ADVANCEMENT FASB FUND ACCOUNTING AND REPORTING

#AItraining

Alan S. Hejnal | alan.hejnal@gmail.com
Best Practices in Records Management | Association of Advancement Services Professionals

ACADEMIC IMPRESSIONS

LEARNING OUTCOME

After participating…

…you will be able to better partner with your advancement or finance counterpart to ensure accurate reporting.

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INTRODUCTION

- Fundraising reporting and financial reporting:
  - Have different objectives
  - Look at gifts in different ways
  - Use different standards
- This session will:
  - Draw on familiarity with fundraising standards (and IRS regulations)
  - Outline some of the essentials of financial reporting and how it differs from fundraising reporting
  - Help understand your counterparts and their concerns

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INTRODUCTION

- Perhaps the main "take away" point:
  - What is really amazing is how **similar** financial accounting rules are to gift reporting rules and the IRS regulations!

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OUTLINE

- The big picture
  - I.R.S. Regulations
    - vs. CASE gift reporting
    - vs. Financial standards/fund accounting
  - Why are there 3 different standards?
- Dealing with the past and the present
- The peculiarity of restricted gift income
- Traditional fund accounting, F.A.S. 116 & 117
- The chart of accounts
- Gift deposit, gift feed processes

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OUTLINE

- Specific topics
  - Closed periods in financial accounting
  - Pledges, payments, and outright gifts
  - Deferred gifts (CGAs, CRUTs, CRATs, etc.)
  - Insurance policies
  - In-kind gifts – tangible property and services
  - Endowment
  - Grants & sponsored research
- Reconciliation
- Proposed changes to FASB standards
- Revenue is a negative number!

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DIFFERENT STANDARDS

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THE BIG PICTURE

- IRS regulations
  - vs. CASE gift reporting
  - vs. Financial standards/fund accounting

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TRACTOR TRAILER WEIGHT

- Gross vehicular weight: 80,000 pounds
- Cargo weight: 50,000 pounds
- What is the maximum weight?
- Which is “right”?

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REPORTING ON GIFTS

- Revenue code & I.R.S. Regulations
- CASE gift recording/reporting
- Fund accounting/financial reporting

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REVENUE CODE AND I.R.S. REGULATIONS

- The focus is on the donor: Is this gift deductible?
- Primary purpose
  - Determine whether the federal government is willing to forego collecting tax on a portion of a taxpayer's income
- Determinations are subject to other considerations specific to the donor, not the gift or recipient:
  - Alternative Minimum Tax (AMT)
  - 50% Limitation
  - How long the donor has held the asset

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CASE GIFT RECORDING/REPORTING

- The focus is on the fundraising effort
- Primary purpose
  - Determine the success of a fundraising program, making comparisons among programs
- Not concerned with a donor's specific circumstances

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FUND ACCOUNTING / FINANCIAL REPORTING

- The focus is on the institution: What is the financial position of the non-profit organization?
- Primary purposes
  - Manage finances of the entire organization
  - Compare revenues to expenses
  - Determine credit-worthiness, ability to function as a "going concern"
- Not concerned with a donor's specific circumstances

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OK, SO WHAT? HERE'S AN EXAMPLE

- Sunflower Valley University is conducting its first capital campaign
- One of the campaign priorities is a new student center
- Bob's Building Company agrees to build the student center for the University at no charge!
- Bob's Building Company will contribute all materials, and do all the work

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TAX DEDUCTABILITY (CHARITABLE CONTRIBUTION)

- Only gifts of **cash**, or **property other than cash**, are deductible as charitable contributions for federal income tax purposes
- Gifts of **services** are **not** deductible
- The donated materials are considered property
- The construction work is considered services
- Bob's Building Company can probably deduct the materials, but not the value of their work
  - (Deduction for materials probably limited to cost)

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GIFT REPORTING STANDARDS

- In-kind gifts of materials and long-lived assets can be counted
- Gifts of **services** are **not** counted
- The donated building materials are considered in-kind gifts
- The construction work is considered services
- Sunflower Valley University can count the value of the materials, but not the value of their work
  - (Materials reported at fair market value)

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FINANCIAL ACCOUNTING STANDARDS

- Contributions of assets such as materials and supplies can be counted
- Certain contributions of services **can** be counted!
- Contributed services can be counted if they
  – Create or enhance nonfinancial assets, or
  – Require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation

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FINANCIAL ACCOUNTING STANDARDS

- The construction work created a non-financial asset
  – Before, there was no student center, and now, there is!
- Sunflower Valley University can recognize the full value of the new student center
- This is completely consistent with the purpose of financial accounting, to present the financial position of the institution

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DEALING WITH THE PAST AND THE PRESENT

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THE PAST AND THE PRESENT IN FUNDRAISING

- Fundraising/gift reporting is concerned with when the gift is actually made
  - The legal date of gift is the basis for a donor's deduction
  - Fundraising results, campaign reporting, performance against goals, etc. all based on when the donor made the gift
- The focus is on when the donor acted

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THE PAST AND THE PRESENT IN FUNDRAISING

- Well, almost.
  - Don't need to research/record/document the legal date of gift
  - Typically use as a stand-in the processing date, when the gift is recorded in the fundraising database
    - Processing date most often a few days after the legal date of gift

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THE PAST AND THE PRESENT IN FUNDRAISING

- Gift reporting isn't concerned with what happens after the gift is complete
  - Not concerned whether an asset subsequently gains or loses value
    - Once stock is received, not concerned with subsequent gain or loss, dividends earned while it is held, expenses associated with its sale, etc.
    - Once real property is received, not concerned with gain or loss, tax payments, repairs, rental income, commission, transfer fee, etc.
    - Once a charitable remainder unitrust is established, not concerned with whether the assets appreciate or depreciate

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THE PAST AND THE PRESENT IN FUNDRAISING

- Gift continues to be associated with its date of gift through subsequent changes
  - Suppose you record a $100 gift in September for the International Education Center, but in November you learn that it was actually intended for **International Studies**, an academic department
    - The donor didn't make a gift in November!
    - The donor quite reasonably thinks of this as a September gift
    - You don't want this gift to show up in November gift totals

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THE PAST AND THE PRESENT IN FUNDRAISING

