

# nonprofit agendas

OCTOBER/NOVEMBER 2009

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# A guide to your galaxy



When new employees join your organization, you likely give them an employee manual, or handbook, to familiarize them with your organization. No matter what topics are included — from office hours to staff evaluations — the purpose of this orientation tool is to prevent workplace confusion.

But what about your board of directors? If you don't give them a board manual, you may be missing out on a valuable opportunity to strengthen your board.

## WHY IS IT IMPORTANT?

Like an employee handbook, a board manual familiarizes readers with your organization's policies and procedures, giving them information at their fingertips. A manual can introduce board members to your nonprofit's reason for being and way of doing things.



A manual also can inform board members of contacts within your organization offering answers to the proverbial question, "Who's responsible for that?" And it can raise awareness of your board's role both inside and outside of your nonprofit, for example, by preparing a board member to be a strong spokesperson in any situation.

Your overall goal should be to supply essential background information to board members when they first walk in the door and a useful reference they can draw on in the future.

## WHAT CONTENT IS CRUCIAL?

While there's no such thing as a *model* manual that fits the boards of all nonprofits, certain information always warrants inclusion:

- \* Articles of incorporation,
- \* The IRS tax determination letter granting 501(c) status, exempting the organization from some federal income taxes,
- \* Board bylaws, resolutions and policies (code of ethics, conflict of interest policy, code of conduct, and so on),
- \* A copy of an in-force policy for directors and officers (D&O) liability insurance,
- \* Your board charter, which may include your mission statement,
- \* Descriptions of any board committees and their members, and
- \* Board and staff contact information.

Additionally, your not-for-profit's unique characteristics may call for the inclusion of other material, such as board election results, recent awards or news articles.

## WHAT'S GOOD TO INCLUDE?

While some information is essential for a board manual, other material is simply desirable to include:

**A strategic planning document.** If your organization has a formal strategic plan (with goals, action plans and status reports), include it to solicit board member feedback and creative ways to reach goals. If the board was involved in that document's development, members should receive a copy of their hard work.

**Financial information.** Your annual budget and audited reports are important financial information. Your board will likely want to review your current (and immediate past) annual budget and audited reports. For new members, this provides a good look at where your organization has been — and where it is now.

**Fiscal and personnel policies and procedures.** The simplest thing to do may be to include your entire employee handbook in the board manual. Reviewing fiscal and personnel policies

and procedures allows board members to get a feel for what's happening in your organization's back office. What are your organization's day-to-day operations? Are effective internal controls in place to help prevent and detect fraud? Are personnel policies and procedures up-to-date? These are the types of matters your board should be aware of and may want to discuss.

## WHERE CAN YOU START?

If your organization doesn't have an up-to-date board manual — or has never had one — consider assembling a *board manual committee*. This short-term unit can create or update board manual contents as it exchanges ideas from other boards on which the members sit or from outside consultants.

Once it's ready, present the new or updated board manual at a retreat or during a board orientation session. And consider going (or staying) green: E-mail an electronic copy of the manual so that board members can have instant access to your nonprofit's world. \*

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# Doing the right thing

## *Avoid excess benefit transactions*

One way to lose your nonprofit's tax-exempt status (or for the individuals who control your organization to rack up excise tax penalties) is to ignore the private benefit and private inurement — also known as excess benefit — provisions of the Internal Revenue Code (IRC). These rules prohibit an individual inside or outside a nonprofit from reaping an excess benefit from a transaction by the organization. Excess benefits can take many forms, such as excessive compensation, favorable sales of assets, below-market property rental and lending money.

## WHAT'S AT RISK

The official IRS stance is that any amount of private benefit or inurement in your organization is enough to cause the loss of your tax-exempt status. Although in practice the agency doesn't strictly enforce this position, it's important to remember that it can do so at any time.

Even if a violation doesn't cause a status loss, those receiving the excess benefit — and any of the organization's managers and board members who willingly participated in the transaction — may be subject to intermediate



sanctions in the form of an excise tax penalty. Penalties can range from a minimum of 10% (maximum of \$20,000) of the excess benefit for managers who knowingly participate up to 200% for the person receiving the benefit.

