



Financial Accountability

What Nonprofit Boards Need to Know
About Managing Money

The Board of Directors is responsible for the financial integrity of the nonprofit organization

- What must a Director know about nonprofit finances?
- Things we will learn today:
 - ◆ Basics of Nonprofit Finances
 - ◆ Accountability
 - ◆ Best Practices
 - ◆ How to Handle Fraud
- Basic - Intermediate Level



What is Financial Accountability?

The Buck Stops With the Board of Directors

- The Board is responsible for:
 - ◆ Knowing the financial status of the NP
 - ◆ Understanding the financial status
 - ◆ Acting on financial needs of the NP
 - ◆ Preventing financial mishaps
 - ◆ Mitigating financial crisis



Step 1: Financial Oversight

Watch the money - Watch the people



- **Financial Oversight** is the review of both finances and financial practices.
 - ◆ Ensures safe, ethical financial procedures
 - ◆ Protects the Nonprofit and the Directors/Staff
 - ◆ Provides integrity and transparency for the public
 - ◆ Catches financial difficulties before they become impossibilities

What are Financial Reports?

How Complicated Must They Be?

- Basic Reports
 - ◆ Income/Expense
 - ◆ Balance Sheet
- Intermediate Reports
 - ◆ Compilation
 - ◆ Review
- Advanced Reports
 - ◆ Audit
 - ◆ Statement of Financial Position



PROGRESS
REPORT

Basic Reports

Nonprofits < \$25,000/year annual income

■ ***Income/Expense***

- ◆ (aka: Profit & Loss, P&L, Cash Flow)
- ◆ Reports income from all sources, all expenses
- ◆ Include Restricted Funds
- ◆ Should be provided at every board meeting

■ ***Account Balance***

- ◆ (aka: Balance Sheet)
- ◆ Cash account balance
- ◆ Asset balance
- ◆ Should be provided at every board meeting (in some form)
- ◆ Retained Earnings – Accumulated net income from all previous years

Intermediate Reports

Annual Income \$25,000 - \$100,000

■ Same Requirements as Basic -PLUS:

- ◆ Internal Audit Team
- ◆ CPA Review or Audit
- ◆ Some detailed reports
- ◆ Additional Financial procedures
- ◆ IRS 990 EZ (not 990N)
- ◆ New 990 Form requires more information

Advanced Reports

Nonprofits > \$100,000 Annual Income
Also - significant government grants

- All Reports in Basic and Intermediate
- PLUS –
 - ◆ Additional Financial Procedures
 - ◆ IRS 990 required
 - ◆ Full Audit
 - ▶ Financial Information
 - ▶ Financial Management
 - ▶ Assets and Inventory

	PAGE NO.
INDEPENDENT AUDITOR'S REPORT	1
FINANCIAL STATEMENTS--	
Statements of Financial Position	2
Statements of Activities	3
Statements of Cash Flows	4
Notes to Financial Statements	5-10
INDEPENDENT AUDITOR'S REPORT ON THE SUPPLEMENTARY INFORMATION	11
SUPPLEMENTARY INFORMATION--	
Schedule of Functional Expenses.....	12

Step 2: Budgets!

Important Tool to Managing Finances



- *Why are Budgets important?*
 - ◆ Nonprofits try to do as much as possible with limited resources
 - ◆ Budgets help measure success (or failure) of projects
 - ◆ Budgets can track progress over time
 - ◆ Budgets help with internal planning and control
 - ◆ Grant applications require budgets
 - ◆ Budgets catch problems early



Budgets

What About Reserves?

- **“Reserves”** – An amount set aside by the Board to be used in case of losses or an unexpected expense.
 - ◆ Can be budgeted (Rainy Day Fund)
 - ◆ Should balance need for reserves with expectations of constituents and service to mission
 - ◆ Cannot include “restricted” or “special use” funds
 - ◆ Amount to reserve depends on the Nonprofit

Step 3: Nonprofits and Taxes

Why should Nonprofits worry about taxes?

