

# Not-for-Profit Audit Guide Update

What Nonprofits Should Know



**CliftonLarsonAllen**

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# About CliftonLarsonAllen

- A national CPA and consulting firm
- Service areas include audit, tax, consulting, and outsourcing
- 3,600+ professionals
- More than 90 offices nationwide
- Nonprofit group serves 6,000 clients across the country



# Speaker Introduction



## Cathy Clarke, CPA

Cathy is an audit and assurance partner at CliftonLarsonAllen with over 20 years of professional experience. Her focus has been working with nonprofit and healthcare organizations, primarily as a technical resource for the practice as well as quality reviewer for assurance and accounting engagements. She is the co-chair of the AICPA Not for Profit Entities Expert Panel and Guide Task Force.

# Agenda

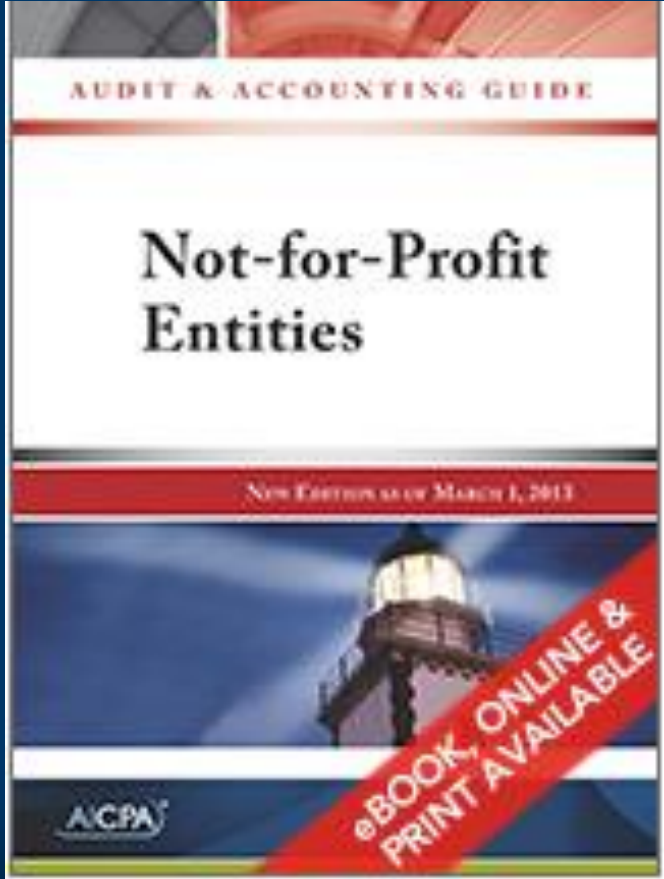
- AICPA's New Overhauled NFP A&A Guide

# Learning Objectives

- AICPA's Not-For-Profit Guide Overhaul project
  - ◇ Understand more about the 2013 Audit and Accounting Guide for Not-for-Profits
  - ◇ Better understand new and existing rules for exempt organizations
  - ◇ Model best practices and tips to assist with accurate reporting

# Polling Question





# Focus of the NFP Guide

- Not-for-profit entities
- GAAP-basis financial statements
- Audited financial statements

# Issuance of Overhauled 2013 Guide

- The AICPA has issued a comprehensive revision of the Audit and Accounting Guide Not-for-Profit Entities in the spring of 2013
  - Financial Reporting Executive Committee (FinREC)
  - Not-for-Profit Entities Expert Panel
  - Not-for-Profit Guide Task Force
- First revision, other than annual conforming changes, since the Guide was released in 1996

# Source of New Guide Content

- Considered over 100 questions that had been asked by members who called the AICPA Help Line
- Authoritative guidance from FASB Codification
- Non-authoritative guidance from FinREC conclusions
- Incorporated relevant nonauthoritative AICPA literature
  - NFP-related Technical Questions and Answers (TIS) section 6140
  - AICPA White Paper on Fair Value Measurement
  - Alternative investments TIS section 2220.18–.27

# Authoritative Status of AICPA Guides

- Accounting & Financial Reporting
  - Basis of accounting content is from GAAP, but Guides provide additional explanation and practical guidance
- Auditing
  - Auditing guidance considered interpretive publication under AU-C section 200, Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with Generally Accepted Auditing Standards
  - “The auditor should consider applicable interpretive publications in planning and performing the audit.” AU-C 200.27

