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THE PPC
NONPROFIT UPDATE

SEPTEMBER 2019, VOLUME 26, NO. 9

# FASB Staff Q&A on Grant Agreements—Part 2

In June 2018, the FASB issued ASU 2018-08, *Not-for-Profit Entities (Topic 958): Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made*. As discussed in Part 1 of this article published in the August 2019 issue of *The PPC Nonprofit Update*, in June 2019, the FASB issued Staff Q&A, *Subtopic 958-605, Application of the Limited Discretion Indicator and Accounting for Cost-Sharing Provisions in a Grant Agreement*, to address a few issues relating to implementation of ASU 2018-08. Subtopic 958-605, *Not-for-Profit Entities—Revenue Recognition*, provides guidance for entities when determining whether a contribution is conditional, including indicators that help an entity assess whether an agreement contains a barrier to entitlement. Stakeholders indicated that additional guidance might be useful in the areas of the *limited discretion indicator* discussed in the August 2019 issue, as well as *cost-sharing provisions*, which are the subject of this article.

## Cost-sharing Provisions

A cost-sharing provision is a provision in an agreement where the grantee must use a certain amount of funds that are not from the grantor toward a program or project in order to be entitled to the granted funds. When entitlement to the grant funds is clearly contingent on the recipient meeting a cost-sharing requirement, the cost-sharing provision should be considered a barrier. Whether or not a recipient is likely to meet the cost-sharing requirement should not be considered as a factor in determining whether a barrier to entitlement exists. As indicated in FASB ASC 958-605-25-5C, a probability assessment is not a factor that should be used in the determination.

The wide variety and types of cost-sharing provisions may or may not make it appropriate to analogize the challenge

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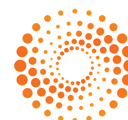

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grant example in Subtopic 958-605 with cost-sharing requirements. An analysis of the specific requirements of the grant agreement is needed to determine—

1. Whether the grant requires raising incremental funds from another source, which is a matching provision, or only spending resources other than resources from the provided grant, which is a cost-sharing provision;
2. Whether entitlement is dependent on meeting that requirement, which indicates that a barrier to entitlement exists; and
3. The appropriate timing and pattern of revenue recognition as required from the provision.

The wording used in the agreement needs to be carefully reviewed to make the determination.

The Q&A provides two scenarios to show how, depending on the specifics of a cost-sharing provision in an agreement, that it may or may not be appropriate to defer the revenue and timing of recognition, as indicated by analogizing to the matching example.

### Practical Consideration:

The FASB Staff Q&A is available at **www.fasb.org/cs/Satellite?c=FASBContent_C&cid=1176172813997&d=Touch&pagename=FASB%2FFASBContent_C%2FGeneralContentDisplay**.

# 2019 Compliance Supplement Released

On July 1, 2019, the Office of Management and Budget (OMB) released the 2019 Compliance Supplement. Unlike the 2018 Compliance Supplement, which was referred to by some as a "Skinny" Supplement (because it only modified sections of the 2017 Compliance Supplement that were in need of significant revisions), the 2019 Compliance Supplement is a stand-alone document that has over 1,600 pages. The 2019 Supplement is effective for audits of fiscal years beginning after June 30, 2018 and supersedes the 2018 and 2017 Compliance Supplements. Unlike last year's Compliance Supplement, this means auditors should only use the 2019 Compliance Supplement for audits of fiscal years beginning after June 30, 2018.

### Practical Consideration:

*PPC's SMART Practice Aids—Single Audit Suite* automates the process of building compliance audit programs from the Compliance Supplement for the programs selected as major programs. It allows the auditor to plan and execute the single audit engagement from beginning to end—including preparation and electronic sign-off of practice aids, federal award audit programs, and compliance audit programs. In addition, it automates the process of determining major programs; low-risk auditee status; and appropriate compliance requirements, objectives, and audit procedures; and prepares the compliance audit program and schedule of expenditures of federal awards (SEFA). Information about other additional features, including automated roll forward from year to year and a federal award import feature, is available by calling (800) 431-9025 or visiting **tax.thomsonreuters.com**.

## Highlights

The changes to the 2019 Compliance Supplement are much more significant than those in the 2018 Compliance Supplement. Appendix V lists the changes from the 2018 and 2017 Compliance Supplement in detail. The following paragraphs highlights some of these changes.

**Limitation of the Number of Compliance Requirements.** One of the most significant changes to the 2019 Compliance Supplement was the limitation of number of compliance requirements Federal agencies could identify as being subject to the compliance audit. In order to reduce the burden on the recipient in accordance with the President's Management Agenda, each federal agency was mandated to limit the number of compliance requirements subject to the audit to six compliance requirements, except for the Research and Development cluster, which was permitted to identify seven compliance requirements as subject to the audit. To get to the six requirements subject to the audit, the requirements relating to A. Activities Allowed and Unallowed and B. Allowable Costs and Cost Principles are treated as one requirement. Many auditors are referring to this new approach in the Compliance Supplement as the six-requirement mandate or Pick Six.

