (unqualified) Audit Reports
 - Does the Auditors have Unrestricted Access to Board and Audit Committee
 - Have All Government Reports (form 990, state filings, etc.) been filed timely

HealthHIV DC | HEALTH

Second Base: Insiders Looking In

Nonprofit Organization – Financial “Check-Up”

- Other
 - Have you Made All Payroll Tax Deposits on a Timely Basis
 - Do you Carry Adequate Insurance
 - Has the Board Adopted a Reserve Policy
 - Has the Board Reviewed and Updated the Investment Policy
 - Has a Code of Ethics been Adopted
 - Has a Whistle Blower Policy been Adopted
 - Has a Knowledgeable Attorney Reviewed Your Activities for Possible Legal Risks
 - Are there any Chapters, Committees, Task Forces Acting on Behalf of the Organization
 - Is there a Board Orientation for New Board Members
 - Are By-Laws and Operating Policies Adhered to and Periodically Reviewed and Updated
 - Have you Analyzed Cash Flows for Possible Problems and Risks

HealthHIV DC | HEALTH

Second Base: Insiders Looking In

Select one sustainability consideration from the Fiscal Sustainability List that you can add to your check list for implementation:

- Item selected: _____
- Discussion: _____

HealthHIV DC | HEALTH

Third Base: Transparency from Staff

- Clear Lines of Communication
- Accounting and Financial Policies and Procedures
- Financial Reporting
- Budgets and Projections
- Strategic Goals Matched to Operating Objectives

Third Base: Transparency from Staff

Accounting and
Financial Policies
and Procedures
Manual Checklist

- Chart of Accounts
- Financial Statements and Management Reports
- Accounting Procedures
- Financial Policies
- Annual Review and Approval

Home Plate: Form 990 and Governance

Governance Policies, Compliance Issues, and Best Practices

- Independence of voting members
- Family or business relationships between the officers, directors, trustees and key employees
- Minutes of meetings
- Board review of Form 990
- Whistleblower policy
- Document retention policy
- Compensation approval process
- Affiliations and joint ventures
- Compliance with other tax filings
- Disclose fraud if occurred
- Annual conflict of interest disclosures
- Document disclosures: financial statements, governing documents and conflict of interest policy

HealthHIV DC | HEALTH

Annual Financial Statement Audits

Annual Financial Statement Audits

- Overview of Why Have Independent Audits
- Key Elements of the Process
- Impacts on Governance
- Outcomes
- Process
- Cost vs. Benefit vs. Compliance
 - Reaching the Decision Point

HealthHIV DC | HEALTH

Budgets

Big Picture Overview of Budgets

- Why so Important
- Role of Staff, Management and the Board
- Key Elements
- Outcomes
- Process
- Impact on
 - Accounting System Design
 - Financial Reporting

HealthHIV DC | HEALTH

Nonprofit Management Learning Series

Register for other sessions in the series:

Session 2: Tax Filing & Responsibilities (**webinar, 10/24 at 12pm**)

Session 3: Board Governance (**webinar, 10/28 at 12pm**)

Session 4: Funding, Support, and Fundraising (**webinar, 10/30 at 12pm**)

Session 5: Sustainability, Common Pitfalls, and Case Studies (**in-person, 11/6**)

HealthHIV DC | HEALTH

Contact

Michelle Rogers
Capacity Building Coordinator

Michelle@HealthHIV.org

202.507.4737

Shayna Linov
Fiscal Health Manager

Shayna@HealthHIV.org

202.507.4739

HealthHIV DC | **HEALTH**