BDO BULLETIN

FASB CLARIFIES AND IMPROVES GUIDANCE FOR NOT-FOR-PROFIT GRANT AND CONTRIBUTIONS ACCOUNTING

JULY 2018

SUMMARY

The FASB issued ASU 2018-08[1] (the ASU) to clarify the accounting guidance related to contributions made or received. This guidance primarily affects not-for-profit (NFP) entities, although it also applies to businesses to the extent that they make or receive contributions, including grants. The ASU will likely result in more grants and contracts being accounted for as unconditional or conditional contributions rather than exchange transactions compared to current guidance. The new ASU has various effective dates beginning after June 15, 2018 with specific transition guidance. Early adoption is permitted.

BACKGROUND

The implementation of ASC 606[2] brought to light diversity in practice in how NFP organizations classify grants and contracts in the financial statements from federal, state and local governments and other funding sources, such as foundations as either contributions (nonreciprocal) or exchange (reciprocal) transactions. Contributions, defined as an unconditional transfer of cash or assets in a voluntary non-reciprocal transfer, are scoped out of ASC 606 whereas exchange transactions, a reciprocal transaction in which two parties exchange items of commensurate value, are within the scope of ASC 606 and must be accounted for following the new revenue recognition guidance.

Diversity also exists in assessments of restrictive conditions specified in the contribution arrangement, including whether the likelihood of failing to meet a condition is remote and whether and how remote provisions affect the timing of when a contribution is recognized. Differences in these conclusions can affect the timing of revenue recognition.

The FASB issued ASU 2018-08 to reduce this diversity by clarifying whether:

- Transactions are required to be accounted for as contributions within the scope of ASC 958[3] or as exchange transactions subject to other guidance
- A contribution is conditional

[1] *Not-for-Profit Entities (ASC 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*

[2] *Revenue from Contracts with Customers*

[3] *Not-for-Profit Entities*

MAIN PROVISIONS

Characterizing Grants and Similar Contracts as Reciprocal Exchanges or Contributions

The ASU clarifies and improves the scope and accounting guidance for both contributions received and made to assist entities in evaluating if those transactions are required to be accounted for as contributions under the scope of ASC 958, or as an exchange transaction subject to other guidance. For purposes of assessing potential contributions, examples of the transactions in question include contributions of cash and other assets, including promises to give, or reductions, settlements, or cancellation of liabilities. Examples of resource providers include a government agency, a foundation, a corporation, or other entity. However, the type of resource provider is not determinative of whether a transaction is reciprocal or nonreciprocal.

The ASU clarifies how an entity determines whether a resource provider is participating in an exchange transaction by evaluating whether the resource provider receives comparable value in return for the assets transferred, based on consideration of the following:

- The resource provider is not one and the same with the general public. That is, a benefit received by the public as a result of the assets transferred is not equivalent to comparable value received by the resource provider. Therefore, if the resource provider receives indirect value in exchange for the assets transferred or if the value received by the resource provider is incidental to the potential public benefit from using the assets transferred, the provider isn't considered to have received comparable value in return.
- Execution of the resource provider's mission or the positive sentiment from acting as a donor doesn't constitute comparable value received by the resource provider for purposes of determining whether the transfer of assets is a contribution or an exchange.

ASC 958-605-15-5A provides additional indicators:

EXCHANGE TRANSACTION INDICATOR	CONTRIBUTION INDICATOR
Expressed intent asserted by both the recipient and the resource provider is to exchange resources for goods or services that are of comparable value.	The recipient solicits assets from the resource provider without the intent of exchanging goods or services of comparable value.
Both the recipient and the resource provider agree on the amount of assets transferred in exchange for goods and services that are of commensurate value.	The resource provider has full discretion in determining the amount of the transferred assets.
The existence of contractual provisions for economic forfeiture beyond the amount of assets transferred by the resource provider to penalize the recipient for nonperformance.	The penalties assessed on the recipient for failure to comply with the terms of the agreement are limited to the delivery of assets or services already provided and the return of the unspent amount.

When a resource provider itself is not receiving comparable value for the resources provided, an entity must determine whether a transfer of assets represents a payment from a third-party payer on behalf of an existing exchange transaction between the recipient and an identified customer. If so, other guidance (for example, ASC 606) applies.

Determining Whether a Contribution is Conditional

The ASU requires an entity to determine whether a contribution is conditional based on whether an agreement includes a barrier that must be overcome and either a right of return of assets transferred or a right of release of a promisors' obligation to transfer assets. If the agreement (or referenced document) includes both, the recipient is not entitled to the transferred assets (or future transfer of assets) until it has overcome the barriers in the agreement.

ASC 958-605-25-5D provides a list of indicators to consider in determining whether an agreement contains a barrier. The indicators include:

- The inclusion of a measurable performance-related barrier or other measurable barrier.
- The extent to which a stipulation limits discretion by the recipient on the conduct of an activity.
- Whether a stipulation is related to the purpose of the agreement.

After a contribution has been deemed unconditional, an entity is required to consider whether the contribution is restricted on the basis of the existing definition of the term "donor-imposed restriction," which includes a consideration of how broad or narrow the purpose of the agreement is, and whether the resources are available for use only after a specified date.

Simultaneous Release Option

The ASU provides a not-for-profit entity with the ability to elect a policy to report donor-restricted contributions whose restrictions are met in the same reporting period as the revenue is recognized as support within net assets without donor restrictions so long as the entity has a similar policy for reporting investment gains and income, reports consistently from period to period, and discloses its accounting policy. An entity electing this policy for donor-restricted contributions that were initially conditional contributions (where the condition has been met) may do so without also having to elect it for other donor-restricted contributions or investment gains and income provided that the entity reports consistently from period to period and discloses its accounting policy.

