BDO KNOWLEDGE

2019 COMPLIMENTARY NONPROFIT
AND EDUCATION WEBINAR SERIES

TRENDS AND ISSUES IN VALUATION OF GIFTS IN-KIND (GIKI) CONTRIBUTIONS

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With You Today

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Learning Objectives:

Participants will have the following after attending this webinar:

- An understanding of what is a “gift-in-kind” and the issues around accounting for such transactions.
- Develop an awareness and understanding of the key pitfalls in valuing in-kind gifts.
- Articulate the key reporting requirements under general accepted accounting principles for gifts-in-kind.
- Familiarity with the latest developments, trends and issues with these types transactions.

Agenda

I. Importance of GIKI

II. Requirements to Recognize Contributed Services

III. Services Received from Personnel of an Affiliate

IV. Requirements to Recognize Contributed Goods

V. International Issues

VI. Typical Issues with GIKI

VII. Issues to Consider

VIII. Practical Tips to Consider in Telling the NFP Financial Story

Importance of GIKI

The FASB in its Concept Statement No. 4, lists several objectives for nonprofit financial reporting which can be simply summarized concisely related to Gifts In-kind (GIKI), which is as follows:

Portray economic reality without misleading the user.

It is important to reflect properly GIKI in the financial statements in order to demonstrate those resources available to the NFP but also how resources were used.

If the portrayal of how GIKI resources were used is not properly communicate in the NFP financial statements, users/reader will receive misinformation about the NFPs financial health and the costs to provide mission related services.

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Requirements to Recognize Contributed Services

Contributions of services shall be recognized if the services received:

1. Create or enhance nonfinancial assets or
2. Require specialized skills are provided by individuals possessing those skills.

The contributed services must also typically be purchased by the NFP if not provided by donation.

Under Generally Accepted Accounting Principles (GAAP) in the United States, contributed services are recognized and recorded as revenue (credit) and expense (debit), and the effect on the statement of activities is a zero.

Requirements to Recognize Contributed Services (Cont'd)

For volunteered services, there are **two** criteria, which must be met in order to recognize revenue and expense, which are as follows:

- The first criterion is that the volunteered services must require **specialized knowledge or skills,** and

  For example, if the NFP needed legal services and received pro bono services from a lawyer, this criterion would be met. However, if a lawyer volunteers to answer phones or paint an office, the criterion is not met.

  The volunteer must have these specialized skills.

Requirements to Recognize Contributed Services (Cont'd)

The second criterion, which must also be met, is that if the service were not donated, **the organization would have purchased the service**. So in the example above, if the donated legal services were so needed that the organization would have purchased them anyway then this criterion is met.

Services Received from Personnel of an Affiliate
(ASU 2013-06)

Personnel services received from an affiliate (parent/sub or common control) for which the affiliate doesn't charge the recipient NFP Recipient NFP recognizes.

Measured at cost incurred by the affiliate:

- Contributed services criteria no longer applicable.
- FV practicability exception if the cost will significantly over-state or understate the value of the services received.
- Entities under Topic 954 (healthcare) would report as equity transfer.

Effective for f/y beginning after 6-15-2014.

Modified retrospective application; early adoption permitted.

Requirements to Recognize Contributed Goods

There are other types of GIKI beyond volunteers' time which are contributed goods. Contributed goods are items such as donated advertising and free rent. For contributed goods, the "specialized knowledge/skills" test is not applicable.

It is important to note that the second test is still applicable. To book any GIKI the organization must be able to say it would have purchased the service if it were not donated. Implied in this statement is the idea the organization could afford to purchase the service.

Requirements to Recognize Contributed Goods (Cont’d)

Consider for a moment two identical not-for-profits with identical fundraising strategies and budgets. (We’ll call them “X” and “Y”). Now imagine that one of these charities (Charity “X”) receives donated advertising, which it would not have otherwise purchased (and therefore does not record as revenue). Charity X clearly benefits from the donated advertising and can reach more donors than Charity Y. As a result, it would seem that revenue is conceptually understated. Therefore, the benefit to the organization would never be recorded on the statement of activities. Additionally, this will impact ratios that some use to evaluate Charity X. If Charity X had recognized revenue the offsetting debit would go to general and administrative and fundraising expense.

As a result, the overhead ratios between these two charities would be different. Namely because, Charity X benefits from the use of more resources than its peer.

