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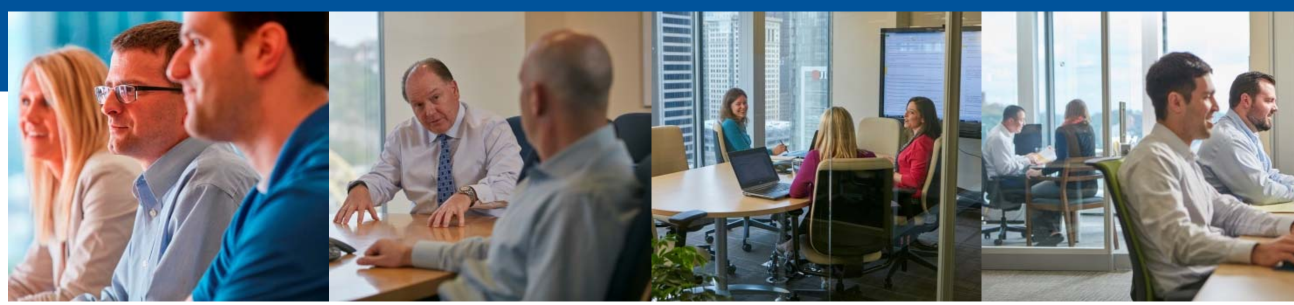
ASU 2018-08 Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made



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Big Thinking. Personal Focus.

Objectives

- Distinguish between contributions and exchange transactions
- Determine if a contribution is conditional or restricted

Current Situation

- Diversity in practice regarding
  - Characterizing grants and contracts as exchange transactions or contributions
  - Determining whether a contribution is conditional
- Differences can affect how revenue is recognized

Agenda Topics

- Scope

- Exchange transactions vs. contributions
- Illustrative examples of exchange vs. contribution transactions

- Evaluation of conditional contributions
- Indicators of a barrier
- Illustrative examples of conditional contributions

- Impact on revenue recognition

- Effective date and implementation

Outcomes

- Distinguish between contributions and exchange transactions
- Reduce difficulties with determining conditional contributions
- Consistent revenue recognition reporting
- Understand effective dates and implementation

Scope

- Primarily issue for not-for-profit (NFP) entities
- Applies to all entities, including business entities
- Applies to both contributions received and contributions made by a resource provider
- Terminology used to label revenue (contribution, grant, donation, etc.) is not a factor in determination of treatment

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2 Key Issues

- Reciprocal (Exchange) vs. Nonreciprocal (Contribution) Transactions

- Distinguishing Conditional from Unconditional Contributions

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Exchange Transactions

- Reciprocal transfers in which each party receives and sacrifices approximately commensurate value

- Example - Grant made by a resource provider that provides materials to be tested and retains the right to any patents or other results of the activity

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Contributions

- Unconditional transfer of cash or other assets
- Nonreciprocal transfers
- Value to general public
- Resource provider receives value indirectly

