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Accounting for Contributions, Pledges, Grants and Donations to Non-Profits

Navigating the Gray Areas Surrounding FAS 116 and FAS 117

TUESDAY, JULY 2, 2013

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

Today's faculty features:

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Accounting for Contributions, Pledges, Grants and Donations to Non-Profits Seminar

July 2, 2013

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Today's Program

Relevant Standards And Guidance — Slide 8 – Slide 26
[Jeff Stone]

Practical Issues Arising With Contribution And Grant Accounting — Slide 27 – Slide 86
[Rob Leslie, Bob Hambrecht and Jeff Stone]

Update On Relevant FASB Projects — Slide 87 – Slide 92
[Rob Leslie]

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Jeff Stone, Macias Gini & O'Connell

RELEVANT STANDARDS AND GUIDANCE

Acronyms And More Acronyms

- GAAP
- GAAS
- AICPA
- ASB
- SAS
- FASB
- ASC

Recent Activity

- Codified accounting principles

  (GAAP, FASB, ASC)

- Clarified auditing standards

  (GAAS, AICPA, ASB, SAS)

GAAP For
Not-For-Profit Entities

GAAP For Not-for-Profit Entities

The Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) is the single authoritative source of U.S. accounting and reporting standards for non-governmental entities.

GAAP For Not-for-Profit Entities (Cont.)

The FASB ASC represents a MAJOR change in the organization and presentation of GAAP.

GAAP For Not-for-Profit Entities (Cont.)

The FASB ASC also includes relevant portions of authoritative content issued by the U.S. Securities and Exchange Commission.

The FASB ASC is not intended to change GAAP; rather, its aims are to:

- Reduce the amount of time and effort required to solve an accounting research issue
- Mitigate the risk of non-compliance with standards, through improved usability of the literature
- Provide accurate information with real-time updates as new standards are released
- Assist the FASB with the research and convergence efforts required during the standard-setting process

GAAP For Not-for-Profit Entities (Cont.)

General provisions vs. industry-specific provisions

- NFPs should follow the guidance in all effective provisions of the FASB ASC, **UNLESS** the specific provision explicitly exempts NFPs.
- FASB ASC 958, *Not-for-Profit Entities*
- Other guidance

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Generally Accepted Auditing Standards (GAAS)

The AICPA's Auditing Standards Board (ASB):

- Authorized to speak for the AICPA on all matters related to auditing
- Audits of NFPs are conducted in accordance with GAAS.

Generally Accepted Auditing Standards (GAAS), Cont.

The clarity project led to the clarified statement on auditing standards. The aims of the clarity project were to:

- Establish objectives for each SAS
- Include a definitions section, where relevant
- Separate requirements from application
- Use formatting techniques to enhance readability
- Include, where appropriate, special considerations relevant to audits of smaller, less complex entities
- International Standards on Auditing convergence

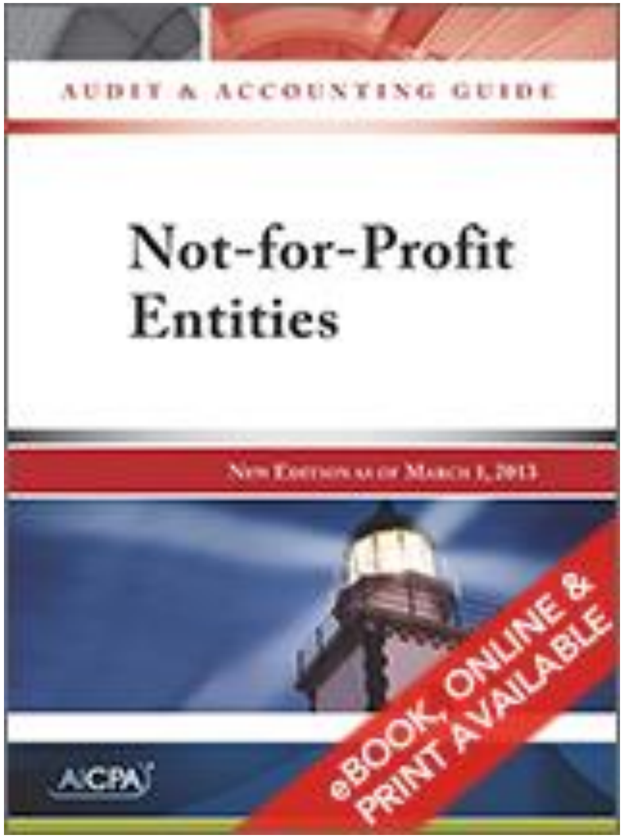
Generally Accepted Auditing Standards (GAAS), Cont.

