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NONPROFIT SYMPOSIUM 2019

The Next 5 Years: The Evolution of Nonprofit Finance

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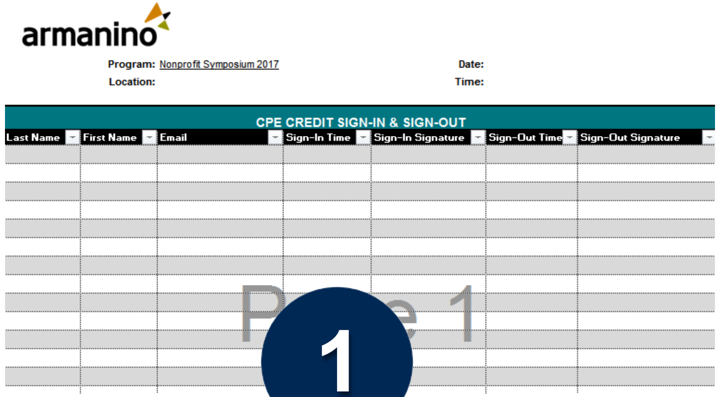
STEPS TO RECEIVE CPE CREDIT

To receive **3 Accounting & Auditing (Governmental) CPE Credits** you must:



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Program: Nonprofit Symposium 2017 Date:

Location: Time:

CPE CREDIT SIGN-IN & SIGN-OUT

Last Name	First Name	Email	Sign-In Time	Sign-In Signature	Sign-Out Time	Sign-Out Signature

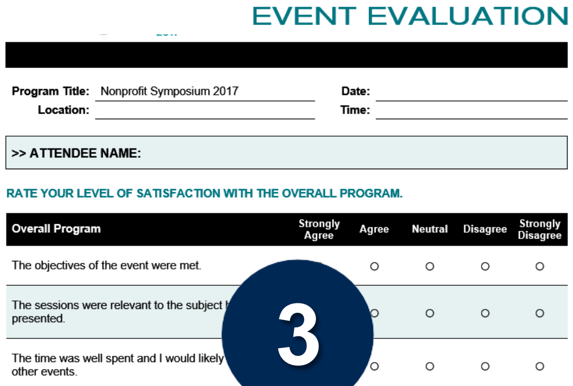
Page 1

1

Sign In & Sign Out
@ Registration Table

2

Stay for the
Entire Event
(It's Worth It!)



EVENT EVALUATION

Program Title: Nonprofit Symposium 2017 Date:

Location: Time:

>> ATTENDEE NAME:

RATE YOUR LEVEL OF SATISFACTION WITH THE OVERALL PROGRAM.

Overall Program	Strongly Agree	Agree	Neutral	Disagree	Strongly Disagree
The objectives of the event were met.		○	○	○	○
The sessions were relevant to the subject presented.		○	○	○	○
The time was well spent and I would likely other events.		○	○	○	○

3

Submit Event Evaluation
@ Registration Table

CPE Learning Objectives

- Evaluate the future for nonprofit organizations, and how finance teams can prepare and persevere going forward
- Determine how CFOs can implement changes to their organization to remain compliant with FASB updates impacting revenue recognition, grants and contributions
- Discuss how nonprofit finance leaders implemented useful technology to sustain their organization
- Review the impact of the Tax Cuts and Jobs Act (TCJA) one year after implementation

Agenda

9:00 – 9:30 AM	*Registration*
9:30 – 9:40 AM	Welcome: Thomas Schulte
9:40 – 10:30 AM	TAX CUTS AND JOBS ACT: ONE YEAR LATER
10:30 – 11:20 AM	NONPROFIT BUSINESS TRANSFORMATION
11:20 – 11:30 PM	*BREAK: Snacks!*
11:30 – 12:20 PM	FASB CLARITY: REV REC, GRANTS, & CONTRIBUTIONS
12:20 – 12:30 PM	*Closing Remarks*
12:30 – 1:30 PM	*Lunch*

Social Media

- Follow **@Armanino** on Twitter
- Engage in the conversation throughout the day

#NPSymposium19

WELCOME

Thomas Schulte
Partner & Southern CA Market Lead

Armanino Overview

PURPOSE

To be **the most innovative** and **entrepreneurial** firm that makes a **positive impact** on the lives of our **clients** and **people**.

SNAPSHOT

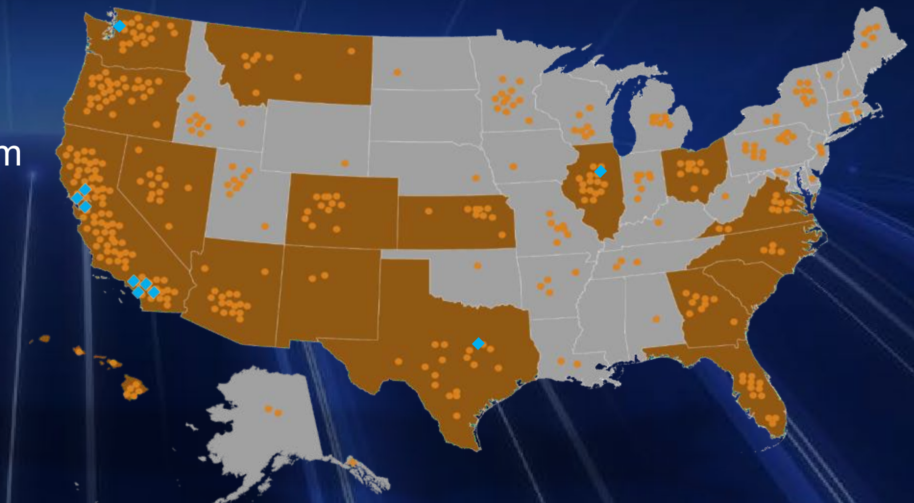
- 1000+ Employees
- Team Members in 22 States
- 22nd Largest CPA & Consulting Firm
- Largest Niche: Technology

