Nonprofit Seminar:
2018 Accounting Standard Changes

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TABLE OF CONTENTS

BACKGROUND

1993 STANDARD	2015 EXPOSURE DRAFT	ASU 2016-14
In 2011 a subcommittee of FASB reviewed to "ensure the standards continue to meet the evolving needs of a dynamic financial reporting environment."	Exposure draft included: - A defined 'operating activity' concept - "Mission and availability" requirement for income - That transfers from reserves would be considered income/expense - A requirement for the direct cash flow method	"Helping the NFP tell its financial story"

LIQUIDITY

QUALITATIVE (LIQUIDITY)

Disclose information on how the entity manages its liquid resources available to meet cash needs for **general expenditures** within **one year** of the date of the statement of financial position

QUANTITATIVE (AVAILABILITY)

Communicates the availability of an entity's financial assets at the date of the statement of financial position to meet cash needs for **general expenditures** within **one year** of the date of the statement of financial position

Availability may be affected by:
- Nature
- External limits imposed by donors, laws and contracts with others
- Internal limits imposed by governing board decisions

LIQUIDITY – FASB Example 1

Note G

The following reflects Not-for-Profit Entity A's financial assets as of the balance sheet date, reduced by amounts not available for general use because of contractual or donor-imposed restrictions within one year of the balance sheet date. Amounts not available include amounts set aside for long-term investing in the quasi-endowment that could be drawn upon if the governing board approves that action. However, amounts already appropriated from either the donor-restricted endowment or quasi-endowment for general expenditure within one year of the balance sheet date have not been subtracted as unavailable.

Financial assets, at year-end	$ 234,410
Less those unavailable for general expenditures within one year, due to:	
Contractual or donor-imposed restrictions:	
Restricted by donor with time or purpose restrictions	(11,940)
Subject to appropriation and satisfaction of donor restrictions	(174,700)
Investments held in annuity trust	(4,500)
Board designations:	
Quasi-endowment fund, primarily for long-term investing	(36,600)
Amounts set aside for liquidity reserve	(1,300)
Financial assets available to meet cash needs for general expenditures within one year	$ 5,370

LIQUIDITY – FASB Example 1, continued

Not-for-Profit Entity A is substantially supported by restricted contributions. Because a donor's restriction requires resources to be used in a particular manner or in a future period, Not-for-Profit Entity A must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditure within one year. As part of Not-for-Profit Entity A's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, Not-for-Profit Entity A invests cash in excess of daily requirements in short-term investments. Occasionally, the board designates a portion of any operating surplus to its liquidity reserve, which was $1,300 as of June 30, 20X1. There is a fund established by the governing board that may be drawn upon in the event of financial distress or an immediate liquidity need resulting from events outside the typical life cycle of converting financial assets to cash or settling financial liabilities. In the event of an unanticipated liquidity need, Not-for-Profit Entity A also could draw upon $10,000 of available lines of credit (as further discussed in Note XX) or its quasi-endowment fund.

LIQUIDITY – FASB Example 2

958-210-55-7 NFP A has $395,000 of financial assets available within 1 year of the balance sheet date to meet cash needs for general expenditure consisting of cash of $75,000, contributions receivable of $20,000, and short-term investments of $300,000. None of the financial assets are subject to donor or other contractual restrictions that make them unavailable for general expenditure within one year of the balance sheet date. The contributions receivable are subject to implied time restrictions but are expected to be collected within one year. NFP A has a goal to maintain financial assets, which consist of cash and short-term investments, on hand to meet 60 days of normal operating expenses, which are, on average, approximately $275,000. NFP A has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, as part of its liquidity management, NFP A invests cash in excess of daily requirements in various short-term investments, including certificate of deposits and short-term treasury instruments. As more fully described in Note XX, NFP A also has committed lines of credit in the amount of $20,000, which it could draw upon in the event of an unanticipated liquidity need.

LIQUIDITY – FASB Example 3

NFP A's financial assets available within one year of the balance sheet date for general expenditure are as follows.

Cash and cash equivalents	$	4,575
Accounts and interest receivable		2,130
Contributions receivable		1,825
Short-term investments		1,400
Other investments appropriated for current use		10,804
	$	20,734

NFP A's endowment funds consist of donor-restricted endowments and a quasi-endowment. Income from donor-restricted endowments is restricted for specific purposes and, therefore, is not available for general expenditure. As described in Note Y, the quasi-endowment has a spending rate of 5 percent. $1.65 million of appropriations from the quasi-endowment will be available within the next 12 months.