- Effective date of the clarified SASes – NOW!
- The clarified SASes do not change in content many of the previous requirements.

AICPA Audit & Accounting Guide

(AAG)

Here It Is, Folks!



AICPA Audit & Accounting Guide

The most recent AG has been conformed to the clarified auditing standards (CAS). The CAS are effective for audits of financial statements for periods ending on or after Dec. 15, 2012.

AICPA Audit & Accounting Guide (Cont.)

The AAG's purpose is to:

- Assist management of NFPs in the preparation of financial statements in conformity with U.S GAAP
- Assist practitioners in performing and reporting on their audit engagements

AICPA Audit & Accounting Guide (Cont.)

Reminder!

- Accounting guidance for non-governmental entities included in an AICPA AAG is a source of NON-AUTHORITATIVE accounting guidance.

- The FASB's accounting standards codification is the AUTHORITATIVE source for U.S. accounting and reporting standards for not-for-profits (Sect. 958).

AICPA Audit & Accounting Guide (Cont.)

- Auditing guidance included in an AICPA AAG is recognized as an "interpretive publication."

- Interpretive publications are recommendations on the application of GAAS in specific circumstances, including engagements for entities in specialized industries.

AICPA Audit & Accounting Guide (Cont.)

Although interpretive publications are not auditing standards, AU-C Sect. 200 of the AICPA's *Professional Standards* **requires** the auditor to consider applicable interpretive publications in planning and performing the audit, **because interpretive publications are relevant to the proper application of GAAS in specific circumstances.**

Rob Leslie, Eide Bailly
Bob Hambrecht, Watkins Meegan
Jeff Stone, Macias Gini & O'Connell

PRACTICAL ISSUES ARISING WITH CONTRIBUTION AND GRANT ACCOUNTING

Fair Value Basic Concepts

Fair Value

Why do you need or want to consider the fair value concept in the reporting for non-profits?

1. Contribution concept
    - Types of contributions
        - Cash
        - Non-cash
2. Economic value vs. cash
    - Show the true impact

Fair Value (Cont.)

To determine fair value:

- Market value
- Quoted market prices for similar assets
- The asset's replacement cost
- Independent appraisals of the asset's fair value
- Other valuation techniques, such as discounting the estimated future cash flows and assessing collectability
- May require subsequent measurement

Contributions Vs. Exchange Transactions

Contribution Concepts

(Income recognition)

- Contributions
  - Cash
  - Non-cash
  - Conditional promises to give
  - Donor restrictions
  - Three classes of net assets
  - Donated services
- Other considerations
  - Exchange transactions
  - Agency transactions

Contribution Concepts (Cont.)

Defined as:

An unconditional transfer of cash or other assets to an entity or a settlement, or cancellation of its liabilities in a voluntary non-reciprocal transfer by another entity acting other than as an owner

Contribution Concepts (Cont.)

Examples of contributions:

- Cash donations
- Grants (government or private)
- Professional services
- Materials and supplies
- Promises to give

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Promise To Give, Defined

A **written or oral** agreement to contribute cash or other assets to another entity. A promise carries rights and obligations.

The recipient of a promise to give has a right to expect:

- That the promised assets will be transferred in the future
- The maker has a social and moral obligation
- Generally a legal obligation, to make the promised transfer

A promise to give may be either **conditional or unconditional**.

Promises To Give

- Promises to give can be either:
  - Conditional
  - Unconditional

- Promises to give can be either:
  - Restricted
  - Unrestricted

Exchange Transactions

Defined as:

- Exchange transactions are **reciprocal** transfers in which each party receives and sacrifices something of approximately equal value.
- (Quid-pro-quo , something for something)

Exchange Transactions (Cont.)

***Examples of potential exchange transactions*:**

- Membership dues
- Grants, awards or appropriations
- Program and/or admission fees
- Sponsorships
- Tuition
- Contracts
- Sales of goods (e.g., gift shop, concessions)
- Special events

Exchange Transactions (Cont.)

Recording:

- Recorded as changes in *unrestricted* net assets in the statement of activities
- Typically involve NPO efforts to provide goods or services to members, clients or others for a fee
- Accounted for under general accrual accounting guidelines; therefore:
  - Fees or revenues collected in advance of providing goods or services may create deferred revenues.

Contributions Vs. Exchange Transactions

Why is there a need to distinguish between contributions and other transactions?

- Revenues and expenses may be misstated as to the timing of recognition.
- Revenues and expenses may misstated if improper determination is made regarding an agency transaction.
- Financial statements may be misstated as to donor-imposed restrictions.

