nonprofit agendas

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News for Nonprofits

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Getting off on the right foot

Merger transitions set the stage for a successful alliance

When two nonprofits merge — as in any alliance that blends two staffs and sets of operations — challenges arise. But knowing what you're up against, and where the pitfalls lie, is half the battle.

ALLIANCES ABOUND

Mergers continue to dot the nonprofit landscape as organizations team up to share resources and expenses, or to avoid a duplication of services in their communities. But a merger won't automatically result in improved economic strength.

Many mergers fail to achieve the financial and strategic results predicted during the planning stage. That's because organizations often make two major mistakes (faulty assumptions and insufficient planning) on the front end, and face two major hurdles (execution and cultural differences) on the back end, once the contract has been signed.

POSTMERGER HOT SPOTS

In a successful blending of two organizations, a lot of legwork — and thoughtful analysis — has taken place before the day of the actual merger. Both nonprofits have, for example, gone through a score of due diligence tasks, making sure that the merger is financially a sensible endeavor.

Following are some of the key issues nonprofits will encounter once the decision to merge is final. Most should be addressed before the date the merged organization goes live. These hot spots will challenge the new management team *and* lay the foundation for the new entity:

Retaining constituent support. Change may make the nonprofits' past supporters jittery. The new organization will need to assure its supporters, by word and by action, that it will fulfill its reshaped mission as well as or better than either organization has in the past.

Communication with constituents will never be more important. The organizations need to make sure that their individual contributors, funders and volunteers, as well as the audience they serve, are fully on board as the new organization sets off to reach its goals.

Blending staff. Merging two staffs often means staff reductions. The transition team, Human Resources and management will examine ways to reduce redundant positions — one, not two, controllers will be needed going forward, for example.

So, how does management decide who stays and who goes? The team can compare employees against their measurable skills, assessing who has performed better in their previous posts. Or they can go a step further by having the "candidates" behaviorally tested as a part of "applying" for the remaining jobs. Which employees have the best personality traits, for example, to stay level-headed under pressure and adjust to change?

Managing employees. In a merger, those who remain after a staff reduction may still worry about changes made to their position or the new supervisor they report to. They also may be concerned that their salary or benefits will be cut.

It's the job of the new leadership to create a sense of continuity and assure employees that their individual strengths and value to the organization won't be lost in the shuffle. Building trust is an essential ingredient in employee retention. Ongoing communication is the best way to get there.

The transition team may have already recommended a similar — or even a better — employee benefits package that will kick in after the merger. Improved options are often the case with the new organization's health insurance plan. A larger pool of employees often equates to economies of scale, and better insurance coverage may become affordable.

Whether employee benefits packages improve or not, management should highlight any pluses under the new plan and consider adding inexpensive perks (a free yoga class at noon, no-cost 15-minute massage sessions, and so on) to help boost morale.

It can be said that an organization is only as good as the policies it adheres to and the procedures it follows.

Standardizing operations. The differences in how the two organizations previously handled their daily affairs may seem overwhelming at first. Merging two IT systems is often a bear of a task that will test all of the organizational skills of the IT management team. A timetable for the changes and ample resources to make it all happen are essential, as are patience and attention to detail in the employees assigned to the task.

Undoubtedly, there will be standardization challenges for other functional areas of the new nonprofit as well. Take accounting, for example. Different accounting systems may be used, and it must be decided which one should prevail. The "up" side: This will be an opportunity to objectively choose which existing practices are most efficient and effective for the new organization.

Standardizing policies and procedures. It can be said that an organization is only as good as the policies it adheres to and the procedures it follows. Standardization won't happen overnight. The new board of directors will need to methodically review the policies, from gift acceptance to whistle blowing, that have been in place.

Again, this is a chance to look for best practices. Procedures for upholding those policies will likewise need to be streamlined or created.

AND IN THE END

There's no question that the transition after a merger is a lot of hard work. But if the transition team and the combined organization's leaders do their job, the new nonprofit will not be as good as the sum of its parts — it will be better. ❋

IRS reviews vary widely

IRS reviews of charities and other nonprofits were once relatively rare. For example, only the largest nonprofits would find an IRS audit team at their door. But in recent years the agency has put an emphasis on enforcement in all areas for all sizes of tax-exempt organizations.

Not all IRS reviews are created equal, however. Here's a rundown of the three main types.

FIELDING AN AUDIT

If your initial contact letter schedules an agent to visit your premises, the IRS is conducting a *field audit* or in-person examination. Field audits are done at a nonprofit's location, their representative's office or an area IRS office. The audit usually happens where the organization's books and records are located.

Field audits fall into two categories. A *general program exam* typically is conducted by a single IRS agent. A *Team Examination Program audit* focuses on large, complex organizations and may involve a team of examiners.

There are many areas an audit can cover. An audit might explore, for example, whether your organization filed all returns and forms as required by law on time and whether they're complete and accurate. Or it might delve into whether your activities were consistent with your tax-exempt purpose, or whether any tax liabilities (for instance, employment taxes or unrelated business income tax) were properly paid.