- Gift continues to be associated with its date of gift through subsequent changes
  - Typically adjust the gift to its revised account/designation, but still report based on the original gift (process) date
    - Fundraising system also keeps track that an adjustment was made
    - Gift table shows the gift in its new designation, in September
    - Reports after the adjustment show a September gift to International Studies
  - The same is true if even if it's the donor who asked that the gift be directed
    - Gift was still made in September

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THE PAST AND THE PRESENT IN FUNDRAISING

- Accounting is primarily concerned with the financial position of the organization at a specific time
  - What happens after a gift is complete **does** matter
    - If a donor contributed $25 million to an endowment, and the assets of that endowment are now worth $400 million, that makes a difference to the organization’s financial position!
    - If a stock gift was worth $10,000 when it was given, but after variation in price and sale expenses only $8,963 was realized, that makes a difference (only $8,963 is available to spend)

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THE PAST AND THE PRESENT IN FUNDRAISING

- Accounting is primarily concerned with the financial position of the organization at a specific time
  - Accounting is based on an accounting period
    - Uses a larger accounting period, the fiscal year, further subdivided into monthly periods
    - Activity (transactions) within a period are recorded
    - At the close of the period, activity is reviewed and “balanced,” and the period is “closed”
    - The next accounting period is opened
  - **No changes can be made to a closed accounting period**

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THE PAST AND THE PRESENT IN FUNDRAISING

- Changes have to be made in the current period
  - Suppose you record a $100 gift in September for the International Education Center, but in November you learn that it was actually intended for International **Studies**, an academic department
    - September is closed.
    - Change has to be recorded in the current period (November)
    - Record an adjustment in November
      - Take $100 out of International Education
      - Put $100 into International Studies

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DEALING WITH THE PAST AND THE PRESENT

- Interface from the gift system to the accounting system need to handle this appropriately
  - Adjustment in gift system, resulting in a record with the original gift date, needs to flow through the interface as a current-period debit and credit
    - For a gift reversal, flows through as only a current-period debit
  - Finance offices often want to review changes to past-period activity
    - May ask you to put adjustments to past-period transactions in separate batches and/or feed them separately
    - May ask for notice of adjustments to past-year transactions

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What a strange concept….

RESTRICTED INCOME FROM GIFTS

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RESTRICTED GIFTS IN FUNDRAISING

- In fundraising, we don't think twice about restricted gifts
  - Many of our fundraising initiatives are for restricted purposes:
    - Capital projects
    - Endowed scholarships
    - Funding for specific initiatives
  - Often, it's unrestricted gifts that are harder to raise, and need special attention

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RESTRICTED GIFTS IN ACCOUNTING

- Financial accounting is concerned with **all** revenue, and **all** expenditures
- There are various types of revenue:
  - Tuition payments
  - Room and board payments
  - Purchases at the bookstore
  - Income from conferences, auxiliary activities
  - Earnings from investments
  - Gifts

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RESTRICTED GIFTS IN ACCOUNTING

- Most types of income are **unrestricted**
  - Students don't get to say "I'll pay my tuition bill, but you have to spend it on salaries for faculty in the Environmental Studies program"
  - Bookstore customers don't get to say, "I'll buy these books, but you have to use the money to support the student health center"

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RESTRICTED GIFTS IN ACCOUNTING

- Gifts are responsible for two of the very few types of restricted income
  - Restricted gifts
  - Income on endowments restricted by the terms of the gifts that created the endowments
    - (Some grants and contracts function similarly)

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THE TERM "RESTRICTED" ITSELF

- Means one thing in fundraising
- Means something slightly different in accounting

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"RESTRICTED" IN FUNDRAISING

- "**Restricted:** This term identifies gifts … that have been restricted by the donor for a specific purpose"

-CASE Management and Reporting Standards, 2003

- The basic idea is whether the donor had a specific purpose in mind

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"RESTRICTED" IN ACCOUNTING

- **"Restricted support:** Donor-restricted revenues or gains from contributions that increase either temporarily restricted net assets or permanently restricted net assets"

-Statement of Financial Accounting Standards No. 116, "Accounting for Contributions Received and Contributions Made"

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"RESTRICTED" IN ACCOUNTING

- "**Temporarily restricted net assets:** The part of the net assets of a not-for-profit organization resulting (a) from contributions and other inflows of assets whose use by the organization is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the organization pursuant to those stipulations, (b) from other asset enhancements and diminishments subject to the same kinds of stipulations, and (c) from reclassifications to (or from) other classes of net assets as a consequence of donor-imposed stipulations, their expiration by passage of time, or their fulfillment and removal by actions of the organization pursuant to those stipulations."

-Statement of Financial Accounting Standards No. 116,
"Accounting for Contributions Received and Contributions Made"

ACADEMIC IMPRESSIONS 37

"RESTRICTED" IN ACCOUNTING

- **"Temporarily restricted net assets:** The part of the net assets of a not-for-profit organization resulting (a) from contributions and other inflows of assets whose **use by the organization is limited by donor-imposed stipulations** that either expire by passage of time or can be fulfilled and removed by actions of the organization pursuant to those stipulations, (b) from other asset enhancements and diminishments subject to the same kinds of stipulations, and (c) from reclassifications to (or from) other classes of net assets **as a consequence of donor-imposed stipulations**, their expiration by passage of time, or their fulfillment and removal by actions of the organization pursuant to those stipulations."

-Statement of Financial Accounting Standards No. 116,
"Accounting for Contributions Received and Contributions Made"

ACADEMIC IMPRESSIONS 38

"RESTRICTED" IN ACCOUNTING

- The basic idea is whether the organization is restricted in its use of the funds
  - The organization is not free to use the funds for its general purposes
  - Restrictions must arise from an **external** source.
    - Funds set aside by the board, the president, a dean, etc., for a specific purpose are **not** restricted; the organization itself is free to decide to use those funds differently
  - Restrictions are not "of a general nature"
    - Not for purposes that the organization would have spent money on anyway

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"RESTRICTED" IN ACCOUNTING

- This makes sense, based on the underlying purpose of assessing the organization's financial position
- Consider a hypothetical non-profit entity
  - Has certain expenses:
    - Salaries, utilities, mortgage payments, program, etc.
  - Has certain revenue:
    - Roughly equal to expenses
  - Has certain assets:
    - Investments in securities

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"RESTRICTED" IN ACCOUNTING

- Suppose the non-profit entity's income consists of donations for its general purposes
  - No problem
  - Spend income on salaries, utilities, mortgage payments, program, etc.