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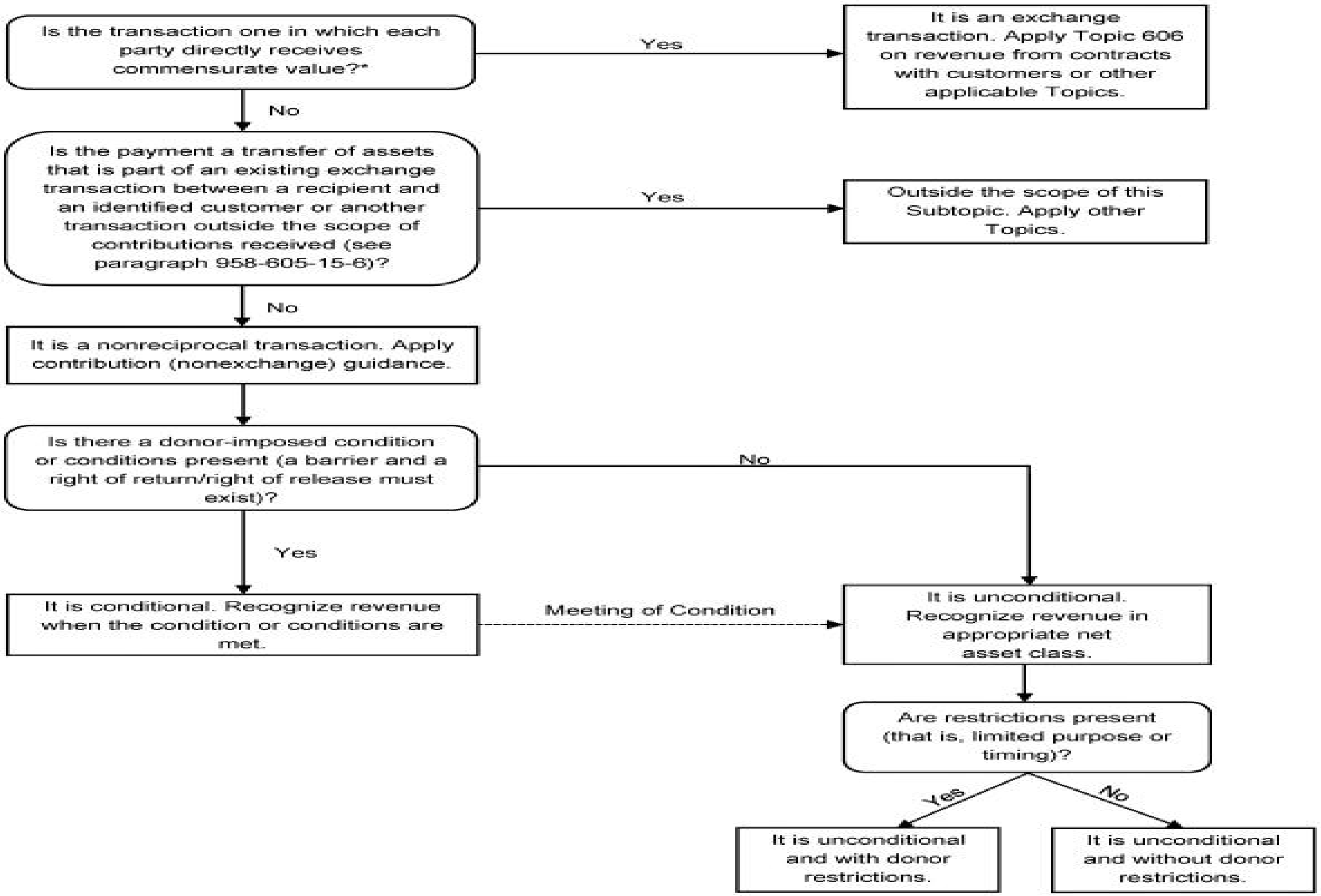
Decision Tree



*See paragraph 958-605-55-6 for guidance about transactions that are in part an exchange and in part a contribution.

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Distinguishing Exchange vs. Contribution

- Items to consider:
  - Appearance of exchange – but sacrifice of little value
  - Type of resource provider does not factor into the determination (gov't, foundation, corporation, etc.)
  - The resource provider is not synonymous with the general public (think mission). Indirect benefit received by the public as a result of the assets transferred is not equivalent to commensurate value received by resource provider.

Distinguishing Exchange vs. Contribution

- Items to consider:
  - Execution of the resource provider's mission or the positive sentiment for acting as a donor shall not constitute commensurate value.
  - If the expressed intent asserted by both the recipient and the resource provider is to exchange resources for goods and services that are of commensurate value, the transaction shall be indicative of an exchange transaction.

