III. County Medical Society Finances

1. Ensuring Fiscal Responsibility

County medical society finances must be among the chief concerns of CMS officers and executives. County medical society members entrust their leaders with the management and administration of the county medical society dues they pay. They want to see a return on their investments in the form of CMS activity and to know that county medical society funds are spent and managed wisely. Directors and managers may assume personal liability for actions taken on behalf of the county medical society — it is important that you have an understanding of the role you are undertaking regarding county medical society finances.

This section contains basic financial guidelines for county medical societies; it does not cover all the legal or accounting requirements the county medical society may need to meet.

To ensure the county medical society is in compliance with all federal and state regulations, it is advisable to consult a local attorney or accountant who is knowledgeable in such rules and regulations. The offices of the secretary of state, state comptroller, and state treasurer also are valuable sources of information. These Internal Revenue Service (IRS) publications will offer helpful guidance as well:

- **Publication 557** (Tax-Exempt Status for your Organization),
- **Publication 525** (Taxable & Non-taxable Income),
- **Publication 598** (Tax on Unrelated Income of Exempt Organizations), and
- **Publication 1771** (Charitable Contributions — Substantiation and Disclosure Requirements).

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2. Records, Financial Guidelines, and Taxes

County medical society leaders must focus on accurately tracking revenues and expenses. This requires maintaining important CMS records, meeting filing requirements, adhering to bookkeeping procedures, and complying with tax laws.

If there is no county medical society office or other permanent location for CMS files, these records should be transferred smoothly from current officers to new officers when elected. The transfer of records can occur at the annual meeting when elections are held or in special meetings scheduled between incoming and outgoing officers. New officers would

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receive current files from the outgoing officers. All county medical society records, including copies of the charter, bylaws, and articles of incorporation, should be reasonably accessible to all CMS members. It may be advisable to scan important documents into an electronic file to expedite both access to and transfer of these records. You will need to ensure there are multiple copies to protect against loss.

If there are extensive records, the CMS may choose to set up a formal filing system and record retention plan. A set of guidelines for record retention developed by the Electronic Wastebasket Corporation is available on the Internet.

County Medical Society Records

Permanent records and other important records must be stored in a safe place and kept current.

Permanent records include:

- County medical society articles of incorporation and related documents
- Articles of incorporation for any related organizations, such as a foundation
- Articles of association for any county medical society political action committee (PAC)
- Record of Taxpayer Identification Number (TIN) or Employer Identification Number (EIN)
- County medical society bylaws (current)
- TMA Bylaws
- County medical society charter issued by TMA
- Minutes of previous board and member meetings
- All federal and state tax and information returns (including PAC reports)
- All payroll tax returns (if county medical society employs staff)
- All audit reports, if any (including both CPA reports and IRS audits)

Other important records include:

- Financial ledger books/records
- Financial statements
- Property rental/ownership records
- Significant contracts and agreements, including insurance policies

These items should be kept/destroyed according to your retention/deletion policy:

- Pertinent correspondence
- Bank statements, canceled checks, and reconciliations
- Records of paid bills
- County medical society account statements

3. Setting Financial Guidelines

County medical society treasurers and other officers serve two roles in dealing with CMS finances: a fiduciary role and a custodial role.

- The fiduciary responsibility ensures the safekeeping of county medical society assets, making sure funds are invested wisely and spent only on productive activities that support the CMS's exempt purposes.
- The custodial duties require oversight of the CMS's financial transactions. These custodial duties also include maintaining of the county medical society's important records, establishing financial policies and guidelines, and communicating the CMS's financial condition.

Before CMS leaders can develop a budget or an accounting system, they must discuss and adopt a set of financial guidelines and controls that spell out acceptable policies and procedures. Give consideration to at least the following areas.

- **Fiscal Year**. TMA's fiscal year runs from Jan. 1 to Dec. 31. As all financial reports the association provides to county medical societies are based on this period, the CMS may want to adopt the same dates for planning, budgeting, and reporting.
- **Fiscal Policies**. Before adopting policies, you need to answer these questions:
  - Who handles receipts and how?
  - Where is the money deposited?
  - Who approves expenditures and how?
  - What documentation is required for expenditures?
  - Who can sign checks? (Remember to have more than one authorized signer.)
  - Is it clear that county medical society monies must be in a separate county medical society account and not mixed with a member's personal or business account?
  - How often should financial reports be prepared and by whom?
  - Will the county medical society use cash or accrual accounting? (The accrual method is preferred.)
  - Will the county medical society defer dues revenue or recognize it as revenue when received?
  - How often (if at all) should the county medical society be audited?
  - How are members reimbursed for travel (airfare, per diem, etc.)?

