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Nonprofit Financial Reporting and Tax-Exempt Compliance Assessment Tool

The following is an assessment tool created by Exponentum™, a national network of business law pro bono providers. The purpose of the assessment is to provide a tool that an attorney can use to determine whether a not-for-profit corporation is complying with state law and IRS requirements. This tool discusses the basic requirements with respect to the organization's governance documents, with a focus on financial transparency, fiscal management and whether the organization generally meets its legal requirements for operating a nonprofit organization as well as best financial governance practices.

After you have had a chance to review the questions below, the nonprofit organization can begin to develop a plan of action to correct any areas where it is not in compliance with the law or good governance standards. Depending on the organization's mission and location, it may be able to access additional help from a member of Exponentum.

Name of Nonprofit Organization	

Names and Contact Information for Pro Bono Attorneys			
Attorney 1 Name:			
Phone:		Email:	
Attorney 2 Name:			
Phone:		Email:	
Attorney 3 Name:			
Phone:		Email:	

The information contained in this document is not intended to constitute legal advice and should not be used as legal advice. Nonprofits should not use this without the help of a lawyer familiar with financial reporting and other corporate governance issues.

SECTION 1: FILING	YES	NO	UNSURE	EXPLANATION
1) Does your organization file the appropriate Form 990 annually with the IRS?				If the organization has gross receipts (which generally means all amounts received from all sources) of $50,000 or less annually, you should file Form 990-N (the e-Postcard) electronically. If you have gross receipts less than $200,000 and total assets at the end of the year less than $500,000, you're eligible to file Form 990-EZ. If you don't qualify for either Form 990-N or 990-EZ, you must file Form 990. Note that the Form 990 must be filed by the 15th day of the 5th month following the end of the organization's fiscal year.
2) Are your organization's Form 1023 and last three years of Form 990 or 990-EZ on file at your organization's main office?				An exempt organization must make available for public inspection its exemption application and annual returns for a three-year period beginning with the due date of the return. Note that if the organization has government contracts, its obligation to retain those records may be longer (e.g., 7 years).
3a) Is your organization fiscally sponsored (or does it fiscally sponsor another organization or program)?				A fiscal sponsorship is an arrangement between an organization that is exempt under 501(c)(3) of the IRC and an organization that has not yet achieved tax exempt status. The "fiscal sponsor," provides fiduciary oversight, financial management, and other administrative services to the sponsored organization. While widely used, fiscal sponsorship does not appear in the IRC. However, in a 1968 ruling, the IRS stated, "An organization will *not* jeopardize its exemption under section 501(c)(3) of the Code, even though it distributes funds to nonexempt organizations, *provided it retains control and discretion over use of the funds* for section 501(c)(3) purposes. IRS Rev. Rul. 68-489, 1968-2 C.B. 210 (1968) (emphasis added).
3b) If yes to either question above, has a lawyer reviewed the related fiscal sponsorship agreement(s)?				

SECTION 1: FILING	YES	NO	UNSURE	EXPLANATION
4) Is your organization registered with the appropriate authorities in all states where it solicits donations and where registration is required?				Many states have laws regarding charitable solicitation. Generally, these laws require a nonprofit to: (1) register with a state's Attorney General prior to conducting any solicitation activities in that state, and (2) make annual financial reports to the state. It is important to understand the charitable solicitation laws in any state in which a nonprofit intends to solicit donations, in order to determine whether the organization is required to register and report in that state. For more on this topic, please see the National Council of Nonprofits' resources on fundraising regulation at https://www.councilofnonprofits.org/tools-resources/charitable-solicitation-registration
5a) Does your organization hire any fundraising consultants (or professional fundraisers or fundraising solicitors) to advise on or assist with fundraising activities? (Note: this question relates only to the use of paid consultants. Bona fide employees, your board members, and volunteers who raise money for your organization would not fall within this category.)				Fundraising consultants are outside consultants hired by a nonprofit to assist with fundraising activities. (Note: employees, volunteers, and board members generally do not fall within this category.) Many states have laws regulating fundraising consultants and the nonprofit organizations that hire them. For example, a fundraising consultant may be required to register with the state Attorney General's office before being hired by any nonprofit in that state. Many states also require that there be a written contract between a nonprofit and a fundraising consultant that the nonprofit hires. In some states, a copy of this contract also must be filed with the state Attorney General's office. For more on this topic, please see the National Council of Nonprofits' resources on fundraising regulation at: https://www.councilofnonprofits.org/tools-resources/charitable-solicitation-registration
5b) If yes, is your organization familiar with the regulations regarding the use of such fundraising consultants in the states where your organization raises money?				

