Behind the scenes

Getting a closer look at Child Crisis Arizona with CEO, Torrie Taj

Contribution clarification reminder

Functional expenses + how you allocate them

Single audit: how do auditors determine which grant to test?

Nonprofits prohibited from lobbying?
Our vision of safe kids and strong families encompasses the hope that all children are in a safe place and that we continue to build strong families.

Nonprofits are a vital part of the community, especially during the COVID-19 pandemic. We sat down with Torrie Taj, CEO of Child Crisis Arizona to talk about her organization’s mission, goals and challenges.

What is the mission of Child Crisis AZ?
The mission has always been to prevent abuse and neglect through strengthening families. Our vision of safe kids and strong families encompasses the hope that all children are in a safe place and that we continue to build strong families.

Have you found a COVID silver lining?
We have found several. One that comes to mind is our Family Education program which is designed to prevent child abuse and neglect. When COVID hit, we were able to pivot in-person classes to online and reach even more parents throughout the entire state and anywhere. This change helped us check off something that has been on our wish list...providing free education and opportunities online for those who couldn’t participate in the past due to transportation barriers.

What unique challenges does your organization have and how have you overcome them?
We have children living in at-risk families in our early education programs who lack basic resources to an even greater extent now. Parents’ jobs were downsized or eliminated and these families were struggling with food insecurity. We immediately began a curbside meal pick-up daily for breakfast and lunch. In addition, we began a new service for a prepared dinner entitled Thankful Thursdays. Many of our families don’t have access to a kitchen 24/7 so on Thursdays we provide a warm meal for the entire family which helps eliminate the stress of where their next meal will come from. It’s a win-win because we are also helping local restaurants at a time when their businesses are suffering.

Have you been able to sustain fundraising?
We are very thankful and fortunate for our community partners who provided emergency funding. We communicate frequently with our donors to ensure they were still operating and providing services for vulnerable children. During this critical time, we are so grateful that individuals in Arizona have continued their sustaining support through the Arizona Qualified Foster Care tax credits.

What are your goals for the future?
That is an easy one...to continue our strategic growth. The pandemic showed us we constantly need to be growing and evolving our services.

What is a best practice that you swear by?
First, nonprofit is just a tax status, NOT a way to operate. The age old best practice of 90 days operational cash-on-hand is no longer enough. We need to be sustainable businesses for our community and COVID revealed how prepared we all were. The PPP was wonderful, but we must still focus on building infrastructure level strength to be sustainable. Because we have been forward thinking as an agency with a Board approved growth plan, we were even able to add staff positions this past year. Another best practice we had in place was our crisis communication plan. It was helpful knowing who was making the decisions that needed to be made and who was the spokesperson.

What do you know now?
Partnerships are key! Collaborating with food banks, businesses, restaurants, donors and other non-profits provided impact. We needed teamwork this past year and my team is an important part of the success of running the organization. I am fortunate that I learned early on to surround myself with the brightest and most innovative people. This is how we will ultimately change lives for the better at Child Crisis Arizona.

Beth Hawley is the Communications Coordinator at Henry+Horne. She can be reached at BethH@hhcpa.com.
You may have heard the phrase functional expenses thrown around, and now I am here to help clarify what that means. First, to understand functional expenses for nonprofit organizations it is important to understand the difference between functional expenses and natural expenses. A natural expense category breaks out expenses by their expense type. This could include salaries and wages, rent, utilities, office supplies, repairs and maintenance, depreciation or information technology.

Now that we know what a natural expense category is, we can cover functional expenses. Functional expenses break out those natural expenses and show which portion is related to a certain “function”. Another way to look at it is allocating each natural expense based on what type of activity the expense is used for. Different activity types are programs, management and general, and fundraising. Program expenses include any costs incurred relating to the programs and services provided by the non-profit organization relating to the organization’s mission. Management and general expenses include supporting costs that do not relate directly to the organization’s mission. This can include costs for management, accounting, budgeting, and so on. Fundraising would include any costs used for soliciting contributions or grants.

Expenses can be either direct or indirect. Direct costs should be allocated directly to the functional category and indirect costs allocated based on some form of a reasonable allocation methodology. The two most common methodologies would be square footage allocation and employee time. Depending on the natural expense type, you would want to use the methodology that would be the most appropriate.

Square footage allocation is typically used for items such as building depreciation, rent, and utilities. To use this methodology, the organization will need to know the square footage of their physical locations and determine which areas relate to the corresponding function. Employee time can be based on employee headcount or time study to determine the amount of time each employee spends on a certain function. After salaries has been allocated, this same allocation can be applied to other natural expenses such as payroll tax and employee benefits. These allocation methodologies should be evaluated each year to make sure that they are still applicable and have been updated for any organizational changes.

