

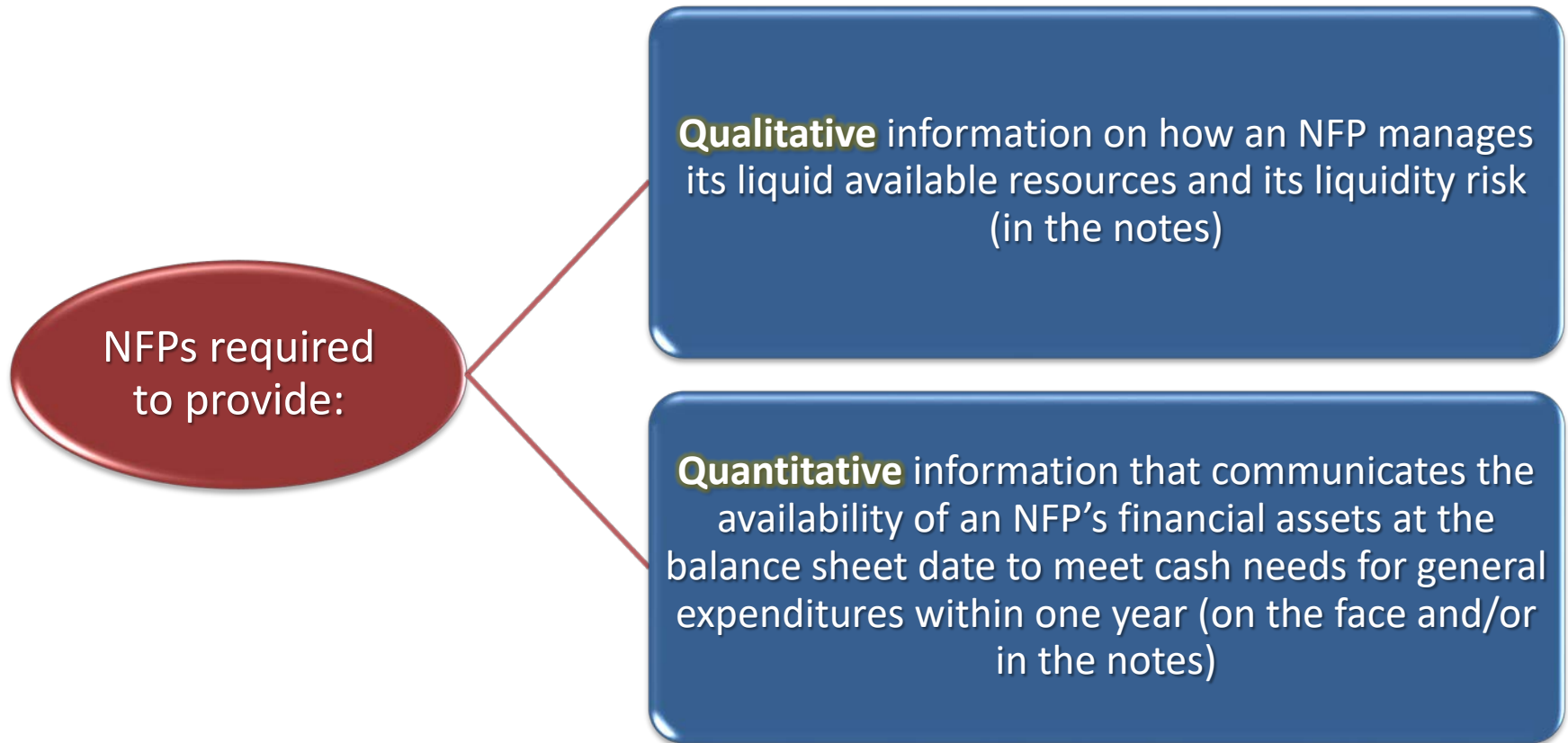
Liquidity and Availability of Resources Disclosures and other Upcoming FASB Requirements

Agenda

- ASU 2016-14 – Liquidity Disclosures
- ASU 2014-09 – Revenue Recognition
 - Subscriptions and Membership Dues
- ASU 2016-02 Leases
- ASU 2018-08 Contributions

Liquidity Disclosures

Liquidity and Availability of Resources



Two New Required Disclosures

1. “Liquidity” Disclosure:

Qualitative information in the notes to financial statements that is useful in assessing an entity’s liquidity and that communicates how an NFP **manages its liquid resources** available to meet cash needs for general expenditures within one year of the date of the statement of financial position.

