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Webinar Series

Implementation Issues Related to ASU 2016-14
Financial Statements of Not-for-Profit Entities

May 30, 2017

Presenters

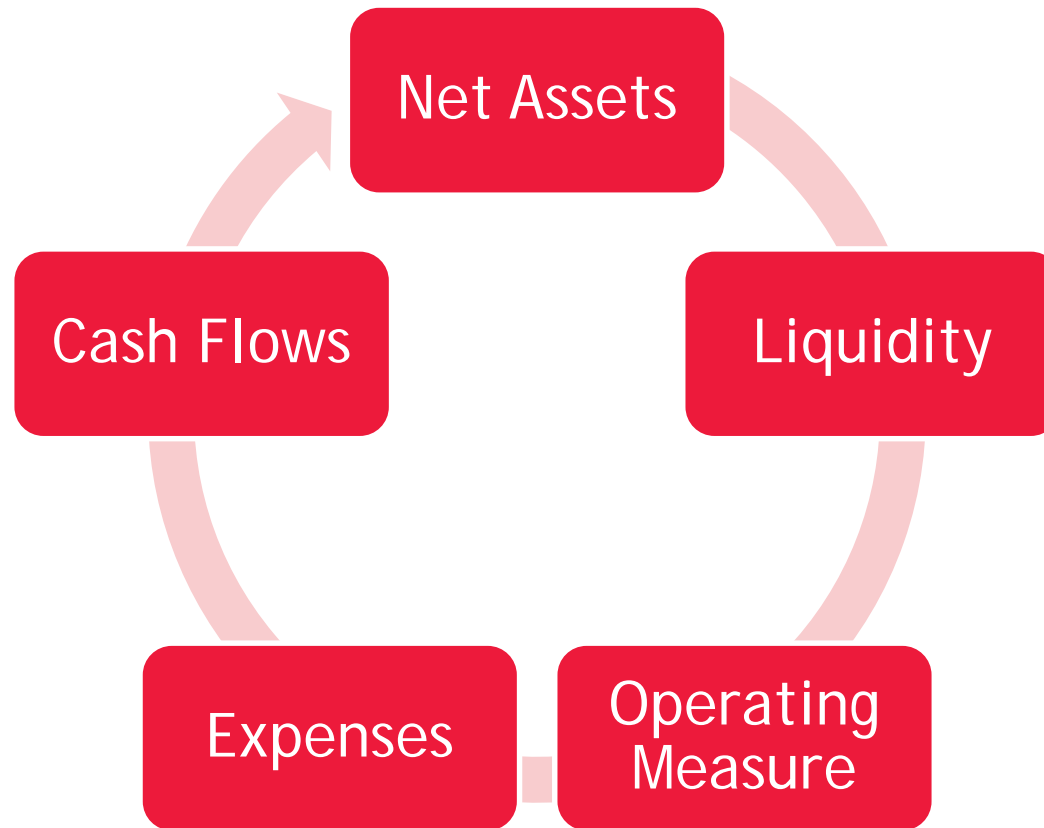
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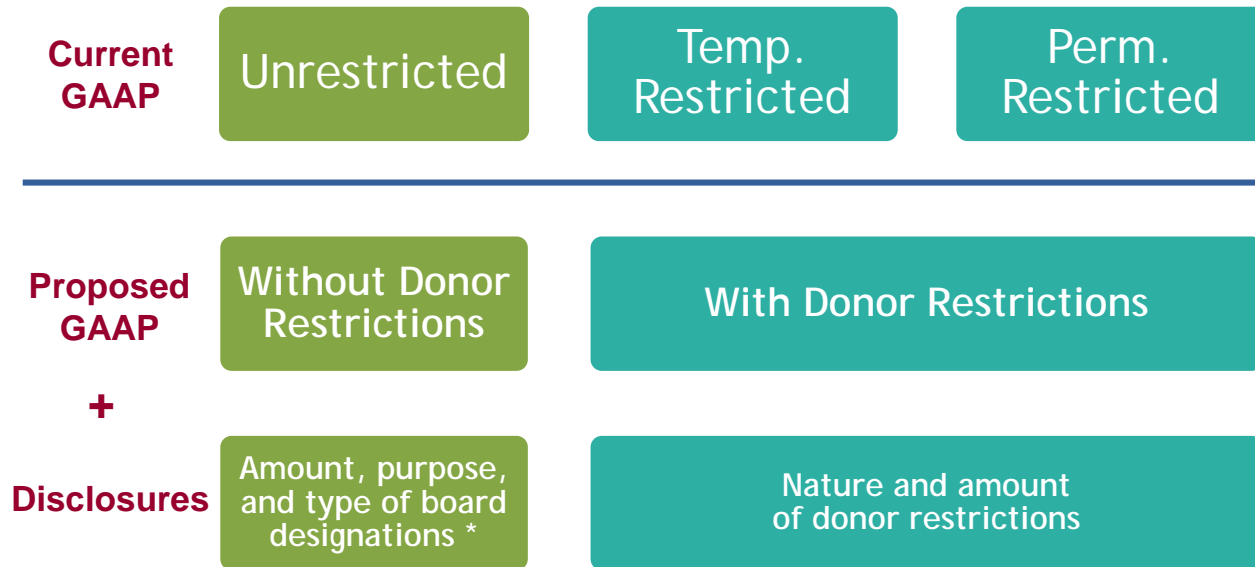