Affiliate Companies

AMF MEDIA GROUP

INTERSECT

LOCATIONS



- Office
- Employee (by State)
- Client (by location in State)

CALIFORNIA
- San Ramon
- San Jose
- San Francisco
- Los Angeles (West LA)
- Los Angeles (Downtown LA)
- El Segundo
- Woodland Hills

WASHINGTON
- Seattle

ILLINOIS
- Naperville

TEXAS
- Dallas

RECOGNITION & AWARDS

INSIDE PUBLIC ACCOUNTING TOP 100 FIRMS 2018

INSIDE PUBLIC ACCOUNTING FASTEST-GROWING FIRMS 2018

INSIDE PUBLIC ACCOUNTING BEST OF THE BEST FIRMS 2018

BEST of Accounting CLIENT SATISFACTION 2019

BPtW 2015 BEST PLACES TO WORK

THE FIRM OF THE Future

vault TOP RANKED

2017 100 accountingTODAY TOP 100 FIRMS

VAR 100

2018 VAR Stars

Nonprofit Capabilities

REPORTING

Real-time data and strong analysis drive board decisions and management strategy, and good financial reporting practices affect how you raise funds, invest contributions, compensate your staff and conduct your day-to-day operations.

COMPLIANCE

Meeting the requirements of the IRS, boards, donors and government entities is crucial to receiving funding & support.

TECHNOLOGY

The right systems, properly deployed, can drive important efficiencies in both finance and operations, helping your nonprofit report on what matters most, while increasing time focused on strategic planning.

HUMAN CAPITAL

Finding the right people, educating them properly and giving them the tools needed to do their jobs efficiently is the cornerstone of any nonprofit organization.

- Private Education
- Foundations
- Social & Human Services
- Performing & Fine Arts
- Animal & Environment
- Religious Organizations

armanino foundation

The Armanino Foundation empowers our employees to give back to the community via:

- THE GREAT GIVE
- DOLLARS FOR DOERS
- VOLUNTEER VACATIONS
- GRANTS

Mission
To assist charitable organizations that create a positive impact on the lives of people in our communities.

armaninofoundation.org

TAX CUTS AND JOBS ACT: ONE YEAR LATER

PRESENTER

Katy Brown

Director, Armanino Advisory LLC

- West Coast Nonprofit Tax Practice Lead
- Leads team of 10 dedicated nonprofit tax specialists
- BA from George Mason University (French) / MA from University of Arizona (French literature) / Master of Science in Taxation (MST) from Golden Gate University
- Member of AICPA, CalCPA, & Center for Nonprofit Volunteerism
- Board member of The Clifford Brown Jazz Foundation
- Grants Committee member of the Armanino Foundation

- West Coast Nonprofit Tax Practice Lead
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- Member of AICPA, CalCPA, & Center for Nonprofit Volunteerism
- Board member of The Clifford Brown Jazz Foundation
- Grants Committee member of the Armanino Foundation

PRESENTER

Andrew Watson

Senior Manager, Armanino Advisory LLC

- 17 years' experience including preparation and review of all entity types with heavy emphasis in partnership, exempt organization and real estate
- Bachelor's degree from UC Santa Barbara in Economics

Agenda

- TCJA – what changed for nonprofits?
  - Excess compensation
  - Excess parachute payments
  - No more advance refunding of tax-exempt bonds
  - Section 529 plan funds may be used for K-12 tuition expenses
  - Siloing of UBTI activities (Section 512(a)(6))
  - Changes to NOL rules
  - **Parking & Commute benefits tax** (Section 512(a)(7))
- Ongoing impacts to nonprofits
- Year-to-date tax news for nonprofits

Excess Compensation

- IRC Section 4960 – excise tax imposed on nonprofit employer
- Effective for tax years <u>beginning</u> after December 31, 2017
- Compensation in excess of $1m paid to a "covered employee"
  - Wages, less Roth contributions, plus 457(f) amounts vested
  - Five highest compensated employees in any year after 2016
- Nonprofit corporations = 21% tax rate
- Exception for medical & veterinary doctors

Excess Parachute Payments

- IRC Section 4960 – excise tax imposed on nonprofit employer
- Effective for tax years beginning after December 31, 2017
- Severance payments that exceed 3x the employee's average comp over the previous five years (the base amount)
- The entire amount in excess of the base amount is taxable
- Nonprofit corporations = 21% tax rate

Tax-Exempt Bond Advance Refunding

- Changes to IRC Section 149(d) eliminate tax-exempt treatment of advance refunding bonds
  - Refunding = refinancing
  - Advance refunding vs. Current refunding
  - Eliminates an org's ability to receive refinancing funds in advance of paying off the original debt
  - In line with current strict enforcement of use of tax-exempt bond proceeds & facilities financed with tax-exempt bonds