Contribution Vs. Exchange Transactions (Cont.)

Classifying asset transfers as exchange transactions or as contributions may require the exercise of judgment concerning whether a reciprocal transaction has occurred; that is, whether a recipient non-profit has given up:

- Assets
- Rights
- Privileges, that are

Of value approximately equal to the value of the assets, rights or privileges received.

Contribution Vs. Exchange Transactions (Cont.)

Distinguishing between exchange transactions and contributions:

- Must consider several factors, including:

  - Resource provider's intent
  - Recipient NPO intent
  - Method of payment
  - Reporting requirements

Contribution Vs. Exchange Transactions (Cont.)

- Special events and fundraisers

  - Can have attributes of both:
    - Contributions
      - Sponsorships
      - Auction items
    - Exchange transactions
      - Advertising
      - Direct donor benefit

Contribution Vs. Exchange Transactions (Cont.)

- Membership dues often have elements of both a contribution and an exchange transaction, because members receive tangible or intangible benefits from their membership in the non-profit.
  - Museums
  - Zoos

- Grants, awards or sponsorships may be entirely a contribution, entirely an exchange transaction, or a combination of the two.
  - Foundation studies

Contribution Vs. Exchange Transactions (Cont.)

Resources received in exchange transactions should be classified as unrestricted revenues and net assets, even in circumstances in which resource providers place limitations on the use of the resources.

For example:

Resources received from governments in exchange transactions (contract) in which those governments have placed limitations (*contractual restrictions*) on the use of the resources should be reported as unrestricted revenues and change in unrestricted net assets, because those limitations (contractual restrictions) are **not donor-imposed restrictions on contributions**.

Agency Transactions

Defined as:

Resources received in transactions in which a non-profit organization is acting as an agent, trustee or intermediary for a resource provider. These amounts should be reported as increases in assets and liabilities, until distributed to recipients.

Agency Transactions (Cont.)

History of current standards

ASC 958-605 (Formally FIN 42 & SFAS 136):

Accounting for transfers of assets in which a not-for-profit organization is granted variance power

Agency Transactions (Cont.)

ASC 958-605 (FIN 42) states that an organization acts as a donee and a donor if a resource provider specifies a third-party beneficiary and explicitly grants the recipient organization the **unilateral** power to redirect the use of the assets away from the specified beneficiary.

Promise Vs. Intent

Promise Vs. Intent

I. Definitions

A. **Promise to give**: A *written or oral* agreement to contribute cash or other assets to another entity. A promise has both rights and obligations:

- The recipient of a promise to give has a right to expect that the promised assets will be transferred in the future.

- The maker of the promise has a social and moral obligation, and generally a legal obligation, to make the promised transfer.

B. **Intent to give**: Intentions to give are merely intentions on the part of the donor. Therefore, they are not recognized by an organization until they become unconditional promises to give; that is, until they meet certain conditions.

Promise Vs. Intent (Cont.)

II. Promises to give

A. A promise to give may be referred to as a "pledge."

B. A promise to give may be either unconditional or conditional.

- An unconditional promise to give is a promise to give that depends either on passage of time or a demand by the promisee (organization) for performance.
- A conditional promise to give is a promise to give that depends on the occurrence of a specified future and uncertain event to bind the promisor (donor).

C. If you are unable to tell if the promise to give is unconditional or conditional, then assume it is conditional.

Promise Vs. Intent (Cont.)

D. A promise to give should be recognized when it is received.

E. A promise should be supported by sufficient verifiable evidence.

F. What is sufficient verifiable evidence?

- From a written perspective, items such as a signed pledge card, or a signed pledge letter or agreement stating the terms of the pledge

- From an oral perspective, verified oral promises to give can be used if you can verify them (for example, by tape recording, written registers or other means that can be supported).

Promise Vs. Intent (Cont.)

G. How to record a promise to give

- Unrestricted
- Temporarily restricted
- Permanently restricted

Promise Vs. Intent (Cont.)

III. Intent to give

A. Intent to give becomes unconditional through either the passage of time or the donee's demand for performance.

B. Example of passage of time: Organization included as beneficiary in will

Conditional And Restricted Contributions

Condition Vs. Restriction

What is the difference between a condition and a restriction?

Consider:

- Is the recipient in control of the outcome?

Are both donor-imposed?

- Yes, they are both donor-imposed.
- Conditions and restrictions are not the same in the classification of net assets categories.

Donor-Imposed Restrictions

- **Only a donor can restrict!**
  - Boards of directors and management can only “designate” unrestricted net assets.”

