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Profitable Solutions for Nonprofits

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NEWSBYTES

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Budgeting in the shadow of COVID-19

Budgeting is always, to some degree, an exercise in uncertainty. But the current budgeting environment is unlike any experienced before. As a result of the COVID-19 crisis, many nonprofits have seen deep declines in revenue while the demand for their services has spiked. These and other pandemic-related factors may call for your organization to take a different approach to budgeting than it has in the past, even as a vaccine is distributed.

Avoid the typical tack

Most nonprofits historically have relied on so-called static (or fixed) budgets that are developed in advance of each fiscal year, based on estimated activity. The numbers don't move as activity levels increase and decrease or circumstances otherwise change.

This approach can work for organizations that generally experience relatively minor changes year to year — for example, a small nonprofit supported largely by stable grant funding. It can pose problems, though, in a turbulent landscape like that of the past year. Rolling budgets or, more drastically, reforecasting may prove necessary to deal with such volatile times.

Roll with the punches

Rolling budgets are more flexible than their static counterparts. Rather than leaving a budget in place for the year, organizations with rolling budgets set times throughout the year to readjust the numbers. For example, you might budget four quarters ahead. At the end of each quarter, you would update the budgets for the next three quarters and add a new fourth quarter.

The rolling approach anticipates changes and encourages your organization's leaders to take a forward-looking perspective. It works well for nonprofits dealing with shifting ground and evolving strategies. That's because it facilitates more timely responses to emerging trends, whether on the revenue side, the expense side or both. Plus, it provides more useful information for decision-making than a backward-looking static budget.

Reforecast for trigger events

However, for most nonprofits, it's probably safe to say that the COVID-19 crisis has represented something more dramatic than simply shifting ground. It has shaken their foundations, including many of the assumptions on which they built their budgets. If your organization is among them, you may want to consider reforecasting your entire budget. It might seem overwhelming or like overkill, but it could boost your nonprofit's odds of survival.

Reforecasting generally makes sense when your organization expects or has undergone a major change that has implications for overall operations (a "trigger event"), such as securing or losing a large grant. It's also wise if it becomes clear the existing budget is materially inaccurate. Reforecasting requires taking a holistic view of your entire budget, accounting for the new circumstances and updating wherever necessary. The final product is a fully revised budget, not just a handful of line item adjustments.

Apply budget modeling

With reforecasting, you typically begin by determining the costs and revenues that are variable (for example, supplies and program revenue) and the effect that the trigger event might have on them. In the case of an event as far-reaching as the pandemic, you also might find that fixed expenses like payroll or rent are affected. You'll need to reforecast any of these items that are likely to differ substantially from original estimates.

You may find it worthwhile to apply budget modeling, considering different scenarios. For example, what would happen if a major revenue source was cut by half? Or if it disappeared altogether? Would you seek a loan, cancel a capital project or trim staff?

It's also a good idea to check in with department managers to get their views from the forefront. They might see trends coming that could affect the bottom line but escape the notice of budget makers.

Stay on top of it

Regardless of whether it's your official "budget season," you need to stay on top of the figures. Regular budget monitoring and review are advisable to catch significant variances and make appropriate adjustments even when a pandemic or other catastrophe isn't in the picture. Be sure your board is active in the monitoring process. ■

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You should plan for COVID-19 expenses, even now

Many nonprofits incurred pandemic-related costs that weren't included in their 2020 budgets. It's a smart practice to budget for some of those expenses for 2021. If they don't end up coming to fruition, you can direct the surplus elsewhere. Costs to consider include:

Sanitation. Most nonprofits have instituted enhanced cleaning protocols and procedures, whether mandated by the government or not. Even as the pandemic dissipates, it's likely that people will remain sensitive to sanitation for a while, so you should budget to continue these measures.

Meetings. Similarly, some people will still resist travel. Your budget, therefore, should include costs for the necessary technology and personnel to support virtual meetings. When you do resume in-person gatherings, you'll probably need to provide masks, hand sanitizer and the like, which you also should include in the budget.

Insurance. Insurance premiums often jump in the wake of catastrophes. Expect to pay more going forward.

Employee assistance. You may want to consider providing tax-free assistance to employees incurring pandemic-related expenses, as long as the pandemic remains a federally declared disaster.

FASB issues new rules for reporting gifts-in-kind

More information will be required from nonprofits that use Generally Accepted Accounting Principles (GAAP) and receive nonfinancial assistance — also known as gifts-in-kind — than in the past as the result of a new Financial Accounting Standards Board (FASB) rule. Accounting Standard Update (ASU) No. 2020-07, *Not-for-Profit Entities (Topic 958): Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets*, is intended to expand the transparency around such gifts, including how they're used and valued. Here's what you need to know.

