

Profitable **Solutions** *for* **Nonprofits**

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Prepare now for ACA
play-or-pay compliance

Buyer beware

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with another nonprofit?

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Prepare now for ACA play-or-pay compliance

The Affordable Care Act's (ACA's) shared-responsibility provision, commonly referred to as "play or pay," has been delayed until 2015. Some "transitional relief" also will be available. But that doesn't mean your nonprofit can afford to sit back on its heels. Do you know if play-or-pay covers your organization? Now's the time to determine whether it does and, if so, what it will mean for your bottom line.

UNDERSTAND WHAT PLAY-OR-PAY IS — AND ISN'T

First things first: The ACA doesn't require any employer to provide health insurance coverage to its employees. But "applicable large employers" — generally those employers, private and nonprofit, with the equivalent of 50 or more full-time employees — may be subject to a penalty if they don't offer their full-time employees "minimum essential health care coverage" — or if they offer coverage that isn't "affordable" or doesn't provide "minimum value."

A full-time employee is any employee working on average at least 30 hours per week. But part-timers must also be factored in by calculating full-time equivalent employees (FTEs).

TEST WHETHER YOU'RE A LARGE EMPLOYER

To compute the number of FTEs for a given calendar month, count the total hours of service (not more than 120 hours for any employee) for all part-time employees and divide that number by 120. For example, an employer with 40 part-timers who average 90 hours per month would have 30 FTEs ($40 \times 90 = 3,600$ total hours; $3,600/120 = 30$) who must be included when determining whether the 50-full-time-employee threshold is satisfied.

You must determine each year, based on your employees' actual hours of service, whether your organization will be considered a large employer for the coming year. Under transitional relief, you generally won't be at risk for penalties in 2015 if you have the equivalent of 50 to 99 full-time employees.

DETERMINE WHETHER COVERAGE IS SUFFICIENT

If you *are* a large employer, you need to assess whether you're offering minimum essential coverage to at least 95% of your full-time employees. Some transitional relief is also available here: For 2015 only, the 95% requirement drops down to 70%. Minimum essential coverage is provided by "eligible employer-sponsored plans." These include plans offered in a state's small or large group market as well as self-funded plans. But they don't include certain limited-coverage plans, such as dental- or vision-only plans.

Even if you do offer the minimum essential coverage, you could be subject to penalties if the coverage:

- ★ Isn't affordable, or
- ★ Doesn't provide minimum value.



Generally, coverage isn't affordable if an employee's share of the self-only premium would cost more than 9.5% of his or her annual household income. You can assume an employee's Form W-2 wages represent annual household income.

The Centers for Medicare and Medicaid Services offers an online calculator to help you determine whether your nonprofit's plan provides minimum value.

Minimum value requires that a health plan cover at least 60% of the covered health care expenses provided under the plan. The Centers for Medicare and Medicaid Services offers an online calculator to help you determine whether your nonprofit's plan provides minimum value. Go to cms.gov and search for "minimum value calculator."

CALCULATE POTENTIAL PENALTIES

Large employers that don't offer minimum essential health coverage will be subject to a penalty of \$2,000 per year (assessed on a monthly basis) for each full-time employee in excess of 30 if any of their full-timers



receive a premium tax credit when buying insurance through a state or federal health insurance marketplace. So, if a nonprofit has 100 full-time employees, the penalty would be \$140,000 ($\$2,000 \times 70$).

Large employers that offer minimum essential coverage, but it's unaffordable or it doesn't provide minimum value, must — if at least one full-time employee receives the tax credit — annually pay the lesser of \$3,000 for each full-timer receiving the credit or \$2,000 for each full-timer in excess of 30 full-timers. Like the penalty for failing to provide minimum essential coverage, the penalty payment is calculated separately for each month, taking 1/12 of the annual amount.

FIGURE IT ALL OUT

The regulations surrounding play-or-pay are complicated. Your financial advisor can help you determine *now* whether your nonprofit will be considered a large employer and, if so, how best to proceed. *

SMALL NONPROFITS AND THE HEALTH CARE COVERAGE TAX CREDIT

The health care coverage tax credit is available to both private and nonprofit entities. Your not-for-profit may be eligible for the tax credit if you employ fewer than 25 full-time equivalent employees and pay at least 50% of employees' premium cost for health insurance coverage purchased on a federal or state health care marketplace, and annual average wages per employee are less than \$50,000 per year.

