



Chapter 5

What Did the Filer Spend its Money On?

Lines 13-18 of Part I on page 1 constitute the Expenses section of Part I. They provide an overview of the filer's expenses which are detailed in Part IX (Statement of Functional Expenses) on page 10. (Part IX is discussed below.)

Line 18 (Total expenses) of Part I reports total expenses. We have already suggested that the total expenses reported at Line 18 is a good way to get a quick idea of how extensive a filer's activities are. The expenses reported on Lines 13-18 of Part I are not broken down into functional categories (program, management and general and fundraising expenses), although they are on Part IX. Thus, so far as determining percents of various functional categories of expenses as a percent of total expenses, with the exception of fundraising costs (Line 16b), one has to turn to Part IX to get an idea of how much the filer spent on program and management and general as compared to total cost and as compared to each other.

There are some valuable things, however, that you can find out from the Expenses section of Part I on page 1. Line 13 (Contributions and grants) gives you an idea of whether the filer made grants and if grant making is major part of the filer's activities. (Many charitable nonprofits do not make grants so this line in many cases will report 0.) Line 14 (Benefits paid to or for members) relates to such things as the filer paying for insurance benefits, death, sickness, hospitalization benefits and the like for its members. (Most charitable nonprofits do not make such payments so this line in many cases will report 0.) Line 15 (Salaries, other compensation, employee benefits) reports total compensation paid to the staff. This number provides the reader with a good idea of the size of the filer. If it is divided by the number at Line 5 (Total number of employees), one can get a rough idea about the level of salaries paid at the filer for the year being reported on. Line 16 has to do with fundraising and it is believed was inserted to satisfy state regulatory authorities that tend to be very concerned

about high fundraising expenses. Line 16a (Professional fundraising fees) reports the amounts paid for professional fundraising services which include such things as solicitation campaigns and advice or other consulting services supporting in-house fundraising campaigns. It may be of interest to a reader how much is paid for these particular services. Line 16b (Total fundraising expenses) reports all fundraising expenses (in-house, outside and everything paid for printing, mailing and the like.) If this figure is divided by total expenses at Line 18 something like a fundraising ratio will result – the amount spent on fundraising as compared total expenses. (This is addressed shortly.) Line 17 (Other expenses) includes a wide range of object expenses (legal fees, office expenses, occupancy expenses (e.g., rent), travel and much else). This total figure does not tell one much, and the reader should go to Part IX on page 10 to find out more about these other expenses.

Part IX (Statement of Functional Expenses) on page 10 elicits information on the filer's expenses. It provides some 24 lines of what accountants call object expenses (compensation, office expenses, travel, etc.) allocated by three functional expense categories: (i) program service expenses, (ii) management and general expenses, and (iii) fundraising expenses. For each line the total amount spent is reported at column (A) and then this amount is broken down between the three functional expense categories: column (B) – program expenses, column (C) - management expenses, and column (D) – fundraising expenses. In some cases an expense will be divided amongst all three categories of functional expenses, as may be the case with compensation and in some cases it may be reported for only one functional expense category or two.

Program services expenses are those incurred to carry out the organization's mission. Thus, expenses incurred by a social services organization in paying its social workers for delivering services to its clients would be program services expenses. By like token, payments made by a performing arts organization to produce a play would be program services expenses. For a 501(c)(3) group, the activities that these expenses support are usually the basis of the organization's tax exemption.

Management and general expenses are those incurred in connection with providing overall administration to an organization. These include such things as the costs of preparing for and holding board meetings, working on office management and personnel problems, and accounting and investment activities. The Instructions make clear

that, for example, the expenses incurred in carrying out activities such as the supervision of program services or fundraising are included under those categories and are not included under management and general. Thus, for example, expenses incurred in preparing for and attending a staff meeting called to plan for a future program initiative or to assess present program activities would be part of the program services category (column B) and not the management and general category (column C). For many small organizations with small staffs, it is likely that management and general expenses will be low as most of management's time of these groups is spent on supervising the program and fundraising and relatively little on overall management activities.

Fundraising expenses are pretty much self-defining. The Instructions define this category as including "... all expenses including allocable overhead costs incurred in: (a) publicizing and conducting fundraising campaigns; and (b) soliciting bequests and grants from foundations or other organizations, or government grants."