### EXCESS BENEFIT TRANSACTIONS

The concept of *private benefit* is easy to understand: It's any payment or transfer of assets made (directly or indirectly) by your nonprofit that's beyond reasonable compensation for the services provided or the goods sold to your organization, or services or products that don't further your tax-exempt purpose. If any of your net earnings *inure* to the benefit of any individual, the IRS won't view your nonprofit as operating primarily to further its tax-exempt purpose.

The *private inurement* rules take the excess benefit transaction concept and extend it to "insiders" of the organization. The term "insider" or "disqualified person" generally refers to any officer, director, individual or organization that's in a unique position to be able to exert significant influence over the

nonprofit's activities and finances. A violation happens when the approval of a transaction ultimately benefits the insider. An insider could include an insider's family members or any organizations they control.

Of course, the rules don't prohibit *all* payments, such as salaries and wages, to an insider. They simply require that a payment be reasonable in relation to the services provided or the goods received — and that it be made with the nonprofit's tax-exempt purpose in mind.

As a result, your organization should document its practices and procedures relating to any payments being made to insiders. This is to ensure that, upon an audit or inquiry, you'd be able to show that there was a reasonable and valid exempt purpose for the transaction to have taken place.

### DUTY OF CARE

Duty of care is a related concept that requires board member understanding. It refers to a board member's responsibility to act in good faith, in the organization's best interest, and with such care that proper inquiry, skill and diligence has been exercised in the performance of duties.

*Board members carry a fiduciary responsibility to act with due care to safeguard assets until they can be spent for the organization's tax-exempt purpose.*

Remember, nonprofits are essentially stewards of the public's money. So, board members carry a fiduciary responsibility to act with due care to safeguard assets until they can be spent for the organization's tax-exempt purpose. This concept extends to all facets of the nonprofit and includes ensuring there are proper procedures in place to receive, hold and, ultimately, expend the assets for their proper purpose.

## Liability for all

If your board of directors knowingly approves an excess benefit transaction, *all* board members could find themselves in a position of having to defend themselves against the 10% excise tax penalty simply because they were on the board at the time the transaction was approved.

It's important, then, that all board members attend board meetings to ensure they individually understand the transactions into which the board is entering.

properly spent and safeguarded. A violation of this duty is most evident when an organization enters into an excess benefit transaction with an insider or an individual or organization outside of it.

The consequences of such a transaction can be devastating to the nonprofit, which may lose its tax-exempt status, and to the individuals involved, who may be subject to significant excise tax penalties.

Because any violation of the excess benefit rules — no matter how small — can be enforced by the IRS, everyone in your organization needs to be intimately familiar with them. \*

## CLEAR CONSEQUENCES

It's the duty of nonprofits and their boards to ensure that their organizations' resources are

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# Set your sights on planned giving

If yours is like many nonprofits, you're seeing a downturn in smaller donations — \$100, \$500 and \$1,000 — that echoes the downturn in the economy. This trend has smart charities focusing their efforts to bring in major gifts from their wealthiest donors. That's because these donors have long planned to leave part of their estate to a favorite organization, and most will follow through on their intentions.

## MAKE ARRANGEMENTS

Here's an overview of three of the most popular planned giving arrangements for major gifts:

**1. Direct gifts and bequests.** These donations go directly from a donor (or a donor's estate, in the case of a bequest) to your organization. Lifetime gifts of cash, property or other assets



are usually fully deductible for income tax purposes. This is the case if the donor itemizes and his or her donations don't exceed the applicable adjusted gross income (AGI) limits. Excess charitable deductions can be carried forward up to five years. Generally, the bigger the donation, the bigger the tax benefit. Direct bequests, typically made via a will, are generally 100% deductible for estate tax purposes.

**2. Charitable gift annuities.** These vehicles can be a good fit for people who want to donate substantial assets during their lifetimes and are concerned about keeping a consistent income flow for themselves while minimizing taxes. With this agreement between you and the donor, your nonprofit receives money, securities or real estate, and in return agrees to pay the donor a fixed income for life. That amount is based on the contributor's age at the time of the gift and the rate of return your organization expects to earn and agrees to pay to the donor.

