# How to Evaluate a Grant Under New FASB Guidance

The webinar will begin in a few moments

*NOTE: Participants will receive an email within 48 hours with a link to the slide deck and recording.*

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# Learning Objectives

- **Evaluate** revenue recognition requirements and identify the proper actions to take
- **Discuss** how the current changes affect grants and related contributions
- **Analyze** recent and ongoing FASB updates

# Today’s Presenters

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# Agenda

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



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# 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.
  - **Example - 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.**
- 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.

 

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# Exchange Transaction vs. Contribution

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# 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.

 

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# 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.



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# Exchange vs. Contribution, continued

- Example 1 – Research Grant
  - **Case Study -** NFP E is a public charity that performs research on various diseases and allergies, including gluten-related allergies, as part of its overall mission. It receives a $100,000 grant from a foundation to perform research on gluten-related allergies over the next year. NFP E retains rights to the research, controls how the research is conducted and the research results will benefit the clients and the public that NFP E serves as part of its overall mission. NFP E has a monthly reporting requirement to the resource provider which includes an overview and analysis of the research conducted and research progress.
  - **Answer -** NFP E determines that the grant is a contribution. The resource provider does not receive commensurate value for the award in this transaction. The reporting requirement is not considered to be something of commensurate value. The benefit of this research is to the general public and the clients served by NFP E.

# 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*).

 

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# Conditional vs. Unconditional Contributions

# 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.



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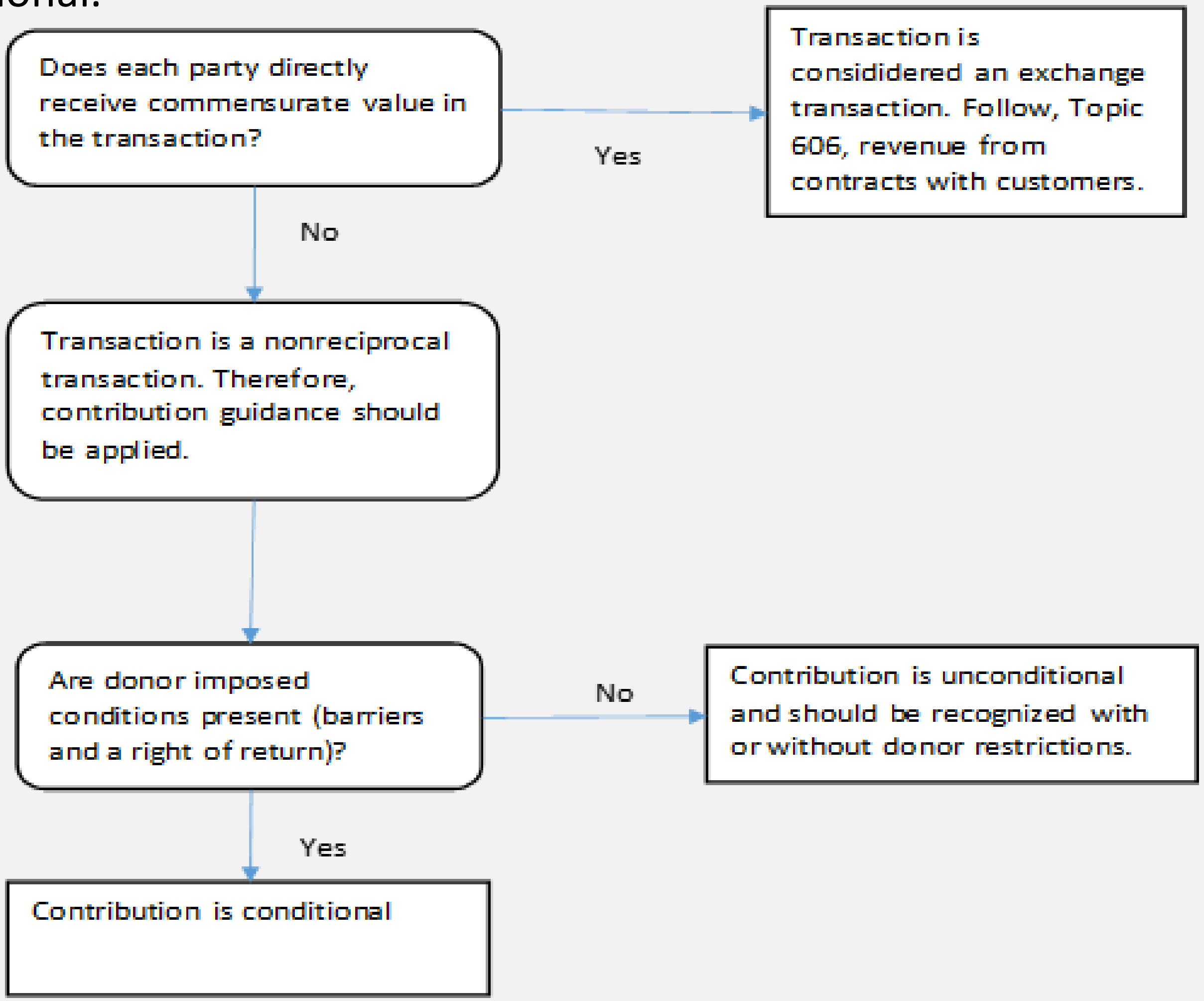
# Conditional vs. Unconditional Contribution, continued