Part 2 of the Compliance Supplement, the Matrix, has been revised to reflect this change for all programs, as well as the related program sections in Parts 4 and 5. Under the new guidelines, a program with a "Y" in the Part 2 matrix means that the compliance requirement is subject to the audit for the program. (Previously, a "Y" in the matrix meant that the compliance requirement applied to the program.) The auditor will still have to determine whether the requirements could have a direct and material effect on the program. A program with an "N" in the Part 2 matrix means that type of compliance requirement is not subject to the audit for the program, and the auditor is not expected to test the requirement. (Previously, an "N" in the matric meant that the compliance requirement normally did not apply to the program.)

**Federal Programs Not Included in the Compliance Supplement.** Auditors should note that the six-requirement mandate does not apply to programs not included in the Compliance Supplement. Auditors should continue to use the Part 7 guidance to identify the compliance requirements that are applicable to the program, and then determine which of the applicable compliance requirements could have a direct and material to the program. As a result, auditors will often end up having to test more than six compliance requirements for programs that are not included in the Supplement.

**Safe Harbor Status and Other Requirements.** Auditors should carefully review the guidance and changes in Part 1 of the Compliance Supplement about the safe harbor status and responsibility for updating compliance requirements. The safe harbor guidance was updated to reflect the new definitions of "Y" (subject to audit) and "N" (not subject to audit). It also emphasizes the auditor's responsibilities for compliance under GAAS and the Yellow Book. It indicates that a requirement may not be subject to the audit for compliance audit purposes, but auditors have a responsibility under GAAS and the Yellow Book related to noncompliance with the provisions of laws, regulations, contracts, and grant agreements that may have a material effect of the financial statements and with requirements relating to the auditor's consideration of fraud and abuse.

**Spotlight on the Student Financial Assistance Cluster.** The single audit requirements for student financial assistance (SFA) programs are included in Part 5—Cluster of Programs. The 2019 Compliance Supplement contains the following changes for the SFA cluster:

- Removal of the Federal Perkins Loan Program. This program was discontinued by the Department of Education and disbursements are not permitted after June 30, 2018.
- New reporting requirements for Pell grants and Direct Loan programs related to the audit sample.
- Added requirements in Compliance Requirement N—Special Tests and Provisions related to (1) excess cash, (2) general program eligibility, (3) distance education programs, and (4) student information security [Gramm-Leach-Bliley Act (GLBA)]. The GLBA-related steps include determining if the institution designated an individual to coordinate the information security program, performed a risk assessment that addresses certain areas in the regulations, and documented safeguards for identified risks.
- Removed requirement in Compliance Requirement N—Special Tests and Provisions related to (1) Federal Work Study agreements, (2) zone alternative testing, and (3) consortium agreements.

**Internal Controls.** The guidance for Internal Controls is included in Part 6 of the Compliance Supplement. The 2019 Compliance Supplement includes updated discussions that focus on entity-wide controls over compliance, and added appendixes that have illustrations of internal controls over federal awards and internal controls specific to each time of compliance requirement.

**Other Changes.** Other changes include the following:

- Part 2—The Matrix of Compliance Requirements highlights the changes in compliance requirements.
- Part 3—Compliance Requirement I, Procurement and Suspension and Debarment, included in Part 3.2 was updated to provide additional information on the National Defense Authorization Acts (NDAA) and audit findings.
- Part 4—Agency and Requirements was updated to reflect changes in program titles, adding new programs, statutory requirements, and references; and to make technical changes and corrections.
- Appendix VII—Other Audit Advisories was updated on several topics.

### Practical Consideration:

The 2019 Compliance Supplement is available on the OMB's website at **www.whitehouse.gov/wp-content/uploads/2019/07/2-CFR_Part-200_Appendix-XI_Compliance-Supplement_2019_FINAL_07.01.19.pdf**. Additionally, the AICPA's Governmental Audit Quality Center (GAQC) presents the 2019 Compliance Supplement by individual section at **www.aicpa.org/interestareas/governmentalauditquality/resources/singleaudit/2019-omb-compliance-supplement.html**.

# Taxpayer First Act Impact on Exempt Organizations

The Taxpayer First Act (Act), signed into law by President Trump on July 1, 2019, makes changes to the management and oversight of the IRS to improve customer service, assist taxpayers with appeals, modify the IRS's organization, and provide additional safeguards to taxpayers in their interactions with the IRS. The Act includes some specific provisions affecting exempt organizations (EOs), which are the subject of this article.