Also, the contributor can defer any capital gains on appreciated property given to you, recognizing gains only as he or she receives annual payments. Meanwhile, a portion of each payment is defined as a tax-free return on principal. Plus, the donor can claim an income tax deduction equal to the present value of the charitable interest the year the annuity is set up.



**3. Charitable trusts.** With a charitable *lead* trust (CLT), the contributor donates assets to a trust, which pays income to the charity for a number of years. Then the property reverts to the donor or a beneficiary. The donor receives a gift or estate tax deduction (depending on whether the trust is funded during life or at death) equal to the present value of the charitable interest when the CLT is set up. Depending on the CLT's structure, the donor also may receive an income tax deduction.

With a charitable *remainder* trust (CRT) the donor (or another noncharitable beneficiary) receives income from the donated assets for a specified period, or for life, and the remainder goes to the charity. As with a charitable annuity, the donor can defer capital gains on certain long-term appreciated property given to the CRT, recognizing gains only as he or she receives annual payments. The donor receives a gift or estate tax deduction equal to the present value of the charitable interest when the CRT is set up and, if it's set up during life, also will receive an income tax deduction.

Other familiar structures for planned giving include donor advised funds (DAFs), supporting organizations and private foundations. Your financial advisor can provide information on these options.

### INFORM YOUR STAFF, BOARD

Designated members of your staff — and all of your board members — should be able to discuss the characteristics of the most common planned giving vehicles with prospective donors. Consider purchasing planned giving software to help in this endeavor. PG Calc and Crescendo Interactive, for example, offer products that do everything from creating elaborate marketing presentations and illustrating gift scenarios to crunching numbers and generating contracts.

Although amounts *may* be somewhat smaller than they were before the recession began, donations in the form of planned giving represent economic stability. Whatever shape they may take, these vehicles are well worth pursuing. \*

# NEWS FOR NONPROFITS

## POLITICAL ACTIVITY

The IRS is continuing its education and enforcement program on political campaign activities by nonprofits. It's reminding *charities* that, as the Internal Revenue Code states, they aren't allowed to participate in, or intervene in, any political campaigning on behalf of, or in opposi-



tion to, any candidate in public office. Nonprofit organizations, *other than charities*, that participate in political campaign activities should discuss the activities with their accountants to ensure that all of the organization's filing requirements for the political activity, if any, are being met. \*

## IRS EXTENDS 403(b) WRITTEN PLAN DEADLINE TO YEAR END

If you sponsor a 403(b) plan, you now have a little more time to get a written policy in place. When 403(b) plan regulations were finalized in July 2007, plan sponsors were required to put in place a written plan of the requirements by Jan. 1, 2009.

The IRS now says it will *not* treat a 403(b) plan as failing to meet the requirements if the plan's sponsor adopts a written plan intended to satisfy the regulations on or before Dec. 31, 2009, as long as the sponsor operates the plan with a reasonable interpretation of the final regulations during all of this year.

Also, before year end, you must make your best efforts to retroactively correct any operational nonconformity to the written plan, such as doing catch-up contributions. \*



## FILING FORM 990-N

The IRS has had to come up with a plan to determine how many of the 650,000 tax-exempt organizations in its master file are still in existence. Because organizations with gross receipts under \$25,000 aren't required to file, the IRS isn't sure which charities are still in existence but under the filing threshold and which charities are nonexistent. To help clean up their master file, charities that normally have annual gross receipts under \$25,000 were required to file Form 990-N (the E-postcard) with the IRS starting in 2008, according to the Pension Protection Act of 2006.



GuideStar, a provider of nonprofit information, predicts that approximately half a million nonprofit organizations could lose their tax-exempt status on May 15, 2010, due to lack of filing the 990-N. Although no penalties are assessed for filing the 990-N late, the IRS states that organizations will lose their tax-exempt status if they fail to file for three consecutive years (that is, 2008, 2009 and 2010). Once an organization loses its tax-exempt status, it must reapply and pay the user fees to have its tax-exempt status reinstated. \*