ACCOUNTING UPDATE FOR NOT-FOR-PROFIT ENTITIES: REVENUE RECOGNITION

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Overview

In May 2014, the Financial Accounting Standards Board (FASB) released Accounting Standards Update (ASU) 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The ASU and its subsequent amendments supersede almost all revenue recognition requirements under accounting principles generally accepted in the United States (U.S. GAAP), including industry-specific guidance.

Does Recognition of Contributions Change?

Contributions are excluded from the scope of Topic 606. However, the determination of what is an exchange transaction (reciprocal transaction) and what is a contribution, which remains within the scope of Subtopic 958-605, *Not-for-Profit Entities – Revenue Recognition*, is now more important than ever. To assist entities in this evaluation, FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made (Topic 958)*, which provides guidance for determining what is an exchange transaction versus a contribution and whether a contribution is conditional.

REVENUE FROM CONTRACTS WITH CUSTOMERS

Five-Step Process

The core principle of Topic 606 is that an entity should recognize revenue to depict the transfer of goods or services to customers in an amount to which the entity expects to be entitled in exchange for those goods or services. Topic 606 states an entity should follow these five steps to recognize revenue:

Step 1: Identify the Contract With a Customer

An entity needs to determine whether there is an explicit or implied contract regarding the transfer of goods or services to a customer, which would be considered an exchange transaction.

Step 2: Identify the Performance Obligations in the Contract

A performance obligation is a promise in a contract to transfer a good or service to the customer. If multiple performance obligations exist in a contract, then revenue is recognized separately for each if they are distinct, which means they can provide benefit on their own or together with other readily available resources and they are distinct within the context of the contract.

Step 3: Determine the Transaction Price

The transaction price is the amount of consideration to which an entity expects to be entitled for the goods or services provided. For not-for-profit entities, the value from the goods or services provided may be less than the amount of consideration. The difference is a contribution, accounted for separately under Subtopic 958-605.

Step 4: Allocate the Transaction Price

When a contract has multiple performance obligations, the transaction price must be allocated based on the actual or estimated stand-alone selling price of each. If the stand-alone selling prices exceed the transaction price, the transaction price is allocated using a relative stand-alone selling price basis.

Step 5: Recognize the Revenue When the Entity Satisfies a Performance Obligation

Revenue is recognized as the performance obligations are satisfied. Revenue may be recognized at a point in time or over time.

Museum Examples

Step 1: An individual purchases a membership to a museum for $200. A contract is established as specified goods or services have been promised to the individual in return for payment based on the stated price of the membership.

Step 2: The membership provides free admission to the museum 12 times over one year, a 10% discount on all purchases at the museum store, and free attendance at the exhibit opening event. The museum determines these represent three separate performance obligations.

Step 3: The transaction price for the membership is $200.

Step 4: The museum needs to allocate the $200 membership price to the three performance obligations.

MUSEUM ADMISSION	STORE DISCOUNT	OPENING EVENT	CONTRIBUTION
Non-members pay $10 per admission. Thus, the stand-alone selling price for 12 admissions is $120.	There is no stand-alone selling price. The museum estimates the stand-alone selling price as $20, based on sales data per admission.	Non-members pay $35 to attend the opening event. Thus, the stand-alone selling price is $35.	The consideration received exceeds the value of the goods and services provided. The remaining $25 is a contribution.

In the above example, if non-members paid $100 to attend the opening event, the stand-alone selling prices would total $240, and there would be no contribution. The price would instead be allocated based on the relative stand-alone selling prices.

Step 5: Admission to the museum and the store discount may be used at any time over one year. Thus, the museum determined that the $100 for admission and $20 for the store discount should be allocated evenly over one year. The opening event occurs in November of each year. Thus, $35 would be recognized in November, regardless of whether the member attends the event.

Disclosure Requirements

In many cases, entities may not see significant changes in the pattern of revenue recognition. However, almost every entity will see expanded disclosures. The objectives of the additional disclosures are to provide users an understanding of the nature, amount, timing, and uncertainty of the entity's revenues and related cash flows.

EFFECTIVE DATES

ENTITY TYPE	EFFECTIVE DATE
Not-for-profit entity 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	Fiscal years beginning after Dec. 15, 2017
All other not-for-profit entities	Fiscal years beginning after Dec. 15, 2018

Early adoption of Accounting Standards Codification® 606 is permitted for all entities.

CONTRIBUTIONS RECEIVED AND CONTRIBUTIONS MADE

FASB issued ASU 2018-08, *Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made (Topic 958)* to address diversity in practice when classifying grants and similar contracts with resource providers as either exchange transactions or contributions and to address whether a contribution is conditional or unconditional.

Distinguishing Contributions From Exchange Transactions

The primary question is who receives the benefit of the transaction. If a resource provider is receiving commensurate value, then the transaction is an exchange transaction. Reciprocal transactions are accounted for as exchange transactions within the scope of Topic 606 while nonreciprocal transactions are considered contributions. Nonreciprocal transactions include transactions in which the beneficiary is the general public.

Conditional Versus Unconditional Contributions

Once the not-for-profit entity has determined the transaction is a contribution, the next step is to determine whether the contribution is conditional or unconditional. A contribution is considered conditional under ASU 2018-08 if the agreement includes a *barrier* that must be overcome and either a *right of return* of the assets transferred or a *right of release* of a promisor's obligation to transfer assets. Conditional contributions will be recognized as revenue as the conditions are met. If the contribution is considered unconditional, it is recognized into revenue immediately.

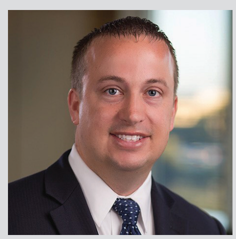
EFFECTIVE DATES

ENTITY TYPE (Resource Recipients)	EFFECTIVE DATE
Not-for-profit entity 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	Fiscal years beginning after Jun. 15, 2018
All other not-for-profit entities	Fiscal years beginning after Dec. 15, 2018

Early adoption of ASU 2018-08 is permitted for all entities.

Questions?

Contact a member of our Not-for-Profit team below.



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