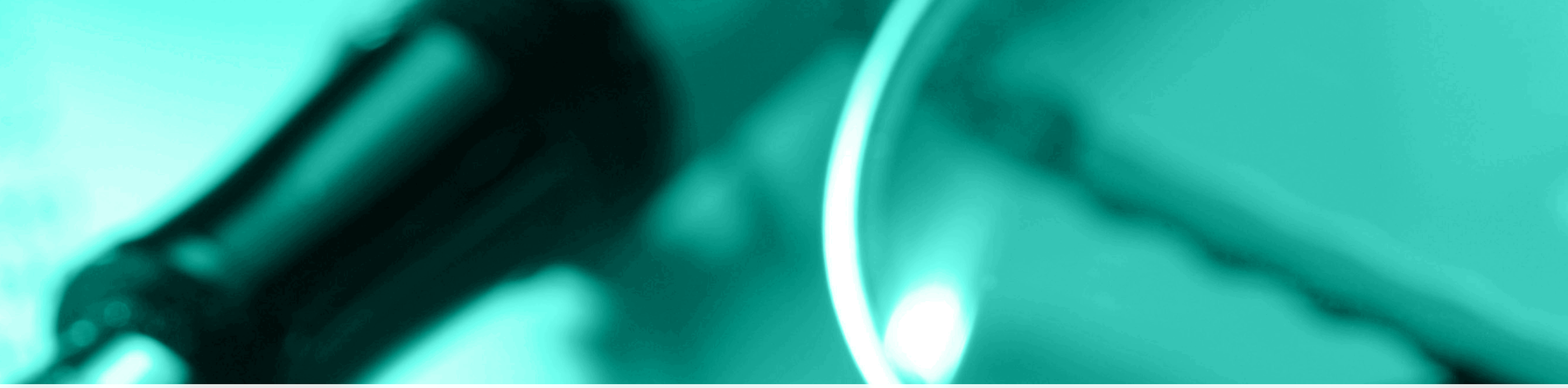

Presentation and Classification of Grants and Net Assets on CDFI Financial Statements

PERFORMANCE COUNTS

Best Practices for CDFI Financial Statements and Management

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I. INTRODUCTION

The Community Development Financial Institution (CDFI) industry has experienced unprecedented growth over the past few years, the result of a higher public profile and increased awareness that CDFIs offer essential solutions to problems in low-income communities. With this growth and opportunity comes greater accountability and scrutiny. While CDFIs have long been responsive to the communities they serve, expansion and growth—particularly with new large-scale capital providers to the industry—make it even more critical to communicate clearly and transparently to external stakeholders and investors about the financial wherewithal and financial management of CDFIs.

In support of this purpose, Opportunity Finance Network (OFN) convened a new industry-led initiative, **Performance Counts: Best Practices for CDFI Financial Statements and Management**, which includes a Working Group to develop financial statement standards, guidance, and best practices by CDFIs for CDFIs.

The goals of the effort are to:

- Achieve greater consensus within the CDFI industry around financial metrics, statements, reporting, and management;
- Promote streamlined reporting and clearer messaging by CDFIs; and
- Ultimately enable increased access to capital sources by helping current and prospective investors better understand CDFI financial statements, financial performance, and financial wherewithal.

This paper is the first in a series of papers that will address specific financial statement and financial management topics, with the goal of encouraging wide participation and sharing of recommendations on how to present financial information in a more clear, standard, and transparent way to both internal and external CDFI stakeholders. OFN welcomes feedback, as continuous communication regarding process and work product is critical to the success of this initiative.

ABOUT THIS PAPER

This paper discusses the purpose of net assets, the presentation of net assets on the Statement of Financial Position (SFP), and the presentation of grants on the Statement of Activities (SOA).

Generally Accepted Accounting Principles (GAAP) requirements and current industry practices and illustrative presentation styles by CDFIs are noted first, followed by guidance and recommendations from the Working Group.

Please note this paper does not include either analysis of net assets on a CDFI's SFP or the adequate level of net assets. The Working Group plans to present future papers discussing ratios, analysis, and covenants for CDFIs.

The information in this paper is intended primarily for nonprofit CDFI loan funds, which hold different accounting requirements than for-profit CDFIs and depositories.

II. GRANTS

GAAP REQUIREMENTS

GAAP requires all grant agreements be reviewed carefully for donor intent to determine when and how to record grants. GAAP requires sufficient evidence in the form of verifiable documentation that a promise was made and received to recognize the income; typically, this is written documentation in the form of a grant agreement or commitment letter, but could also be a corporate e-mail communication or verbal indication if there is a verifiable document (e.g., board minutes).

Please note the word "grant" and "contribution" can be used interchangeably and follow the same accounting guidelines. Many CDFIs refer to funding from individuals as "contributions" and funding from institutions as "grants".

Restrictions

When booking a grant, GAAP requires that the grant be classified in one of three categories—unrestricted, temporarily restricted, or permanently restricted—based on donor-imposed restrictions as follows:

- Unrestricted have no donor imposed restrictions;
- Temporarily restricted have restrictions of either time and/or purpose; and
- Permanently restricted have restrictions imposed by donors to be maintained into perpetuity.

Grants initially booked as temporarily restricted are released when restrictions are met. Common examples of temporarily restricted grants are those that are time-restricted or restricted for purpose (e.g., operation of a program). The grants are released when the time restriction has elapsed, the donor's purpose restriction has been fulfilled, or both. If an organization is able to satisfy a donor's restriction in the same period the contribution is received, the restricted contribution may be reported as unrestricted at the discretion of the nonprofit. Permanently restricted grants are restricted into perpetuity by the donor. CDFIs should not use (or release) their permanently restricted grants unless instructed to do so by the donor.

