

*Please note: This is a transcription so there may be slight grammatical errors.*

Hello, and welcome to Mission and Markets, a podcast by CAPTRUST where we explore trends and best practices for endowments and foundations related to mission engagement, fiduciary governance, and investment management, hosted by CAPTRUST's Heather Shanahan, director of the Endowments and Foundations practice. Each episode shares research resources and recommendations from industry insiders so your nonprofit can focus on what's most important: the mission.

Heather Shanahan:

Hello, and welcome to our latest episode of Mission and Markets. My name's Heather Shanahan, I'm your host. And I have the pleasure today of having with me Kristen Hoyle, CPA with Thomas, Judy, Tucker. Kristen, would you be willing to share a little bit of information about yourself and your practice, and what you do every day?

Kristen Hoyle:

Absolutely. Thank you, Heather. We're a local firm in Raleigh, North Carolina. We have four offices in Raleigh, Durham, Wilmington, and Cape Carteret on the coast. I have been with the firm for 25 years, and I've been a partner since 2001. And I've done a little bit of everything over my career, but for the last 15 years, I've concentrated on not-for-profits, doing audit, tax, and advisory services. It's where my heart is and where I really enjoy working.

Heather Shanahan:

The work that you do is fairly specific, and to have that expertise in the nonprofit space is really valuable to the clients with whom we work as well. And so maybe let's start high level, because I think even for folks that are in front of this every day, sometimes it gets confusing. So can we clarify what are the differences between private foundations and public nonprofits? And then in the middle of all of that, what's an endowment? Can you kind of give us some perspective on those categories?

Kristen Hoyle:

Sure. Sure. So the IRS allows an entity to be tax exempt. And it's under certain code sections. And you hear 501(c)3, 4, 5, 6, and 7. And those are different types of not-for-profits. A c3 is the most common, and that's one that has a charitable purpose for it. So within that c3, you can have the public charity or a private foundation. So that's very distinct separation between the two organizations. A c3 gets the majority of its revenue from the general public, multiple sources. It could be government grants, it could be private contributions, it could be foundation grants, it could be admissions for their program purposes. And a private foundation, however, it gets the majority of its revenue from smaller pools, say for instance, one or two people that fund the organization, or the majority of their revenue is from investment earnings. So they're still a tax-exempt, for the most part, entity, but they have some other rules for a private foundation.

From a donor standpoint, if I'm just a general donor, I want to give to a public charity because I get a bigger tax deduction. So you have 50% of your AGI. Versus with a private foundation, you only get 40% of your AGI that you can deduct. So also, different foundations that give grants, they like to give it to public charities versus private foundations. So there's a lot of different nuances with it. And neither one is bad. I work with a number of private foundations. So they might have had an individual donor that set it up originally, and therefore they had to be a private foundation. So now, the question about an endowment... a lot of people think, oh, an endowment's a separate entity, but it's not. Within the organization, they have investments that they've set aside for a particular purpose, and they have restrictions on how that can be used.

Heather Shanahan:

The IRS doesn't give as much guidance on a year-to-year basis for nonprofits. So what's the latest? When's the last time there was new information? And what did that look like in terms of nonprofit guidance?

Kristen Hoyle:

Well, the biggest sea change came 15 years ago when they changed the actual 990 form, and they expanded it to ask a lot of questions regarding governance. How many board members do you have? How many are independent? Do you keep minutes? A lot of this information is not code related. But to be honest, there hasn't been a lot of changes to the not-for-profit code section. There's been a few tweaks here and there over the years. A few years back, there was a change regarding... a potential change regarding fringe benefits, but that didn't pass. So there's little IRS changes. They keep talking about it. They keep saying, "OK, we're going to have more auditors looking at not-for-profits," but that never came to pass. There's been more accounting changes for not-for-profits. The AICPA and the Financial Accounting Standards boards, around 2008, also started programs to make not-for-profits' financial statements more comparable.

Because donors want to know, is this entity taking care of the assets that I'm giving them? So they want to compare, especially foundations, if they're trying to decide a grant. And they look at one organization, one school versus another school. Can they compare them? So there's been some new changes about making it, how the allocation of functional expenses happen.

Heather Shanahan:

Right. So let's talk about that for two seconds then. If I'm a donor, what am I looking for? What's ideal? If 50% is going to management fees, or 30% or 20%, it better not be 50, what am I looking for? And as an organization, how do I manage that?

