nonprofit agendas

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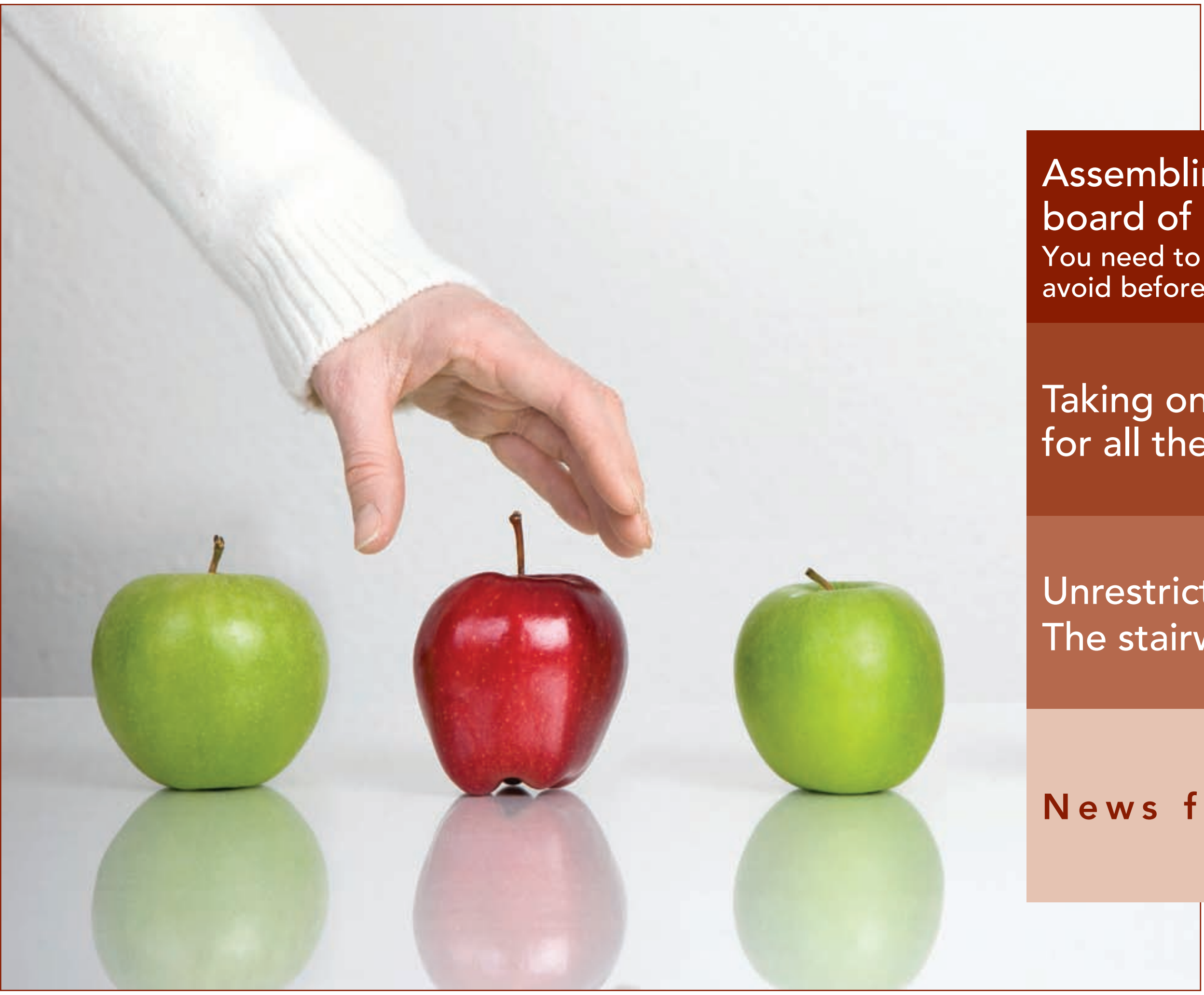


Assembling a *bad* board of directors
You need to know what to avoid before you can succeed

Taking on debt for all the right reasons

Unrestricted funds: The stairway to flexibility

News for Nonprofits

Sassetti
CERTIFIED PUBLIC ACCOUNTANTS

Sassetti LLC

6611 W. North Avenue
Oak Park, IL 60302
708-386-1433
www.sassetti.com

Assembling a *bad* board of directors

You need to know what to avoid before you can succeed

The conventional way to discuss what to look for when you select board members is to focus on positive traits and desirable skills. But in order to put together a strong board of directors that will steer your not-for-profit to great things, you also need to foresee what characteristics might create problems — or render your board imbalanced, improperly motivated or ineffective.