Greater transparency

Gifts-in-kind include fixed assets (such as land, buildings and equipment); the use of fixed assets or utilities, materials and supplies (such as food, clothing and pharmaceuticals); and intangible assets, contributed services and the unconditional promises of those assets. Many nonprofits, including smaller organizations, rely on such contributions.

Until now, the FASB didn't specify how nonprofits must present gifts-in-kind on their financial statements. Nonprofits also weren't subject to specific disclosure requirements for such donations, other than for contributed services.

According to the FASB, the new ASU responds to input from nonprofit stakeholders. Some were concerned because they lacked information about the amount of gifts-in-kind received and used in their organization's programs and other activities. Others didn't think aspects of the FASB's guidance on valuing certain gifts-in-kind were clear.

In particular, stakeholders raised concerns about nonprofits applying U.S. wholesale market prices to determine the value of donated pharmaceuticals that can't be legally sold in the United States. For example, a donor might contribute such items for use only outside the country. If the values are inflated, an organization's revenue and program expense would likely increase. This could make the nonprofit appear larger and more efficient than a smaller organization or one that uses lower values for gift-in-kind donations.

New requirements

Under the new standard, a nonprofit must report gift-in-kind donations as a separate line item in its statement of activities, apart from contributions of cash or other financial assets. In the notes to the financial statements the nonprofit is required to further report such donations by category of asset (for example, land, food or pharmaceuticals).

In addition, for each category of gifts-in-kind recognized, a nonprofit is required to disclose:

- Information about whether the donations were monetized (for example, by selling them) or used in its operations. If used, the nonprofit must describe the programs or other activities in which the assets were employed,
- Its policy, if any, about monetizing rather than using gifts-in-kind, and
- Any donor-imposed restrictions associated with the gifts-in-kind.

The nonprofit also must provide a description of the valuation techniques and data used to calculate a gift-in-kind donation value. And it might be required to disclose the *principal* (or *most advantageous*) market used to calculate the value.

The principal market is that with the highest volume of activity for the donated asset. The most advantageous market generally is the one that maximizes the amount that would be received if the donated item were sold. This disclosure is necessary if it's a market in which donor restrictions prohibit the nonprofit from selling or using the donation. Previously required disclosures relating to contributed services haven't changed under the new ASU.

The ASU contains several examples of Statement of Activity presentation, as well as financial statement note disclosures, to assist in understanding the requirements. The examples also highlight various valuation techniques.

Coming soon

The new gifts-in-kind reporting standard is effective on a retrospective basis for annual periods starting after June 15, 2021, and interim periods with annual periods starting after June 15, 2022. Early adoption is permitted. Consult your CPA to make sure you're taking the necessary steps to prepare for compliance. ■

Prevent the UBIT trap of corporate sponsorships

Landing a corporate sponsorship is an accomplishment, especially in today's economy. If you do get lucky, you'll want to prevent unrelated business income tax (UBIT) from cutting into your new income. If you meet the requirements for a qualified sponsorship payment *exception*, you should be in good shape.

What are the exceptions?

Generally, "qualified sponsorship payments" received by a nonprofit are *exceptions* to what's considered unrelated (trade or) business income (UBI). A qualified sponsorship payment is a payment of money, transfer of property or performance of services with no expectation that the sponsor will receive any "substantial return benefit." Benefits returned to the sponsor may include advertising; goods, facilities, services or other privileges; rights to use an intangible asset such as a trademark, logo or designation; or an exclusive provider arrangement.

To be considered "substantial" by the IRS, the aggregate fair market value (FMV) of all benefits given to the sponsor during the year must exceed 2% of the sponsor's payment to the nonprofit. If the total benefit exceeds 2% of the payment, the entire FMV of the benefits (not just the excess amount) is a substantial return benefit.

What does "use" or "acknowledgment" mean?

The regulations specify for purposes of the exception that a nonprofit's "use or acknowledgment" of a sponsor's name, logo or product lines associated with the sponsored event won't constitute a substantial return benefit to the sponsor. Your organization's use or acknowledgment (as opposed to promotion, marketing or endorsement) can include:

- The display of the sponsor's brand or trade names and product or service listings, as well as a listing of the sponsor's locations, telephone numbers or website address,
- Logos and slogans that contain no qualitative or comparative descriptions of the sponsor's products, services, facilities or company such as "the best car insurance money can buy," and
- Display or distribution of the product itself, free or for remuneration (at the sponsored event), if there's no agreement to provide the sponsor's product exclusively.