Distinguishing Exchange vs. Contribution

- Items to consider:
  - If resource provider has full discretion in determining amount of transferred assets – indicative of contribution.
  - If both the recipient and resource provider agree on amounts transferred in exchange for goods or services of commensurate value – indicative of exchange transaction

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Distinguishing Exchange vs. Contribution

- Items to consider:
  - If the penalties assessed on the recipient for failure to comply with the terms of the agreement are limited to the delivery of assets provided and the return of unspent amounts – indicative of contribution.
  - Exchanges of commensurate value typically include contractual provisions for economic forfeiture beyond the amount of assets transferred by the resource provider to penalize the recipient for nonperformance.

Example 1

FACTS:

NFP A is a large research university with a cancer research center. NFP A regularly conducts research to discover more effective methods of treating cancer and often receives contributions to support its efforts. NFP A receives resources from a pharmaceutical entity to finance the costs of a clinical trial of an experimental cancer drug the pharmaceutical entity developed. The pharmaceutical entity specifies the protocol of the testing, including the number of participants to be tested, the dosages to be administered, and the frequency and nature of follow-up examinations. The pharmaceutical entity requires a detailed report of the test outcome within two months of the test's conclusion. Additionally, the rights to the results of the study belong to the pharmaceutical entity.

Example 1

ANSWER:

This is an exchange transaction.

Because the results of the clinical trial have particular commercial value for the pharmaceutical entity, the pharmaceutical entity is receiving commensurate value as the resource provider. Therefore, the receipt of the resources is not a contribution received by NFP A, nor is the disbursement of the resources a contribution made by the pharmaceutical entity.

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Example 2

FACTS:

Student L is enrolled at University A. Student L's total tuition charged for the semester is $30,000. Student L received a grant in the amount of $2,000 to use toward the tuition fee, which is paid directly by the grantor to University A.

Example 2

ANSWER:

This is an exchange transaction.

The grant was awarded to Student L, not to University A. University A entered into an exchange transaction with Student L and accounts for the $30,000 of revenue in accordance with the guidance in the appropriate Subtopic. The $2,000 grant does not create additional revenue but, rather, serves as a partial payment against the $30,000 due to University A. Student L is an identified customer of University A who is receiving the benefit from the grant transaction.

Example 3

FACTS:

Patient R is a patient at Hospital B. The total amount due for services rendered is $10,000. Patient R has Medicare, and it covers $8,000 of the services, which is paid directly by the government to Hospital B. Hospital B bills Patient R for $2,000.

Example 3

ANSWER:

This is an exchange transaction.

Medicare is a form of insurance. Hospital B has a contract with a customer (Patient R) and determines that the $10,000 should be accounted for as an exchange transaction in accordance with the guidance in the appropriate Topic. The Medicare payment of $8,000 and Patient R’s payment of 2,000 serve as a payment source for services rendered in the amount of $10,000 owed to Hospital B. The payment to Hospital B relates to an existing exchange transaction between Hospital B and an identified customer (Patient R).

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Example 4

FACTS:

The local government provided funding to NFP C to perform a research study on the benefits of a longer school year. The agreement requires NFP C to plan the study, perform the research, and summarize and submit the research to the local government. The local government retains all rights to the study.

Example 4

ANSWER:

This is an exchange transaction. NFP C concludes that this is a procurement arrangement in which commensurate value is being exchanged between two parties and that it should follow the relevant guidance for exchange transactions. NFP C is to perform a research study for the local government and turn over a summary of the study's findings to the local government. The local government retains the rights to the study.

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Example 5

FACTS:

University D applied for and was awarded a grant from the federal government. University D must follow the rules and regulations established by the Office of Management and Budget of the federal government and the federal awarding agency. University D is required to incur qualifying expenses to be entitled to the assets. Any unspent money during the grant period is forfeited, and University D is required to return any advanced funding that does not have related qualifying expenses. University D also is required to submit a summary of research findings to the federal government, but University D retains the rights to the findings and has permission to publish the findings if it desires.

Example 5

ANSWER:

University D concludes that this grant is not a transaction in which there is commensurate value being exchanged.

