

NONPROFIT AGENDAS FEBRUARY 2009

WHEN FISCAL SPONSORSHIP IS RIGHT ...

Imagine this: A family member is afflicted with a strange new disease that no one is studying. You want to take action immediately to support a group of scientists willing to research it. But you don't have time to form your own nonprofit and build the infrastructure to run it.

You do, however, have people willing to donate to your cause. What can you do? Finding a fiscal sponsor could be the answer. A nonprofit with 501(c)(3) status can act as a fiscal sponsor for a group that hasn't obtained its own 501(c)(3) status but has a charitable project to pursue. And for many nonprofits, serving as a fiscal sponsor can be beneficial.

Agent vs. sponsor

Some relationships that portray themselves as fiscal sponsorships are merely fiscal agencies. In a fiscal *sponsorship*, the 501(c)(3) sponsor is responsible for the funds and is legally responsible for the project. The sponsor acts as a "guardian" for the donations and grants the project receives. Donations are made to the fiscal sponsor, qualifying the donors for a charitable deduction. The employees working on the project are employed by the sponsor, not the project. The project must be consistent with the sponsor's mission, and the sponsor controls the project.

In a fiscal agency arrangement, the 501(c)(3) organization is merely the project's conduit. The conduit accepts the donations and transmits them to the intended recipients. The IRS considers the donations to be made from the donors directly to the intended recipients.

The danger with a fiscal agency structure is that, if the recipient isn't a charity, the donations won't qualify for a charitable deduction. For example, if a family's house is destroyed by fire, and an individual uses a church as the fiscal agent to donate money to the family, the donation isn't deductible because the family isn't a charity.

Benefits for sponsorees

Obtaining a fiscal sponsorship can be advantageous for projects that are too small to have staff or much infrastructure for pilot projects where longevity is in question. Groups waiting to secure 501(c)(3) status, but that want to operate now, also are good candidates.

A fiscal sponsorship relationship can provide much-needed infrastructure and fiscal management to a project. By making it possible to receive charitable donations, the sponsorship can make more funds available. Associating with an established charity also can enhance the project's credibility.

Benefits for sponsors

The fiscal sponsor can gain from the relationship as well. The project can provide more exposure to that organization, possibly resulting in new funders for established programs.

Often the sponsor will charge a nominal fee for the sponsorship to offset some of its overhead costs. The project under sponsorship could give the sponsor a more competitive edge by providing a service that other similar agencies aren't providing. For example, your nonprofit may provide medical services to the underprivileged, but no organization in town offers dental services to the same group. You are approached by a group that doesn't have 501(c)(3) status, but wants to start offering dental services to the indigent. Becoming its fiscal sponsor can broaden your reach and increase your profile in attracting donations.

This example also points out an additional benefit — by becoming a fiscal sponsor, your organization can enhance its own program offerings with minimal monetary outlay.

Both parties must understand the key responsibilities in the relationship. First and foremost, the fiscal sponsor is ultimately responsible because the project and the sponsor are legally one entity. This arrangement requires proper oversight by the sponsor. See the sidebar, “Forming the relationship,” for specific factors to consider.

Just as important as these start-up considerations is the plan for terminating the relationship. This would include defining the project’s life, if desired, and determining how the project’s assets and activities will be severed from the sponsor.

A favorable union

Fiscal sponsorship can be a win-win situation for both parties involved, but the devil is in the details. The relationship must be thoughtfully designed with mutual understanding and agreement on the key factors.

Forming the relationship

The terms of the fiscal sponsorship relationship should be mutually agreed upon before the relationship begins. Some factors to consider:

- When will the relationship begin?
- How and when will the relationship be evaluated?
- Who is authorized to make decisions?
- How will disbursements be handled?
- Who will handle any reporting requirements, such as an audit and reporting to funders?
- What fee will the sponsor charge? (Up to 10% is typical.)
- What are the major business decisions that need to be made, such as staffing and insurance?

