NONPROFIT ADVISOR
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WINDES NONPROFIT ADVISOR

The Windes Nonprofit Advisor is a periodic technical publication focusing on the tax, regulatory, and accounting issues that nonprofit organizations routinely confront.

The Windes Nonprofit Group possesses extensive experience in preparing and reviewing more than 150 Forms 990, 990-T, 990-PF, and state tax-exempt forms, in addition to having experience in the preparation and filing of both federal and state tax exemption applications for public charities, private foundations, and other exempt organizations. Furthermore, we can assist in providing valuable guidance (governance / reasonable compensation documentation / public support test / special events / lobbying / transactions with related parties) to nonprofit organizations.

The Windes Nonprofit Group prepares audited financial statements and ERISA audits for more than 100 nonprofit organizations. For retirement plans, Windes has experts on staff for 403(b) plan administration and compliance, including plan document issues, Form 5500 preparation and filing, non-discrimination testing, and government compliance programs.

Our Nonprofit Group is composed of the following individuals who are dedicated to providing nonprofit organizations with high-level tax, regulatory and accounting consulting, tax compliance services, and financial statement audit and assurance services:

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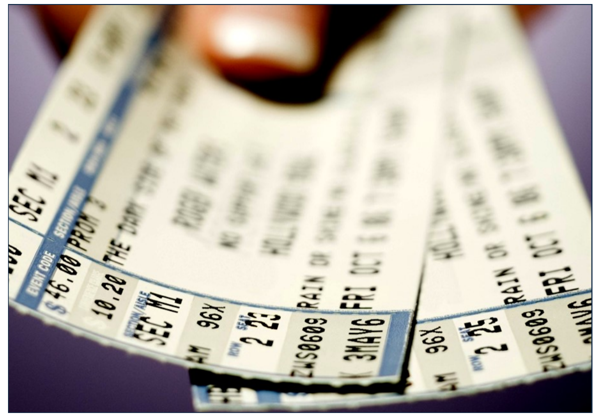
Please do not hesitate to contact any member of the Windes Nonprofit Group toll free at **844.4WINDES** (844.494.6337) or via email at nonprofit@windes.com.

Fringe Benefits and UBTI: What Nonprofits Need to Know



Under the 2017 Tax Cuts and Jobs Act (TCJA), Congress imposed an unrelated business income tax on certain fringe benefits a nonprofit employer might provide to its employees. Nonprofit employers that exclude certain fringe benefit amounts from taxable employee compensation will be required to report the amount as unrelated business taxable income (UBTI). The inclusion of these benefits as UBTI could lead to a required Form 990-T filing and tax liability for organizations that previously had no such filing requirement.

QUALIFIED TRANSPORTATION BENEFITS

An employer cannot deduct the expenses for providing qualified transportation benefits under the new tax law. These benefits include commuter transportation benefits, transit passes and any qualified bicycle commuting reimbursement. A nonprofit organization can avoid the addition of these items to UBTI if it provides the benefits as taxable compensation to the employees and includes the cost of the benefits on employees' Forms W-2.

QUALFIED PARKING BENEFITS

Qualified parking benefit deductions are also disallowed under the new tax law. These benefits include parking provided to an employee on or near the business premises of the employer, or on or near a location from which the employee commutes to work by transportation. If a nonprofit organization treats the benefits as taxable wages, it is not required to include the benefits in UBTI and pay tax on them, but the organization will incur additional payroll taxes.

ON-PREMISES ATHLETIC FACILITY

While the new tax law states that UBTI should increase by employee use of on-premises athletic facilities, the expanded definition of UBTI under IRS code section 512(a)(7) does not include these types of benefits. Although such benefits are not yet UBTI, it is possible that future provisions of the law may make these benefits taxable. These benefits include expenses paid for use of athletic facilities located on property that the organization owns or leases.