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- Chapter 1 – Introduction
- Chapter 2 – General auditing considerations
- Chapter 3 – Financial statements, the reporting entity, and general financial reporting matters
- Chapter 4 – Cash, cash equivalents, and investments
- Chapter 5 – Contributions received and agency transactions
- Chapter 6 – Split-interest agreements and beneficial interests in trusts
- Chapter 7 – Other assets
- Chapter 8 – Programmatic investments
- Chapter 9 – Property and equipment
- Chapter 10 – Debt and other liabilities
- Chapter 11- Net assets and reclassifications of net assets
- Chapter 12 – Revenues and receivables from exchange transactions
- Chapter 13 – Expenses, gains, and losses
- Chapter 14 – Reports of independent auditors
- Chapter 15 – Tax and regulatory considerations
- Chapter 16 – Fund accounting
- Appendices

## Chapter 2, General Auditing Guidance

- Conformed to the Clarity project; includes NFP-specific guidance (e.g. fraud risks specific to NFPs)
- Other guide chapters have NFP-specific suggested audit procedures relating to the chapter's topic

# Polling Question



# Chapter 3, Financial Statements, the Reporting Entity, and General Financial Reporting Matters

- Significantly expanded guidance on interests in related entities
  - Summary chart of examples that reference to sections of both the Guide and the FASB ASC
    - ◇ NFP entities
    - ◇ For-profit entities
    - ◇ Special-purpose leasing entities

## Excerpt from Exhibit 3-2

Relationship	Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Reference	Discussion in This Chapter
The reporting entity controls another NFP through a majority voting interest in its board and has an economic interest in that other entity.	Use the guidance in FASB ASC 958-810-25-3.	<a href="#">Paragraphs 3.67–.69</a>
The reporting entity controls an NFP through a form other than majority ownership, sole corporate membership, or majority voting interest in the board of the other entity and has an economic interest in that other entity.	Use the guidance in FASB ASC 958-810-25-4.	<a href="#">Paragraph 3.70</a>
The reporting entity has control over another NFP or an economic interest in the other, but not both.	Use the guidance in FASB ASC 958-810-25-5.	<a href="#">Paragraph 3.71</a>

# Chapter 3, continued

- Statement of functional expenses
  - Required as a basic financial statement for voluntary health and welfare entities
  - FinREC encourages presentation by all NFPs that are supported by the general public
    - ◇ NFP with contributions of 20-30% of total revenue presumed to be supported by general public (excluding gov't support)
    - ◇ Consider facts & circumstances and use judgment

# Chapter 4, Cash, Cash Equivalents, and Investments

- Significantly expanded guidance on common investments by NFPs
  - Summary chart of examples that reference to sections of both the Guide and the FASB ASC

## Excerpt from Exhibit 4-1

Relationship	Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Reference	Discussion in This Chapter
<b>Relationships With Entities Held for Investment</b>		
<p>The reporting entity owns 50 percent or less of the common voting stock of an investee and the reporting entity neither controls nor can exercise significant influence over the investee's operating and financial policies. The stock is an equity security that has a readily determinable fair value.</p>	<p>FASB ASC 958-320-35-1</p>	<p><a href="#">Paragraph 4.17</a></p>
<p>The reporting entity owns 50 percent or less of the common voting stock of an investee and the reporting entity neither controls nor can exercise significant influence over the investee's operating and financial policies. The stock does not have a readily determinable fair value.</p>	<p>FASB ASC 958-325-35</p>	<p><a href="#">Paragraph 4.37</a></p>

# Chapter 5, Contributions Received and Agency Transactions

- Receipt of resources by a NFP ---  
a contribution or an exchange transaction?
  - Flowchart (Table 5-1)
  - When elements of both are present, divide the transaction in two, measuring exchange first
- Examples
  - Membership dues
  - Grants

# Chapter 5, continued

- Membership Dues

- Is the value received by the member commensurate with the dues paid?
- Often elements of both contribution and exchange
  - ◇ Measure exchange portion first and recognize as revenue as the earnings process is completed
  - ◇ Remainder is contribution, recognize as revenue upon receipt
- Example – aquarium offers varying levels of membership; each level receives annual admission; varying other benefits depending on the level

# Chapter 5, continued

- Grants
  - Use Table 5-1 to determine if grant is contribution or exchange based on the facts and circumstances
  - If contribution - consider if any conditions exist, consider donor restrictions
  - If exchange – determine revenue recognition
  - NFP should establish accounting policy for grants so they are accounted for consistently
  - Government grants
    - ◇ Apply the above guidance
    - ◇ FASB Not-for-Profit Advisory Committee topic