- IRS Reporting Requirements
 - ◆ < \$25K – 990N
 - ◆ >\$25K – 990 EZ or 990
- State Reporting Requirements
 - ◆ NP-20 – Attach copy of 990, if one is filed
- Sometimes, taxes must be paid
 - ◆ “Unrelated Business Income Tax” (UBIT)
 - ◆ Gambling Revenue
 - ◆ Employment taxes
- Penalty for failure to report –
 - ◆ LOSS of nonprofit status!



IRS 990-N

Nonprofits < \$25,000/year annual income

- **Required for ALL Small Nonprofits**
 - ◆ Due May 15 or 5+15 after fiscal year end
 - ◆ IRS will automatically revoke nonprofit status 3 years + 30 days of non-filing
 - ◆ IRS “at risk” nonprofit list on IRS website
 - ◆ Extension to 10/15/10 this year ONLY

Information copy. Do not send to IRS.

<p>Form 990-N Department of the Treasury Internal Revenue Service</p>	<p style="text-align: center;">Electronic Notice (e-Postcard) for Tax-Exempt Organizations not Required To File Form 990 or 990-EZ</p>	<p>OMB No. 1545-2085</p> <hr/> <p style="font-size: 24pt; font-weight: bold;">2009</p> <p>Open to Public Inspection</p>
<hr/> <p>A For the 2009 calendar year, or tax year beginning 1/1/2009, and ending 12/31/2009.</p> <hr/>		
<p>B Check if applicable</p> <p><input type="checkbox"/> Terminated, Out of Business</p> <p><input checked="" type="checkbox"/> Gross receipts are normally \$25,000 or less</p>	<p>C Name of organization: _____ d/b/a: _____ _____ _____</p>	<p>D Employer Identification Number _____ _____</p>
<p>E Website: _____ _____</p>	<p>F Name of Principal Officer: _____ _____ _____</p>	

Privacy Act and Paperwork Reduction Act Notice. We ask for the information on this form to carry out the Internal Revenue laws of the United States. You are required to give us the information. We need it to ensure that you are complying with these laws.

The organization is not required to provide the information requested on a form that is subject to the Paperwork Reduction Act unless the form displays a valid OMB control number. Books or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law. The rules governing the confidentiality of the Form 990-N is covered in Code section 6104.

The time needed to complete and file this form and related schedules will vary depending on individual circumstances. The estimated average times is 15 minutes.

Note: This image is provided for your records only. Do NOT mail this page to the IRS. The IRS will not accept this filing via paper. You must file your Form 990-N (e-Postcard) electronically.

This Form 990-N (e-Postcard) was accepted by the IRS on 5/18/2010.

IRS 990 (EZ)

Information Return Required for Nonprofits

- 990EZ or 990 required of all nonprofits with gross receipts \$25K or more
 - ◆ Watch “floating 3-year average” rule, which requires a 990 EZ or 990 for ALL years where the average gross receipts are \$25K or more
- Due May 15 or 5+15 after fiscal year end
- Extensions may be granted for six months
- Compliance form - financial information required plus proof of nonprofit compliance.

IRS Compliance Check

Failure to File Proper Forms = Loss of NP Status



- 2010 marks the push for nonprofit compliance with IRS reporting
- Any nonprofit that has failed to file the proper paperwork within the past three (3) years risks automatic revocation of status
- One-time extension to October 15, 2010
- Is YOUR charity at risk?
 - ◆ <http://www.irs.gov/charities/article/0,,id=225889,00.html>

Step 4: Directors & Officers Insurance

Protecting Board and Key Staff

- D&O Insurance

- ◆ Breach of Duty
- ◆ Wrongful Acts
- ◆ Mismanagement

- What it does

- ◆ **Provides legal defense**
- ◆ Pay claims

- What it doesn't do

- ◆ Normal liability claims
- ◆ Criminal acts

**Read
the
Policy!**

D&O Insurance

Common Myths

- *My homeowners insurance will cover it*
 - ◆ Many homeowners' policies specifically EXCLUDE nonprofit board service

