

WINDES NONPROFIT ADVISOR



The [Windes Nonprofit Advisor](#) is a periodic technical publication focusing on the tax, regulatory, and accounting issues confronting nonprofit organizations.

The [Windes Nonprofit Group](#) possesses extensive experience in preparing and reviewing more than 150 Forms 990, 990-T, 990-PF, and state tax-exempt forms, in addition to having experience in the preparation and filing of both federal and state tax exemption applications for public charities, private foundations, and other exempt organizations. Furthermore, we can assist in providing valuable guidance (governance / reasonable compensation documentation / public support test / special events / lobbying / transactions with related parties) to nonprofit organizations.

The Windes Nonprofit Group prepares audited financial statements and ERISA audits for more than 125 nonprofit organizations. For retirement plans, Windes has experts on staff for 403(b) plan administration and compliance, including plan document issues, Form 5500 preparation and filing, non-discrimination testing, and government compliance programs.

Our [Nonprofit Team](#) is composed of the following individuals who are dedicated to providing nonprofit organizations with high-level tax, regulatory and accounting consulting, tax compliance services, and financial statement audit and assurance services:

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Please do not hesitate to contact any member of the Windes Nonprofit Group toll free at **844.4WINDES** (844.494.6337) or via email at nonprofit@windes.com.

HOW LLCs CAN BE RECOGNIZED AS TAX-EXEMPT ORGANIZATIONS

On October 21, 2021, the IRS released an advance version of Notice 2021-56 that sets forth standards that a limited liability company (LLC) must satisfy to receive a determination letter recognizing it as tax-exempt under section 501(a) and described in section 501(c)(3).

[Notice 2021-56](#) notes that the IRS will issue a determination letter recognizing an LLC as described in section 501(c)(3) only if both the LLC's articles of organization and its operating agreement include:



- Provisions requiring that each member of the LLC be either
 - an organization described in section 501(c)(3) and exempt from taxation under section 501(a); or
 - a governmental unit described in section 170(c)(1) (or wholly-owned instrumentality of such a governmental unit).
- Express charitable purposes and charitable dissolution provisions in compliance with existing regulations under section 501(c)(3)
- The express chapter 42 compliance provisions described in section 508(e)(1), if the LLC is a private foundation
- An acceptable contingency plan (such as suspension of its membership rights until a member regains recognition of its section 501(c)(3) status) in the event that one or more members cease to be section 501(c)(3) organizations or governmental units (or wholly owned instrumentalities thereof)

BACKGROUND

Regulations surrounding exempt organizations were issued well before any states enacted the first LLC statute. As a result, the regulations don't specifically address LLCs.

Historically, IRS standards applied in issuing determination letters to LLCs generally required LLC members be 501(c)(3) organizations, governmental units, or wholly owned instrumentalities of a state or political subdivision of a state.

STATE LAWS

If an LLC is formed under a state LLC law that prohibits the addition of provisions to articles of organization other than certain specific provisions required by the state LLC law, the above requirements will be deemed satisfied if the LLC's operating agreement includes the provisions described above and if the articles of organization and operating agreement do not include any inconsistent provisions.

The notice also provides that the LLC must represent that all provisions in its articles of organization and operating agreement are consistent with applicable state LLC law and are legally enforceable.

In addition, to assist the U.S. Treasury Department and the IRS in determining whether additional guidance is needed, the notice requests public comments on this notice, as well as specific issues relating to tax-exempt status for LLCs.

This notice does not affect the status of organizations currently recognized as described in section 501(c)(3).

For more information or questions about this article, or to find out how [Windes can assist](#), please contact Shalini Saidha at ssaidha@windes.com or **844.4WINDES** (844.494.6337).