# Chapter 5, continued

- Recognition and Measurement of Contributions
  - Contributed fundraising material, informational material, or advertising, including media time or space
  - Below-market interest rate loans
  - Administrative costs of restricted contributions

# Chapter 5, continued

- Contributed Fundraising Material, Info Material, or Advertising, Including Media Time or Space
  - Examples –public service announcements, radio advertising time, newspaper print space
  - Donated asset, not a donated service –
    - ◇ Record contribution even if the asset would not typically needed to be purchased if not provided by donation
  - FinREC recommends: Recognize a contribution if NFP has active involvement in determining and managing the message and use of the materials; otherwise not a contribution

# Chapter 5, continued

- Below-Market Interest Rate Loans
  - No or low-interest loan of funds is a contribution to the NFP
  - Record contribution revenue and interest expense for fair value of the contribution
    - ◇ Fair value typically estimated at difference between market rate interest and actual interest
  - Related party status doesn't impact recording
  - Recognition of contribution/interest different for long-term loan vs. due-on-demand loan

# Chapter 5, continued

- Example 1 – Long-term loan from a foundation
  - On 1/1/2013 NFP receives 0% interest loan of \$200,000 payable 12/31/2015
  - Market interest rate is 6%

# Chapter 5, continued

## Record receipt of loan -

1/1/2013	DR Cash	\$200,000
	CR Loan payable *	(167,924)
	CR Contribution revenue **	(32,076)

*\* calculated at PV of \$200K at 6% over 3 years*

*\*\* donor restricted, release over term of loan*

## Record annual interest (similar entries also booked at 12/31/2014 and 12/31/2015)

12/31/2013	DR Interest expense	\$10,075
	CR Loan payable	(10,075)

## Record repayment of loan

12/31/2015	DR Loan payable	\$200,000
	CR Cash	(200,000)

## Chapter 5, continued

- Example 2 – Due on demand loan from a foundation
  - On 1/1/2013 NFP receives 0% interest loan of \$200,000, due on demand, repaid 12/31/2015
  - Market interest rate is 6%

# Chapter 5, continued

## Record receipt of loan -

1/1/2013	DR Cash	\$200,000
	CR Loan payable	(200,000)

## Record annual interest and contribution (same entry also booked at 12/31/2014 and 12/31/2015)

12/31/2013	DR Interest expense	\$12,000
	CR Contribution Revenue	(12,000)

## Record repayment of loan

12/31/2015	DR Loan payable	\$200,000
	CR Cash	(200,000)

# Chapter 5, continued

- Loans - Other issues
  - Gov't loans at below-market interest rates
    - ◇ First consider whether loan has contributory intent (contribution vs. exchange transaction)
    - ◇ Reference FASB ASC 835-20-15-3 by analogy (imputing interest) – the following type of loans are exempt from interest imputation rules:
      - Transactions where interest rates are affected by the tax attributes or legal restrictions prescribed by a governmental agency (for example, industrial revenue bonds, tax exempt obligations, government guaranteed obligations, income tax settlements)



# Chapter 5, continued

- Loans - Other issues
  - Forgivable loans
    - ◇ Determine if there is contributory intent
    - ◇ Determine if conditions on the contribution exist
    - ◇ Is forgiveness automatic, is it dependent on lender's action, or is it dependent on borrower's actions?
- \*\*See Chapter 8 for corresponding accounting by the lender for making this contribution

# Chapter 5, continued

- Administrative Costs of Restricted Contributions
  - Policy of designated a certain % of restricted gifts to offset the costs of raising and administering those gifts
    - ◇ Example – Policy that 5% of contributions to scholarship fund go to pay administrative costs; so \$95 of a \$100 gift is restricted for the scholarship fund
  - Policy needs to be effectively communicated to or from the donor prior to receipt of the contribution
    - ◇ If not, then 100% of gift should be donor restricted

# Polling Question

# Chapter 6, Split Interest Agreements and Beneficial Interests in Trust

- Beneficial interest in a trust held by another entity – Questions:
  - What if NFP isn't notified about trust until years after it is created?
  - What if NFP is unable to obtain information to verify it is named as an irrevocable beneficiary?
  - What if NFP is unable to obtain information to measure the beneficial interest?