Implementation Issues Related to ASU
2016-14 *Financial Statements of
Not-for-Profit Entities*



Net Assets

Net Assets



** New disclosure requirement*

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Example Effect on Statement of Financial Position

Not-for-Profit Entity A
 Statements of Financial Position
 June 30, 20X1 and 20X0
 (in thousands)

	20X1	20X0
Assets:		
Cash and cash equivalents	\$ 4,575	\$ 4,960
Accounts and interest receivable	2,130	1,670
Inventories and prepaid expenses	610	1,000
Contributions receivable	3,025	2,700
Short-term investments	1,400	1,000
Assets restricted to investment in land, buildings, and equipment	5,210	4,560
Land, buildings, and equipment	61,700	63,590
Long-term investments	218,070	203,500
Total assets	\$ 296,720	\$ 282,980
Liabilities and net assets:		
Accounts payable	\$ 2,570	\$ 1,050
Refundable advance		650
Grants payable	875	1,300
Notes payable		1,140
Annuity trust obligations	1,685	1,700
Long-term debt	5,500	6,500
Total liabilities	10,630	12,340
Net assets:		
Without donor restrictions (Note DD)	92,600	84,570
With donor restrictions (Note B)	193,490	186,070
Total net assets	286,090	270,640
Total liabilities and net assets	\$ 296,720	\$ 282,980

Note: Shaded lines are required to be presented.

Source: ASU 958



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Example of Effect on Statement of Activities - Columnar Format

Not-for-Profit Entity A
Statement of Activities
Year Ended June 30, 20X1
(In thousands)

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Revenues, gains, and other support:			
Contributions	\$ 8,640	\$ 8,390	\$ 17,030
Fees	5,200		5,200
Investment return, net	6,650	18,300	24,950
Gain on sale of equipment	200		200
Other	150		150
Net assets released from restrictions (Note D):			
Satisfaction of program restrictions	8,990	(8,990)	
Satisfaction of equipment acquisition restrictions	1,500	(1,500)	
Expiration of time restrictions	1,250	(1,250)	
Appropriation from donor endowment and subsequent satisfaction of any related donor restrictions	7,500	(7,500)	
Total net assets released from restrictions	<u>19,240</u>	<u>(19,240)</u>	<u>-</u>
Total revenues, gains, and other support	<u>40,080</u>	<u>7,450</u>	<u>47,530</u>
Expenses and losses:			
Program A	13,296		13,296
Program B	8,649		8,649
Program C	5,837		5,837
Management and general	2,038		2,038
Fundraising	2,150		2,150
Total expenses (Note F)	<u>31,970</u>		<u>31,970</u>
Fire loss on building	80		80
Actuarial loss on annuity trust obligations		30	30
Total expenses and losses	<u>32,050</u>	<u>30</u>	<u>32,080</u>
Change in net assets	<u>8,030</u>	<u>7,420</u>	<u>15,450</u>
Net assets at beginning of year	<u>84,570</u>	<u>186,070</u>	<u>270,640</u>
Net assets at end of year	<u>\$ 92,600</u>	<u>\$ 193,490</u>	<u>\$ 286,090</u>

Note: Shaded lines are required to be presented.

