NONPROFIT ADVISOR

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ACCOUNTANTS AND ADVISORS
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A Friedman LLP publication on accounting and tax issues impacting not-for-profits

Issue No. 15 | WINTER 2012

MAKING THE MOST OUT OF MERGING - PART 2

A discussion with Susan Brooks, CEO, Girl Scouts Heart of New Jersey

In the Fall 2011 issue of *Nonprofit Advisor,* we reported on the United Way of Northern New Jersey ("UWNNJ") merger experience. This next part in our series focuses on the 2008 merger of three New Jersey Girl Scout councils, covering seven New Jersey counties,that created the Girl Scouts Heart of New Jersey ("GS"). As the new entity approaches the end of its third year of operations, I met with CEO Susan Brooks to learn about the challenges GS encountered and the lessons learned.

History

In 2004, facing declining membership nationwide, Girl Scouts USA ("GSUSA") mobilized to make the changes needed to become more relevant in the marketplace. As part of its core business strategy to create "high-capacity councils that have the funding, connections and scale" to achieve the purpose of "creating preeminent leadership experiences for girls," GSUSA began to incorporate realignment of the jurisdictional boundaries of councils nationwide.

Scope

Susan joined GS just one month before the merger, with the merger plan already in place, including support from the merger consultant employed by GSUSA. Like UWNNJ, GS is an affiliate of a national organization and was able to draw upon resources made available by the national organization to facilitate the merger. As the process unfolded, Susan discovered that flexibility in the implementation of the plan was key. The merged council unified 25,000 Girl Scouts, 11,000 volunteers, and 62 service units which represent 138 communities spread over seven counties.

Challenges

The merger was charged with advancing the evolution of Girl Scouts from its public perception of "cookies, craft and camping" to a "professional women's leadership organization". It was a challenge to unify activities of staff and volunteers spread across three separate locations. During the first year, staff was not relocated and was assured they would not be asked to significantly increase their commute. During the second year, functional teams were consolidated. The culture shifted gradually from one of "informality" to "presenting a very professional image all around".

Costs

The biggest costs included severance payments, vacation pay-outs and technology upgrades. The merger took place concurrently with the onset of the recession, so unanticipated contributions to the pension plan offered by GSUSA were necessary to cover distributions to staff who chose to participate in the voluntary retirement incentive program. CEOs from each historic council opted for the voluntary retirement option, so the senior team was created by promoting existing staff, augmented by new hires. Turnover as a result of the merger was below the average of councils nationwide as reported by GSUSA; however, Susan believes this was primarily due to the economic downturn.

One-time costs included rebuilding the data structure, a new website and telecommunication system, and creating unified systems for fund development, finance, membership, retail, and camp and program registration. The financial system Sage MIP (also used by GSUSA) was installed, and applications on the Council Enterprise System built by GSUSA was implemented.

Communication

Susan visited 52 of the Council's 62 service units (with more visits planned) over the past three years to facilitate integration of systems and culture. These face-to-face meetings and communication were critical to the success of the merger. GS relies upon 11,000 volunteers to run the troops and work with the girls, so everyone, including the volunteers, had to be kept informed of changes triggered by the merger. Equally important, was communication with donors. If you are considering a merger, Susan advises that communication and dialogue are key to preparing staff, volunteers and funders.

Impact

The board evolved from assisting the staff with the merger, to strategically assisting with fiduciary accountability and fundraising. The merged councils have gained a greater advocacy presence in Trenton, along with their three sister New Jersey councils, and now have a bill on the Assembly floor to make a check-the-box donation to the GS annually on the personal income tax return. The highly anticipated Girl Scouts' 100th anniversary celebration commencing later in 2011 includes a "bridging" event in which thousands of Girl Scouts will walk over the George Washington and Ben Franklin bridges. Also, funding to provide Girl Scout programming to underserved communities within the council has been made possible by strategic partnerships and collaboration in the community.

Conclusion

If you are considering merging, Susan advises that communication is crucial to prepare people for changes wrought by the merger process. The professionals at Friedman LLP are available to advise nonprofits with concerns regarding the tax and accounting implications of merging or consolidating nonprofit organizations.

