Profitable Solutions for Nonprofits

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Building a better audit committee

Start with a clear picture of its roles and responsibilities

Public companies have been required to have an audit committee for about a decade now (due to the Sarbanes-Oxley Act of 2002), and many nonprofits have started their own such committees during that time. The result? Some organizations have learned the hard way that good intentions aren't enough to ensure an effective audit committee — both the nonprofit and committee members must fully understand the committee's role and responsibilities.

UNDERSTANDING THE MISSION

An audit committee should operate as the arm of the board of directors that assures proper financial management. As such, it's an integral part of good governance, making it relevant for nonprofits of all sizes. After all, poor governance and accountability can cost any organization support, financial and otherwise.

The committee's job largely comes down to oversight, which is usually focused on financial reporting, external and internal audit functions, compliance with legal and regulatory requirements and the internal controls over these areas. An effective audit committee can lead to improved financial practices and reporting, reduced fraud and enhanced internal and external audits.

Smaller nonprofits may be tempted to assign audit committee functions to their finance committee, but that committee has different responsibilities — it's tasked primarily with monitoring the budget and approving the distribution of the organization's financial resources.

OVERSEEING FINANCIAL REPORTING

The audit committee should take a much broader view, overseeing the conduct and integrity of financial reporting, including establishing and implementing accounting policies and internal controls to promote good financial stewardship. The goal is to protect the nonprofit's assets, strengthen the reliability and accuracy of financial reporting, and reduce the risk of fraud.

On a practical level, financial reporting oversight translates to, among other things:

- Reviewing Forms 990 and reporting to regulatory agencies,
- Looking for red flags in financial statements that might signal improper revenue recognition or other kinds of fraud (for example, unexplained fluctuations in revenues or expenses),
- Reviewing audit results, the nonprofit's responses and follow-up actions, and
- Evaluating the appropriateness of getting a second opinion on auditing issues.

Ultimately, the audit committee should ensure that all financial reports are accurate and transparently portray the organization's performance.

FINANCIAL EXPERTISE: AN AUDIT COMMITTEE NECESSITY

The composition of nonprofit audit committees might vary, but one thing is certain — at least one member of the committee should have strong financial expertise.

The committee's financial expert will bring a working knowledge of financial reporting (including Generally Accepted Accounting Principles) and internal controls. Bear in mind that it's not enough that he or she have experience in the for-profit world — the expert should have knowledge of nonprofit-sector accounting and financial reporting issues.

And don't make the mistake of turning to the organization's treasurer. Because the audit committee is charged with independently monitoring financial results, appointing the treasurer to the committee could create a conflict.

MANAGING RISK

The committee must understand the nonprofit's overall risk profile (as determined by a comprehensive risk assessment). The risk profile considers, among other things, investment practices, disaster recovery plans, insurance coverage, and compliance with laws, regulations and donor and grantor requirements. It also looks at internal policies and procedures. The organization's risks are evaluated in light of its "appetite for risk." The committee should assess internal controls over those risks and, if necessary, see that remedial measures are effectively implemented.

INTERACTING WITH AUDITORS

The audit committee should regularly interact with both internal and external auditors, which includes approving the annual internal audit plan and reviewing internal auditors' reports. The committee also may be responsible for approving the appointment of the head of internal audit.

Additionally, the audit committee is responsible for hiring, compensating and overseeing external auditors and is therefore considered the auditors' client. It should have regular communications with the auditors, including meetings to discuss a workplan before the audit and to review any findings before they're presented to the board.

MAINTAINING INDEPENDENCE

Besides the roles and responsibilities described above, the committee must maintain its independence. That means audit committee members can't accept any consulting, advisory or other compensatory fee from the organization.

Independence from management also is critical. Committee members shouldn't have been an officer or employee of the nonprofit in the prior three years, or the immediate family member of such a person.

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The American Institute of Certified Public Accountants recommends that some audit committee members also be members of the board of directors. But some states limit the number of audit committee members who also are on the finance committee.

BETTER SAFE THAN SORRY

Audit committees may seem like just one more layer of bureaucracy, but they're rapidly becoming a nonprofit "best practice." Your CPA can help you establish a new committee or make sure that your existing committee is operating as it should be. ❋

Is it time for "software as a service"?

Nonprofits increasingly are following the path of their for-profit cousins and shunning traditional software arrangements for "software as a service" (SaaS) provided over the Internet for a monthly fee. The potential benefits make SaaS worth considering for nonprofits of all sizes, but some caveats are in order.