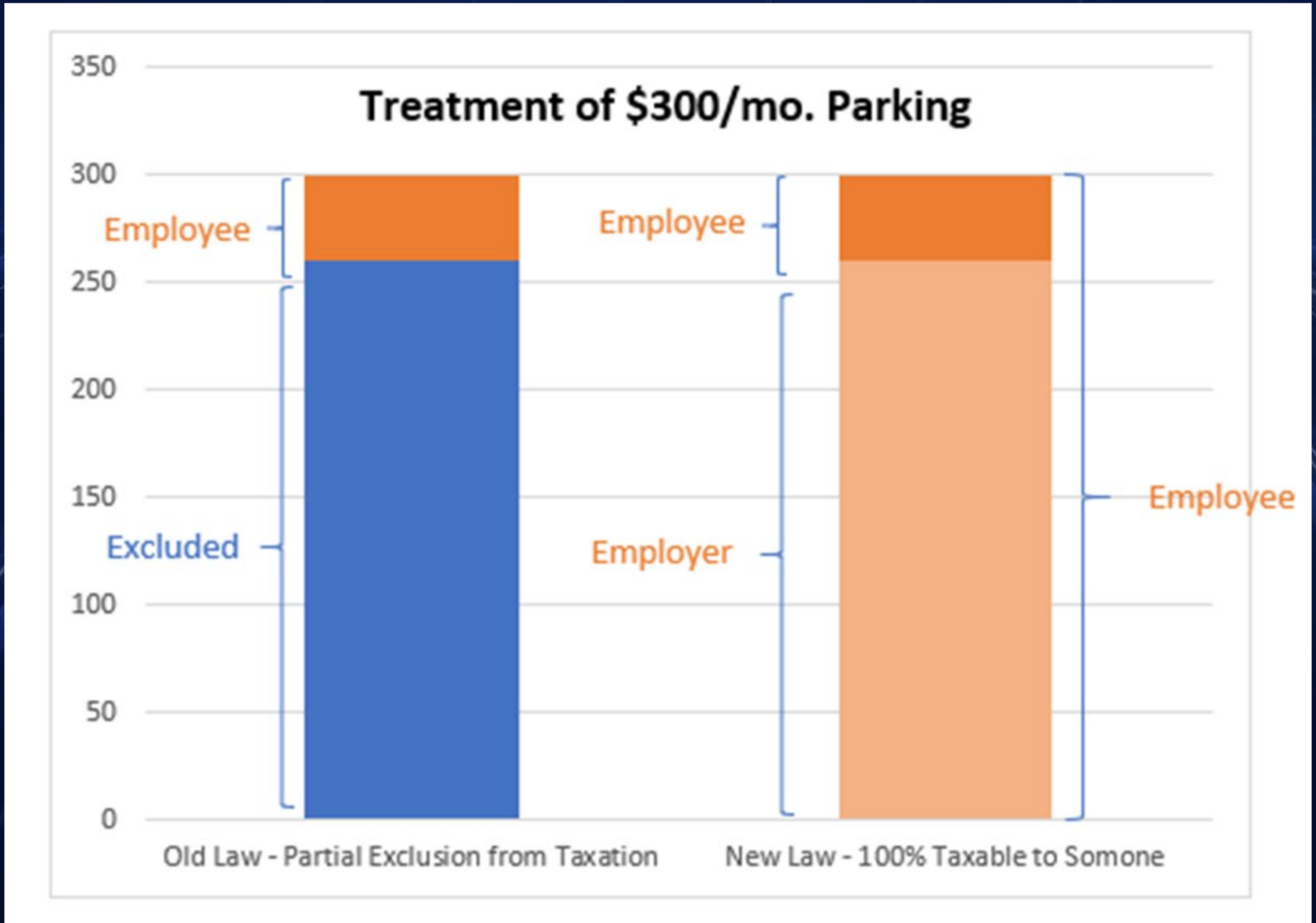
Section 529 Plan Usage for K-12 Tuition

- IRC Section 529(c)(7) amended
  - Special tax-advantaged savings programs
  - Some states allow pre-tax contributions or other tax incentives (not CA)
  - Originally only usable for qualified higher education expenses
  - Amended code allows up to $10,000 per student per year to be withdrawn for K-12 tuition expenses
  - State conformity issues (CA did not conform)

Tax on Employee Parking & Commute Expenses

- Exempt orgs must add to their UBTI the amounts spent on qualified transportation fringe (QTF) benefits and qualified parking
- IRC Section 512(a)(7) (with reference to Section 274)
- QTF is excludable from employee income up to $260/mo (2018) - $265/mo for 2019
  - Any amount in excess must be included in employee wages
  - Any amount the employee doesn't pay tax on, the employer must pay tax on
- Qualified parking is also excludable from employee income up to the same limits
  - We originally thought owned parking lots would not be subject to this, because it is not generally considered an employee benefit
  - Notice 2018-99 indicates that maintenance costs for owned parking lots are also subject to the tax
- Qualified bicycle commute reimbursements ($20/mo) are now taxable

Employee Can Still Be Exempt from $260 per month, but Employer Must Now Pay



Notice 2018-99 Parking Tax Calculation

Depends on the parking lot arrangement

- Scope – any parking provided to employees at work
  - Employer-owned parking lots
  - Parking included in lease & not separately stated
  - Leased parking lots and spaces
  - Beginning Jan 1, 2018 for all tax years
- General principles –
  - Focus on normal business hours (not 24 hours per day)
  - Spots that are typically empty = non-employee
  - May remove signage or barriers by Mar 31, 2019 it will be retroactive back to 1/1/18 when the change became effective

IRS' Suggested Four-Step Process (Notice 2018-99)

- Step 1 – Calculate the disallowance for reserved employee parking (taxable)
- Step 2 – Calculate the primary use of remaining area: employee or non-employee
  - 50%+ actually used by non-employees, entire area is non-taxable
  - 50%+ actually used by employees, allocate between emp/non-emp use
    - Number of spots, number of employees, hours of use, etc.
  - If usage varies, estimate using any "reasonable" method - documentation
- Step 3 – Calculate the exclusion for reserved non-employee parking
- Step 4 – Determine remaining use & allocable expenses

Office Leases Treat Parking in A Lot of Different Ways

- Spaces paid directly to a third-party parking company
- Spaces with a per month rate
- Spaces included in leases but without a specific charge
- Common area maintenance (CAM) costs that include the cost of parking

What Documentation is Required?