Conditional Versus Unconditional

In reviewing a grant agreement, the CDFI must consider whether the grant is "unconditional" or "conditional." Unconditional means that there are no conditions or contingencies placed on the organization before receiving the grant. Conditional means there are certain benchmarks, events, or other conditions that the organization needs to meet before receiving the grant.

GAAP requires all unconditional grants be booked on the SOA when the CDFI receives a commitment for the grant (a promise to give). For conditional grants, income is booked when the condition or benchmark is met. An exception to this rule is when the expectation that the condition would not be met is remote. For example, a CDFI can consider if the condition can be easily met in normal operations (e.g., continue to provide a regular program) or if failure to meet the condition is unlikely (e.g., maintain 501c3 status). If the condition can be easily met, these are not considered restrictions or conditions. If a CDFI receives a conditional grant and receives the cash for the grant before the condition is met, it should not book the income, but rather book it to a liability account such as "Conditional Advance Liability." Grants are typically not booked to a deferred revenue account.

Fair Value

Grants are booked at fair value. For example, if a CDFI receives a multi-year grant commitment and will receive the payments in multiple years, the grant is booked at the present value of estimated future cash flows using an appropriate discount rate.

Exchange Transactions Versus Grants

GAAP also makes a distinction between an exchange transaction (or contract) and a grant for program purposes. In the case of a contract, the recipient of the contract is being asked to provide a service with specific deliverables. A contract is viewed as an exchange between two parties and has characteristics similar to a vendor relationship; the CDFI should book these contracts as earned income, even if they are from the same funder that also provides the CDFI with grants. In some cases, the agreement may say "grant," but the characteristics of the agreement are of an exchange transaction. CDFIs should focus on the content of the agreement in determining whether it is a grant or exchange transaction. In the case of an exchange transaction, if the CDFI has received the cash from the third party, but has not yet performed the services, it will book the amount as deferred revenue (a liability account) until the services have been performed.

CURRENT CDFI INDUSTRY PRACTICES

Classification of Grants

Accounting for operating grants is relatively consistent across the industry:

General operating support grants (with no time restrictions) are booked as unrestricted income at the grant confirmation date.

Operating grants for a particular program, purpose, or time period are booked as temporarily restricted income at the grant confirmation date; these grants are released from restriction (i.e. transferred from temporarily restricted to unrestricted) when the CDFI has spent the funds for the particular program or purpose, when the restriction has been met, or when the required time has passed.

The type of and accounting for grants for financing activities vary widely within the CDFI industry. Potential restrictions placed on grants for financing include the following:

- Restricted in general for financing
- Restricted to make loans until the funds are deployed
- Restricted to make loans in a specific geography or for a specific purpose
- Restricted for loan loss reserves
- Restricted to make loans; as long as loans are not written off, funds need to revolve to make additional loans.

CDFIs use many different approaches to booking grants for financing depending on the nature of the restriction and their past practices. A few approaches to booking grants for financing used in the industry include:

- Classified as unrestricted if they support the primary business of the CDFI (i.e. financing);
- Classified as temporarily restricted until the funds are deployed for the purpose intended at which time the funds are released from restriction;
- Classified as temporarily restricted into perpetuity or until a loan is charged off or a loan loss reserve is expensed; for some CDFIs that release the grant when the LLR is expensed, they will replenish or rebook the grant if the loan is repaid and the LLR expense is reversed; or
- Classified as permanently restricted. In certain situations, these funds will be used to write off a non-performing loan, which is charged directly against permanently restricted net assets on the SFP.

Auditors note that often times grants will be classified based on how a similar grant was classified historically. If a CDFI previously received grants for financing and classified them as permanently restricted, the CDFI would typically apply that classification to a new grant for a similar purpose.

CDFI Fund Grants

Similarly, grants from the CDFI Fund are also accounted for in various ways by CDFIs. The typical CDFI Fund grant agreement indicates grants be used for a variety of purposes, which include financial products, financial services, development services, loan loss reserves, capital reserves, or other uses that directly or indirectly support the activities in the CDFI awardee's business plan. In practice, CDFIs currently book these grants in multiple ways:

- Classified as unrestricted as the use of funds is broad enough to support an enterprise whose main purpose is lending (unless there are specific restrictions related to a certain type of lending or a certain geography or target market);
- Classified as temporarily restricted but released from restrictions when the funds are lent out or otherwise deployed for the first time;
- Classified as temporarily restricted until there is a loan loss expense at which time the funds are released (if loan repays, the grant is sometimes replenished or rebooked); or
- Classified as deferred revenue until funds are spent. The Working Group and accounting advisors agree and advise that this is an incorrect way to book CDFI Fund grants. (See Working Group Recommendations on page 7.)

Presentation of Grants

There currently exists wide variation among CDFI financial statements in the presentation of grants. GAAP requires that nonprofits distinguish between grants and contributions received that increase permanently restricted net assets, temporarily restricted net assets, and unrestricted net assets. GAAP also requires recognition of the expiration of donor-imposed restrictions in the period in which the restrictions expire. Some CDFIs present the minimum number of grant categories, while others present substantially more detail on types of grants on the SOA, such as purpose of grant (e.g., capital, operations) or source of grant (e.g., federal grants, state grants, corporate grants) or in some cases the specific donors.

Below are two typical examples of how CDFIs present grants on the SOA.

