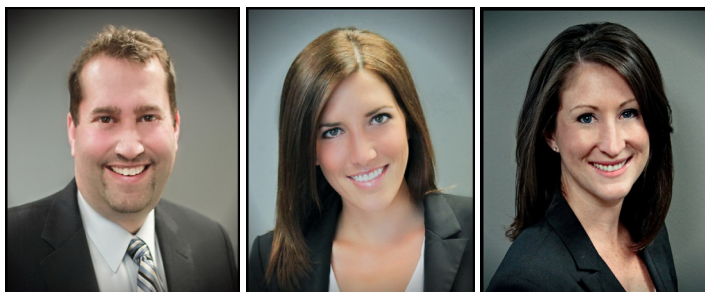




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## YH ADVISORS IS PROUD TO PUBLISH AND DISTRIBUTE THE YH EXEMPT ORG ADVISOR A QUARTERLY PUBLICATION FOCUSED EXCLUSIVELY ON THE TAX, LEGAL AND ACCOUNTING ISSUES OF ALL DIFFERENT TYPES OF EXEMPT ORGANIZATIONS.



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**YH Advisors, located in Huntington Beach, California, is solely focused on addressing the tax, legal and accounting needs and issues of exempt organizations.** The firm's Partners, Brian Yacker and Lauren Haverlock, have cumulatively consulted with exempt organizations for over 30 years.

The YH Exempt Org Advisor is electronically available on a complimentary basis to anyone who is included in our e-mail database. If you happen to be forwarded a copy of this publication and would like to receive future copies, please contact us with your e-mail address at [info@yhadvisors.com](mailto:info@yhadvisors.com).

### in this issue:

ripped from the eo headlines | 2

The latest news from the EO sector

focus on IRS TE/GE division | 2

News and updates from the Exempt Organization division of the IRS

charitable solicitation scoreboard | 5

Latest on state charitable solicitation registrations

YH case study | 5

What should an exempt organization do if it has problematic bylaws?

YH quick tips | 6

Quick tips and guidance on some of the issues often faced by EO practitioners and exempt entities

YH timely guidance | 6

Undertaking a governance check-up

YH accounting + audit | 7

Bookkeeping tips and guidance on structuring the chart of accounts for an exempt organization

YH resources, news & updates | 8

## Ripped from the EO Headlines

charity board members:  
be afraid, be very afraid

Over the past number of years, Board members of charitable organizations (even those serving on a volunteer basis) have been under an ever-increasing amount of scrutiny from the Internal Revenue Service, state Attorneys General and the media. One of the byproducts of this heightened scrutiny is that more Board members are being found to have breached their legal oversight and governance duties owed to the charitable organization, and accordingly, are being monetarily fined. The following case is an unfortunate illustration of just that.

Relatively recently, a federal jury awarded the unsecured creditors of the former Lemington Home for the Aged ("Lemington") \$5.75 million in damages. The jury arrived at this award after being presented with compelling evidence that former Administrator of Lemington, the former Chief Financial Officer, and the Board of Directors drove Lemington into bankruptcy through their actions and inactions. Lemington, which was founded in 1883, was the oldest African-American sponsored nursing home until it closed its doors in 2005. The jury award of \$5.75 million to be paid to the creditors of the charitable organization was allocated amongst the Administrator, Chief Financial Officer and 13 of the 15 Board of Directors members.

telemarketers gone wild

In late February of 2014, the Wall Street Journal reported that in 2012, for every \$1 raised for charity by professional fundraisers (specifically telemarketers) operating in New York, such paid telemarketers kept 62 cents on average, according to a report by the New York Attorney General's Charities Bureau. According to the Wall Street Journal, the annual "Pennies for Charity" fundraising report showed telemarketing firms raised a record \$249.3 million in 2012, the latest year that data was available, however, in 459 of

the 589 campaigns, charities could only keep less than half of the money raised (such charities ranged from Amnesty International to the Port Washington Police Benevolent Association).

Fundraising firms contracted by charitable organizations and working in New York must file financial reports with the office of Attorney General in New York. Telemarketing done by a charity isn't included in the report. The reasoning behind this legal requirement is that it is important for New Yorkers to know how much of their money will pay telemarketers' salaries and costs.

The "Pennies for Charity" report has served as the basis for investigations into paid telemarketers that repeatedly raised little or no money, yet charged high fees. In 2012, for example, 91 campaigns netted more for the telemarketers than for a charity. In 80% of campaigns, charitable organizations either lost money or retained less than half of what was raised. Despite the high fees, it is likely that charities use paid telemarketing mainly to expand their donor bases.

