Nonprofit Observer

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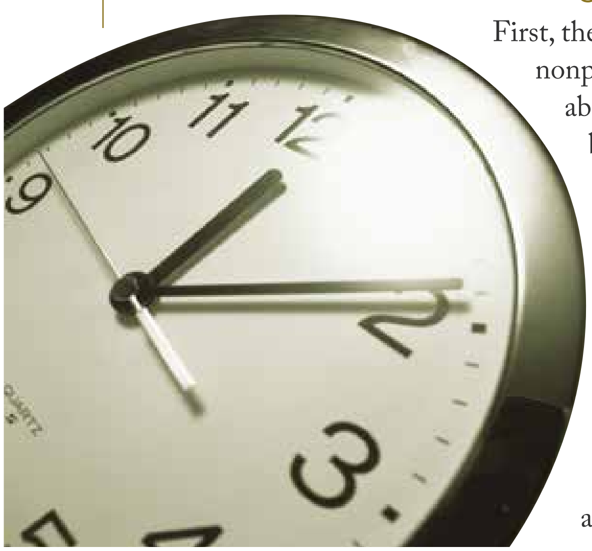
What the new overtime rule could mean for your nonprofit

Under the Fair Labor Standards Act (FLSA) employers must pay their employees a minimum of time-and-a-half for hours worked over the standard 40-hour work week. Traditionally, most white-collar employees were exempt from this rule. But that's about to change.

On May 18, the federal Department of Labor (DOL) issued its final rule updating overtime regulations. The rule changes the annual salary threshold for overtime pay from $23,660 to $47,476 — with automatic adjustments every three years — and there's no exception for nonprofits. This threshold applies to both white- and blue-collar workers, regardless of their duties. (See "Employee classification: The never-ending challenge" on page 3.)

The new rule becomes effective December 1, 2016. So you need to determine as soon as possible whether any of your staff members will become newly eligible for overtime pay.

Affected organizations



First, the good news for nonprofits concerned about shrinking budgets and rising costs: Most smaller organizations are unlikely to become subject to the new overtime rules. Nonprofits generally must have an annual dollar volume of at least $500,000 in sales or business to be subject on an "enterprise" level. Charitable, educational and other tax-exempt activities won't be considered — only activities performed for the purpose of making a profit, such as selling merchandise in your charity's gift shop or donated items in your thrift store.

Although your nonprofit likely wants to pay employees well for their hard work, the new rule may force you to make difficult decisions.

What types of nonprofits could be subject to the new rules, then? Hospitals, businesses that provide medical and nursing care, educational institutions and government agencies fall under FLSA rules regardless of their annual sales volume. Other large charities that compete with for-profit businesses are also likely to be affected.

Also, nonprofit employees of all sizes of organizations may qualify for overtime pay on an individual level if they're engaged in interstate commerce. For example, if a development staffer's primary responsibility is soliciting out-of-state donations via phone calls and U.S. Mail, that employee may be eligible for overtime pay. Even administrators and accounting staffers recording and processing interstate donations could qualify.

To illustrate who's exempt and who isn't, the DOL has used the example of a nonprofit animal shelter. In addition to providing free veterinary care and other services for homeless animals, the shelter offers veterinary care for a fee to pet owners. Assuming such fee services generate less than $500,000 per year, shelter employees who might otherwise be eligible for overtime under the new rule, aren't. But an employee who otherwise meets the FLSA's salary requirements and whose sole responsibilities are to solicit funds from animal lovers across the country may fall under the rule.

Implications for employees and employers

The federal government's proposed overtime rule change is the first in more than a decade — it's intended to help American workers keep up with rising costs. Where the old threshold set salaried employees eligible for overtime pay at the 20th percentile of weekly earnings, the new minimum is set in the 40th percentile. (Note that some states, such as California, have set their own overtime thresholds at higher amounts than those traditionally enforced by the federal government.) The DOL has estimated that at least four million salaried American workers will be affected, but some researchers have put that number at closer to 13 million.

Although your nonprofit likely wants to pay employees well for their hard work, the new rule may force you to make difficult decisions. Either you increase your staffing budget to pay overtime (or pay higher salaries that would make eligible employees exempt from overtime) or you limit employees' workweeks to 40 hours. The first option will be a financial strain if your budget is already stretched to its limits. The second option could force you to scale back services or even eliminate programs.

Looking forward

Now that the final rule has been issued, your nonprofit can't ignore the possibility that some of your staff members will be reclassified. Review the current FLSA classifications of your staff and determine who might be affected by the change. Particularly note the hours worked by staffers who are at or near the $47,476 threshold. Also talk to your financial advisor about your nonprofit's specific situation and what you may need to do before December 1.

EMPLOYEE CLASSIFICATION: THE NEVER-ENDING CHALLENGE

Deciding which employees are exempt from overtime and which are nonexempt has always been a challenge for employers. But it's important: Misclassification can result in financial penalties and other negative consequences most nonprofits can't afford.