## All EOs Subject to Mandatory Electronic Filing

While perhaps a burden to initially comply with the requirement, electronic filing provides benefits to taxpayers as well as the IRS—typically by providing for faster and more accurate returns. Electronically filed returns—

- are processed upon receipt and are acknowledged by the IRS within 24 hours;
- provide built-in accuracy checks, embedded in electronic return preparation software, that reduce taxpayer errors before the return is submitted;
- eliminate the need for EOs to make copies and assemble forms/schedules/attachments; and
- enable an EO to comply with the public disclosure requirements more easily by posting electronic forms on the web.

**Old Law.** Only certain EOs were required to electronically file their annual information returns—generally the largest and smallest organizations. Tax exempt corporations with assets of $10 million or more and that filed at least 250 returns (each Form W-2, 1099-MISC, and 941 is considered a separate return) during a calendar year were required to electronically file their Form 990 information returns [Reg. 301.6011-5 and Reg. 301.6033-4(a)]. To determine if the organization met the $10 million asset test, the amount on Form 990, Part X, line 16 (total assets), column (B) was used. Small organizations that filed Form 990-N (e-Postcard) were required to file electronically. Private foundations and charitable trusts, regardless of asset size, that filed at least 250 returns during a calendar year were required to electronically file [Reg. 301.6033-4(a)].

**New Law.** The Act extends the requirement to electronically file (e-file) to all EOs required to file statements or returns in the Form 990 series or Form 8872 (Political Organization Report of Contributions and Expenditures) [IRC Sec. 6033(n)]. Form 990-T must also be electronically filed.

## IRS to Make Tax Forms Available in a Machine-readable Format

**Old Law.** To request to inspect or obtain a copy of a return, report, notice, or an exemption application from the IRS, Form 4506-A (Request for Public Inspection or Copy of Exempt or Political Organization IRS Form) was filed. The IRS could provide copies of EO returns on a DVD. There was no requirement to make the returns available in a machine-readable format.

**New Law.** The Act requires the IRS to make the information provided on the e-filed returns available to the public as soon as practicable in a machine-readable format [IRC Sec. 6104(b)]. Providing access to the returns should be consistent with the disclosure rules of IRC Sec. 6104. Therefore, the names and addresses of contributors are not required to be disclosed unless the organization is a private foundation or a Section 527 political organization.

## Effective Date and Transitional Relief

The requirements listed previously are generally effective for tax years beginning after July 1, 2019. However, transitional relief is provided for certain *small organizations*, extending the effective date to the tax year beginning on or after July 1, 2021 (i.e., two years). A *small organization* must have gross receipts of less than $200,000 for the tax year, and aggregate gross assets of less than $500,000 at the end of the tax year. In addition, the IRS may delay, at their discretion, the effective date by two years for other organizations if the requirement to e-file will impose an undue hardship. The IRS also has the discretion to delay the effective date for filing Form 990-T electronically to tax years beginning no later than July 1, 2021 [IRC Sec. 6011(h)].

## IRS to Notify Organizations that Failed to File for Two Consecutive Years

**Old Law.** Charities and other nonprofits automatically lost their tax-exempt status for not filing annual information returns—including the postcard return for very small organizations—for three consecutive years. Once revoked, the organization was required to reapply for exempt status [IRC Sec. 6033(j)]. This law has resulted in many organizations having their tax-exempt status automatically revoked, and viable organizations had to reapply to obtain exempt status.

**New Law.** The Act requires that the IRS provide notice to an organization that fails to file a Form 990-series return or postcard for two consecutive years. The notice

must state that the IRS has no record of having received such a return or postcard from the organization for two consecutive years and inform the organization that the organization's tax-exempt status will be revoked if the organization fails to file a return or postcard by the due date for the next return or postcard. The notice must also contain information about how to comply with the annual information return and postcard requirements [IRC Sec. 6033(j)(1)].

**Effective Date.** The amendment made by this section applies to failures to file returns or notices for two consecutive years if the return or notice for the second year is required to be filed after December 31, 2019.

# Effective Board Meeting Minutes

Most state nonprofit corporation statutes establish the minimum number of member and board of directors' meetings that the organization must hold per year. However, the needs of the organization and best practices often dictate that the organization hold meetings more frequently than the statute requires. At a minimum, the members should meet annually, and the board of directors should meet at least twice per year.

A board of directors cannot operate informally. Action on behalf of the organization may only be taken by the board through a properly determined method (i.e., at a board meeting or by a board-designated committee). Since others must implement the board's decisions, the board must keep formal records of its decisions, commonly referred to as minutes. Minutes should reflect all the elements necessary to prove that the meeting conformed to all the legal requirements for a meeting.