International issues

GIKI can become more complicated in an international setting. While US GAAP guidance is very specific, IFRS does not specifically address GIKI. As a result, there is room for a wider range of practice. Many offices simply do not book GIKI at all.

International Issues (Cont'd)

In fact in some countries, Canada for example, recording GIKI is prohibited by statutory requirements. Absent these restrictions, I believe that it is reasonable for an NFP reporting under IFRS to reference to US GAAP under IAS 8.

I believe that absent specific guidance under IFRS, a charity could book GIKI without considering whether or not it would have purchased the service anyway.

Based on the current diversity of practice, which clouds comparability and global reporting makes it difficult for international organizations to set a global GIKI policy.

Typical Accounting Issues with GIKI

Typical questions around GIKI relate to three issues around the fair value of the gift:

- Fair Value determination
- Origin or destination,
- Donor restrictions, and
- Asset attributes (i.e. product expiration date).

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Fair Valuing GIKI

GIKI fair value is based on the guidance promulgated by the FASB's Accounting Standards Codification Topic ASC 820, *Fair Value Measurement* (formerly FAS 157)

Fair value is defined as "the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date."

So what does this mean for GIKI, which typically isn't sold but instead is distributed to beneficiaries?

Fair Valuing GIKI (Cont'd)

Generally, neither the origin of the GIKI nor its intended programmatic destination would affect its fair value.

Fair value would be affected by changes in the market prices where the GIKI would be normally be sold (i.e. the principal market).

The principal market is the market in which the reporting entity would sell the asset with the greatest volume and level of activity for the asset.

Origin or destination:

The fact that the NFP will actually be sending the donated goods it to beneficiaries in a developed or developing country has **no effect** on the principal market since the goods would be normally sold in, the market which would be used for valuing the goods.

Beneficiaries, by definition, are not market participants. Market participants are entities who would transact for goods and are able to buy the products from the reporting entity.

GIKI by its nature is excess goods donated to NFPs for distribution to beneficiaries. Therefore, it may be difficult to identify a market where the goods are sold.

Donor Restrictions

Donor restrictions can be entity attributes or asset attributes. Two examples of entity attributes include IRS Section 170(e) 3 restrictions or temporary donor restrictions for time or purpose.

Entity restrictions do not affect the underlying asset since market participants wouldn’t consider it. Therefore, entity restrictions should not affect the fair value.

Donor Restrictions

Example:

A donor restriction, which becomes an asset attribute, is a restriction on the use of land for which the underlying deed has been altered to include development restrictions. Donor restrictions, which affect the underlying asset generally have an effect on the fair value because these are restrictions which market participants would consider when buying the asset.

Assets may have attributes which are considered “standard” in the marketplace. When the GIKI received differs from these market “standards”, an adjustment to its value may be necessary.

Issues to Consider

Several issues that the NFP should consider are as follows:

- Product expiration dates – if the product received is short-dated compared to products available to most market participants, a discount should be applied.
- Quantities of products received – if the product is received in a wholesale quantity, but retail values are readily available, a wholesale discount should be applied, and
- Quality of products received – if the product received is lower quality than products typically sold in the marketplace, a discount should be applied.

For more information, you may want to review the AERDO standards (now The ACCORD Network).

Practical Tips to Consider in Telling the NFP Financial Story

- Large capital gifts can cause misleading surpluses and deficits.
- For capital gifts of depreciable assets (or cash to purchase them), prevent this problem by recognizing the gift gradually over the life of the asset. Nonprofits adopting such a policy must disclose it.
- For capital gifts of non-depreciable assets (or cash to purchase them), prevent the problem by segregating capital from operating items in the Statement of Activities.
- In-kind gifts can cause misleading surpluses and deficits, and mask the scale and financial condition of a nonprofit.
- Prevent these problems by segregating in-kind revenue and expense items from monetary items on the Statement of Activities.
- Use the direct method for presenting the Statement of Cash Flows.

Questions?