Source: ASU 958-205-55-14



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Disclosures Related to Net Assets

- Ø Amounts and purposes of governing board designations, appropriations, and similar actions that result in self-imposed limits on the use of resources without donor-imposed restrictions as of the end of the period.
- Ø Composition of net assets with donor restrictions at the end of the period and how the restrictions affect the use of resources.
- Ø Additional information related to underwater endowment funds.

Disclosures Related to Net Assets (Cont'd)

- ∅ Information about the nature and amounts of different types of donor-imposed restrictions should be reported either on the face of the statements or in the notes. Separate line items that distinguish between the different types of restrictions may be used such as:
- Assets, such as land or works of art, donated with stipulations that they be used for a specified purpose, be preserved, and not be sold.
 - Assets donated with stipulations that they be invested to provide a permanent source of income.
 - Support of particular operating activities.
 - Investment for a specified term.
 - Use in a specified future period.
 - Acquisition of long-lived assets.

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Net Asset Disclosure Example

With donor restrictions		
Perpetual in nature	\$	200,000
Purpose restricted		1,840,000
Time-restricted only, for periods after 20X1		150,000
		<hr/>
	\$	2,190,000
Without donor restrictions		
Designated by the Board for [purpose]	\$	1,000,000
Undesignated		24,000,000
		<hr/>
Net assets		25,000,000
		<hr/>
	\$	27,190,000
		<hr/> <hr/>

Excerpt from ASC 958-210-55-3

Source: ASU 958

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“Underwater” Endowments

Revised net asset classification

- To be reflected in net assets with donor restrictions rather than in net assets without donor restrictions

Enhanced disclosures

- In addition to aggregate amounts by which funds are underwater (current GAAP), also disclose aggregate of original gift amounts (or level required by donor or law) for such funds, fair value, and any governing board policy or decision to reduce or not spend from such funds.

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Endowment disclosures

A nonprofit is required to report the following for endowments:

- Ø Net asset classification (i.e., With or without donor restrictions)
- Ø Net asset composition (i.e., Board-designated endowment or with donor restrictions)
- Ø Changes in net asset composition
- Ø Spending policies
- Ø Related investment policies

No substantial changes here other than in naming convention of net asset classifications and 'underwater endowments' as described on previous page.

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Expiration of Capital Restrictions

Gifts of cash restricted for acquisition or construction of PP&E

- NFPs would be required to use the placed-in-service approach (*no more implied time restrictions*)



Liquidity

Liquidity and Availability

NFPs are required to provide the following information that will be useful for a reader to determine how the organization manages its liquid assets to meet cash needs for general expenditures within one year of the Statement of Financial Position (SOFP) date:

- u **Qualitative** information on how an NFP manages its liquid available resources and its liquidity risk (in the notes)
- u **Quantitative** information that communicates the availability of an NFP's current financial assets at the balance sheet date to meet cash needs for general expenditures (on the face and/or in the notes)

Availability of financial assets may be affected by the nature of the asset, external limits imposed by donors, laws or contracts with others, or internal limits imposed by governing board decisions.

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Quantitative and Qualitative Liquidity and Availability of Resources Disclosure Example

Note T

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
	<u>\$ 20,734</u>

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).