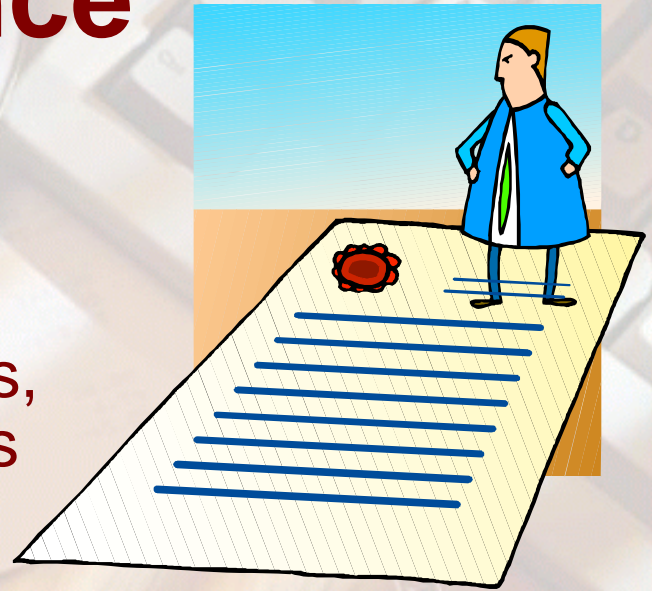
- *I'm protected by law*
 - ◆ There is State protection for volunteer boards, but it can cost \$\$ to prove it

- *We're a nonprofit - We'll never be sued*
 - ◆ You've got to be kidding!

D&O Insurance

Types of Claims

- Board “wrongful acts”
 - ◆ Board Decisions regarding policies, programs, distribution of donations
- Employee issues
 - ◆ Misconduct
 - ◆ Sexual (or other) harassment
 - ◆ Wrongful termination (or failure to hire)
 - ◆ Criminal conduct by employees
- Mishandling funds
 - ◆ Negligence
 - ◆ Deliberate (versus criminal)



Step 5: Accountability

More than Dollars and Sense (Cents)

- Financial Policies

- ◆ Handling money
- ◆ Recording money
- ◆ Reporting money

- Financial Controls

- ◆ Deposits
- ◆ Checks
- ◆ Documentation

- Audit-Review Process

- ◆ Internal Team
- ◆ External (independent)



Nonprofit Financial “Best Practices”

Compliance, Competence and Confidence

- Practice clear, decisive financial governance
- Adopt Ethics and Conflict of Interest Policies
- Implement Financial Controls
- Engage regular, independent financial review
- Promote transparency of Reporting
- Develop a Risk Management Plan
- Know emerging nonprofit financial issues

Clear, Decisive Governance

Best Practices for Conduct

- Proper policies in place
- Review all financial documents
- Procedures to verify data
- Safeguard Nonprofit assets
- Compliance with legal and tax reporting



Ethics/Conflict of Interest

Best Practices for Integrity



- *Conflict of Interest Policy*
 - ◆ Signed by Board and Staff annually
 - ◆ Practiced openly
 - ◆ Transparency critical to credibility!
- *Ethics*
 - ◆ Newspaper Headline Test
 - ◆ Appearance of Impropriety

Financial Controls

Best Practices for Management



- GAAP Standards
- Financial Procedures Manual
- Restrictions documented and honored
 - ◆ Donor restrictions
 - ◆ Grant requirements
 - ◆ Commingling Funds
- Training program for Staff and Board
- Document Retention Policy

Independent Review

Best Practices for Accountability

- Internal Audit Team
 - ◆ Board Members
 - ◆ “Friends of Nonprofit”
 - ◆ Report to Treasurer, Board
- External Audit
 - ◆ Independent review of books
 - Does not also provide bookkeeping
 - ◆ Independent review of practices
 - ◆ Notes issues with methods
 - ◆ Suggests reforms