With that in mind, here's a look at four things you shouldn't do when selecting board members and why avoiding these moves is important to your organization's well-being. Keep these tips in mind as you interview potential board members and vet referrals.

1. Don't choose overly dominant personalities. Nonprofits often look for successful, sometimes highly visible, leaders in their community, and many of these individuals have strong personalities. That's fine. Just be careful that you don't get an outspoken "my way or the highway" individual to whom other board members feel they always must defer.

To be effective, board members must work as a team as they determine strategic direction, establish policy, provide fiduciary oversight and so on. Board members need to know how to compromise and provide mutual support — in other words, there's no room for superegos. You can promote teamwork by holding special events outside of the boardroom, such as mixers, workshops and retreats where board members can get to know and respect one another.

2. Don't select all followers. Conversely, some nonprofits gravitate toward individuals who they perceive, consciously or not, will "go with the program." But every board needs strong leadership ability, vision and foresight. Board members also need to act independently from staff and management. And there's not much room for wallflowers when key responsibilities include an active role in fundraising, recruiting and promoting the organization's programs.

Nonprofits also need board members who will take their fiduciary responsibilities seriously and are willing to speak up — and blow

whistles — if they see wrongdoing. Moreover, they must be brave advocates of your mission as they carry your banner within, and perhaps outside, the community.

3. Don't end up with opportunists. Another bad choice is an individual who looks at the organization only for what it might do for him (or her) personally or professionally. For example, consider the bank vice president whose interest in the organization doesn't exceed getting your nonprofit's business, which is clearly a conflict of interest.

Board members are pieces of a larger puzzle, and everyone should bring something to the game. As the organization eyes potential board candidates, it should have particular skill sets in mind, such as financial expertise, HR background, business leadership skills and so on. Board members should complement, rather than echo, one another in their strengths and experience — and be dedicated to putting the organization first.

4. Don't throw them into the mix without direction. Some nonprofits are so caught up in day-to-day operations that they fail to take time to properly offer new board members insight into the structure of their organization and its culture. Make sure you present a brief history of your nonprofit and introduce staff as part of the orientation process.

New members will benefit from formal training in governance, fiduciary duties, financial oversight, organizational assessment, fundraising and other topics that are particular to your organization and its mission. A specialist in nonprofit board member training can help facilitate your program. ❋

Taking on debt for all the right reasons

Did your parents teach you to never buy anything on credit — or at least try? Avoiding debt is almost always good advice. But borrowing money can be a smart solution if it's used for the right reasons. Sometimes it might even catapult an organization from a tough financial situation.

IS BORROWING NECESSARY?

Emergencies and unforeseen problems happen. Roofs leak, donors pull away, fundraisers are canceled — and sometimes it may be weeks or months before you receive grant money. A loan can be a quick source of cash to handle such unanticipated situations.

There also are times when an organization just needs to stabilize its cash flow. Frequently, nonprofits must bridge the gap between a project's startup and its ongoing program revenues.

Other not-for-profits need funds at different times of the calendar year than their funders' grant schedules dictate. Still others need a line of credit to have a steady source of cash between billing and collection. Borrowing for short periods to stabilize cash flow can help keep your organization running smoothly.

WHEN DOES BORROWING MAKE SENSE?

A capital purchase is another situation when borrowing money may be justified. Say that your copier breaks down or you've outgrown your office or warehouse space. Taking on a loan for "big ticket" capital purchases provides an immediate source of cash that can be repaid over time. It avoids the time and cost involved in writing and waiting for a grant, and it keeps you from depleting your carefully built cash reserves.