REFORMING DISTRIBUTION REQUIREMENTS FOR DONOR ADVISED FUNDS AND PRIVATE FOUNDATIONS

In the summer of 2021, The Accelerating Charitable Efforts (ACE) Act was introduced in the US Senate. The goal of the proposed legislation is to have the funds held within private foundations (PFs) and donor advised funds (DAFs) moved into the hands of charitable organizations faster. Individuals can then take advantage of the tax deductions to PFs and DAFs even though their donations are not going directly to working charities. The bill would impact individual donors, PFs, DAFs, and also public charities that receive donations from DAFs.

IMPACT ON DONOR ADVISED FUNDS

At issue with DAFs is the lack of a requirement for when the funds must be distributed to a public charity, unlike private foundations that must distribute 5% of assets annually. To address this, the Ace Act would divide DAFs into qualified and nonqualified funds (with a special exemption for DAFs held in certain community foundations). Qualified DAFs (Q-DAFs) would be required to distribute funds within 15 years of their contribution or have the donor's privileges released, while Non-qualified DAFs (NQ-DAFs) would have 50 years. Sponsoring organizations will face an excise tax equal to 50% of the amount of the contribution and attributable earnings that have not been distributed.

Donors who contribute to a Q-DAF would still be able to immediately deduct contributions on their individual taxes, while contributions to a NQ-DAF would only be deductible when the funds are ultimately distributed by the DAF. Gifts of complex assets that cannot be readily valued would be deductible when the assets are sold by the DAF and cash proceeds are distributed (and the eventual deduction would be limited to the cash proceeds from the asset's sale). Donors who contribute to a NQ-DAF, though not immediately deductible, would still be able to receive capital gains and estate tax benefits upon donation.

Community foundations (CFs) holding DAFs would be offered a limited exemption from these required distribution rules and different distribution requirements for those DAFs that are not exempted. Again, the legislation would divide



CFs into Qualified and Non-qualified organizations. A qualified CF (Q-CF) must be a 501(c)(3), serve the needs of a geographic community that is not larger than 4 states, and whose total assets must exceed 25% from non-DAFs funds.

A DAF held at a Qualified Community Foundation will be exempted from required distribution rules if its value does not exceed \$1 million, or the aggregate value of all DAFs held by one individual does not exceed \$1 million. If the value exceeds \$1 million, then it must distribute at least 5% of the DAFs assets annually, or distribute funds within 15 years of their contribution, to be a Qualified DAF.



IMPACT ON PRIVATE FOUNDATIONS

With respect to DAFs, the bill would no longer allow distributions to DAFs from PFs to count towards the PFs annual distribution requirement unless the DAF distributes those funds by the end of the following year.

PFs already have an annual distribution requirement for 5% of total assets, but this bill would offer an exemption from the 1.39% excise tax on investment earnings for any year when the organization distributes 7% or more.

PFs could also be exempt from the 1.39% excise tax if it is a “limited duration” private foundation, (which has a duration of 25 years or less specified in its governing documents) and it makes no distributions to other private foundations (other than limited duration PFs) which share a disqualified person in common.

Also, at issue with PFs (not specifically related to DAFs) are the salaries, travel, and administrative expenses deemed reasonable and necessary expenses of the foundation that count toward its annual distribution requirement but are paid to family members of disqualified persons. Under the act, such expenses would no longer count toward the annual distribution requirement, but administrative expenses paid to a foundation manager who is not a family member of a disqualified person would continue to count.

IMPACT ON PUBLIC CHARITIES

Working charities that receive contributions from DAFs may also be impacted by the Ace Act, which makes reforms to the reporting of DAFs on the Public Support Test (Schedule A of Form 990). Under current law, DAFs and sponsoring organizations are considered 501(c)(3) public charities and their contributions are thus excluded from consideration as excess contributors. The Ace Act would require that DAFs which identify the original donor would be aggregated with other donations received from that donor. If the original donor is not identified then, the organization must combine all the anonymous DAF contributions received from all sponsoring organizations and consider them to be received by a single donor, subject to the excess contributor rules.

However, if a sponsoring organization made a donation from its own funds (not from a DAF), this would continue to be considered as received by a 501(c)(3) public charity that is exempt from consideration as an excess contributor.

