Clarity on Nonprofit Conditions for Contributions

The webinar will begin in a few moments

NOTE: Participants will receive an email within 48 hours with a link to the slide deck and recording.

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Learning Objectives

- **Evaluate** barriers and identify the proper actions to take when receiving grants
- **Identify** the differences between conditional and unconditional contributions
- **Analyze** recent and ongoing FASB updates

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Today’s Presenters

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Conditional vs. Unconditional Contributions

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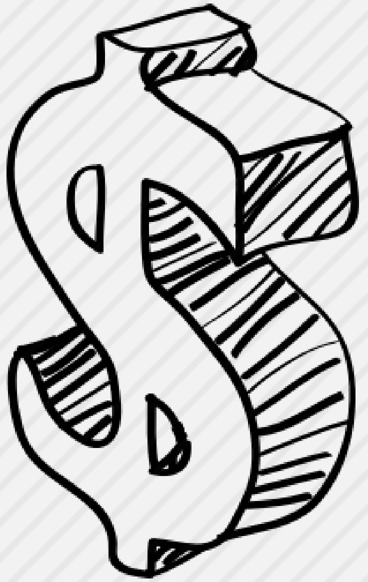
Contributions – A Quick Refresher

- Recognition of contribution revenue must meet the following criteria

- V – Voluntary
- **U – Unconditional**
- N – Non-reciprocal
- I – Irrevocable
- T – Transfer from another entity acting as other than an owner



There Were So Many Questions from our First Webinar!!

Is “conditional” synonymous with “restricted”?

A donor condition is different than a restriction?

Can you have a conditional restricted grant?

Does programmatic reporting indicate the existence of a barrier?

Why is denoting conditional vs. unconditional important?

Conditional vs. Unconditional Contribution

- **Decision Flowchart -** The following is a diagram of a process for a nonprofit organization to take to determine whether the transfer of assets to a recipient is a contribution or exchange transaction and if a contribution whether the transaction is conditional or unconditional.

Does each party directly receive commensurate value in the transaction? → **Transaction is considered an exchange transaction. Follow, Topic 606, revenue from contracts with customers**

↓

Transaction is a nonreciprocal transaction. Therefore, contribution guidance should be applied.

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Are donor imposed conditions present (barriers and a right of return? → **Contribution is unconditional and should be recognized with or without donor restrictions**

↓

Contribution is conditional

We will focus here for purposes of this webinar

Is “Condition” Synonymous with “Restricted” – NO!

- **Donor-Imposed Restriction**
  - Applies to a contribution not an exchange transaction
  - A stipulation that specifies a use for a contributed asset that is more specific than broad limits resulting from the following:
    - The nature of the NFP
    - The environment in which it operates
    - The purposes specified in its articles of incorporation or bylaws or comparable documents
  - Restrictions can be temporary (specific date or programs) in nature or perpetual (held in perpetuity)
  - Gifts with donor-imposed restrictions can be recognized as revenue when they are unconditionally promised with the correct restriction classification

- **Donor-Imposed Condition**
  - Applies to a contribution not an exchange transaction
  - Must have both:
    - A stipulation that represents a barrier that must be overcome before the recipient is entitled to the assets transferred or promised
    - Failure to overcome the barrier gives the donor a right of return of the assets it has transferred or gives the donor a right of release from its obligation to transfer its assets
  - Gifts with donor-imposed conditions should be substantially met before contribution revenue recognition occurs.
    - When revenue recognition occurs essentially the condition has been met and the award is now deemed “unconditional”

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Best Practices

- If donor stipulations do not clearly state whether the right to receive or retain payment or take delivery depends on meeting those stipulations, or if those stipulations are ambiguous, distinguishing a conditional promise to give from an unconditional promise to give may be difficult.
- An agreement does not need to include the specific phrase *right of return* or *release from obligation*; however, an agreement should be sufficiently clear to be able to support a reasonable conclusion about when a recipient would be entitled to the transfer of assets.
- In the absence of any apparent indication that a recipient is only entitled to the transferred assets or a future transfer of assets if it has overcome a barrier, the agreement shall not be considered to contain a right of return of assets transferred or a right of release from obligation and shall be deemed a contribution without donor-imposed conditions.
- A probability assessment about whether the recipient is likely to meet the stipulation is not a factor when determining whether an agreement contains a barrier.