Transparency of Reporting

Best Practices for Public Access

- Audited Financial Statements
- IRS Tax returns
- State Reporting



Risk Management Plan

Best Practices to Prevent Financial Crisis

- Identifies risk
- Ranks risk
- Identifies policies
- Implements protections
- Provides procedures in event of crisis



Risk Management Plan

Types of “Risk” to “Manage”

- **People** -- board members, volunteers, employees, clients, donors, the public.
- **Property** -- buildings, facilities, equipment, materials, copyrights, trademarks.
- **Income** -- sales, grants, contributions, sponsors, fund raising
- **Goodwill** -- reputation, stature in the community, and the ability to raise funds and appeal to prospective volunteers

Risk Management Plan

Managing the “People” Risk

- Poor economy has resulted in an increase in criminal conduct against nonprofits
 - ◆ Embezzlement by employees
 - ◆ Embezzlement by officers
 - ◆ Fraud from “outsiders”

- Phrase of the Day – “Trust But Verify”

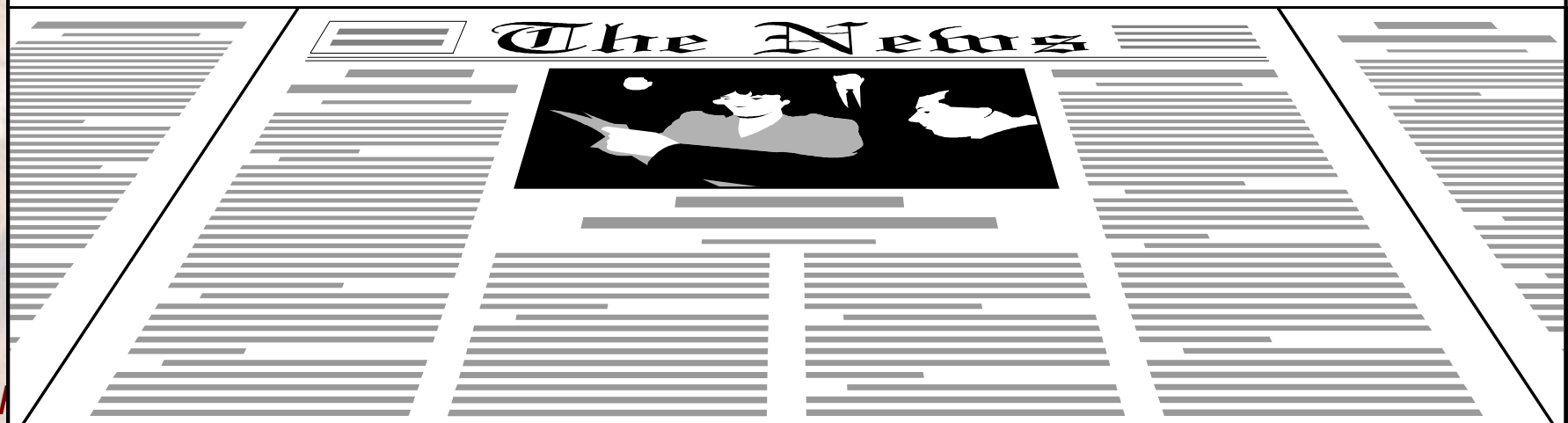
Nonprofit Headlines

INDYSTAR.COM

December 31, 2008

Penrod Society, host of annual art fair, robbed of \$380,000

Society, known for annual fair at IMA, says theft jeopardizes grants for local art groups



Nonprofit Headlines

More on Charity Embezzlement From Chronicle of Philanthropy

- November 11, 2009 – (KY) Woman Ordered to Repay Charity in Embezzlement Case
- November 6, 2009 – (KY) Youth Group Did Not Notice Missing Money
- May 7, 2010 – (MS) Museum Ex-Finance Chief Admits \$1.3M Theft
- May 13, 2010 – (MS) Former Hospital Executive Charged with Embezzling Funds
- June 23, 2010 – (NY) Bronx Nonprofit Leader Gets 10 Months for Embezzlement

Preventing Fraud

Tips to Protect Your Nonprofit Against Fraud

- Have and use financial control policies
- Know who handles the money
- Remove temptation
- Review financial information
 - ◆ ALSO - have independent review of finances
- Be aware that it can happen to your nonprofit!