FAIR GAME

New accounting standard may affect your financial statement

If you thought the new accounting standard that requires organizations to measure assets at fair value doesn’t apply to your nonprofit, think again. It’s likely your organization will need to use it starting with your next financial statement.

Does it apply to you?

FASB Statement No. 157, *Fair Value Measurements* (SFAS No. 157), defines fair value, provides for tools to measure it and expands footnote disclosures required under Generally Accepted Accounting Principles (GAAP) in financial statements. It applies to fiscal years starting after Nov. 15, 2007, and interim periods within those fiscal years, if your nonprofit has any of the following:

- Noncash contributions,
- Financial assets held as an agent, such as cash or investments held by your organization when you agree to distribute those assets to a specified beneficiary,
- Beneficial interests in trusts,

- The contribution portion of split-interest agreements,
- Certain investments, such as the fair value of restricted stock acquired without a readily available quoted market price,
- Derivative instruments, such as interest rate swaps,
- Accounts receivable and other financial instruments, or
- Long-lived assets.

The pronouncement is delayed until fiscal years beginning after Nov. 15, 2008, for fair value measurement of most nonfinancial assets and liabilities, such as assets measured at fair value in a business combination whose fair values are not remeasured in subsequent periods.

How is “fair value” defined?

Fair value is the price that market participants would settle on to transfer an asset or liability on a particular measurement date. SFAS No. 157 dictates that fair value measurement take into account the asset's value “in-use” (if the asset is used in conjunction with other assets) or “in-exchange” (if the asset is used on a standalone basis). In addition, the fair value measurement of a liability should reflect the risk that the obligation won't be fulfilled — for example, that an entity will default on payment.

How can you value assets at fair value?

More than likely, your organization has been using valuation techniques to value assets and liabilities. If you've entered into a charitable gift annuity agreement, the present value of the liability to the donor is calculated using a discount rate at each year end. This is an example of the income approach, as defined in SFAS No. 157. The income approach is a valuation technique that takes into account current market expectations about those future amounts.

Two other techniques are the market approach and the cost approach. The market approach uses prices in market transactions for comparable assets or liabilities. This approach is similar to the way that a real estate agent compares recently sold and currently listed homes to find a market price.

The cost approach is based on the asset's current replacement cost. Think of the amount for which your engagement ring, home or car is insured. The amount that you'd receive if anything should happen to one of those assets is its current replacement cost. It takes into account wear and tear and, particularly in the case of a home, the money that you've put into it.

Of course, the appropriate valuation technique must be used. Your organization most likely uses the income approach on a continuing basis to value certain assets or liabilities due to its widespread use in the accounting community. The present value of the asset or liability is calculated using an applicable discount rate (often the risk-free rate or an applicable Treasury bill rate). Whatever the case may be, the American Institute of Certified Public Accountants' *Audit and Accounting Guide for Not-for-profit Organizations* notes that “a fair value measurement is the point within that range that is most representative of fair value in the circumstances.”

How can you prepare for the change?

SFAS No. 157 expands the required disclosures for assets and liabilities measured at fair value. As your year end audit approaches, it's time to get ready to use the new measurement. If you haven't already, you should meet with your accountants to discuss the effect of this standard on your audited financial statements. Finally, prepare your users, such as your board of directors, for the change.

NEWS FOR NONPROFITS

New Form 990: Are you prepared?

Starting with your next federal income tax returns, you'll need to take a more active role in preparing Form 990, even if your accountant handles it. You'll be gathering an abundance of information and will need to:

- **Prepare descriptions and explanations in critical areas of the form.** Expect this step to be time-consuming.
- **Make sure your board is familiar with the form.** It thrusts more responsibilities upon them, including governance-making decisions.
- **Review Part VI of the core form, which asks governance and policy questions.** Decide if your organization will adopt any of these policies, and which ones.
- **Determine from Part IV which additional schedules you'll be required to submit outside of the core form.** Note that significant emphasis is placed on compensation issues, with a major increase in informational disclosures — at a minimum, for your top management official and top financial official.
- **Understand what information is required on the statement of revenue, statement of functional expense and the balance sheet.** You may need to make changes to your general ledger.

