Financial Accounting Standards Board Issues NEW accounting guidance for Contributions Received & Contributions Made

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Over the years there has been a lot of confusion about whether to treat certain types of transactions as contributions or as exchange transactions especially when it involves government grants. There has been further confusion if the transactions include donor-imposed dictates called restrictions or conditions. Many people including accountants don't always know the difference between a restriction or condition and how to treat a transaction that has one or the other or both elements.

The correct treatment of transactions as exchange transactions or contributions, and then as contributions with donor-imposed conditions or restrictions can have a significant impact on the timing of recognizing revenue which is extremely important for accurate financial reporting and comparability. So proper treatment of these transactions is imperative.

Although this update does not make any fundamental changes to the existing rules for how to treat contributions and exchange transactions, it aims to clarify the meaning of these terms and provide more succinct guidance for determining which classification to apply for reporting purposes. It also aims to clearly define and qualify what a donor-imposed condition is and how it is accounted for and how a donor-imposed condition differs from a donor-imposed restriction.

It is believed that the amendments in this update will likely result in more grants and contracts being accounted for as either unconditional or conditional contributions instead of exchange transactions.

In addition to providing clearer definitions and examples of how to treat cash and other resources received and paid through grants and contracts, the update suggests a methodology for determining the proper classification and treatment of these type of transactions. The methodology involves a step-down approach as follows:

1. Has the resource provider (e.g. Not-For-Profit entity) received commensurate value in return for the resources transferred? If Yes, then the transaction is an Exchange Transaction and one must follow the appropriate accounting rules for Exchange Transactions. If no, go to #2.

2. Is the transaction a nonreciprocal transaction (i.e. Contribution)? If Yes, follow contribution (non-exchange) accounting rules and go to #3.

3. Determine if there is a donor-imposed condition or conditions (i.e. a barrier). If yes, only recognize revenue when the condition or conditions are met. If no, then go to #4.

4. If it is determined that there are no donor-imposed conditions the transaction is deemed an unconditional contribution and a determination must be made if there are donor-imposed restrictions. Then depending on whether there are or aren't donor-imposed restrictions, recognize revenue as either contributions with or without donor restrictions.

The update provides the following definitions or clarifications:

Exchange Transaction – Reciprocal transfers in which each party receives and sacrifices approximately commensurate value

Conditional Contribution – A contribution with a donor/contributor/grantor 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/contributor a right of return of the assets it has transferred or gives the promisor a right of release from its obligation to transfer its assets.

Unconditional Contribution – A transfer of cash or other assets, as well as promises to give, with no donor-imposed conditions, to an entity or a reduction, settlement, or cancellation of its liabilities in a voluntary nonreciprocal transfer by another entity acting other than as an owner.

Conditional Contributions

May times it is difficult to ascertain whether a donor-imposed condition exists. A thorough reading of the agreement or other referenced document must be made to determine if a barrier exists. The update states very clearly that a donor-imposed condition must have both:

a) One or more barriers that must be overcome before a recipient is entitled to the assets transferred or promised **AND**

b) A right of return to the contributor for assets transferred (or the reduction, settlement, or cancellation of liabilities) or a right of release of the promisor from its obligation to transfer assets (or reduce, settle or cancel liabilities).

If only one of these two elements exist then the contribution will not be deemed conditional. Furthermore, it is important to note that a probability assessment about whether the recipient is likely to meet the stipulation is not a factor in determining if a barrier exists and whether the contribution is conditional. In those cases where it isn't clear whether the stipulation is unconditional (and no further information is available) then the contribution shall be considered conditional.

The update provides many examples of what defines a barrier or condition such as when:

- A measurable performance (e.g. level of service, number of output units, specific outcome or milestones) must be obtained or obtained within a specified time frame.
- An identified event occurs (e.g. receiving matching funds, receiving governmental approval)
- Recipient has limited discretion on activities such as incurring qualifying expenses (e.g. first expending funds) or hiring specific individuals.

It also states clearly that administrative and trivial stipulations are not indicative of a barrier such as a requirement to provide an annual report or report summarizing recipient's performance of terms of the contribution/grant. As such, these stipulations will not cause the transaction to be conditional.

Cash or other assets received as a conditional contribution will be accounted for as a refundable advance until the conditions have been substantially met or waived by the donor. Conditional promises to give which contain a donor-imposed condition (i.e. barrier) that must be overcome shall be recognized when the condition or conditions are substantially met.

Government Grants or Contracts

Whether to treat resources received from a federal, state, city or other governmental agency as a contribution or as an exchange transaction has been one of the more perplexing challenges faced by accountants over the years. This update attempts to resolve the issue by requiring that a determination first be made of who is the ultimate customer or benefactor of the resources. In many cases the ultimate customer or benefactor is not the government but the general public and as such the transaction is between the recipient of the resources (i.e. the Not-For-Profit entity) and the general public. The government agency in many cases is merely an agent or third-party payer.

Once the true beneficiary of the resources is determined, it has to be determined whether the transfer of assets will be benefiting the general public or part of an existing exchange transaction between a recipient and an identified customer.

If it is determined that the transaction is furthering the Not-For-Profit entity mission and benefiting the public then the transaction will be treated as an unconditional or conditional contribution.

If it is determined that the transaction is between the Not-For-Profit and an identified customer (and not the government who is just a funds transfer agent) then the transaction will be treated as an exchange transaction. The update provides some examples of these transactions such as payments received under Medicare and Medicaid programs, provisions of health care or education services by a government for its employees, and Pell Grants or similar state or local government tuition assistance programs.

Effective Date

For most entities the that are resource recipients the effective date for applying the amendments of this update will be for annual periods beginning after **December 15. 2018**. For either a public business entity or a Not-For-Profit that has issued, or is a conduit bond obligor for, securities that are traded, listed or quoted on an exchange or an over-the-counter market the effective date will be periods beginning after **June 15, 2018**.