A not-for-profit occasionally needs to take advantage of an opportunity. A local food pantry, for example, has an opportunity to start a hot lunch program and will receive funding based upon the number of meals served.

But to meet health department requirements, the pantry must purchase a commercial stove. This could be an opportunity of a lifetime that could expand the organization's income and diversify its services. But if there's no time for grant proposals and your group doesn't have the money in its savings account, financing can make it all possible.

WHERE CAN YOU FIND LOAN MONEY?

Banks are still the primary source of loans for nonprofits, so it's always a good idea to build a relationship with a banker who understands your industry. And in larger banks you're apt to find associates who specialize in services to nonprofits.

But you may be able to find a low- or even no-interest short-term loan program somewhere other than a bank. Some community-based foundations provide funds that allow not-for-profits to continue operating until they receive contract monies. The Cash Flow Loan Program, created in 1976 by the Fund for the City of New York, is the granddaddy of them all, but there are many others.

HOW CAN YOU SECURE A LOAN?

Applying for a loan doesn't require any more time or skills than writing a grant or contract proposal. In fact, it may be easier. But you must demonstrate your ability to repay.

First, apply at the right time: Your chances to negotiate are better when you're in a position of financial strength. Consider establishing a line of credit with a local bank when you *don't* need to draw on the funds.

> *A capital purchase is a situation when borrowing money may be justified. Taking on a loan for a "big ticket" purchase provides an immediate source of cash that can be repaid over time.*

When talking to the banker, be specific about how the loan will be used. Thoroughly describe the proposed project, your readiness to launch the project and its timing. Be prepared to specify the amount you need to borrow and the date you'll need the loan.

WHAT WILL YOU NEED TO PROVIDE?

Come prepared for your meeting with the lender. Be ready to present your organization's budget, a current and accurate statement of financial position, prior statements of activities, cash flow projections, and an annual report if you have one. And keep in mind that lenders want to know who your executives and board members are so they can judge the management strength of your not-for-profit.

To protect their interests, banks may expect you to secure the loan with collateral, which is generally based on contracts and accounts receivable. But they also may require assets such as unencumbered real estate, automobiles or equipment. You might need to produce cash collateral from board members, supporters or constituents — who place an amount of money into a special interest-bearing account, which is pledged to the bank. Another scenario: Instead of collateral, the bank may ask you to have a co-signer or guarantor of the loan.

BE CAREFUL

Borrowing money should only be considered in the right circumstances. But, if you believe it's the correct step for your nonprofit, examine interest rates and loan terms carefully before jumping in. ❋

Unrestricted funds: The stairway to flexibility

The Greater Anytown All-Needs Association is in trouble. Individual, corporate and state funding has dwindled in recent years. And the 501(c)(3) organization doesn't know where the money will come from to pay its bills — and its staff — next month.

Greater Anytown has over $2 million in endowments, but all of these funds' earnings are earmarked for food and shelter programs. And a recent bequest of $450,000 is restricted for funding educational activities for the next 10 years. What a pickle the 20-year-old nonprofit has found itself in!

WANTED: FUNDING WITHOUT STRINGS

The above example is fictitious and, with responsible planning, could likely be avoided. But it illustrates an elementary point: Charitable organizations need cash to carry out their daily operations. And having an adequate and steady stream of funds *without strings attached* — also known as "unrestricted funds" — is the best way to keep a charity's operations and programs strong and sustainable.

Unlike temporarily or permanently restricted funds (see "Know your funding" on page 6), unrestricted funds can be used to cover the cost of operating expenses, such as rent, utilities, salaries and other day-to-day expenses. The grants and individual donations a nonprofit receives for general operating support allow it to refocus its efforts from raising funds to improving its programs and responding to emerging community needs.

