



LOCAL COUNCIL AUDIT AND TAX UPDATE 2018

Financial Statements of Not-for-Profit
Entities and

the Tax Cuts and Jobs Act

Presenter: Ken Moran, CPA, CGMA



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About the presenter.....

Ken is a CPA and CGMA, licensed in Virginia and North Carolina, with over 20 years' experience in not-for-profit accounting and taxation. Ken audited local councils with McGladrey & Pullen (now RSM) and served as CFO of the Heart of Virginia Council in Richmond, VA for 8 years on a contract basis as managing principal of his own CPA firm in Richmond. Ken authors both the *Local Council Guide to the Audit* and *Local Council Guide to IRS Form 990*, among other publications, and can be reached at ken.moran@scouting.org.

Note: The following information is being provided for educational purposes only and should not be acted upon before consulting your council's locally licensed professionals.





Presentation of Financial Statements of NFP Entities

(ASU 2016-14, Issued August 2016)





ASU 2016-14 Overview

- After 20-plus years, the FASB issued new standard on financial statements of not-for-profit entities.
- All not-for-profit organizations affected—including local councils.
- Goal is to simplify, clarify, and make transparent.
- Effective for 2018 financial statements (audits in 2019).
- Phase 1 of 2.

(Phase 2 rolled into Financial Performance Reporting Research Project)





ASU 2016-14 Key Provisions

- Liquidity and Availability
- Net Asset Classification
- Investment Return
- Board Designations/Appropriations
- Functional Expenses
- Statement of Cash Flows
- Underwater Endowments
- Gifts of PP&E





Liquidity and Availability

- **Quantitative information** that communicates the *availability of an NFP's financial assets at the balance sheet date* to meet cash needs for general expenditures within one year of the balance sheet date.
- **Qualitative information** that communicates *how an NFP manages its liquid resources* that are available to meet cash needs for general expenditures within one year of the balance sheet date.





L&A—Quantitative information

The Council's financial assets available for general expenditure, that is, without donor or other restrictions limiting their use, within one year of the statement of financial position date, are as follows:

| | 2018 | 2017 |
|---|---------|---------|
| Cash—Operating Fund | \$X,XXX | \$X,XXX |
| Contributions receivable—Operating Fund | X,XXX | X,XXX |
| Accounts receivable—Operating Fund | X,XXX | X,XXX |
| Short-term investments—Operating Fund | X,XXX | X,XXX |
| Total financial assets as of end of year | X,XXX | X,XXX |
| Appropriation from quasi-endowment for for general expenditure in subsequent year | X,XXX | X,XXX |
| Financial assets available to meet cash needs for general expenditures within one year | \$X,XXX | \$X,XXX |





L&A—Qualitative information

The Council's endowment funds consist of donor-restricted endowments and a quasi-endowment. Income from donor-restricted endowments is restricted for specific purposes and, therefore, is not available for general expenditure. As described in Note X, the quasi-endowment has a spending rate of X percent. \$X,XXX and \$X,XXX of appropriations from the quasi-endowment will be available within the next 12 months as of December 31, 2018 and 2017, respectively.

As part of the Council's liquidity management, it has a policy to structure its financial assets to be available as its general expenditures, liabilities, and other obligations come due. In addition, the Council invests cash in excess of daily requirements in short-term investments. To help manage unanticipated liquidity needs, the Council has committed lines of credit in the amount of \$X million, which it could draw upon. Additionally, the Council has a quasi-endowment of \$XX million. Although the Council does not intend to spend from its quasi-endowment other than amounts appropriated for general expenditure as part of its annual budget approval and appropriation process, amounts from its quasi-endowment could be made available if necessary. However, both the quasi-endowment and donor-restricted endowments contain investments with lock-up provisions that would reduce the total investments that could be made available (see Note X for disclosures about investments).