The maximum credit for nonprofits was 25% of premiums paid for employee health coverage in 2010 through 2013 and increased to 35% for tax years beginning in 2014 or later. The tax credit is reduced if an employer has more than 10 FTEs or pays average annual wages of more than \$25,000. Refund payments processed on or after Oct. 1, 2013, and on or before Sept. 30, 2014, will be reduced by the 2014 sequestration rate of 7.2%.

You can file an amended tax return to claim the credit for previous years. In fact, you can potentially claim the credit for a total of six years — 2010 through 2013 plus any two consecutive years beginning in 2014 or later.

Buyer beware

UBIT can take a bite out of alternative investments

The uncertain economy and tempestuous financial markets of recent years have led some nonprofit organizations to turn to alternative investments. While these investments may hold the potential of higher returns, they also come with the risk of unrelated business income tax (UBIT). Even in the absence of tax liability, alternative investments can involve significant filing requirements.

IN A NUTSHELL

Nonprofits have long put their money in traditional investments like stocks, bonds and real estate. But the recession and slow economic recovery have prompted some to consider investments in domestic or foreign hedge funds, private equity funds, commodity funds and private investment funds.

These entities typically are formed as partnerships or limited liability companies (LLCs), with the income and income tax liability passing through to investors.

THE UBIT ISSUE

As you probably know, revenue that a nonprofit generates from a trade or business that isn't substantially related to furthering the organization's tax-exempt purpose may be subject to the UBIT. Investment income — for example, dividends, gains on the sale of securities, and interest — is usually excluded from UBIT.

But when a partnership or LLC engages in a trade or business, its investors are treated for tax purposes as if they conducted that activity themselves. As a result, if a partnership or LLC generates income from an activity that's unrelated to a nonprofit investor's purpose, the nonprofit must treat its share of the income as unrelated business income.

The risk of UBIT doesn't end there. Although interest, dividends and capital gains are generally exempt



from the UBIT as investment income, nonprofits should bear in mind the exception for income from debt-financed property. If a nonprofit took out a loan to make an alternative investment, *all* of the income produced by that investment is subject to the UBIT, including any gain when the investment is sold. The debt-financed income exception also applies if the partnership or LLC used debt to finance the purchase of an income-producing asset, such as a rental property, that passes income through to the nonprofit.

Alternative investments often require the filing of additional tax forms. The failure to comply can result in costly penalties.

ROLE OF SCHEDULE K-1

Nonprofit investors in alternative investments generally receive a Schedule K-1, which reports the investor's income broken down by the nature of the activity that generated it. The form usually includes both income from unrelated business activity and

traditional investment income. The Schedule K-1 should report income subject to the UBIT on a separate line or in a footnote. However, the investment entity might not do so if it's unaccustomed to following applicable UBIT rules. Nonprofits, therefore, should closely scrutinize their Schedules K-1.

FILING OBLIGATIONS

Alternative investments often require the filing of additional tax forms. And the failure to comply can result in costly penalties. For example, you may need to plan for:

- ★ Form 990-T for unrelated business income,
- ★ Form 926 for certain investments in foreign corporations,
- ★ Form 8865 for investments in foreign partnerships,
- ★ Form 8886 for transactions with the potential for tax evasion, and
- ★ Estimated tax payments.



Remember, too, that you may have state filing obligations related to activities of the LLC or partnership, including in those states where your not-for-profit has no presence. As of this writing, 39 states tax unrelated business income and 13 require a distinct 990-T.

LOOK BEFORE YOU LEAP

Alternative investments can prove lucrative for nonprofits, but it's critical to consider the implications of the UBIT and filing rules. In the long run, tax and administrative burdens could outweigh the potential advantages. *

Should you join forces with another nonprofit?

Forming an alliance with a like-minded organization can be a smart strategic move. But think things through thoroughly before making the leap.

EXAMINE YOUR MOTIVES

First off, why are you considering hooking up with another organization? Do you want to save money by sharing operating expenses? Would the union enable you to take on a project or expand your reach in a way that you couldn't do alone?

Your motives for joining forces should make good sense. Then, once you and your potential partner (or

partners) have a specific alliance in mind, your accountant can perform a cost analysis to make sure that financial expectations are on track.



GET VERSED IN JOINT VENTURES

For nonprofits, "joint venture" involves a contractual arrangement with another nonprofit, a for-profit entity or a governmental agency. The two entities become engaged in a solitary enterprise without incorporating or



forming a legal partnership. A joint venture is otherwise similar to a business partnership, except that the relationship typically has a single focus and is often temporary.