SECTION 2: ACCOUNTING AND AUDIT	YES	NO	UNSURE	EXPLANATION
1) Does your organization's accounting system include maintenance of accounts (either internally or through an outside accountant or bookkeeper)?				Fiscal accountability is one of the most important obligations of any nonprofit organization. Government regulators, such as the IRS or the state Attorney General, and private and government funders expect that the organization will keep accurate records of income and expenses and make efficient use of funds.
2) Is there an annual audit or review by a certified public accountant?				The organization should periodically examine financial records to determine if they are reasonably accurate. An external independent Certified Public Accounting ("CPA") firm should perform reviews, if required or recommended. Many states require a charitable corporation, unincorporated association, or trust to prepare financial statements audited by an independent CPA if its annual gross revenue exceeds a certain amount, i.e., $2 million in California, currently $750,000 in NY. If there were any issues detected during the audit, or actions recommended, it is important that the organization follow up to address those issues.
3) If any audit or review has been conducted, do you have a copy of the report, including any letters from the auditor describing recommended actions?				
4) Does your organization have an audit committee?				Certain states require a charitable corporation, unincorporated association, or trust, if its annual gross revenue exceeds a certain amount, *i.e.,* $2 million in California, to have an audit committee.
5) Is there an audit committee charter?				An audit committee charter is not required in many states, but can be useful when there are special audit committee obligations required by state law.

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SECTION 2: ACCOUNTING AND AUDIT	YES	NO	UNSURE	EXPLANATION
6a) Does your organization provide periodic financial statements to the Board at least quarterly?				One of the Board's foremost responsibilities is to secure adequate resources for the organization to fulfill its mission. A not-for-profit corporation uses and holds in trust money that is raised for it. Its Board is responsible for assuring funds are used to get the results for which they have been given. Complete, accurate financial statements are important for ensuring appropriate oversight by the Board. The Independent Sector has issued several suggestions for sound fiscal oversight, including regular reviews of financial statements, as part of its Principles for Sound Governance and Ethical Practice, available at: www.independentsector.org/wp-content/uploads/2016/11/Principles2015-Web-1.pdf. Depending on the size of the Board and the complexity of the financial statements, best practices may warrant a finance committee of the Board or an outside accountant.
6b) In addition to your Board's review of the organization's finances, does your organization also have a finance committee of the Board, or perhaps an outside accountant, review financial statements before they are reviewed by the whole Board?				

SECTION 3: INTERNAL CONTROLS	YES	NO	UNSURE	EXPLANATION
1) Do the same individuals serve on your organization's audit committee and finance committee?				Some states require that these committees be separated, and that the audit committee cannot perform finance committee functions and vice versa, while others do not have a specific rule. Factors such as board size, director's independence and expertise, and scale of operations also may affect what is prudent, possible, and legally appropriate for the organization. Some states, including New York, specify that only independent directors can serve on an audit committee.
2) Does your organization have written internal financial controls (e.g. policies and procedures such as check signature requirements, separating logging receipt of checks from entry of deposits, etc.). If so, is the organization following it?				Internal controls are designed to protect from the loss or misuse of assets. The controls aim to ensure that all transactions are properly authorized, and the information contained in financial reports is reliable. If the organization does not have written internal controls, it may want to speak with a financial management consultant. Tools are available on www.strongnonprofits.org.

SECTION 3: INTERNAL CONTROLS	YES	NO	UNSURE	EXPLANATION
3) Does your organization have an executive compensation policy or a process/written policy for determining that the compensation your organization pays is reasonable?				Per the IRS, reasonable compensation is the value that would ordinarily be paid for like services by like enterprises under like circumstances. The test for reasonableness should be determined based on all the facts and circumstances. Note that the organization's Executive Director is most likely a key person, who is subject to the IRS's excess benefit transaction regulations as well as the organization's Conflict of Interest policy.
4a) Does your organization have a conflict of interest policy consistent with the policy suggested by the IRS in the instructions to Form 1023?				A conflict of interest policy is recommended by the IRS and mandated by certain state laws. A conflict of interest arises when a person in a position of authority over an organization, such as a director, officer, or manager (or a member of their family), may personally benefit from a decision she or he makes. Having a clearly worded conflict of interest policy helps to resolve potential conflicts and assists the board in fulfilling its fiduciary duties. At its most basic level, a conflict of interest policy should require those with conflicts to disclose the potential conflict and prevent interested parties from voting on any matter involving the conflict. The Board should periodically review the organization's Conflict of Interest policy. More information can be found here: https://www.councilofnonprofits.org/tools-resources/conflicts-of-interest
4b) If yes, when was your Conflict of Interest policy last updated and approved by the Board?				
4c) Do all directors, officers, and other persons covered by the policy certify annually their compliance with the policy in writing?				
5) Has your organization signed any contracts with, made a loan to, or engaged in another practice that might confer a financial benefit upon any director or officer, a member of their family, or any other entity in which any director or officer has a financial interest?				
6) Does your organization have a line of credit or any significant loan obligations?				Loans to the organization can be valuable tools for cash flow and financial stability, but the best time to consider a loan is generally when the organization knows how it will use the funds and has a realistic plan for repayment and support from the Board. In contrast, a charitable organization should not provide a loan to directors or officers.