Cash Accountability and Check Handling Procedures

The county medical society can create the proper checks and balances on the spending and accounting of CMS funds with simple procedures. The complexity of these financial control procedures depends in part on the

dollar amounts the CMS handles. County medical societies whose annual revenue is $500,000 will need more formal controls than those with annual revenue of $50,000.

One of the simplest things the county medical society can do to monitor expenditures is to require two signatures on checks over a set amount from the CMS account. Although cumbersome, this safeguard will guarantee that payments are reviewed. The amount set will depend on the CMS's budget, but consider $1,000 or $2,500 as possible benchmarks. If the CMS requires two signatures, designate a minimum of three authorized signers with the bank in case of emergency, illness, or death.

In larger county medical societies, and particularly in staffed county medical societies with executive directors responsible for day-to-day office management, double signatures may be unnecessary. Checks can be written by the county medical society staff executive, with a timely review of bank and financial statements by a member of the board or finance committee.

Dealing With Banks

The bank will need current signature authorization cards indicating who can sign checks on the county medical society account. The account authorization process varies from bank to bank but usually requires the formal approval of a bank resolution by the county medical society board on the bank's form. If two signatures are required on any county medical society checks, designate a minimum of three authorized signers (generally, the county medical society president, treasurer, county medical society staff executive, vice president, or other officer). If only one signature is required on county medical society checks, two authorized signers may be sufficient (president, treasurer, county medical society staff executive). The county medical society may want to consider insurance for all officers and employees who have access to county medical society funds.

Keeping track of county medical society receipts and expenditures is necessary. If finances are complex, a formalized accounting system is helpful.

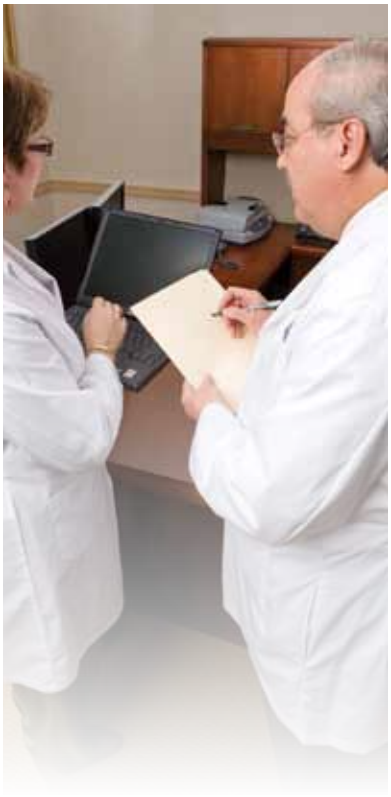
Bookkeeping

Keeping track of county medical society receipts and expenditures is necessary. If finances are complex, a formalized accounting system is helpful. Smaller CMSs may only need to maintain an accurate checkbook. Whatever method you choose, keep these records — and make sure they're transferred appropriately when a new treasurer is elected. Each treasurer must ensure that an effective bookkeeping system is in place.

Some important bookkeeping, reporting documents, and accounting issues follow.

- **Financial Statement**. Accurate, timely, and understandable financial statements are an important tool to safeguard the county medical society's financial stability and integrity. CMS financial statements indicate how much money the county medical society received and spent during the reporting period. The statements should include enough detail to allow accurate review. The complexity of these statements will depend on the accounting system used and on the CMS's decision to defer dues revenue or recognize it upon receipt.

- **County Medical Society Account Statement**. The monthly account statement that county medical societies receive from TMA is not a complete financial statement unless the county medical society's fiscal year coincides with TMA's (currently, Jan. 1 to Dec. 31) and the county medical society has no activity that is not recorded at TMA.



Audits

TMA recommends that large, active county medical societies consider periodic outside audits or reviews. An outside audit firm reports directly to the CMS's board of directors on issues determined or requested by the board.

An audit may include:

- Internal control;
- Financial reports (investments, insurance, compensation, restricted funds, inventories); and
- Tax compliance.