For example, a few years ago the American Institute of Certified Public Accountants (AICPA) teamed up with the London-based Chartered Institute of Management Accountants (CIMA). The two professional associations formed a joint venture to develop and promote a new global management accounting designation. The AICPA owns 60% of the joint venture — the Association of International Certified Professional Accountants — and CIMA owns 40%. The board of directors is split evenly between the organizations, with CIMA and AICPA leaders rotating in the role of chair.

STUDY UP ON STRATEGIC ALLIANCES

“Strategic alliance” is a blanket term typically used among nonprofits to represent a wide range of affiliations, including joint ventures. Like a joint venture, a strategic alliance can involve a relationship with another nonprofit, a for-profit or a governmental entity.

The motivations for forming a strategic alliance can vary greatly. For example, Metropolitan Nashville Public Schools formed a strategic alliance with the for-profit Warner Music Nashville to create a student-run record label. Concurrent Technologies Corporation and Renewable Manufacturing Gateway, both nonprofits, drafted a “Memorandum of Understanding” combining their strengths to recruit new companies to locate manufacturing operations in western Pennsylvania.

In another instance, the Council for Christian Colleges & Universities forged a strategic alliance with Christianity Today International to offer a Christian college search website. And a Midwest homeless shelter aligned itself with a community center that offered free classes. By referring its residents to the center, the shelter expanded opportunities for the homeless. And the community center now reaches more needy people.

CONSIDER ALL FACTORS

No matter what type of alliance you make, you should look into the other organization’s finances. First, does the entity pursuing you — or the entity you’re pursuing — have ample means? An alliance between two nonprofits is like any business partnership. Make sure the organization has a good net asset balance and can live up to its financial commitments. There’s no synergy to be had if one of the partners is going to bear the full burden of the arrangement.

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Also consider if the other organization’s values align with yours. Does the entity have a similar sense of business ethics — and strong internal controls? Two working as one requires a great degree of openness and trust between the two parties. You’ll be sharing credit *and* responsibility for initiatives. Because the reputations of both are at stake, the two entities need to be jointly accountable.

PATIENCE IS A VIRTUE

Careful planning is essential before teaming up with another organization. So, too, is careful oversight of all activities once the two entities have begun the cooperative effort. Patience and hard work will be necessary — it usually takes a significant amount of time before the new venture can reach its highest level of effectiveness. *

Newsbits

TWITTER INPUT USED TO GUIDE GRANT MAKING



The Intel Foundation, which aims to foster “educational opportunities and quality of life improvements for communities worldwide,” took to Twitter last fall to solicit input on how the foundation should award \$100,000 in education grants to celebrate its 25th anniversary. During this crowdsourcing campaign, Twitter

users employed the hashtag #Intel100K to suggest programs and organizations that should receive support. A selection committee composed of foundation board members and volunteers reviewed the Twitter-generated themes and chose the grant winners. *

IRS ISSUES PROPOSED 501(c)(4) GUIDANCE

The U.S. Department of the Treasury and the IRS have issued initial proposed guidance on how applicants qualify for tax-exempt status as a social welfare organization under Section 501(c)(4) of the Internal Revenue Code. The proposed guidance defines the term “candidate-related political activity” as including certain communications, grants and contributions, and activities closely related to elections or candidates. It would change the current regulations to exclude such activities from qualifying as the promotion of social welfare.

The IRS says the proposed rules would reduce the need to conduct fact-intensive inquiries, including probes into whether activities or communications are neutral and unbiased. Future guidance will address other related issues, particularly the proportion of a 501(c)(4) organization’s activities that must promote social welfare. Several more steps in the regulatory process, including the review of comments, must be taken before the IRS will issue final guidance. *

SURVEYS REVEAL CEO PAY

The results of two surveys have uncovered some notable trends in executive compensation practices at nonprofits. The *Chronicle of Philanthropy*’s most recent annual compensation survey found that CEOs at the nation’s biggest charities and foundations received a median salary increase of 3.1% in 2012.

That increase was half as large as the pay raises corporate executives received and a drop-off from the previous year’s figure of 3.8%. The median compensation in 2012 for CEOs at all nonprofits was \$417,989.

GuideStar’s 2013 *GuideStar Nonprofit Compensation Report* examines, among other things, the compensation paid to women nonprofit executives. It found that the pay for these executives continues to lag behind that of men in comparably sized organizations. According to GuideStar, the gap ranged from 9% for CEOs of nonprofits with budgets of \$250,000 or less to 21% at organizations with budgets between \$5 and \$10 million.

Notably, the majority of nonprofits with budgets of \$1 million or less had female CEOs in 2011. But the prevalence of female CEOs dwindles as budget size increases: Only 16% of organizations with budgets exceeding \$50 million had women in the top spot. *

