Summer 2017

Profitable Solutions for Nonprofits

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When should you report grant and contribution revenues?

When the Financial Accounting Standards Board's (FASB's) new revenue recognition standard was released in 2014, it caused quite a stir across industries. But the standard applies only to revenue from "exchange transactions," also known as reciprocal transactions. Contributions to nonprofits are nonreciprocal, and your grants may be, too — meaning different rules apply.

Recognizing contributions

In Accounting Standards Update (ASU) No. 2014-09, *Revenue from Contracts with Customers*, the FASB defines a contribution as an unconditional transfer of cash or other assets to an entity in a voluntary nonreciprocal transfer. It specifically distinguishes contributions from exchange transactions, which it describes as reciprocal transactions where each party receives and sacrifices approximately equal value.

That means that contributions don't fall within the rules in ASU 2014-09, including its voluminous disclosure requirements. Instead, you generally should report contributions in the period you receive the pledge or commitment to donate. Restrictions imposed — directions given by the donor — as to how or when the funds may be used don't change the timing of recognition.

But when the donor's gift is available only after certain requirements are met by your organization, the timing may be different. Specifically, you shouldn't recognize a conditional promise to give as revenue until the conditions are substantially satisfied. For example, a promise to give, requiring a minimum matching contribution, can't be recognized until the match is received. Transfers of assets with donor-imposed conditions should be reported as refundable advances until the conditions are substantially met or explicitly waived by the donor.

But you can recognize a conditional promise to give upon receipt of the promise, if the possibility is "remote" that the condition won't be met. An example is a grant requiring you to submit an annual report to receive subsequent annual payments on a multiyear promise.

Recognizing grants

Determining whether a grant is an exchange transaction, where the grantor expects goods and services for its money, or a type of restricted or conditional contribution, where the grantor intends to make a gift to support the organization, can be more complicated. For example, a grant based on the number of meals or beds a nonprofit provides its client population could be considered an exchange transaction, because it's essentially a contract to provide goods or services. Similarly, a research and development grant could be characterized as an exchange transaction, if the grantor retains intellectual property rights in the outcomes.

A grant that's an exchange transaction is subject to ASU 2014-09's five-step framework:

1. Identify the contract (or contracts) with a customer.
2. Identify the performance obligations in the contract.
3. Determine the transaction price.
4. Allocate the transaction price to the performance obligations in the contract.
5. Recognize revenue when (or as) you satisfy a performance obligation.

Nonprofits can find it challenging merely to determine whether a grant is an exchange transaction or a contribution — or a combination of the two.

Say you received a fixed-fee grant to perform specific research for a governmental agency, and the agency will own the outcome. The grant is a contract because the parties each receive something of equal value (grant funds and research) (step 1). The provision and delivery of the research is the performance obligation under the contract (step 2). The fixed fee is the transaction price (step 3). With only one performance obligation, the entire transaction price is allocated to it (step 4), and you will recognize the grant revenue when you deliver the research to the agency (step 5).

This is a simplified example. Nonprofits can find it challenging merely to determine whether a grant is an exchange transaction or a contribution — or a combination of the two, requiring "bifurcation" for proper accounting treatment. And, when a grant is an exchange transaction, it can be tough to identify the performance obligations, when they're satisfied and the proper allocation of the transaction price to those obligations.

Be prepared

ASU 2014-09 will take effect for some nonprofits as soon as 2018. Now is the time to start analyzing *all* of your revenues to determine when and how you should report them. ■

FASB works on more guidance

The determination of how and when to recognize grant and contribution revenue can be tricky for many nonprofits, particularly those receiving government funds. The good news is that the Financial Accounting Standards Board (FASB) is at work on an Accounting Standards Update that will provide more guidance. As part of its "Revenue Recognition of Grants and Contracts by Not-for-Profit Entities" project, the board is considering two main issues:

- How to distinguish between grants and similar contracts that are exchange transactions (which are subject to the FASB's five-step revenue recognition framework) and those that are contributions (which aren't subject to the framework), and
- How to distinguish between conditions and restrictions for contributions.

Although still in the early stages of the project, the FASB has already tentatively decided that a donor-imposed condition will require: 1) a right of return (either a return of the assets transferred or a release of the donor from its obligation to transfer the assets), and 2) a barrier that must be overcome before the recipient is entitled to the assets transferred or promised. (For example, the recipient must raise a threshold amount of contributions from other donors.) A final ASU is expected in first quarter 2018.