Kristen Hoyle:

So the statement of functional expenses is key. And that was one item that donors should look at. And that's the expenses that are put into buckets of the different programs versus management in general, versus fundraising. And there's no bright line, no percentage that the IRS says that you have to expend towards the program.

Heather Shanahan:

But it's public perception, right?

Kristen Hoyle:

Right.

Heather Shanahan:

And it gets people in trouble. Yeah.

Kristen Hoyle:

Right. Right. So it's generally... a rule of thumb is 75% or more of your expenditures should go towards program. That's what funders like to look at. And the thing is, it's hard to compare one versus the other. And it's also hard because donors want to give their money for the programs. They don't want to give money for turning on the lights, for getting an auditor, for paying for the tax return, but those are necessary items. So you have to have some general and administration, and you have to have fundraising. So what I say is look at an organization. First off, make sure that you're allocating the dollars correctly to the buckets. Most of it's pretty easy. You know that

school supplies go into program. You know that the audit goes into general and administration. But the executive director wears a lot of hats.

They're doing program one day, they're working with the auditors the next, and then they're at a fundraiser. So that individual's salary needs to be allocated into those different buckets. And so that's where it's really important to work with an auditor or your tax preparer to make sure that that's in there correctly.

Heather Shanahan:

So you mentioned, of course, engaging an auditor. Let's talk about that. Does everybody need an audit? And why and why not?

Kristen Hoyle:

Well, I've talked quite a few people out of having audits by saying, "Well..."

Heather Shanahan:

It seems surprising.

Kristen Hoyle:

Yeah, I'd love to overcharge you for something you don't need, but no, not everyone needs an audit. So an audit can be expensive. So there's different levels of financial statements. There's an audit, a review, and a compilation, a compilation being the lowest. What the audit does is it looks at internal controls and then it opines on your financial statements that your balance sheet and income statement and footnotes are materially correct. We don't opine on your internal controls, but we do, if there are any breaks in internal controls, we report on those, and then we also give recommendations.

Now, where an entity, an organization will need an audit is if they receive federal or state funding. Not all ... if you receive \$1, you have to have an audit. If you received more than \$500,000 of North Carolina state funding or \$750,000 of federal funding, you have to have an audit.

Heather Shanahan:

Is that pretty standard across the states?

Kristen Hoyle:

Yes. And if you have a large bank loan, you typically have to have an audit, or if you are filing for certification. So there's an organization called the Evangelical Financial Accountability Standards Board, and they're really great. I'll recommend them for all of my religious not-for-profits. They have a lot of really good documentation on internal controls or keeping books and board governments, but they will come in and certify a church's or school's financial information, not the financial statement, but how their procedures are. It's kind of like the Good Housekeeping seal of approval. So they require an audit.

And then there's certain... for some of the independent schools, if they're in a regional organization, they might require an audit. Some church affiliations, like the Episcopal Church or the Methodist Church, require an audit. But if you're just a small not-for-profit, maybe you have \$600,000 or \$700,000 of revenue, which is a lot, it's good, but do you really need an audit? I know board members think, "We need to have an audit. We need someone to look at it," but if an audit is going to cost you \$10,000 on a \$600,000 budget and you're bootstrapping it...

Heather Shanahan:

Yeah, maybe not.

Kristen Hoyle:

... you might want to consider something else.

Heather Shanahan:

If you weren't going to do that, then, and you want to take a look at internal controls and make sure that you've got best practices in place, where would you go for that type of checks and balance and guidance?

Kristen Hoyle:

So you could have a consulting agreement or an agreed-upon procedures, quote-unquote, audit, where you would engage a CPA to come in and just look at your internal controls, and test them, and do the internal control procedures that you would've done in an audit, and do that, because over my 37 years I've worked in public accounting, I've encountered eight different instances of fraud and embezzlement. And of those eight, seven have been with not-for-profits. And it's because, one, especially with the religious organizations, they think the best of everyone, so they want to trust them, even though there's warning signs, or they don't have funds to be able to hire enough people to have internal controls, segregation of duties. So if I'm working at a church, or small school, or any small non-for-profit, and I'm opening the mail, I'm hoarding the deposit, I'm going to the bank, I'm doing all the QuickBooks, I could steal you blind.

Heather Shanahan:

That's right. Yeah.

Kristen Hoyle:

Not that I wouldn't ever be caught, but by the time it was noticed, you could lose \$100,000, \$200,000.

Heather Shanahan:

Sure.

