Managing and Accounting for Alternative Investments

patrick MILLER

In an effort to maximize returns on investments while diversifying their portfolios, many non-profit organizations are investing in assets without readily determinable fair values, or "alternative investments". Examples of alternative investments include hedge funds (most common), private equity funds, venture capital funds, derivatives, natural resources and real estate funds.

As these types of investments do not have a readily determinable fair value, the guidance furnished in SFAS 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations* cannot be applied. Instead, non-profits may use the guidance provided in Appendix A to Chapter 8 of the AICPA Audit and Accounting Guide, *Not-for-Profit Organizations* for measuring these alternative investments. The Appendix discusses the evaluation of these investments to determine whether the investments should be recorded at cost, under the equity method, or in accordance with SFAS 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others.*

To assist auditors with performing their work on these alternative investments, the AICPA released a practice aid, *Alternative Investments – Audit Considerations* (Practice Aid). While designed for auditors, non-profit organizations would benefit from reading this Practice Aid. Appendix 2 to the Practice Aid includes information on controls a non-profit organization may choose to implement for evaluating potential alternative investments, monitoring their performance, and properly reporting on them in the organization's financial statements. Documentation of the controls and procedures adopted in each of these three areas will lend itself to an investment policy for your alternative investments, and assist your auditors with evaluating and testing those controls.

While alternative investments may be a creative way to seek higher returns on investment dollars and/or to diversify a portfolio, non-profit organizations need to consider the additional time and processes required to properly evaluate, monitor and report on these investments.

For additional information, please contact Pat Miller.

Did you know?

On June 5, 2007 the La Salle Nonprofit Center presented a full-day Nonprofit Strategies Forum with an in-depth look at a major area of interest in the non-profit and tax-exempt world. This year's Forum was titled "Managing Change Before It Manages You: Evolution, Revolution, and Transition in the Nonprofit Sector."

From marketing and communications to fundraising, to human resources on a shoestring, and beyond, participants were joined together by their desire to explore and learn from a slate of experts.

THE NONPROFIT CENTER
La Salle University

Sample of Targeted Strategy Sessions:

- Overcoming resistance to change
- Developing your nonprofit's brand
- Dealing with leadership change
- Navigating new technology
- Personal career development
- Managing internal change for success
- Evaluating the virtues of mergers, acquisitions & organizational restructuring
- Riding the financial roller coaster
- Fundraising in a changing environment

...and more

For details, please visit www.lasallenonprofitcenter.org.

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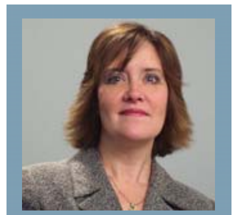
News Updates for Non-Profit and Tax-Exempt Organizations

NP Advisor

2007 Volume I

Highlights

New Law Revises EO Tax Rules



bernadette CHIOCCO

The name is deceiving, but the Pension Protection Act of 2006 contains numerous changes to the tax law provisions affecting exempt organizations (EO).

Key provisions of the legislation include the following:

- Controlling organizations must report income from and loans to controlled organizations as well as transfers between controlled and controlling organizations. This provision is effective for returns due (without regard to extensions) after the date of enactment (August 17, 2006).
- Section 501(c)(3) organizations that file unrelated business income tax returns (Form 990-T) must now make them available for public inspection. Along with Form 990, this provision is effective for returns filed after the date of enactment.
- Private foundation and excess benefit penalty excise taxes are doubled.
- Donor advised funds, supporting organizations, and credit counseling organizations are subject to new requirements.
- Applicable exempt organizations are subject to new reporting requirements when they acquire life insurance contracts that are structured to give both the exempt organization and private investors an interest in the contract. For purposes of this reporting requirement, applicable exempt organizations include governmental organizations (including Indian Tribal Governments) and employee stock ownership plans.
- Individual Retirement Account (IRA) owners age 70 ½ or older are permitted to directly transfer tax-free, up to $100,000 per year to an eligible charity.
- Charitable contribution deductions for food, book, and certain conservation property are increased.
- Charitable contribution deductions for monetary donations, certain easements, taxidermy property, clothing and household goods, and certain other items are limited.
- Beginning in 2008, exempt organizations with gross receipts under $25,000 must file an annual notice with the IRS.

For more information, please contact Bernadette Chiocco.

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Pennsylvania Solicitation Act Amended

robin
FRITZ

The Pennsylvania Solicitation of Funds for Charitable Purposes Act (Act), 10 P. S. § 162.1 et seq., has been amended to increase the review and audit thresholds for **all charitable organizations**. The new thresholds apply to **financial reports covering fiscal years which conclude after December 26, 2006,** the effective date of the new thresholds.

The purpose of the Act is not only to require the proper registration of charitable organizations, professional fundraisers, and professional solicitors, but also to protect the public by requiring full public disclosure of the identity of those soliciting contributions, the purpose for soliciting those contributions, and the manner in which they are actually used.

In carrying out this purpose, the Act sets certain thresholds with respect to the amount of gross contributions a charitable organization may have solicited to determine the level of reporting required. Overall, the new thresholds have been increased thereby giving some smaller organizations a break on the level of reporting that will be required with their filing to the state of Pennsylvania. The new thresholds are outlined in the following chart:

Gross Contributions	**Type of Financial Statements Required**
Less than $50,000	Internally Prepared
	*Compiled, Reviewed, or Audited (Optional)
$50,000 to less than $100,000	Compiled, Reviewed, or Audited
$100,000 to less than $300,000	Reviewed or Audited
$300,000 and over	Audited

**The fiscal year ending 12/31/06 is the first fiscal year the new thresholds apply.*

For more information, please contact Robin Fritz.

