

## What Nonprofits Need to Know About Accounting

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**Tax requirements for nonprofits are stringent, and it can be hard to track all your variable funding sources if you don't have an accountant on staff.**

The ins and outs of accounting can get tricky for any business, but it's especially hard for nonprofits. Tax requirements are stringent, funding sources are variable and many times there isn't even an accountant on staff. Business.com talked to nine accounting and tax professionals to learn what every nonprofit needs to know about accounting.

### 1. Make professional accounting a priority

Many nonprofit organizations don't allocate resources for a professional accountant to manage their finances. Rather than making professional accounting a budget priority, they assign the task to an untrained member of the staff or a volunteer. Tiffany Couch, CEO of forensic accounting firm [Acuity Forensics](#), says this is one of the biggest mistakes not-for-profit organizations make.

Nonprofits run a risk of fraudulent activity if the bookkeeping is not carefully managed. This is often unintentional, through a lack of oversight or experience. Volunteers, which often make up a large part of a nonprofit's staff, often leave an organization with short notice, which can cause gaps in record-keeping.

Hiring a professional ensures that someone with training and experience is always paying attention to the accounts.

"Don't have a mindset of scarcity when it comes to ensuring you have appropriate resources in terms of handling your money," Couch said. "There are plenty of CPAs who would be willing to provide a discount or pro bono services to either provide that oversight or assist in the preparation of your tax returns." [[Check out our top picks for accounting software.](#)]

### Plan for changes to the tax code

The tax code for nonprofits can be confusing, and tax reforms can affect everything from how you report your income to how you manage volunteers. If not reported or managed correctly, for example, some income earned by nonprofits can be taxable. And, with the passage of a new tax law in 2017, many of the rules have changed.

"Under the 2017 Tax Cuts and Jobs Act, a nonprofit can no longer aggregate the profits and losses from various trades and businesses in computing their unrelated business taxable income (UBTI)," warned Julie A. Treppa, a tax attorney and partner at [Farella, Braun and Martel LLP](#). "Be sure to segregate income and expenses from each trade or business in which it engages ... UBTI is now computed separately with respect to each trade or business."

Other changes include the valuation of certain employee benefits, which can count as taxable income if not reported properly.

"A nonprofit's UBTI includes any qualified transportation fringe benefits and on-premises athletic facilities provided to employees," said Treppa.

But, she added, proper reporting can save you from paying taxes on these benefits: "The organization can avoid the addition of these items as UBTI if it includes the cost of the benefits on its employees' form W-2."

Rick M. Smetanka, a CPA and the partner-in-charge of the audit and business advisory services group for [Haskell & White](#), advised having a professional keeping an eye on changes to the tax code so that your nonprofit can make any necessary adjustments to your policies and procedures.

"Strategize now with key advisors to understand potential impacts [of the tax law]," Smetanka said. "Nonprofits should not procrastinate and should begin preparing for this change now."

## Know the value of volunteers

Accounting for nonprofits doesn't just involve expenses and donations. You also need systems to track labor and services. Volunteers, for example, may provide unpaid labor, but that labor still has value that can affect both your taxes and overhead.

"The market value of the donated services are reportable on [tax form] 990 as program service revenue and can reduce the percentage of administrative and management costs that is directly paid for by the organization's cash contributions," said Tab Burkhalter, a CPA and tax attorney in the firm [Burkhalter & Burkhalter](#).

To ensure proper tax reporting and guarantee that you get the most value from volunteers, establish a system to track and record the work they do. Updating these records should be part of regular operations, and the tracking system should be standardized across the organization.

## Pay attention to donor activity

Donations should be something your accountant or accounting staff monitor closely. Jennifer Barnes, co-founder of financial services firm [Pro Back Office](#), has worked extensively with nonprofit organizations, and recommends following up with donors as a part of regular accounting activity.

"Sometimes the follow-through is more important than finding new donors. Track when your donors last gave and remind them that it's that time again," recommended Barnes. "A simple reminder can make a huge difference to your bottom line."

If you can, offer donors the opportunity to set up recurring monthly donations, rather than giving a single large lump sum once a year. Recurring donations require less action on the donor's part and are easier for you to track. They also provide predictable cash flow, which makes monthly budgeting easier.

Your accounting staff should also keep close track of when funds are pledged by donors, advised Smetanka.

"Pledges – or promises to pay in future periods – are required by GAAP [generally accepted accounting principles] to be recorded when received, rather than when a nonprofit actually receives the cash," he said.

## Watch your functional expenses

Eileen Gwaltney, the audit senior manager at [Wall, Einhorn & Chernitzer, P.C.](#), said one of the biggest mistakes nonprofit organizations can make is the improper allocation of functional expenses. It is important to budget enough that the organization can function and grow. However, if your functional expenses become too large, donors might hesitate to give.

"With donors focused on making the most of their contribution, it is important for nonprofits to allocate costs correctly," said Gwaltney.

The best way to do this is to make data management and analysis an integral part of your accounting process, said Maggie Tallman, the product manager at [Oracle NetSuite](#).

"Real time insight into program, operational and financial metrics is imperative in today's environment," said Tallman, who works closely with nonprofits to streamline their accounting and business operation practices. She recommends that nonprofits take a lesson from for-profit businesses and use data gathering to show funders the connection between donations and outcomes.

"Those nonprofit organizations that understand how to manage their data, and the insights and results derived from that data, are the ones that will leapfrog everyone else in donor and constituent engagement and organizational sustainability," she added.

## Track funding sources and restrictions

As a nonprofit, it is just as important to track funding that comes in as it is to track expenses that go out. This is especially true if your funding comes from grants or government agencies.

"If funds are coming from a grantor, they are required to tell you if those funds are from Federal or State sources," said Angela Kerns, a CPA and advisor at Wall, Einhorn & Chernitzer. The source of grant money can trigger different reporting requirements for tax purposes, which Kerns advised nonprofits to be careful about monitoring.

And don't forget about temporarily restricted funds. Many times, organizations meet the requirement that release these funds but don't realize it because no one is keeping track.

"Too often temporarily restricted funds are kept out of mind until cash flow needs are tight," said Adam Holcombe, the audit manager at Wall, Einhorn & Chernitzer. "Maintaining an up-to-date net asset schedule allows for management to have a better idea of what funds are available to better budget their operating needs."

## Make communication part of accounting

Donations, taxes and fund allocation are all vital parts of a nonprofit's accounting systems. But the most important part may actually be communication.

Couch recommends that staff and board members be kept up-to-date on what accountants do and discover. "Make sure you have a CPA who will walk you through all of your numbers, ensuring that you understand the profit and loss statement, the balance sheet and your cash flow statement," advised Couch. "The more knowledgeable you become, the more empowered you become to make financial decisions that will lead to your success."

This communication between accountants and decision-makers, Couch advised, is essential to creating a sustainable nonprofit. "If you don't have a CPA assisting you in this understanding, find one who will."

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