L&A—Preparing for the Audit

| Liquidity and Availability Schedule | | |
|--|--------------|--------------|
| Periods ending December 31, 2018 and 2017 | | |
| | 2018 | 2017 |
| Cash - Operating Fund | 7,035,430 | 7,005,851 |
| Short-term investments - Operating Fund | 0 | 0 |
| Accounts receivable - Operating Fund | 384,238 | 288,580 |
| Contributions receivable - Operating Fund | 590,705 | 1,100,561 |
| Total financial assets as of end of year | 8,010,373 | 8,394,992 |
| Appropriation from endowment for general expenditures in subsequent year | - | - |
| Appropriation from quasi-endowment for general expenditures in subsequent year | - | - |
| Bank Line of Credit | - | - |
| Financial assets available to meet cash needs for general expenditures within one year | \$ 8,010,373 | \$ 8,394,992 |
| Explanation Notes: | | |





Net Asset Classification

Old (Three Categories)

- Unrestricted
- Temporarily Restricted
- Permanently Restricted

New (Two Categories)

- Without Donor Restrictions
- With Donor Restrictions





Net Asset Classification

Q: Why the need for change?

A: FASB felt that UPMIFA blurred the line between PRNA and TRNA—if you can spend from an underwater endowment fund, is it really permanently restricted?





Net Asset Classification

Q: What has changed?

A: Your PeopleSoft “audit format” Statement of Financial Position and Statement of Activities and Changes in Net Assets have been updated to comply with the new ASU (examples follow).





| | | | | | | | | |
|---|------------------|------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Total noncurrent assets | 1,591,367 | 1,075,611 | 34,096,248 | 34,675,278 | 31,409,762 | 28,920,308 | 67,097,377 | 64,671,196 |
| Total assets | 7,596,033 | 5,995,336 | 37,189,891 | 36,521,759 | 33,466,569 | 29,182,960 | 78,252,494 | 71,700,054 |
| Current liabilities: | | | | | | | | |
| Accounts payable | 1,066,474 | 266,569 | 5,698 | 7,772 | | | 1,072,171 | 274,341 |
| Accrued expenses | 313,982 | 1,294,220 | | | | | 313,982 | 1,294,220 |
| Taxes & benefits withheld | 246 | 234 | | | | | 246 | 234 |
| Custodial accounts | 796,071 | 726,400 | 140,585 | 140,585 | | | 936,657 | 866,985 |
| Deferred activity revenue | 552,782 | 99,661 | | | | | 552,782 | 99,661 |
| Deferred camp revenue | 27,727 | 23,382 | | | | | 27,727 | 23,382 |
| Deferred special event revenue | | | | | | | | |
| Other deferred revenue | 33,304 | 33,508 | | | | | 33,304 | 33,508 |
| Other current liabilities | | 611 | | | | | | 611 |
| Total current liabilities | 2,790,586 | 2,444,584 | 146,283 | 148,357 | | | 2,936,869 | 2,592,941 |
| Total noncurrent liabilities | | | | | | | | |
| Total liabilities | 2,790,586 | 2,444,584 | 146,283 | 148,357 | | | 2,936,869 | 2,592,941 |
| Net assets: | | | | | | | | |
| Without donor restrictions | 2,667,783 | 2,244,683 | 34,427,095 | 34,939,811 | 2,222,395 | 124,715 | 39,317,273 | 37,309,209 |
| With donor restrictions | 2,137,665 | 1,306,069 | 2,616,513 | 1,433,591 | 31,244,174 | 29,058,244 | 35,998,353 | 31,797,904 |
| Total net assets | 4,805,448 | 3,550,752 | 37,043,608 | 36,373,401 | 33,466,569 | 29,182,960 | 75,315,626 | 69,107,113 |
| Total liabilities and net assets | 7,596,033 | 5,995,336 | 37,189,891 | 36,521,759 | 33,466,569 | 29,182,960 | 78,252,494 | 71,700,054 |