As part of NFP A's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, NFP A invests cash in excess of daily requirements in short-term investments. To help manage unanticipated liquidity needs, NFP A has committed lines of credit in the amount of $20 million, which it could draw upon. Additionally, NFP A has a quasi-endowment of $33 million. Although NFP A does not intend to spend from its quasi-endowment other than amounts appropriated for general expenditure as part of its annual budget approval and appropriation process, amounts from its quasi-endowment could be made available if necessary. However, both the quasi-endowment and donor-restricted endowments contain investments with lock-up provisions that would reduce the total investments that could be made available (see Note X for disclosures about investments).

LIQUIDITY – Next steps

- Get your Finance Committee or Board involved EARLY
- Determine what you want to communicate with the footnote
- Come up with a liquidity policy – what is considered a liquid asset? How much of savings are you going to plan on spending annually?
- Define or re-define any reserves/savings or board designations
- Be mindful of investment types – CDs, Bonds – is your policy to hold to maturity?
- Pick a preferred format and draft a note

FUNCTIONAL EXPENSE REPORTING

- All NFPs shall report information about **all expenses** in one location:
  - on the face of the statement of activities;
  - as a schedule in the notes to financial statements;
  - or in a separate financial statement (statement of functional expenses)

- Disclosure – a description of the methods used to allocate costs among program and support functions.

  The financial statements report certain categories of expenses that are attributable to more than one program or supporting function. Therefore, these expenses require allocation on a reasonable basis that is consistently applied. The expenses that are allocated include depreciation, interest, and office and occupancy, which are allocated on a square-footage basis, as well as salaries and benefits, which are allocated on the basis of estimates of time and effort.

FUNCTIONAL EXPENSE REPORTING

958-720-45-2A Activities that represent direct conduct or direct supervision of program or other supporting activities require allocation from management and general activities. Additionally, certain costs benefit more than one function and, therefore, shall be allocated. For example, information technology generally can be identified as benefiting various functions, such as management and general (for example, accounting and financial reporting and human resources), fundraising, and program delivery. Therefore, information technology costs generally would be allocated among the functions receiving direct benefit.

- Management and general activities include the following:
  - Oversight
  - General recordkeeping and payroll processing
  - Budgeting
  - Soliciting funds other than contributions and membership dues (advertising)
  - Grant and contract financial reporting
  - Disseminating information to inform the public of the NFP's stewardship of contributed funds (annual report)
  - Employee benefit management and oversight (HR)

FUNCTIONAL EXPENSE REPORTING – Next Steps

- Get your Finance Committee or Board involved EARLY
- Are you currently accurately tracking expenses – how can you start and which method should you use for which expense:
  - Square footage
  - Head Count
  - Time studies
  - Direct costs
- Should you expand the number of programs that are represented on the statement of functional expenses?
- Review previous disclosure example – create policy describing the allocation method which will create the additional disclosure and help in the calculation of functional expenses

NET ASSET CLASSIFICATION

WITH DONOR RESTRICTIONS

Can include detail on the statement of financial position or within the footnotes. Footnotes will include more detail on the balances and the changes within the balances and when they can be used (specified purpose, specified time, or held for perpetuity)

WITHOUT DONOR RESTRICTIONS

Board designated net assets require more disclosure – Amount and reason for designation will need to be disclosed

NET ASSET CLASSIFICATION – Next Steps

- Revisit Board designations
- Change internal financial statements to new terminology
- Leave current permanently restricted accounting policies and procedures in place
- Consider how much information will be on face of financial statements versus the footnotes

INVESTMENT INCOME

- Eliminates the requirement to disclose the composition of investment return
- Eliminates the requirement to disclose investment expenses
- Required to report investment income, less all external and direct internal investment expenses (direct conduct or supervision of the strategic and tactical activities involved in generating investment return)

INVESTMENT INCOME – Next Steps

- Verify no internal direct investment expenses

STATEMENT OF CASH FLOWS

- NFP have the option to use the direct method to present their cash flow statement

Direct Method

Cash Flows From Operating Activities	
Cash received from donors	**2,168,739**
Cash received from program fees	**664,789**
Cash paid to employees	**(1,579,541)**
Cash paid to vendors	**(1,220,604)**
Investment income retained in investments	**(17,168)**
Net Cash Provided by Operating Activities	**16,215**