# Chapter 6, Split Interest Agreements and Beneficial Interests in Trust

- Answers:
  - NFP generally needs the following information in order to record beneficial interest in the trust:
    - ◇ Copy of executed trust document, statement from the trustee, or other information to verify existence
    - ◇ Sufficient information about the trust in order to value it (e.g. trust assets, payout rate/amount, age of life beneficiaries)
  - Make reasonable efforts to obtain necessary information

# Chapter 6, Split Interest Agreements and Beneficial Interests in Trust

- Answers, continued:
  - Recognize beneficial interest in the trust and contribution revenue in the first year the necessary information becomes available.
  - Should not record a prior period adjustment if the NFP made, and continues to make, reasonable efforts to obtain necessary information

# Chapter 8, Programmatic Investments (NEW)

- Programmatic investments are any investment by an NFP that meets the following two criteria:
  - Its primary purpose is to further the tax exempt objectives of the NFP.
  - The production of income or the appreciation of the asset is not a significant purpose (that is, an investor seeking a market return would not enter into the investment).
- Similar to program-related investment, IRS Sec. 4944(c).

# Chapter 8, continued

- Specific examples discussed in the chapter:
  - Loans
    - ◇ Low or no interest loans
    - ◇ Forgivable loans
  - Guarantees
    - ◇ Guarantee provided without commensurate return
  - Equity investments
    - ◇ Often no contribution element



# Chapter 8, continued

- Core Considerations
  - Determine when the initial transaction occurs whether the investment is programmatic
  - If there is a contribution element, report it as contribution expense
  - Use GAAP for similar financial instruments, except for the contribution element, if any
  - Significance of the investments and the quantitative and qualitative risks determine the type of financial statement presentation and the extent of disclosures

# Chapter 10, Debt and Other Liabilities

- New section on tax-exempt (municipal bond) debt based on the AICPA Audit and Accounting Guide Health Care Entities
- Expanded discussion of credit enhancements, debt extinguishments, debt modifications, and classification

# Chapter 11, Net Assets and Reclassifications of Net Assets

- Significantly expanded guidance on expiration of restrictions
  - Using restricted contributions first
  - Promises to give, including implied time restriction on multi-year pledges
  - Gifts of long-lived assets or gifts for their purchase
  - Donor restricted endowment funds
  - Restrictions met in the same year as the contribution was received

# Chapter 11, continued

- Expiration of restrictions on promises to give
  - By specifying future payment dates donors indicate that their gift is to support activities in each period in which a payment is scheduled (i.e. an implied time restriction)
  - Time restrictions lapse when the receivable is due; gift becomes available for the donor-specified purpose
  - If gift is for the construction or purchase of a specific long-lived asset, the donor supports activities of the period in which that asset is constructed or placed in service, even though the payment dates extend beyond that period

# Polling Question

# Chapter 15, Tax and Regulatory Considerations

- Greatly expanded discussion about legal and regulatory environment
  - Maintaining the NFP's tax-exempt status
  - Unrelated business income and income tax positions
  - State and local regulations issues (state charitable solicitation laws, state and local gaming regulations, UPMIFA)

# Issues referred to FASB in Guide Revision

Issue	Question	FASB Action Taken
Reporting the Contribution Portion of Charitable Gift Annuities	Should state law requirements regarding required levels of annuity reserves impact the net asset classification?	Net Asset Classification being address in NAC Financial Report, Financial Statements Project
Reporting Investment Expenses	How should investment expenses be presented and disclosed?	Reporting Investment Expenses being address in NAC Financial Report, Financial Statements Project
Recognition of Beneficial Interest in Trusts Held by Others when Information to Measure is Unavailable	How should an entity report a BIT when fair value information is not readily available?	Added to list of technical corrections to codification

# Issues referred to FASB in Guide Revision

Issue	Question	FASB Action Taken
Subsequent Measurement of Other Investments	Should ASC 958-325-35 be updated to be consistent for all NFP's?	Added to FASB's Accounting for Financial Instruments Project
Statement of Functional Expense	Should the statement be required by more donor supported organization?	Added to NAC's Financial Reporting, Financial Statements Project
Classification in Cash Flow Statement of Gifts of Securities Immediately Sold	If donated securities are immediately converted to cash, where should proceeds be classified?	ASU 2012-5 "Not-for-Profit Entities: Classification of the Sale of Donated Securities in the Statement of Cash Flows"
Employee Services Contributed by an Affiliate	Should definition of contributed service ASC 958-605-25-17 be expanded so it is more consistently applied?	ASU 2013-6, "Not-for-Profit Entities: Personnel Services Received from an Affiliate for Which the Affiliate Does Not Seek Compensation."





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