Audits can be expensive. The scope of the audit as directed by the board will affect the amount of time required and the cost. The board should discuss its need for an audit, whether annual or periodic, with its advisors on legal and tax matters. Most small county medical societies will not need an audit if there are adequate control measures in place.

4. Audits/Reviews/Compilations

Audits

- Involve the gathering of evidence to support the fair presentation of financial statements and related disclosures for the purpose of expressing a positive opinion.
- Determine if the statements have been properly prepared within a framework of recognized accounting practices and applicable legislation.
- Fairly present the financial position and results of the organization.

Reviews

- Involve performing inquiries and analytical procedures to support the fairness of financial statements and related disclosures for the purpose of expressing a negative opinion (i.e., nothing came to attention).
- Require a general knowledge of the entity — its business (organization, personnel, basic accounting records, operating characteristics, nature of assets, liabilities, revenues, and expenses) and industry.
- Consist primarily of inquiries of the entity's personnel.

Compilations

- Involve the preparation of financial statements without giving any assurances.
- Are limited to the presentation of financial information that is provided by the entity.

5. Insurance

Depending on the scope of its activities, the county medical society may want to consider purchasing business insurance. Common coverage for county medical societies includes general and professional liability, directors' and officers' liability coverage, as well as property policies — fire and extended liability coverage. Many CMSs also invest in dishonesty coverage (replaced fiduciary bonding from years past) for all officers and employees with access to county medical society funds.

6. Taxes

Probably the best source of advice about county medical society taxes is a qualified accountant knowledgeable in the affairs of tax-exempt organizations. Leaders should have a basic understanding of the various types of not-for-profit organizations and know the status of the organization they are working with. Even though a qualified accountant is the best source, CMS leaders also need to know the basic compliance requirements of tax-exempt organizations.

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Tax-Exempt Status

To apply for recognition of tax-exempt status, the county medical society must send (at a minimum):

- **A completed Form 1024** (to file as a 501[c][6]) or **Form 1023** (to file as a 501[c][3]).
- **Form SS-4:** Application for an Employer Identification Number (EIN). Caution: Use this form only if the county medical society does not already have an EIN.
- **Form 2848:** Power of Attorney form to authorize the representative completing the application to work with the IRS. This form is needed only if the representative is not a county medical society officer.
- A conformed (attested) copy of the organizing document(s). This is usually the articles of incorporation.
- A copy of the most recently adopted county medical society bylaws.

The IRS may request additional information. In addition to any fees paid to an accountant or attorney who prepares the filing, there are filing fees that must be paid to the IRS with the application.

State and Local Reporting Requirements

State and local tax requirements vary from location to location, and what the county medical society and its affiliated organizations owe in federal/state/local taxes depends on the types of organizations involved and the amounts of revenue they generate. The information below outlines the general requirements. Be sure to consult an accountant or attorney who is familiar with local and state requirements.

Individual and Organizational Penalties

If filing and other requirements are not met, the most severe penalty that may be assessed a tax-exempt organization is the revocation of its

tax-exempt status. Care must be taken to ensure all filings are made accurately and timely. It is important to remember that not only is the organization subject to penalties for late filings and/or failure to file returns, but also the **individuals responsible for the filing may be subject to penalties.** Board members typically are considered responsible parties. Be sure to check the county medical society bylaws, job description(s), and county medical society financial policies to determine who is a "responsible" individual.

Federal Reporting Requirements

- **Form 990-N**. Most small tax-exempt organizations with gross receipts that are normally $25,000 or less must file. This form must be filed electronically — no paper — and is referred to as the e-Postcard.

- **Form 990 EZ**. This is a short version of Form 990 that can be filed if:
  - There is less than $100,000 in gross receipts, and
  - There is less than $250,000 in assets at year end.

- **Form 990** (Return for Organization Exempt from Income Tax). Form 990 is an information return required by federal tax code if an exempt organization has "average" (special rules) gross receipts of more than $25,000 per fiscal year. 501(c)(3) organizations also must file a Schedule A to the Form 990. If the county medical society receives a form from the IRS, the county medical society is required to take action. Please contact the TMA Finance Department for assistance. Each county medical society should review the requirements and be sure it is collecting information that will facilitate timely filing of the return. The form is available at www.IRS.gov.