| | | | | | | | | |
|---|------------------|------------------|-------------------|-------------------|-------------------|-------------------|-------------------|-------------------|
| Indirect support: | | | | | | | | |
| United Way | 457,320 | 473,810 | 0 | 0 | 0 | 0 | 457,320 | 473,810 |
| Total indirect support | 457,320 | 473,810 | 0 | 0 | 0 | 0 | 457,320 | 473,810 |
| Investment revenue - net | 0 | 0 | 1,877 | 3,101 | 0 | 0 | 1,877 | 3,101 |
| Net assets released from restriction | (903,963) | (1,230,898) | (174,850) | (289,131) | 0 | 0 | (1,078,813) | (1,520,029) |
| Total support and revenue | 831,596 | (386,328) | 1,182,923 | (281,030) | 2,185,930 | 1,855,794 | 4,200,449 | 1,188,436 |
| Increase (decrease) in net assets with donor | 831,596 | (386,328) | 1,182,923 | (281,030) | 2,185,930 | 1,855,794 | 4,200,449 | 1,188,436 |
| Increase (decrease) in total net assets | 1,284,696 | (7,592) | 640,207 | (773,992) | 4,283,610 | 956,610 | 6,155,622 | 175,027 |
| Net assets, beginning of year: | | | | | | | | |
| Without donor restrictions | 2,244,683 | 1,865,947 | 34,939,811 | 35,432,772 | 124,715 | 1,023,899 | 37,309,209 | 38,322,618 |
| With donor restrictions | 1,306,069 | 1,692,397 | 1,433,591 | 1,714,621 | 29,058,244 | 27,202,451 | 31,797,904 | 30,609,468 |
| Total net assets, beginning of year | 3,550,752 | 3,558,344 | 36,373,401 | 37,147,393 | 29,182,960 | 28,226,349 | 69,107,113 | 68,932,086 |
| Board authorized transfers | (30,000) | 0 | 30,000 | 0 | 0 | 0 | 0 | 0 |
| Net assets, end of year: | | | | | | | | |
| Without donor restrictions | 2,667,783 | 2,244,683 | 34,427,095 | 34,939,811 | 2,222,395 | 124,715 | 39,264,383 | 37,309,209 |
| with donor restrictions | 2,137,665 | 1,306,069 | 2,616,513 | 1,433,591 | 31,244,174 | 29,058,244 | 35,998,353 | 31,797,904 |
| Total net assets, end of year | 4,805,448 | 3,550,752 | 37,043,608 | 36,373,401 | 33,466,569 | 29,182,960 | 75,262,735 | 69,107,113 |





Net Asset Classification

Q: Do local councils need to change their accounting procedures to comply with the new rules?

A: **No***. The way you account for donor restrictions has not changed! With minimal exceptions, your chart of accounts has not changed. *Except for underwater endowments discussed later.





Net Asset Classification

Q: What about footnote disclosure for *net assets with donor restrictions* in our audit—do they change?

A: Yes—disclosures are “enhanced” to include how donor restrictions affect the use of resources (see following example).





2018

| | General Operating Fund | Capital Fund | Endowment Fund | Total |
|--|---------------------------|-----------------|-------------------|-----------------|
| Subject to expenditure for specific purpose: | | | | |
| Scouting activities | \$ X,XXX | \$ - | \$ - | \$ X,XXX |
| Learning for Life program | X,XXX | - | - | X,XXX |
| All Markets program | X,XXX | - | - | X,XXX |
| Marketing salary reimbursement | X,XXX | - | - | X,XXX |
| Designated donation from United Way | X,XXX | - | - | X,XXX |
| Building, equipment and maintenance | | | | |
| Pavillion at ABC Lodge | | X,XXX | | X,XXX |
| Smith Scout Ranch | | X,XXX | | X,XXX |
| Council service center | | X,XXX | | X,XXX |
| Capital campaign projects | | | | |
| Camp Jones | | X,XXX | | X,XXX |
| Smith Scout Ranch | | X,XXX | | X,XXX |
| Sawgrass Scout Camp | | X,XXX | | X,XXX |
| Total purpose restrictions | <u>X,XXX</u> | <u>X,XXX</u> | | <u>X,XXX</u> |
| Perpetual in nature | | | | |
| Capital improvement | | X,XXX | | X,XXX |
| Land use restrictions | | X,XXX | | X,XXX |
| Total perpetual in nature | <u>-</u> | <u>X,XXX</u> | <u>-</u> | <u>X,XXX</u> |
| Subject to the passage of time: | | | | |
| Community campaign donations | <u>X,XXX</u> | <u>-</u> | <u>-</u> | <u>X,XXX</u> |
| Endowment: | | | | |
| Subject to endowment spending policy and appropriation: | | | | |
| General use | - | - | X,XXX | X,XXX |
| Program activities | - | - | X,XXX | X,XXX |
| Total subject to endowment spending policy and appropriation | <u>-</u> | <u>-</u> | <u>X,XXX</u> | <u>X,XXX</u> |
| Subject to appropriation and expenditure when a specific event occurs: | | | | |
| Capital improvement projects | - | - | X,XXX | X,XXX |
| Program activities | - | - | X,XXX | X,XXX |
| Total subject to appropriation and expenditure when a specific event occurs | <u>-</u> | <u>-</u> | <u>X,XXX</u> | <u>X,XXX</u> |
| Total net assets with donor restrictions | <u>\$ X,XXX</u> | <u>\$ X,XXX</u> | <u>\$ X,XXX</u> | <u>\$ X,XXX</u> |