Example Liquidity Disclosure

- **Note 5 – Information About Liquidity**

Note 5 – Continued

The Organization has an operating reserve that had a balance of \$2.7 million and \$2.8 million at June 30, 2015 and 2014, respectively. This is a governing board-designated reserve with the objective of setting funds aside to 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’s target for this reserve is a total of \$3.0 million, which was determined based on management’s judgment about the appropriate amount of funds to have set aside in addition to working capital. The operating reserve funds are held in lower-risk cash and fixed-income securities. The operating reserve balance is included in the cash and cash equivalents and investments lines on the statement of financial position (2015 - \$1.21M in cash and cash equivalents and \$1.74M in investments; 2014 - \$1.26M in cash and cash equivalents and \$1.70M in investments).

In the event of an unanticipated liquidity need, the Organization also could draw upon \$2,500,000 of an available line of credit (as further discussed in Note 8).

Two New Required Disclosures

2. “Availability” Disclosure:

Quantitative information either on the face of the statement of financial position or in the notes, and additional qualitative information in the notes as necessary, that communicates the **availability of an NFP’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 of a financial asset may be affected by

- Its **nature**
- **External limits** imposed by donors, laws, and contracts with others
- **Internal limits** imposed by governing board decisions.

Example Availability Disclosure

Note 6 - Availability of Financial Assets

The following reflects the Organization's financial assets as of the balance sheet date, reduced by amounts not available for general use within one year of the balance sheet date because of contractual or donor-imposed restrictions or internal designations. Amounts not available include amounts set aside for long-term investing in the operating and capital reserves that could be drawn upon if the governing board approves that action.

	<u>12/31/X1</u>	<u>12/31/X0</u>
Cash	\$ 9,210	\$ 8,750
Investments	185,100	190,100
Receivables	4,100	3,509
Total financial assets	<u>198,410</u>	<u>202,359</u>
Receivables scheduled to be collected in more than one year	(2,200)	(2,050)
Contractual or donor-imposed restrictions:		
Endowment funds	(180,600)	(185,610)
Other donor restrictions	(1,940)	(1,010)
Investments held in charitable remainder trust	(4,500)	(4,490)
Funds restricted by lender	(150)	(150)
Board designations:		
Capital reserves	(2,500)	(2,500)
Operating reserves	<u>(1,300)</u>	<u>(1,300)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 5,220</u>	<u>\$ 5,249</u>

Example of Combined Disclosure

Note X – Liquidity and Availability of Financial Assets

The Theater’s working capital and cash flows have seasonal variations during the year attributable to the annual cash receipts for subscriptions and a concentration of contributions received near calendar year end. To manage liquidity the Theater maintains a line of credit of \$3 million with a bank that is drawn upon as needed during the year to manage cash flow and is then repaid in full by the end of the fiscal year. See Note Y for further description of this line.

The following reflects the Theater’s financial assets as of the balance sheet date, reduced by amounts not available for general use within one year of the balance sheet date because of contractual or donor-imposed restrictions or internal designations. Amounts available include the Board-approved appropriation from the endowment fund for the following year as well as donor-restricted amounts that are available for general expenditure in the following year. Amounts not available include amounts set aside for operating and other reserves that could be drawn upon if the Board of Directors approves that action.

	<u>2016</u>	<u>2015</u>
Current assets, excluding non-financial assets	\$ 3,183,318	\$ 2,710,890
Add: endowment fund appropriation for following year	547,700	591,554
Subtract: cash restricted by lessor to specific uses	(942,941)	(823,430)
Subtract: donor restrictions for specific purposes	(250,000)	
Subtract: board-designated operating reserves and other	<u>(225,129)</u>	<u>(299,011)</u>
Financial assets available to meet cash needs for general expenditures within one year	<u>\$ 2,312,948</u>	<u>\$ 2,180,003</u>

Example – NFP with Deficiency in the Composition of Assets to Comply with Donor-Imposed Restrictions

	Option 1	Option 2
Cash	\$ 1,050	\$ 1,050
Receivables	<u>3,210</u>	<u>3,210</u>
Total financial assets	4,260	4,260
Receivables scheduled to be collected in more than one year	(2,200)	(2,200)
Contractual or donor-imposed restrictions		
Donor contrib restricted to specific purposes	(3,750)	(1,910)
Funds restricted by lender	<u>(150)</u>	<u>(150)</u>
Financial assets available to meet cash needs for general expenditures within 1 year	<u>\$ (1,840)</u>	<u>\$ -</u>

Codification references:

958-210-50-2: An NFP shall disclose the following, if applicable, in the notes to the f/s and may include that information in qualitative disclosures on the availability of an NFP's financial assets in accordance with paragraph 958-210-50-1A(b):

b. The fact that the NFP has not maintained appropriate amounts of cash and cash equivalents to comply with donor-imposed restrictions (see 958-450-50-3).