- **Form 990T** (Exempt Organization Business Income Tax Return). Form 990T is a tax return required by federal tax law from exempt organizations that have unrelated business income (UBI). UBI is generated by activities that are not substantially related to accomplishing the purpose for which the exempt status was granted. Examples include mailing label and novelty item sales, and commercial advertising. The first $1,000 of UBI is not taxable. Only net amounts over $1,000 create a tax liability.

- **Form 1120 POL** (U.S. Income Tax Return for Certain Political Organizations). Form 1120 POL must be filed for certain income on political activities and for certain taxable expenditures. See an accountant to determine if the county medical society is required to file this return. It may be required for both your PAC and your county medical society — be sure to check the instructions for this form.

- **Forms 8871 and 8872**. These are new forms required to be filed with the IRS for all political action committees that (generally) have contributions of $25,000 or more. Form 8871 is filed once and is a "notice of status." Form 8872 is an annual return that discloses contributors and expenditures. These forms are open to public inspection. Only organizations that file with the Federal Election Commission are exempt from filing these reports.

Withholding Tax/Reporting Requirements

If the county medical society employs staff, check with an attorney and/or accountant to verify compliance with all payroll requirements.

- **Form W3** (transmittal document for forms W2)
- **Forms W2** (wage and tax statement to IRS and employees)
- **Form 941** (to report Social Security and federal income tax withholdings and liabilities)
- **Form 940** (to report federal unemployment tax)
- **Forms 5500/5500C/5500R** (to report on qualified employee benefit plans)
- **Form 8109** "Federal Tax Deposit Coupon" — Used when paying Social Security and federal income tax withholding to a federal depository. You also must check to see if you meet the requirements for electronic payment of tax deposits. If you meet these requirements, the process can be completed on a touch-tone phone but does require an agreement with your bank. There are specific timing requirements for making these deposits after pay dates, based on the total dollar amounts to be deposited. Make sure the county medical society meets the applicable deposit deadline.

Nonstaff Service Payments

All payments for services in excess of $600 per year to nonemployees (i.e., not salary or wages) are subject to an Information Return filing in the l099 series. The county medical society should require a Form W9 from the provider prior to making any payments. Form 1096 (transmittal document for Forms 1099) and Forms 1099-Misc (both to IRS and recipient) are required (there are some exceptions). The county medical society should identify all payments over $600 (cumulative for year) and ensure required forms are filed timely.

7. Affiliated Organizations

Foundations

The rules and reporting requirements of foundations (which are normally 501[c][3] organizations) are different from requirements for 501(c)(6) organizations. Some differences for 501(c)(3)s include:

- Testing to determine if the organization is a publicly supported charity or a private foundation,
- Different rules for public vs. private charities, and
- A completed Schedule A is required with the Form 990.

Political Action Committees

There are different rules for political action committees and political activities of certain tax-exempt organizations. One such difference is the taxable treatment of interest income on funds used for contributions to candidates for federal offices. Each state establishes its own laws regarding state PACs. See IRS federal rules for political activities and certain tax-exempt organizations. The state also may provide such a chart for

reference. Check with an accountant if the county medical society has an affiliated foundation or PAC.

8. Disclosure Requirements: Documents Required to Be Made Available

Since 1988, as explained in IRS Notice 88-120, all exempt organizations have been required to provide for public inspection at their principal office:

- Copies of **Form 990**, **Form 990N**, or **Form 990 EZ** (information returns) for the three preceding years (Section 501c organizations — except for names and addresses of contributors. Section 527 organizations must disclose contributors);
- A copy of the **Application for Recognition of Exempt Status**;
- Any papers submitted in support of the above returns or application;
- A copy of the **IRS Determination Letter**;
- A copy of **Form 8871**;
- A copy of **Form 8872** for the three preceding years; and
- Filings with the Federal Election Commision are considered public information.

No Disclosure Required

The following tax returns/portions of return are not required to be made available for public inspection:

- **Form 990 T** (although this may change in the near future),
- **Form 990**: Individual contributor name and amounts, and
- **Form 1120 POL**.

Solicitation Disclosures

If soliciting contributions, political organizations and tax-exempt organizations that are not eligible to receive tax-deductible charitable contributions must disclose in conspicuous and easily recognizable formats statements declaring all fund-raising solicitations after Jan. 31, 1988, are nondeductible as charitable contributions. For those items billed through TMA, disclosures are provided on the county medical society's behalf.