ENTERTAINMENT EXPENSES

Section 13304 of TCJA disallows the deduction of certain entertainment expenses that are not "directly related to" or "associated with" the tax-exempt organization's trade or business. Entertainment expenses are considered to be "directly related to" the business when:

- the main purpose of the combined business and entertainment is the active conduct of business,
- the organization engages in business during the entertainment period,
- the organization has more than a general expectation of getting income or some other specific business benefit at some future time, and
- the entertainment takes place in a clear business setting.

Entertainment is considered to be “associated with” the organization's trade or business if there is a clear business purpose for the expenditure, such as to get new business or to encourage the continuation of an existing business relationship.

GENERAL BUSINESS CREDITS

Unrelated business income tax is reduced by any applicable tax credits, including the general business credits. The new tax law created a general business credit equal to 12.5% of wages paid to qualifying employees who are on family or medical leave. To be eligible, the organization must have a written policy allowing full-time employees two weeks of annual leave (and part-time employees a pro-rata amount) with at least 50% of normal wages. For an employer claiming a credit for wages paid to an employee in 2018, the employee must not have earned more than $72,000 in 2017. In addition, the leave cannot be paid for by a state or local government.

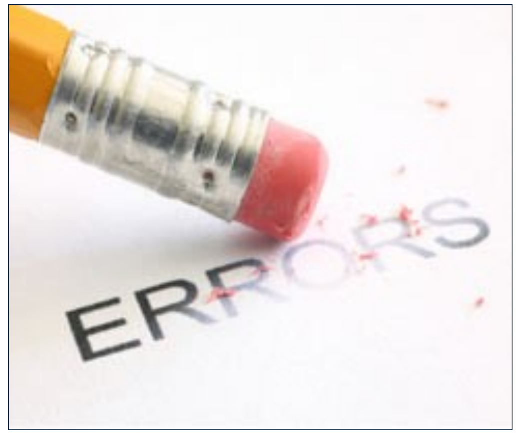
The credit is increased by 0.25% for each percentage point by which the amount paid to a qualifying employee exceeds 50% of the employee’s wages, with a maximum of 25%. In certain cases, an additional limit may apply. The credit is for wages paid in 2018 and 2019.

A tax-exempt organization is to include as UBTI any disallowed deduction incurred by the organization after December 31, 2017. This rule does not apply to the extent the amount paid or incurred is directly connected with an unrelated trade or business which is regularly carried on by the organization. For an exempt organization organized as a corporation, UBTI would be taxed at a rate of 21% beginning with tax year 2018.

For help analyzing any potential tax liability for your organization and for more information, please see P.L. 115-97, IRS Publication 15-B, or you may contact Donita Joseph at djoseph@windes.com, Chérie Williams at cwilliams@windes.com, or **844.4WINDES** (844.494.6337).

403(b) Plans: The IRS Changes the User Fees for Voluntary Compliance

On January 2 of this year, the IRS published Revenue Procedure 2018-4 (Procedure), which outlined new fees for Voluntary Compliance Program (VCP) submissions to correct plan errors.



Prior to the new Procedure, fees were based on participant count, with a scale ranging from $750 for plans with less than twenty participants, to $25,000 for plans covering over ten thousand employees. In addition, there have been reduced fees for correcting common errors relating to participant loans, missed plan amendments, and required minimum distributions.

Without explanation, the new Procedure changes the basis of the fees from participant count to asset size, effectively creating a flat three-tiered schedule as follows:

Assets	User Fee
$500,000 or less	$1,500
$500,001 - 10,000,000	$3,000
Over $10,000,000	$3,500

Besides this radical change in the user fee basis, the Procedure also eliminated the discounts for the common errors mentioned above. The new fees are retroactive to the beginning of the year and allowed no time for public comment or for submissions in process to qualify under the old fees.