- Any reasonable method is allowable
  - Guidance from IRS Notice 2018-99 will be considered reasonable
  - Not the only “reasonable” method
  - Document how the costs were allocated
  - Areas / items that are adjacent to parking lots may be allocated away
  - Maintain records for the length of the statute of limitations
    - Federal: 3 years from date of filing or original due date, whichever is earlier

What Costs Are Taxable?

Once the total % of employee use is determined, apply it to the total of these costs:

- Utilities
- Insurance / interest
- Maintenance / repair
- Leaf, trash, snow removal
- Parking lot attendants / valet
- Security
- Property taxes
- Rent or lease payments for the parking spaces or parking lot
- **NOT DEPRECIATION**

Are Expenses Allowed Against This Addition to UBTI?

Form 990-T does not allow for expenses against 512(a)(7) taxable expenditures

- Difference between for-profit and nonprofit entities
- Suggest providing comment to the IRS on this issue
- Suggest calling / writing your Congresspeople – there is some effort in Congress to repeal

Reporting Details

- Tax rates:
  - Blended rate for orgs with fiscal years beginning in 2017
  - Flat 21% rate for 2018 and later tax years for corporations
  - Trusts are still taxed at graduated rates
- Automatic relief from underpayment penalties for first-time filers (Notice 2018-100)
- What if a client chooses not to file? Impact on audit?

Reporting and Payment

Report on Form 990-T

- New schedules to allow for siloing rules
- Fringe benefits appears at the end
- $1,000 specific deduction

Payment requirements

- Once you must make a payment of $500+, EFTPS is required
- www.eftps.gov
- 10 business days from online sign-up to ability to schedule online payments (48 hours to schedule phone payments)
- Quarterly estimate payments required if total amount due is $1,000+

Article in Last Thursday's Nonprofit Times


THE NONPROFIT TIMES
The Leading Business Publication For Nonprofit Management

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NPT > News & Articles > Legislation To Repeal Nonprofit Tax Getting Bipartisan Support

TAX CUTS & JOBS ACT

Legislation To Repeal Nonprofit Tax Getting Bipartisan Support

MARCH 7, 2019 PAUL CLOLERY

"James Lankford (R-Okla.) and Chris Coons (D-Del.) introduced the legislation in the U.S. Senate. Mark Walker (R-N.C.) and Tom Suozzi (D-N.Y.) introduced the companion bill in the House of Representatives. U.S. Representatives Randy Weber (R-Texas), Doug Lamborn (R-Colo.), Jeff Duncan (R-S.C.), Matt Gaetz (R-Fla.), and Jody Hice (R-Ga.) are also co-sponsors on the House of Representatives version."

FAQs

- We already filed our 2017 990-T back in November prior to the IRS guidance. Do we have to amend?
- Are volunteers “employees” for the purpose of the parking tax?
- If our signage says “for our company’s use only,” does that indicate employee or customer use?
- Do we have to make quarterly estimated payments?
- How do we pay this tax? Can we pay online?
- What other deductions can we find against our UBTI?
  - Consider charitable contributions – 10% limitation
  - Review expense allocations each year

Siloing of UBTI Revenue Streams

Income/loss from different UBTI activities may not offset each other, including for NOL purposes

- Section 512(a)(6)
- Effective for tax years 2018 and later (beginning after Dec 31, 2017)
- Notice 2018-67
  - Suggests using NAICS codes or maybe the first three digits
  - States that we may group all partnership passthrough UBTI into one activity (passive investment activities may be treated as one trade or business)
    - De minimus = 2% or less ownership
    - Lack of control = 20% or less ownership, no actual control

Other Common Sources of UBTI

- Advertising of any kind
- Passthrough UBTI on investment partnership K-1s
- Rental of debt-financed property (exception for schools)
- Private business use of tax-exempt bond financed property
- Rental of facilities that includes significant services
- Rental of property other than real estate (personal property)

Changes to NOL Rules

- Section 172(a) limits Net Operating Loss carryovers to 80% of taxable income
  - NOLs generated in one UBTI activity will only be applicable to that activity
  - Also subject to the 80% limitation
- Section 172(b) eliminates the two-year carryback provision
  - All NOLs will carry forward 20 years
- Effective for tax years beginning after Dec 31, 2017

Orgs will be paying tax on UBTI activities with net income in future years, even if they have net operating losses

Net Operating Loss Rules

- NOL ordering rules –
  - Use 2018 & later specific NOLs first, subject to 80% limitation
  - Then use 2017 all-purpose NOLs
- 2017 and prior NOLs may be used against any activity, including Section 512(a)(7) parking and commute costs
  - No 80% limitation on 2017 and prior NOLs

Ongoing Impacts to Nonprofits

- TCJA creates new filing and recordkeeping requirements
- State conformity issues
- Other Breaking Tax News for nonprofits

Breaking Tax News for Nonprofits

- Wayfair's impact on nonprofit organizations
  - Sales of tangible items across to out-of-state purchasers
- Rev Proc 2019-17 (effective 5/28/19)
  - Nonprofit school nondiscrimination policy publication requirements
- Commentariat updates
  - Charitable giving YTD
    - Challenging environment for donation-dependent organizations
  - Donor Advised Funds
    - Some loosened restrictions
    - Incentivized for large donors so they can control the timing of their giving and deductions

QUESTIONS?

RAISE YOUR HAND!

NONPROFIT BUSINESS TRANSFORMATION

Nonprofit Business Transformation

Dean Quiambao
Partner
Armanino Advisory LLC

Ryan Prindiville
Partner
Armanino Advisory LLC

Alice Galstian
CFO and VP of Finance and Administration
Kavli Foundation

Background

- The Kavli Foundation (“TKF”) is a private foundation founded in 2000 by Fred Kavli and is dedicated to advancing science for the benefit of humanity, promoting public understanding of scientific research, and supporting scientists and their work.
- Mission
  - The Kavli Foundation is dedicated to advancing science for the benefit of humanity, promoting public understanding of scientific research, and supporting scientists and their work.