958-450-50-3: If the noncompliance results from a NFP entity's failure to maintain an appropriate composition of assets in amounts needed to comply with donor restrictions, the amounts and circumstances shall be disclosed.

Other Liquidity Disclosure Examples

- Slide examples (pgs 1 – 2)
- AICPA examples (pgs 3 – 13)
- Big National Charity, Inc. (pg 14)
- Dallas Theological Seminary (pg 15)
- PCORI (pg 16)
- The University of Chicago (pg 17)
- United Way World Wide (pg 18)
- University of Southern California (pg 19)
- Foundation for the Carolinas (pg 20)

Other Key Notes

- Net Assets
- Liquidity and Availability
- Cash Flows
- Investment Return
- Capital Restrictions

Leases Project – New Developments and Implications (ASU 2016-02)

Overview

- FASB issued ASC 842 in February 2016 – Concluded 10 year joint project with the IASB to improve financial reporting of leasing activities
- About 85% of all leases are not currently reported on the balance sheets globally
- In U.S. alone, public companies' operating leases carried off-balance sheet amount to more than \$1 trillion in leasing obligations
- Requires lessees to classify leases as Financing (similar to current capital lease) or Operating (similar to current operating lease)
- Lessors will classify all leases as Type A (similar to current sales-type or direct financing leases) or Type B (similar to current operating lease)

Scope

- Topic 842 guidance includes leases of all property, plant and equipment (PP&E) and excludes:
 - Leases of intangible assets
 - Leases to explore for or use non-regenerative resources (i.e oil, natural gas)
 - Leases of biological assets, (including timber)
 - Leases of inventory
 - Leases of assets under construction

Key Changes

- Lessee
 - Requires recognition of most leases on their balance sheets as lease liabilities with corresponding right-of-use (ROU) assets
 - Recognize expenses on their income statements in a manner similar to today's accounting
 - Requires impairment testing for new ROU assets

Key Changes

- Lessor
 - Aligns certain classification criteria and accounting guidance with lessee guidance and with the revenue recognition model in Topic 606
 - Includes an assessment of collectability to support classification as a direct financing lease and de-recognize asset & record revenue for sales-type lease
 - Leveraged lease accounting not permitted for new transactions or existing transactions modified after the effective date

Key Changes

- Industry sectors expected to be most impacted:
 - Drugstore chains
 - Telecommunications
 - Retail store chains
 - Restaurant chains
 - Airlines
 - Banks
 - Grocery Stores

Lessee Classification

Classification of leases is based on criteria in International Accounting Standards (IAS) 17 (similar to existing U.S. GAAP regarding capital vs. operating lease)

- Classification will be determined in accordance with the principles in current lease requirements, but without the bright-line tests (e.g. by determining whether a lease is effectively an installment purchase by the lessee)
 - Lease will be classified finance lease if it transfers substantially all risks & rewards incident to ownership (***meets one of the 5 criteria on the next slide***)
 - All other leases will be classified as operating leases by lessee
- Classification continues to contain no bright-line criteria, but contains one additional criterion regarding the specialized nature of the underlying asset

Finance Lease Criteria (Sales-Type for Lessor)

1. Ownership of asset transfers to lessee by end of lease term
2. Lessee has option to purchase asset at price which is expected to be sufficiently lower than FV at date option becomes exercisable such that it is reasonably certain option will be exercised
3. Lease term is for major part of the economic life of asset
 - Lessees (and lessors) are afforded an exception to the lease classification test and do not need to consider this criterion for leases that commence “at or near the end” of the underlying asset’s economic life (e.g. in the final 25% of an asset’s economic life).
4. PV of minimum lease payments amounts to at least substantially all of fair value of leased asset
5. **NEW:** The underlying asset is of such a **specialized nature** that it is expected to have no alternative use to the lessor at the end of the lease term

Lessee Accounting – Initial Measurement

All leases result in a liability for its lease obligation and an asset representing a lessee's right to use the underlying asset for the lease term

Amount initially recorded as an ROU asset and lease liability is computed the same regardless of whether the lease is classified as an operating lease or as a finance lease

The recognition, measurement, and presentation of expenses and cash flows arising from a lease by a lessee have not significantly changed from previous GAAP.