Organizations that receive a large amount of anonymous DAF gifts could see their public support percent drop if this becomes law. Public charities must keep their public support percent above 33.33% each year to maintain their tax-exempt status. If this rule could jeopardize an organization's public support test, it is recommended they request that sponsoring organizations identify the original donors.

STATUS OF THE ACE ACT

The Ace Act was introduced in the summer of 2021 and was referred to the Committee on Finance. There has been no other action.

While the reforms in the bill have been called for by coalitions of philanthropic and nonprofit leaders to hasten access to hundreds of billions of dollars held in DAFs and PFs, sponsoring organizations and their advocates say that the regulatory requirements are too complex and would make administering DAFs too difficult, and thus reduce overall amount of giving.

Steve Taylor, Senior Vice President and Counsel for Public Policy at United Way Worldwide, believes the bill will not move forward because there are many important bills already in Congress, and because the nonprofit sector itself is not unified behind the bill.

If the Ace Act does fail to move forward, this will likely not be the last time these or similar reforms are considered. Four years before the bill was introduced, the IRS released Notice 2017-13 stating that the agency was considering developing regulations to address the concerns of DAFs. The IRS has not taken further action since releasing the notice, but the Ace Act did attempt to move forward on DAF regulations, and the concerns around DAFs has not diminished.

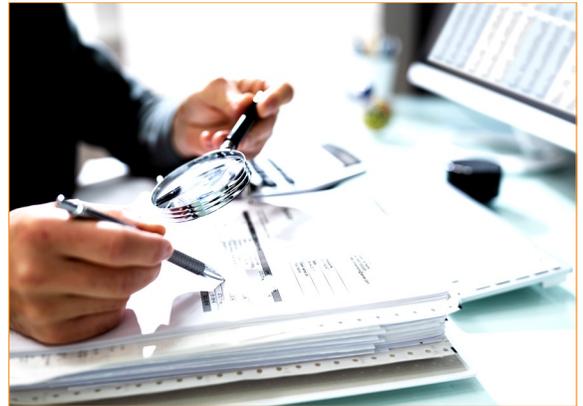
For more information or questions about this article, or to find out how [Windes can assist](#), please contact Aaron Phillips at aphillips@windes.com or **844.4WINDES** (844.494.6337).



EMPLOYEE BENEFIT PLAN AUDIT: WHAT IT IS & WHY IS IT IMPORTANT?

What is an employee benefit plan (EBP) audit, and how can it help businesses? This is an important question. An audit is essential to ensure that your employee benefit plan complies with all applicable rules and regulations and to comply with Department of Labor (DOL) requirements.

The primary goal of ERISA is to safeguard EBP participants and their benefits. ERISA guarantees that EBPs follow guidelines that protect the employee benefit plan administrators from misusing plan assets.



When your plan reaches a certain participant count, it's time to hire a certified public accountant (CPA) to audit financial statements to ensure your plan is compliant with regulations. In general, an audit is required if your plan has more than 100 participants as of the beginning of the plan year. The audited plan financial statements are filed with Form 5500 on an annual basis and are subject to DOL and IRS review. Form 5500 is part of ERISA's comprehensive reporting and disclosure framework designed to verify that EBPs are managed and operated in accordance with relevant standards and procedures. The main goal of this system is to deliver crucial information to participants, beneficiaries, and regulators to preserve beneficiaries' and participants' rights.

It is critical to carefully follow each stage of this process because if Form 5500 is not filed on time, or the submission is refused, a fine may be levied until the filing is completed accurately.

WHAT IS AN EMPLOYEE BENEFIT PLAN AUDIT?

The purpose of an audit of an employee benefit plan's financial statement is to ensure the plan's financial integrity in order to deliver health, retirement, and other benefits to plan participants throughout the course of payments.