Please do not hesitate to contact Brian Yacker at 310-982-2803 or at [byacker@yhadvisors.com](mailto:byacker@yhadvisors.com) if you have any questions regarding the foregoing or if you need any additional information whatsoever regarding the exempt organization tax, legal and accounting services which YH Advisors provides.

## Focus on the IRS TE/GE Division

streamlined form 1023-ez

As has been addressed in prior editions of the **YH Exempt Org Advisor**, because of a perfect storm of various circumstances (the §501(c)(4) political targeting fiasco / the retroactive reinstatement requests of organizations whose tax-exemptions were automatically revoked / personnel changes within TE/GE), a tremendous backlog of Tax Exemption Applications has developed within IRS Determinations in Cincinnati. As of April of 2014, Sunita Lough, the Commissioner of TE/GE at the Internal Revenue Service,

CONTINUED ON PAGE 3

reported that the Internal Revenue Service was receiving approximately 5,000 more Tax Exemption Applications each month than they can review and make a final determination.

One of the solutions which the Internal Revenue Service has identified for this backlog problem is the introduction of the proposed Form 1023-EZ. The proposed Form 1023-EZ, which is still in draft form, is a greatly streamlined version of the Form 1023. In essence, the Form 1023-EZ as it is currently drafted, would take significantly less time to complete (and hence for the Internal Revenue Service to review) than the current version of the Form 1023. As is contemplated by the Internal Revenue Service, the Form 1023-EZ could only be filed by the following organizations:

- Those with projected annual gross receipts expected to be below \$200,000 in any of the next three years or has had annual gross receipts below \$200,000 in both of the past two years
- Those with total gross assets of less than \$500,000
- Not a foreign organization
- Not an organization that is a successor to, or controlled by, an entity suspended under 501(p)
- Not a limited liability company
- Not a successor to a for-profit entity
- Not a previously revoked organization or a successor to a previously revoked organization (other than automatic revocation for failure to file Form 990)
- Those entities not considered to be churches, schools, hospitals, or supporting organizations.

As of publication, the Internal Revenue Service was still seeking comments regarding the Form 1023-EZ. The majority of comments which we have reviewed have been critical of the introduction of the Form 1023-EZ from the perspective it will remove necessary barriers to entry for smaller exempt organizations, thus leading to an eventual glut of smaller exempt organizations not prepared or willing to operate the organization in the manner that such should be operated.

### 2013 changes to the form 990

Ever since the massive overhaul of the Form 990 first effective for the 2008 tax year, the Internal Revenue Service has not annually made very many significant revisions to the Form 990 core form or the 16 different Schedules. The Form 990 for the 2013 tax year is no different in that regard. As you can see from the following revisions / clarifications made by the Internal Revenue Service related to the 2013 version of the Form 990, there is really nothing of significance that a Form 990 preparer/reviewer should note:

- The Form 990 General Instructions clarify that a short period return cannot be filed electronically unless it is an initial or final return for which the "Initial return" or "Final return" box is checked in Item B of the Heading.
- The Form 990 Heading Instructions clarify what documentation must be attached to Form 990 to support a name change.
- The Instructions for Part IV, Line 25b clarify when an organization needs to answer "Yes" to report it learned of an excess benefit transaction with a disqualified person in a prior year.
- The Part VI, Line 3 Instructions clarify what compensation from a management company to interested persons should be reported on Schedule O.
- The Instructions for Part VIII, Line 1 clarify that discounts on services rendered to a charity cannot be reported as contributions revenue.
- The Schedule F Instructions no longer require that filers explain how they estimate the number of recipients reported on Part III, column (c) and they clarify that Forms 3520, 3520-A and 5713 should not be attached to Form 990.
- The Schedule I Instructions provide new definitions of domestic organizations, domestic governments and domestic individuals.
- The Schedule L Instructions explain when a foreign organization may be treated as a 501(c)(3) charity for purposes of the Schedule L, Part IV reporting exceptions.

CONTINUED ON PAGE 4

- The Form 990 Glossary clarifies that “contributions” include neither donations of services nor discounts provided on sales of goods in the ordinary course of business.
- The Form 990 Glossary now includes a new definition of “domestic individual.”

Additionally, within the past couple of weeks, the Internal Revenue Service has released a draft of the 2014 version of the Form 990 core form and our review of such indicates no substantial revisions / clarifications there either.

