



**NONPROFIT SEMINAR:
2018 ACCOUNTING STANDARD CHANGES**

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SMITH•SCHAFER
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Certified Public Accountants and Consultants

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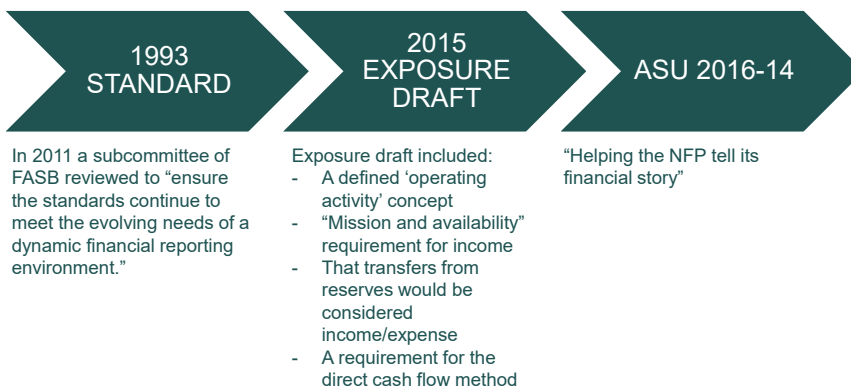
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BACKGROUND



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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

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

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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.

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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.

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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
	<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).

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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

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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)
- The relationship between functional classification and natural classifications for all expenses shall be presented in an analysis that disaggregates functional expense classifications, such as **major classes of program services and supporting activities** by their natural expense classifications such as salaries, rent, etc.
- 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

SAMPLE CLIENT

STATEMENTS OF FUNCTIONAL EXPENSES

For the Year Ended September 30, 2017

	Program Services			Supporting Services			Totals
	Program One	Program Two	Program Total	Management and General	Development	Total	2017
Salaries and wages	\$ 159,474	\$ 60,399	\$ 210,873	\$ 65,559	\$ 61,874	\$ 127,433	\$ 338,306
Employee benefits	12,989	5,196	18,185	5,484	5,196	10,680	28,865
Payroll taxes	9,622	3,849	13,471	4,063	3,849	7,912	21,383
Total Salaries and Benefits	173,085	69,444	242,529	75,106	70,919	146,025	388,554
Subsistence	87,225	10,152	97,377	17,623	3,790	21,413	118,790
Stipends	90,402	-	90,402	-	-	-	90,402
Transportation	30,115	12,068	42,183	11,222	2,346	13,568	55,751
Office facilities	-	15,166	15,166	15,166	15,166	30,332	45,498
Bank and investment fees	15,074	6,029	21,103	6,365	6,029	12,394	33,497
Printing, publicity and conferences	22,253	1,767	24,020	916	1,511	2,427	26,447
Executive director search	6,727	2,690	9,417	2,840	2,690	5,530	14,947
Consulting	5,980	2,392	8,372	2,524	2,392	4,916	13,288
Equipment and maintenance	3,955	-	3,955	6,757	1,334	8,091	12,046
Accounting services	3,983	1,593	5,576	1,691	1,593	3,274	8,850
Insurance	442	2,638	3,080	2,638	2,638	5,276	8,356
Postage and shipping	2,035	1,733	3,768	845	3,625	4,470	8,238
Interest expense	3,649	1,459	5,108	1,541	1,459	3,000	8,108
Hospitality	6,513	-	6,513	403	875	1,278	7,791
Student life	7,757	-	7,757	-	-	-	7,757
Office supplies and expense	1,869	93	1,962	2,606	1,776	4,381	6,343
Taxes and fees	2,303	921	3,224	973	921	1,894	5,118
Telephone	277	1,203	1,480	1,873	1,031	2,904	4,384
Depreciation	-	-	-	731	-	731	731
Dues, membership, subscriptions	-	120	120	566	-	566	686
TOTAL FUNCTIONAL EXPENSES	\$ 463,644	\$ 129,468	\$ 593,112	\$ 152,375	\$ 120,095	\$ 272,470	\$ 865,582

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
- 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)

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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

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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

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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