Net Asset Classification

Q: What about net asset *reclassifications*—any changes there?

A: Just a change in presentation in the Statement of Activities and Changes in Net Assets. We also added another account, 4502, Contributions – Other Direct – Purpose to delineate between time and purpose restrictions in Other Direct gifts.





| | | | | | | | | |
|--|-------------------|-------------------|------------------|------------------|------------------|------------------|-------------------|-------------------|
| Activities | 1,001,623 | 936,231 | 0 | 0 | 0 | 0 | 1,001,623 | 936,231 |
| Other revenue | 721,560 | 619,479 | 15,472 | 0 | 0 | 0 | 737,032 | 619,479 |
| Total revenue | 5,567,792 | 5,309,524 | 433,872 | 422,000 | 2,168,615 | (786,797) | 8,170,279 | 4,944,727 |
| Net assets released from restrictions: | | | | | | | | |
| Satisfaction of program restrictions | 213,098 | 433,618 | 174,850 | 289,131 | 0 | 0 | 387,948 | 722,749 |
| Expiration of time restrictions | 690,864 | 797,280 | 0 | 0 | 0 | 0 | 690,864 | 797,280 |
| Satisfaction of equipment acquisition restrictions | | | | | | | | |
| Appropriation from donor endowment and subsequent satisfaction of any related donor restrictions | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Total net assets released from restriction | 903,962 | 1,230,898 | 174,850 | 289,131 | 0 | 0 | 1,078,812 | 1,520,029 |
| Total support and revenue | 13,100,619 | 12,787,042 | 628,426 | 748,090 | 2,231,859 | -759,183 | 15,960,904 | 12,775,949 |
| Expenses: | | | | | | | | |
| Program services | 11,109,549 | 10,872,161 | 1,095,371 | 1,162,971 | 102,000 | 102,000 | 12,359,810 | 12,137,132 |
| Support services: | | | | | | | | |
| Fundraising | 624,757 | 606,284 | 25,257 | 26,027 | 6,000 | 6,000 | 656,013 | 638,311 |
| Management and general | 841,151 | 857,798 | 50,514 | 52,054 | 26,179 | 32,000 | 917,844 | 941,852 |
| Total support services | 1,465,907 | 1,464,082 | 75,770 | 78,081 | 32,179 | 38,000 | 1,573,857 | 1,580,163 |
| Total expenses | 12,575,457 | 12,336,243 | 1,171,141 | 1,241,052 | 134,179 | 140,000 | 13,933,667 | 13,717,295 |





Investment Return

- Now *required* to report investment return *net of external and direct internal investment expenses*.
- FASB believes will provide better comparability across all NFPs—regardless of whether investments managed internally, externally, or both—OR—whether the NFP invests in vehicles that have embedded fees (mutual funds, hedge funds, etc.).
- No longer requiring disclosure of netted fees will ease administrative burden/reduce costs.
- Still required to report separately on IRS Form 990.





