BY DESIGN:

Best Practices for Organization Governance and Operations

By Design was created by NeighborImpact after August 2021 listening sessions during which NeighborImpact partners said they needed more information on the management and operation of a nonprofit. NeighborImpact needs reliable partners to leverage its work and resources, and investing in the operational strength and capacity of our partners help us do more. We are proud to bring you the inaugural edition of our newsletter, which is distributed quarterly.

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Talk with Me:

Suzette Chapman, NeighborImpact's Chief Development Officer, moved to Central Oregon from the Columbia Bottomlands ecosystem, south of Houston, Texas, where she lived on 48 glorious acres of old growth, forested wetlands and

Managing Restricted Gifts

Good News! You organization has just received a generous gift from a devoted donor or a substantial grant from a supportive foundation. Hopefully, either gift will give you a great opportunity to move forward with your mission and strengthen your nonprofit.

But before you blow up the balloons or pop the cork on the champagne, be sure you've really understood any restrictions or limitations the donor/foundation has imposed on how or when you may use their gift. While these sound like straight-forward questions, they are not always easy to answer. And getting the answer is only the starting point for the care you may need to take to be sure you have not only honored the donor's intentions but have documented how and when you used the funds.

Some donors make their intentions explicitly clear. They provide written descriptions of any limitations they want to impose on the use of the funds and specific guidance on the timing for their use. Unfortunately, many donors are not quite this clear. *You have a really strong* worked as a grant proposal writer. She holds a BA and MA in English from the University of Houston, graduating Summa Cum Laude. Suzette was born in Corpus Christi, Texas, but grew up in Caracas, Venezuela and graduated high school from the American School in Mexico City, Mexico. She speaks fluent Spanish and just enough French to confuse people. Suzette is responsible for fund development, marketing, and fundraising activities. She supervises the Development, Communications and Social Media programs and (still) writes grant proposals. She reads a lot and regales us with trivia; she also corrects our grammar and punctuation. She lives on 40 acres near La Pine with her two dogs (Julie and Joe) and her cat (Moira Rose.) Suzette loves nature, dogs, thought-provoking movies, fine literature, '60s and '70s music, and Bruce Springsteen.

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need to know the answer in order to meet your legal responsibilities and maintain positive relationships with donors. So, when gifts arise without explicit instructions, you'll need to do some detective work. First, review any correspondence you've had with the donor. Did you ask for funding for a specific purpose or specific time period? Did you say things like "your gift will be used exclusively for our new children's project" or did you simply describe the new children's project and then say, "We need your help to make needed services like this possible". Did a representative of your organization have a conversation with the donor in which they asked for support for a specific project or cost? Similarly, if you submitted a written proposal to a foundation, did you ask for support for specific activities and costs?

Of course, what you said (in writing or in conversation) is only part of the story. Your detective work will need to include gathering information about what the donor said – in conversation with a representative of your organization or in writing.

If your research shows that the donor responded to an appeal for a specific purpose or defined a specific purpose for their gift, and your organization accepted the gift, then *you have a legal responsibility to be sure that the gift is used only for the purposes the donor has intended it for.* Accountants will call such gifts "donor restricted". Before we dive into how you will make sure you are managing these donor-restricted gifts properly, we need to clarify an important distinction: Only a donor can create a donor-restricted gift. If you've received gifts or grants that have no donor restrictions, but your Board or your staff have decided that they intend to use such gifts for a specific purpose, the gift itself is still considered unrestricted, not donor-restricted.

Once you're clear that you have received a donor-restricted gift, you'll need to be sure that your accounting system is ready to record both the gift as donor-restricted and the ways that you have used it.

Your system needs to make it simple for you to see how much of the restricted gift you have used for the restricted purposes and how much is left to be spent on those purposes. Very small organizations will sometimes try to do this tracking by placing the restricted gift in a separate bank account and only drawing from that account for expenses that meet the donor's restrictions. This approach becomes problematic as your organization grows and has more than one restricted gift to manage. A much simpler and more reliable approach involves setting up your accounting system to make tracking and reporting easy.

Using QuickBooks to Track Use of Restricted Gifts

If your nonprofit uses QuickBooks for its accounting, the simple way to do the tracking is to use the "Classes" feature. You can set up a simple system for tracking restricted gifts by establishing a "Class" for

Using Spreadsheets to Track the Use of Restricted Gifts

If you're hesitant to use the QB Classes, you can continue using QB to record all your expenses by category and then set up a spreadsheet to list the date, amount, each restricted gift or grant. Use your basic account structure to identify the purpose of each expense – for example – salaries, supplies, transportation, utilities. When recording expenses that meet a donor's restrictions, you'll first code the expense by purpose- for example, supplies – and then add a Class code to tag the expense as supported by a restricted gift or grant. You can produce a report of expenses by Class for any time period and see how you have used each of your restricted gifts.

payee, and check number (or ACH transaction number) of each expense that meets the requirements of a specific restricted gift.

This method creates some extra work but will result in a complete list of the expenses you've attributed to each restricted gift or grant.