## IRS releases dirty dozen tax scams for 2014

As is their custom in recent memory, the Internal Revenue Service issued their listing of the Dirty Dozen Tax Scams for 2014. And similar to the past number of years, an entry on this listing was especially pertinent to the exempt organization sector. In particular, an entry on the Dirty Dozen Tax Scams for 2014 was the following:

**Impersonation of charitable organizations.** Taxpayers need to be sure they donate to recognized charities. Following major disasters, it’s common for scam artists to impersonate charities to get money or personal information from well-intentioned people. They may even directly contact disaster victims and claim to be working with the IRS to help the victims file casualty loss claims and get tax refunds.

## summary of recent eo plrs

**PLR 201415003** – The Internal Revenue Service revoked the tax-exemption of an organization because of a failure to prove that they furthered exempt purposes. The organization in question here was organized to conduct certain kinds of games (Motto) to raise funds to make an insubstantial amount of grants to other charities.

**PLR 201403018** – Organization devoted to Talmudic scholarship denied tax-exemption on the basis of private inurement and the lack of adequate internal controls and proper recordkeeping (to substantiate that grants made by the organization were in furtherance of their stated exempt purposes).

**PLR 201403017** – Organization’s application for tax-exemption was denied by the Internal Revenue Service because of the fact that the entity’s operations were deemed too commercial from an Internal Revenue Service perspective (fees charged by the applicant were not discounted and the applicant did not focus solely on providing their services to a charitable class.)

**PLR 201404012** – Applicant was denied recognition of tax-exemption by the Internal Revenue Service because of the organization’s Tax Exemption Application containing a variety of ambiguities and contradictions. For example, the Internal Revenue Service obtained no clear description of the exempt purpose activities of the applicant on Part IV of the Form 1023.

**PLR 201404013** – Locally-owned grocery store was denied recognition of tax-exemption by the Internal Revenue Service because of several reasons, including that there were deficiencies in their Tax Exemption Application, there was more than incidental private benefit and the applicant was proposed to be operated in a manner too commercial from an Internal Revenue Service perspective.

Please do not hesitate to contact Brian Yacker at 310-982-2803 or at [byacker@yhadvisors.com](mailto:byacker@yhadvisors.com) if you have any questions regarding recent IRS activities in the exempt organizations sector.



## Charitable Solicitation Registration Scoreboard

Within the past couple of months, there has been a significant amount of news on the state charitable solicitation registration front.

**Florida** – it has been recently proposed by the legislature in Florida to significantly “tighten” the Sunshine State’s charitable solicitation regulations. Specifically, it is currently proposed that nonprofit employees and paid solicitors who have violated certain rules in other states would be barred from soliciting funds in Florida, professional solicitors must submit to background checks and fingerprinting, telephone scripts of telemarketers would have to be reviewed for accuracy and honesty, charities generating more than \$500,000 per year must submit reviewed financial statements, those bringing in more than \$1 million annually must provide audited financial statements, and charities earning more than \$1 million per year and spending over 75 percent on administration and other overhead expenses must provide a list of Board members and family relationships of the Board and staff.

**Massachusetts** – during a presentation at the recent Georgetown Law Exempt Organization Legal Conference, a representative from the Massachusetts Attorney General’s office revealed that they are going after a professional fundraiser operating in Massachusetts because of the fact that such professional fundraiser is not appropriately registered with the Massachusetts Attorney General and there have been allegations that the fundraiser has been making inaccurate statements during their solicitations in Massachusetts.

## YH Case Study

### problematic bylaws

Unfortunately, often, we come across exempt organizations, big and small, across all different types of exempt organizations, that have significant issues with their Bylaws, including the following:

- The exempt organization never had Bylaws drafted.
- The exempt organization cannot locate a copy of their Bylaws.
- The exempt organization’s Bylaws were not customized for an exempt organization in general or for their particular tax-exempt entity in particular.
- The exempt organization is not familiar with their Bylaws, and hence, does not follow them in practice.
- The exempt organization is familiar with their Bylaws, but nevertheless, does not follow them in practice.
- The exempt organization has not updated / amended their Bylaws in quite a long time.
- The exempt organization’s Bylaws contradict their other governing documents.
- The exempt organization thinks that they amended their Bylaws, but they do not know for sure.