Source: ASU 958-210-55-8



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Quantitative Disclosure of Financial Asset Availability

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	<u>\$ 5,370</u>

* Total assets, less nonfinancial assets (e.g., PP&E, inventory, prepaids)

** Excludes amounts that have been appropriated for next 12 months that do not have purpose restrictions

Source: ASU 958-205-55-21

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Operating Measure

Operating Measure: Improved Disclosures

- u For those NFPs that utilize an operating measure and show governing board designations, appropriations, and similar actions (internal transfers) in the measure
- u These NFPs must report these types of internal transfers appropriately disaggregated and described by type (either on the face of the financial statements or in the notes)



Example of Operating Measure Presentation

Not-for-Profit Entity A Statement of Activities Year Ended June 30, 20X1

	<u>Without Donor Restrictions</u>	<u>With Donor Restrictions</u>	<u>Total</u>
Operating revenues, gains, and other support:			
Contributions	\$X,XXX	\$ X,XXX	\$XX,XXX
Less:			
Contributions designated by board for capital projects	(3,000)		(3,000)
Contributions and bequests designated by board for quasi-endowment	(5,000)		(5,000)
Investment returns appropriated from quasi-endowment	1,025		1,025
Programmatic investing return	XX		XX
Other	XXX		XXX
Net assets released from restrictions			
Investment return appropriated and released for current operations from donor-restricted endowment	X,XXX	(X,XXX)	
[Other net assets released from restrictions]	X,XXX	(X,XXX)	
Total operating revenues, gains, and other support	<u>XX,XXX</u>	<u>X,XXX</u>	<u>XX,XXX</u>
Operating expenses:			
Program A	XX,XXX		
Program B	X,XXX		
Program C	X,XXX		
Management and general	X,XXX		
Fundraising	X,XXX		
Total operating expenses	<u>XX,XXX</u>		<u>XX,XXX</u>
Operating revenues and support in excess of operating expenses	XX,XXX	X,XXX	X,XXX
Investment return, net	X,XXX	XX,XXX	XX,XXX
[Other items considered to be nonoperating]	X,XXX	X,XXX	X,XXX
Investment returns appropriated for current operations from quasi-endowment	(1,025)		(1,025)
Contributions designated by board for capital projects	3,000		3,000
Contributions and bequests designated by board for quasi-endowment	5,000		5,000
Loss on extinguishment of debt	(X,XXX)		(X,XXX)
Change in fair value of interest rate swap	X,XXX		X,XXX
Change in net assets	<u>\$XX,XXX</u>	<u>\$ X,XXX</u>	<u>\$XX,XXX</u>

Source: ASU 958-225-55-17



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Expenses

Expense Reporting

∅ Report expenses, either on the face of financial statements or in the notes, by:

- Function *
- Natural classification
- Analysis (disaggregate function by nature)

* *currently required in GAAP*

∅ NFPs are now required to provide qualitative disclosures about methods used to allocate costs among program activities and supporting services

∅ ASU 2016-14 also provides enhanced guidance on allocations from management and general (M&G) expenses

- **Key concept:** direct conduct or direct supervision

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Expense Reporting

∅ Additional Information

- If expenses are reported in other line items within the statement of activities (e.g., salaries are included in costs of goods sold) they should be included in the functional reporting schedule by their natural classification.
- External and direct internal investment expenses that are netted against investment return should not be included in the functional expense analysis.

Expenses By Both Nature and Function for a College/University

Analysis of Expense by functional and natural Categories

Total expenses include all operating expenses and the nonoperating expense of other components of net periodic pension cost.