The NEED

- TKF evaluated options to strengthen the organization, and improve use of current technology and streamline processes:
  - Evaluated current technologies and processes leveraged
  - Assessed the organization’s current state
  - Built a roadmap of recommendations for potential future state

Measurable Outcomes

- People
  - Enable people and growth plan
  - Improve employee job satisfaction
  - Increase clarity of roles and ownership
- Technology
  - Increase access and visibility to reliable data
  - Increase automation through integration
  - Focus on enablement vs. increase of staff workload
  - Encourage user adoption of new systems
- Processes
  - Reduce operational uncertainty
  - Focus on manual task reduction
  - Increase time spent on high value tasks
  - Alignment with organizational objectives

Nonprofit Business Transformation

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QUESTIONS?

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BREAK

Please Return by 11:30AM

FASB CLARITY: REV REC, GRANTS & CONTRIBUTIONS

Renee Ordeneaux,

Partner, Armanino Advisory LLC

- More than 25 years of experience in public accounting
- Expertise extends to income tax matters pertaining to unrelated business income and non-recurring business transactions
- Board treasurer for the Theodore Payne Foundation and past chair of Upward Bound House
- Member of AICPA and CalCPA
- BA, University of Texas and MBA, UCLA

Agenda

- Background
- Nonprofit Accounting Overview
- Effective Date and Transition
- Systems Update

Background

- ASU 2018-08 issued in June of 2018
  - Clarify the scope and accounting guidance for contributions received and contributions made.
  - Many stakeholders have noted difficulty in characterizing grants and similar contracts with resource providers as either exchange transactions or contributions, and further whether a contribution is a conditional or restricted contribution under current GAAP.
  - Diversity in practice
- For nonprofits that rely on government grants, accounting for the grant money has historically been a matter of interpretation since the FASB has not provided definitive guidance on the matter.
- Additionally, the issuance of the revenue recognition guidance for contracts with customers under Topic 606 raised questions as to whether grants and contracts are within scope of that guidance as being either reciprocal or nonreciprocal.

Background, continued

- Standard provides nonprofits with a robust framework for evaluating and determining if a transaction should be accounted for as a contribution or an exchange transaction
- Standard provides guidelines for distinguishing between conditional and restricted contributions.
- Amendments in the standard apply to all entities, including those that receive or make contributions of cash or other assets including promises to give.
- Amendments do not apply to government entities involved in transfers of assets to business entities.

What are the Challenges in Recognizing Revenue in Nonprofits?

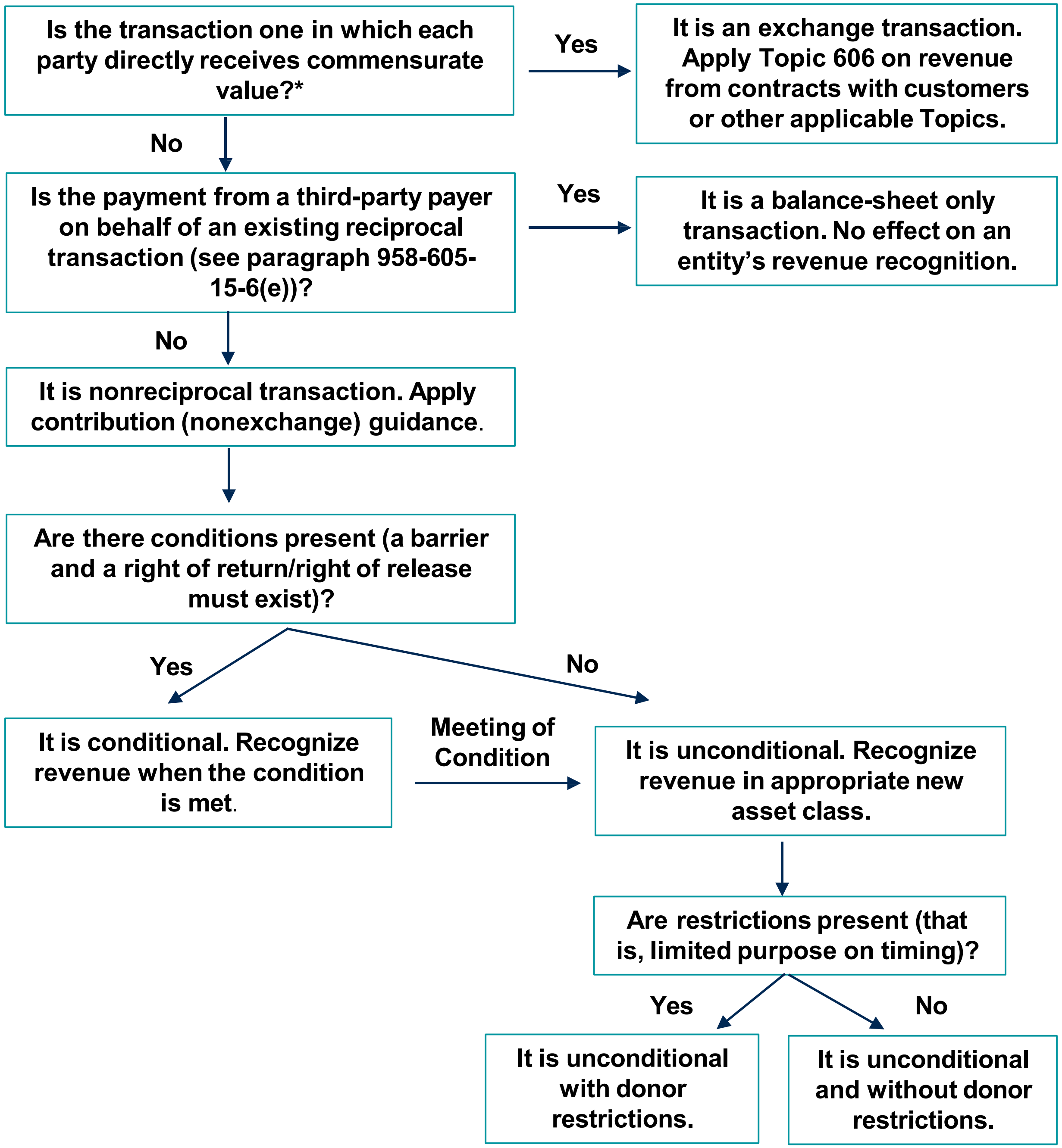
- Did the organization earn the revenue?
- When should the revenue be recognized?
- Are there conditions attached? Restrictions?
- Is it actually revenue to your organization at all?

