NOT FOR PROFIT REVENUE RECOGNITION & LEASES

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Smith Schafer & Associates is an award-winning accounting and business consulting firm offering proactive services, deep expertise, innovative solutions and personal relationships.

We are local to Minnesota with offices in:

- Minneapolis
- Rochester
- Red Wing

ADAM J. KELLERHALS, CPA

- ***SENIOR AUDIT MANAGER***
- ***Expertise***
  - Audit & Attest Services
  - Financial Statement Presentation
  - Business Consultation
- ***Background***
  - Bachelor of Arts degree in Accounting and Management from Luther College.
  - Joined the Twin Cities practice in June 2007.
- ***Member***
  - AICPA & MNCPA
  - Nonprofit Financial Group - Twin Cities
  - Minnesota Construction Association

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TODAY'S AGENDA

- Revenue Recognition – General
- Revenue Recognition – Contributions
- Leases
- Q & A
- Wrap-up

TERMINOLOGY

- Accounting Standards Update (ASU) – Issued by the Financial Accounting Standards Board (FASB) to revise the Accounting Standard Codification (ASC) which is Generally Accepted Accounting Principals (GAAP).

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ASU 2014-09 REVENUE RECOGNITION

- Removed virtually all current GAAP related to revenue recognition
- Introduced a new <u>five step</u> approach to recognize revenue
- Created new terminology
- Effective for years beginning after December 15, 2018

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ASU 2014-09 REVENUE RECOGNITION

If you have the following accounts on your statement of financial position, you may be affected by revenue recognition:

- Deferred revenue
- Prepaid membership
- Customer deposits
- Or you should have any of these or similar accounts

Do you offer any of these services?

- Discounts on programing when you become a member or a donor
- Multiple Services/goods throughout a single transaction

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FIVE STEP PROCESS

Step 1
- Identify the Contract 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

REVENUE RECOGNITION EXAMPLE

Trade Association charges $1,000 for an annual membership. Member's dues renew on their anniversary date (their original date of joining the Association). Membership includes a quarterly publication, monthly emails related to the industry, access to exclusive content on their website, and a 10% discount to the annual conference.

The Association's quarterly publication discusses and highlights research, issues, and trends of interest to its members and others in the industry. The Association also sells the quarterly publications to non-members for $150 per issue.

The standard cost of the conference is $250 and, based on historical trends, the Association expects 40% of the members to take advantage of the 10% discount and attend the conference. The conference is in October every year.

A new member has joined the Association and paid their $1,000 in dues on June 1, 2019.

Step 1

- Identify the Contract with a Customer

Trade Association is providing members with membership benefits

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Step 2

- Identify the Performance Obligations in the Contract

What is the total number of Performance Obligations?

Six

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Step 3

• Determine the Transaction Price

$1,000

Having discounts on membership, early bird registration for the conference, different membership levels all can make the transaction price more complicated

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Step 4

- Allocate the Transaction Price to the Performance Obligations in the Contract

	Member Fee	Standalone	Allocation
Quarterly Publication		$ 150	
Quarterly Publication		150	
Quarterly Publication		150	
Quarterly Publication		150	
Membership benefits *		500	
Discount to conferences		10	
	$ 1,000	$ 1,110	$ 1,000

* The Association does not sell membership separately without including the quarterly publications. The Association should estimate the standalone selling price because there is no directly observable selling price.

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Step 4

- Allocate the Transaction Price to the Performance Obligations in the Contract

The discount on conference registration is a separate performance obligation and is valued below:

Conference registration	$	250		
Discount		10%		
Anticipated discount			$	25
Likelihood of use				40%
Standalone price of discount			$	10

Step 4

- Allocate the Transaction Price to the Performance Obligations in the Contract

	Member Fee	Standalone	Allocation
Quarterly Publication		$ 150	$ 135
Quarterly Publication		150	135
Quarterly Publication		150	135
Quarterly Publication		150	135
Membership benefits		500	450
Discount to conferences		10	10
	$ 1,000	$ 1,110	$ 1,000

Step 5

- Recognize Revenue When (or as) the Entity Satisfies a Performance Obligation

New member Joins	Cash	1,000	
	Contract liability		1,000
Quarterly publication delivered to member	Contract liability	135	
	Membership revenue		135
Monthly membership benefit	Contract liability	37.50	
	Membership revenue		37.50

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Step 5

- Recognize Revenue When (or as) the Entity Satisfies a Performance Obligation

Member registers for Conference

Cash	225	
Contract liability	10	
Membership revenue		10
Conference revenue		225

This all goes away if your membership year and your fiscal year are the same.

A 501(c)3 who has 'dues' may have to bifurcate the dues and the contribution.

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PRESENTATION

- Contract Asset or Liability
- Transition
- Disclosures

FUTURE STEPS

1. Do you have these and how will you treat them:
   – Multiple performance obligations
   – Distinct goods and services
2. Document your five steps.