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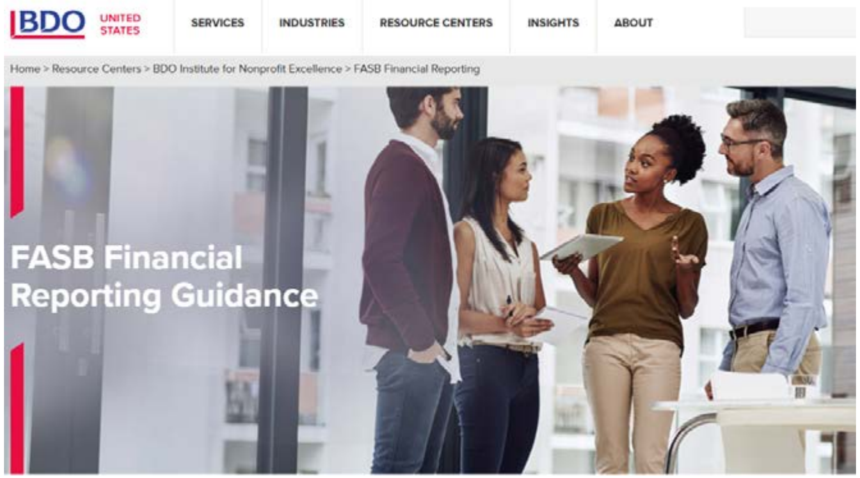
BDO Resources

Resources

BDO's Institute for Nonprofit Excellence Resource Center for our FASB Financial Reporting Guidance page for information on ASU 2016-14 that includes:

- Podcasts and videos
- Articles and blog posts
- Links to FASB Resources
- https://www.bdo.com/resource-centers/institute-for-nonprofit-excellence/fasb-financial-reporting

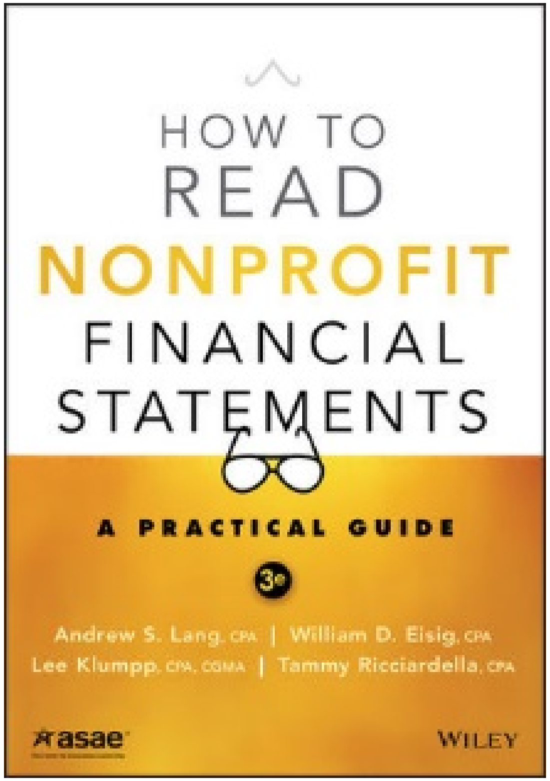


Resources

BDO's Publication:

How to Read Nonprofit Financial Statements:
A Practical Guide

https://www.bdo.com/resource-centers/institute-for-nonprofit-excellence/book-promo



Resources – Upcoming Webinars

Nonprofit & Education Webinar Series

The BDO Institute for Nonprofit Excellence provides a complimentary educational series that is designed specifically for busy professionals in nonprofit and educational institutions.

Our 2019 BDO KNOWLEDGE Nonprofit and Education Webinar Series will keep you abreast of trends, timely topics and challenges that are impacting the nonprofit environment and provide you with key takeaways relevant for busy professionals working in and with nonprofit and education organizations. We invite you to take part in this program with members of your organization. Including board members.

Stay tuned to the Nonprofit Standard blog or refer to www.bdo.com/resource-centers/institute-for-nonprofit-excellence for further details and registration information.

4/25/2019 1:00 - 2:15 PM ET
Trends and Issues in Valuation of Gifts In-Kind
1.5 CPE hours

5/23/2019 1:00 - 2:00 PM ET
State and Local Tax Environment for Nonprofits - Impact of Wayfair
1 CPE hour

6/27/2019 1:00 - 2:15 PM ET
What You Need To Know About the New Lease Accounting
1.5 CPE hours

7/25/2019 1:00 - 2:40 PM ET
Complex Structures and Nonprofit Organizations/Section 199A
2 CPE hours

9/11/2019 1:00 - 2:15 PM ET
2019 Benchmarking Survey Results
1.5 CPE hours

10/24/2019 1:00 - 2:15 PM ET
Annual Nonprofit Tax Update
1.5 CPE hours

11/21/2019 1:00 - 2:40 PM ET
Annual Nonprofit Accounting & Auditing Update
2 CPE hours