Comparison of Lessee Accounting Models

Finance Lease

Balance Sheet

Right of Use (ROU) Asset*
Lease Liability

Income Statement

Interest Expense (on lease liability)
Amortization Expense (on ROU asset)

Cash Flow

Cash paid for principal payments (financing activities) & interest payments (operating activities)

*Periodically reduced by straight-line amortization

Operating Lease

Balance Sheet

Right of Use (ROU) Asset**
Lease Liability

Income Statement

Lease/Rent Expense (straight-line)

Cash Flow

Cash paid for lease payments

**Periodically reduced by the difference between straight-line lease expense & interest cost on lease liability, *i.e.*, “plug figure”

Related Party Leases

- Recognition and measurement:
 - Account for related-party leases based on legally enforceable terms and conditions of the lease
 - Some transaction are not documented or are not “arm’s length”

Disclosures

- Disclosures are required by lessees and lessors to meet a disclosure objective, which would enable users of financial statements to assess amount, timing, & uncertainty of cash flows arising from leases
 - Requires qualitative disclosures along with specific quantitative disclosures
 - Intent is to require enough information to supplement the amounts recorded in the financial statements so that users can understand more about the nature of an entity's leasing activities
- Entities will consider level of detail necessary to satisfy disclosure objective
- Entities will provide transition disclosures required by Topic 250

Transition

- Entities will use modified retrospective approach (assets & liabilities measured at implementation date over remaining life of lease; specific guidance provided)
 - Lessees - Transition method applies to all capital & operating leases
 - Lessors - Applies to all sales-type, direct financing & operating leases (leveraged leases grandfathered, but otherwise phased out)
- Applies to all outstanding leases, not just new leases
- Specific transition guidance for sale & leaseback transactions, build-to-suit transactions, leveraged leases, & amounts previously recognized under business combinations guidance for leases

Impact to Debt Agreements

- Definitions within agreement:
 - Debt
 - Assets
 - EBITDA

Impact to Debt Agreements

- Covenant compliance (typical ratios):
 - Basic fixed charge coverage
 - Current ratio/Working capital
 - Debt service coverage
 - Debt to net worth
 - Funded debt to EBITDA

Effective Date

- New standard is effective for fiscal years beginning after December 15, 2018 for public entities – December 15, 2019 for all other entities
 - *(Most debt agreements will be renewed prior to effective date)*

Revenue Recognition

ASU 2014-09:
Revenue from
Contracts with
Customers (*Amended
by ASU 2014-14*)

FINANCIAL ACCOUNTING SERIES

FASB ACCOUNTING STANDARDS UPDATE

No. 2014-09
May 2014

Revenue from Contracts with Customers
(Topic 606)

An Amendment of the FASB Accounting Standards Codification®

Financial Accounting Standards Board

ASU 2014-09/14: Revenue from Contracts with Customers

- 2002 – Joint project revenue was added to FASB and IASB agendas
- Project goal: consolidate and unify revenue recognition globally
- Over 1,300 comments letters were received

Why All the Fuss!

- Removes hundreds of pieces of industry-specific U.S. GAAP literature
- Lots of Judgement!
- Standard can change economic behavior
- 14% of restatements related to revenue (Center for Audit Quality 10-year study)

Why All the Fuss!

- “When identifying and assessing the risk of material misstatement due to fraud the auditor should, based on a **presumption that risks of fraud exist in revenue recognition**, evaluate which types of revenue, revenue transactions, or assertions give rise to such risks.”