The effect of the new fee structure is to provide a dramatic reduction for large plans, while increasing the cost of compliance for most small plans. This may serve as a disincentive to some plan sponsors to voluntarily correct plan issues that are not eligible for self-correction. With the elimination of the determination letter program, the IRS will likely shift more resources to plan examinations, so employers are cautioned against ignoring plan compliance issues. The cost of correcting an issue through an audit still greatly outweighs the user fees detailed above.

Section 403(b) plans also have a unique opportunity to correct plan compliance issues through a plan amendment and restatement, which is required to be completed by 2020. As we have reported previously, the IRS announced a window for plans to restate their 403(b) plans to an IRS-approved document no later than March 31, 2020. These new documents will replace the “good faith” documents that were required to be adopted by 2009.

Many of the plan document or operational issues that would otherwise need to be corrected through a VCP application can be corrected through the plan restatement. The restated documents will be effective back to January 1, 2010, and the sponsor can correct any plan provisions that caused compliance issues and receive retroactive qualification back to that date. Plan sponsors are encouraged to engage in a thorough administrative review of their plans to take advantage of this unique opportunity to correct any errors that may have occurred over the last eight years.

Please contact us with any questions about your plan's compliance. The following is a link to the IRS announcement of the new Procedure:

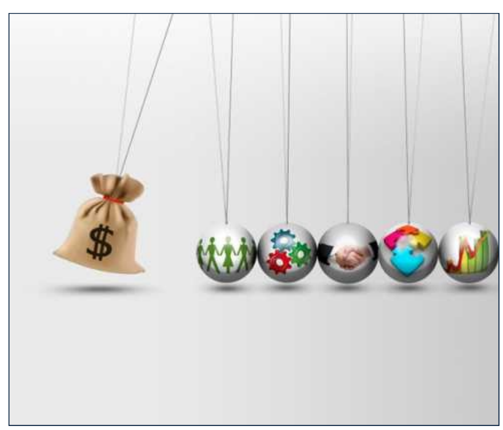
https://www.irs.gov/retirement-plans/voluntary-correction-program-user-fees-changes

If you have any concerns about your plan's compliance with these requirements, please contact Richard Green at rgreen@windes.com or toll free at **844.4WINDES** (844.494.6337).

Have You Analyzed the Impact of the New Accounting Guidance on Your Organization?

Regular readers of the *Nonprofit Advisor* will be aware of the variety of new and amended accounting rules that will affect nonprofit organizations in the coming years. The sector is facing a flurry of significant new guidance that will require thoughtful evaluation to ensure smooth adoption by affected organizations. The three most significant accounting changes on the horizon are the new Nonprofit Financial Statement presentation rules (ASU 2016-14), the new revenue recognition rules (ASU 2014 –09), and the new lease rules (ASU 2016 -02). All of these changes have been discussed in previous editions of the *Nonprofit Advisor* (click here). However, as adoption dates begin to approach, it is worth considering some practical steps preparers can take now to help ensure a smooth transition for your organization.

The first change will be the required adoption of the new rules on the presentation of financial statements for nonprofit entities. These rules were finalized in August of 2016 and are required to be adopted beginning with fiscal years ended December 15, 2018 or later. Because early adoption is permitted, we have started to see the first financial statements publicly available of early adopters. These real life examples are adding to the examples contained within the guidance and can help inform decisions that an organization needs to make about how to apply the standard. We encourage preparers of nonprofit financial statements to get a handle on the changes that will affect their specific organization and to start discussions with those in governance (board or audit committee) now about the changes that will result. In particular, the inclusion of a liquidity disclosure in the financial statements of the organization is perhaps the biggest change of the guidance, and we encourage that financial statement preparers begin to prepare for this disclosure. Preparation would include understanding the flexibility that the standard offers for disclosure options and also to consider the released illustrative examples available. Management should consider what message it wishes to convey in the liquidity discussion and have a robust conversation with the board to explain the disclosure requirements and discuss the best presentation for achieving the transparency and impact it desires. Due to expanded required disclosures, policies on board designations on net assets should also be reviewed with the board and recommendations and policy changes should be discussed as well. Now is the time to have these discussions so board members are able to offer their thoughtful input in a timely manner for efficient adoption of the standard.