Reframing

How nonprofit leaders can keep learning on the job

Whether an executive on staff or a member of the board, new to the organization or a long-time veteran, a nonprofit leader sometimes faces tough challenges that a formal development class won't address. But don't lose heart.

According to the nonprofit Community Resource Exchange (CRE), learning on the job itself can be a rich source of leadership and management development. The CRE advocates two self-coaching opportunities that lean on resources you can find in yourself, within the workplace and among your networks.

Strategies that work

The CRE's first technique is a method known as "reframing." It refers to the ability to shift your perspective and unlock a fresh approach to problems.

The organization also urges leaders to follow what it calls the 1-2-3 steps, which target low-hanging fruit first. This approach calls for beginning with the first few, relatively easy actions you can take to address a specific challenge. The idea is that these initial steps will help move you from understanding the problem to taking action and accomplishing real change.

Example 1: Managing an inadequate infrastructure

These strategies can work, for example, to reframe a problem familiar to many nonprofits — the lack of the strong accounting systems and staff needed to ensure the accurate and timely reporting required for continued funding of your organization.

You could reframe this situation by shifting staff from other areas of the organization to shared responsibilities in finance, thus encouraging managers to think beyond narrow roles. Would involvement of a board member or volunteer supply the manhours and controls you're missing? You also can get past hiring the additional person you can't afford by trying to improve the processes in place, and by inviting and seriously considering creative suggestions from your staff.

From here, you can identify the 1-2-3 steps to get the ball rolling. For instance, you might establish a team from various areas of the organization to outline what needs to be completed on a project and when. Are there tasks that should be prioritized to satisfy government and grantor requirements? Are there other nonessential recordkeeping tasks that could be minimized or eliminated? You also could obtain information and pricing from professional outside accounting firms that specialize in this type of work. Then compare those costs with providing accounting in-house.

Example 2: Managing differences

The CRE also has applied its suggested strategies to the challenges of managing differences. Imagine you're dealing with several diverse groups that use your library's services. Reframing would shift from viewing the different groups as a hodgepodge to seeking common ground among the personalities, demographics and needs. Are these groups all from the local community? Do they all need access to the programs in person? Are they all readers? You also could move from trying to achieve uniformity of interest to mining their diversity.

Easy steps might include convening all of the relevant parties to develop an initial plan for priority activities in the coming year. How best can these groups interact? Possibly, you could bring the children from Story Hour to share an activity with the Writers' Group.

You also could take time to learn more about strategies for managing differences by reading relevant books and articles, meeting to share what you've learned, and planning how to handle future interactions with the various groups that benefit from your services.

Learning as a lifelong pursuit

The most effective leaders always encourage their employees to seek more knowledge and then lead by example. Employing the methods above can help you continually hone your leadership and management skills, even when you don't have the time or money for formal development. ■

8 tips for writing, or revising, a whistleblower policy

Whistleblower policies encourage staff, volunteers and others to discreetly provide credible information on illegal practices or violations of organizational policies. They protect individuals who risk their careers or take other kinds of risks to report illegal or unethical practices. According to its *Report to the Nations*, the Association of Certified Fraud Examiners identified tips as the No. 1 method by which fraud is detected. Whistleblower policies (and the use of hotlines) are important to ensuring tips are received by the organization.

IRS Form 990 asks nonprofits to report whether they've adopted a whistleblower policy. And although no federal law specifically requires organizations to have such policies in place, several state laws do.

Policy essentials

Your whistleblower policy should be tailored to your not-for-profit's unique circumstances. But here are some general tips to consider when forming, or refining, your policy's provisions:

1. Be clear about whom the policy covers. Spell out who's covered by your policy. In addition to employees, volunteers and board members, you might want to include clients and third parties that conduct business with your organization, such as vendors and independent contractors.

2. State which types of wrongdoing are covered. Financial misdeeds often get the most attention, but whistleblower policies can have a longer reach. For example, you might include violations of your organization's client protection policies, conflicts of interest and unsafe work conditions.