[AU-C 240.28 (emphasis added)]

ASU 2014-09/14: Revenue from Contracts with Customers

Summary of Model:

Identify the contract(s) with the customer



Identify the separate performance obligations in the contract



Determine the transaction price



Allocate the transaction price to the separate performance obligations



Recognize revenue when each performance obligation is satisfied

ASU 2014-09/14: Revenue from Contracts with Customers

- Applies to all contracts with customers, except:
 - Leases
 - Insurance contracts
 - Financial instruments
 - Guarantees
 - Non-monetary exchanges in same line of business to facilitate sales to customers

ASU 2014-09/14: Revenue from Contracts with Customers

- Top impacted areas:
 - Minimum requirements to recognize revenue
 - Ability to recognize revenue over life of contract (formerly percentage of completion) and pattern of recognition
 - Future of loyalty programs and other promotions
 - Customer acceptance and satisfaction guarantees
 - Faster recognition of variable consideration
 - Multiple units of account for licenses of intellectual property
 - Changes in accounting for licenses and intellectual property
 - Disclosures

ASU 2014-09/14: Revenue from Contracts with Customers

- Retrospective presentation to all periods presented or by recognizing a cumulative effect to opening balance of retained earnings
- If cumulative effect, entity would have to include certain additional disclosures about the financial statement line items effected

ASU 2014-09/14: Revenue from Contracts with Customers

- Transition Considerations
 - Will require management to exercise significant judgment, including aspects of the ASU related to estimating transaction price
 - Retrospective application – If elected, may need to perform dual tracking of revenue balances during the retrospective period
 - Systems and processes associated with tracking information may need to be modified to support the capture of additional data elements not currently supported by legacy systems

ASU 2014-09/14: Revenue from Contracts with Customers

- Effective Date and Transition:
 - Public Entities: Effective for annual reporting periods (including interim reporting periods within those periods) beginning after December 15, 2017.
 - Nonpublic Entities: Effective for annual periods beginning after December 15, 2018, and interim periods within annual reporting periods beginning after December 15, 2019.

ASU 2014-09/14: Revenue from Contracts with Customers

- Transition Resource Group:
 - 73 issues addressed to date
- 16 Industry taskforces
- New ASUs being issued to clarify topics arising out of these initiatives

Subscriptions and Membership Dues

Distinguishing Contributions from Other Transactions: Exchange Transactions

- Exchange transaction vs contribution
- How contribution differs from exchange transaction

Indicators Useful for Determining the Contribution and Exchange Portion of Membership Dues

Indicator	Contribution	Exchange Transaction
Recipient NFP entity's expressed intent concerning purpose of dues payment.	The request describes the dues as being used to provide benefits to the general public or to the NFP's service beneficiaries.	The request describes the dues as providing economic benefits to members or to other entities or individuals designated by or related to the members.
Extent of benefits to members.	The benefits to members are negligible.	The substantive benefits to members may be available to nonmembers for a fee.
NFP's service efforts	The NFP provides service to members and nonmembers.	The NFP benefits are provided only to members

Indicators Useful for Determining the Contribution and Exchange Portion of Membership Dues (Continued)

Indicator	Contribution	Exchange TransactionDura
Duration of benefits.	The duration is not specified.	The benefits are provided for a defined period; additional payment of dues is required to extend benefits.
Expressed agreement concerning refundability of the payment.	The payment is not refundable to the resource provider.	The payment is fully or partially refundable if the resource provider withdraws from membership.
Qualifications for membership.	Membership is generally available to the general public.	Membership is available only to individuals who meet certain criteria (for example, requirements to pursue a specific career).

Example – Subscriptions Received as Part of Membership

An NFP trade association produces a quarterly journal that discusses and highlights research, issues and trends of interest to its members and others in the respective discipline related to the NFP’s mission. Members receive the NFP’s quarterly journal as part of their annual membership dues, which are \$300 per year. In addition to the quarterly journal, members receive other membership benefits, such as access to the members-only section of the association’s website and legislative advocacy services. The NFP sells individual journals to others that are not members of the NFP for \$25 per journal. The NFP has determined there is no contribution included in the payment from the customer.

Example – Subscriptions Received as Part of Membership (Continued)

- Step 1 – Identify the Contract: There is a contract between the NFP and the member related to both membership and the journal subscription.
- Step 2 – Identify Performance Obligations: There are six promised goods or services that are to be evaluated whether they are performance obligations that meet the criteria in FASB ASC 606-10-25-19:
 - The promise to provide access to the website during the one-year term.
 - The promise to provide legislative advocacy services during the one-year term.
 - The promise of a subscription to provide four quarterly journals.