Know your funding

As a 501(c)(3) nonprofit, your organization likely receives a mix of contributions it can use in different ways. Decide from the onset what type of funds you want to solicit — and what types you're willing to accept. Here are three categories to consider:

Unrestricted funds are free of donor stipulations. Nonprofits need an adequate and steady supply of unrestricted funds to meet ongoing operating expenses and unanticipated costs. *Board-designated funds* are included in this category because they aren't restricted by the donor. Although the board has decided to use these funds for a certain purpose, it can "undesignate" the funds at a future date.

Temporarily restricted funds are subject to donor-imposed stipulations that can be removed with the passing of time or when spent for the purpose intended by the donor.

Permanently restricted funds, often called endowments, are subject to lasting donor stipulations, which mandate that the funds be "held in perpetuity." The *earnings* can be used for a specific purpose or to support operations.

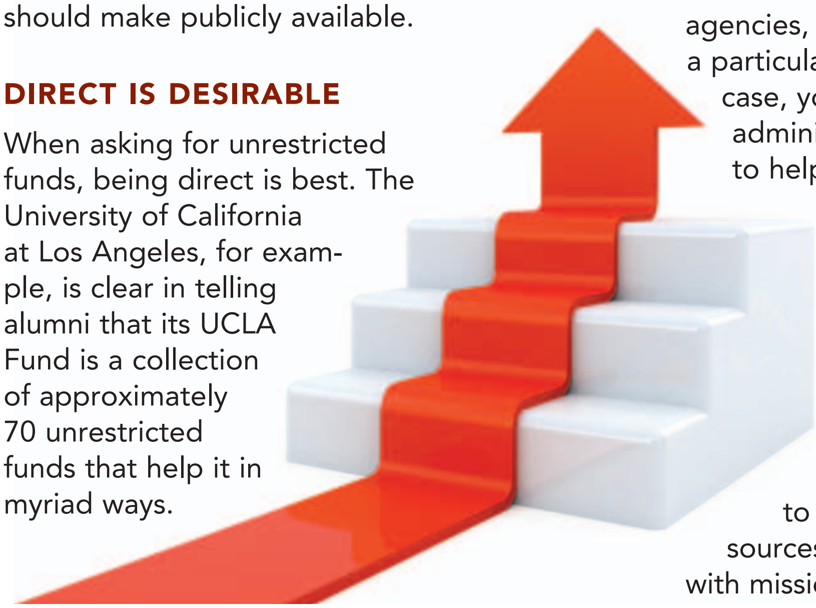
NOT ALWAYS AN EASY TASK

Before an organization sets out to solicit unrestricted funds from individual and corporate donors, it should understand what it's up against: There's a public sensitivity toward nonprofits that spend too much money on administrative costs and too little on programs that fulfill their mission.

To secure funds without restrictions, prove to donors that you'll use their money wisely. One way to do that is by presenting a healthy program service expense ratio and results-focused information on your Form 990, which you should make publicly available.

DIRECT IS DESIRABLE

When asking for unrestricted funds, being direct is best. The University of California at Los Angeles, for example, is clear in telling alumni that its UCLA Fund is a collection of approximately 70 unrestricted funds that help it in myriad ways.



Also explain in your fundraising materials how unrestricted gifts offer greater flexibility than restricted gifts and how they help ensure you have adequate funds to keep the doors open. Moreover, encourage donors to make multiyear commitments for unrestricted gifts.

Ask funders to designate their donations "as unrestricted funds that help the organization." You also might consider naming a fund after a family or individuals who only give unrestricted funds. It might just help encourage contributions of this type.

Sometimes grantors, such as government agencies, require that funds be restricted to a particular program or function. If that's the case, you may still be able to factor in an administrative component of, say, 8%–10% to help cover operational costs.

WIDEN YOUR NET

Even with unrestricted funds, make sure you're involving a variety of funding sources. If one large source of unrestricted funding dries up, for example, you'll still have a number of other sources to draw from. Look for and identify new sources each year that fund organizations with missions on a par with yours. ❋

ATRA gives contributors incentives and disincentives

Thanks to the American Taxpayer Relief Act of 2012 (ATRA), taxpayers have some new and renewed incentives to make charitable donations in 2013 and beyond. Unfortunately, in some cases ATRA brings *dis*incentives.