Some believe that nonprofits should not spend an overly large part of their resources on fundraising. If a reader of the Form 990 is of this view, she might look to see what percent of total expenses is made up of fundraising expenses (Line 25, column D – Fundraising expenses divided by Line 25, column A – Total expenses).¹ For example, if Line 25, column D reports \$300,000 of fundraising expenses and Line 25, column A reports \$2,000,000 in total expenses, fundraising expenses make up 15% of total expenses ($\$300,000/\$2,000,000 = 15\%$). Some refer to this as the "fundraising ratio." As suggested, the reader may have views about how low this ratio should be. We suggest, however, that care should be taken in interpreting this "fundraising ratio." If, for instance, a group is new or advancing an unpopular cause, it may need to spend more on fundraising than a group that has been around for some time or is doing something recognized by all as useful. The Form 990 does not elicit these kinds of qualitative differences.² Furthermore, a group which spends a fair amount on fundraising (and has a high "fundraising ratio") may, as a result of the increased revenue resulting from such efforts, be able to do a lot more

¹ As suggested above, this ratio can also be derived by dividing Part I's Line 16b (Total fundraising expenses) by Part I's Line 18 (Total expenses) found on page 1.

² By looking at Line L (Year of formation) at the top of page 1 of the Form 990, one can determine how long the filer has been in existence.

than a group which spends very little on fundraising (and has a low “fundraising ratio”) and consequently generates less income.³

As mentioned above, Part IX on page 10 breaks down all expenses into 24 object expenses. We now address this component of Part IX.

Lines 1-3 report information about grants: Line 1: grants to governments and other U.S. organizations; Line 2: grants to individuals in the U.S.; and Line 3: grants to organizations and individuals outside of the U.S. The total of these three lines is reported at Line 13, Part I on page 1. These three lines provide a somewhat more detailed picture of the filer’s grant-making activity. As suggested above many filers will not show any grant making activity.

Line 4 reports on benefits paid to members. This amount is also reported at Line 14 of Part I. (Discussed at the beginning of this chapter.)

Lines 5-10 report on compensation information: Line 5 reports on top management officials and Line 7 on other salaries. As explained in Chapter 6, there is a way for approximately comparing how much top management officials get paid to how much the rest of the staff is paid. Line 6 reports on compensation paid to disqualified persons (not included in Line 5) as defined under section 4958. See the Expansion on section 4958. Line 8 reports on pension plan contributions (including 401(k) employer contributions). And Line 9 reports on other employee benefits.

Lines 11-23 report on various kinds of expenses and are pretty self-explanatory. We will comment on just a few of them. Line 11b reports on legal expenses. If the amount is large, a question may be raised. And this is particularly so if the reader has access to several of the filer’s Forms 990 which do not report high legal expenses. Line 17 reports travel expenses. If the filer does not seem to be the kind of organization which would normally incur travel expenses and the number is large, a question may be raised in the reader’s mind. A similar comment applies to Line 19 (Conferences, conventions and meetings). Line 20 reports on

³ Similar ratios can be derived showing what percent of program expenses is made up of total expenses (Line 25, column (B) – Program service expenses divided by Line 25, column (A) – Total expenses) or what percent of management and general expenses is made up of total expenses (Line 25, column (C) – Management and general expenses divided by Line 25, column (A) – Total expenses).

interest payments, not including mortgage interest. If these are large, it may warrant some further attention. In particular one may want to look at Line 24 (Unsecured notes and loans payable) of Part X (Balance Sheet) on page 11.

Line 24 reports on the filer's other expenses that are not reported at Lines 1-23. Five sublines (a-e) are supplied for the five largest dollar amounts, and a final subline, f (All other expenses), reports the total of all other expenses. In the previous Form 990, this breakout didn't exist, and this had been a line where some filers put some expenses they would rather not have seen under the category miscellaneous. This line now makes clear that if Line 24f expenses grouped together and labeled miscellaneous exceed 10% of total expenses reported on Line 25 to list them in Schedule O.

Line 25 reports the total of all the expenses listed at Lines 1-24.

Line 26 reports joint costs. Some organizations include program related (educational) material in their fundraising solicitations. In such cases the filer would report the costs that were for such "educational," etc., material as program expenses on Line 25, column B (and in column B on some line or lines above Line 25) and on Line 26, column B. It would also report the costs of fundraising incurred in connection with such solicitations as fundraising expenses on Line 25, column D (and in column D on some line or lines above Line 25) and on Line 26, column D. As making this allocation below Line 25 suggests, the amounts reported on Line 26 are not additional expenses but are expenses that have already been reported in lines above Line 26.