CDFI 1 Grants and Contributions Presentation on SOA

	Unrestricted	Temporarily Restricted	Permanently Restricted
Grants and contributions	$100	$100	$100
Net assets released from restrictions	$25	($25)	$0

CDFI 2 Grants and Contributions Presentation on SOA

	Unrestricted	Temporarily Restricted	Permanently Restricted
Grants and contributions, operating	$100	$100	$100
Grants and contributions, financing	$0	$200	$0
Grants and contributions, re-granting	$0	$100	$0
Total grants and contributions	**$100**	**$400**	**$100**
Net assets released from restrictions, operating	$25	($25)	$0
Net assets released from restrictions, capital	$25	($25)	$0

WORKING GROUP RECOMMENDATIONS

Classification of Grants

While the first priority is to have grants classified in a way that is GAAP compliant, it is clear from the discussion above that there is some ambiguity within GAAP related to the classification of grants, particularly related to grants for financing.

In general, when there is ambiguity, the Working Group agrees that it is best to have grants classified in the least restrictive manner possible based on the terms of the grant agreement—unrestricted is preferred to temporarily restricted and temporarily restricted is preferred to permanently restricted.

This approach gives the CDFI more flexibility and gives creditors more protection. In the event of a default, unrestricted net assets are more readily available to creditors subject to lien priorities. State law varies as to the consequences to creditors of various treatments of net assets and grants. Temporarily restricted net assets and particularly permanently restricted net assets may only be available on a limited basis, and depending on individual state laws and restrictions placed on the grants, may be returned to a grantor. While we are not aware of the return of temporarily restricted or permanently restricted net assets to funders in the CDFI industry because there is no precedent for nonprofit CDFIs that have gone through bankruptcy, the Working Group recommends classifying the grants in the least restrictive ways possible to provide the maximum flexibility to the CDFI and protection to the lender.

Below are the Working Group's recommendations on treatment of grants to support financing:

- Grants for financing should generally *not* be classified as permanently restricted unless specified by the grantor that they are restricted into perpetuity and are not to be used to fund loan losses. The permanently restricted category is intended for grants that will remain into perpetuity. Because of the nature of the financing business, grants for financing typically may be utilized at some point to cover loan losses and are, therefore, not restricted into perpetuity. Only grants that are truly restricted into perpetuity (e.g., an endowment) should be classified by a CDFI as permanently restricted.[1]
- Grants that are for a CDFI's financing in general (which include loan capital, loan operations, loan loss reserves, etc.)—with no other restrictions—should be classified as unrestricted. Because a CDFI's main business activity is financing, GAAP provides enough flexibility to allow these grants to be treated as unrestricted since they support the general business and mission of the CDFI.
- Grants for financing that have a time restriction should be classified as temporarily restricted and should be released when the time restriction is met.
- Grants for financing that have a purpose restriction (e.g., restricted to make loans or investments, restricted to make loans in a specific geography, restricted to make loans for a specific type of lending, restricted for loan loss reserves) should be classified as temporarily restricted and released when the purpose restriction is met. However, if the CDFI meets the restriction in the same year they receive the grant, the CDFI has the option to classify the grant as unrestricted. The grant should not be rebooked or replenished after it is released.
- Grants for financing that specify a restriction to use the grant for revolving loan funds (that are relent after loans are repaid) should be classified as temporarily restricted. As indicated earlier, due to the nature of the lending business, it is typical that a CDFI use these grants at some point for loan write-offs and/or reserves, so they should not be considered permanently restricted.
- Standard CDFI Fund Financial Assistance grants that do not have further restrictions (i.e. geographic, sector, use) should be classified as unrestricted as they support the general business and business plan of the CDFI. If a CDFI Fund grant has a further restriction (geography, sector, use), the CDFI should classify the grant as temporarily restricted and release the grant from restriction when a loan has been made to satisfy the grant or the funds have been spent to satisfy the grant.

[1] NeighborWorks America provides permanently restricted grants to some CDFIs in their network which are used primarily for lending. A CDFI that would like to use the permanently restricted grant for loan loss reserves or to cover losses may request this in writing to NeighborWorks America. There is precedent for converting some of these grants into temporarily restricted or unrestricted grants.

Reporting

For all grants classified as unrestricted, temporarily restricted, or permanently restricted, CDFIs may still need to report back to the funder on the use of these grants. The accounting treatment of the grant does not free the CDFI of any obligations to report and track use and outcomes of the grant.

Grant Agreements

When CDFIs receive new grants, particularly those to support financing activity, CDFIs may try to influence the wording of grant agreements to provide clarity and maximum flexibility. If there are restrictions, CDFIs should try to incorporate specific language into the agreement indicating the nature of the restriction to clarify the issues discussed above. A few items CDFIs can consider in grant agreements are as follows:

- *Grants for general financing of the CDFI:* Propose language such as "to support the CDFI's financing business and consistent with the mission of the organization" so it is clear the broad use of the grant is to support the CDFI's primary business, which the CDFI can book as unrestricted.
- *Grants with geographic or sector restrictions:* Propose language indicating that the restriction is met after the funds are deployed.
- *Grants to remain as financing capital* (and recycle into new loans after loans are repaid): Propose language that places a time restriction on the grant for financing (i.e. restricted for a five year period for making loans) so it is clear when the funds may be released from restriction. CDFIs can also try to clarify that they can use grants for financing to cover loan losses and loan loss reserves related to the financing activity.