Kristen Hoyle:

So that happens, unfortunately. So having that segregation of duties or having someone come in and say, "OK, this is where you're vulnerable. You have the same person opening the mail, making the deposit, and entering it. So how could you split that up?" If you don't have the funds to be able to hire a second person, it might be talking to one of your board members and having them open the bank statements. So it was funny. Of course, every organization I become involved with, they want me to be the treasurer.

Heather Shanahan:

It's the curse of the CPA.

Kristen Hoyle:

I know. So I was treasurer for this one organization, a rather large, multi-location organization. And one of the things I did was, and this was 15 years ago, so it was before everything was online, I would get the actual canceled checks and open the bank statement, look at it, and look through them. And I was flipping through the canceled checks and I noticed that the signature on the back was the same, same handwriting, but for different names, and they were paychecks.

Heather Shanahan:

Oh.

Kristen Hoyle:

So it was an organization that hired a lot of part-time people and part-time college students. And so they would forget about their paychecks. And so the secretary at the front desk took those paychecks, signed their names, and had someone at the bank deposit them into her account.

Heather Shanahan:

Oof. Wow.

Kristen Hoyle:

Yeah.

Heather Shanahan:

All right. Well, that's why you look, right?

Kristen Hoyle:

Yeah, that's why you look.

Heather Shanahan:

Geez. Yeah.

Kristen Hoyle:

There's different ways that you can have that, but it's all dependent upon your particular organization, what steps you can and cannot take.

Heather Shanahan:

Well, that makes sense. Well, all right. So I'm an organization and I've decided that we need an audit or I'm an organization that's had the same auditor for a while, and it's time for an RFP. What do I need to consider?

Kristen Hoyle:

So the first thing you need to consider is references from other organizations that are similar to you. You want to get a CPA that, one, does work with not-for-profits because it's different, it's unique.

Heather Shanahan:

Not all the same. Yeah.

Kristen Hoyle:

And two, one that is familiar with your organization. So private schools have unique areas with tuition or their endowments, religious organizations have unique concerns with contributions that are for private inurement or housing allowances, trade associations have political and lobbying expenses that might come up.

I just had a question that came up yesterday with a trade association. They gave a contribution to an organization, it's called the C4, that was created not too long ago, that might have some political leanings. And so is this contribution a political donation or lobbying cost? And how would that affect their proxy tax? So knowing what questions to ask is important. So getting references and then sending the RFPs out and asking questions, like who are some of your clients, who are some of your clients that we can talk to, how would you do the audit, what is your methodology, and then interview the fine list.

Heather Shanahan:

Actually follow up. Yeah.

Kristen Hoyle:

Yeah. And maybe this is self-serving, but don't always pick the cheapest. I've taken on audits where the prior auditor might've charged a few thousand dollars, but then they can't make any money on it. So they're cutting corners and it's a poor audit and a poor tax return, which reflects badly on the organization. Don't pick the most expensive. My grandmother was of the thought that, if it was more expensive, it was higher quality.

Heather Shanahan:

Yes. Right. Not always. Not always here, right?

Kristen Hoyle:

Not always. But, I mean, try not to pick it solely on price. Look at quality, how you work well with the auditor. And are they going to be on site? Are they going to do it 100% remote? Are they going to promise to keep the same people on the audit as much as possible? Or what if you have a personality clash with the manager? Will they assign someone else? So looking at that, it's really key to have what's their experience with not-for-profits.

Heather Shanahan:

I mean, one red flag, too, I mean you and I have both seen this, the numbers on the 990 are the exact same numbers year over year over year over year. That's really unlikely in certain areas. Yeah. And that might be an opportunity to say, "Huh, maybe somebody's not quite doing their job." Yeah, for instance.

All right. So I know we talked about document retention in the context of endowment document. And certainly I think that's such a struggle if you get notification of a gift that will be given by bequest, but it goes first to the children and then anything remaining in estate goes to the nonprofit organization. Well, good grief, that could be 30 years from now. And so what happens to that document? So what types of things do organizations need to make sure that they hold onto and what's kind of big rocks into perpetuity? And then what are some things that may be more time sensitive, three years, seven years?

Kristen Hoyle:

Sure, sure. So as you said, anything related to endowments or bequests, keep those indefinitely. And anything related to large purchases or loans, keep those indefinitely also. For one thing, with loans and documents, you want to make sure that you keep the documentation that it was paid off because if anything, if you had to transfer the property, you need to have all of that information available. Tax returns, I generally recommend tax returns be kept indefinitely, either in electronic format or paper format, because it has a lot of good information, too. You can go back a number of years because that will also list your copy of it. Not the public copy; your copy of it will have the list of contributors on it. So sometimes that gives us clues.