During the audit the IRS will examine various records. The IRS provides a listing of records it's likely to want to see. (A search for "Charity and Nonprofit Audits: Exempt" on Google leads to the "Charity and Nonprofit Audits: Exempt Organizations Audit" link.)

CORRESPONDING WITH THE IRS

If the initial letter asks you to deliver documents to an IRS office by mail, you are undergoing an *office or correspondence audit.* An agent generally conducts the audit using letters and phone calls to work with the organization's officers or a representative.

But a correspondence audit can expand to become a field audit if the issues grow more complex or the not-for-profit doesn't respond. Both correspondence and field audits can expand to include prior and subsequent tax years.

CHECKING 1, 2, 3

The initial contact letter might indicate that the IRS is conducting a *compliance check.* This isn't an audit but may include a checklist with specific questions. Or it may ask about information and forms that your nonprofit is requred to file or maintain, such as Forms 990, W-2 or W-4.

A compliance check is made to determine whether an organization is adhering to recordkeeping and information reporting requirements. This is usually related to a specific issue —

The IRS review processes in a nutshell

The process differs depending on the type of IRS review a nonprofit undergoes.

An *audit* begins with the initial contact and continues until audit findings are discussed in a closing conference (in person or by phone) and a closing letter is issued. An officer, your representative and the agent will discuss the agent's conclusions at the closing conference. Both the conference and the letter will explain your appeal rights.

Compliance checks and compliance questionnaires also start with the initial contact letter. IRS personnel will review requested items submitted via mail and follow up as needed. They may request additional information. The IRS likely will contact your organization again if you don't respond.

At the end of a compliance check, the agent typically issues a closing letter. But if you've received just a compliance questionnaire, once you have provided the requested information, you may never hear from the IRS again.

Form 990 disclosures, for example — and whether the nonprofit's activities are consistent with its tax-exempt purpose.

According to the IRS, "The IRS uses the Form 990 responses to select returns for examination, so a complete and accurate return is in your best interest."

Compliance checks are an accountability tool, like audits, but are simpler and less burdensome and don't directly determine a tax liability for any particular period. They can, however, lead to an audit.

BECOMING A TARGET

Nonprofits are chosen for reviews for several reasons. The igniting spark might be an IRS examination initiative or project. Or the agency may have received complaints about potential noncompliance at your organization.

Other reasons for a review include risk modeling from the revised Form 990; related examinations of other taxpayers, such as business partners, clients or vendors, whose returns were selected for audit; and document matching — when payer records, such as Forms W-2 or 1099, don't match the information you've reported. Additionally, certain claims for refunds or requests for abatements also can bring about further review.

In general, though, Form 990 plays a strong role in the selection process. In its *FY 2012 Annual Report & FY 2013 Workplan,* the IRS delivered this bottom-line message to nonprofits: "The IRS uses the Form 990 responses to select returns for examination, so a complete and accurate return is in your best interest."

FOLLOWING THE RULES

The IRS says its job is to review exempt organizations for a number of reasons, including ensuring that they're truly operated in the public interest and aren't engaged in any substantial nonexempt (taxable) activities. If your organization is following the rules, you have nothing to fear from a review. Your CPA can give you advice along the way to help make sure your organization is compliant. ❋

The annual budget: Who's on 1st (and 2nd and 3rd)?

Developing an annual budget can be complex and time-consuming. The job will be less daunting if everyone knows their role. Each nonprofit handles budgeting a little differently, but here's a quick summary of the key roles in this team project:

Management and staff. Following the not-for-profit's strategic plan, the CEO or executive director and the finance director will decide which programs and activities to include for the coming year. Then staff responsible for each activity will crunch the numbers to contribute to the budget. They should base revenue and expenses on historical data — what's happened in the past — and on any expected changes for the coming year. Accounting usually will create the budget for overhead and pull together the numbers from the rest of the staff to create the first budget draft.

The draft should include the previous year's budgeted and actual totals, and the current year-to-date actual and budgeted amounts. It also may be helpful to annualize the current year numbers. Having this information in one place will facilitate answering questions as the process unfolds. Notes on the logic behind any new revenues or expenses and on any items that will change from the current year should also be included in the budget draft.