Presentation of Grants

For presentation purposes on the SOA, the Working Group recommends a simplified approach for reporting grants. As indicated above, GAAP requires that nonprofits distinguish between grants received that are unrestricted, temporarily restricted, or permanently restricted, as well as the recognition of the expiration of donor-imposed restrictions. The Working Group recommends not making further distinction on the SOA (such as grants for operations, grants for financing, grants for re-granting, or the names or types of donors). This gives the financial statement reader a consistent and clear snapshot of unrestricted grants, as well as temporarily restricted and permanently restricted grants. CDFIs should provide more detail on the nature of various types of grants in the notes to the financial statements. Please see the section on Financial Statement Notes (page 12) for further detail.

Recommended Presentation of Grant and Contributions (in column or list form) on SOA

	Unrestricted	Temporarily Restricted	Permanently Restricted
Grants and contributions	$100	$100	$100
Net assets released from restrictions	$25	($25)	*this category will not be applicable*

Explanation of Multi-Year Grants

A common challenge for CDFIs is explaining how multi-year grants flow through the SOA. These grants are initially recorded as temporarily restricted revenue for the total amount of the grant in the year the grant is committed. As the funds are deployed in future years, these grants are released to unrestricted, causing temporarily restricted net assets to decline. This can cause fluctuations in total net assets (an increase in total net assets in the year the multi-year grant is received and decrease in total net assets in subsequent years as the grant is spent).

CDFIs should provide additional detail in the notes to the financial statements if they receive significant multi-year operating grants to clarify this trend. Financial statement readers should focus on changes in unrestricted net assets to assess operating performance (and not changes in total net assets, which may fluctuate up and down due to multi-year grants). A management discussion of the financial statements can highlight this point as well.

III. NET ASSETS

PURPOSE OF NET ASSETS

Net assets are an important source of information for funders and investors externally and for board members and management internally to assess the financial health of a CDFI. Each category of net assets, depending on its purpose and its presentation, can apprise the reader of the financial statement about the depth of the organization's capital structure, operating sustainability, financial strength, as well as its ability to withstand unexpected operating shocks. For example, unrestricted net assets, temporarily restricted net assets for financing, and permanently restricted net assets for financing are an indication of the CDFI's ability to meet its future debt obligations. Alternatively, unrestricted net assets and temporarily restricted net assets for operations show the depth of the organization's operating sustainability and its capacity to withstand unexpected operating shocks, and invest in future growth.

GAAP REQUIREMENTS

In alignment with grants and contributions, GAAP also requires net assets be classified in one of three categories—unrestricted, temporarily restricted, or permanently restricted—based on donor-imposed restrictions:

- Unrestricted net assets have no donor imposed restrictions;
- Temporarily restricted net assets have restrictions of either time and/or purpose; and
- Permanently restricted net assets have restrictions imposed by donors to be maintained into perpetuity.

Further, GAAP requires the dollar amount of each category be presented on the SFP and additional detailed information about temporarily restricted net assets and permanently restricted net assets be reported either on the SFP or in the notes to the financial statements.

If a nonprofit designates some of its unrestricted net assets for a specific purpose, accounting guidelines require that significant designations either be reported on the SFP or disclosed in the notes to the financial statement. Designations of unrestricted net assets are voluntary board-approved segregations of unrestricted net assets for a specific purpose, which may be reversed at any time by the CDFI's board.

For consolidated financial statements, the net assets of noncontrolling investors must be presented separately from net assets of the CDFI. A noncontrolling interest (previously called a minority interest) is the portion of equity in a subsidiary not attributable, directly or indirectly, to a parent. According to GAAP, the ownership interests in subsidiaries held by parties other than the parent must be clearly identified, labeled, and presented in the consolidated statement of financial position within equity, but separate from the parent's equity. In the case of nonprofit CDFI financial statements, the noncontrolling interest is part of unrestricted net assets, but must be broken out separately from other unrestricted net assets that the parent controls.

CURRENT CDFI INDUSTRY PRACTICES

CDFIs currently use a number of approaches to present net assets on the SFP. Beyond the required separation of unrestricted, temporarily restricted, permanently restricted net assets, some CDFIs include designations of unrestricted net assets and the purpose of temporarily restricted and permanently restricted net assets on the SFP, while others include these details in the notes to the financial statements. In some cases, CDFIs will use separate columns on the SFP to differentiate between operating, financing activities, and other purposes. Often times, the presentation of net assets on the CDFIs interim financials is different than the presentation on the CDFIs audited financial statements. Below are the most commonly used classifications of net assets within the industry.

Most Commonly Used Classifications of Net Assets seen on CDFI Statements of Financial Position:

Unrestricted net assets

- Unrestricted, undesignated
- Board designated, operating reserve
- Board designated, loan loss reserves
- Board designated, capital
- Unrestricted, property and equipment
- Unrestricted, contractually limited in use
- Noncontrolling interest in subsidiaries

Temporarily restricted net assets

- Operating
- Capital (general or program/sector specific)
- Loan loss reserves/credit enhancement
- Pass-through grants or re-granting

Permanently restricted net assets

- Capital
- Other

Because of the differences in the ways CDFIs classify their net assets (and the differences in the grants and contributions discussed earlier), it makes it difficult for financial statement readers to understand and analyze a CDFI's net assets, and compare net asset levels among peer institutions.

WORKING GROUP RECOMMENDATIONS

The Working Group recommends a simplified, clean, and standard presentation of net assets on the SFP. The Working Group recommends the following presentation format, which addresses the issues and distinctions discussed below, for net assets on the SFP. The Working Group also recommends standard definitions for a few of the categories where there are currently inconsistencies.