ACADEMIC IMPRESSIONS 41

"RESTRICTED" IN ACCOUNTING

- Suppose a significant part of the non-profit entity's income consists of donations with restrictions of a general nature
  - Donations restricted to salaries, program, etc.
  - No problem
  - Spend income on salaries, utilities, mortgage payments, program, etc.

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"RESTRICTED" IN ACCOUNTING

- Suppose a significant part of the non-profit entity's income consists of donations with restrictions specifying other, unbudgeted activities
  - Donations are to hire **additional** staff and start a **new** program
  - Big problem!
  - No funds to spend on budgeted salaries, utilities, mortgage payments, program, etc.
  - Question of whether the entity can continue as "a going concern"

ACADEMIC IMPRESSIONS 43

"RESTRICTED" IN ACCOUNTING

- Suppose unrestricted income is not sufficient to meet its expenses, but there are invested assets that the board has set aside to provide additional income (investment earnings)
  - Not a great situation
  - The board can elect to use those assets to meet expenses

ACADEMIC IMPRESSIONS 44

"RESTRICTED" IN ACCOUNTING

- Suppose unrestricted income is not sufficient to meet its expenses, but the invested assets are permanently restricted by donors, and board is **not** free to spend those funds
  - Big problem!
  - Board can **not** use those assets to meet expenses
  - Question of whether the entity can continue as "a going concern"

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"RESTRICTED" IN ACCOUNTING

- "Discretionary accounts"
  - Donors sometimes designate gifts to be used "at the discretion of the President" (or dean, or chair)
  - Institutions may set up a "President's discretionary account"
- Discretionary accounts are **unrestricted**
  - Person deciding how to use the funds is part of the organization
  - Funds are not subject to **external** constraints
  - The **organization** is free to use the funds however it wants

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Traditional Fund Accounting vs. F.A.S. 116 & 117
Big Changes in 1993

REVISING FUND ACCOUNTING

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TRADITIONAL FUND ACCOUNTING

- Based on a set of funds
  - Current unrestricted
  - Current restricted
  - Capital (plant)
  - Endowment
  - Loan
- Used by non-profit and governmental entities
- Very different from accounting used by the for-profit center

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CHANGES IN THE 1990s

- Governing boards of non-profits typically came from the for-profit sector
  - Boards have oversight responsibilities, need to understand the organization's financial position
  - Fund-accounting financial statements were unfamiliar
- Changes made to financial accounting standards to make statements of non-profits more like those of for-profit entities

CHANGES IN THE 1990s

- Two key changes:
  - Pledges treated as revenue when commitments were made, rather than when they were paid
  - "Funds" largely replaced by three "asset classes"
    - Unrestricted
    - Temporarily restricted
    - Permanently restricted

PLEDGES

- Financial statements of for-profit corporations include outstanding "receivables"
  - Products sold but not yet paid for
  - Outstanding debts of various sorts
- Non-profit accounting didn't recognize pledges in financial statements until the pledges were paid
- An organization's financial position can look very different depending on whether there are commitments for future gifts!
- Extensive debate about whether pledges were "like" traditional receivables

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PLEDGES

- FAS 116 changed the definition of "contribution":
  - A contribution is an unconditional transfer of cash or other assets to an entity or a settlement or cancellation of its liabilities in a voluntary nonreciprocal transfer by another entity acting other than as an owner. Other assets include securities, land, buildings, use of facilities or utilities, materials and supplies, intangible assets, services, **and unconditional promises to give those items in the future.**

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PLEDGES

- Under FAS 116
  - Outright gifts are revenue
  - Unconditional pledges are revenue
  - Payments on unconditional pledges are **not** revenue!
    - Pledge payments pay down outstanding pledge receivables

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ASSET CLASSES

- Unrestricted
  - Neither permanently restricted nor temporarily restricted by donor-imposed stipulations
- Temporarily restricted
  - Use by the organization is limited by donor-imposed stipulations that **either expire by passage of time or can be fulfilled and removed by actions of the organization** pursuant to those stipulations
- Permanently restricted
  - Use by the organization is limited by donor-imposed stipulations that **neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the organization**

ACADEMIC IMPRESSIONS 54

ASSET CLASSES

- Unrestricted
  - General non-gift income, gifts for the general purposes of the organization, gifts with restrictions of a general nature
- Temporarily restricted
  - Expendable gifts for specific programs, capital gifts for buildings
- Permanently restricted
  - Typically gifts for endowment where the principal can't be spent

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Gifts are only a small part…

GIFT DEPOSIT, GIFT FEED PROCESSES, AND CHART OF ACCOUNTS

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CHART OF ACCOUNTS

- Gifts are just one type of entry on the general ledger
  - General ledger deals with both income and expenses
  - Gift income is just one type of income
    - Tuition
    - Investment income
    - Federal grants & contracts
    - Etc.

CHART OF ACCOUNTS

- Finance needs to analyze financial data different ways.
  - Income vs. expense
  - Specific types of income and expenses
  - Larger units of the university, like schools and divisions
  - Smaller units of the university, like departments and offices
  - Etc.

CHART OF ACCOUNTS

- Fully-qualified account number made up of different parts.
  - Unit with a budget (may be called "index")
  - Restricted fund ("fund")
  - Specific type of income or expense ("account", "object", "natural")
  - Other parts
    - Organization, program, activity, location,…
- Not too different from what we do with solicitation code, gift type, designation type, campaign, etc.

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CHART OF ACCOUNTS

- Gift recording typically reflected on a small number of accounts/objects
  - 4201 private grants
  - 4211 gifts
- For reconciliation, easy for finance to just pull activity on gift accounts/objects
  - A few types of transactions may be on different accounts/objects
    - E.G.: Insurance premium underwriting

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CHART OF ACCOUNTS

- In particular, finance's continuing review of gift-based items is isolated on different codes
  - Gain or loss on stock
  - Commission on sale of stock
  - Appreciation of assets of a charitable trust
- For reconciliation, easy for finance to just pull activity on gift accounts/objects!