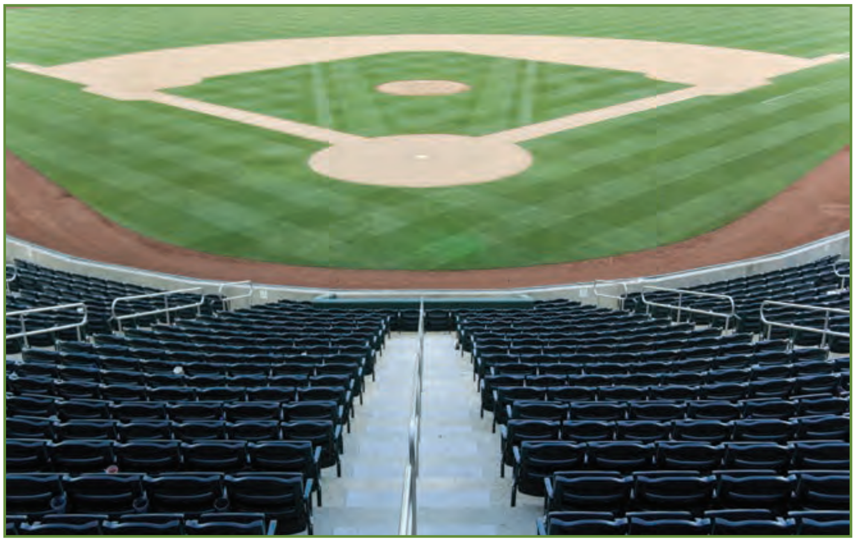
The finance committee. If your nonprofit has one, the finance committee will review the budget and likely ask questions. Its job is to ensure that the budget is reasonable and supported by sufficient revenue to be sustainable.

The committee will need to understand whether the budget is done on the cash or accrual basis and may ask to see the effects of your plan on cash flows. The budget may go through several drafts before it's ready to be presented to the full board.

The board of directors. The board often takes the finance committee's recommendation and approves the budget as presented. But when significant new programs are in the works, the board may have revisions, too.

The approved budget will be the organization's road map for the year. But adjustments may be needed as the year progresses — if, for example, revenues turn out to be different than projected or unexpected expenses surface. These changes will require board approval.

It's the prerogative of the board members to disallow unbudgeted expenditures. The responsibility of "proving" why unplanned expenditures — for instance, $1,000 to fund a new program activity — are necessary or desirable generally falls to staff. ❋



NEWS FOR NONPROFITS

ONLINE FUNDRAISING SCORES ON "GIVE LOCAL" DAY

More than 305,000 donors contributed over $50 million in this year's inaugural Give Local America fundraising drive, a single-day charitable event held in May. The average donor gift was approximately $113. The donations were distributed to 7,700 nonprofit groups participating in 120 communities, according to event organizer Kimbia, a provider of online-giving technology.

The event, which introduced many participating nonprofits to online-donation technology, celebrated the 100th anniversary of U.S. community foundations. Donations were funneled to nonprofits in two ways: 1) Community foundations collected and distributed the funds to participating area nonprofits, and 2) Network for Good filled that role in communities where a foundation wasn't involved. Kimbia received a fee of 2.99% of funds processed to cover project management and related expenses. A second-year event is scheduled for May 2015. ❋

NEW "NATURAL" EXPENSE REPORTING ON THE RUNWAY

The Financial Accounting Standards Board (FASB) has voted to require all nonprofits to present expenses by both functional and natural classifications on their financial statements. Currently, all nonprofits generally must use functional reporting, but only health and welfare organizations must also use reporting by natural category.

FASB's Accounting Standards Codification® defines natural classification as "a method of grouping expenses according to the kinds of economic benefits received in incurring those expenses." Rent, salaries and employee benefits are types of classifications used under the natural classification method.

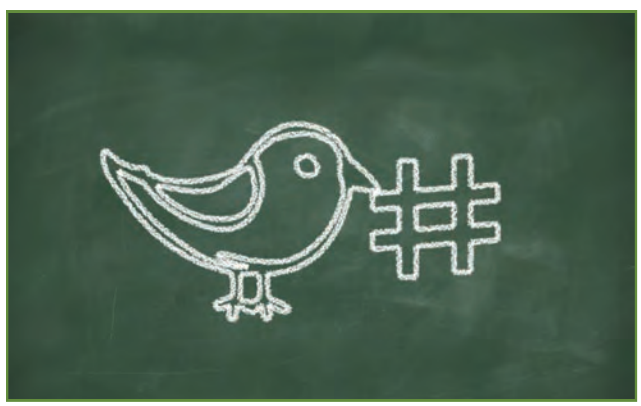
Under the current proposal, not-for-profits could present the information in the statement of activities, in a separate statement of functional expenses, as a narrative discussion or in footnotes in a matrix format.

An exposure draft that details the new requirement and requests comments is expected to be issued later this year. ❋

OF HASHTAGS COUNTS

If you've already incorporated posts to Twitter as part of your social media strategy, heed this advice: Use, but don't *over*use, the popular hashtag (the # symbol usually followed by a few words or a sequence of letters, numbers and symbols).

Buddy Media analyzed user engagement from 320+ Twitter handles of the world's biggest brands, reaching these conclusions: Tweets with one or two hashtags get 21% higher average engagement than tweets with no hashtags. But tweets with three or four hashtags get 17% *less* engagement than tweets with no hashtags. Using an existing hashtag that's trending will increase your exposure even more. ❋



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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!!