Also keep in mind that payments made in connection with a trade show or convention aren't qualified sponsorship payments, nor are contingent payments. If a sponsor's payment is dependent on event attendance, broadcast ratings or other measures of public exposure to the sponsored activity, the payment falls outside the exception.

What's a "substantial return benefit?"

When a sponsorship comes with a substantial return benefit, only the part of the sponsor's payment that exceeds the substantial return benefit is considered a qualified sponsorship payment. The remainder is UBI.

Consider, for instance, a nonprofit that receives $50,000 from a sponsor to help fund an event. The organization recognizes the support by using the sponsor's name and logo in promotional materials. It also hosts a dinner for the sponsor's executives, and the FMV of the dinner is $1,500, exceeding 2% of the sponsor's payment.

The use of the sponsor's name and logo constitutes permissible acknowledgment of the sponsorship, but the dinner is a substantial return benefit. As a result, only that portion of the sponsorship payment that exceeds the dinner's FMV, or $48,500, is an exempt qualified sponsorship payment.

Avoid a liability

Value your corporate sponsorship. Hopefully, it'll be one of many your organization secures going forward. But keep an eye on qualified sponsorship payment exceptions so that receiving such a payment doesn't have a liability attached. ■

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Charity Navigator acquires ImpactMatters

The well-known nonprofit rating website Charity Navigator recently announced its acquisition of ImpactMatters, a startup that measures nonprofits' impact. The company developed a method for rating impact that estimates cost-effectiveness based on publicly available data as well as social science theories and evidence.

The acquisition coincides with Charity Navigator's rollout of the second of the four "beacons" in its new Encompass Rating System — a beacon dubbed "Impact & Results." The other beacons are Finance & Accountability, Leadership & Adaptability and Culture & Community. The new system marks a shift toward ratings more heavily based on effectiveness, rather than only on measures of financial indicators and accountability. ■

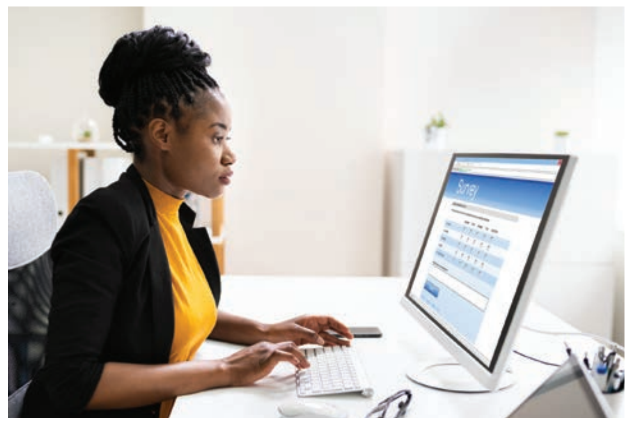
How do voters view nonprofits' COVID response?

A plurality of registered voters says nonprofits have done a better job of meeting the needs created by COVID-19 than the federal government or for-profit businesses. That's according to a survey of more than 1,000 registered voters nationwide conducted in October 2020 on behalf of Independent Sector.

Forty percent of respondents said nonprofits have done the best job, compared with 21% who chose the federal government and 16% citing businesses. Twenty-three percent said the three sectors performed equally. Three-quarters of respondents strongly or somewhat agreed that Congress and the president need to take urgent action to provide support for charities so they can continue to provide assistance to their communities.

The survey also found widespread support for a universal charitable tax deduction. Eighty-eight percent strongly or somewhat supported such a deduction. In line with this opinion, the Consolidated Appropriations Act, signed into law by President Trump in December 2020, extends the $300 above-the-line deduction for nonitemizers through 2021. For 2021, the deduction is doubled to $600 for married couples filing jointly. ■

Survey examines sentiments toward nonprofits



Independent Sector and public relations firm Edelman Intelligence have launched an annual series of surveys intended to explore the nuances of trust in American nonprofit and philanthropic organizations. The first survey — of 3,000 Americans aged 18 or older — brought mixed news for nonprofits.

For example, although 59% of respondents reported high trust in nonprofits to do the right thing, that trust was concentrated among urbanites with high levels of income and education. Rural Americans and those with lower incomes and less education were more likely to express skepticism. Worse, respondents from underserved communities most in need of support reported the lowest levels of trust.

The researchers also applied statistical analysis to predict the actions nonprofits can deploy to strengthen public trust. They recommend that nonprofits be clear about their mission and purpose, demonstrate impact, and show integrity through transparency and independence. ■

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