The final rule issued by the Department of Labor in May makes no changes to the duties test, which must be considered in addition to how your staffers are paid (hourly or salaried) and how much. Also be sure to take into account the knowledge, skills and educational background employees need to perform their jobs. In general, executives, professionals and many administrators are exempt. Manual laborers, customer service personnel, and clerical and data-entry workers typically aren't. For more detailed guidance, check the Department of Labor's website at dol.gov/elaws.

FASB's proposed financial statement changes: A cheat sheet

Your nonprofit's financial statements may look very different for fiscal years starting after December 15, 2017, than they do now. In April, the Financial Accounting Standards Board (FASB) made its final recommendations for changes to how organizations classify net assets and account for liquidity, performance and cash flows in financial statements. Although the FASB's suggestions aren't yet set in stone, the comment period is over and final guidance is expected to be issued before the end of 2016.

Key recommendations

Prepare now for the following changes:

Net assets. Nonprofits have been able to classify assets as unrestricted, temporarily restricted and permanently restricted. But temporarily and permanently restricted net assets will be combined into "net assets with donor restrictions," and unrestricted net assets will be characterized as "net assets without donor restrictions."

Your nonprofit also will need to disclose the amount and purpose of board-designated net assets. And, the amount by which endowment funds are underwater will be a component of net assets with donor restrictions rather than net assets without restrictions.

Currently, nonprofits can recognize the expiration of a donor restriction over time. But under the new rules, you'll need to reclassify net assets with donor restrictions that are used to acquire or construct long-lived assets as "net assets without donor restrictions" when the asset is placed in service.

Reporting expenses. Your nonprofit will be required to disclose expenses by both function (for example,

programs and supporting activities) and natural classification (such as salary, depreciation and professional fees). These can be reported either on the face of the statement of activities or in the notes.

Phase 2 will consist of broader, more fundamental changes that reflect revisions to the private and public business reporting models.

Investment returns. You'll need to present investment returns net of external investment expenses and the salary and benefits of certain employees directly involved in investment management. It will no longer be necessary to disclose investment expenses and details of investment components in the endowment net assets roll-forward in the notes.

Liquidity and availability. The rule change calls for "enhanced" qualitative and quantitative reporting on spendable financial resources.

Operating measure. If you report an operating measure in your statement of activities *and* report decisions your board has made (such as designating or appropriating earnings), you'll need to describe in detail how such board decisions have affected your statement of activities.

Cash flows. You'll still be allowed to use either the direct or indirect (reconciliation) method of reporting cash flows. If you choose the direct method, you'll no longer be required to provide indirect reconciliation.

Only Phase 1

These targeted changes represent only Phase 1 of the FASB's nonprofit accounting rules revision. Based in part on comments the FASB received from nonprofits about its original proposal, the board has pledged to keep nonprofit accounting rules in sync with those of for-profit entities.

Phase 2, therefore, will consist of broader, more fundamental changes that reflect revisions to the private and public business reporting models. That said, the FASB has also stated that it wants to continue to provide nonprofits with reporting flexibility. For the latest information on new nonprofit accounting guidelines, talk to your financial advisor.

A donation's a donation … except when it's a gift in kind

Some supporters give your nonprofit money, others give goods and still others give intangibles, such as use of a facility for a fundraiser. A donation's a donation, right? Not quite. Under certain circumstances, gifts in kind and donations of services must be recorded and recognized at year end as revenue, expenses or assets. Here's what you need to do when your nonprofit receives one of these gifts.

Does it have value?

Gifts in kind generally involve the receipt of a piece of tangible property or property rights. They can take many forms, including:

- Free or discounted use of facilities,
- Collections, such as artwork to display or sell, and
- Office furniture or supplies.

To determine whether you need to record the amount of these gifts in your financial statements, ask the following question: Does this item have value to our nonprofit? In other words, can you use it to carry out your mission or sell it to help fund operations? If so, it should be recorded at fair value as revenue in the period it's received. If the gift is a pledge, it's recordable in the period the pledge is made.

What would it cost to purchase?

You'll also need to decide what value to assign to the gift in kind. Consider: What would the item cost your nonprofit if it were to purchase that item

don't need to be specialized for them to be recognized. For example, the value of a contractor's time (a specialized service) to renovate your offices would be capitalized as part of the building, as would the value of a volunteer's time to pack up items for safekeeping during the renovation (a nonspecialized skill).

Second, consider whether the service requires specialized skills, is provided by persons with those skills and would have been purchased if it hadn't been donated. These services are accounted for by recording contribution income at the fair value of the service provided. You also must record such donations as a related expense, in the same amount, for the professional service provided.