After the implementation of the new financial statement presentation standard, organizations will have a short turnaround before needing to implement new standards on revenue and lease accounting that will be effective for fiscal years ending after December 15, 2019 and December 15, 2020, respectively. From a practical standpoint, the current thinking is that many organizations will elect to adopt the lease standard early, so both of these pieces of new guidance will be implemented together in the first fiscal year end after December 15, 2019. The revenue recognition standard is expected to be further complicated with a forthcoming amendment from the Nonprofit Advisory Council of FASB, which will make some clarifications on grant accounting. Financial statement preparers should begin the process of evaluating their revenue streams under the new standard to determine whether any current accounting treatment may need to be changed. A first step would be to compile a list of all the organization's exchange transaction revenue streams specifically looking for items such as membership dues, royalties, advertising and sponsorship revenue, tuition or federal, state or private grants where the donor is receiving commensurate value in return. All of these types of revenue would be subject to the new standard. We recommend that an organization evaluate each type of revenue under the standard and evaluate any difference between existing accounting and accounting under the new guidance. Any immaterial variances can be passed upon, and that may be the most likely outcome; however, in order to reach that conclusion, an organization must perform its evaluation and reach a conclusion in consultation with its outside CPAs. The aforementioned new amendment that is forthcoming in final form soon, is expected to result in certain contracts that are currently accounted for as exchange transactions to instead be looked upon as conditional contributions. One example of this would be a grant where the value of services to be performed is not going to the donor but instead to the general public. Because an exchange transaction can only exist where the donor is also the primary beneficiary, many grants where this is not the case will no longer be considered exchange transactions but instead fall into contribution accounting. These types of contracts should be evaluated and when it is determined that there is a right of return **and** a barrier to overcome, the organization would account for this as a conditional contribution and revenue would be earned as the conditions are satisfied. This change ultimately may not have an impact on timing of revenue recognition, but it will be necessary for management to evaluate this and discuss its conclusions with its auditors.

The lease standard will have the impact of quantifying operating lease payment commitments and grossing up the liabilities (future payments) and assets (right to use asset) of the Statement of Financial Position. We recommend that organizations take steps now to quantify the leases that may be impacted and to be prepared to quantify the initial adoption entry and ongoing accounting under the new standard. Most importantly, organizations need to evaluate any impact on financial covenants as a result of these structural changes of the statement of financial position and make plans to accommodate as necessary.

These three new accounting rules will affect the financial statements and accounting for every nonprofit organization. The time is now for proactive preparation and analysis to reduce any negative impacts of adoption when the time comes. To ensure a smooth transition, the best approach is for management of each organization to evaluate each of these items independently and to reach conclusions as to what changes are or are not necessary. At that point, consultation with independent auditors can occur and a shared conclusion from both parties should allow for a smooth adoption of the new standards. At Windes, we expect to have regular engagement with our clients to help them through this transition period smoothly. Please reach out if we can help with any clarification on the new standards.

If you have questions or would like more information about the new standards, please contact Michael Barloewen at mbarloewen@windes.com or **844.4WINDES** (844.494.6337).

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Windes is a recognized leader in the field of accounting, assurance, tax, and business consulting services. Our goal is to exceed your expectations by providing timely, high-quality, and personalized service that is directed at improving your bottom-line results. Quality and value-added solutions from your accounting firm are essential steps toward success in today's marketplace. You can depend on Windes to deliver exceptional client service in each engagement. Since 1926, we have gone beyond traditional services to provide proactive solutions and the highest level of capabilities and experience.

The Windes team approach allows you to benefit from a wealth of technical expertise and extensive resources. We service a broad range of clients, from high-net-worth individuals and nonprofit organizations, to privately held businesses. We act as business advisors, working with you to set strategies, maximize efficiencies, minimize taxes, and elevate your business to the next level.

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