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House Panel Seeks Details on IRS Investigations of Nonprofits

As the U.S. Federal Government continues to struggle with the challenges of containing its budget deficit, House Committee on Ways and Means' Subcommittee on Oversight has sought to explore issues involving the tax-exempt sector. The Subcommittee acknowledges that Congress and the IRS have focused on the tax-exempt sector in response to demands from the public for greater transparency in the sector. Charles Boustany Jr., Chairman of the Subcommittee, sent a letter to the IRS Commissioner on October 6, 2011, asking for information on the tax-exempt sector. Boustany's letter to the IRS addressed the following broad areas:

Increased Transparency And Accountability On The New Form 990

When the IRS revised the Form 990, it focused on increased transparency (additional questions about the board's activities), compliance (legal requirements), and ethics (stressing avoidance of conflicts of interest and personal benefit.). The IRS had three main objectives in mind when revising the Form 990. First, the IRS wanted to enhance transparency so that it and the public would have a more realistic picture of an organization. Second, the IRS wanted filers to provide greater detail on the organization's operations. And third, the IRS wanted to minimize the burden on filing organizations by streamlining the document.

Changes To The Form 990

In September 2011, the IRS finalized modifications to Form 990. The updated Form 990 provides new threshold amounts for reporting compensation, requiring that compensation be reported on a calendar-year basis, modifies the rules requiring information reporting upon a "substantial contraction" (i.e., any partial liquidation or other significant disposition of assets), and eliminates the advance ruling process for new organizations.

Information On Related And Subsidiary Organizations

One of the key concerns of the IRS is the potential use of related organizations for questionable purposes. For example, a related organization might be used to pay an employee of the filer to avoid having to disclose on the filer's Form 990 the full extent of the compensation received for performing services for the filer. A filing organization needs to be aware of the ramifications of its relationships with related parties.

Unrelated Business Taxable Income

Unrelated Business Income Tax ("UBIT") is the tax on unrelated business income, generated from an activity engaged in by a tax-exempt organization that is not related to the tax-exempt purpose of that organization. One of the major issues involves claims of loss deductions against "UBIT". This results in little or no taxable income from the unrelated business activity and the carryforward of net operating losses (NOLs) being applied to future "UBIT". The IRS is looking at why that type of activity generates a loss year after year. The IRS's concern is that losses from a specific activity are being used to offset other "UBIT". In some cases, the IRS is questioning whether there was ever intent for the activity to make any real profit. The IRS is also closely examining the deduction of indirect costs, such as depreciation, that, in the case of universities, is turning "UBIT" into a loss

Excessive Political Activity

Given that 2012 is a presidential election year, the IRS will be closely scrutinizing any political activity deemed to be excessive. The IRS wants to ensure that tax-exempt organizations are not acting as conduits for major donors to advance their own private political interests and that tax-exempt organizations are not providing major donors with excessive benefits.

Excise Taxes Related To Lobbying Rules

Organizations that are private foundations are subject to excise tax on any amounts paid or incurred (i) in an attempt to influence legislation, or (ii) in an attempt to influence the outcome of any public election or to conduct certain voter registration drives. As long as a private foundation does not earmark a grant for lobbying, it may make a general purpose grant to a 501(c)(3) public charity that lobbies without incurring penalty tax liability. A private foundation also may make a grant to support a specific public charity project that includes lobbying, so long as the grant is not earmarked for lobbying and so long as it is not larger than the amount budgeted by the grantee for the nonlobbying portion of the project.

Tax Shelter Transactions

One doesn't think of tax shelters and tax-exempt entities in the same breath, but tax-exempt entities may be subject to an excise tax for being a party to prohibited tax shelter transactions. The circumstances under which a tax-exempt entity becomes a party to a "prohibited transaction" can be complicated. The salient point is how the IRS will allocate net income or proceeds of the entity that are attributable to the prohibited tax shelter transaction.

IRS Scrutiny of AARP

Early in 2011, Congress took a close look at the American Association of Retired Persons ("AARP"), one of the oldest and largest tax-exempt organizations. Many issues were raised regarding AARP's tax-exempt status, including its organizational structure and business activities, casting doubt as to whether the organization acts exclusively to promote the welfare of all seniors or if it has simply become a for-profit enterprise. In essence, Congress questioned whether AARP was benefitting from tax-exemption but operating like a for-profit organization. Boustany's letter stated that, "Indeed, AARP is not the only tax-exempt organization that more closely resembles a for-profit enterprise, rather than an organization formed for social welfare or public charity."

