NONPROFIT NAVIGATOR

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ABOUT US

Our not-for-profit niche at Henry & Horne, LLP was officially formed 28 years ago, but we have been serving the not-for-profit community since we opened our doors in 1957. We are dedicated to Arizona's nonprofit community, and as a local firm with such a long history, we truly understand what is important to our nonprofit clients. Our team members receive quality continuing education specifically in non-profit topics and are continually researching various nonprofit issues, which results in a very broad level of nonprofit expertise.

HENRY & HORNE, LLP
Certified Public Accountants

Executive Compensation
How a Nonprofit Can Protect Itself

By Colette Kamps, CPA

Executive compensation is a hot button for the IRS and an area they are more inclined to inquire about if the Form 990 reports high numbers for the compensation of top management officials. If any individual receives $150K or more in total compensation, that information is required to be reported on Schedule J of the Form 990. If a tax exempt entity completes Schedule J and is audited, it is very likely that the IRS agent will ask for documentation showing comparability data used to determine executive compensation. The IRS is looking for the possibility of the executive compensation being excessive. The basic rule is that the compensation should not be more than the value of the services being provided in exchange for that compensation. If the compensation is determined to be "excessive", the IRS could label this an excess benefit transaction, subject to a substantial tax on the individual and any officials who participated in the determination of that compensation.

So how does an organization protect itself to ensure that proper documentation is maintained to prove the compensation is not excessive? The following conditions should be met:

(1) The Board of Directors should approve the executive compensation in advance of it being paid.
(2) Rely on comparability data.
(3) Document (and maintain documentation) for #1 and #2.

In performing the above 3 steps, any other types of benefits provided to the individual being compensated (such as the right to use property and benefits or other privileges) should also be included as part of the overall compensation when the assessment of reasonableness is made.

There are various ways to obtain comparability data including reviewing the Forms 990 of other similar organizations (similar in size, geographical area, etc.), hiring a consultant to compile comparability data, reviewing salary surveys, or comparing to another employment offer for that individual (at the time he/she is first hired). The IRS requires that sufficient information is available to those determining the compensation, and that those making the determination have the knowledge and expertise to be able to make that determination of reasonableness. So what does this mean exactly? Here is an example: In a case where the board members of a tax exempt hospital consulted a national salary survey specifically for hospital executives, the IRS felt that the Board did not rely on appropriate comparability data because the survey did not divide the data by hospital size and the board members did not have any particular expertise in hospital compensation issues. Also, in a recent IRS project relating to compensation at colleges and universities, the IRS concluded that approximately 20% of the schools did not have adequate comparability data. The lesson to learn from these examples is that the comparability data must be detailed enough to truly be comparable.

There is a "safe harbor" that allows smaller organizations to meet the requirement for adequate comparability with less detailed information. For those smaller organizations (with annual revenues of less than $1M), they only need compensation information for similar services for 3 comparable organizations in the same or similar communities.

If you have any questions Colette can be reached at (480) 839-4900 or ColetteK@hhcpa.com.

COORDINATES

According to The Chronicle of Philanthropy, a recent study found that social causes drove almost 30% of all crowdfunding activity.

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Form 1023-EZ (only 3 pages long) was posted to the IRS website on July 1. Most organizations with gross receipts of $50,000 or less are eligible to complete this form as their application for tax exempt status, versus the much longer Form 1023.

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The Phoenix Business Journal recently reported that St. Mary's Food Bank Alliance was the No. 1 nonprofit organization in Phoenix, AZ, based on budget size.

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According to an article published by GuideStar, a GrantStation study revealed that 95% of the nonprofit respondents do not use any grant industry benchmarks to compare their grant seeking performance with external standards.

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Donated Services from Related Affiliates

By Sharlynn Garza, CPA

In April 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-06. This ASU was released to clarify the guidance related to contributed services received from related non-profit and for-profit affiliates. Most non-profits know the general rule when recognizing donated services from non-related donors, however there were differing views as to whether or not a non-profit entity should record donated services received from personnel of a related affiliate.

Some non-profit organizations took the stance that since the donated service was coming from a related affiliate, the service received is not a contribution. This stance is based on how the term "contribution" is defined. A contribution by definition is "an unconditional transfer of cash or other assets to an entity in a voluntary nonreciprocal transfer by another entity acting other than as an owner." Some organizations concluded that the donated services received do not strictly meet the definition of a contribution as there is generally an arrangement or agreement between the entity receiving the benefits and the entity providing the service, and therefore the services provided are not voluntary and not nonreciprocal.

This ASU clarifies that all non-profit entities should recognize services received from personnel of related affiliates that directly benefit the organization. According to this ASU, the services received should be measured at the cost recognized by the related affiliate. However, consideration should be given to the value of the services received. If it is determined by the non-profit organization receiving the benefits that actual costs incurred by the related affiliate are significantly more or less than the actual value of the services, then the non-profit entity may elect to recognize the services received at the cost recognized by the affiliate or at the fair value.

This ASU, effective for fiscal years beginning after June 15, 2014, will help reduce the differences in accounting treatment found with these types of transactions. It will also provide a true picture of the resources needed to operate the non-profit organization, as well as the resources available to the non-profit organization, which is important in understanding how the organization was able to accomplish its mission. The ASU does not provide for any additional disclosure requirements related to this update. Currently, non-profit organizations are required to disclose details of any related party transactions and the recognition of donated services from related affiliates would fall under these present requirements. It is important to note that if the donated services received from related affiliates are significant, then consideration should be given as to whether the policy for recognizing and measuring these donated services from related affiliates should be included as an accounting policy disclosure as well.

If you have any questions Sharlynn can be reached at (480) 839-4900 or SharlynnG@hhcpa.com.