	Program Activities			Supporting Activities			Total Expense 2016
	Academic and Student Programs	Public Service	Auxiliaries	Administrative Support	Facilities operation & maintenance	Fundraising	
Salaries and wages	\$ 10,026,575	\$ 251,127	\$ 627,796	\$ 3,506,843	\$ 884,896	\$ 1,305,958	\$ 16,603,194
Employee benefits	3,590,259	65,647	268,684	2,288,274	493,262	116,938	6,823,064
Services, supplies, and other	2,667,856	217,448	602,060	1,193,442	298,397	1,168,202	6,147,405
Occupancy, utilities, and maintenance	83,221	1,339	499,092	94,233	2,303,240	6,697	2,987,823
Grants to others	285,658	2,409,061	-	-	-	-	2,694,719
Depreciation and amortization	808,039	26,947	1,394,612	284,313	49,833	8,788	2,572,532
Interest	-	-	689,145	-	-	-	689,145
	<u>17,461,608</u>	<u>2,971,569</u>	<u>4,081,389</u>	<u>7,367,106</u>	<u>4,029,628</u>	<u>2,606,582</u>	<u>38,517,882</u>
Facilities operation and maintenance	1,859,326	76,466	897,467	1,022,227	(4,029,628)	174,142	-
Total operating expense in FY 16	<u>\$ 19,320,935</u>	<u>\$ 3,048,035</u>	<u>\$ 4,978,856</u>	<u>\$ 8,389,333</u>	<u>\$ -</u>	<u>\$ 2,780,724</u>	<u>\$ 38,517,882</u>

The financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the Seminary. These expenses include depreciation and amortization, interest, the president's office, communications, media production, information technology, and facilities operations and maintenance. Depreciation is allocated base on square footage and interest is allocated based on usage of space. Costs of other categories were allocated on estimates of time and effort.

For example: 958-205-55-21 Note F (Page 66 of ASU)

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Cost Methodology Issues - College/University

Allocation	Current Cost Allocation Method	Revised Allocation Method
Facilities Operation & Maintenance	Sq. Footage basis	Service & effort estimate
Depreciation & amortization	Sq. Footage basis	No change
Interest	Usage of Space	No change
IT related costs	Do not allocate	Service & effort estimate and costs of specific technology utilized
Media production & Communication	Do not allocate	Service & effort estimate

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Example Disclosure for Expense Allocation

Disclosure

NOTE X. METHODS USED FOR ALLOCATION OF EXPENSES FROM MANAGEMENT AND GENERAL ACTIVITIES

The financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the Organization. Those expenses include depreciation and amortization, the president's office, communications department, and information technology department. Depreciation is allocated based on square footage, the president's office is allocated based on estimates of time and effort, certain costs of the communications department are allocated based on estimates of time and effort, and the information technology department is allocated based on estimates of time and costs of specific technology utilized.

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Investment Return

Reporting of Investment Returns

- u Net presentation of investment expenses against investment return on the face of the statement of activities
 - *Netting limited to external and **direct** internal expenses*

- u Disclosure of investment expenses **no longer required**, no longer require disclosure of investment income **components**

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Investment Return

- Ø Direct internal investment expenses involve the direct conduct or direct supervision of the strategic and tactical activities involved in generating investment return including:
 - Salaries, benefits, travel, and other costs associated with the officer and staff responsible for the development and execution of investment strategy.
 - Allocable costs associated with internal investment management and supervising, selecting, and monitoring of external investment management firms.
- Ø Direct internal investment expenses do not include items that are not associated with generating investment return. For example, the costs associated with unitization and other such aspects of endowment management would not be allocated.



Cash Flow Statement

Cash Flow Statement

Continue to Allow free choice between the **Direct Method** and the **Indirect Method**

- However the Indirect reconciliation will no longer be required for Direct Method

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Implementation and Effective Date

Effective Date, Early Adoption, and Transition

Effective Date: For fiscal years beginning after 12/15/2017 (e.g., FY 2018-19 for Higher Eds)

- Interim financials the following year

Early Adoption: Permitted, but must apply the regular transition provisions.

Transition:

- For year of adoption: apply all provisions.
- For comparative years presented: apply all provisions, except can choose not to present:
 - Analysis of expenses by nature and function, and/or
 - Disclosures around liquidity and availability of resources

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Important Notes

NFPs are *already permitted* to incorporate many of the changes in the ASU

The only changes that cannot be done without formally adopting the ASU are:

- (1) Presenting one class of restricted net assets (consolidating temporarily and permanently restricted)
- (2) Underwater endowment accounting
- (3) Eliminated disclosures of investment return components and netted expenses
- (4) Eliminated requirement to provide indirect reconciliation if using direct method for operating cash flows

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QUESTIONS

