BKD NATIONAL NOT-FOR-PROFIT GROUP

COMMON NOT-FOR-PROFIT REPORTING ERRORS

PRESENTED BY: **BKD, LLP**

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AGENDA

- About the AICPA report
- Identification of contributions
- Classification of net assets
- Presentation of cash and investments
- Other common errors
- Questions

ABOUT THE AICPA REPORT

- Common Financial Statement Errors for Not-for-Profit Entities
  - AICPA Not-for-Profit Section Advisory Council
  - Published in 2015
  - Common errors for small and medium NFPs
  - Not comprehensive but representative
  - Not all items will apply or be material
  - Available to NFP Section members

IDENTIFICATION OF CONTRIBUTIONS

- Failure to properly classify transactions as contributions or exchange transactions
  - Contribution – unconditional, voluntary and nonreciprocal
  - Exchange transactions - reciprocal and equal value
  - Why is it important to properly classify transactions?
    - Contributions can be restricted
    - Exchange transactions cannot be restricted
  - Tip: refer to ASC 958-605-55 – “Indicators Useful in Distinguishing Contributions from Exchange Transactions”

IDENTIFICATION OF CONTRIBUTIONS

- Grant: Contribution or Exchange Transaction?
  - No formal definition of “grant”
    - Term is used interchangeably with both terms “contribution” and “exchange transaction”
    - It is important to determine classification as that will determine accounting treatment of grant
  - Tip: classification determines the timing of when the revenue is recognized and the treatment of any restrictions on the funds
  - Tip: look at substance of agreement rather than term

IDENTIFICATION OF CONTRIBUTIONS

- Failure to properly classify conditional vs. unconditional promises to give/pledges
  - Pledge must be unconditional to recognize contribution revenue
  - Conditional pledge - donor promises to contribute only if certain conditions are met
  - Tip: consider the following factors if a promise to give is conditional:
    - Promise has explicit matching requirement
    - Promise states that specific outcomes must be achieved
    - Promise requires that amounts not be expended by a certain date be returned to the donor
    - Promise includes words “if”, “subject to”, “when”, etc.

IDENTIFICATION OF CONTRIBUTIONS

- Failure to recognize contribution of services that meet the recognition criteria or recognizing contributed services that do not meet the criteria of p. 16-17 of ASC 958-605-25
  - In-kind contributions (property, food, supplies, etc.)
    - Record the estimated fair value of in-kind contributions as an expense in the financial statements and similarly increase contribution revenue by like amount
  - Contributed services are recognized as revenue at their estimated fair value only when the services received:
    - Create or enhance nonfinancial assets; or
    - Require specialized skills possessed by the individuals providing the service and typically would need to be purchased if not donated

IDENTIFICATION OF CONTRIBUTIONS

- Failure to recognize contribution of services that meet the recognition criteria or recognizing contributed services that do not meet the criteria of p. 16-17 of ASC 958-605-25 (Continued)
  - Tip: consider the quality and quantity of the assets received
  - Tip: be alert of any pro-bono services provided (example: legal services)
  - Tip: educate staff across the Organization for when items (other than cash) are donated

CLASSIFICATION OF NET ASSETS

- Improperly recording board designated net assets as temporarily restricted or permanently restricted net assets
  - Net assets without donor restrictions subject to self-imposed limits by action of the governing board
  - Board-designated net assets may be earmarked for future programs, investment, contingencies, purchase or construction of fixed assets, or other uses
  - Board-designated net assets are classified as unrestricted net assets on the face of the statement of financial position
  - Tip: remember that only donors can restrict

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CLASSIFICATION OF NET ASSETS

- Failure to properly record contribution revenue related to pledges due in future periods as temporarily restricted net assets
  - Generally, there is an implied time restriction unless circumstances indicate the donor intended to support activities of the current period
  - ASC 958-605-45-5 provides guidance for receipts of unconditional promises to give in future years – generally increase temporarily restricted net assets
  - Tip: consider if the donor restricted the funds for use in a certain time period
  - Tip: if pledges receivable is due in more than 1 year – look for it to be in temporarily restricted net assets

CLASSIFICATION OF NET ASSETS

- Failure to identify and properly record net assets released from restrictions
  - Net assets released from restrictions results when a temporarily restriction (purpose or time) has been satisfied
  - Generally, this results in a reduction in temporarily restricted net assets and an increase in unrestricted net assets
  - Net assets released from restrictions on the face of the statement of activities should net to zero between unrestricted and temporarily restricted net assets
  - Tip: keep track of what your restrictions are
  - Tip: use disclosures of restrictions and releases

PRESENTATION OF CASH AND INVESTMENTS

- Failure to separate restricted cash
  - No formal definition of restricted cash
    - Cash held temporarily in investment account
    - Cash included in an endowment fund
    - Cash restricted for a long-term purpose
  - Tip: identify accounts with restricted cash
- Netting purchases and sales on cash flow
  - Required to be gross unless certain criteria met
  - Tip: look for use of word “net” on cash flow

PRESENTATION OF CASH AND INVESTMENTS

- Inconsistent valuation of "other" investments
  - ASC 958-325-15 gives scope
  - Generally investments that are not equity securities with readily determinable fair values or debt securities
  - NFP may elect cost or fair value but must be used for all types of "other" investments
  - Tip: review portfolio to identify "other" investments, review investment policy disclosure for inconsistencies
  - Tip: consider electing fair value option for certain "other" investments

PRESENTATION OF CASH AND INVESTMENTS

- Fair value disclosures
  - Not including all fair value measurements (remember derivatives, beneficial interests in perpetual trusts, anything else measured at FV)
  - Including cash and traditional certificates of deposit (not securities, not carried at fair value)
  - Tip: search financials for any use of phrase “fair value” and make sure those items are included
- Endowment disclosures
  - Failing to include them at all
  - Missing board-designated endowments
  - Tip: if permanently restricted net assets, likely should be endowment disclosures

OTHER COMMON ERRORS

Improper lease classification and not straight-lining rent when required

Checklist for new lease contracts to include classification and rent terms

Not identifying split-interest agreements

Investigate regular checks for not-round amounts from bank or trustee

OTHER COMMON ERRORS

Improper allocation of functional expenses and joint fundraising costs

Develop policy, review any expense types not allocated to all functions

Missing various disclosures

Use a disclosure checklist

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QUESTIONS?

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THANK YOU!

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