How are Different Types of Revenues Recognized?

Type of Transaction	Typical Revenue Recognition
Exchange transaction	When goods or services are provided
Conditional contribution	When condition is fulfilled
Restricted contribution	Restricted revenue recognized when granted; release from restriction upon satisfaction of restriction
Unrestricted contribution	When received

A Revised Order of the Thought Process for Revenue Recognition

1. Was the revenue ***earned*** in a process in which value is ***exchanged?***
2. Are there ***conditions*** on a contribution?
3. Are there ***donor restrictions?***



EXCHANGE TRANSACTION VS. CONTRIBUTION

Exchange vs. Contribution

- A nonprofit must identify whether the resource provider (such as a government agency, private foundation, individual donor or other nonprofit) receives something of commensurate value in return for the resources transferred
  - Commensurate value means something of equal measure or amount is given or received.
- FASB clarifications on commensurate value
  - A benefit received by the general public as a result of a transfer of assets from a government agency is not equivalent to commensurate value received by the resource provider.
  - Execution of a resource provider’s mission or the positive sentiment from acting as a donor does not constitute commensurate value received by a resource provider.
  - A government agency that bestows a grant often receives an indirect benefit in the form of services provided to the constituents of that government. Under the proposed new rules, such indirect benefit does not constitute commensurate value.

Exchange vs. Contribution, continued

- Evaluation criteria for determining whether a resource provider is receiving commensurate value:
  - The resource provider's mission and purpose for the transfer
  - The express intent of the institution and the resource provider
  - Which party has discretion in determining the amount of the grant
  - The penalties to the recipient for nonperformance
  - Whether the recipient has discretion over how the funds are used

Exchange vs. Contribution, continued

- Example 1 – Government Funding
  - **Case Study -** The local government provided funding to NFP B to perform a research study on the benefits of a longer school year. The agreement requires NFP B to plan the study, perform the research, and summarize and submit the research to the local government. The local government retains all rights to the study.
  - **Answer -** This example should be considered an exchange transaction. NFP B concludes that this is a procurement arrangement in which commensurate value is being exchanged between two parties and that it should follow the relevant guidance for exchange transactions. NFP B is to perform a research study for the local government and turn over a summary of the study's findings to the local government. The local government retains the rights to the study.

Exchange vs. Contribution, continued

- Example 2 – Government Funding
  - **Case Study** – Los Angeles provides a $500,000 grant to Homeless Services, Inc. to provide mental health services to homeless individuals on Skid Row.
  - **Answer** - This is a contribution. Although the beneficiaries of the services are residents of Los Angeles, the new standard clarifies that “a benefit received by the public as a result of the assets transferred is not equivalent to commensurate value received by the resource provider.”

Exchange vs. Contribution, continued

- Most government grants would be accounted for as contributions under the new guidance (and as we will explain further in this webinar, most will be conditional contributions).
- There will be some exceptions.
  - **Example** - a research grant might be classified as an exchange transaction if the funding agency retains all rights to the research results. Like other exchange transactions, this type of grant would be accounted for under the new revenue recognition standard (FASB Codification topic section 606, *Revenue from Contracts with Customers*).

Exchange <u>and</u> Contribution: Special Events

Example #3 – Museum gala with ticket price of $500

- Cost of dinner and entertainment is $100
- Fair value of dinner and entertainment is $175
- Purchasers of dinner ticket also receives guaranteed entry to special museum exhibit – admission to museum is free, but the museum has donated event entry to other nonprofits with a suggested price of $50

How much of this is a contribution?

How would you allocate the price of the exchange transaction portions?

How does the museum present this on its financial statements?

CONDITIONAL VS. UNCONDITIONAL CONTRBUTIONS

Conditional vs. Unconditional Contribution

- Once a transaction has been deemed a contribution, the next determination is whether that gift comes with strings
- Although grants and similar contracts always have terms that could be interpreted as conditions, these terms only create a “conditional” contribution if they introduce ***barriers*** that must be overcome by the recipient.
- The donor must have the right of return of assets, or a right of release from its obligation to transfer assets for an award to be conditional.