DONATION DEDUCTIONS MAY BE WORTH MORE — OR LESS

Higher-income taxpayers now may have the incentive of a potentially larger tax benefit from their charitable contributions because of the increase in the top marginal tax rate from 35% in 2012 to 39.6% in 2013. The higher rate applies to taxable incomes exceeding $450,000 (married taxpayers filing jointly), $400,000 (singles) and $425,000 (heads of households). Under the 35% rate, the tax savings from a $1,000 deduction was $350, whereas under the 39.6% rate, the savings may be as high as $396.

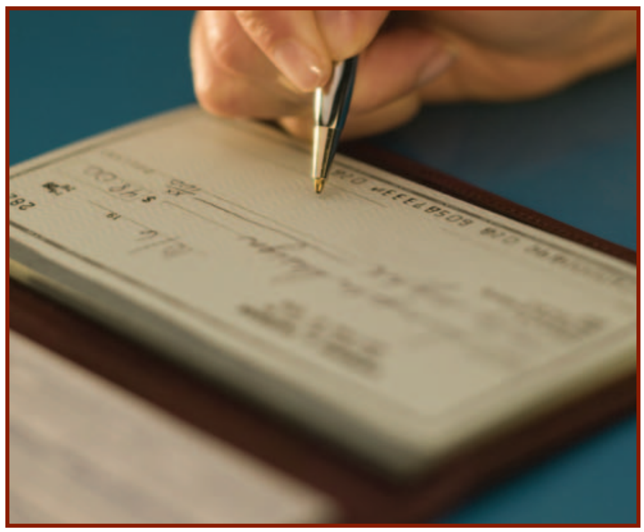
But in many cases, this incentive may be counteracted by the *dis*incentive of the 2013 return of the itemized deduction phaseout.

The phaseout goes into effect when adjusted gross income (AGI) is greater than $300,000 per married couple, $250,000 for singles and $275,000 for heads of households. It reduces certain itemized deductions, including those for charitable donations, by 3% of the excess over the threshold.

Let's say that a married couple with AGI of $1 million makes a donation to your nonprofit. The phaseout would be $700,000 ($1 million - $300,000) × 3%, or $21,000.

If the couple's itemized deductions subject to the phaseout are $100,000, their deduction will be limited to $79,000. At the 39.6% rate, this saves $31,284 in taxes ($79,000 × 39.6%). This is a smaller benefit than if they'd had the same deductions in 2012, when the top rate was 35% but no income phaseout applied, because their tax savings would have been $35,000 ($100,000 × 35%).

But some taxpayers may see a larger tax benefit despite the phaseout. Let's say our couple has the same $1 million AGI, but their itemized deductions are $300,000. After the phaseout, their deductions total $279,000 ($300,000 - $21,000), for tax savings of $110,484 ($279,000 × 39.6%). In 2012, the tax savings would have been only $105,000 ($300,000 × 35%).



MORE TO LIKE THAN NOT

ATRA extends through 2013 the ability of taxpayers age 70½ or older to make tax-free distributions up to $100,000 from an IRA directly to a charity. And by setting a permanent estate tax rate of 40% and an exemption amount of $5 million (annually indexed for inflation), ATRA allows for more informed discussions about planned giving with your donors as they draft estate plans. So, overall, ATRA should be good news for charitable organizations seeking to boost donations. ❋

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ABOUT SASSETTI LLC

Our firm was originally founded by Frank L. Sassetti in 1921. For more than 90 years, the firm has provided creative and proactive tax, accounting and audit services to its diverse client base.

Today, Sassetti LLC's clients consist of a broad range of family-owned businesses, SEC regulated companies, employee benefit plans and not-for-profit organizations. Our goal is to maximize business effectiveness and cost-efficiency, and to help clients understand the ever-changing complex accounting and tax rules.

Our staff of 25 experienced professionals strive to understand your needs, propose solutions and deliver timely and cost effective products.

EXPERIENCE COUNTS

For more information on how we can help your organization, contact Jeff Schroeder at **(708) 386-1433** or email **Schroeder@sassetti.com**. We look forward to speaking with you!!