- Generally, restrictions are stipulated explicitly by the donor in a written or oral communication accompanying the gift.
  - Verifiable
  - Collateral materials

- In addition to explicit donor-imposed restrictions, there are certain contributions that may have **implied** restrictions.
  - Long-lived assets

Types Of Restrictions

Donor-imposed restrictions consist of two basic types:

- Purpose restriction
  - Program
  - Specific expense
- Time restriction
  - Temporary period
  - Permanent period
- *Or both!*

Restriction Policy Consideration

In some cases, donor-imposed restrictions are met in the same period that the contribution is received. An organization may adopt an accounting policy that would report such contributions as unrestricted support.

Or, it may report the contributions as temporally restricted and show a release occurring in the same period.

Conditions

The two questions to consider first:

What is a condition, rather than a restriction on a contribution?

If a condition were present , what type of contribution is most likely to contain one?

Promises To Give: Conditions

Promises to Give

Unconditional Promises to Give

An unconditional promise to give is a promise to give that depends only on passage of time or demand by the promisee for performance.

An unconditional promise to give is recognized as revenue when received.

Conditional Promises to Give

A conditional promise to give is a promise to give that depends on the occurrence of a specified future and uncertain event to bind the promisor.

A conditional promise to give is recognized as revenue when it becomes unconditional.

Conditions: When To Record

Conditional promises to give:

- **Do not record, unless:**
- The likelihood of not meeting the condition is remote (double negative).
    - Management’s reasonable assertion concept

- Other considerations
    - Record at stages – is that permitted?
    - Disclose – when to do that?

Promises To Give: Conditions (Cont.)

Another important consideration with donor-imposed conditions:

Even if the condition were met, for it to be recognized, there must be sufficient evidence in the form of verifiable documentation that a promise was made and received!

Intentions To Give

Is it a *promise to give* or not?

Defined as: Communications from individuals indicating that a non-profit has been included in an individual's will as a beneficiary are intentions to give. Such communications are not **unconditional** promises to give, given the fact individuals retain the ability to modify their wills during their lifetimes.

Another common intention to give can be found in certain expected future "church offerings" forms that clearly state it is not a promise.

Intentions To Give (Cont.)

Another consideration for both conditions and intentions:

There may be cases of vague donor stipulations, that a *promise* containing stipulations that are not clearly unconditional or deliberate will be presumed to be a conditional promise or just an intention to give.

Contribution Recording In The Right Year And Right Amount

Contribution Recording In The Right Year

- Contributions should be recognized as revenues or gains in the period received.
  - Contributions that are part of an organization’s ongoing central activities are reported as revenues.
  - Contributions that are peripheral or incidental to the organization’s activities are reported as gains.
  - Restrictions on the contributions do not affect the valuation or period in which the contributions should be recognized.
  - Unconditional promises to give should be recognized when received, so long as there is sufficient evidence to support the promise made and received.

Contribution Recording In The Right Amount

- Contributions should be recorded at fair value of the assets (cash or non-cash) received or services received (non-cash) or liabilities satisfied.
- **Valuing an unconditional promise to give (cash)**
  - Those that are due to be collected within one year are generally measured at fair value, but may also be recorded at their net realizable value, which is the best estimate of fair value.
  - Unconditional promises to give that are due beyond one year should be valued using a present value technique.
    - For cash transactions, the NPO needs to determine the amount and timing of future cash flows.
    - For non-cash transactions, the NPO needs to determine the quantity and nature of assets expected to be received.

Contribution Recording In The Right Amount (Cont.)

- Factors to consider when using present value:
  - When the promise is expected to be collected
  - Donor’s creditworthiness
  - Past collection experience
  - NPO’s policy on enforcing promises to give
  - Any uncertainty in the amount and timing of cash flows

Contribution Recording In The Right Amount (Cont.)

- Determine the discount rate to be used
- Discount rate should approximate the rate that an independent borrower and lender would have negotiated in a similar transaction.
- The discount amortization should be recorded as contribution revenue.

Contribution Recording In The Right Amount (Cont.)

- **Valuing an unconditional promise to give (non-cash)**
  - Promises collected within one year are generally measured at fair value, but may also be recorded at their net realizable value, which is the best estimate of fair value.
  - Unconditional promises to give that are due beyond one year should be valued using a present value technique.
    - » For non-cash transactions, the NPO needs to determine the quantity and nature of assets expected to be received.

Contribution Recording In The Right Amount (Cont.)

- NPO must also consider factors related to the timing and uncertainty of the items' future delivery; that is, what discount rate to be used and the collectability of the promise.

- If projected FV is difficult to determine on underlying non-cash assets, then FV of promise to give may be based on FV of assets when the promise is made. In that case, no discount rate should be applied. You would still need to determine the collectability of the promise.