Heather Shanahan:

You know what? Stop right there for one second. OK. Because I see all the time your copy, not the public copy. And it's always done when we run into the non-public version out there that lists donors. Can you talk about that schedule and what should and shouldn't be done there just for a second, because that's important.

Kristen Hoyle:

Sure. That is very important. So the 990, whether you do a full 990 or an easy, you have to have a Schedule B attached, which is a schedule of contributors who have given in total for the year greater than \$5,000, or if they're a larger not-for-profit, it's 2% of a calculation. So it is required to have the name of the donor and the address and the amount. So if you get \$100,000 donation from the Triangle Community Foundation, that will be on there. So the IRS uses that for one, to see where you're getting your money from to see if you have any ineligible donors. And also to see if it's greater, if you have someone that's giving a lot over a number of years, it might throw you into private foundation status. But [inaudible] another big complicated.

And then also to match it up if someone with their personal return to see if it does that way. So that goes to the IRS. If you go to [irs.gov](http://irs.gov) and you look up a not-for-profit's 990, which anybody can do, that Schedule B will not be in there. They automatically keep it out.

Heather Shanahan:

Or will it? They keep it out.

Kristen Hoyle:

Yeah, they keep it out.

Heather Shanahan:

The IRS. But other sites...

Kristen Hoyle:

Yeah. Other sites... GuideStar is generally pretty good about that too, that they won't keep it. But where I see a problem is when an organization posts their 990 on their website, they put it up with the Schedule B, all the information on there. And well, you've just given private information about some of your individual donors, which is terrible.

Heather Shanahan:

No, it's for the donor, but then not say for any other organization that might be interested in soliciting, now all of a sudden it happens. Oh, well, here's your list. Yeah.

Kristen Hoyle:

Yeah, yeah.

Heather Shanahan:

Reach out to...

Kristen Hoyle:

Yeah. So yeah.

Your CPA should be able to give you a redacted copy of your Schedule B that will have the names and the addresses redacted and just the amounts, or you can just take the Schedule B out. But it's easier just to have a redacted copy. And if I came to your not-for-profit and I said, "I want a copy of your 990, your most current," because what's on the IRS website and GuideStar are at least two years old. So if you filed your 12/31/22 990 already, and I came to your organization and said, "I want a copy of your 990," you're required to give it to me. By IRS law, you're required... Regulations, not law, regulations, you're required to give the 990. So you should keep a copy with the redacted Schedule B or just take the Schedule B out to have it on file, so when you make a copy, you don't accidentally get the wrong one.

Heather Shanahan:

Right, exactly.

Kristen Hoyle:

And it happens.

Heather Shanahan:

Here's a quick question. Who signs the 990? What's the best practice for that?

Kristen Hoyle:

Well, it should be either the executive director or the finance director. It needs to be an officer, but it will be the individual who is taking responsibility for the 990, which is important to realize. And this is another reason, very important reason, to make sure that the 990 is right, because whoever is signing it could be personally liable if there are inaccuracies or false statements within it. So they could have penalties assessed against them. And I don't think a lot of organizations realize that.

Heather Shanahan:

Right.

Kristen Hoyle:

And the board members who are listed on there also have a duty and a responsibility to make sure it's there. So there's a question on the full 990, not the easy, but a question on the 990 that asks, what is your policy for reviewing the 990? And has it been given to all your board members before it's been filed? So that is very important because if I'm on a board, I want to see the 990. Usually I prepare it, so of course I see it. If I'm a board member and my name is on it and it's going out, I would want to see it to make sure that there's nothing crazy. I've seen spelling errors. I've seen things that don't foot, don't add up correctly, that programs are listed incorrectly, the percentages are off. And so it's really important to review it. And if you're signing it, especially if you're signing it, is to make sure that it's correct because your name is on the line. Yeah. You're the responsible person. Who's the reporter going to call? The reporter's going to whoever's signing it.

Heather Shanahan:

Right. Well, our board president sometimes. Did you review it? Do you know what's on there? Your name's listed first. So board member signing it versus staff of a nonprofit, it should be staff of the nonprofit, or what are the circumstances there to consider?