Recommended Presentation of Net Assets on SFP

Unrestricted	$100
Unrestricted, noncontrolling interest in subsidiaries	$50
Total unrestricted	**$150**
Temporarily restricted, operating	$100
Temporarily restricted, financing	$100
Temporarily restricted, re-granting	$100
Total temporarily restricted	**$300**
Permanently restricted	**$100**
Total net assets	**$550**

Definitions:

> **Temporarily restricted net assets, operating**: Include net assets which are restricted to cover operating expenses of the CDFI which could include salary, program costs, overhead, and other expenses. These net assets may be restricted for the operating expenses of a particular program or may be general operating support which carries a time restriction.
>
> **Temporarily restricted net assets, financing**: Include net assets which are restricted for a time period or use for lending and investing, real estate development, or other financing activities that can be used to create an asset. These also include net assets restricted for loan loss reserves and loan losses related to a CDFI's financing.
>
> **Temporarily restricted net assets, re-granting**: Includes net assets which are restricted to re-grant to another organization. These net assets cannot be used for financing activities or operations.

To develop a recommended format for the presentation of net assets, the Working Group discussed the following issues and provides the following guidance:

- The most important distinction for readers of the financial statements is to understand whether restricted net assets are for financing purposes, or for other purposes, such as re-granting or operations. Therefore, it is important to break out temporarily restricted net assets for financing purposes. The net assets that would most readily be available for loan losses and to repay lenders would include unrestricted net assets and temporarily restricted net assets, financing.
- Net assets available for re-granting are unique in nature in that they are not available to cover any operating expenses or any loan losses and do not contribute to the financial strength and viability of the organization. Therefore, they should be broken out and presented separately.
- The notes to the financial statements and/or any consolidating schedules to the financial statements should provide further detail on temporarily or permanently restricted net assets, operating and financing restrictions, and/or management's intent and strategy to support the presentation of net assets on the SFP.
- The Working Group recommends not including board designations on the SFP. The notes should contain detail on designations of unrestricted net assets, particularly if they are material in nature (e.g., financing). These reflect management's intent and strategy, but can be reversed at any time and not warranted to show on the SFP.

The Working Group recommends that the presentation of net assets in an organization's unaudited financial statements should mirror the presentation of net assets on the audited financial statements. Financial statement readers will have an easier time reviewing and analyzing the interim unaudited statements if they conform in format to the audit.

VI. NOTES TO FINANCIAL STATEMENTS

Working Group Recommendations

The notes to the financials should contain additional information that will help explain specific items in the financial statements, as well as clarify individual line items in the financials. Having more consistent notes will also provide clarity and consistency on financial statements. The Working Group has the following recommendations related to notes for net assets and grants.

- **Unrestricted net assets**: CDFIs should disclose any significant board designations of unrestricted net assets. Designations are voluntary and may be reversed at any time by the Board.
- **Temporarily restricted net assets**: As indicated above, the Working Group recommends including the following three temporarily restricted categories on the SFP: operating; financing; re-granting. In the notes, the Working Group recommends including any significant restrictions in any of those categories. For example, a CDFI may want to break out significant operating purpose restrictions and group together grants with time restrictions. In addition, a CDFI should indicate if any of the temporarily restricted net assets for financing have restrictions that would prevent them from being available to protect investors (i.e. for development activities). The Working Group recommends a table format summarizing the beginning-of-year balance, temporarily restricted contributions received, releases from restrictions, and the end-of-year balance.
- **Permanently restricted net assets**: CDFIs should include the nature of any permanently restricted net assets and if they are available to cover loan losses or to repay debt.
- **Grants and grant receivables**: CDFIs need to disclose the amounts of grant receivables in different categories: 1) less than one year, 2) one to five years, and 3) more than five years. CDFIs should disclose the allowance for any uncollectible grants receivable, as well as if there is a discount associated with multi-year contributions receivable. If CDFIs have received any conditional promises to give, they should disclose the amount of the conditional promise and the nature of the condition.

Sample Notes to Financial Statement

The following provides sample notes to the financial statements related to net assets and grants. CDFIs can provide additional detail in any of the below categories.

Grants and Contributions Received

Grants and contributions were received for the following purposes in 2013:

	Unrestricted	Temporarily Restricted	Permanently Restricted
Grants and contributions, operating	$100	$200	$0
Grants and contributions, financing	$0	$325	$0
Grants and contributions, re-granting	$0	$100	$0
Total grants and contributions	**$100**	**$625**	**$0**

Grant Receivables

Grants receivables are due to be collected as follows:

	12/31/12	12/31/13
Receivables in one year or less	$300	$300
Receivables in 1-5 years	$100	$100
Receivables greater than 5 years	$200	$200
Less: Present Value Discount	($25)	($25)
Total grants receivable	**$575**	**$575**

Unrestricted Net Assets

The Board designated unrestricted net assets for the following purposes:

	12/31/12	12/31/13
Unrestricted, undesignated net assets	$100	$100
Unrestricted, board designated, financing	$150	$100
Unrestricted, board designated, operating reserve	$50	$50
Total unrestricted net assets	**$300**	**$250**

Temporarily Restricted Net Assets

Temporarily restricted net assets consist of the following:

	12/31/12	Grants and contributions	Net assets released	12/31/13
Operating				
Program 1 (e.g., childcare program)	$100	$25	($50)	$75
Program 2 (e.g., policy program)	$100	$0	($25)	$75
General operating support (time restriction)*	$100	$50	($100)	$50
Total operating	**$300**	**$75**	**($175)**	**$200**
Financing				
Loan capital	$100	$100	($50)	$150
Loan loss reserves	$50	$0	($25)	$25
Credit enhancement (e.g., Dept. of Education)	$100	$0	$0	$100
Development	$25	$50	($25)	$50
Total financing	**$275**	**$150**	**($100)**	**$325**
Re-granting	**$100**	**$50**	**($50)**	**$100**
Total temporarily restricted net assets	**$675**	**$275**	**($325)**	**$625**

*CDFI received $50 in general operating support in 2013, of which $25 is for 2014 and $25 is for 2015.