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GIFT DEPOSIT PROCESS

- Cash and checks are deposited as they are received
  - May be endorsed and taken to the cashier/bursar, with a transmittal form that pretty much just counts and totals them
  - May be done with a scanner that "truncate" and electronically submits the checks
  - Very little detail
- Credit card vendor transfers proceeds electronically to organization's account
- Very little detail, nothing about purposes of gifts

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GIFT FEED PROCESS

- Transfer of information from fundraising system to general ledger
  - Identifies purposes and amounts of gifts
  - May run
    - As each batch is closed
    - Daily
    - Weekly
    - Monthly
  - Different levels of detail
    - Individual transactions
    - Summary for fund during the period

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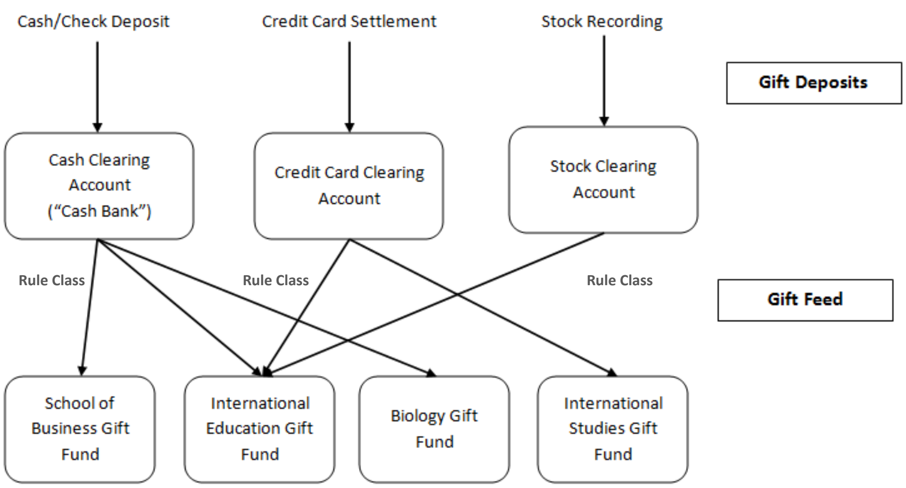
GIFT DEPOSITS, GIFT FEED



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PROCESS FIALURE

- A department may get a check and deposit it in their budget account as miscellaneous income
  - Department may not get many gifts, be unfamiliar with processes
  - Cashier/bursar a key ally in trying to catch these
  - Important to do regular education and send reminders about processes

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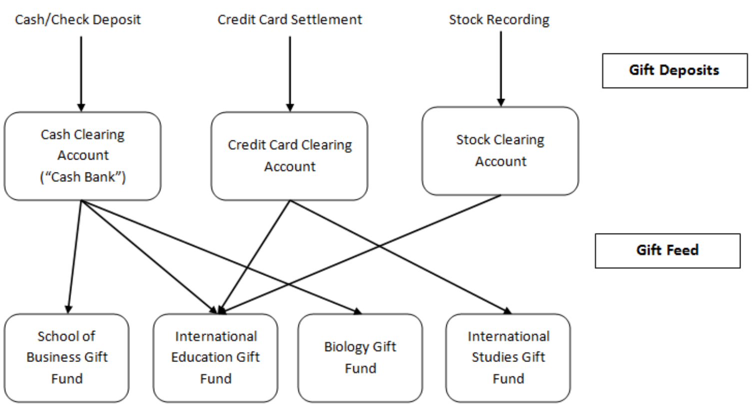
GIFT DEPOSITS, GIFT FEED

- Where is that transaction in this picture?



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PROCESS FAILURE

- Amount typically reversed and re-entered as a journal transaction on the ledger
- Also needs to be recorded in the fundraising system, but don't want it to go through the gift feed processing
  - Usually have special coding in the gift system to support this
  - May be called a "journal cash" transaction

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SPECIFIC ISSUES/DIFFERENCES

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Most gift reporting is traditionally on a "cash" basis
  - Pledge payments and outright gifts added to totals as cash is received
  - The main part of the CAE's "Voluntary Support of Education" Survey (VSE) is based on "cash" only

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Gift reporting includes pledges in some contexts
  - Campaign reports, including CASE Survey of Cumulative Campaign Activity by Educational Institutions
  - Some management reports of "new commitment" activity as a measure of productivity
  - Some management reports of what additional cash is expected by the end of the period (pledge payments due)

ACADEMIC IMPRESSIONS 70

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- In financial reporting
  - Unconditional pledges are recognized as revenue when the pledge is made
    - Revenue is recorded
    - An offsetting receivable is also recorded
  - Pledge payments are **not** recognized as revenue
    - The revenue was recognized when the pledge was made
    - Payments fulfill the receivable recorded when the pledge was recorded
  - Outright gifts are recognized as revenue when the gift is made

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Financial reporting
  - As cash, securities, etc. are received, it's important to distinguish pledge payment from outright gifts
    - Treated differently under financial accounting standards
  - Outstanding pledges have to be reviewed annually
  - Make specific allowances for uncollectible pledges
    - Just like allowances made for other "bad debts"

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Well, almost…
  - This can be an enormous amount of work!
    - Think of all the small annual fund pledges that would need to be booked, paid, reviewed, written off, adjusted if the donor only partially pays or overpays, etc.
  - Some institutions do it exactly this way
  - Most phonathon pledges are made for the current year and paid within a few months, certainly in the same fiscal year
    - How much difference would it make to just record the payments?

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Materiality
  - Accounting uses a concept of "materiality":
    - **Measure of the estimated effect that the presence or absence of an item of information may have on the accuracy or validity of a statement. Materiality is judged in terms of its inherent nature, impact (influence) value, use value, and the circumstances (context) in which it occurs. Opposite of triviality. See also material fact.**

-*http://www.businessdictionary.com/definition/materiality.html*

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Phonathon pledges
  - Can decide not to book phonathon pledges, but book other pledges
    - Greatly reduces the number of pledges that need all this extra attention
    - Payments on phonathon pledges are treated as income, like outright gifts
    - Payments on other pledges are treated as receivables
    - Need to code different pledge types so that the interface to finance can make the distinction

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- But wait, there's more!
  - Nothing magical about phonathon pledges
  - A handful of large pledges generally represent 95%+ of all pledge commitments
    - May be pledges over $5,000, or over $25,000, or over some other amount, depending on the organization
    - Other pledges are not material
    - Payments on these large other pledges are treated as receivables
    - Payments on other pledges are treated outright gifts
    - Need to code different pledge types

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- But wait, there's even more!
  - Even some of those large pledges get paid within the year, at least in part
  - Fiscal year is the key accounting period
  - May decide
    - Not to record **any** pledges during the year
    - Treat **all** pledge payments just like outright gifts
    - Address material pledges in the fiscal year close process

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- How does this work?
  - Fiscal year-end process might look like this:
    - Ignore all single-year phonathon pledges
      - No longer intend to collect them
      - Write them off in the fundraising system
    - Look at outstanding balance of all remaining new pledges
    - Determine threshold for materiality and record those pledges
    - Look at pledges booked as material in past years, and adjust for any payments made during the year on those pledges
    - Still extremely helpful for fundraising system to be able to identify selected pledges!

