

2016 Nonprofit Accounting Updates



About DZH Phillips

- Specialize in assurance, tax, forensics, and outsourced accounting for nonprofit organizations
- 28th Largest Women-Owned Business in the San Francisco Bay Area
- Top 15 largest accounting firms in the San Francisco Bay Area
- Top 200 accounting firm in the nation



Hydeh Ghaffari, Partner

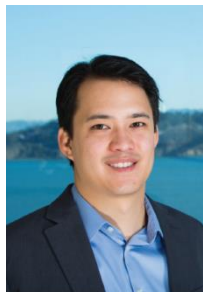


Hydeh Ghaffari brings more than 30 years of experience as a financial manager and 25 years as a Certified Public Accountant to DZH Phillips. She offers services in financial management, including audits, reviews, and compilation of financial statements. With 22 years of experience with client accounting for nonprofit organizations, Hydeh specializes in grant management and understands the specific needs that come with an outsourced CFO or Controller. Hydeh also excels in accountancy education, frequently speaking at nonprofit conferences and facilitating auditing workshops locally and nationally for nonprofit organizations and nonprofit funding organizations, including governmental agencies and their board members and staff. She also offers consultations regarding assessment of accounting functions, including staffing, software, and internal controls; agency and funding source budgeting; cash flow projection; single audits; and indirect cost proposals.

Hydeh holds an MBA from Golden Gate University and a bachelor's degree in accounting from University of Tehran, Iran. She has taught at the University of San Francisco as an adjunct faculty member. Hydeh has been a regular speaker at AICPA National Nonprofit Conference for the past several years, and is a member of CalCPA and the AICPA. She is the former co-chair of the California Nonprofit Conference and is on the planning committee of the AICPA National Nonprofit Conference, and past President of the board of directors of Tenderloin Neighborhood Development Corporation.

Hydeh's mission is to provide quality service, establish a true partnership with clients, and assist them in building a stronger infrastructure so they can make informed decisions and accomplish their mission and objectives. Her ideal client is a mid-sized nonprofit looking to grow with their accountant. Outside of the office, Hydeh likes to stay active, enjoying running, biking, swimming, skiing, traveling, playing tennis and golf, and shopping with her girls.

Kevin O'Connell, Audit Manager



Kevin specializes in audit and compliance services for commercial enterprises and nonprofit organizations, with additional expertise in forensic accounting. He has sharp organizational skills, a wide range of technical research experience and in-depth knowledge of GAAP accounting.

Kevin attained his Bachelor of Science degree in business administration with a concentration in accounting at California Polytechnic State University, San Luis Obispo. He maintains affiliations with the American Institute of Certified Public Accountants (AICPA), the California Society of Public Accountants (CalCPA) and the Association of Certified Fraud Examiners (ACFE).

Kevin believes that when an accounting team comes in to audit, they are not just putting the numbers together for clients, but are helping them with internal control systems and revenue recognition, as well as strengthening each member of the accounting team. He strives to manage a personable and friendly team and is dedicated to respecting and working collaboratively to help his clients succeed, since they know their businesses inside-out. Kevin works with a broad range of industries, and has a passion working specifically with consumer goods, technology, construction, and nonprofits involved with youth arts or athletics, independent schools and social service organizations.

While growing up, Kevin was highly involved in athletics and the arts. He recognizes the importance of these activities within today's education system and now serves as a board member of the San Francisco Arts Education Project. When not at work, Kevin enjoys volleyball, running, music and being an active member of the DZH Phillips soccer and basketball teams.

2016 Nonprofit Accounting Update



Topics Covered in This Nonprofit Accounting Update



- ✓ Revenue from contracts with customers
- ✓ Accounting for leases
- ✓ Changes to going concern considerations
- ✓ Statements on standards for accounting and review services – (SSARS 21)
- ✓ Single audit update.
- ✓ Proposed changes to accounting and reporting for nonprofit organizations

Revenue from Contracts with Customers

What?

FASB ASC 606 *Revenue from Contracts with Customers*

Why?

FASB wants to eliminate the need for industry specific guidance and take a principles-based approach for recognizing revenue.

When?

Annual reporting periods beginning after December 31, 2018.
Early adoption is permitted.

Revenue from Contracts with Customers

The following revenue streams are specifically exempt from ASC 606:

- Debt and equity securities
- Derivatives
- Financial instruments
- Guarantees
- Insurance contracts
- Leases
- Nonmonetary exchanges
- Transfer and servicing rights

Revenue from Contracts with Customers

What about contributions?

Although not specifically scoped out of ASC 606, we believe that the definition of contributions as being voluntary and nonreciprocal exempts contribution revenue from the new guidance.