Example – Subscriptions Received as Part of Membership (Continued)

- Step 3 – Determine the Transaction Price: The transaction price is the contract price of \$300 for a one-year membership, which includes the subscription.
- Step 4 – Allocate the Transaction Price to Performance Obligations: The transaction price should be allocated between the five performance obligations based on the relative standalone selling prices of each performance obligation.

Example – Subscriptions Received as Part of Membership (Continued)

- Step 4 – Allocate the Transaction Price to Performance Obligations:
 - The standalone selling price for each journal would be the observable price of \$25, since that is the price at which the NFP separately sells the journals to the customers.
 - The NFP doesn't sell membership separately without including the quarterly journals. Since there is no directly observable selling price, the NFP should estimate the standalone selling price. The NFP determines that the adjusted market assessment approach is a suitable method to use to estimate the standalone selling price for the membership, as the estimate will refer to prices charged by other NFPs for similar services. In this case, the standalone selling price was determined to be \$250.
 - The NFP would then allocate the transaction price to the performance obligations based on the relative standalone selling price as follows:

Example – Subscriptions Received as Part of Membership (Continued)

Performance Obligation	Standalone selling price	Percentage
1. Quarterly Journal	\$25	7%
2. Quarterly Journal	\$25	7%
3. Quarterly Journal	\$25	7%
4. Quarterly Journal	\$25	7%
5. Membership benefits	\$250	72%
Total	\$350	100%

Example – Subscriptions Received as Part of Membership (Continued)

Performance Obligation	Allocated Transaction Price
1. Quarterly Journal	\$21
2. Quarterly Journal	\$21
3. Quarterly Journal	\$21
4. Quarterly Journal	\$21
5. Membership Benefits	\$216
Total	\$300

Example – Subscriptions Received as Part of Membership (Continued)

- Step 5 – Recognize revenue when each performance obligation is satisfied: The NFP concludes that:
 - The member simultaneously receives and consumes the benefits of membership, and the membership performance obligation is satisfied over time. The NFP also concludes that the best measure of progress toward complete satisfaction of the membership performance obligation over time is a time-based measure. Thus, \$216 is recognized ratably over the one-year membership period.
 - The performance obligation for each quarterly journal is satisfied as a point in time, and revenue should be recognized when control of the journal has been transferred to the customer. Assuming the NFP concludes control of the journal transfers to the customer upon shipment, \$21 is recognized when each quarterly journal is shipped.

What about Contributions & Grants?

*Clarifying the Scope and Accounting Guidance for
Contributions Received and Contributions Made
(ASU 2018-08)*

Contributions

- Background
 - Purpose is to improve and clarify existing guidance
 - Clarifies: Revenues vs. Contributions
 - ASU 2014-09 raised question as to whether grants and contracts are in scope (reciprocal or nonreciprocal)
 - Long-standing diversity in practice
 - Reciprocal vs nonreciprocal
 - Conditional vs unconditional

Contributions

- Applies to all entities (NFPs and business entities) that receive or make contributions unless otherwise indicated.
- Provides more robust framework for determination
- Clarifies how a NFP determines if resource provider is participating in an exchange transaction.

General

- General thoughts:
 - These are subtle changes and shifts in criteria
 - Therefore may not significantly impact many NPOs
 - Many NPOs
 - More likely to classify Government Grants as Contributions
 - However can result in judgment that changes facts pattern.....so some things may change.....

Summary of Two Topics

- Funds Received: Revenues vs. Contributions
 - Is it a revenue (i.e. earned) vs. a contribution
 - Issues:
 - For NPOs what about Government Funds, Foundation Grants, or other Government Contracts
 - Practice has varied
 - Specifically – are we getting equivalent value?

Contributions

- Revenues vs. Contributions (continued):
 - Resource provider (including Foundations and Governments) is not synonymous with the general public. Indirect benefit received by the public is not equivalent to commensurate value received.
 - Furthering a resource provider’s mission or “feel good” sentiment does not constitute commensurate value received.
 - If the primary beneficiary is a third party, NFP must use judgement to determine if the transaction is reciprocal or nonreciprocal.
 - Type of resource provider should not override the substance of the transaction.

Contributions

- Conditional vs Unconditional Contributions
 - In practice: donor-imposed condition vs. donor-imposed restriction
 - Condition impacts recognition
 - Restriction impacts type of classification
 - Determination based on if agreement includes:
 - A barrier that must be overcome, and
 - Either a right of return or assets transferred or a right of release of a promisor's obligation to transfer assets.