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Non-Cash Contributions

Non-Cash Contributions: Services

- If services contributed to a non-profit organization (NPO) create or enhance a non-financial asset (such as property and equipment) **or** meet the following three criteria, they should be recognized as contributions:

  1) The service requires specialized skills.

  2) The service is provided by individuals who possess those skills.

  3) The service would typically need to be purchased if not contributed.

Non-Cash Contributions: Services (Cont.)

- Contributions of services should be measured at fair value (FV).
  - Record at FV regardless of whether your organization could afford to purchase the services
  - If the contributed services create or enhance a non-financial asset, you can estimate the FV by either using the FV of services received or the FV of the resulting asset or asset enhancement, whichever is easier to determine. Non-financial assets include land, buildings, use of facilities or utilities, materials and supplies, intangible assets and services.

Non-Cash Contributions: Services (Cont.)

- The update is effective for fiscal years beginning after **June 15, 2014**. NPOs won't have to restate past results using the new accounting, but will have the option to adjust all prior periods presented at the date of adoption.

- Early adoption is permitted.

Non-Cash Contributions: Materials

- Examples: Gifts-in-kind including inventory (food, clothing, medical, supplies, etc.); long-lived assets; and items used for fundraising purposes
- Record materials as either contributions or assets, depending on nature of gift(s)
- When to record contributed materials?
  - If contributed materials can be used or sold by an NPO, then they should be recorded at FV. (i.e., donated medical supplies).

Non-Cash Contributions: Materials (Cont.)

- When to record contributed materials (continued)?
  - If contributed materials cannot be used internally or sold or have little or no value, then they should not be recognized as contributions or assets. (i.e., trinkets with little or no value).
  - FV of gift received should be the value at which it was received, unless NPO adds value to the gift (example: cleaning or packaging the gift).

Non-Cash Contributions: Materials (Cont.)

- Determining fair value:
  - Use of measurements from published catalogs, vendors, independent appraisals, other sources
  - Can be difficult; GAAP allows the use of estimates, averages or other computational averages (i.e., average per pound, subsequent sales)
  - These methods can be used if they are used consistently and deemed to be reasonable as compared with FV.

Non-Cash Contributions: Materials (Cont.)

- Record contribution of long-lived assets
  - Record value of assets donated plus costs incurred to place asset in service (i.e., freight, installation)
  - Normally recorded as temporarily restricted support when received, especially if donor states the asset's period of use. Net assets are reclassified from temporarily restricted to unrestricted ratably over the period of use.
  - If no period of time is noted by the donor, then an NPO may make that determination by adopting an accounting policy and placing a time restriction on the asset. As the time restriction expires, net assets are reclassified from temporarily restricted to unrestricted.
  - If no period of time is noted, then a contribution would be unrestricted.

Non-Cash Contributions: Materials (Cont.)

- Record contribution of items used for fundraising purposes
  - Examples: Tickets, gift certificates, merchandise from donors to be sold at a fundraising event
  - Record items at their FV. When an item is ultimately sold, adjust contribution income by the amount for which it was sold (either increase or decrease contribution revenue).

Financial Statement Disclosures

Financial Statement Disclosures

- Majority of the disclosure requirements for contributions found in the “Disclosures” section of FASB ASC 958, including:
  - Information about the accounting policies adopted by the NFP
  - Information about contributions received and receivable
  - Information about contributions of services
  - Information about fair value of contributed services, if determinable

Rob Leslie, Eide Bailly

UPDATE ON RELEVANT FASB PROJECTS

FASB: Discussion Points

- ASU No. 2012-05, Statement of Cash Flows
  - Donated investments, when to record a record as operating, investing financing
    - Diversity of practice
    - Timing of conversion to “cash”
- ASU No. 2013-06, Services received from an affiliate organization
    - Value of services received
- Going concern reporting model
- Leases

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NAC Of The FASB Update

NAC: Discussion Points

- In 2009, the FASB established the FASB Not-for-Profit Advisory Committee (NAC).
- The NAC was created to be a resource for the FASB in obtaining input from the NFP sector on existing guidance, current and proposed technical agenda projects, and longer-term issues affecting NFPs.
- In 2011, the NAC began a standard-setting project to reexamine the existing standards for financial statement presentation by NFPs.
- In 2012, the NAC provided recommendations from the financial statement presentation project to the FASB for further consideration.

NAC: Discussion Points (Cont.)

- Projects
  - Financial statement presentation
    - Net assets reporting model
    - Measure of operations reporting
  - Communications other than financial statements
    - MD&A
    - “Tell the story”