Nonprofits and Fraud

What You DO When It Happens To YOU

■ *If you suspect fraud...Act immediately*

- ◆ Lock-down data
- ◆ Start a formal audit process with outside auditor
- ◆ Change procedures and rotate staff responsibilities

■ *If you verify fraud*

- ◆ All of the above, PLUS
- ◆ Confront the perpetrator (employee, officer, outside contractor)
- ◆ Copy and compile evidence in a separate, protected and confidential file
- ◆ Contact the police, if appropriate

PR for Nonprofits

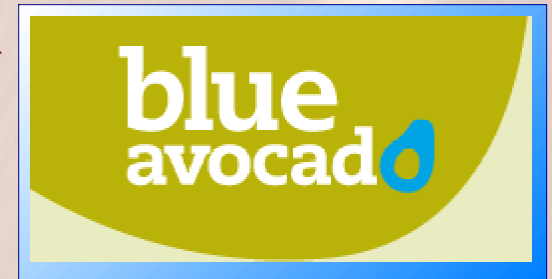
Public Relations During Crisis of Nonprofit Fraud

- **If Fraud or embezzlement finds your Nonprofit**, how the public hears about and perceives the incident can drastically affect the nonprofit's ability to move beyond the event.
- **DO NOT HIDE** or Minimize the seriousness of the event
 - ◆ If you are contacted by the press, answer! - if you don't get your story out, no one will, and speculation will replace facts
- **Have a plan of action for response**
 - ◆ If employee: suspension, termination
 - ◆ If board member: resignation, removal
 - ◆ Note appearance of impropriety is enough to take action for a board member, but more evidence is needed to take action against an employee

For More Reading

Articles About Nonprofit Fraud and Options

- Blue Avocado – www.blueavocado.org
 - ◆ “Our Executive Director is Embezzling”
 - ◆ “Treasurer’s of All-Volunteer Organizations – Eight Key Responsibilities
 - ◆ “Five Internal Controls for Very Small Nonprofits”
 - ◆ “Nonprofit Embezzlement: More Common and More Preventable Than You Think



Know Emerging Nonprofit Issues

Best Practices to Staying Current

- Subscribe to Nonprofit forums
 - ◆ Board Source, INRN workshops
- Listen to your stakeholders
 - ◆ What concerns affect them?
- Listen to your professionals
 - ◆ Attorney, CPA



A Word About SOX

Sarbanes-Oxley Act and Nonprofits

- History of SOX
- Nonprofits (voluntary) adoption
 - ◆ Greater threshold of accountability
 - ◆ More formal review structure
 - ▶ Internal Controls
 - ▶ Internal Audit Team
 - ▶ Procedures, Policies in place
 - ▶ FOLLOW procedures and policies
- SOX and the future of Nonprofits



Financial Accountability

Managing Nonprofit Finances

- *Nuts-and-bolts*
 - ◆ Financial Statements, P&L, Balance Sheet
 - ◆ Reporting requirements - State and Fed
- *Philosophy of effective financial governance*
 - ◆ Financial Policies
 - ◆ Financial Procedures
 - ◆ Risk Management Policy
 - ◆ Board and Staff Conduct Policy
 - ◆ 10 Financial Priorities for Nonprofits
 - ◆ 10 Ways to Catch Fraud (and Mistakes) from Outside the Nonprofit
 - ◆ 15 Ways to Minimize Employee Fraud

Things You Should Do Today

Confirm that your NP is in compliance

- Make sure STATE status is current
 - ◆ www.in.gov/sos – follow the link to corporations
- Confirm that IRS status is current
 - ◆ <http://www.irs.gov/charities/article/0,,id=225889,00.html> (Sorted by State)



Effective Financial Oversight

Managing Nonprofit Finances



ACHIEVE SUCCESS!

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