Revenue from Contracts with Customers

The following revenue streams are likely to be subject to ASC 606:

- Government contracts
- Licensing
- Memberships
- Products and services
- Royalty agreements
- Sponsorships
- Subscriptions
- Tuition

Revenue from Contracts with Customers

An entity recognizes revenue in accordance with the core principle by applying the following steps:

- Step 1: Identify the contract(s) with a customer: A contract is an agreement between two or more parties that creates enforceable rights and obligations
- 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 from Contracts with Customers

Example – Quarterly Newsletters

NPO has dues of \$500 per year. Member benefits include the right to use facilities and quarterly newsletters with a fair value of \$25 per issue.

Step 1: Identify the contract

A contract exists between the NPO and member related to dues for the right to use facilities and the quarterly newsletters

Step 2: Identify the performance obligations

Obligation 1: Use of facilities

Obligation 2: Subscription to quarterly newsletter

Step 3: Determine the transaction price

The total transaction price is \$500 per year for membership which includes the right to use facilities and quarterly newsletters

Revenue from Contracts with Customers

Example – Quarterly Newsletters

NPO has dues of \$500 per year. Member benefits include the right to use facilities and quarterly newsletters with a fair value of \$25 per issue.

Step 4: Allocate the transaction price to the performance obligations in the contract

Since the NPO sells its quarterly newsletters for \$25 per issue for nonmembers, that would create a standalone selling price for the newsletter subscription.

\$100 would be allocated to the newsletters
\$400 would be allocated to the membership

Step 5: Recognize revenue when each performance obligation is satisfied

Membership dues (paid annually) would be recognized over a 12-month period

Newsletter subscription revenue would be recognized quarterly, as each issue is delivered to the subscribers.

Accounting for Leases

What?

Accounting Standards Update (ASU) 2016-02 *Leases (Topic 842)*

Why?

- 1) Convergence with International Accounting Standards Board
- 2) Put true liabilities on the balance sheet

When?

Annual reporting periods beginning after December 31, 2019.
Early adoption is permitted.

Accounting for Leases

Current GAAP

Two Classifications:

- **Operating leases**
 - No liability for future commitments
 - Future commitments disclosed
- **Capital leases**
 - Record asset and amortize over life of lease
 - Record liability to be reduced as lease payments are made

Future GAAP

Two classifications:

- **Finance lease**
 - Similar to capital leases in current GAAP
- **Operating lease**
 - Recognize a right-to-use asset and a lease liability measured at the PV of future lease payments
 - Total cost of lease over the lease term recognized generally on a straight-line basis

Accounting for Leases

Other key provisions



- Short term leases excluded (12 months or less)
- Include lease options only if reasonably certain that option will be exercised
- Lease modification/subleases = separate contracts
- Initial direct costs are amortized over the lease term

Changes to Going Concern Considerations

Issued August 2014



- Applies to all entities
- Incorporates and expands upon certain principles that are currently in U.S. auditing standards
- Requires management to evaluate going concern status
- Effective for periods beginning after December, 15, 2016
- Should be based on events known or knowable at the date that the financial statements are issued
- Evaluation considers events within one year after the date that the financial statements are available to be issued

Changes to Going Concern Considerations



Management must consider whether it is probable that plans will be effectively implemented and that the plans will mitigate the conditions that raised substantial doubt about the entities ability to continue as a going concern

Disclosure requirements

If plans alleviate doubt based on consideration of managements plans:

- Principal conditions or events that raised substantial doubt about the Organizations ability to continue as a going concern (before consideration of managements plans)
- Management's evaluation of the conditions in relation to the entities ability to meet its obligations
- Management's plans that alleviated substantial doubt about the entities ability to continue as a going concern

Changes to Going Concern Considerations



Disclosure requirements (continued)

- If plans **do not** alleviate doubt based on consideration of management's plans, would additionally disclose a statement indicating there is substantial doubt about the Organizations ability to continue as a going concern within one year after the financial statements are issued
- No change to auditors reporting requirements or requirements to perform procedures on management's plans

Statements on Standards for Accounting and Review Services

SSARS 21:

Effective for periods ending on or after 12/15/15

New report language for compilations and reviews

New “Preparation” service

Eliminates **management’s use only** financial statements prepared by CPAs

Compilations:

Retains requirement to indicate in report if independence is impaired

Statements on Standards for Accounting and Review Services

Preparation Services

When Required

- When financial statements are provided by a CPA firm to clients (excluding financial statements prepared only for tax preparation purposes)