Please note that CDFIs may want to disclose any significant multi-year grants that may cause fluctuations in overall net assets over a multi-year period.

Permanently Restricted Net Assets

Permanently restricted net assets carried the following restrictions:

	12/31/12	12/31/13
Permanently restricted, endowment	$100	$100
Permanently restricted, financing*	$25	$25
Total permanently restricted	**$125**	**$125**

* As indicated in the recommendations, the Working Group is recommending that grants for financing generally not be classified as permanently restricted unless specified by the funder. If a CDFI does have permanently restricted net assets for financing, the CDFI should disclose further detail on those restrictions, including whether the CDFI can request to use those funds to cover losses.

V. CONCLUSION

The Working Group encourages CDFIs to implement the recommendations set forth in this paper related to grants and net assets and share the working paper with their auditors in an effort to move to more consistency and transparency in the presentation of CDFI financial statements across the industry.

The Working Group will publish papers on additional topics in the future. Over time, we expect this effort to benefit the industry overall by making it easier for funders, investors, and other key stakeholders to understand the industry's financial statements and financial wherewithal—and to ultimately lead to new sources of capital and resources for the CDFI industry.

APPENDIX A

Working Group and Advisors

OFN would like to thank the following CDFIs for their participation in the Working Group. One or more individuals from these organizations met to review the issues and arrive at the recommendations and guidance presented in this paper. These recommendations are endorsed by the Working Group members.

Working Group

Chicago Community Loan Fund
Community Reinvestment Fund
Corporation for Supportive Housing
Craft3
FAHE
Florida Community Loan Fund
Low Income Investment Fund
New Hampshire Community Loan Fund
Nonprofit Finance Fund
Opportunity Finance Network
Opportunity Fund
The Progress Fund
The Reinvestment Fund
Self-Help Ventures Fund

Additionally, a number of experts provided legal and accounting advice and guidance to the Working Group to ensure that the information and recommendations presented in this paper are compliant with GAAP and other accounting and legal guidance.

Accounting and Legal Advisors

Alexander, Aronson, Finning & Company
Arent Fox
Novogradac & Company LLP
Reznick Group

OFN is coordinating with CARS to ensure that this effort is complimentary to the data collection platform that CARS has developed.

The Working Group also received input from many other CDFIs, CDFI funders and investors, and industry advisors. OFN appreciates the feedback from these various parties, which contributed to the final paper content.

Finally, the Working Group would like to thank consultant Mary Vasys for her contribution to the initiative.

APPENDIX B
Detail on Accounting Guidelines and Standards

The different Financial Accounting Standards Board pronouncements and other authoritative accounting literature have been captured in one source: **The FASB Accounting Standards Codification**. The information related to nonprofit accounting is included in one section (Section 958). The sections of the codification that provide further detail on the issues discussed in this working paper related to the grants and contributions and net assets are excerpted below from the FASB Accounting Standards Codification.

Excerpted from Glossary of Terms Referenced in the FASB Accounting Standards Codification

Contribution

An unconditional transfer of cash or other assets to an entity or a settlement or cancellation of its liabilities in a voluntary nonreciprocal transfer by another entity acting other than as an owner. Those characteristics distinguish contributions from exchange transactions, which are reciprocal transfers in which each party receives and sacrifices approximately equal value; from investments by owners and distributions to owners, which are nonreciprocal transfers between an entity and its owners; and from other nonreciprocal transfers, such as impositions of taxes or legal judgments, fines, and thefts, which are not voluntary transfers. In a contribution transaction, the value, if any, returned to the resource provider is incidental to potential public benefits. In an exchange transaction, the potential public benefits are secondary to the potential proprietary benefits to the resource provider. The term contribution revenue is used to apply to transactions that are part of the entity's ongoing major or central activities (revenues), or are peripheral or incidental to the entity (gains).

Donor-Imposed Restriction

A donor stipulation that specifies a use for a contributed asset that is more specific than broad limits resulting from the following:

a. The nature of the not-for-profit entity (NFP)

b. The environment in which it operates

c. The purposes specified in its articles of incorporation or bylaws or comparable documents for an unincorporated association.

A donor-imposed restriction on an NFP's use of the asset contributed may be temporary or permanent. Some donor-imposed restrictions impose limits that are permanent, for example, stipulating that resources be invested in perpetuity (not used up). Others are temporary, for example, stipulating that resources may be used only after a specified date, for particular programs or services, or to acquire buildings and equipment.

Noncontrolling Interest

The portion of equity (net assets) in a subsidiary not attributable, directly or indirectly, to a parent. A noncontrolling interest is sometimes called a minority interest.

Permanently Restricted Net Assets

The part of the net assets of a not-for-profit entity (NFP) resulting from the following:

a. Contributions and other inflows of assets whose use by the NFP is limited by donor-imposed stipulations that neither expire by passage of time nor can be fulfilled or otherwise removed by actions of the NFP

b. Other asset enhancements and diminishments subject to the same kinds of stipulations

c. Reclassifications from or to other classes of net assets as a consequence of donor-imposed stipulations.

Permanent Restriction

A donor-imposed restriction that stipulates that resources be maintained permanently but permits the NFP to use up or expend part or all of the income or other economic benefits derived from the donated assets.