Conditional vs. Unconditional Contribution, continued

Type of Barrier	Measurable Metric	Example
Measurable performance-related	Specific outcome, certain level of service, identified number of units	A nonprofit receives a certain amount of money contingent upon the nonprofit raising matching funds
Stipulation related to the purpose of the agreement	Additional activity or event (general excludes administrative tasks and trivial situations)	Funding to address cybersecurity risks is contingent on the institution engaging an external consultant to perform a cybersecurity risk assessment
Limited discretion by recipient	Specific guidance on how assets should be spent	A grant that is designated for a specific program or activity

Performance-Related Barriers

- Specified level of service
- Specific output or outcome
- Matching
- Outside event

Conditional vs. Unconditional Contributions

- Example 4 – Multi-year Grant
  - **Case Study –** An organization that provides pro bono legal services receives a multi-year grant to provide services only in Orange County. The grant agreement includes a right of return as part of the foundation’s standard wording and a requirement that at the end of each year, a report must be filed with the foundation that explains how the assets were spent. The organization will not receive the second installment until they have filed the first annual report.
  - **Answer –** The organizations determines that the grant is not a conditional contribution. The requirement to provide services only in Orange County results in donor-restricted revenue because the location restriction is narrower than the overall mission of the entity. There are no requirements in the agreement that would indicate that a barrier exists, which must be overcome before the recipient is entitled to the resources. The organization also determines that the reporting requirement alone is not a barrier because it is an administrative requirement and not related to the purpose of the agreement, which is the actual research. This is an example in which a grant including a right of return could not be considered conditional because the return clause is not coupled with a barrier to be overcome.

Conditional vs. Unconditional Contributions

- Example 5 – Contribution to a Nursing Program
  - **Case Study -** An institution applied for and received a grant from a funder to provide career training in its nursing program. The grant requires a minimum number of patients who must receive services provided by nurse trainees in the program. Payments are made quarterly after the funder receives a report showing the number of patients served.
  - **Answer -** In this example, the award is classified as a contribution because the public is benefiting from the award rather than the resource provider. Further, the agreement includes a barrier, which is a right of release for a measurable performance-related metric in the minimum number of patients who must be seen each year. Therefore, the contribution would be considered conditional until the performance-related barrier is satisfied.

Example #6

- Hound House is an animal shelter and receives a 2-year unsolicited grant from a private foundation in the amount of $500,000 provided upfront to be used to expand its operations. The agreement indicates that Hound House must expand its facility by 5,000 square feet to accommodate additional animals by the end of the 2 years. The grant contains a right of return for any unused assets.

Example #7

- Brighter Path operates as a homeless shelter and provides meals to the homeless. Brighter Path receives an upfront grant of $75,000 from the city. The grant requires Brighter Path to use the assets to provide 5,000 meals to the homeless. The grant contains a right of return for meals not served, and there are no minimum thresholds.

Limited Discretion by the Recipient

- If usable for general operations, and there are no other barriers, then the grant is unconditional
- Examples of limited discretion: qualifying expenses
  - OMB allowable costs
  - Specific budget that cannot be modified

Example #8: Federal Grant for Services to Children in Foster Care

- Children's Advocates receives a grant from the Federal government to provide services to 13-16 year-old children in the foster care system. Children's Advocates' mission is to serve children in foster care. The organization was required to submit a line-item budget. The organization must apply for a budget modification if it wants to reallocate costs that exceed 10% of a budget line item. The organization is allowed to make quarterly draws against its grant and must provide a report each quarter on the actual use of funds.

Condition v. Restriction

- Restrictions are more specific than broad limits resulting from the following:

  a. The nature of the not-for-profit entity (NFP)

  b. The environment in which it operates

  c. The purposes specified in its articles of incorporation or bylaws or comparable documents for an unincorporated association.

- Lack specific performance requirements or other conditions
- Not subject to right of return/release

Effective Date and Transition

- Resource recipients:
  - Effective date same as Topic 606 – Contracts with Customers
    - Annual periods beginning after **December 15, 2018**
    - For public business entities or conduit debt obligors, amendments would apply to contributions received in annual periods beginning after **June 15 2018**.
- Resource Providers:
  - Effective for annual periods beginning after **December 15, 2019**
    - For public business entities or conduit debt obligors, amendments would apply to contributions made in annual periods beginning after **December 15, 2019**.

Effective Date and Transition, continued

- For organizations applying the standard on a modified prospective basis, the amendments should be applied to agreements that are either not completed as of the effective date or entered into after the effective date for the first set of financial statements following the effective date.
- The amendments should apply only the portion of revenue not recognized before the effective date in accordance with the current guidance.
- No prior period results should be restated.
- Under the approach the organization will be required to disclose the nature of and reason for the accounting change and the explanation of the reasons for significant changes in each financial statement line item resulting from applying the amendments instead of the previous guidance.
- Retrospective application is also permitted.
- Early adoption of the amendments is permitted.

ACCOUNTING FOR CONTRACTS WITH CUSTOMERS

ASU 606: Accounting for Contracts with Customers

- Key word is “Customer”
- The new pronouncement applies only to earned revenue
- Generally applies to the same types of revenue that the previous standard (ASU 605) applied to
- Creates a new model for recognition
- Effective 1/1/2019

Application of the Standard to the Nonprofit Sector

What organizations are likely to be impacted?

- Museums
- Performing Arts Groups
- Schools
- Colleges and Universities
- Trade Associations
- Hospitals and Clinics
- Other Specialized Nonprofits
- Organizations holding fundraising events

What types of revenue are exempt?

- Contributions
- Many, if not most, government contracts
- Many, if not most, foundation grants
- Certain “memberships” that are actually annual giving campaigns

New Approach to Earned Revenue

1. Identify a contract with a customer
2. Separate the contract's commitments
3. Determine the transaction price
4. Allocate a price to each promise
5. Recognize revenue when or as the organization transfers the promised good or service to the customer, depending on the type of contract

Identify Contract with a Customer

- (606-10-25-1) An entity shall account for a contract with a customer that is within the scope of this Topic only when all of the following criteria are met:

a) The parties to the contract have approved the contract (in writing, orally, or in accordance with other customary business practices) and are committed to perform their respective obligations.

b) The entity can identify each party's rights regarding the goods or services to be transferred.

c) The entity can identify the payment terms for the goods or services to be transferred.

d) The contract has commercial substance (that is, the risk, timing, or amount of the entity's future cash flows is expected to change as a result of the contract).

e) It is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

Not-for-profit consideration: donor or customer?

