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Non-Profit Notes Newsletter

Reporting Management and General Expenses: Getting It Right under FASB ASU 2016-14

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As required by the Financial Accounting Standards Board's (FASB) Accounting Standards Update (ASU) 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities*, not-for-profit organizations (NFPs) must include in their financial statements or note disclosures total expenses by function and natural class. Functional expense classifications include major classes of program services and supporting activities. The new ASU also requires enhanced disclosure regarding the method(s) used to allocate indirect expenses, or those costs allocated to more than one activity.

As defined by the FASB:

> *Program services are the activities that result in goods and services being distributed to beneficiaries, customers, or members that fulfill the purposes or mission for which the NFP exists. Those services are the major purpose for and the major output of the NFP and often relate to several major programs.*

Most NFPs are quite familiar with the program services expenses associated with their mission. But, in some cases, NFP organizations are hesitant as to which expenses should be identified as supporting activities, particularly those classified as management and general.

Supporting activities are all activities of an NFP other than program services. They generally include the following:

- Management and general activities
- Fundraising activities
- Membership development activities

Management and General Activities

As stated above, NFPs are, at times, unsure how to categorize certain expenses as management and general. According to FASB guidance, management and general activities include the following:

a. Oversight
b. Business management
c. General recordkeeping and payroll
d. Budgeting
e. Financing, including unallocated interest costs
f. Soliciting funds other than contributions and membership dues; for example, the costs associated with:

    1. Promoting the sale of goods or services to customers, including advertising cost
    2. Responding to government, foundation, and other requests for proposals for customer-sponsored contracts for goods and service
    3. Administering government, foundation, and similar customer-sponsored contracts, including billing and collecting fees and grant and contract financial reporting
g. Disseminating information to inform the public of the NFP's stewardship of contributed funds
h. Making announcements concerning appointments
i. Producing and disseminating the annual report
j. Employee benefits management and oversight (human resources)
k. All other management and administration expenses except for direct conduct of program services, fundraising activities, or membership development activities.

The costs of oversight and management usually include the salaries and expenses of the governing board, the chief executive officer of the NFP, and the supporting staff. However, if such personnel spend a portion of their time *directly* conducting or supervising program services or categories of other supporting services, their salaries and expenses shall be allocated among those functions.

Allocating Expenses from Management and General Functions

FASB guidance contains several examples of certain management and general activities that illustrate direct conduct and direct supervision of program or support activities which, accordingly, should be allocated to the program or support functions that receive a benefit:

Example A: Chief Executive Officer Allocation

The broad responsibilities of a chief executive officer generally include administrative and programmatic oversight. At Not-for-Profit Entity A (NFP A), the chief executive officer spends a portion of time directly overseeing the research program. Additionally, a portion of time is spent with current and potential donors on fundraising cultivation activities. A portion of the chief executive officer's compensation and benefits and other expenses would be allocated to the research program and to the fundraising function representing the portion of time spent on those activities because they reflect *direct conduct* or *direct supervision*. If the remainder of the chief executive officer's time is spent indirectly supervising the other areas of NFP A, including the administrative areas, those activities would not constitute direct conduct or direct supervision, and the ratable portion of compensation and benefit amounts would remain in management and general activities.

Example B: Chief Financial Officer Allocation

The chief financial officer at Not-for-Profit Entity B (NFP B) has primary responsibility for (a) accounting and reporting, (b) short-term budgeting and long-term financial planning, (c) cash management, and (d) direct oversight of NFP B's endowment. A portion of the chief financial officer's compensation and benefits and other expenses would be allocated to management and general activities for the accounting and reporting, the short-term budgeting and long-term financial planning, and cash management functions because they benefit the overall organization. A portion also would be allocated to investment expenses for management of the investment strategy of the endowment and would be netted against investment return. However, any portion of time spent supervising the accounting for investments or other fiduciary oversight would not be allocated to investment expenses because that time is related to an accounting and general management activity that benefits the overall organization and should be allocated to management and general activities.

Example C: Human Resources Department Allocation

The human resources department at Not-for-Profit Entity C (NFP C) generally is involved in the benefits administration for all personnel of NFP C. The human resources department's related costs would not be allocated to any specific program. Rather, those costs would remain a component of management and general activities because benefits administration is a supporting activity for the entire entity.

Example D: Grant Accounting and Reporting Allocation

Not-for-Profit Entity D (NFP D) receives federal grants and employs an accountant who is responsible for grant accounting and reporting. In some cases, under the terms of the grant agreement, a fiscal report is required to be filed that details expenses incurred and charged against the grant. The fiscal report is not part of the direct conduct or direct supervision of the grant but rather is an accounting function. Therefore, the grant accountant's compensation and benefits would not be allocated to the programmatic area. However, a scientific report prepared by a principal investigator who is responsible for the research activity would be indicative of direct conduct and/or direct supervision of the grant activity, and the principal investigator's compensation and benefits would be allocated to the grant.

Required Disclosure

The information required to be disclosed by the ASU includes the cost allocation method(s) used to allocate costs of activities identifiable with one or more programs, fundraising, or membership-development. The ASU provides the following example of the required note disclosure:

Note X. Methods Used for Allocation of Expenses from Management and General Activities

The financial statements report certain categories of expenses that are attributable to one or more program or supporting functions of the Organization. Those expenses include depreciation and amortization, the president's office, communications department, and information technology department. Depreciation is allocated based on square footage, the president's office is allocated based on estimates of time and effort, certain costs of the communications department are allocated based on estimates of time and effort, and the information technology department is allocated based on estimates of time and costs of specific technology utilized.

Contact Us

If you have any questions about properly reporting functional expenses — or not-for-profit accounting and auditing matters in general — please contact Mark Piszko, CPA, CGMA, Partner-in-Charge, Not-for Profit Services, at mpiszko@pkfod.com or 646.449.6316 or the partner in charge of your account.

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