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Another variation
  - May decide to treat certain pledges differently
    - Pledges above a certain amount
    - Multi-year pledges above a certain amount
  - Use different coding for those pledges
    - FASB pledges
    - Small pledges

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Another variation (cont'd.)
  - Also need to treat payments against those pledges differently!
    - Payments against most pledges treated as income
    - Payments against special pledges recorded against outstanding receivables
  - Options for identifying the different payment types
    - Special pledge payment coding
    - Look back to coding of the related pledge
      - Don't have to worry about keeping pledge and payment coding "in sync"

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Standard for recording pledges
  - Accounting standard is "verifiable"
    - Idea is that, is the institution (or auditor) went to the donor, the donor would confirm the pledge
      - No expectation that every pledge will actually be verif<u>ied</u>!

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PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Standard for recording pledges (cont'd.)
  - Accounting standard is "verifiable"
    - Pledges generally considered verifiable if organization has documentation of the commitment
      - Often a hierarchy of preferred/acceptable documentation
        - » Official pledge form
        - » Other written communication from donor
        - » Letter from fundraiser confirming verbal commitment

ACADEMIC IMPRESSIONS 82

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Standard for recording pledges
  - CASE standard talks about "legally enforceable" pledges
    - Legal enforceability is a **big deal**
      - Determined by state law, varies from state to state
      - Based on legal doctrines of "consideration" or "detrimental reliance" (or both)

ACADEMIC IMPRESSIONS 83

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Standard for recording pledges
  - **Shhh, it's a secret!**
    - In practice, no one actually makes any effort to determine that all pledges are in fact legally enforceable, whatever case says
      - May be a consideration for some large, capital pledges

ACADEMIC IMPRESSIONS 84

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Standard for recording pledges (cont'd.)
  - **Shhh, it's a secret!**
    - In practice, gift recording/reporting standard is essentially the accounting standard, verifiability
      - Means that there really **isn't** a difference in practice
      - Some pledges, like phonathon pledges, are only verbal pledges
        - » Probably never going to hit the accounting system anyway

ACADEMIC IMPRESSIONS 85

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Allowance for uncollectable pledges
  - Sadly, not all pledges are ultimately paid
  - Understanding what is likely **not** to be paid is important for understanding the financial position of the institution
  - Financial accounting handles this by "discounting" pledges, or recording an offsetting "allowance" for uncollectable pledges
    - FAS 116 made handling uncollectable pledges similar to what happens in for-profit accounting with other uncollectable debts

ACADEMIC IMPRESSIONS 86

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Allowance for uncollectable pledges
  - Finance looks to advancement for information to determine these allowances
    - Historical pledge fulfillment rates
    - Historical fulfillment rates may be further refine by donor characteristics
      - Board member vs. Non-board member
      - Alum vs. Non-alum
      - Degreed alum vs. Non-degreed alum
      - Whether the donor has fulfilled pledges in the past
    - For a given pledge, what are the characteristics of the donor?

ACADEMIC IMPRESSIONS 87

PLEDGES, PAYMENTS, & OUTRIGHT GIFTS

- Pledges and donor advised funds
  - Charitable distributions from donor advised funds (DAFs) cannot be pay a donor's personal pledge
  - Typical advancement process in this case is
    - Record outright gift from DAF, with soft-credit to donor
    - Separately, review pledge, and write off a portion (or, at some institutions, the whole pledge)
  - An amount is written off, but this is not the typical discount/allowance for bad debt scenario!
    - May need to design process to communicate/coordinate this between advancement and finance

ACADEMIC IMPRESSIONS 88

CHAT

What's your procedure for working with finance on pledges?

89

DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Gift reporting
  - Traditionally, such deferred gifts were counted at face value
    - Not really a good reflection of the value to the organization
    - A million dollars that you don't get to use for your program for 20 years is worth a lot less than a million dollars today!

90

DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Gift reporting
  - Currently, counted at net present value (NPV)
    - Value of the amount that the organization will receive when the instrument matures, discounted for how far in the future that is projected to be
    - Approximates the amount that the donor can take as a tax deduction

ACADEMIC IMPRESSIONS 91

DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Gift reporting
  - Count the deferred gift only when it is established
    - Don't adjust the gift for gains or losses
    - Don't count the gift again when it matures
  - Count it once, and then you're done!

ACADEMIC IMPRESSIONS 92

DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Financial reporting
  - Record an asset when the deferred gift is established
  - Record a payable for the stream of projected payments to the income beneficiary
  - Annually adjust the asset based on its current value
    - Investment gains/losses, etc.
  - Annually adjust the payable based on projected payment stream
    - Actuarially, even for an annuity, the projected monthly payments to this year's 73 year-old is **not** the stream projected for last year's 72 year-old minus the 12 payments already made!

ACADEMIC IMPRESSIONS 93

DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Financial reporting
  - Basic valuation very similar to gift recording valuation
    - Value of assets (e.g. investments that are part of the trust)
    - Present value of anticipated payment stream
      - Specific rate used in calculation may vary slightly

ACADEMIC IMPRESSIONS 94

EXTERNALLY HELD DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Irrevocable externally held deferred gifts
  - Completed gifts at time of establishment under both gift reporting and financial accounting standards if irrevocable
    - Instrument itself is irrevocable
    - Non-profit is irrevocable beneficiary
  - Need access to relevant portions of trust agreement to establish revocability, assets, share of remainder
  - Without access to trust documents, may only be able to record remainder at maturity

ACADEMIC IMPRESSIONS 95

EXTERNALLY HELD DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Irrevocable externally held deferred gifts
  - Financial reporting
    - Need to restate value every year
      - Important that finance has ongoing access to information from the external trustee about assets, changes to status of income beneficiaries, etc.
      - Without access to trust documents, may only be able to record remainder at maturity

ACADEMIC IMPRESSIONS 96

EXTERNALLY HELD DEFERRED GIFTS (CGAs, CRUTS, CRATS, ETC.)