New AICPA Pronouncements – Not Just Your Auditor's Problem

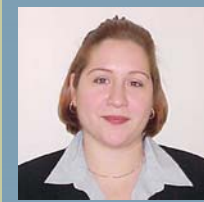
elizabeth
PILACIK

The American Institute of Certified Public Accountants concluded an exceptionally busy 2006 in which they issued eleven new Statements on Auditing Standards (SASs). While under normal circumstances, a new SAS would only cause your auditor headaches, some of the new SASs will directly affect you, the client. The impact will be felt throughout the duration of audits and can result in additional audit-related documents and fees.

These new standards will require auditors to expand documentation and testing of the auditee's internal controls, requiring more time and expense in these areas. Inquiries and observations will have to be performed and thoroughly documented in order to mitigate potential audit risks. Also, these new standards require the auditors to convey to management and those charged with governance whether there are "significant deficiencies and material weaknesses identified in the audit." These new terms might cause a strain on the auditor-auditee relationship, since certain aspects of the audit, such as auditor-proposed journal entries and auditor assistance in preparing the financial statements, will have to be evaluated to assess whether or not a "significant deficiency" or "material weakness" exists.

Please contact Elizabeth Pilacik or Pat Miller for more information.

Classification of Certain Revenue and Expenses on Form 990



jennifer
SILVAN

It has become increasingly important for non-profit and tax-exempt organizations to properly reflect items of revenue and expense on their annual filing of their Form 990, 990-EZ or 990-PF. An improperly completed return can affect both an entity's exempt status as well as potential donations. This can be an area of confusion for many organizations, specifically in identifying the differences between contributions, revenues from special events, and membership dues.

Fundraising activities relate to soliciting and receiving contributions. However, special fundraising activities such as dinners, door-to-door sales of merchandise, carnivals, and bingo games can produce both contributions and revenue that are considered a *special event*.

If a buyer at such a special event pays more for goods or services than their retail value, the excess amount is considered a contribution. The retail value is generally not the amount that the organization paid for the goods or services provided, rather it is the fair market value that would be paid by the general public. This situation usually occurs when an organization seeks public support through solicitation programs that are in part special events or activities and are in part solicitations for contributions. The primary purpose of such solicitations is to receive contributions and not to sell the merchandise at its retail value even though this might produce a profit.

If an organization offers goods or services of only nominal value through a special event or distributes free, unordered, low-cost items to patrons, the entire amount received for such benefits is reported as a contribution.

In addition, any membership dues or assessments that exceed the value of available membership benefits are also considered contributions.

Lastly, it is important to note that all expenses of raising contributions must be reported separately as *fundraising expenses*. These would include even those costs viewed as incidental such as postage, supplies or even the salaries of staff who are stuffing envelopes for mailers.

Filing an accurate and complete return is essential to non-profit and tax-exempt organizations as this is often one of the first things that donors see with regards to your organization, its goals and its needs. Your return can leave a lasting impression on a potential donor and can be the deciding factor for many in choosing to whom they wish to contribute. Any questions regarding the classification of certain revenues and expenses should be directed to your tax representative. Proper evaluation of these items will ensure that the filing requirements of your organization are met. For more information on this article, please contact Jennifer Silvan.

For information on our Not-for-profit Financial Professionals Group, please visit:

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Using Your 990 as a Marketing Tool

patrick
MILLER

The combination of the internet and the publication of the IRS Form 990 (via www.guidestar.org), the annual information return for a non-profit organization has changed from an annual deadline with no tangible benefits to a marketing prospect, free of any additional advertising costs. While the change has definitely increased the time associated with the completion of the 990, the potential value of this investment could be priceless to your organization.

Foundations use 990s to prescreen organizations they invite to submit requests for funding. Major donors utilize the 990s to research for potential new beneficiaries. Taxing authorities (Federal and state) use the 990s to monitor tax compliance. Media outlets use the returns as a main source of background information on a particular non-profit organization. Many agencies, organizations and individuals are already reviewing your 990. The question is: what are they focusing on?

While many areas are read by these users, certain sections are examined more thoroughly than others. Executive compensation, compensation of board members, and payments to independent contractors are all areas that are evaluated for fiscal responsibility and reasonableness. However, in order to fully employ the marketing potential of the 990, there are two key areas that are more heavily scrutinized by granting or donating organizations: Part II – Statement of Functional Expenses, and Part III – Statement of Program Service Accomplishments.

Part II – Statement of Functional Expenses requires that the organization report expenses by function: Program, Administrative or Fundraising. The average non-profit has the administrative and fundraising functions accounting for about 30% of overall expenses. However, organizations historically under-report fundraising expenses for fear of how the spending will be perceived by an outside party. While this is common practice, the number one complaint by oversight agencies, watchdog groups and the media is that non-profits misrepresent fundraising costs. Examples of common practices are:

- Not properly allocating personnel expense based on actual time spent on fundraising activities
- Materials (hand-outs, pamphlets, etc), postage and other costs utilized
- Netting of fundraising costs against profits

Part III – Statement of Program Service Accomplishments is a section of the return that does not particularly enable the filer to explain the achievements of the organization related to its mission. Typically, an overall description is inserted and the next inquiry is addressed. No where in the directions does it state that a supplemental schedule for this section may not be included. Take advantage of that and draft a schedule highlighting not only the mission, but what significant accomplishments had been achieved during the year and what may lie on the horizon going forward. Here is where it is encouraged to enlist the assistance of your marketing department to maximize the promotional potential of this section.

For additional information, please contact Pat Miller.