| 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 (generally 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 |
| Requires additional action | Additional action(s) taken for a new or existing activity | The recipient is required to expand its facility |

# Conditional vs. Unconditional Contribution, continued

**Decision Flowchart -** The following is a diagram of a process for a nonprofit organization to take to determine whether the transfer of assets to a recipient is a contribution or exchange transaction and if a contribution whether the transaction is conditional or unconditional.



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# Conditional vs. Unconditional Contributions

- Example 1 – Research Grant
  - **Case Study -** NFP E is a public charity that performs research on various diseases and allergies, including gluten-related allergies, as part of its overall mission. It receives a $100,000 grant from a foundation to perform research on gluten-related allergies over the next year. The grant agreement includes a right of return as part of the foundation’s standard wording and a requirement that at the end of the grant period a report must be filed with the foundation that explains how the assets were spent.
  - **Answer -** NFP E determines that the grant is not a conditional contribution. The purpose of research on gluten-related allergies results in donor-restricted revenue because the purpose of the grant (working on gluten-free allergies) 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. NFP E 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, as determined by NFP E using judgment to assess the indicators of a barrier..

 

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# Conditional vs. Unconditional Contributions

- Example 1 – 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 during the year provided by nurse trainees in the program before the funder will transfer the assets.
  - **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..



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# Conditional vs. Unconditional Contributions

- Example 1 – Contribution from a Foundation
  - **Case Study -** ABC Foundation receives a grant proposal from an animal rescue facility, Nonprofit A, which requests a 3-year grant in the amount of $1,000,000 upfront to be used to expand its operations. The agreement indicates that Nonprofit A must expand its facility by at least 5,000 square feet to accommodate additional animals by the end of the 3 years. The grant contains a right of return if the minimum expansion target is not achieved.
  - **Answer -** This is an example of a conditional grant as there is a barrier regarding the 5,000 additional square feet which must be achieved by Nonprofit A to be entitled to assets and a right of return for unused assets or unmet expansion requirements.



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# System Considerations


- Ability to take an inventory of all active grants to evaluate for:
  - Contribution vs Exchange Transaction
    - Information to determine ***commensurate*** value
  - Conditional vs Unconditional
    - If there a right of return of a right of release

- Controlling the Narrative
  - How will donors perceive any significant changes to year-over-year revenue?
  - Is there any implication on debt covenants or other agreements such as leases?



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# Effective Date and Transition

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# 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**.



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# 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.



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