According to the American Institute of Certified Public Accountants (AICPA), financial statement audits for all employee benefit programs should cover benefit payments, participant data, contributions (employer and employee), investments, participants' loans, participants' allocations, costs of administration, and obligations and responsibilities under the plan.

However, employee benefit plan audits can be tricky and require auditors experienced in plan audits. In addition to financial reporting and audit requirements, the plan is also reviewed for certain DOL and IRS compliance requirements which can sometimes make it more complex than a financial statement audit.

THE EMPLOYEE BENEFIT PLAN AUDIT PROCESS

During an [employee benefit plan audit](#), the audit firm looks for any major misstatements in the financial accounts, which could result from deceitful reporting or unintentional errors. The auditor works with plan management, the recordkeeper, and the third-party administrator to perform detailed tests on a sample of transactions. The audit firm will also look to identify control weaknesses and operational errors as part of the audit process and make recommendations for control improvements or corrections to get the plan into compliance.

By assessing the strengths of the internal controls involved in financial reporting, an employee benefit plan audit may assist a company in streamlining and making the plan's operations more efficient.

HOW WINDES CAN HELP

Windes is dedicated to providing clients with the highest level of trust and confidence when it comes to auditing their employee benefit plans. Our members are experts in auditing standards, DOL, and ERISA filing requirements.

For additional information on how we may assist your company, or for a [complimentary plan audit quote](#), connect with us today.

CYBER INSURANCE AND PREMIUM INCREASES

While businesses are susceptible to numerous physical dangers, including property damage, loss, and injury, your firm also faces hazards associated with technology use. These range from data breaches to cyberattacks. To mitigate these risks, many organizations supplement their business insurance coverage with cyber insurance. This provides additional protection beyond their existing cybersecurity efforts. Read on to learn more about cyber insurance and the latest premium increases.



WHAT IS CYBER INSURANCE?

Cyber insurance is a type of insurance that provides comprehensive coverage to safeguard businesses against various technology-related threats. Generally, two distinct cyber insurance products are available: Data breach insurance and cyber liability insurance.

Data breach insurance assists your firm in responding to security breaches and may provide sufficient coverage for small and medium-sized business owners. Cyber liability insurance is often reserved for larger firms and provides additional coverage to assist with the prevention, response, and recovery from cyberattacks.

WHY BUSINESSES REQUIRE CYBER LIABILITY OR DATA BREACH INSURANCE

Hackers target sensitive information, including personally identifiable information (PII) or protected health information (PHI), stored on your organization's computers. That is why it may be critical to safeguard your organization with a data breach or cyber liability insurance, which will assist you in quickly responding to a data breach or cyberattack.

These coverages may be beneficial if your business's computers become infected with a virus, exposing private and confidential data. It can also assist businesses in case customers or patients sue the organization over the loss of PII or PHI. Hefty public relations expenditures as a result of a data breach may also be covered.

It is critical to understand what your business insurance covers. This is particularly true in the case of cyber insurance. While both policies have some benefits, they safeguard your organization in unique ways and should be considered supplemental to your cybersecurity efforts.

WHAT IS DATA BREACH INSURANCE?

This insurance covers you in the event that PII or PHI is lost or stolen, whether as a result of your network being hacked or an employee leaving their laptop in a restaurant. If your small business is a victim of a data breach, this coverage can assist in paying for the notices to customers, patients, or employees who are impacted, and also the services of a public relations business.

It may also help provide credit monitoring services to victims of data breaches. You can consider adding the following coverages to your plan:

- Coverage for company income and additional expenses to replace lost income if you are unable to operate your business due to a data breach.
- Prior actions coverage to pay for claims resulting from a breach that occurred prior to the effective date of your policy.
- Extortion Coverage to cover the cost of ransoming your business's data if someone steals it and demands a ransom.

WHAT IS CYBER LIABILITY INSURANCE?

