



# Fiscal Responsibilities of Attorneys Serving on Nonprofit Boards

*By Carianne Geerts and Deirdre Hodgson*

Nonprofit organizations often seek out attorneys to serve on boards and subcommittees. It is a common way for legal professionals to support charitable activities through means other than cash contributions. Attorneys can be a valuable resource to an organization, but many may not realize their responsibilities as a board member and the impact they will have on the organization.

As a board member, it is important for an attorney to be informed about nonprofit financial statements and to know the right questions to ask in order to reduce fraud risks. Every board member has a fiscal responsibility to the organizations they serve, and understanding these key concepts is a great first step toward embracing that duty.

### Understand how the board can reduce fraud risks

When fraud occurs in any organization, be it a nonprofit or a for-profit business, the organization loses more than just money. While it is true that most organizations that experience fraud never recover the funds lost, there is also the risk of damage to the group's reputation. Here are some critical actions that the board can take to help prevent and/or detect fraud.



#### Establish two key policies

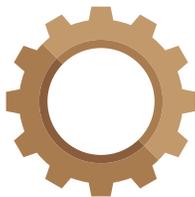
According to statistics compiled by the Association of Certified Fraud Examiners (ACFE) in its 2018 *Report to the Nations*, most fraud is detected through tips from employees, customers, or vendors. Organizations should have a whistleblower policy that includes detailed instructions on how to anonymously report information, how to respond to reports, and what actions can or cannot be taken. Nonprofits should also consider opening a whistleblower hotline (free hotline services are available to nonprofit organizations) to make it easy for informants to step forward. As a board member, you should receive regular reports of whistleblower activity to ensure timely and effective investigation of complaints.

A second action is to establish a conflict of interest policy. Some argue this is the most important organizational policy a nonprofit can have. This written policy will help guide

the organization in determining when a conflict exists and directing administrators on how to handle the situation. The policy should require board members to disclose all conflicts, direct the board on how to discuss conflicts, require the board to document proceedings in the meeting minutes, and require the conflicted member to exclude himself or herself from voting on certain issues.

#### Understand fraud risks

An important part of any management or board position is understanding that fraud risks affect every business, including the nonprofit industry. Boards should encourage management to complete periodic fraud risk assessments and work to identify key areas where controls need to be established. The assessment should address the potential for misappropriation of assets and the risks around fraudulent financial reporting.



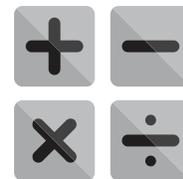
#### Create internal controls

In some cases, board members may think that knowing internal control processes is too “in the weeds” for their role. However, internal controls are the first line of defense to protect an organization against fraudulent activity. ACFE reports that internal control weaknesses are responsible for nearly half of all frauds.

Ensuring a proper segregation of duties, whereby no one person is responsible for initiating, authorizing, and recording a transaction, can reduce the risk that any individual can act alone to commit fraud. The board should be involved in setting the control processes with management if needed. At a minimum, processes should be reviewed annually for potential weaknesses. Ensure that management carries out control processes—any override can lead to fraud risk opportunities. At times, the board may even be a critical part of internal controls, as noted in the next item.

#### Review credit cards and expense reimbursements

Credit cards and employee expense reimbursements create an opportunity for employees to misappropriate the resources of a nonprofit organization. Establishing a clear policy on credit card use and reimbursable expenses is the first step toward preventing this abuse. The policy should detail acceptable use of employer-issued credit cards, travel policies and requirements, and receipt requirements. All transactions, whether by credit card or expense reimbursement, should require review and approval by a supervisory-level position, including board member review of management transactions.



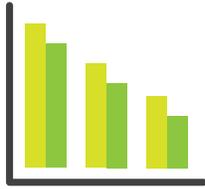
#### Understand nonprofit financial statements

If a board member is new to working with nonprofits, there is a good chance that he or she is not familiar with nonprofit financial statements. The statement of financial position, statements on activities and cash flow, allocation of expenses, endowment requirements, and restrictions on uses of funds are all key areas for board members to have experience with in order to assess fraud risks.

### Take steps to improve your nonprofit financial literacy

Board members and management are responsible for the current and long-term financial health of a nonprofit organization. The topics that follow are just the tip of the iceberg, but they are a good starting point.

## “Taking fiscal responsibility seriously will elevate you as a board member and provide valuable insights to the organization.”



### Financial statements

Four statements are provided to most board members as part of their pre-meeting financial information packets.

#### 1. Statement of financial position:

Shows the assets, liabilities, and net asset balances of the organization at a specific point in time. Analyzing this statement can help assess the reserves and debts of the organization.

**2. Statement of activities:** Shows the revenues and expense of the organization for a period of time. The activity within this statement can be compared against prior periods to assess trends.

**3. Cash flows:** Many organizations prepare this statement to show the sources and uses of cash for a period of time. The statement can also be used to assess trends over time and predict future cash requirements.

#### 4. Statement of functional expenses:

Expenses are allocated into three main categories: program, management and general, and fundraising. This statement can be used to assess how much of each dollar raised is spent on programmatic activities, which is often scrutinized by donors. Understanding allocation methodologies and overhead is a key aspect of this statement.

### Support versus earned income

Generally speaking, nonprofits can categorize income into two main sources: support revenue and earned income. Support revenue includes grants and contributions that may or may not include donor restrictions on the uses of the funds. Earned income includes program revenue, fee for services, and other sales-type revenues. Understanding the difference between these categories can also help identify opportunities for a nonprofit to expand or contract programming.

### Net assets

In business terms, this is the equity of the organization. Net assets are categorized as with or without donor restrictions. Net assets without donor restrictions are available for use as determined by the board and management. Good financial management includes ensuring that net assets without donor restrictions are not negative, as this indicates the organization has greater liabilities than assets.

### With or without donor restrictions

When a nonprofit receives a grant or contribution, the donor can attach restrictions to the use of the funds. The Financial Accounting Standards Board (FASB) recently issued Accounting Standards Update (ASU) 2016-14, which reduced the classes of net assets from three to two: contributions with donor restrictions and contributions without restrictions. Operating a nonprofit comes with an obligation to carry out donor intent.

### Reserves

Determining the proper level of reserves for a nonprofit is an age-old question. While there is no correct answer that applies to every organization, many say that six months of operating reserves is a good amount to have on hand. Board members and management should work to determine what operating reserve goal is best for their organization. In addition, consideration should be given to other reserves, such as a working capital reserves or endowment reserves.

### Increase your value as a nonprofit board member

Taking fiscal responsibility seriously will elevate you as a board member and provide valuable insights to the organization. The above items are just a few of the ways you can jump-start the learning process and get up to speed on key financial topics that will make you a more effective contributor to the board.



**Carianne Geerts**

[Carianne.Geerts@claconnect.com](mailto:Carianne.Geerts@claconnect.com)

Ms. Geerts is a manager with CliftonLarsonAllen and has seven years of experience. She specializes in nonprofit audit and tax.



**Deirdre Hodgson**

[Deirdre.Hodgson@claconnect.com](mailto:Deirdre.Hodgson@claconnect.com)

Ms. Hodgson has 14 years of experience in public accounting and works exclusively in the nonprofit area for CliftonLarsonAllen. She leads the global services initiative for the Nonprofit Group and is a member of the firm's Young Executive Team.