The federal government, as the resource provider, does not receive direct commensurate value in exchange for the assets provided to University D because University D retains all rights to the research and findings. University D and the public receive the primary benefit of any findings, and the federal government receives an indirect benefit because the research and findings serve the general public. Thus, University D determines that this grant should be accounted for under the contribution guidance in this Subtopic.

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Evaluation of Conditional vs. Unconditional Contributions

- Donor-imposed conditions must have:
  - One or more barriers and
  - A right of return

- Indicators of a barrier
  - Measurable barrier
  - Limited discretion
  - Stipulations

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Indicators of a Barrier

- Measurable performance-related barrier
  - Outcomes to be achieved within a time frame
  - Contingent upon level of service, number of units, or a specific outcome
  - Matching requirements
  - Outside event
- Limited discretion
  - More specific than donor-imposed restrictions
  - Follow specific guidelines for qualifying expenses
- Stipulations
  - Related to purpose of agreement
  - Administrative and trivial are not barriers

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Example 6

FACTS:

NFP H is a recreational organization that provides various sports programs to children who live in the community. NFP H receives an upfront grant in the amount of $40,000 from a foundation to be used toward its tennis program. Consistent with NFP H’s grant proposal, the agreement includes specific guidelines for which NFP H could use the assets (for example, to hire 10 tennis instructors or to provide a summer camp for 9 weeks) but does not specify that NFP H’s entitlement to the $40,000 is dependent upon NFP H meeting any of the specific indicated guidelines in the agreement. The grant contains a right of return for funds not spent on the tennis program.

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Example 6

ANSWER:

NFP H determines that this grant is not conditional because it does not contain a barrier to overcome to be entitled to the transferred assets. Although the grant agreement contains guidelines for how NFP H could spend the $40,000, the agreement does not specify that entitlement to the transferred assets are dependent upon meeting any of the guidelines. Because the guidelines in the grant agreement were not required to be met to be entitled to the funding, the agreement does not contain a barrier to overcome. NFP H should recognize the revenue upon receipt of the assets as donor restricted because it is required to use the assets for the tennis program, which is narrower than NFP H's overall mission.

Example 7

FACTS:

NFP J operates as a homeless shelter that provides individuals with temporary accommodations, meals, and counseling. NFP J receives an upfront grant of $75,000 from the city for its meals program. The grant requires NFP J to use the assets to provide at least 5,000 meals to the homeless. The grant contains a right of return for meals not served.

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Example 7

ANSWER:

NFP J determines that this grant is conditional because it contains a measurable performance-related barrier (to provide 5,000 meals) and a right of return. NFP J recognizes assets received in advance of satisfying the conditions as a refundable advance liability and will then recognize $75,000 as donor-restricted revenue when at least 5,000 meals are served because the purpose of the grant is narrower than the overall purpose of NFP J. The likelihood of providing the meals is not a consideration when assessing whether the contribution is deemed conditional.

Example 8

FACTS:

NFP I is a museum that receives a grant from an individual donor to build a new wing on the existing museum building. The agreement contains a $1 million multiyear promise to give the money to be used for the new wing on the building. The agreement also includes specific building requirements, including square footage and that the new wing must be environmentally friendly with Leadership in Energy and Environmental Design certification. The first installment of the gift will not be paid until NFP I submits architectural designs that meet the building requirements. Additional installments of the grant will be paid in specified increments upon achieving other milestones identified in the grant agreement. If a particular milestone is not achieved, the donor is released from its obligation to make installment payments.

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Example 8

ANSWER:

NFP I determines that this agreement is conditional because NFP I is not entitled to the assets until a milestone is met (for example, an architectural plan including square footage and Leadership in Energy and Environmental Design certification). In this example, a milestone is deemed a measurable performance barrier because NFP I's entitlement to the transferred assets is contingent upon the completion of a milestone. In addition, the agreement includes a release of the resource provider's obligation to transfer assets if the stipulations are not met. NFP I recognizes the revenue as the barriers are overcome, which is upon meeting the specific requirements as NFP I builds the new wing. The likelihood of meeting a milestone is not a consideration when assessing whether the contribution is deemed conditional.