It is important to remember these allocation methodologies are not limited to the natural expenses listed above and these are not the only methodologies available to your organization. When deciding how to allocate you will want to make sure you are making the choices best suited for your organization and that the reasoning behind those decisions is supported.

For more of the latest insights on not-for-profit accounting issues, head to our website [www.hhcpa.com](http://www.hhcpa.com) and check out The 501 S(c)ene blog.

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Lobbying. What exactly is it? Lobbying is defined by the IRS as activities that attempt to influence legislation. This includes contacting or encouraging others to contact members and/or employees of the legislature for the purpose of supporting, opposing or proposing legislation or advocating for or against legislation. The IRS does allow a tax-exempt 501(c)(3) organization to incur some lobbying expenses. However, if it is considered substantial the organization could be at risk of losing its tax-exempt status. Unfortunately, the IRS does not give a clear-cut definition of how much lobbying is too much or excessive. It states that lobbying cannot constitute a substantial portion of the organization’s overall activities. This is known as the substantial part test.

Why is this important? If the IRS determines that, in any taxable year, an organization conducted excessive lobbying (lobbying that is a substantial portion of the organization’s overall activities) the organization may lose its tax-exempt status and all its income may become subject to tax. Additionally, an excise tax equal to 5% of the lobbying costs incurred for the tax year may be assessed, and the IRS may also impose a tax on the organization’s management.

There is an election that organizations can make which would allow the use of an expenditure test under Section 501(h). This election enables the use of an alternative to the substantial part test mentioned above and provides a means for measuring lobbying activity based on the size of the organization and the lobbying expenditures for the tax year. This method allows organizations to calculate the maximum amount of lobbying costs they can incur per year without jeopardizing their tax-exempt status. Lobbying under the expenditure test may not exceed $1,000,000 in any tax year.

Under the Section 501(h) election if an organization has excess lobbying activities in one year it is subject to an excise tax equal to 25% of the dollar amount of the excess. An organization may lose its tax-exempt status if it engages in excessive lobbying over a four-year period.

A Form 5768 must be filed to elect the expenditure test. The election remains effective for all subsequent tax years unless revoked by the organization.

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Contribution Clarification

By Colette Kamps, CPA

In our last newsletter, we gave you a “contributions refresher”. Here we dig deeper into one aspect of recording contribution income to provide you with a “contributions reminder”.

In June 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2018-08, Not-for-Profit Entities—Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made. The ASU clarifies and improves guidance for contributions received and contributions made by clarifying whether to account for transactions as contributions or exchange transactions. The ASU is effective for nonpublic companies for annual reporting periods after December 15, 2019. Although this ASU came out back in 2018, this can still be a confusing issue.

When it comes to non-profits, determining whether funding is actually a contribution or exchange transaction can get a bit tricky. ASU No. 2018-08 was issued to help make the determination between a contribution and exchange transaction a bit more black and white and not so grey.

The first question you might have is why does the determination between contribution and exchange transaction matter? The answer is that contributions are accounted for differently than exchange transactions when recognizing revenue.

Contributions are defined by the FASB as “nonreciprocal transfers of cash or noncash items, as well as promises to give.” In other words, if a person or organization decides to give cash or a noncash item to a nonprofit organization without receiving any sort of benefit, the transaction is considered a contribution.

Exchange transactions are defined by the FASB as “reciprocal transfers in which each party receives and sacrifices approximately commensurate value”. What this means is if Organization A provides cash to nonprofit Organization B and Organization A receives a benefit (such as a service) equal in value to the amount of cash given to nonprofit Organization B, the transaction is considered an exchange transaction as both organizations are benefiting from the transaction.

This is not always clear, as sometimes Organization A may provide funding to nonprofit Organization B where A does not receive the benefit directly, but instead the general public receives the benefit. In this scenario, since Organization A is not directly receiving a benefit, the funding would be a contribution (possibly restricted for a specific purpose or possibly conditional).

The clues as to whether the funded amount is an exchange transaction versus a contribution are in the wording of the grant agreement, so it is very important to read these agreements carefully in making the determination.

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Your nonprofit leaders

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About Henry+Horne’s nonprofit team

Charities and nonprofit organizations need the same kind of sound business advice as for-profit organizations because your success depends on more than just maintaining your tax exempt status. Our nonprofit accounting specialists offer all of the financial services your organization needs to operate smoothly so you can focus on what matters most – making a difference in the communities you serve.

Our nonprofit group is a well-known leader in CPA services for nonprofit organizations in Arizona. They work exclusively with the nonprofit industry and receive CPE customized to your needs. They volunteer on boards and committees for local charities, so they see the challenges you face first-hand and can provide valuable feedback and recommendations.

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