The legal requirements for a proper board meeting are found in the state nonprofit corporation statute and the organization's articles of incorporation and bylaws. Legal requirements include the following:

- Only designated persons (typically the chairperson) may call a meeting. Sometimes, the bylaws will dictate the date, time, and place for regular meetings. Note that failure to adhere to the date, time, or place as dictated by the bylaws has been deemed by the IRS to be a failure of the operational test.
- Each director is entitled to the notice of the meeting in a manner approved by the state nonprofit corporation act as implemented by the organization's bylaws. Some state nonprofit corporation statutes do not allow for notice by email or other electronic communication.
- The chairperson must call the meeting to order with a quorum (usually determined in the bylaws) present.

Most state nonprofit corporation statutes allow members or directors to adopt resolutions by executing unanimous written consents. These consents have the same effect as an actual meeting and should be included with the organization's minutes. The key is that each member or director must agree to the actions.

The minutes should reflect all items presented to the board during the meeting and also include—

- a copy of the notice of the meeting;
- the meeting's date, time, and place;
- the names of all persons present at the meeting (directors and guests);
- the time and place where the meeting was called to order by the chairperson and whether a quorum was present;
- an exact transcription of a resolution's motion, who made the motion and the second;
- the means and outcome of the resolution vote; and
- any resolutions adopted by unanimous written consent.

A board meeting should be a place of healthy discussion of the organization and its various issues. Many discussions may take place prior to a board drafting a resolution for consideration by the board. Minutes should not reflect all of the discussions that occur during the board meetings. Because an organization is not attempting to document discussions verbatim, it is generally not advised that board meetings be recorded. Minutes should reflect the decisions of the board. Types of decisions that should be documented in the minutes include—

a. resignation of officers or directors;
b. termination of officers or directors;
c. appointment of additional officers or directors or appointment of officers or directors to fill vacancies;
d. change of corporate name;
e. adoption of any amendments to the bylaws;
f. change of corporate registered office or registered agent;
g. execution of major contracts;
h. purchase, sale, or lease of real property;
i. change of bank account or signatures on existing accounts;
j. loan or borrowing of money;
k. annual budget and adjustments, if any;
l. adoption of health or accident plan;
m. adoption of medical reimbursement plan;
n. major purchase or sale of corporate assets;
o. employment contracts;
p. salaries and bonuses of officers and key employees;
q. dissolutions and mergers; and

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r. any other significant corporate activity that is not in the ordinary course of business.

This list is not all-inclusive. The minutes should contain any item that the board of directors determines is significant. An organization may have legal counsel: (1) draft a template that may be used to easily gather the necessary information, and/or (2) review the minutes prior to officially adopting them to ensure that all items have been properly reflected.

## Documentation and Director Liability

An organization must keep current records. A significant advantage of a corporation is that it offers protection to its members who are not otherwise personally liable for corporate obligations. To aid in providing liability protection for directors, the minutes should be prepared shortly after the meeting and the board should approve the minutes promptly after the meeting. The IRS considers board meetings to be contemporaneously documented when the secretary presents the minutes by the latest of the next board meeting or sixty days after the meeting occurred.

Properly executed and approved minutes should be maintained in a secure central location (i.e., a part of the organization's offices). Many organizations maintain a corporate minutes book. Minutes may be maintained electronically as long as a common program is used and the software will track access and prevent changes to approved minutes. Often, the corporate secretary is an organization volunteer. A well-defined process for securing the minutes will allow for an easier transition between secretaries as well as prevent minutes from being inadvertently lost or disposed.

Both voting "no" and abstaining should be reflected in the minutes. If a director does not agree with a decision, it is in his or her best interest to have the minutes reflect the dissent. This is especially true in votes concerning transactions with disqualified persons. Agreement with decisions later ruled to be unreasonable that involve disqualified persons can result in a penalty being assessed on the decision makers.

### Practical Consideration:

The IRS is interested in whether an organization is documenting the decisions of the board. Consequently, Form 990, Part VI, includes a question as to whether or not the organization contemporaneously documents the meetings of the governing body and/or any committee with the authority to act on behalf of the governing body.

# Tax Brief

**NOTICE TO OPERATE AS A SECTION 501(c)(4) ORGANIZATION.** The Treasury recently issued final regulations (T. D. 9873), removing temporary regulations under IRC Sec. 506 that were effective July 8, 2016. The temporary regulations provided that the notification must be submitted on Form 8976 [Notice of Intent to Operate Under Section 501(c)(4)] no later than 60 days after the organization is established. Rev. Proc. 2016-41 (2016-30 IRB 165) provided additional information on the process for submitting the form and for requesting relief if not timely filed. The final regulations adopt without substantive change the temporary regulations. For clarity and continuity, the final regulations apply on and after July 8, 2016.