SAAS IN A NUTSHELL

The definitions of SaaS are plentiful. Generally, it's best described as software that's delivered via the Internet to subscribers. A nonprofit essentially leases the software, which is housed on the provider's servers, and pays a subscription fee. This contrasts with the historical approach of purchasing or licensing an application or suite of applications and having it installed on the organization's own server, which leaves you responsible for the maintenance and overhead needed to operate the software.

THE BENEFITS

Perhaps the primary benefit of SaaS for a nonprofit is that, applied properly, it can free up resources, including time and money, which the organization can use to further its mission. For example, your IT staff could use the time it would otherwise allocate to updating software, a service that's included in the subscription fee with SaaS, to purposes directly related to your mission. The SaaS provider typically handles system updates and maintenance automatically with a minimum of disruption.

Cost is another major reason more nonprofits are turning to SaaS. The option requires little upfront investment and provides a cost-efficient way to "test drive" software — if you don't like it after a month or two, you usually can cancel your subscription and get your data back. You also don't pay for functions you don't need. Moreover, you won't end up on the hook for costs associated with building infrastructure, upgrades, maintenance and support. And the monthly subscription model facilitates more accurate budgeting for IT.

Software provided online means employees can reliably access it from anywhere with an Internet connection.

Additionally, software provided online means employees can reliably access it from anywhere with an Internet connection, giving them greater flexibility and boosting productivity. Most SaaS providers claim to provide 99.9% uptime.

POTENTIAL RISKS

As with data stored on your own computers, security is paramount when using SaaS. For instance, how can you ensure protection of donor and credit card information?

The good news is that the right provider can probably offer better security on its closely monitored servers than you could on your own. When it comes to credit card information, the "right provider" is one that complies with the Payment Card Industry Data Security Standard (PCI DSS). PCI DSS was promulgated by the credit card industry's PCI Security Standards Council and applies to all entities that store, process or transmit payment cardholder data. It outlines technical and operational system requirements to protect cardholder data.

Availability of your data is another concern. Before selecting a SaaS vendor, make sure to research the financial stability and ability of the company to follow through on their promises. Not having access to your accounting system when payroll is due can quickly override any benefits.

Also ask to see a copy of the provider's Service Organization Control 2 or 3 Report. They test and report on the design and operating effectiveness of the controls at the SaaS provider that may affect its customers' data security, availability, processing integrity, confidentiality and privacy. Your CPA can help you decipher the report.

Finally, evaluate the total costs over the long term. Even though your up-front investment is limited, over time the monthly fees may surpass the cost to purchase and maintain your own system.

BEFORE YOU LEAP ...

Your CPA can break down the financial pros and cons for you, too, as well as explain how the switch to SaaS could affect your financial statements by reducing capital expenditures and increasing operating expenses. Looking at the big picture will facilitate a more informed decision. ❋

Managing staff

How to treat the real gems of your organization

Has your nonprofit frozen wages or awarded minimum pay increases over the last few years while asking employees to take on new responsibilities? Are they being asked to contribute more to your benefit plan, or take a benefits cut?

Such organizational moves often are necessary during tough economic times. That said, don't lose sight of the importance of your staff, from hiring and training them to rewarding them for their performance, and providing motivation to stay.

RECOGNIZE YOUR GREATEST WEALTH

When asked to list their organization's assets, nonprofit leaders are likely to name investments, facilities, real estate, cash and other tangible assets. Too often, personnel are left off the list.

But without a knowledgeable and committed staff, you stand little chance of delivering program services or raising enough money to fund them. And when you consider the cost of hiring, training and mentoring

staff, not to mention the losses your nonprofit incurs when an experienced employee leaves, it's easy to see why you should assign a high value to your people.

ADD TO STAFF WISELY

Finding and keeping good staff starts with smart hiring. Just as you wouldn't buy a mutual fund without researching its performance and strategy, don't hire staffers without thoroughly vetting them for potential rewards and risks.

Experience, education, skills and employer recommendations are merely a starting place. Good hiring requires employers and job candidates to honestly assess their respective objectives. Don't hire someone simply because you're desperate to fill an empty position. Shaky starts rarely lead to long-term success. Similarly, don't court a candidate who seems likely to jump ship when a "better" offer comes along — no matter how impressive his or her resumé.