Example 9

FACTS:

NFP B is a hospital that has a research program. NFP B receives a $300,000 grant from the federal awarding agency to fund thyroid cancer research. The terms of the grant specify that NFP B must incur certain qualifying expenses (or costs) in compliance with rules and regulations established by the Office of Management and Budget and the federal awarding agency. The grant is paid on a cost-reimbursement basis by NFP B initiating drawdowns of the grant assets. Any unused assets are forfeited, and any unallowed costs that have been drawn down by NFP B are required to be refunded.

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Example 9

ANSWER:

NFP B determines that this grant is conditional. The grant agreement limits NFP's discretion as a result of the specific requirements on how NFP B may spend the assets (incurring certain qualifying expenses in accordance with the Office of Management and Budget rules and regulations). The grant also includes a release from the promisor's obligation for unused assets. The requirement to spend the assets on qualifying expenses is a barrier to entitlement because the requirement limits NFP B's discretion about how to use the assets, and the assets would need to be spent on specific items on the basis of the requirements of the agreement (for example, adherence to cost principles) before NFP B is entitled to the assets. This is in contrast to a restriction that typically places limits only on a specific activity that is being funded. NFP B records revenue during the grant period when the barriers have been overcome as it incurs qualifying expenses. The likelihood of incurring qualifying expenses is not a consideration when assessing whether the contribution is deemed conditional.

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Example 10

FACTS:

NFP E is a public charity that performs research on various diseases and allergies, including gluten-related allergies, as part of its overall mission. It receives a $100,000 grant from a foundation to perform research on gluten-related allergies over the next year. The grant agreement includes a right of return as part of the foundation's standard wording and a requirement that at the end of the grant period a report must be filed with the foundation that explains how the assets were spent.

Example 10

ANSWER:

NFP E determines that the grant is not a conditional contribution. The purpose of research on gluten-related allergies results in donor-restricted revenue because the purpose of the grant (working on gluten-free allergies) is narrower than the overall mission of the entity. There are no requirements in the agreement that would indicate that a barrier exists, which must be overcome before the recipient is entitled to the resources. NFP E also determines that the reporting requirement alone is not a barrier because it is an administrative requirement and not related to the purpose of the agreement, which is the actual research. This is an example in which a grant including a right of return could not be considered conditional because the return clause is not coupled with a barrier to be overcome, as determined by NFP E using judgment to assess the indicators of a barrier.

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Impact of Revenue Recognition

- Exchange transactions
  - Topic 606, Revenue from Contracts with Customers
- Contributions
  - Subtopic 958-605, Not-for-Profit Entities
- Contributions vs. conditional contributions

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Effective Date Information

- Resource recipient
  - Public business entity or NFP bond obligor
    - Periods beginning after June 15, 2018 (6/30/19 & 12/31/19 year-ends)
  - All other entities
    - Periods beginning after December 15, 2018 (12/31/19 & 6/30/20 year-ends)

- Resource provider
  - Public business entity or NFP bond obligor
    - Periods beginning after December 15, 2018 (12/31/19 & 6/30/20 year-ends)
  - All other entities
    - Periods beginning after December 15, 2019 (12/31/20 & 6/30/21 year-ends)

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Implementation Method

- Modified prospective basis
- No prior-period restatement
- No cumulative-effect adjustment
- Required disclosures
  - Nature of and reason for the accounting change
  - Explanation of the reasons for significant changes in each financial statement line item

Conclusion

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- Effective date and implementation

Outcomes

- Distinguish between contributions and exchange transactions
- Reduce difficulties with conditional contributions
- Consistent revenue recognition reporting
- Understand implementation dates and method