Not all organizations are required to file the new Form 990 the first year. For 2008, nonprofits with gross receipts under \$1 million and assets under \$2.5 million can file the Form 990-EZ. For 2009, these amounts decrease to gross receipts under \$500,000 and assets under \$1.25 million. For 2010 and after, only organizations with gross receipts under \$200,000 and assets under \$500,000 may file 990-EZ. That doesn't mean you're off the hook if you come under these thresholds, though. Even Form 990-EZ filers must file new Schedules A, B, C, E, G and L if they meet the requirements outlined in the instructions for those forms.

Contact your accountant to learn how you can be ready to file an accurate form.

Model act affects endowment funds

The way you manage and disclose certain endowment funds is likely to change due to a legislative model gaining nationwide momentum. The Uniform Prudent Management of Institutional Funds Act of 2006 (UPMIFA), which already has sparked legislation in about two-thirds of the states, is likely to affect your organization if it has endowment funds with donor restrictions or board designations.

The proposed act eliminates the "historic dollar-value" rule requiring that any endowment restricted by its donors into perpetuity not fall below the amount of the original gift. The act also outlines stronger guidance for the definition of "prudence" than provided in previous guidance, suggesting that spending more than 7% of an endowment in any one year is not a prudent decision. This recommendation hasn't been included in all states where the act has been legislated.

UPMIFA also makes it easier for charities to identify new uses for older and smaller endowments that may be dedicated to obsolete or impractical purposes.

The act is likely to affect the way endowment funds are disclosed in your financial statements. For example, you will be required to detail the restrictions on your investments and how the amount that is spendable each year is calculated.

As the act becomes the national norm, you can expect to see changes in the standard of care required of those who manage endowments. Increased public confidence should follow.

SPOTLIGHT ON MP&S

The New Form 990 continues to spark interest in the industry. On January 14, 2009, **Michael L. McNee** and **Robert Lyons** of the Marks Paneth & Shron LLP Nonprofit and Government Services Group presented on the New 990 at the Foundation for Accounting Education (FAE) "31st Annual Nonprofit Conference" in New York City. In addition, Mike and Rob served on the FAE event's "Ask the Experts Panel."

While the New Form 990 certainly remains at the forefront in the nonprofit industry, various economic issues continue to be top of focus for many of our peers in the New Year. You'll likely have already received the communication the MP&S **Nonprofit and Government Services Group** sent on behalf of **Michael Bekas**, partner in the MP&S Tax Group, about his white paper on tax vehicles known as "Charitable Remainder Unitrusts" (CRUTS) and how nonprofit institutions can apply CRUTS in their own donor relations programs — particularly in the current economic environment. A copy of the paper can be found at www.markspaneth.com.

Finally, the MP&S Nonprofit and Government Group continues to contribute to the academic health of our industry. **Warren Ruppel** was recognized by *The CPA Journal* for his participation in the publication's Editorial Review Board and evaluation of manuscripts submitted during the past New York State Society of Certified Public Accountants (NYSSCPA) fiscal year (June 1, 2007, through May 31, 2008.)

MP&S WELCOMES THESE NEW CLIENTS

- Richmond Community Services, Inc.
- Girls Incorporated
- Hebrew Academy of Nassau County

MP&S FAST FACTS

- Nationally, among the top 30 largest accounting firms and a leader in accounting and auditing (*Accounting Today*)
- The New York Area's 15th largest accounting firm and one of the five fastest growing firms in our market (*Crain's New York Business*)

FOR FURTHER INFORMATION

If you have any questions, please contact **Michael L. McNee, CPA, Partner-in-Charge** of the Nonprofit and Government Services Group, at 212.503.8954 or mmcnee@markspaneth.com or one of the following members of the group:

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In addition, more information on the MP&S Nonprofit and Government Services Group can be found at www.markspaneth.com.

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