Barriers Exist with Donor-Imposed Conditions

Type of Barrier	Example	Barrier to Overcome
Specified Level of Service	▪ An entity is given assets, the resource provider stipulates that the assets must be used to provide 1,000 meals per week for a soup kitchen	▪ 1,000 meals per week
Specific Output or Outcome	▪ An entity is given assets, entitlement to which is contingent upon producing a specific output or achieving a measurable outcome stemming from the entity’s activities	▪ Students achieving a minimum standardized test score or decline in drop-out rates following an entity’s educational efforts
Matching	▪ A resource provider specifies matching contributions which must be raised by the entity to receive the promised assets	▪ The match
Outside Event	▪ A resource provider specifies that a certain outside event needs to occur for the recipient to be entitled to receive the assets	▪ A resource provider promises to contribute a certain amount of assets if the resource provider's net worth reaches a certain level

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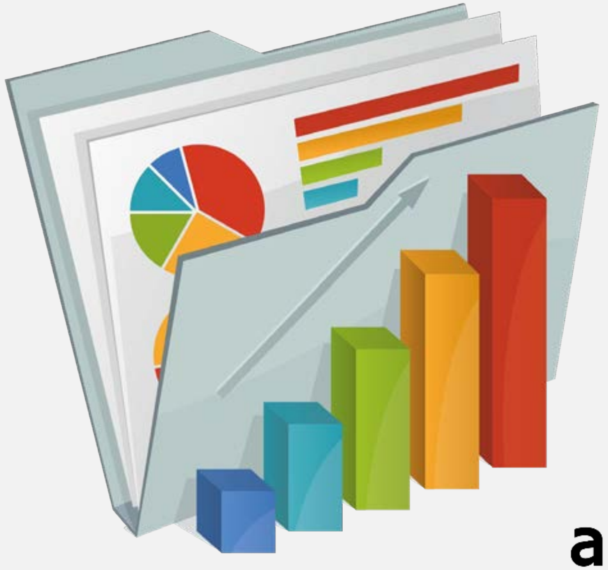
Do Reporting Requirements Indicate Barriers?

- Administrative and trivial stipulations could include routine reporting such as a requirement to provide (a) an annual report or (b) a report that summarizes the recipient's performance to demonstrate the underlying actions that were taken to meet the barrier(s) specified in the agreement. For example, a report that indicates the number of meals that a homeless shelter provided to the homeless is typically not a stipulation that would contribute to achieving the purpose of the agreement. Rather, the action of providing a specified number of meals to the homeless would meet the stipulation that is required by a recipient to achieve the purpose of the agreement.



Can Barriers be Overcome in Stages? Absolutely!!

- Certain promises become unconditional in stages because they are dependent on several or a series of conditions (milestones) rather than on a single condition.
  - With milestones, revenue is recognized in increments as each of the conditions is met.
- Other examples could be promises that are conditional on the organization incurring certain qualifying expenses or costs. These awards will become unconditional and recognized as revenue to the extent expenses are incurred which could be in stages.

Once a NPO Meets a Condition Can the Award Still be Restricted by Specific Donor Stipulation?

- Nonprofit receives an award to build a building for a new program A. Once the building is built the nonprofit has to comply with a restriction to use it only for program A for a period of 20 years.

Is there a donor-imposed condition or conditions present (a barrier and a right of return/right of release must exist)?

No

Yes

It is conditional. Recognize revenue when the condition or conditions are met.

Meeting of Condition

It is unconditional. Recognize revenue if appropriate net asset class.

Are restrictions present (that is, limited purpose or timing)?

Yes

No

It is unconditional and with donor restrictions.

It is unconditional and without donor restrictions.

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Example 1

- Example 1 – Contribution that Includes Qualifying Expenses
  - **Case Study** - 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.
  - **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.

Example 2

- Example 2 – Contribution to a Homeless Shelter
  - **Case Study -** 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.
  - **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 3

- Example 3 – Contribution from a Foundation
  - **Case Study -** ABC Foundation receives a grant proposal from an animal rescue facility, Nonprofit A, which requests a 3-year grant in the amount of $1,000,000 upfront to be used to expand its operations. The agreement indicates that Nonprofit A must expand its facility by at least 5,000 square feet to accommodate additional animals by the end of the 3 years. The grant contains a right of return if the minimum expansion target is not achieved.
  - **Answer -** This is an example of a conditional grant as there is a barrier regarding the 5,000 additional square feet which must be achieved by Nonprofit A to be entitled to assets and a right of return for unused assets or unmet expansion requirements.

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Example 4

- Example 4 – Contribution to a Recreational Organization
  - **Case Study -** NFP H is a recreational organization that provides various sports programs to children that 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 or funds not spent on the tennis program..
  - **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.

Would an NPO Record Deferred Revenue for Conditional Awards?

- If a nonprofit receives a transfer of assets that qualifies as a conditional contribution then it shall be accounted for as a refundable advance until the conditions have been substantially met or explicitly waived by the donor (**similar to current practice**).
- If the nonprofit does not receive a transfer of assets with a conditional award then the nonprofit would footnote disclose the conditional awards (**similar to current practice**).
- Similarly a pledge receivable would not be recorded with a deferred liability or refundable advance. **A nonprofit would not gross up their balance sheet**.
  - A nonprofit would only record a pledge receivable when it has an unconditional contribution that it has not yet received the transfer of assets for.
  - A nonprofit would only record a refundable advance for a conditional contribution that they have received a transfer of assets for.

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