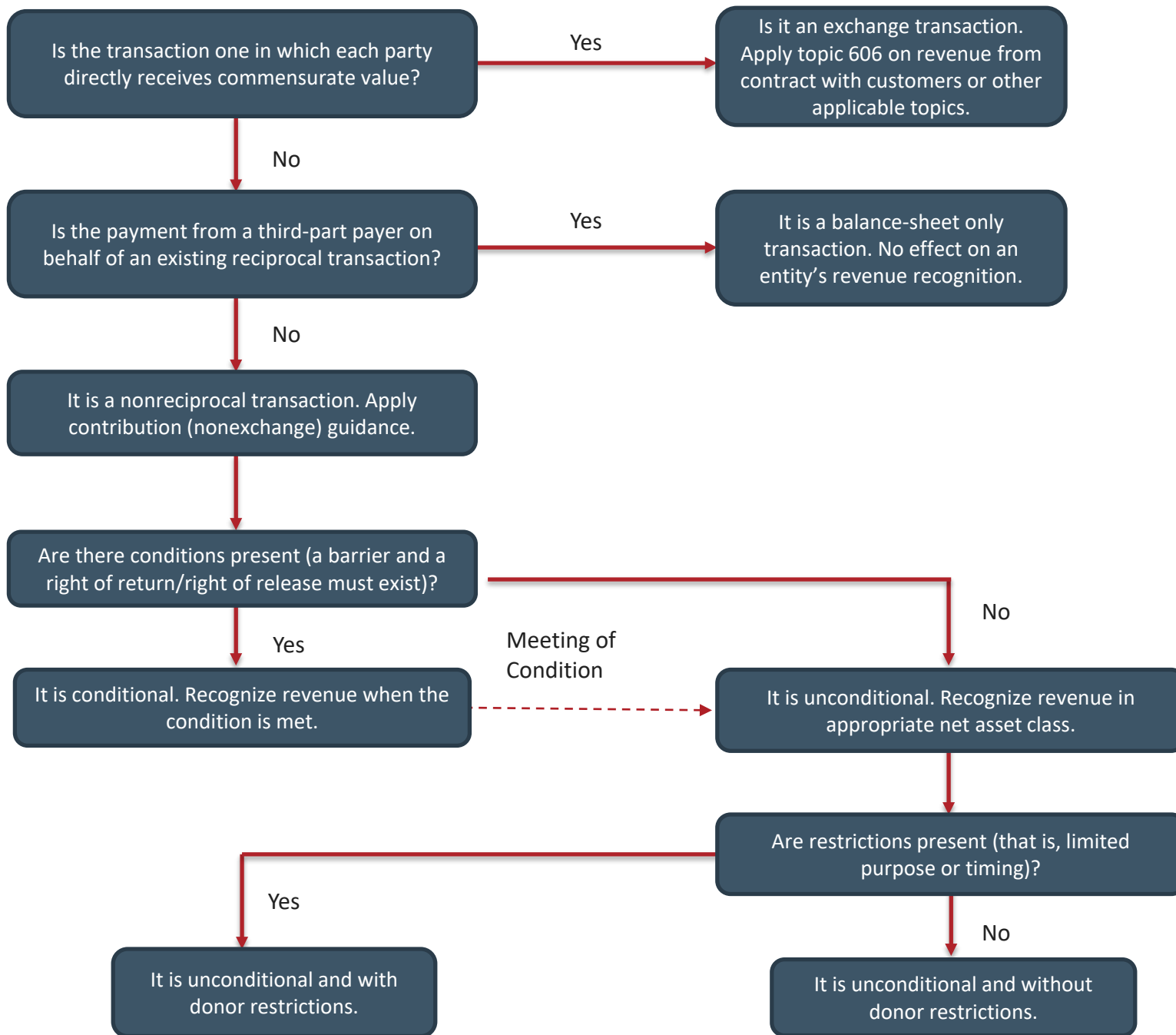
Contributions

- The likelihood that a condition will be met is no longer relevant in the determination
 - Big change – new standard removes the term “remote”

Contributions

- Indications of a barrier:
 - Inclusion of a measurable performance-related barrier or other measurable barrier
 - Whether a stipulation is related to the purpose of the agreement
 - The extent to which a stipulation limits the discretion by the recipient
 - The extent to which a stipulation requires an additional action or actions.

Framework for Classifying Transfers of Assets



Thank You

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