Intermediate Sanctions

Included in the 1996 Taxpayer Bill of Rights 2 was the long-awaited concept of intermediate sanctions for exempt organizations. Prior to this legislation, the only remedial action available to the IRS was the revocation of exempt status. This legislation covers only 501(c)(3) nonprivate foundation charitable organizations and 501(c)(4) social welfare organizations.

The primary focus of this legislation is on "excess benefit transactions." Such transactions are defined as any transaction in which an economic

benefit is provided by an applicable tax-exempt organization for the benefit of a "disqualified person" if the economic value exceeds the value of the services performed by the disqualified person. Such transactions may include excessive or unreasonable compensation, unreasonable or unfair rental arrangements, provision of services to individuals, certain assumptions of liability, certain sales of assets, certain participation in partnerships, certain revenue sharing arrangements, and the like. A disqualified person is defined as any person who was, at any time during the five-year period ending on the date of the excess benefit transaction, in a position to exercise substantial influence over the affairs of the organization. The legislation provides substantial penalties for (1) the disqualified person(s), (2) the organization, and (3) organizational managers who participated in a transaction knowing that it was an excess benefit transaction.

Lobby Disclosure

Compliance with the Omnibus Budget Reconciliation Act of 1993 requires that your county medical society members be notified as to the percentage of their dues that are not deductible for federal income tax purposes as a result of the lobbying activities of your CMS. This requirement became effective Jan. 1, 1994.

The county medical society must provide the required written notification upon receipt of the dues payment if the percentage is not reflected on the dues billing. Failure to provide the required notification may incur penalties for the CMS. Please consult your tax advisor for details that relate to your specific county medical society.

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TMA will be happy to assist your county medical society in fulfilling the member notification aspect of this requirement by printing the percentage of nondeductibility on the member renewal notice. This will alleviate the need for you to notify your members after payment has been made. If your county medical society wishes to use this method, please submit the county medical society Lobbying Estimate form to the TMA Membership Operations Department no later than Aug. 15 to be placed on the dues statements for the following calendar year.

9. Equity/Reserve Policies

- Equity reserve: the net amount of income in excess of expense over the life of the organization. For the organization to be viable and have an expectation of continuing, this number must be positive over time.
- Cash reserve: the amount of cash or near cash funds available to the organization in excess of funds required for current operations.

It is important to remember that a large member equity balance is not the same as a large cash balance as these may have been invested in fixed assets or other assets that are not cash. Also, a large cash balance may not be sufficient to meet unexpected needs if all available funds will be required for current operations.

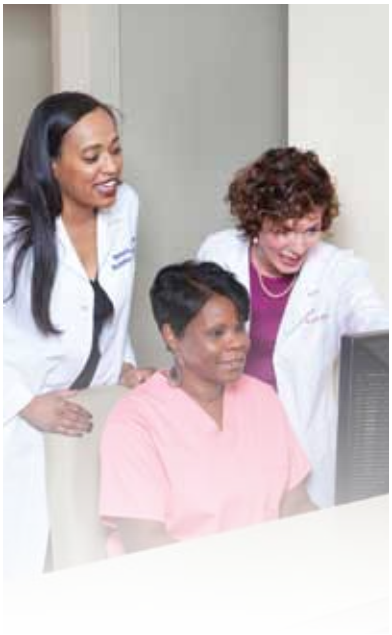
Why should the county medical society have an equity policy?

- **Unexpected Events**. A major shortfall in an activity that is expected to provide a high positive net revenue over expense in a fiscal year can severely impact the organization's ability to meet its current objectives. To the extent feasible, you can insure major events (such as an annual meeting) to replace such losses, and effective management of expenses related to anticipated shortfalls in revenue can help offset or reduce (but not remove) the need to build a reserve for potential shortfall areas. Consider — if the shortfall is experienced in the area of member dues, would the organization have additional time to deal with the related causes and to reduce expense? This additional time may be provided by receiving dues in advance of the period(s) that you incur the expense; however, these funds must be maintained in cash or near cash to be considered such a reserve. Determine what the organization needs to do to maintain a sufficient reserve to fund current operations.
- **Expected Future Events.** A second area to consider is the provision for future events and/or activities. Some of these can be anticipated and planned several years ahead (additional facility, computer upgrades), while some cannot be specifically anticipated but are required in order to serve your membership (new legislation, regulation, or lawsuit that requires immediate and significant expenditure). To the extent that needed cash outlays can be anticipated, an annual targeted provision should build adequate reserves to ensure these funds are available when required. As depreciable assets are placed into service, they become part of future periods' operating expense (as depreciation) and are appropriately considered in the budgeting process. In effect, they are "funded" in the operating cycle that they benefit.
- **Unexpected Future Events.** A more difficult area is in nonspecific future events that may require significant cash outlays. A policy is needed to, at a minimum, provide funds to initiate required immediate actions while allowing a structured look at the potential need for obtaining contributions and/or member assessments in extremely pressing matters. Again this minimum reserve should be available in cash (or near cash).