AARP has defended itself against charges that it doesn't deserve its tax exemption. Barry Rand, the organization's Chief Executive Officer, testified in April 2011 that AARP is "strictly nonpartisan" and said the revenue it collects helps keep membership dues low. This questioning by Congress of the mission of a long-established tax-exempt organization is no doubt indicative of the closer scrutiny in store for the nonprofit sector.

The not-for-profit professionals at Friedman LLP continue to advise not-for-profits to adhere to the highest level of transparency in their financial reporting practices not only in form but in substance as well.

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RELIEF FOR AUTOMATIC REVOCATION

Application For Reinstatement

Background

The Pension Protection Act of 2006 passed by Congress includes a provision requiring all tax-exempt organizations (with specific exceptions) to file annually (for taxable years beginning in 2007) with the Internal Revenue Service using one of four formats:

- **Form 990**
- **Form 990-EZ**
- **Electronic postcard - Form 990-N**
- **Form 990-PF (for private foundations exempt under section 501(c)(3))**

The Internal Revenue Service is required by law to revoke an organization's tax exemption for failing to file the applicable form over a consecutive three-year filing period. Tax-exempt status for organizations that failed to file from 2007 to 2009 has now been automatically revoked. Notice CP-120A is generated and sent to the last known address of the organization stating that the tax exemption has been revoked effectively as of the filing due date of the third year's return (May 15, 2010 for calendar year-ends). Additionally, the name of the organization is published on the revocation list on the IRS website and contributions to the organization will no longer be tax-deductible.

Transition Relief

To reinstate tax-exempt status, the organization must file an application for recognition of exemption (Form 1023 or 1024). Small organizations eligible for transition relief (see IRS Notice 2011-43) may qualify for a reduced user fee of $100 provided the application for reinstatement of tax-exempt status is postmarked no later than **December 31, 2012**. Small organizations eligible for transition relief should label their application "Notice 2011-43" at the top and on the mailing envelope. A small organization is defined as one that normally has annual gross receipts of not more than $50,000.

The IRS will reinstate the tax-exempt status of an eligible small organization retroactive to the date of revocation if these criteria are met.

Application For Retroactive Reinstatement

Organizations not qualifying for transition relief may request reinstatement of the organization's tax-exempt status retroactively to the date of automatic revocation if it can be established that the organization had reasonable cause for not filing an annual return or notice for three consecutive years.

The organization must file an application for recognition of exemption (Form 1023 or 1024) and include completed annual forms 990, 990-EZ or 990-PF as applicable, for all of the years during and after the consecutive three-year period, and the appropriate user fee. A written statement establishing reasonable cause for failure to file and a description of safeguards implemented to prevent future failure must be included with a signed declaration (see IRS Notice 2011-44). The application for reinstatement should be labeled "Automatically Revoked" at the top and on the mailing envelope to ensure that a trained specialist handles the application.

If you have questions or need assistance with an automatic revocation, the professionals at Friedman LLP are available to advise and assist with the process of applying for reinstatement.

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OUR NOT-FOR-PROFIT SERVICES GROUP

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We have access to worldwide resources as an independent member firm of DFK International, so we are well positioned to assist you wherever the need arises.

SERVICES

Audits—Yellow Book, OMB A-133, 403(b) Benefit Plans + Tax Filings—Form 990 and 990 PF + Unrelated Business Income Tax Analysis + Internal Control Assessment and Review + Accounting Manuals and Procedures + Board Governance Review and Best Practices + Forensic Consulting

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Upcoming Deadlines – Not-for-Profit Organizations

Year-End	Required Filing	Date
June 30	1st Extension Deadline for Federal Form 990	February 15
June 30	OMB Circular A-133 Report Due	March 31
August 31	1st Extension for Federal Form 990	April 15
September 30	Federal Form 990 Deadline	February15

Extended Deadline for Certain Tax-Exempt Entities:

Fiscal year tax-exempt organizations filing Form 990, Form 990-EZ , Form 990-PF, or Form 1120-POL with due dates (original or extended) of 1/17/12 or 2/15/12 now have an extended deadline of 3/30/12 to file their annual returns because the e-file system that processes tax-exempt returns will be off-line in January and February. Form 990-N filers will not be affected. News Release IR-2011-120 and Notice 2012-4, 2012-3 IRB .