Board Designations/Appropriations

- New ASU calls for “enhanced” disclosures about amounts and purposes of governing board designations, appropriations, and similar actions that result in self-imposed limits on the use of resources without donor-imposed restrictions as of the end of the period.
- FASB felt that, without such disclosure, financial statement users might make erroneous assumptions regarding net assets *available* to meet cash needs for general expenditures in the coming year.





Board Designations/Appropriations

NET ASSETS

Without donor restrictions

| | | | | | |
|-----------------------------------|---------|------------|-----------|------------|------------|
| Undesignated | 564,670 | (419,255) | - | 145,415 | 1,501,596 |
| Designated by board for endowment | - | - | 3,863,410 | 3,863,410 | 3,321,046 |
| Designated by board for capital | - | 800,000 | - | 800,000 | 800,000 |
| Board designated | - | 14,311,851 | - | 14,311,851 | 13,015,800 |
| Total without donor restrictions | 564,670 | 14,692,596 | 3,863,410 | 19,120,676 | 18,638,442 |

With donor restrictions

| | | | | | |
|-----------------------------------|-----------|------------|-----------|------------|------------|
| Perpetual in nature for operating | - | - | 992,633 | 992,633 | 976,073 |
| Perpetual in nature for capital | - | 151,000 | - | 151,000 | 166,000 |
| Purpose restrictions | 356,792 | 1,764,496 | 75,187 | 2,196,475 | 1,264,537 |
| Time restrictions | 1,807,026 | - | - | 1,807,026 | 2,090,606 |
| Total with donor restrictions | 2,163,818 | 1,915,496 | 1,067,820 | 5,147,134 | 4,497,216 |
| TOTAL NET ASSETS | 2,728,488 | 16,608,092 | 4,931,230 | 24,267,810 | 23,135,658 |

| | | | | | |
|----------------------------------|--------------|---------------|--------------|---------------|---------------|
| TOTAL LIABILITIES AND NET ASSETS | \$ 3,252,855 | \$ 21,781,932 | \$ 4,931,230 | \$ 29,966,017 | \$ 29,118,969 |
|----------------------------------|--------------|---------------|--------------|---------------|---------------|





Board Designations/Appropriations

Endowment net asset composition by type of fund as of December 31, 2017 consisted of the following:

| Description | Without Donor Restrictions | With Donor Restrictions | Total |
|---|----------------------------|-------------------------|--------------|
| Donor-restricted endowment funds perpetual in duration, original gift | \$ - | \$ 992,633 | \$ 992,633 |
| Donor-restricted endowment funds program services | - | 75,187 | 75,187 |
| Board-designated endowment funds | 3,863,410 | - | 3,863,410 |
| Board-designated capital funds | 800,000 | - | 800,000 |
| Donor-restricted capital funds | - | 300,000 | 300,000 |
| Donor-restricted capital funds perpetual in duration, original gift | - | 150,000 | 150,000 |
| Total endowment net assets | \$ 4,663,410 | \$ 1,517,820 | \$ 6,181,230 |





Board Designations/Appropriations— Preparing for Your Audit

- Inventory your board designations and appropriations.
- Transfers will require explanation in footnotes.
- Auditors will be paying special attention to board minutes—make sure they are complete/up-to-date.





Functional Expenses

- ASU 2016-14 requires all NFPs to present now (previously applied to just VH&W orgs).
- Not new to the BSA, however requirement to disclose method(s) of allocating *unallocated expenses* is new.
- Expect increased focus by auditors on allocation methods.





Functional Expenses— Preparation for Your Audit

- Review chart of accounts for proper set up of *class codes* (the last two digits in the chartfield string).
- Ensure that all pure program expenses are charged directly program activities (class codes 20, 21, 25)
- Ensure M&G exp. charged to class code 50





Functional Expenses— Preparation for Your Audit

- Ensure pure fundraising expenses are charged to class code 70.
- Unallocated expenses should be charged to class code 99.
- BSA has typically relied on the *Time Study* to allocate “99” expenses—make sure Time Study data is current and available.