What should the county medical society consider in an equity/reserve policy?

Establishing policy(ies) regarding the use of accumulated equity and the accumulation of equity should be undertaken in conjunction with a focused look at the status and long-term objectives of the organization. The primary issues to be addressed in such a review are:

1. How to weigh the benefits of serving current member needs vs. building a reserve to serve future and potentially different members' needs,
2. How to maintain an adequate cash reserve to provide for current operations in order to run the business soundly, and
3. How to determine to what extent investment income is desired to contribute to the operating budget each fiscal year.



Generally, the smaller an organization and the more subject the organization is to large swings in activity and/or income, the larger the desired reserve.

Set Policies

Setting policies can be accomplished with various methods including establishing different targets or requirements regarding:

- Equity balance,
- Annual contributions to equity, and
- Negative budget limitations (spending more than you bring in for the year).

Some of the options available include:

- A desired target of providing an equity reserve of XX percent of annual operating expense in members' equity (usually by X date),
- Required minimum annual contribution to equity,
- A requirement that a balanced budget be presented to the finance committee/board,
- Specific processes (restrictions) for large expenditures, and
- Budget modification limitations based on equity reserve requirements.

Keep This in Mind

- Required annual contribution. This should be a guideline that controls not the budget, but the process that requires specific consideration in light of all other objectives and activities during the budgeting process. Don't establish a policy that prohibits the organization from using the reserves they have worked so hard to create.
- Investment income. The investment of reserve funds may contribute (significantly) to your annual operating revenue. Some organizations require that earnings from invested funds be added to the funds being invested rather than allowing these funds to be used in the annual operating budget. This policy might be appropriate if the organization is at or below a minimum equity requirement or should it fall below the required minimum.

10. Budgeting

All county medical society officers have a fiduciary role in developing a budget. The budget should be a planning and control tool that helps measure actual results against projections. It assists in developing affordable CMS activities within the limits of revenues, and helps in understanding how to use revenues to develop programs to meet member needs and achieve county medical society goals.

Budget Type

The county medical society's choice of accounting methods will determine whether the budget is developed according to:

1. A revenue and expense plan (sometimes called “line items” or “natural accounts”),
2. A per-project basis (sometimes called “functional reporting”), or
3. Both.

A county medical society’s budget doesn’t have to be complicated. It only needs to reflect the degree of complexity that is expected to be reported for actual results. Spending money where it will have the greatest effect is one way for the CMS to protect the future of medicine. The budgeting process helps identify these areas of opportunity, and it should always reflect the county medical society’s priorities in accordance with its exempt purposes.

The budget process can be outlined as follows:

- Where are we now?
- Where do we want to be one year from now, and beyond?
- How can we reach our goals … short-term and long-term?

Assess Income

Begin the budgeting process with a realistic assessment of county medical society income at the present dues and nondues revenue levels. For most CMSs, there are two major sources of revenues: dues and educational meetings/nondues revenue. Evaluate the membership base. Is the county medical society membership stable — are there trends that may reduce or increase dues revenue? Some options for increasing revenue include grants and sponsorships from corporations, increasing charges for educational sessions or county medical society services, and selling advertising.

Compare Income With Costs

Do member dues provide a sufficient working base to support these core activities? If the present revenue level cannot support planned projects and activities, explore ways of increasing revenue or reducing planned expenditures. Possibly the county medical society can reduce cost by:

1. Coordinating efforts with other county medical societies or organizations for joint ventures, or
2. Cutting some services or activities.

With a well-thought-out revenue projection (including proposals for increasing revenue) coupled with a projection for the year’s expenses (including proposals for cost reductions), the county medical society can develop an effective, realistic budget.

Summary

Effective financial management is one of the biggest challenges for a county medical society leader. For any questions not covered in this overview, call the TMA Finance Department at (800) 880-7955.