3. Spell out reporting procedures. Explain the procedures for reporting concerns. Must claims be made to a compliance officer or can they be reported anonymously? Is a confidential hotline available? Whom can whistleblowers turn to if the designated individual is suspected of wrongdoing? Your procedures should be clear and simple enough to encourage individuals to come forward.

4. Describe investigative procedures. State that every concern raised by a whistleblower will be promptly and thoroughly investigated and that designated investigators will have adequate independence to conduct an objective query. Ideally, investigators should report directly to your nonprofit's board of directors.

Make clear that no retaliation — including harassment, termination or blacklisting — will be tolerated against anyone who raises concerns about potentially illegal or otherwise wrongful practices *in good faith*.

5. Describe postinvestigation steps. Let everyone know what will happen after the investigation is complete. For instance, will the reporting individual receive feedback? Will the individual responsible for the illegal or unethical behavior be punished? If your organization opts *not* to take corrective action, be sure to document your reasoning.

6. Promise confidentiality. A guarantee of confidentiality can make whistleblowing more appealing. But it may not be possible to make such promises if whistleblowers need to become witnesses in criminal or civil proceedings. However, your policy should assure confidentiality to the greatest extent possible.

7. Describe disciplinary action. Not every whistleblower is motivated by pure intentions. State that your organization will take disciplinary action against individuals who make unfounded allegations that are reckless, malicious or intentionally false.

8. Forbid retaliation. A critical component of a whistleblower policy is the prohibition against retaliation. Make clear that no retaliation — including harassment, termination or blacklisting — will be tolerated against anyone who raises concerns about potentially illegal or otherwise wrongful practices *in good faith*. "Good faith" means the individual has a reasonable belief that a problem exists. Specify the party to whom complaints of retaliation can be addressed. Violators should be disciplined promptly and appropriately.

A strong commitment

Whistleblower policies send a strong message about your commitment to good governance and ethical behavior. Make sure that your policy echoes your adherence to an environment of accountability and employee empowerment. ■

NEWSBITS

Proposed Free Speech Fairness Act: Will it pass?

A number of nonprofit leaders — BoardSource, the National Council of Nonprofits, Independent Sector, and the Council on Foundations — have voiced opposition to President Trump's promise to eliminate the Johnson Amendment. The amendment bars tax-exempt charities from using their resources for partisan political purposes.

H.R. 781, the "Free Speech Fairness Act" to appeal the amendment, was introduced in Congress in February and has been assigned to committee. Opponents fear that allowing charities to participate in partisan political activities will make political contributions tax-deductible. Conservative groups that favor greater advocacy in the public space, such as the Alliance Defending Freedom, have long sought repeal of the restriction. ■

New tool makes it easier to see nonprofit tax records

Charity Navigator recently released a new digital tool for "researchers', data scientists' and enthusiasts'" use to explore nonprofits' public tax records. The Digitized Form 990 Decoder features a database of more than 1.7 million tax records. Of these, more than 900,000 have been processed, ranging from over 33,000 2009 Form 990 filings to nearly 216,000 2014 Form 990 filings.

The project is ongoing and open-source. Charity Navigator, which aims to inform donors in their contribution choices, hopes other developers will design improvements to make the tool even more "robust and comprehensive." Go to 990.charitynavigator.org to find the Decoder. ■

IRS warns about W-2 phishing scheme targeting NFPs

The IRS has issued an urgent alert about a Form W-2 phishing scam that targets nonprofits. According to the agency, cybercriminals send an email that appears as if it's from an organization executive to an employee in the payroll or HR department requesting a list of all employees and their Forms W-2.

The scam first appeared last year. But now, the fraudster follows up with an "executive email" to the payroll manager or comptroller and asks that a wire transfer be made to a certain account. If you get either of these emails, tell the IRS right away. ■

FASB issues guidance on partnership consolidation

A recent Financial Accounting Standards Board (FASB) update outlines the rules for when certain nonprofits should consolidate activities of their other partners in financial statements. This continues current guidance that a nonprofit general partner controls the partnership — unless the limited partners have certain rights.

Accounting Standards Update No. 2017-02, *Not-for-Profit Entities — Consolidation (Subtopic 958-810): Clarifying When a Not-for-Profit Entity That Is a General Partner or a Limited Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity*, takes effect for fiscal years starting after December 15, 2016. ■