Tracking How Much Of Each Restricted Gift is Left to be Expended

If you decide to use QB Classes to track donor restricted gifts, you will want to record each restricted gift you receive in the Class you have set up for that gift. Once you have the restricted gift recorded as donor restricted income and have recorded the expenses that meet the restrictions for that gift in the correct Class, you can easily compute the difference to see how much of the gift is left to be spend. If you are using spreadsheets to track restricted gifts, you'll need to add an income section to your spreadsheet and then compute the difference between the gift you received and the expenses you have recorded that meet the donor's restrictions.

This process becomes more complicated when you are not able to fully expend the restricted gift in the year in which you receive it. More sophisticated accounting systems will record the receipt of a restricted gift in a separate Donor Restricted Fund (an accounting fund, not a bank account). At the end of each month, they will total up all the expenses which met the requirements of that restricted gift and post a journal entry to "release" that total amount from the Donor Restricted Fund. At the end of the fiscal year, any donor restricted funds that have not yet been "released" will be considered part of the Donor Restricted Net Assets on the Balance Sheet.

> "The small amount that you may have to pay for assistance will produce big savings when you have easy access to all the info you need."

Less sophisticated accounting systems will use an old fashioned but simpler method. Rather than immediately recording a donor restricted gift as revenue, they will initially record it as Deferred Revenue or Funds Received in Advance, which is a liability-type account on the Balance Sheet. Each month, after they have totaled up the expenses which meet the donor's restrictions, they will post a journal entry to reduce the Deferred Revenue liability account and increase the Restricted Gift revenue account. At the end of the fiscal year, any of the donor restricted gift that has not been expended will remain in the Deferred Revenue account. Throughout the year, you will be able to see how much of each restricted gift is left to be expended by looking at the Deferred Revenue account.

If your systems aren't making it easy to record and report on Donor Restricted gifts, you'll want to get help from an accountant with experience dealing with donor restricted accounting systems. The small amount that you may have to pay for that assistance will produce big savings when you have easy access to all the info you need to make good decisions about using the restricted gift and to produce clear, consistent reports for your funders.

Once a gift is restricted, it remains restricted in perpetuity. Neither staff nor board can release a restricted gift to an unrestricted or other-restricted purpose. If there are funds left over after a project is completed, you must seek input and permission (preferably written) from the original donor before changing status for the funds.

Key Strategies for Soliciting and Managing Gifts

Of course, accounting and reporting isn't the only challenge that comes with receiving donor restricted funds. The bigger challenge may lie in deciding how you will actually use the donor restricted gift in ways that fulfill the donor's restrictions and being sure that you follow through on those decisions as you incur and record expenses.

"Even donors with great respect for your organization may have very strong preferences or priorities for which of your programs/projects they want to support."

A still bigger challenge lies in being strategic about how you ask for gifts and grants. Ideally, all of your donors and funders will have tremendous respect for your organization and have confidence that you will make wise decisions on how to use all of the funds you are able to obtain. Donors with this confidence will be willing to make their gifts without restrictions, counting on your staff and Board to make good decisions on spending choices.

However, even donors with great respect for your organization may have very strong preferences or priorities for which of your programs/projects they want to support. Working with these donors, you'll want to propose that they restrict their gift at the program/project level rather than at a line-item level. For example, an organization that provides services for seniors, for preschoolers, and for people experiencing homelessness, may identify a funder that is only interested in supporting services for seniors.

In this situation, the organization will want to ask for a gift to support our work with seniors, rather than assuming that the donor wants to see a very detailed list of specific expenses in the senior program that their funds will purchase. The donor may be satisfied to simply review the full budget for the senior program and be asked to contribute towards the program as a whole. For such donors, a report on the total costs of the senior program, that also shows the sources that contributed, will probably be fine.

" Focusing your initial conversations on what the program or organization will accomplish often results in stronger, long-term relationships."

Of course, some donors and funders will insist on seeing which supplies for seniors their dollars will buy as opposed to supplies that other funders will buy. Often this preoccupation with "slice and dice" presentations of the exact expenses a donor's funds will cover comes from a miscommunication between nonprofit and donor – with the nonprofit assuming that the funder requires much more detailed info than the funder actually wants or needs. Experienced fund raisers learn to focus first on building the donor's interest in either the work of the entire organization or the accomplishments of a specific program, and then provide fairly summarized information about the costs involved. They can always follow up with more details if the funder requests them but focusing your initial conversations on what the program or organization will accomplish often results in stronger, long-term relationships, as well as significantly less time being devoted to detailed record keeping and reporting.

About NeighborImpact: NeighborImpact is a private non-profit governed by a board of directors drawn from across the community. Since 1985, NeighborImpact has led the region in developing solutions and bringing resources to Crook, Deschutes and Jefferson counties and the Confederated Tribes of Warm Springs. We help meet the basic needs of Central Oregonians, build economic security and create a community where everyone thrives. To learn more about NeighborImpact please visit www.neighborimpact.org.

About The Author: Kay Sohl has provided training and consultation for Executive Directors, CFOs, and Boards of Directors of over 8,500 nonprofit organizations throughout the United States. Kay founded and lead TACS, now known as the Nonprofit Association of Oregon. She is a licensed CPA and a frequent consultant and presenter. She is co-author of the Oregon Nonprofit Corporation Handbook.

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