That being said, please find following tips/guidance to avoid some of the pitfalls identified immediately above:

- Make certain that the drafter of the exempt organization’s Bylaws possesses a proper understanding of state exempt organization laws.
- Verify that the provisions of the exempt organization’s Bylaws are compared and reconciled to the other governing documents of the exempt organization.
- Consider updating Bylaws at least every 3-5 years.
- Do not to get too detailed when drafting the exempt organization’s Bylaws.
- Ensure that the exempt organization’s Bylaws can be rather easily amended, if necessary.
- Validate that the exempt organization’s Bylaws are not just a boilerplate template; they should be customized to the particular exempt organization.

Please do not hesitate to contact Brian Yacker at 310-982-2803 or at [byacker@yhadvors.com](mailto:byacker@yhadvors.com) if you have any questions regarding the Bylaws of an exempt organization.



## YH Quick Tips

### creating a donation policy

Most exempt organizations will gratefully accept non-cash contributions and donations from their donors. But what if a donor wishes to donate a non-cash item that may not be of great use or value to the exempt organization? Or what if the cost of obtaining or maintaining such a donation outweighs its benefits? Having a gift acceptance policy addressing the who, what, when, where and how contributions or donations can be accepted and utilized by an exempt organization will help ensure that the exempt organization does not accept a non-cash contribution that could be an overall detriment to the charitable organization.

Please find following a brief set of questions to assist a charitable organization in drafting and creating an effective gift acceptance policy (from an accounting perspective):

- Who is responsible within the charitable organization for sending charitable contribution acknowledgements to donors?
- Will a contribution be accepted if such does not advance the mission, goals and objectives of the exempt organization?
- When non-cash contributions are donated to the exempt organization, who will be responsible for valuation of such for internal accounting purposes? Do remember not to note a value for non-cash items when preparing a charitable contribution acknowledgement for a non-cash contribution received by the charitable organization.
- When securities are donated to an exempt organization, is a pre-designated account set up to receive them?

Please do not hesitate to contact Stacey Bergman at (310) 982-2805 or [sbergman@yhadvisors.com](mailto:sbergman@yhadvisors.com) if you have any questions regarding the foregoing or if you need any additional information whatsoever regarding the exempt organization accounting services which YH Advisors provides.

## YH Timely Guidance

### governance check-up

Since the Internal Revenue Service and state regulators have increasingly focused their scrutiny upon whether exempt organizations, particularly charities, are well-governed, we have seen a corresponding increase in the Governance Check-Up engagements which we conduct for our clients. One of the key elements in the Governance Check-Ups which we conduct is reviewing the following documents/information of the exempt organization to ensure that the exempt organizations is compliant from a governance perspective:

- Articles of Incorporation (including any amendments to such)
- Most recent version of the organization's Bylaws
- Tax Exemption Application (if applicable)
- Determination Letter
- Board of Directors minutes for the past year (including any Board Committees)
- Audited financial statements for the past three years
- Form 990 / Form 990-T for the past three years
- Any filings made with the state Attorney General (e.g. solicitation documents / raffle registrations)
- Any correspondence / communications with the Internal Revenue Service and the state Attorney General
- Written policy documents (e.g. conflict of interest policy)
- Any contracts with fundraisers
- Loan documents
- Insurance documents

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## YH EO Practical Bookkeeping Guidance

### tracking matching grants

Charitable organizations often receive matching contributions or grants. Accounting for such contributions does not differ from that of “regular” grants or contributions. However, tracking matching grants and the associated contribution can be tricky for charitable organizations using “off the shelf” accounting software. Most pre-packaged accounting software for exempt organizations has a “Ship Via” section on an invoice or donation acknowledgement. Utilizing this input to track the donor for whom funds are being matched will allow a charitable organization to produce reports necessary to monitor matching contributions.

## YH EO Accounting Spotlight

### streamlined chart of accounts

A Chart of Accounts is the bedrock of an exempt organization’s accounting infrastructure and paves the way for transparent financial reporting. A cluttered and cumbersome Chart of Accounts significantly lessens the transparency of financial records and increases a perpetrator’s chances of fraudulent behavior going unnoticed. Conversely, a concise and well organized Chart of Accounts lends for greater transparency to the readers/users of an exempt organization’s financial statements.

When creating or updating a Chart of Accounts, ensure that all existing accounts have a purpose beyond a single transaction. Creating a new account for every miniscule charge will lead to a bulky Chart of Accounts that lacks value. Accounts should be created based on the need of the exempt organization to summarize amounts spent in that natural category. It is equally important that an exempt organization not combine varying charges into a few accounts in a means to keep a Chart of Accounts concise. Revenue, expense, asset and liability accounts should detail out the nature of the transactions being recorded to those accounts.