ASU 2018-08 CONTRIBUTIONS

- Assist in evaluating if transactions are contributions or exchanges
- Determine if a contribution is conditional
- Effects timing of when revenue will be recognized
- Effective for years beginning after December 15, 2018

ASU 2018-08 CONTRIBUTIONS

Reciprocal (Exchange) → ASU 2014-09 ASC 606 → Sales transaction

Nonreciprocal (Nonexchange) → ASU 2018-08 ASC 958 → Contribution

ASU 2018-08 CONTRIBUTIONS

Reciprocal
vs
Nonreciprocal

Conditional
vs
Unconditional

With vs
Without
Donor
Restriction

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ASU 2018-08 CONDITION

For a donor imposed condition to exist:

A right of return of funds or release of future payments MUST exist

A barrier MUST be included

If the gift is deemed conditional – it is not revenue until the condition is met.

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ASU 2018-08 BARRIERS

- Measureable Performance
  - Provide 1,000 meals
  - If you raise $1,000 I will contribute $1,000
- Limited Discretion by the Recipient
  - Guidelines about qualifying expenses
  - Specified workforce
- Excludes administrative or trivial tasks

PRESENTATION

- Disclosures
  - Conditional gifts – no new disclosure
- Transition
  - Only need to look forward

FUTURE STEPS

1. Review contracts and grants for rights of return
2. Review grants with rights of return for barriers

ASU 2016-02 LEASES

- New presentation and disclosure requirements.
- Lease expense (rent expense) is recognized in a similar matter as today.
- Effective for years beginning after December 15, ~~2019.~~
  2020

LEASE TYPES

- Finance Lease
- Short Term Lease
- Operating Lease

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PRESENTATION – STATEMENT OF FINANCIAL POSITION

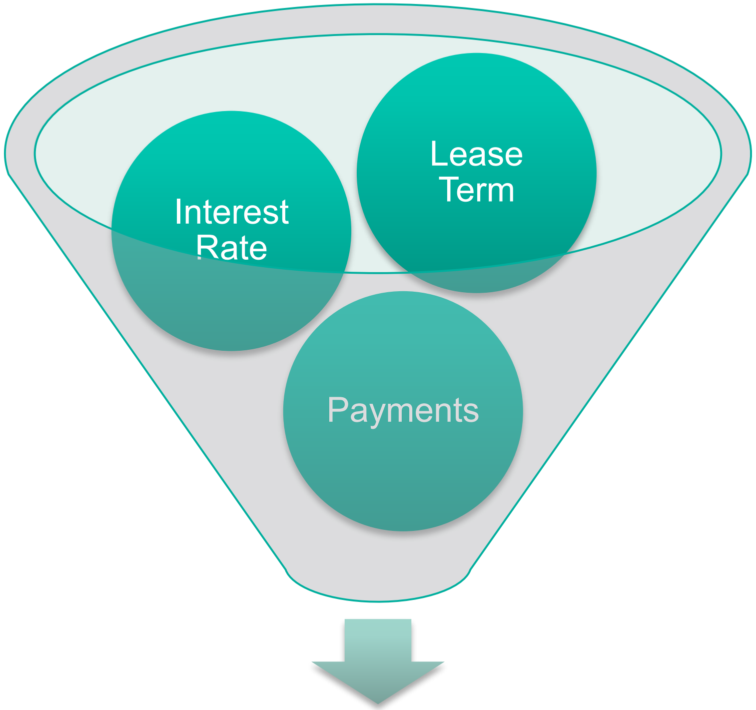
Finance Lease	Operating Lease	Short Term Lease
• Right of use asset • Lease liability	• Right of use asset • Lease Liability	• Not Applicable*

PRESENTATION – STATEMENT OF ACTIVITIES

Finance Lease	Operating Lease	Short Term Lease
• Amortization Expense • Interest Expense	• Rent Expense	• Rent Expense

EMBEDDED LEASE

CALCULATION INPUTS



Right of Use Asset (ROU)

REAL ESTATE TAXES AND CAM

- Net Lease
  - Variable lease payment that is not dependent on an index or rate of change and excluded from ROU calculation
- Gross Lease
  - Standalone cost of the CAM is excluded in ROU calculation or use the practical expedient to include

Real estate taxes and insurance will not receive an allocation of the lease payment

INTEREST RATE OPTIONS

- Rate implicit in the lease:
  - To determine the lessee must know the lessor's:
    - Initial cost of the asset
    - Upfront costs
    - Residual value of the asset
  - Example
    - A lessor pays a total of $60,000 for an asset with a five-year life and agrees to lease the asset $1,200 a month for five years. The implicit rate is 7.42%

INTEREST RATE OPTIONS

- Incremental borrowing rate:
  - The rate of interest that a lessee would have to pay to borrow on a collateralized basis over a similar term an amount equal to the lease payments in a similar economic environment.
- Risk free rate:
  - Must be for the same term as the lease

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TRANSITION

- Adjust the earliest period presented (including retained earnings)
- Adjust only the year of adoption – however – more disclosure is required

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FUTURE STEPS

1. Find leases and service contracts.
2. Lease capitalization policy.

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Q & A

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October 17 – Tax & Retirement Planning Tips – Golden Valley, MN

December 3 – Business Tax – Rochester, MN

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