Indirect Method

Cash Flows From Operating Activities	
Increase in net assets	**$ 25,686**
Adjustments to reconcile change in net assets to net cash from operations:	
Investment income retained in investments	**(17,168)**
Depreciation	**6,511**
(Increase) Decrease in:	
Pledges receivable	**(3,500)**
Prepaid expenses	**1,700**
Increase (Decrease) in:	
Accounts payable	**(2,082)**
Accrued payroll	**5,068**
Net Cash Provided by Operating Activities	**16,215**

CAPITAL GIFTS

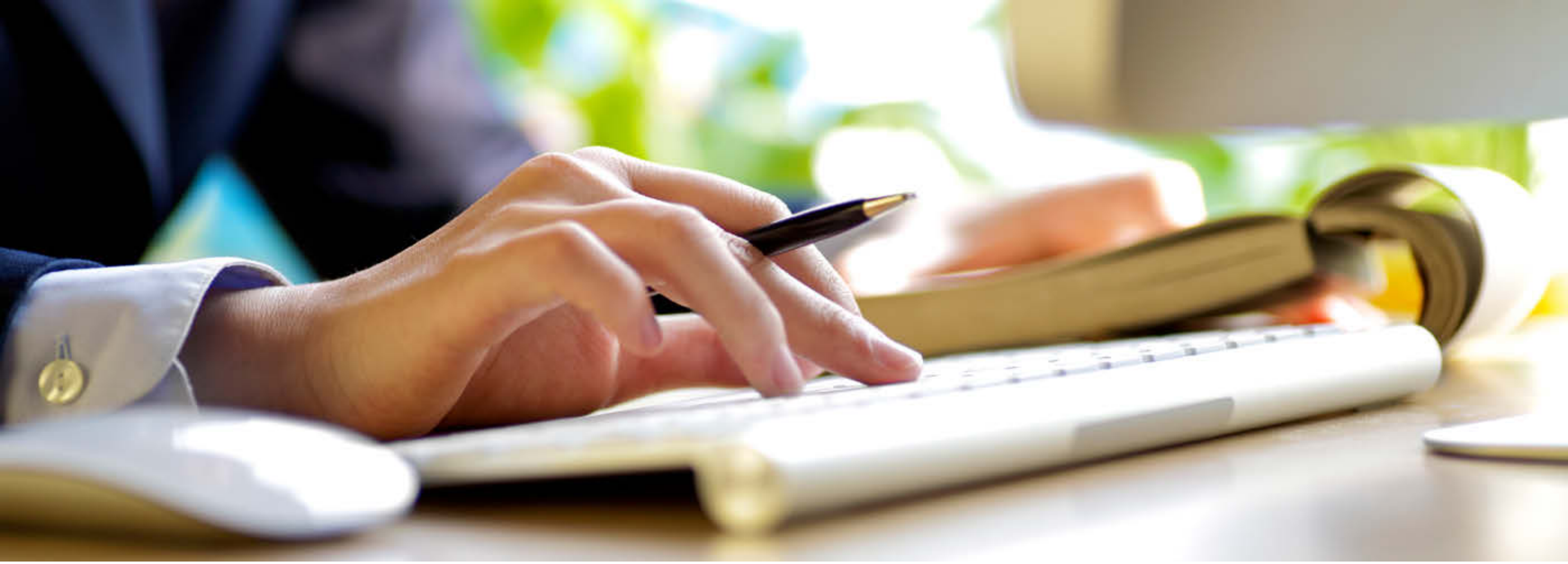
- Capital gifts (building, equipment, construction costs) are recognized when the asset is placed in service, unless donor stipulations limits the use of the asset for a period of time. Must adopt the placed in service approach if you have been using the over-time approach.

IMPLEMENTATION

Entities must apply all provisions during their year of implementation, except for comparative statement of functional expenses (unless currently required) and comparative information on liquidity and availability of resources.

EFFECTIVE FOR YEARS BEGINNING AFTER DECEMBER 15, 2017

Year of implantation will include a disclosure of the nature of any reclassifications or restatements and their effects, if any, on changes in the net asset classes for each period presented.



SUMMARY OF ACTION ITEMS

- Liquidity – Have a policy, define reserves, and know what you want to tell the reader of the financial statements
- Functional Expenses – Set up a system that allows you to allocate time and space correctly, revisit historic allocation and determine if breaking out major programs would improve the financial statements
- Net Asset Classification – Board should re-designate funds and define them within the context of the liquidity policy
- Investment Income – Determine any internal expenses
- Cash Flows – Assess if direct method would improve the financial statements
- Other Changes – Reassess items in your financial statements

ANY QUESTIONS?

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