New Nonprofit Reporting Standards

Accounting Standards Update 2016-14 provides the most significant changes to nonprofit financial reporting in more than 20 years. Although the standard does not significantly change the underlying non-profit accounting, it does change how activity is presented and disclosed in the financial statements. The changes are effective for fiscal years beginning after December 15, 2017. The ultimate goal is to make nonprofit financial statements more transparent and useful for a wider array of potential financial statement users. Below is a discussion of the five key areas impacted by these changes and recommendations to assist with implementation.

Key Financial Reporting Areas Impacted by the New Standards

1) Net Asset Classes

The new standard changes the terminology associated with net assets and provides additional requirements pertaining to board designated funds, contributions for acquisition/construction of property, and underwater endowments.

Net asset presentation is reduced from three classes to two classes.

Unrestricted net assets (including board-designated net assets) are now “Net Assets Without Donor Restrictions”.

Temporarily restricted net assets and permanently restricted net assets are now “Net Assets With Donor Restrictions”.

The composition of both board designated net assets and net assets with donor restrictions are required to be disclosed either in the statement of financial position, or in the notes to the financial statements.

Organizations with board-designated net assets should establish appropriate policies and procedures detailing the establishment of board-designated net assets, designated conditions, and how funds are released from those designations.

Contributions restricted for acquisition or construction of property and equipment must be released from restriction when the property is placed in service. There is no longer the option to release the restriction over time.

If a donor endowment is underwater, the entire balance is reported in the “Net Assets With Donor Restrictions” class (previously, the underwater portion was considered unrestricted). Required disclosures for underwater endowments include:

- Policies related to appropriation from underwater funds
- For each period presented: the fair value of underwater endowment funds, the amounts required to be maintained, and by how much the amount required to be maintained exceeds the fair value.

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Organization Implementation Advice

* Review the current funds to ensure they are properly classified and adhere to donor restrictions and board designations.
* Determine the level of detail to track and report, including whether the detailed composition of net assets will be presented in the statement of financial position or in the notes to the financial statements.
* Revise the chart of accounts to reflect new terminology and new account groupings.
* For board designated net assets, review or implement the appropriate policies and procedures associated with each fund.

2) Liquidity and Availability

The standard requires new disclosures in the notes to the financial statement narrating how the organization manages its liquidity and detailing how much of an organization's financial assets are available for use on future general expenditures.

Liquidity – Qualitative (descriptive) information on how an organization manages its available liquid resources to meet cash needs for an operating cycle. This is intended to be one to two paragraphs discussing how an organization will manage its liquidity over the next year, including general cash flow management and managing for emergency cash flows should the need arise.

Availability – Quantitative information presented in a table format that communicates how much of an organization's financial assets at the balance sheet date are available to meet cash needs for general expenditures within one year of the balance sheet date.

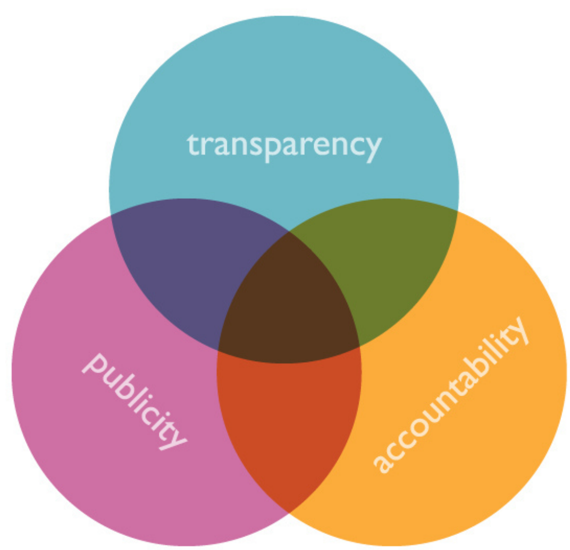
Financial assets are defined as cash, receivables (including pledges) and investments. Financial assets do not include prepaid expenses, inventory, or fixed assets.

"General expenditures" are not defined in the standard, in order to allow nonprofit organizations some flexibility in determining what they consider to be a general expenditure.

The availability of financial assets is impacted by three elements:

- The nature of the asset – The underlying characteristic of an asset may prevent it from being available. For example, a long-term receivable balance is not available for use on general expenditures because the cash will not be received until more than a year after the balance sheet date.
- External limits – Limits imposed by donors, grantors, laws, and contracts with others may prevent an asset from being used on general expenditures. For example, a contribution restricted by the donor for use on a special program activity that the organization does not consider a "general expenditure" for the organization.
- Internal limits – Internal limits on an asset are limits imposed by governing board decisions. For example, board designated net assets designated for purposes outside of what the organization considers to be a "general expenditure".

Organization Implementation Advice - Use prior year financial statements to take a "practice run" with the liquidity and availability disclosures. This will help to identify any issues that need to be evaluated and resolved.



3) Expense Reporting

Functional Expense Schedule - All nonprofit organizations are required to report an analysis of expenses by function (program, management & general, and fundraising) and nature (such as salaries, occupancy, consulting, etc.). Although many organizations already chose to present this schedule, previously only health and welfare organizations were required to.

Expanded disclosures are required in the notes to the financial statements describing which expenses are allocated among program and support functions, and the methodology used.

The new standard provides additional guidance about what to include under management & general as well as recommendations for how costs can be allocated. Only activities that represent the direct conduct or direct supervision of program or other supporting activities can be allocated from management and general activities to those programs or other supporting activities.

Organization Implementation Advice – Review and document current allocation methodologies to be sure they are accurate, consistently applied, and meet accounting standards. Prepare the required footnote disclosure.

4) Investment Return

Investment return must be shown net of all external and direct internal investment management expenses in the Statement of Activities. Direct internal expenses include the direct supervision of the activities involved in generating investment return.

The following investment activity disclosure requirements are no longer required (although the information is still needed for Form 990 presentation):

- Composition of investment return
- Amount of investment expenses
- Components of investment return in endowment disclosure

Organization Implementation Advice - Establish a methodology to accumulate all external and direct internal investment expenses so that they can be included as a component to net investment return in the Statement of Activities.

5) Cash Flow Statement

Similar to before, organizations may continue to present their cash flow statement using either the direct method or the indirect method. For organizations choosing to present cash flow information using the direct method, it is no longer required to present the additional indirect method reconciliation.

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