Cyber liability insurance, tailored for larger businesses, assists in recouping financial losses incurred as a result of cyberattacks or other technology-related dangers, as well as private investigations or lawsuits in the aftermath of an attack. For instance, if a hacker seizes control of your systems, begins deleting files, and demands a ransom, this insurance can assist you in responding to the attack and reclaiming lost assets and revenue.

In case of a cyberattack, cyber liability insurance can assist in covering the legal services that assist you in complying with state and federal rules, expenses associated with notifying impacted customers, and extortion payments made to unlock encrypted files following a ransomware assault.

It will also cover income lost due to a network failure and any fines imposed by state and federal regulatory agencies.

WHAT IS NOT COVERED IN CYBER LIABILITY AND DATA BREACH INSURANCE

It is critical to understand that these insurance policies do not cover all types of claims. Additional types of business insurance may be required to establish a full protection plan, including the following:

- Commercial property insurance protects the physical site and equipment of your firm, whether it is owned or rented.
- General liability insurance protects your organization against accusations that it caused property damage or personal injury.
- Employment practices liability insurance can help protect your business against employee claims of harassment, discrimination, or wrongful termination.
- Professional liability insurance protects you against claims arising from errors or omissions in the performance of your professional business services.

THE COST OF CYBER INSURANCE

With numerous factors to consider, the cost of cyber insurance will vary from one organization to another. The cost of a data breach or cyber liability may vary depending on the customer, client or patient count, the type of sensitive data and information, and revenue history.

Cyber insurance rates for small firms have grown 7% year over year, and smaller organizations classified as low-risk pay an average yearly cyber insurance premium of \$1,589 for \$1 million in coverage. These increases were closer to 20% for midrange and larger firms. An ongoing cyber insurance premium rise is expected until 2022.

One specialty insurance distributor warned that there are fewer insurers willing to insure \$10 million limits, and the majority of customers that acquired a \$10 million limit from a single carrier in 2020 will see their limits halved.

As ransomware extortion demands continue to rise, limit adequacy may become an issue. However, benchmarking acceptable limitations is impossible given the current level and continuous expansion of ransomware demands. Ransomware has been the leading cause of claims in the last year, both in terms of severity and frequency.

DOES YOUR ORGANIZATION NEED CYBER INSURANCE?

All businesses should consider making an [investment in cybersecurity](#), especially if their operations involve handling sensitive business, customer, or patient data. Here is what to consider when deciding whether your organization requires additional data breach or cyber liability insurance:

- Do we collect, store, transmit, or receive personally identifiable information (PII) or protected health information (PHI)?
- What would we do if we were subjected to a cyberattack?
- Do we operate in an industry that requires us to adhere to strict privacy regulations, such as healthcare, education, or finance?

PROTECT YOUR DATA WITH WINDES CYBER SECURITY

Most small firms may not require more than data breach insurance. On the other hand, larger organizations or small businesses with a high volume of sensitive data may require cyber liability insurance for additional protection beyond standard data breach coverage.

In any case, it is essential to understand that cyber insurance is an additional safeguard to the [comprehensive cybersecurity services](#) provided by Windes. Insurance does not replace having reliable cybersecurity in place.

To learn more about our services and how to better safeguard your organization, request a [complementary cybersecurity health check](#) from Windes today.



WINDES

AUDIT | TAX | ADVISORY

Windes is a recognized leader in the field of accounting, assurance, tax, and business consulting services. Our goal is to exceed your expectations by providing timely, high-quality, and personalized service that is directed at improving your bottom-line results. Quality and value-added solutions from your accounting firm are essential steps toward success in today's marketplace. You can depend on Windes to deliver exceptional client service in each engagement. Since 1926, we have gone beyond traditional services to provide proactive solutions and the highest level of capabilities and experience.

The Windes team approach allows you to benefit from a wealth of technical expertise and extensive resources. We service a broad range of clients, from high-net-worth individuals and nonprofit organizations, to privately held businesses. We act as business advisors, working with you to set strategies, maximize efficiencies, minimize taxes, and elevate your business to the next level.



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