Promise to Give

A written or oral agreement to contribute cash or other assets to another entity. A promise carries rights and obligations—the recipient of a promise to give has a right to expect that the promised assets will be transferred in the future, and the maker has a social and moral obligation, and generally a legal obligation, to make the promised transfer. A promise to give may be either conditional or unconditional.

Temporarily Restricted Net Assets

The part of the net assets of a NFP resulting from the following:

a. Contributions and other inflows of assets whose use by the NFP is limited by donor-imposed stipulations that either expire by passage of time or can be fulfilled and removed by actions of the NFP pursuant to those stipulations

b. Other asset enhancements and diminishments subject to the same kinds of stipulations

c. Reclassification from or to other classes of net assets as a consequence of donor-imposed stipulations, their expiration by passage of time, or their fulfillment and removal by actions of the NFP pursuant to those stipulations.

Unrestricted Net Assets

The part of net assets of a NFP that is neither permanently restricted nor temporarily restricted by donor-imposed stipulations. The only limits on the use of unrestricted net assets are the broad limits resulting from the following:

a. The nature of the NFP

b. The environment in which the NFP operates

c. The purposes specified in the NFP's articles of incorporation or bylaws

d. Limits resulting from contractual agreements with suppliers, creditors, and others entered into by the NFP in the course of its business.

Unrestricted net assets generally result from revenues from providing services, producing and delivering goods, receiving unrestricted contributions, and receiving dividends or interest from investing in income-producing assets, less expenses incurred in providing services, producing and delivering goods, raising contributions, and performing administrative functions.

E**xcerpted from Section 958-210: Balance Sheet**

Classification of Net Assets

Subsection 45-9 The amounts for each of three classes of net assets—permanently restricted, temporarilyrestricted, and unrestricted—are based on the existence or absence of donor-imposed restrictions. Information about the nature and amounts of different types of permanent restrictions or temporary restrictions shall be provided either by reporting their amounts on the face of the statement or by including relevant details in notes to financial statements. Separate line items may be reported within permanently restricted net assets or in notes to financial statements to distinguish between permanent restrictions for both of the following holdings:

a. Assets, such as land or works of art, donated with stipulations that they be used for a specified purpose, be preserved, and not be sold

b. Assets donated with stipulations that they be invested to provide a permanent source of income. These result from gifts and bequests that create permanent endowment funds.

Subsection 45-10 Similarly, separate line items may be reported within temporarily restricted net assets or in notes to financial statements to distinguish between the following temporary restrictions:

a. Support of particular operating activities

b. Investment for a specified term

c. Use in a specified future period

d. Acquisition of long-lived assets.

Donors' temporary restrictions may require that resources be used in a later period or after a specified date (time restrictions), or that resources be used for a specified purpose (purpose restrictions), or both. For example, gifts of cash and other assets with stipulations that they be invested to provide a source of income for a specified term and that the income be used for a specified purpose are both time and purpose restricted. Those gifts often are called term endowments.

Subsection 45-11 Information about self-imposed limits also may be useful, including information about voluntary resolutions by the governing board of an entity to designate a portion of its unrestricted net assets to function as an endowment (sometimes called a board-designated endowment). That information may be provided in notes to or on the face of financial statements.

Excerpted from Section 958-225: Income Statement

Subsection 45-1 A statement of activities provided by a NFP shall focus on the entity as a whole and shall report the following amounts for the period:

a. The change in net assets

b. The change in permanently restricted net assets

c. The change in temporarily restricted net assets

d. The change in unrestricted net assets

Subsection 45-6 Pursuant to the Contributions Received Subsections of Subtopic 958-605, in the absence of a donor's explicit stipulation or circumstances surrounding the receipt of the contribution that make clear the donor's implicit restriction on use, contributions are reported as unrestricted revenues or gains (unrestricted support), which increase unrestricted net assets. The classification of contributions received as revenues or gains depends on whether the transactions are part of the NFP's ongoing major or central activities (revenues), or are peripheral or incidental to the NFP (gains). Donor-restricted contributions are reported as restricted revenues or gains (restricted support), which increase temporarily restricted net assets or permanently restricted net assets depending on the type of restriction. However, donor-restricted contributions whose restrictions are met in the same reporting period may be reported as unrestricted support provided that an NFP has a similar policy for reporting investment gains and income, reports consistently from period to period, and discloses its accounting policy.

Excerpted from Section 958-605: Revenue Recognition

Unconditional Promises to Give

Subsection 25-8 Pursuant to paragraph 958-605-25-2, an unconditional promise to give shall be recognized when it is received. However, to be recognized there must be sufficient evidence in the form of verifiable documentation that a promise was made and received.

Subsection 25-9 A communication that does not indicate clearly whether it is a promise is considered an unconditional promise to give if it indicates an unconditional intention to give that is legally enforceable. Legal enforceability refers to the availability of legal remedies, not the intent to use them.

Subsection 25-10 Solicitations for donations that clearly include wording such as information to be used for budget purposes only or that clearly and explicitly allow resource providers to rescind their indications that they will give are intentions to give rather than promises to give and shall not be reported as contributions.

Conditional Promise to Give

Subsection 25-11 Conditional promises to give, which depend on the occurrence of a specified future and uncertain event to bind the promisor, shall be recognized when the conditions on which they depend are substantially met, that is, when the conditional promise becomes unconditional. Imposing a condition creates a barrier that must be overcome before the recipient of the transferred assets has an unconditional right to retain those promised assets. For example, a transfer of cash with a promise to contribute that cash if a like amount of new gifts are raised from others within 30 days and a provision that the cash be returned if the gifts are not raised imposes a condition on which a promised gift depends.