- Revocable externally held deferred gifts
  - May be revocable in one of two ways
    - Instrument itself is revocable (unusual)
    - Non-profit is revocable beneficiary
      - Donor/trustee has discretion among certain organizations
  - Gift reporting and financial accounting standards treat similarly
    - Only be able to record remainder at maturity, or at such time as you become the irrevocable beneficiary

ACADEMIC IMPRESSIONS 97

EXTERNALLY-HELD, PERPETUAL TRUSTS

- Trusts held by an external trustee, from which your institution gets the income in perpetuity
  - Completed gifts at time of establishment under both gift reporting and financial accounting standards if irrevocable
    - Instrument itself is irrevocable
    - Non-profit is irrevocable beneficiary
  - Very similar to endowment, except you don't hold the assets
    - Income essentially the same as from an internal endowment (depending on the skill of the investment management!)
  - Value is the value of the assets

ACADEMIC IMPRESSIONS 98

EXTERNALLY-HELD TRUSTS

- One final thought
  - Advancement needs to record irrevocable trusts in very similar ways, regardless of whether the institution is the trustee
  - Advancement also needs to make sure that the appropriate distinctions are made in their system to support the distinctions that finance needs to make
    - For example, identify externally-held trusts!
      - May need to feed to finance differently, be handled differently in other ways

ACADEMIC IMPRESSIONS 99

INSURANCE

- Gift reporting
  - Initial gift the cash value of the policy at the time of gift
  - Subsequent checks written by the donor to pay premiums are also gifts
    - The organization owns the policy, so paying the premiums is the organization's obligation/expense. The donor is essentially contributing to underwrite the organization's expense (or paying the expense on behalf of the organization).
    - Can record a pledge for those payments
    - (Better if written to the non-profit, not paid directly to the insurer)

ACADEMIC IMPRESSIONS 100

INSURANCE

- Financial reporting
  - Record an asset when the insurance policy is gifted (cash surrender value)
  - Annually adjust value of the asset (based on current cash surrender value)
  - Premium payments have the effect of increasing the cash surrender value of the policy
    - Showing gifts to underwrite premium payments as revenue would duplicate that increase in value
    - Such tax-deductible gifts not usually classified as gifts under financial accounting standards

ACADEMIC IMPRESSIONS 101

IN-KIND GIFTS – TANGIBLE PROPERTY

- Gift reporting
  - Record at fair market value
    - Value that the institution would have had to pay for that item (including any educational discount)

ACADEMIC IMPRESSIONS 102

IN-KIND GIFTS – TANGIBLE PROPERTY

- Financial reporting
  - Also record at fair market value
  - Subsequent treatment varies
    - Capitalized (usually over a certain dollar threshold)
    - Not capitalized (usually under a certain dollar threshold)
    - Special collections

ACADEMIC IMPRESSIONS 103

IN-KIND GIFTS – SERVICES

- Deductibility as charitable contributions for federal income tax purposes
  - Not deductible
- Gift reporting
  - Not countable

ACADEMIC IMPRESSIONS 104

IN-KIND GIFTS – SERVICES

- Financial reporting
  - Certain contributions of services **can** be counted!
  - Contributed services can be counted if they
    - Create or enhance nonfinancial assets, or
    - Require specialized skills, are provided by individuals possessing those skills, and would typically need to be purchased if not provided by donation

ACADEMIC IMPRESSIONS 105

IN-KIND GIFTS – SERVICES

- Financial reporting
  - One more example
    - An organization may require specific professional services, such as those provided by an attorney, investment manager, printer, etc.
    - Purchasing those services is an ordinary business expense, and possibly a significant expense
    - If, instead, those services are contributed, that expenditure is not required, and the organization is in a different financial position as a result
    - Therefore, the value of those contributed services can be recognized for financial accounting purposes

ACADEMIC IMPRESSIONS 106

IN-KIND GIFTS – SERVICES

- Financial reporting
  - Important to make sure that finance is aware of any such gifts of services

ACADEMIC IMPRESSIONS 107

ENDOWMENT

- Gift reporting
  - Pretty easy!
    - Only care about the value at the time of the gift

ACADEMIC IMPRESSIONS 108

ENDOWMENT

- Financial reporting
  - Not so easy!
  - Need to track value of each endowed fund over time
  - All endowment is typically invested together as part of the "endowment pool" that includes many different assets, that appreciate and depreciate over time, are sold to purchase other assets, etc.
  - How does this work?
    - "Unitized" endowment

ACADEMIC IMPRESSIONS 109

ENDOWMENT

- Financial reporting
  - How does this work?
    - The endowment is divided up into units that represent a certain portion of its value
    - Say you receive $100K for a new endowed scholarship
      - When the funds are to be moved into the endowment, finance determines the current unit value per share—say $745.2660
      - $100,000 is then 134.180279 units
    - As the endowment value goes up (hopefully!) And down, the value of a unit goes up and down
      - The scholarship endowment is 134.180279 times the value of a unit

ACADEMIC IMPRESSIONS 110

ENDOWMENT

- Financial reporting
  - How does this work?
    - Adding funds to the endowment takes a certain amount of work
      - Finance/treasury services may quite reasonably resist going through the whole process to add $25 to an endowment!
      - Good practice to aggregate small gifts, move funds to endowment in aggregate
      - Need to coordinate practices, procedures with finance

ACADEMIC IMPRESSIONS 111

ENDOWMENT

- Financial reporting (cont'd.)
  - How does this work?
    - Taking funds back out of endowment is an even bigger deal!
      - Good practice to hold funds in a non-endowment account until it is clear that endowment minimums will be met

ACADEMIC IMPRESSIONS 112

GRANTS & SPONSORED RESEARCH

- Gift reporting
  - Only includes **private**, **gift** (non-exchange) research
    - Doesn't include government grants, even if they are otherwise very like a private grant
    - Doesn't include sponsored research contracts