Implementation Guidance and Illustrations

The ASU includes implementation guidance and practical illustrations of the amendments. Refer to Appendix 1 for a diagram illustrating the framework for classifying transfers of assets.

EFFECTIVE DATES AND TRANSITION

Public entities are required to apply the amendments on contributions received to annual periods beginning after June 15, 2018, including interim periods within those annual periods. All other entities are required to apply the amendments on contributions received to annual periods beginning after December 15, 2018, and interim periods within annual periods beginning after December 15, 2019.

Public entities[4] are required to apply the amendments on contributions made to annual periods beginning after December 15, 2018, including interim periods within those annual periods. All other entities are required to apply the amendments on contributions made to annual periods beginning after December 15, 2019, and interim periods within annual periods beginning after December 15, 2020.

Early adoption of the amendments is permitted.

The guidance many be applied either through a modified prospective or a full retrospective approach.

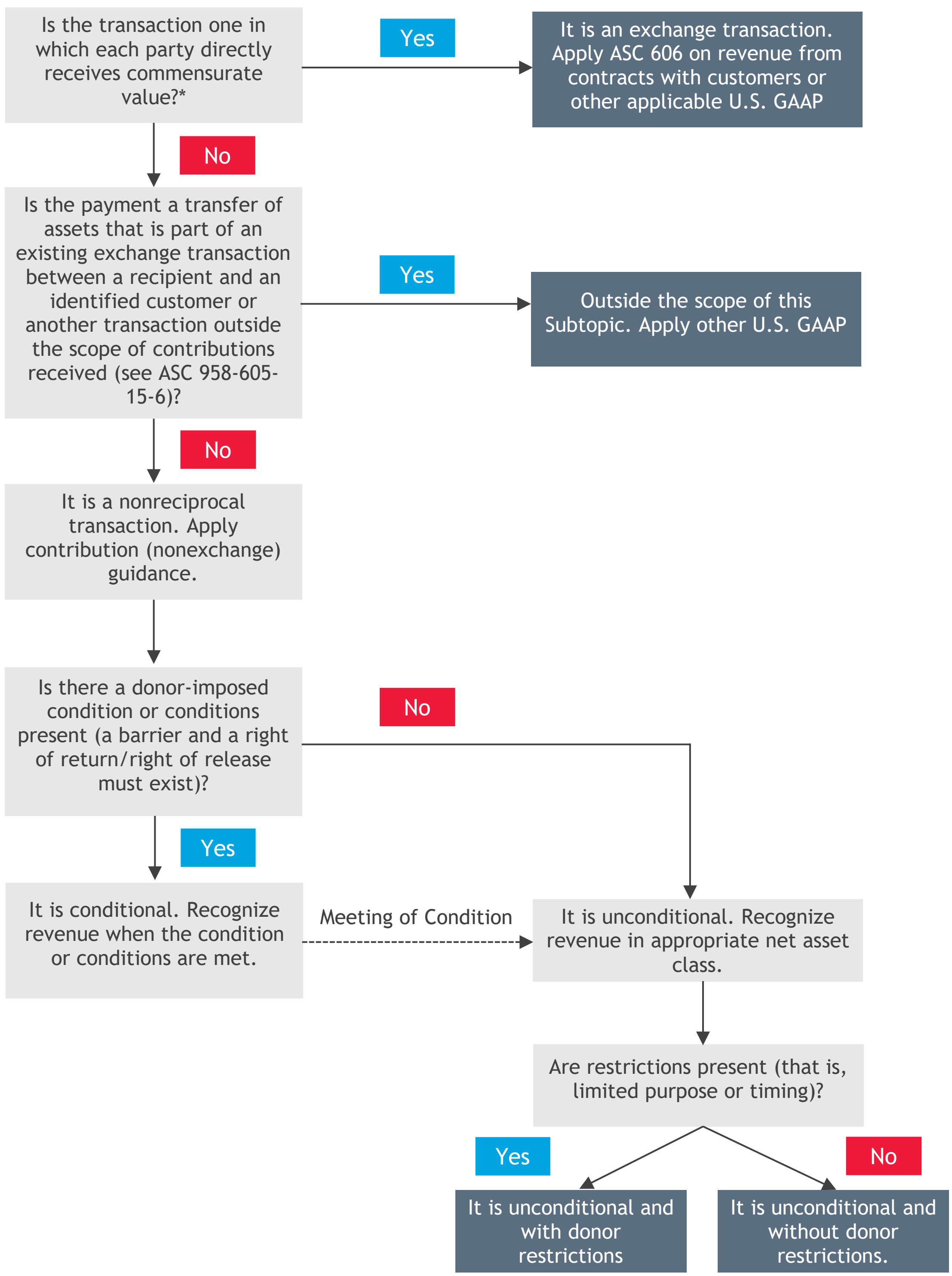
Under the modified prospective approach, the amendments are required to be applied to agreements that are not completed as of the effective date and to all agreements entered into after the effective date. Additional clarifying transition guidance is provided for this approach.

[4] Defined for purposes of this ASU as a public business entity or an NFP that has issued, or is a conduit bond obligor for, securities that are traded, listed, or quoted on an exchange or an over-the-counter market and serves as a resource recipient.

APPENDIX 1

Framework for Classifying Transfers of Assets

The following diagram excerpted from ASC 958-605-55-1A illustrates the process for determining whether a transfer of assets to a recipient is a contribution, an exchange transaction, or another type of transaction and whether a contribution is conditional. The diagram also illustrates whether a contribution includes an associated donor restriction.



*See paragraph 985-605-55-6 for guidance and transactions that are in part an exchange and in part a contribution