Kristen Hoyle:



It should be whoever has greater knowledge of the financial information. Ideally, it should be both. If you have an executive director and a chairman of the board, they both should review it in detail because they're both ultimately responsible for the financial statements. I'm sort of ambivalent about whether it should be a board member versus an employee as long as that person is knowledgeable and can understand. So under accounting regulations, when I finish an audit and I give a draft to the executive director to review, I have to document why I think that person has the skills, knowledge, and experience to be able to review it properly. Because I've had people look at it and go, "I don't know what this means. You audited, so it must be correct."

Kristen Hoyle:

I don't know what this means. You audited, so it must be correct.

Heather Shanahan:

Yeah, not necessarily. Yeah.

Kristen Hoyle:

It's the only thing in the audit that's mine, that's TJT's, is the audit opinion. The rest of the numbers are yours.

Heather Shanahan:

You provided them.

Kristen Hoyle:

The organization is ultimately responsible for it. I'm going to say if I feel it's incorrect, but that organization has to take some responsibility for it. So you have to be able to at least review it. You don't have to be a CPA, you don't have to ... They changed the rules. You used to have to have been able to draft the statements yourself to be competent to review, but they changed that.

Heather Shanahan:

So I think we see this a lot, speaking of competency and costs and staffing. For an organization, what's better? To hire an accountant internally or outsource? What does that look like these days? What are you seeing?

Kristen Hoyle:

I see more organizations going to outsourcing, because it's hard to hire staff, accounting. The great resignation in the last two years has really done a number on the accounting profession, plus salaries have increased tremendously. So you really need someone that has experience, especially if you're a large, complicated, not-for-profit. If you have a thrift store, and you have inventory and you have contributions and an endowment, you need to have someone that can understand basic accounting. And if it's full time, salaries are 60, 70, \$80,000, depending on the experience. So hard to find someone to be able to do that. You've got to find someone that has the mission heart for it, because it's not going to be for the salary.

So outsourcing allows the organization to maybe hire that same person on a part-time basis to do the basic data, or even to do some of the finance functions. There's a number of firms that do that, and again, like hiring an auditor, you need to vet them and make sure they understand how to do not-for-profit accounting, because it's different with funds and endowments and restrictions. It's really quite complicated. My own church, we had a finance director that had to leave suddenly because she had carpal tunnel syndrome. And just trying to find someone was just heck on wheels. So we ended up hiring outsourcing for our church. So it depends on the individual organization. On one hand, if you need to have someone there on a day-to-day basis that you can

interact with, then you need to hire someone internally. If you can split it and you're OK with not having someone in the office, or if you have multi-locations, churches with lots of locations, my church doesn't have that, but you have lots of locations, or you have a not-for-profit that runs group homes, outsourcing might work better. It might be more cost effective.

Heather Shanahan:

It's hard. I think it's hard either way, outsourcing just the amount of work that it takes to communicate your individual processes and needs to someone to get them up to speed, and they're not going to be physically there. But there's certainly a lot of things to consider. And like you said, they're not great accountants hanging out there, unemployed and wanting to take these things on. It's tough right now.

Well, I could probably ask you a million more questions. This has been super helpful. I think for a lot of organizations it's just things that come up on a day-to-day basis. You just don't know what you don't know. That's the tough thing, too. So truly appreciate all the time that you've spent with us today, and probably need to have you back to get to part two of my questions. But in closing, we always like to ask everyone mission impact, since our name is Mission and Markets. Mission impact, what does that mean to you, either high level or personally, what does that mean for Kristen?

Kristen Hoyle:

So people think accountants just worry with the debits and the credits. And as I said at beginning, I feel a great sense of pride that my work helps an organization to be able to help children. To be able to save horses that actually help children get over trauma. I'm just getting teary-eyed thinking about it.

So I can't do what these organizations do. I want to be able to help the world. It's just the way I am. I'm a bleeding heart. So this is my way to be able to help the world, is to help the organizations help the world. And that's my mission and impact. I feel like if you're more efficient, you're more effective, by the small little things that I do.

Heather Shanahan:

That's awesome. Well, and you do those small little things very well.

Kristen Hoyle:

Thank you.

Heather Shanahan:

Grateful for your time today and for all that you do both professionally and then also personally. You're involved in a lot of different things, so we're fortunate to call you a friend as well. Kristin Hoyle, Thomas Judy, Tucker, appreciate your time today, and we'll talk soon.

Kristen Hoyle:

Thank you, Heather.

Thomas Judy Tucker:

Thank you.

Kristen Hoyle:

Thank you.

Heather Shanahan:

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