Utilizing sub-accounts is a good way to summarize related

accounts. For instance, many exempt organizations track contributions from individuals, corporations, foundations, and so on. By creating an account entitled “Contributions”, an exempt organization could then create sub-accounts to capture contributions made by each of the different donor types. This allows a Chart of Accounts to remain concise, while still offering a financial statement reader valuable insight into the nature of the contributions received.

Pre-packaged “off the shelf” accounting software often comes with a template Chart of Accounts. Included in these are accounts such as “Suspense” or “Ask My Accountant”. Using vague account titles such as those adds no value to an accounting infrastructure and only tells the reader of the financial statements that the preparer does not understand what is going on within the exempt organization’s books and records. It is recommended these accounts be eliminated from the Chart of Accounts.

Exempt organizations often find it useful to track revenue and expenses within a class structure and most accounting software typically has this feature built in. This allows an organization to note whether revenues and expenses were incurred for programmatic purposes, general and administrative or for fundraising. Using a class structure is valuable as it can save time when preparing both the Form 990 and the Statement of Functional Expenses in financial statements. Having a Statement of Activities available by class can also offer valuable insight to an exempt organization’s upper management in determining how funds are being earned and used. It is recommended that, if using a class structure, the classes do not duplicate any of the accounts in the natural revenue and expense categories.

From a Form 990 reporting perspective, the only classes considered necessary are a total program service class, general and administrative and fundraising. However, from an internal financial reporting framework perspective, it’s helpful to have classes for major programs or major fundraising events. Once a streamlined Chart of Accounts has been created, management should review it regularly to ensure the accounts and classes remain appropriate through organizational changes.

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## YH EO Resource Alert

This is a relatively new regular feature of the YH Exempt Org Advisor which will highlight different exempt organization resources which are free of charge in the public domain.

This quarter we are highlighting the slides from two recent Internal Revenue Service exempt organization phone forums. First up are the presentation materials from an Internal Revenue Service presentation titled, "Stay Exempt! A Guide for Charitable Organizations with Changing Leadership".

[http://www.irs.gov/PUP/charities/charitable/StayExempt\\_PhoneForum\\_Slides\\_v2.pdf](http://www.irs.gov/PUP/charities/charitable/StayExempt_PhoneForum_Slides_v2.pdf)

Second, are the presentation materials from an Internal Revenue Service presentation titled, "Good Governance Makes Sense for Exempt Organizations".

<http://www.irs.gov/PUP/charities/Governance%20Phone%20Forum%20Q&A%20FINAL.pdf>

## YH Presentations

Please find following a listing of the presentations which YH Advisors has presented, or will present, during the March 2014 – July 2014 time period. Please do not hesitate to contact us for more information if you have interest in receiving the presentation materials or attending any of the upcoming presentations.

Mar 25, 2014	Internal Controls for Exempt Orgs (LBNP), Long Beach, CA
Apr 26, 2014	Tax Issues for §501(c)(6) Organizations (Bar Asso'n), Long Beach, CA
Apr 29, 2014	Fundraising Legal Issues (OneOC), Orange County, CA
May 15, 2014	Nuts & Bolts of Exempt Organizations (NV Legal Society), Las Vegas, NV
May 16, 2014	EO Workshop (NV Legal Society), Las Vegas, NV
May 19-20, 2014	Exempt Organization Tax Update (Texas CPA Society), Dallas, TX

June 18, 2014	Financial Hot Buttons for EOs (SD Planned Giving), San Diego, CA
July 9, 2014	Form 990 Overview (CA Board of Equalization), San Diego, CA
July 14, 2014	Form 990 Overview (CA Board of Equalization), Fullerton, CA

## Upcoming Webinars

YH Advisors will continue to periodically conduct (about 8 times per year) 100-200 minute interactive technical webinars focusing on the tax, legal and accounting issues most relevant to exempt organizations. Please find following our upcoming YH Webinar schedule (please be aware that this is of course subject to change):

July 8, 2014	Tour of the Form 990 Core Form
July 15, 2014	Form 990: The Schedules
July 22, 2014	Form 990-PF Tax Primer
July 29, 2014	Private Foundation Excise Taxes

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***The Summer 2014 edition of the YH Exempt Org Advisor will be published after the busy August 15, 2014 exempt organization information tax return filing deadline.***