INSTILL "BUY-IN"

When a new employee comes aboard, ensure he or she receives comprehensive training — not only related to job responsibilities, but also about your not-for-profit's culture and ethics. Staffers need to buy in to your mission and support the programs you've established.

Also ensure that employees understand your evaluation and compensation system — and feel like full participants. Often, they leave a job claiming their employment expectations weren't met and the employers are left scratching their heads about what went wrong. Staffers must be able to voice perceived obstacles to their successful long-term employment without fear of reprisal. If you want to keep them, listen and try to find ways to help them succeed.

BE CREATIVE WITH NONMONETARY REWARDS

Although financial compensation is generally the best way to reward and retain people, there are other ways you can let employees know you value them — without busting your budget. For example, consider tangible rewards other than money. You could write a personal "thank you" note and enclose a small gift card when a staff member achieves something special. Or you could reward that person with an extra vacation or personal day. Another idea: Offer the employee more flexible hours, such as earlier starting and leaving times or the option to telecommute.

Invite "star" employees to be introduced at a board meeting, or to represent your nonprofit at an industry conference.

And don't forget the value of praise and recognition. Acknowledge employees for a job well done at staff meetings or in your nonprofit's newsletter. Or invite "star" employees to be introduced at a board meeting, or to represent your nonprofit at an industry conference. All of these actions reflect your confidence in those individuals and indicate their importance to the organization.

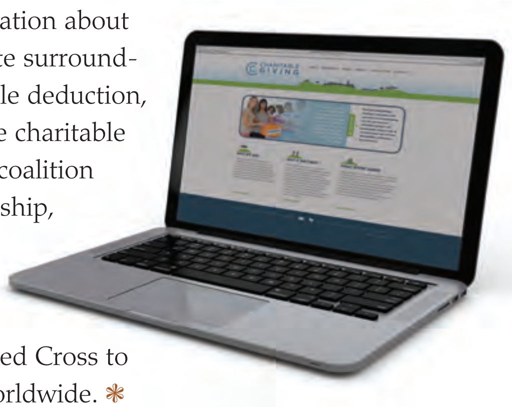
VALUE THEM ANYWAY

Your nonprofit may be unable to compensate employees quite as well as its for-profit counterparts. But, if your focus is on valuing and growing your assets — that is, your employees — all you need is a little creativity in order to reward them in many other ways. *

Newsbits

COALITION LAUNCHES CHARITABLE DEDUCTION WEBSITE

The Charitable Giving Coalition has launched a new website designed to provide user-friendly, accessible information about the vital role of charitable giving in U.S. communities. Formed in 2009, the coalition is dedicated to preserving the tax deduction for those who give to charities. The website (protectgiving.org) includes information about the policy debate surrounding the charitable deduction, the effect on the charitable sector, and the coalition and its membership, which includes organizations ranging from the American Red Cross to United Way Worldwide. ❋



EITF ISSUES RULE ON AFFILIATE PERSONNEL SERVICES

The Financial Accounting Standards Board's Emerging Issues Task Force (EITF) has issued a new rule that addresses the proper accounting for services received from personnel of an affiliate for which the affiliate doesn't seek compensation (*EITF Issue 12-B*).

Currently, the recipient organization only recognizes contributed services from an affiliate if the services either create or enhance nonfinancial assets, or require specialized skills and would typically need to be purchased if they hadn't been donated. Such contributed services are recognized at fair value.

Under the new standard, a nonprofit generally should recognize personnel services that are performed by an affiliate's employees at the affiliate's cost of such services, rather than at fair value. The cost components would depend on the nature and type of service provided, but, at a minimum, costs should include all direct personnel costs (for example, compensation and payroll-related fringe benefits) incurred by the affiliate. The guidance will be effective for fiscal years beginning after June 15, 2014. ❋

WHO GIVES BIG GIFTS?

A new study sponsored by international consultants CCS, through its William B. Hanrahan Fellowship at the Lilly Family School of Philanthropy at Indiana University, has found that the majority of charitable contributions of $1 million or more come from local donors. About 60% come from donors from the same state or geographic region as the recipient's and about half of all publicly announced gifts of this size (47% of the total number of gifts and 52% of the total dollar amount) come from donors living in the same state.

Health nonprofits; arts, culture and humanities organizations; higher education institutions; foundations; and government agencies received more than half of their million-dollar-plus gifts from donors in the same state.

Nonprofits may want to focus their efforts on cultivating relationships with donors invested in their local communities — and who have the financial capacity to make significant gifts. ❋