ACADEMIC IMPRESSIONS 113

GRANTS & SPONSORED RESEARCH

- Financial accounting
  - Encompasses public and private, grants and contracts
  - Similar issues in managing this whole range—public and private, grants and contracts
    - Managing budgets, tracking expenditures, reporting to funders
    - Have one office use the same staff/application to manage it all
    - Different paths to get the data to that office
  - Need to make sure that gift reporting needs are also accommodated
    - The private grant piece still needs to be the fundraising system

ACADEMIC IMPRESSIONS 114

#AItraining

Showing that development's figures and finance's figures really do have something to do with each other…

RECONCILIATION

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RECONCILIATION

- Two sets of standards, two different numbers
  - Each make perfect sense in its own context
- Confusing to people who see both figures
  - "Which is right?"
  - Senior leadership, board members want to:
    - See that the figures have integrity
    - Cross-check between the two areas

116

RECONCILIATION

- Essentially a simple process
  - Identify the data that links the two systems
    - Fundraising system usually records the accounting Fund Number
    - Date
  - Align the data from both systems
    - Here's the fundraising total
    - Here are the items treated differently by the two standards
      - Subtract the fundraising value of the transaction
      - Add the finance value of the transaction
    - Adds up to the finance total

ACADEMIC IMPRESSIONS 117

RECONCILIATION

- Fundraising report/worksheet may look something like this

Desig. Code	Designation	Fund	Account	Donor	Gift Number	Date of Gift	Amount
BUS	School of Business	20002	4211	Lawrence Dominic	1042977	11/17/2010	$1,500.00
		20002 Total					$1,500.00
INTED	International Education	20026	4211	Caroline Farrell	1021976	11/3/2010	$25.00
INTED	International Education	20026	4211	Boyd Langton	1024542	11/17/2010	$75.00
INTED	International Education	20026	4211	Matthew Harding	1029953	11/30/2010	$500.00
		20026 Total					$600.00
BIOL	Biology	20031	4211	Bennett Halverson	1021983	11/3/2010	$2,000.00
BIOL	Biology	20031	4211	Topher Brink	1027131	11/22/2010	$2,000.00
		20031 Total					$4,000.00
INTST	International Studies	20044	4211	Adelle DeWitt	1023357	11/16/2010	$25.00
		20044 Total					$25.00
		Grand Total					$6,125.00

ACADEMIC IMPRESSIONS 118

RECONCILIATION

- Finance

FUND CODE	ACCOUNT CODE	DESCRIPTION	DATE	AMOUNT
20002				
	4211	1042977 Lawrence Dominic	11/17/2010	$1,500.00
		TOTAL		$1,500.00
20026				
	4211	1021976 Caroline Farrell	11/3/2010	$25.00
	4211	1024542 Boyd Langton	11/17/2010	$75.00
	4211	VOID 09/11/2010 1004375 BALLARD, PAUL	11/23/2010	-$100.00
	4211	102995 Matthew Harding	11/30/2010	$500.00
		TOTAL		$500.00
20031				
	4211	1021983 Bennett Halverson	11/3/2010	$2,000.00
	4211	1027131 Topher Brink	11/22/2010	$2,000.00
		TOTAL		$4,000.00
20044				
	4211	1023357 Adelle DeWitt	11/16/2010	$25.00
	4211	JOURNAL 09/11/2010 1004375 BALLARD, PAUL	11/23/2010	$100.00
		TOTAL		$125.00
		REPORT TOTAL		$6,125.00

ACADEMIC IMPRESSIONS 119

RECONCILIATION

			Gift System	General Ledger			Notes
Fund 2xxxx - Current Restricted							
20002	*4211*	*School of Business*			*BUSINESS*		
	4211	*Reconciling Items*	*$0.00*	*$0.00*		*==> $0.00*	
		Report Totals	*$1,500.00*	*$1,500.00*		*==> $0.00*	*Reconciled*
20026	*4211*	*International Education*			*INTL EDUCATION*		
				($100.00)	VOID 09/11/2010 1004375 BALLARD, PAUL		Adjust from previous period
	4211	*Reconciling Items*	*$0.00*	*($100.00)*		*==> ($100.00)*	
		Report Totals	*$600.00*	*$500.00*		*==> ($100.00)*	*Reconciled*
20031	*4211*	*Biology*			*BIOLOGY*		
	4475	*Reconciling Items*	*$0.00*	*$0.00*		*==> $0.00*	
		Report Totals	*$4,000.00*	*$4,000.00*		*==> $0.00*	*Reconciled*
20444		*International Studies*			*INTL STUDIES*		
				$100.00	journal 09/11/2010 1004375 BALLARD, PAUL		Adjust from previous period
	4483	*Reconciling Items*	*$0.00*	*$100.00*		*==> $100.00*	
		Report Totals	*$25.00*	*$125.00*		*==> $100.00*	*Reconciled*
Fund 2xxxx		*Reconciling Items*	*$0.00*	*$0.00*		*==> $0.00*	
		Report Totals	*$6,125.00*	*$6,125.00*		*==> $0.00*	*Reconciled*
Grand Total		*Reconciling Items*	*$0.00*	*$0.00*		*==> $0.00*	
		Report Totals	*$0.00*	*$0.00*		*==> $0.00*	*Reconciled*

ACADEMIC IMPRESSIONS 120

RECONCILIATION

	GENERAL LEDGER	RECLASS		DEVELOPMENT (Fund&Matrix Rpt)
Annual Fund (11100)	982,055.98	(972.00)	GIK	687,568.11
		(213,816.00)	LIB IAG GRT/OPERS	
		(120.00)	TELECOM-AT&T	
		(79,579.87)	ORANGE&BLUE	
Annual Fund (27000-28999)	16,860.32			16,860.32
Orange&Blue (11100)		79,579.87		79,579.87
Current Other (26000-26999)	802,902.98	972.00	GIK-41531-11100	865,650.34
		9,194.56	INSUR CLRG-21110-11100	
		197,796.06	NO RECEIV GRANTS	
		(146,215.26)	NO DVLP GRANTS	
		1,000.00	DONOR-ENDOW	
Current Other (16710)	10,005.90			10,005.90

ACADEMIC IMPRESSIONS 121

RECONCILIATION

- What do reconciling items look like?
  - Previous-period adjustment
    - Ledger shows reversal, re-entry transactions in later period
  - Insurance premium payment gift
    - Ledger records on a non-gift line, may not appear on general ledger reconciliation report
  - Services recordable under accounting standards
    - Appears on ledger, not in fundraising system
    - May be on a special object code, so that you never see it
  - Items deposited outside regular process
    - Appears on ledger, not in fundraising system

ACADEMIC IMPRESSIONS 122

RECONCILIATION

- Who should do the reconciliation?
  - Development can do the reconciliation
  - Finance can do the reconciliation
  - **Somebody** needs to do a reconciliation!

