



## Evaluating Complex Funding Sources

By Erin Welch

During tough economic times, an increasing number of not-for-profit boards may feel pressured to accept various types of funding sources in order to meet their fundraising objectives, a number of which may lead to accounting complexities, donor management issues and other unforeseen costs. Knowing what to expect before your organization pursues more complex funding sources can limit your exposure to unnecessary financial and operational difficulties. Below is an overview of the most common types of complex funding sources to be aware of:

**Restricted Contributions.** Individuals, corporations or private foundations may often restrict the use of their gift on a temporary or permanent basis. These gifts are typically not intended for general operations or administrative and fundraising costs, but there is often a significant cost associated with tracking this income, so the gift should be large enough to merit the additional monitoring expense.

**Donor-Advised Funds.** Some funding organizations allow individual donors to provide advice as to how grants of their funds will be made. However, this practice can lead to issues with tax deductibility and appropriate accounting. To avoid these issues, foundations and other funding organizations hosting donor-advised funds should make sure prospective donors understand the limits of their influence after the contribution to the donor-advised fund is made. Organizations who are recipients of grants from foundations and other funding sources using donor-advised funds should make sure that any understanding with the individual donor is clear prior to accepting funding, to avoid any negative impact on the donor relationship.

**Government Funding.** While government funds typically come with extensive tracking and reporting requirements, the recipient may also be barred from using grant money to manage or administer the programs that the funding was intended to support. In addition, if the organization spends more than \$500,000 in federal funds each year, it is required to have a compliance audit in addition to the financial statement audit. This leads to increased audit fees, which are not always covered by funding source.

**Pass-Through Relationships.** Many not-for-profits receive donations on behalf of another organization that has not yet received its tax-exempt status. There are generally administrative costs associated with these funds, for which the host organization may not receive reimbursement. In addition, there are fiscal responsibilities to ensure that the funds are used for charitable purposes.

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**Annual Auctions and Other Fundraisers.** It is common for not-for-profits (or someone on their behalf) to host a fundraising event. However, in addition to requiring a significant time commitment from staff and volunteers (and placing the organization at risk for fraud if they are not properly supervised), there are numerous other accounting and donor perception issues that can diminish the returns these events ostensibly deliver.

In addition to the above, there are other enticing revenue streams such as land grants and stock gifts that may include unanticipated tax consequences. Your organization should also be cautious about accepting revenue from advertising, parking fees, rent and retail sales, which can lead to additional recordkeeping requirements and unrelated business income (“UBI”).

Fortunately, there are ways to protect your organization, including the following:

- Read the fine print on grants and federal funding programs
- Implement a comprehensive gift acceptance policy that establishes gift evaluation, acceptance and acknowledgement processes
- Before hosting a fundraising event, evaluate cost and benefits against required resources
- Always consider how funding sources may or may not align with your mission

Not all money is good money, but with the right set of tools and procedures to determine appropriate funding sources, your organization will be better prepared to proactively assess risk and to simplify decision-making in the future

#### **About the Author**

*Consulting and Audit partner, Erin Welch, has been with Jacobson Jarvis since October 2000 and was promoted to partner in January 2010. Erin has managed and performed audits exclusively for not-for-profit organizations for the past 10 years. At the same time, she has worked as a consultant to clients, helping them to develop internal control programs and other processes, conducting financial health assessments, reviewing and designing charts of accounts, assisting clients with board communications and conducting board trainings.*