SECTION 4: FUND ALLOCATION	YES	NO	UNSURE	EXPLANATION
1) Does your organization make sure that your current and future funding is consistent with your articles of incorporation, bylaws, and statement of charitable purpose?				A 501(c)(3) nonprofit must have a charitable purpose as defined by IRS section 501(c)(3). As a result, a nonprofit must make sure that its funding is not tied to acts that a nonprofit must take that falls outside of its charitable purpose. Nonprofits should be transparent with funders with respect to how funds will be used.
2) Is your organization able to meet your commitments to funders?				
3a) Does your organization have any funds that are restricted?				Donors to a nonprofit may restrict the use of their donations to a specific purpose or project. Nonprofits that receive restricted funds should use fund accounting, which is an accounting management system by which a nonprofit organization records, accounts for, and reports finances in a way that clearly distinguishes the funds that have donor restrictions from funds that are unrestricted. More information on FASB's new accounting standards can be found here: https://www.councilofnonprofits.org/tools-resources/understanding-the-new-fasb-accounting-standards-overview
3b) If so, does your organization use fund accounting?				
3c) Is your organization using restricted funds for the specific purpose for which they were donated?				

SECTION 5: OPERATIONS	YES	NO	UNSURE	EXPLANATION
1a) Does your organization make certain that it withholds payroll taxes?				A nonprofit employer must withhold certain taxes from employees' pay checks, including federal income tax, Social Security and Medicare taxes.
1b) Does it make timely payments of tax withholdings to the government?				
1c) Does it file completed W-2 by January 31 for the previous calendar year?				

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SECTION 5: OPERATIONS	YES	NO	UNSURE	EXPLANATION
2a) Does your organization classify its workers as employees or independent contractors?				Worker classification determines whether an employer must withhold income taxes and pay Social Security, Medicare taxes and unemployment tax on wages paid to an employee. Businesses normally do not have to withhold or pay any taxes on payments to independent contractors. Earnings of a person working as an independent contractor are subject to self-employment tax. (Source: IRS).
2b) Does your organization have written job descriptions for all of its employees?				
2c) If yes, have the job descriptions been reviewed to confirm the appropriate classification of employees as exempt or non-exempt from overtime pay under relevant federal and state laws?				
3) Does your organization have investments? If so, is there a written investment policy?				A charitable organization should have policies and procedures in place related to the management, investment, and expenditure of organizational funds. A written investment policy should comply with legal requirements and regularly be reviewed by the Board and management to ensure that they are followed.
4) Does your organization have earned income, aside from charitable funding and government contracts? For example, does it engage in a trade or business that is regularly carried on, that makes a profit, and that is not substantially related to your tax-exempt purposes?				Tax-exempt organizations that run a trade or a business that fits this description may have to report unrelated business taxable income on Form 990-T.

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SECTION 5: OPERATIONS	YES	NO	UNSURE	EXPLANATION
5a) Does your organization sell any goods at retail?				In some states, a nonprofit organization must register for sales tax with the appropriate department (e.g. Treasury) before selling personal property. Exemption on sales tax may vary depending on a given state's laws. For example, in Michigan, a nonprofit organization is exempt from collecting sales tax only if it is tax-exempt under either 501(c)(3) or 501(c)(4), has aggregate annual retail sales of tangible personal property of less than $5,000, and the transaction does not fall under an exception.
5b) If so, has the organization registered with the appropriate agency regarding possible collection of sales tax?				
6) Has your organization paid all property taxes for land it owns, or for other assets, that haven't been determined to be exempt from property taxes?				Property tax exemption is governed by state and local law. For example, in Michigan, real property owned and occupied by a nonprofit charitable institution while occupied by that nonprofit solely for its charitable purposes is exempt from the collection of taxes. Check your state and local laws regarding taxes on real property or other types of property taxes that may be applicable.

CONCLUDING QUESTIONS	RESPONSE
1) Based on the assessment above, what areas of compliance does the organization need and/or want to address?	
2) Would the organization like pro bono counsel to address any of the issues noted above?	
3) Other comments, questions, or requests from the organization (if any).	

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