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CAPITAL GIFTS

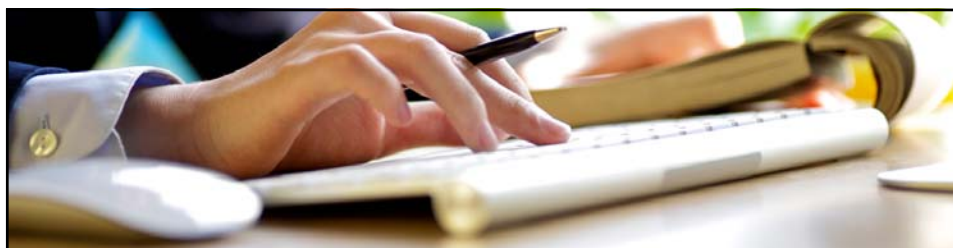
Capital gifts (building, equipment, construction costs) are recognized when the asset is placed in service, unless donor stipulations limits the use of the asset for a period of time. Must adopt the placed in service approach if you have been using the over-time approach.

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 implementation 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

FUTURE STANDARDS

- Revenue Recognition – Periods beginning after December 15, 2018
 - New Five Step Process to Revenue Recognition
 - Step 1: Identify the contract(s) with a customer.
 - Step 2: Identify the performance obligations in the contract
 - Step 3: Determine the transaction price
 - Step 4: Allocate the transaction price to the performance obligations in the contract
 - Step 5: Recognize revenue when (or as) the entity satisfies a performance obligation
- Leases – Periods beginning after December 15, 2019

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#. Liquidity and Availability

Financial assets as of December 31, 2018, available for general expenditure within one year of the statement of financial position date, were comprised of the following:

	Amounts
Cash and cash equivalents	\$ 50,697
Investments held by others	25,796
Grants receivable	65,498
Accounts receivable	5,000
	<hr/>
Total	<u><u>\$ 146,991</u></u>

Financial assets are considered available for general expenditure if there are no restrictions limiting their use.

The Organization's board designated funds are subject to board approval prior to being available to use within the next year. Although the board does not currently intend to spend from the board designated funds, these amounts could be made available if necessary.

As part of the Organization's liquidity management plan, cash in excess of short-term needs is invested in savings and money market funds.

#. Liquidity and Availability

The following reflects the Organization's financial assets as of December 31, 2017, reduced by amounts not available for general use within one year of the statement of financial position date because of contractual, donor-imposed or board-imposed restrictions. Balances not available include amounts set aside by the board that could be drawn upon with board approval.

Financial assets, end of year	\$ 869,436
Less those unavailable for general expenditures within one year due to:	
Restriction by donor for purpose	(350,000)
Restriction by the board	(300,000)
Restriction due to time	<hr/> -
Financial assets available to meet cash needs for general expenditures within one year	<u><u>\$ 219,436</u></u>

As part of the Organization's liquidity management plan, financial assets are structured to be available as its general expenditures, liabilities and other obligations come due. The Organization's board designated funds may be drawn upon in the event of financial distress or an immediate liquidity need resulting from events outside of typical operations. Additionally, as further described in Note #, the Organization has a line of credit agreement with its bank in the amount of \$50,000, which the Organization could draw upon in the event of an unanticipated liquidity need.

#. Liquidity and Availability

The Organization is substantially supported by restricted contributions. Because donor restrictions require resources to be used in a particular manner or in a future period, the Organization must maintain sufficient resources to meet those responsibilities to its donors. Thus, financial assets may not be available for general expenditures with one year. As part of the Organization's liquidity management plan, the Organization structures its financial assets to be available as its general expenditures, liabilities and other obligations come due. In addition, the Organization 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 \$25,000 as of December 31, 2018. These funds 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. The Organization has \$400,000 of financial assets available within one year of the statement of financial position date to meet cash needs for general expenditure consisting of cash of \$100,000, grants receivable of \$250,000 and investments of \$50,000.

Selected additional options:

The Organization has a goal to maintain financial assets, consisting of cash and short-term investments, on hand to meet 60 days of normal operating expenses, which are, on average approximately \$275,000.

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 statement of financial position date.

When considering which assets are available to meet current needs, the availability of our assets and the financial flexibility of our Organization would be underestimated without including certain assets with donor restrictions in the total available as of December 31, 2018. Financial assets available and estimated to be released for program activities within one year of the statement of financial position were \$125,000.

In addition to the assets available listed above, the Organization considers financial assets with donor restrictions that are intended to cover the day to day expenses related to certain programs to be available for use in the current period. While technically donor restricted, \$75,000 of financial assets are included in our regular cash flow planning. The donor-imposed restrictions for these program related assets are satisfied as a matter of course in our daily program operations.