Subsection 25-12 A conditional promise to give is considered unconditional if the possibility that the condition will not be met is remote. See paragraph 958-605-55-16 for examples of conditions that are remote of occurrence.

Subsection 30-2 Contributions received shall be measured at their fair values. Topic 820 establishes a framework for measuring fair value. See the Fair Value Option Subsections of Subtopic 825-10 for guidance about electing at initial recognition to subsequently measure financial instruments and certain other contracts at fair value.

Unconditional Promises to Give

Subsection 30-4 If present value techniques are used to measure the fair value of unconditional promises to give, the entity shall determine the amount and timing of the future cash flows of unconditional promises to give cash (or, for promises to give noncash assets, the quantity and nature of assets expected to be received). In making that determination, the entity shall consider all the elements in paragraph 820-10-55-5, including the following:

a. When the receivable is expected to be collected
b. The creditworthiness of the other parties
c. The entity's past collection experience
d. The entity's policies concerning the enforcement of promises to give
e. Expectations about possible variations in the amount or timing of the cash flows (that is, the uncertainty inherent in the cash flows)
f. Other factors concerning the receivable's collectibility.

Subsection 30-5 If present value techniques are used to measure fair value, the present value of unconditional promises to give should be measured using a discount rate that is consistent with the general principles for present value measurement discussed in paragraphs 820-10-55-5 through 55-9. In conformity with paragraph 835-30-25-11, the discount rate shall be determined at the time the unconditional promise to give is initially recognized and shall not be revised subsequently unless the entity has elected to measure the promise to give at fair value in conformity with the Fair Value Option Subsections of Subtopic 825-10.

Subsection 30-6 Unconditional promises to give that are expected to be collected in less than one year may be measured at net realizable value because that amount results in a reasonable estimate of fair value.

Subsection 30-7 If a promise to give has not previously been recognized as contribution revenue because it was conditional, fair value shall be measured when the conditions are met.

Contributions Received

Subsection 45-3 Contributions received by not-for-profit entities (NFPs) shall be reported as restricted support or unrestricted support. An NFP shall distinguish between contributions received with permanent restrictions, those received with temporary restrictions, and those received without donor imposed restrictions. Contributions without donor-imposed restrictions shall be reported as unrestricted support that increases unrestricted net assets.

Subsection 45-4 Restricted support increases permanently restricted net assets or temporarily restricted net assets. A restriction on an NFP's use of the assets contributed results either from a donor's explicit stipulation or from circumstances surrounding the receipt of the contribution that make clear the donor's implicit restriction on use. Contributions with donor-imposed restrictions shall be reported as restricted support; however, donor-restricted contributions whose restrictions are met in the same reporting period may be reported as unrestricted support provided that an NFP has a similar policy for reporting investment gains and income (see paragraph 958-320-45-3), reports consistently from period to period, and discloses its accounting policy.

Distinguishing Between Donor-Imposed Conditions and Donor-Imposed Restrictions

Subsection 55-15 Distinguishing between a condition stipulated by a donor and a restriction on the use of a contribution imposed by a donor may require the exercise of judgment. Conditional transfers are not contributions yet; they may become contributions upon the occurrence of one or more future and uncertain events. Because of the uncertainty about whether they will be met, conditions imposed by resource providers may cast doubt on whether the resource provider's intent was to make a contribution, to make a conditional contribution, or to make no contribution. As a result of this uncertainty, donor-imposed conditions should be substantially met by the entity before the receipt of assets (including contributions receivable) is recognized as a contribution. In contrast to donor imposed conditions, donor-imposed restrictions limit the use of the contribution, but they do not change the transaction's fundamental nature from that of a contribution.

Subsection 55-16 If donor stipulations do not clearly state whether the right to receive payment or take delivery depends on meeting those stipulations, or if those stipulations are ambiguous, distinguishing a conditional promise to give from an unconditional promise to give may be difficult. First, review the facts and circumstances surrounding the gift and communicate with the donor. If the ambiguity cannot be resolved as a result of those efforts, presume that a promise containing stipulations that are not clearly unconditional is a conditional promise to give. However, if the possibility that the condition will not be met is remote, a conditional promise to give is considered unconditional. For example, a stipulation that an annual report must be provided by the donee to receive subsequent annual payments on a multiyear promise is not a condition if the possibility of not meeting that administrative requirement is remote.

Subsection 55-17 A challenge grant is a common form of a conditional promise to give. For example, a resource provider promises to contribute $1 for each $1 of contributions received by a NFP, up to $100,000, over the next 6 months. As contributions are received from other resource providers, the conditions would be met and the promise would become unconditional. For example, if $10,000 is received in the first month from donors, $10,000 of the conditional promise would become unconditional and should be recognized as contribution revenue.

Excerpted from Section 958 – 810: Consolidation

Presentation of Noncontrolling Interests

Subsection 45-1 Noncontrolling interests in the equity (net assets) of consolidated subsidiaries shall be reported as a separate component of the appropriate class of net assets in the consolidated statement of financial position of a NFP. That amount shall be clearly identified and described (for example, as noncontrolling ownership interest in subsidiaries) to distinguish it from the components of net assets of the parent, which includes the parent's controlling financial interest in its subsidiaries. The effects of donor-imposed restrictions, if any, on a partially owned subsidiary's net assets shall be reported in accordance with Subtopics 958-205 and 958-320.

NOTES

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PERFORMANCE COUNTS

Best Practices for CDFI Financial Statements and Management