Note that specialized skills usually refer to those provided by professionals such as attorneys, accountants, architects, carpenters and electricians. Normally, this would exclude general volunteer time because volunteers typically don't use specialized skills to perform their assigned tasks. Nonetheless, your nonprofit may want to disclose the total number of volunteer hours it received during the year in its financial statement footnotes to help emphasize the commitment made by the community to your nonprofit.

All gifts are welcome

Your nonprofit likely welcomes all donations — whatever form they might take. Just remember that, from an accounting standpoint, gifts in kind and donations of services and facilities should be treated differently from financial donations. If you're unsure about whether you need to record and value a gift, contact your financial advisor.

outright from an unrelated third party? It's fairly easy to assign a fair value to property, such as furniture, equipment or inventory — you can look up the going price for a similar item in the marketplace. But when the gift is something that doesn't have a readily determinable market value, fair value is more difficult to assign.

Without an independent appraisal to substantiate the gift's value, you may need to rely on a good faith estimate from its donor. Be sure to obtain all corroborating evidence that the donor can give you, and then evaluate whether the amount was reasonably assessed. For gifts valued at more than $5,000, donors are required to obtain an independent appraisal for tax purposes. And this provides documentation for your records, as well.

How are services different?

Donated services are handled a little differently. Accounting guidelines specify two criteria for determining when donated services should be recognized and how to determine their fair value.

First, consider whether the service creates or enhances a nonfinancial asset. These types of donations should be capitalized at fair value on the date they're given. In such situations, the services

Carpe diem

Use a giving day to raise money — and awareness

Do you have plans for November 29, 2016? If that date doesn't ring a bell, your organization probably isn't participating in National Giving Tuesday. But considering the opportunities associated with it, maybe you should.

What is it?

Giving Tuesday, or National Day of Giving, was created to encourage Americans to contribute to charity during the holiday season, similarly to how they participate in commercial shopping events such as Black Friday and Cyber Monday. Like Cyber Monday, Giving Tuesday wouldn't be possible without technology. Participants use social media to raise awareness about issues and how their nonprofits are responding to them. Raising money online is a central goal, but Giving Tuesday is also intended to educate potential supporters and encourage them to volunteer in their communities.

Since its establishment almost five years ago by New York City's 92nd Street Y, Giving Tuesday has grown into an enormously successful global event. It currently has more than 40,000 charitable, for-profit business and government participants. In 2015 it raised more than $117 million in a 24-hour period — a 150% increase over the previous year — and received 1.3 million Twitter mentions, according to NBC News.

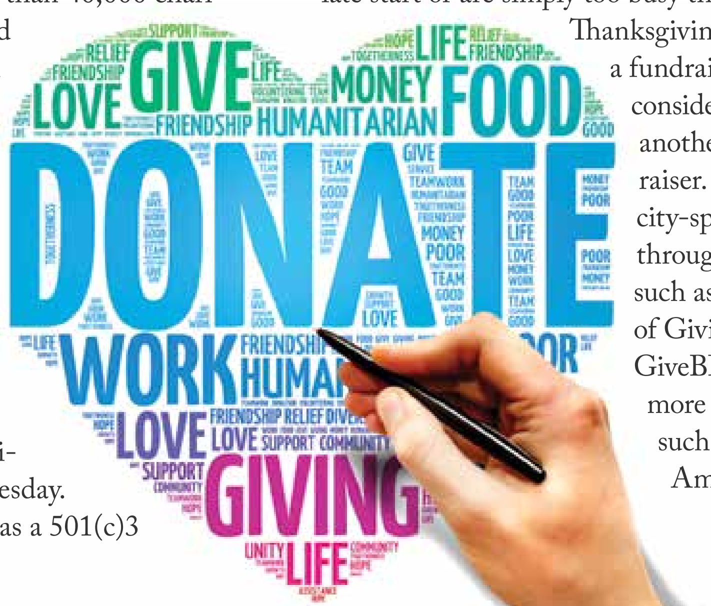
Get involved

If you're interested in participating, sign up at GivingTuesday.org. You must be registered as a 501(c)3 organization and you'll need to provide a link to your own website or a third-party payment service that supporters can use to make donations. Donors *can't* directly give money to your charity through the Giving Tuesday website. What the site does offer, however, are free marketing tools, including logos and banners, and advice on leveraging your social media presence and support base for maximum impact.

Your nonprofit's participation in this designated day can be minimal or substantial, depending on your resources and greater objectives. If this is your first year, try a simple goal. For example, use the day to remind supporters to make their deductible gifts by year end. Or publicize the list of supplies your facility needs on an ongoing basis. It's easier to both accomplish and measure progress toward such focused goals.

Start planning

At a minimum, start planning several months in advance of November 29. If you're getting a late start or are simply too busy the week after Thanksgiving to spearhead a fundraising campaign, consider participating in another 24-hour fundraiser. In addition to city-specific events held throughout the year, such as Pittsburgh's Day of Giving and Seattle's GiveBIG, there are more general options, such as Give Local America®. ●



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