Requirements

- Engagement letter signed by the accounting firm and management (annually)
- No accountant's report
- Basis of accounting disclosed in financial statement headings
- Legend indicating no assurance is provided
- Departures from GAAP or other reporting framework need to be disclosed
- Independence does not need to be considered; applies to financial statements with disclosures and no disclosure financial statements

Amendments to Single Audit Act

	Current	New
Single Audit Threshold	\$500,000	\$750,000
Type A Program Determination	\$300,000	\$750,000
Threshold for reporting a questioned cost	\$10,000	\$25,000
<u>Minimum Coverage</u>		
Low risk auditee	25%	20%
Not low risk auditee	50%	40%

Effective for fiscal years beginning on or after
December 26, 2014

Amendments to Single Audit Act



OMB Uniform Grant Guidance

Combines the following OMB Circulars into one:

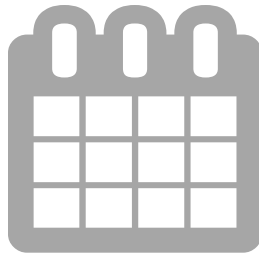
- A-133 (audit)
- A-102 and A-110 (administrative)
- A-87, A-122 and A-21 (cost principles)
- A-89 (Federal domestic assistance program information)
- A-50 (audit follow-up for single audits)

Effective for some new grants, including new funding from existing grants

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Why should we care about proposed changes?

Proposed Changes to Accounting and Reporting for Nonprofit Organizations



Proposed Changes

Still in exposure draft:

- Comment period ended in August 2015

Effective date TBD

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Net Asset Classifications

Current GAAP

Three Net Asset Classifications:

- Unrestricted
- Temporary Restricted
- Permanently Restricted

Proposed Changes

Two Net Asset Classifications:

- Without Donor Restrictions
- With Donor Restrictions

* Plus disclosure of nature and amounts of different types of donor-imposed restrictions, governing board designations and information about how these restrictions affect use of resources and liquidity.

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Underwater Endowments

Current GAAP

Underwater endowment amounts reported in unrestricted net assets



Proposed Changes

Underwater endowment amounts reported in net assets with donor restrictions, with enhanced disclosures

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Changes in Net Assets

Current GAAP

- Present the amounts of the net change in **three** classes of net assets and of total net assets

Proposed Changes

- Present the amounts of the net changes in **two** classes of net assets and of total net assets
- Present two measures of operating activities; both of which are within changes in net assets without donor restrictions



Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Changes in Net Assets

Two Measures of Operating within changes in net assets without donor restrictions. Reflecting:

- (1) whether resources are directed at carrying out an NFP's purpose for existence and
- (2) whether resources are available for current period activities

First Subtotal

Before internal transfers

Second Subtotal

Includes effects of internal transfers resulting from governing board designations, appropriations and similar actions that place (or remove) self-imposed limits on the use of resources that make them unavailable (or available) for current-period operating activities.

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Functional Expenses

Current GAAP

- Statement of functional expenses required for voluntary health and welfare organizations
 - Not required for other organizations

Proposed Changes

- Present information about expense by function, nature or both with enhanced disclosures in notes if both are not on the face of the statement
- Present investment return net of related investment expenses
 - Currently acceptable, but disclosure needed

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Statement of Cash Flows

Current GAAP

Present the net amount for operating cash flows using the **indirect method** (with additional presentation of the direct method permitted)

Proposed Changes

Present the net amount for operating cash flows using the **direct method** (with additional presentation of the indirect method permitted, but not required)

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Other Changes

Cash Flow Activity

Current GAAP

Proposed Changes

Purchase of long-lived assets

Investing

Operating

Contributions restricted to acquire long-lived assets

Investing

Operating

Sales of long-lived assets

Investing

Operating

Payment of interest on borrowings

Operating

Financing

Receipts of interest and dividends on loans and investments other than those made for programmatic purposes

Operating

Investing

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Enhanced Disclosures

- Governing board designations, appropriations and similar transfers that result in the addition or removal of self-imposed limits on the use of resources without donor-imposed restrictions.
- The composition of net assets with donor restrictions at the end of the period and how such restrictions affect the use of resources.
- Management of liquidity, including quantitative information as of the reporting date about financial assets available to meet near-term demands for cash.

Proposed Changes to Accounting and Reporting for Nonprofit Organizations

Enhanced Disclosures

- Expenses, including amounts for operating expense by both their nature and function.
- The method used to allocate costs among program and support functions.
- Underwater endowment funds (i.e., donor-restricted endowment funds for which the fair value of the fund is less than either the original gift amount or the amount required to be maintained by the donor law).

Questions?



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