Separate the Contract Commitments

At contract inception, an entity shall assess the goods or services promised in a contract with a customer and shall identify as a performance obligation each promise to transfer to the customer either:

a) A good or service (or a bundle of goods or services) that is distinct
b) Distinct within the context of the contract – the promise to transfer the good or service is separately identifiable from other promises in the contract

Not-for-profit consideration: combination of exchange and contribution

Determine the Transaction Price

(606-10-32-2) An entity shall consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both.

Not-for-profit consideration: combination of exchange and contribution

Determine the Transaction Price

Must consider effects of all the following:

- Variable consideration, including right of return, rebates, etc.
- Constraining estimates of variable consideration
- Existence of significant financing component
- Non-cash consideration
- Consideration payable to a customer

Allocate Price to Each Promise

Once the separate performance obligations are identified and the transaction price has been determined, the standard requires an entity to allocate the transaction price to the performance obligations. This is generally done in proportion to their standalone selling prices (i.e., on a relative standalone selling price basis). As a result, any discount within the contract generally is allocated proportionally to all of the separate performance obligations in the contract.

- There are exceptions! For example, an entity could allocate variable consideration to a single performance obligation in some situations. The standard also contemplates the allocation of any discount in an arrangement to only certain performance obligations, if specified criteria are met.

Recognize Revenue Upon Transfer of Goods or Services

- Under the standard, an entity recognizes revenue only when it satisfies an identified performance obligation by transferring a promised good or service to a customer.
  - A good or service is considered to be transferred when the customer obtains control.
- Under the new standard, the transfer of control to the customer represents the transfer of the rights with regard to the good or service.
- The standard indicates that an entity must determine at contract inception whether it will transfer control of a promised good or service over time. If an entity does not satisfy a performance obligation over time, the performance obligation is satisfied at a point in time.

Example #1 of Revenue Recognition Under 606

Symphony has a Membership Program

- Members pay $60 in annual dues
- Members receive
  - A monthly newsletter - $30 value
  - Access to the museum's archives - $10 value
  - One free admission - $15 value
  - Designated parking – $20 value

Analysis

Allocate member dues to each of the 4 elements, and recognize each as delivered.

- Monthly newsletter - \$24 (\$30/\$75x\$60)
- Museum's archives - \$ 8 (\$10/\$75x\$60)
- One free admission - \$12 (\$15/\$75x\$60)
- Designated parking - \$16 (\$20/\$75x\$60)

Analysis

Allocate member dues to each of the 4 elements, and recognize each as delivered.

- Monthly newsletter - $24 ($30/$75x$60)
- Museum's archives - $ 8 ($10/$75x$60)
- One free admission - $12 ($15/$75x$60)
- Designated parking - $16 ($20/$75x$60)

What if archives are available to the general public?

Analysis

Allocate member dues to each of the 4 3 elements, and recognize each as delivered.

- Monthly newsletter - $27.69 ($30/$65x$60)
- Museum's archives - $ 8.00 ($10/$75x$60)
- One free admission - $13.85 ($15/$65x$60)
- Designated parking - $18.46 ($20/$65x$60)

If available to everyone, not part of the customer contract

Sales prices per individual item increased because overall membership price remained the same, and one element was removed.

Planning for Implementation

- Determine whether your organization has any arrangements that would be considered contracts with customers. Consider materiality.
- Analyze identified contracts to determine specific deliverables.
- If your recognition pattern will change, develop a communication plan for stakeholders such as your board and funding sources.
- Consideration of this should be occurring now, as this is effective 1/1/19 for calendar year entities and 7/1/19 for June 30 fiscal year organizations.

QUESTIONS?

RAISE YOUR HAND!

CLOSING REMARKS

Thomas Schulte
Partner & Southern CA Market Lead

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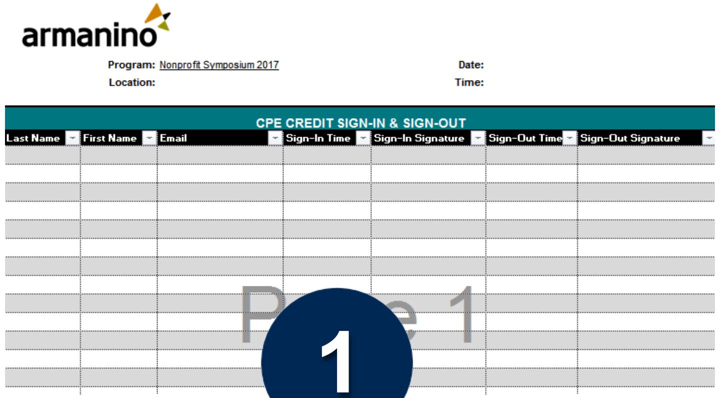

1

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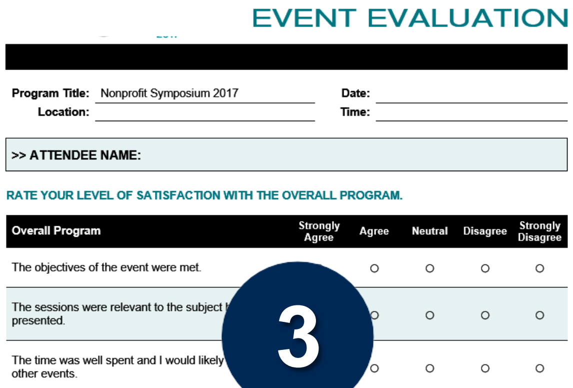
@ Registration Table

2

Stay for the
Entire Event
(It's Worth It!)



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Thank You!

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