ACADEMIC IMPRESSIONS 123

RECONCILIATION

- Whoever does the reconciliation needs access to data from both the fundraising system and the general ledger
- Possible to have a program do most of the work
  - Zero in on funds that don't match
  - Match up transactions
  - Highlight unmatched transactions

ACADEMIC IMPRESSIONS 124

RECONCILIATION

- How often should a reconciliation be done?
  - Monthly is usually about right
    - Can make any necessary corrections in a timely manner
    - Volume relatively manageable
    - Identify any systemic issues before they get out of hand!

ACADEMIC IMPRESSIONS 125

#AItraining

Current Project Financial Statements of Not-for-Profit Entities

SMALL COURSE CORRECTION AHEAD?

ACADEMIC IMPRESSIONS 126

PROPOSED ACCOUNTING STANDARDS UPDATE

- On April 22, 2015, the Board issued an Exposure Draft of a proposed Accounting Standards Update, Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954), for public comment
- The revisions are "intended to improve existing standards for financial statement presentation by not-for-profit organizations (NFPs)."
- Focuses on improving
  - the current net asset classification requirements
  - information useful in assessing an NFP's liquidity, financial performance and cash flows

ACADEMIC IMPRESSIONS 127

PROPOSED ACCOUNTING STANDARDS UPDATE

- Net Asset Classification
  - Confusion about "whether and how limits imposed by laws, contracts, and governing boards affect an NFP's classes of net assets, and how those kinds of limits and donor restrictions affect liquidity, financial performance, and cash flows."
  - Misunderstanding of the term "unrestricted net assets"
  - Confusion about "the way underwater donor restricted endowment funds are classified"

ACADEMIC IMPRESSIONS 128

PROPOSED ACCOUNTING STANDARDS UPDATE

- Net Asset Classification
  - Would now have two classes of net rather than three
  - Net assets <u>with</u> donor restrictions
  - Net assets <u>without</u> donor restrictions

ACADEMIC IMPRESSIONS 129

PROPOSED ACCOUNTING STANDARDS UPDATE

- Net Asset Classification
  - *Net assets with donor restrictions* would replace
    - temporarily restricted net assets
    - permanently restricted net assets
  - *Net assets without donor restrictions* the same category as
    - unrestricted net assets
      - Change in terminology for greater clarity
  - Recall that we said that restrictions arise from <u>donor</u> action, so the new terminology just makes that explicit

ACADEMIC IMPRESSIONS 130

PROPOSED ACCOUNTING STANDARDS UPDATE

- Net Asset Classification
  - Underwater endowment amounts reported in *net assets with donor restrictions*, with enhanced disclosure

ACADEMIC IMPRESSIONS 131

PROPOSED ACCOUNTING STANDARDS UPDATE

- Other Proposed Changes to Financial Reporting
  - Less directly related to Advancement, changes to
    - *Statement of Activities*
    - *Cash Flows*
    - *Liquidity*

ACADEMIC IMPRESSIONS 132

PROPOSED ACCOUNTING STANDARDS UPDATE

- Other Proposed Changes to Financial Reporting
  - *Statement of Activities*
    - Changes intended to present financial performance "in ways that are more comparable—and thus more understandable—to creditors, donors, and other external users."
      - Separate operating activities from internal transfers like board designations
      - Report expenses by both their function and nature
      - Present net investment return

ACADEMIC IMPRESSIONS 133

PROPOSED ACCOUNTING STANDARDS UPDATE

- Other Proposed Changes to Financial Reporting
  - *Cash Flows*
    - Changes intended to "increase the understandability and usefulness of the statement of cash flows"
    - Classify certain cash flows differently
      - Distinguish investments from capital purchases
      - Show the cost of borrowing as financing expenses not operating expenses
      - Show interest and dividends as investment income not operating income (unless your charitable purpose is providing loans!)

ACADEMIC IMPRESSIONS 134

PROPOSED ACCOUNTING STANDARDS UPDATE

- Other Proposed Changes to Financial Reporting
  - *Liquidity*
    - Enhanced disclosures

ACADEMIC IMPRESSIONS 135

PROPOSED ACCOUNTING STANDARDS UPDATE

- Current Status
  - Proposed changes are tentative and do not change current accounting
  - "Extensive due process and deliberations" now underway
  - If changes are made, there will be an implementation period

ACADEMIC IMPRESSIONS 136

REVENUE IS A NEGATIVE NUMBER!

- Just trust me…

ACADEMIC IMPRESSIONS 137

TAKEAWAYS

- What's really amazing is how similar financial accounting rules are to gift reporting rules and the IRS regulations!
- Gift reporting focuses on the gift as it is made
  - It's **gift** reporting!
- Accounting reporting continues to look at assets and liabilities over time
  - Concerned with the continuing financial status of the institution
  - No changes can be made to a closed period. All transactions recorded as current.

ACADEMIC IMPRESSIONS 138

TAKEAWAYS

- Financial accounting standards are different from the more gift reporting because financial accounting is intended to accomplish a different purpose.
  – To a very considerable extent, financial accounting makes the same distinctions that gift reporting does!
- For maximum success
  – Keep in mind areas where the standards differ
  – Keep in mind the purpose of financial accounting
  – Develop and maintain a good relationship with your counterparts in finance!

ACADEMIC IMPRESSIONS 139

TAKEAWAYS

- Revisions to FASB standards are under discussion.
  – To the extent that the changes affect Advancement, they may simplify the classifications that colleagues in Finance use.
  – May affect the data items that we use to classify funds.

ACADEMIC IMPRESSIONS 140

QUESTIONS

ACADEMIC IMPRESSIONS 141

EVALUATION

Thank you!

Please remember to complete the event evaluation. Your comments will help us continually improve the quality of our programs.

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