Functional Expenses— Preparation for Your Audit

- Depending on the floor plan of the LC Service Center, Time Study may not accurately reflect occupancy costs, depreciation, office expense, interest (auditor may raise this).
- In some cases, allocation of the above best accomplished by Occupancy Study (based on square footage)—may prove advantageous.
- Crunch the numbers/compare.





Statement of Cash Flows

- For *Direct Method* preparers, ASU 2016-14 eliminates the reconciliation of changes in net assets to net cash provided(used) by operating activities.
- *Most councils unaffected by this provision of the new ASU.*





Underwater Endowments

- “Underwater” = FMV of underlying assets < original gift amount (or amount to be maintained by donor or law).
- ASU 2016-14 requires disclosures of (1) an NFP's policy, and any actions taken during the period, concerning appropriation from underwater endowment funds, (2) the aggregate fair value of such funds, (3) the aggregate of the original gift amounts (or level required by donor or law) to be maintained, and (4) the aggregate amount by which funds are underwater (deficiencies), which are to be classified as part of net assets *with* donor restrictions.





Gifts of PP&E

- Or gifts of cash to acquire or construct PP&E
- Used to be able to release restrictions over the useful life of the asset.
- Now must release when “placed in service”.
- Requires adjustment to fully reclassify as of Jan. 1, 2018





NFP Tax Matters 2018

TCJA Creates Issues for Local
Councils/Employees



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Moving Expenses

- Prior to 2018, deductible by employees for work-related move 50 miles or more from previous work place—reimbursable by employers tax-free to employees.
- TCJA suspended from 2018 through 2025.
- **Breaking news—in *Notice 2018-75 (9/21/2018)*, IRS will allow employers to reimburse employees tax-free (in 2018) for qualified moving expenses incurred in a prior year.**
- **Also OK if employer pays moving company in 2018 for employee's qualified moving expenses incurred prior to 2018.**





Unreimbursed Employee Expenses

- Prior to 2018, employees could deduct (on Sch A, >2% AGI) certain job-related expenses not reimbursed by their employer including:
 - Job-related mileage
 - Long-distance travel expenses
 - Continuing education expenses required for current job
 - Work-related dues/subscriptions
 - Uniforms/work clothes
 - Home computer used for work
- TCJS suspended from 2018 through 2025
- *However*, above are reimbursable tax-free using accountable plan.





Potential Unrelated Business Taxable Income (“UBTI”) **On Certain Employee Benefits**

- Previously tax-free to employees, now taxable:
 - Expenses paid by a nonprofit organization that would be considered qualified transportation fringe benefits (such as bus passes, van pools, parking passes/reimbursements, and bicycle commuting reimbursements).
 - Expenses associated with any parking facility used to provide employee parking (the “parking lot tax”).
 - Expenses associated with an on-premises athletic facility.
- Options:
 - Include value in employee W-2s
 - File Form 990-T and pay UBIT (if value >\$1,000)





Potential Unrelated Business Income Tax (“UBIT”) On Councils with Multiple “Businesses”

- **Previously**—a nonprofit that operated multiple unrelated businesses could deduct the losses from one business from the profits from another to determine the amount of net unrelated business income subject to UBIT.
- **Now**—losses from one unrelated business cannot offset profits from another unrelated business in determination of unrelated business taxable income. As a result, it’s likely that more nonprofits will have to pay UBIT.





Resources Available to Local Councils

- *Local Council Guide to the 2018 Audit*
 - *Illustrative financial statements, footnotes and implementation guidance*
 - *This year will include downloadable sample footnotes (MS Word format)*
 - *Available in December 2018*
- *Local Council Guide to the 2018 IRS Form 990*
 - *Sample returns and checklists for local councils and trust funds*
 - *Updated for TCJA*
 - *Available March 2019*





Resources Available to Local Councils

<https://www.scouting.org/council-support/finance-impact/council-fiscal-management/document-library/>

Or— Google “Finance Impact BSA” and click “Fiscal Documents”

BSA Member Care (972) 580-2489

Ken.moran@scouting.org





Thank you!



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