Giving Outlook

How the New Tax Law Has Affected Nonprofits

Did the Tax Cuts and Jobs Act have a significant impact on charitable giving in the U.S.? When the new law was issued, there were dire predictions that it would affect nonprofits in an extremely negative way, especially smaller, community-based organizations. And in 2018, individuals did give less to charity than in the prior year.

But what was responsible? Was the fourth-quarter decline in the stock market the primary contributor? Or was it the new tax law?

Four Changes
The new tax law included four changes with the potential to affect charitable giving:

1. Standard deduction increase: Doubling the standard deduction for individuals and families significantly reduced the number of households itemizing deductions, down from 33 percent to 5 percent, according to the Congressional Joint Committee on Taxation.

2. AGI limit: The new law increased the limit on deductions for charitable contributions from 50 percent to 60 percent of adjusted gross income (AGI).

3. Estate and gift tax exemption: Doubling the estate and gift tax exemption for individuals and couples lowered the tax burden on heirs. This had the potential to reduce the incentive for wealthy contributors to consider bequests as part of their estate planning.

4. Corporate tax rate: A reduction in the corporate tax rate from 35 percent to 21 percent not only spurred corporate profits and improved the economy, but it also reduced the tax benefits to be gained by charitable giving.

The Numbers
How did these changes actually affect the numbers in 2018? According to “Giving USA 2019: The Annual Report on Philanthropy for the Year 2018,” total charitable giving rose 0.7 percent over 2017.

Here’s a by-the-numbers summary:
• Individual giving (68 percent of total) declined 1.1 percent.
• Foundation giving (18 percent of total) increased 7.3 percent.
• Bequests (9 percent of total) remained flat.
• Corporate giving (5 percent of total) increased 5.4 percent.

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Consider the Nature of a Transfer of Assets

In June 2018, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2018-08 to provide guidance about accounting for nonprofit organizations’ grants and contracts. This new ASU clarifies when to account for a transfer of assets as an exchange transaction versus as a contribution and how to determine whether a contribution is unconditional or conditional.

The first determination is important because these two types of transactions are governed by different accounting standard codifications. Exchange transactions are covered by ASC 606, Revenue from Contracts with Customers, while contributions fall under ASC 958-605, Not-for-Profit Entities – Revenue Recognition.

If the transaction is considered a contribution, the new ASU also provides guidance on how to determine if the contribution is conditional or unconditional. A contribution is conditional if it satisfies both of the following criteria:

1. Specific barriers are in place that the recipient must overcome to gain access to the contribution.
   - “Barriers” include performance-related or other measurable barriers such as a specific outcome, a matching requirement, or an achievement of a certain level of service or units of output. Limits on the recipient’s discretion about how to conduct an activity are also considered to be a barrier, as is a stipulation related to the purpose of the agreement.

2. If the barriers are not met, the donor is released from its obligation or the recipient must return any advanced assets.

Conditional or Unconditional?

Next, the nonprofit organization must determine whether the contribution is conditional or unconditional. A contribution is conditional if it satisfies both of the following criteria:

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   - “Barriers” include performance-related or other measurable barriers such as a specific outcome, a matching requirement, or an achievement of a certain level of service or units of output. Limits on the recipient’s discretion about how to conduct an activity are also considered to be a barrier, as is a stipulation related to the purpose of the agreement.

Ask for Assistance

ASU 2018-08 will go into effect for resource recipients after December 15, 2019. Please contact your CPA to discuss your grants and contracts and how to implement this guidance.

Our team can help you make these determinations. Call us today to discuss next steps.

Word to the Wise

Consider the Nature of a Transfer of Assets

Exchange Transaction vs. Contribution

The new ASU has a robust framework to determine whether a transaction is considered to be an “exchange transaction” or a “contribution.”

In an exchange transaction, the donor transfers assets and receives commensurate value in return. According to the ASU, nonprofit organizations must use two criteria to determine if the donor (resource provider) is receiving commensurate value:

1. The resource provider—a private foundation, government agency, or other organization—is not synonymous with the general public. Indirect benefit received by the public as the result of the transaction doesn’t constitute commensurate value received by the resource provider.

2. Furthering the resource provider’s mission or generating “positive sentiment” by acting as a donor doesn’t constitute commensurate value for the purposes of the ASU.

Note that, consistent with GAAP, if the resource provider is not itself receiving commensurate value, the nonprofit organization must determine whether the transfer represents a payment from a third-party payer on behalf of an existing exchange transaction between the recipient and an identified customer. If so, other FASB guidance applies.

If the nonprofit organization determines that the resource provider receives no commensurate value, the transaction is considered a contribution.
UBTI and Parking

Yes, Employee Parking Is Really Taxable

One of the more confusing provisions of the 2017 Tax Cuts and Jobs Act is that employer-provided parking is now considered unrelated business taxable income (UBTI)—and is therefore taxable. In other words, if you provide a parking benefit for your employees, you may need to pay unrelated business income tax (UBIT) on that expense.

As a reminder, UBTI is income that a nonprofit organization generates from a trade or business that is regularly carried on and is not substantially related to the organization’s mission or “exempt” purposes. If your organization owns or leases a parking lot or pays employee parking expenses, you are affected.

Parking = QTF

Why the confusion? The tax law now includes parking as a qualified transportation fringe benefit (QTF) and mandates that all expenses related to QTF be considered UBTI. Previously, these expenses could be deducted.

To clarify, the new IRC Section 274 denies all employers—for-profit entities as well as nonprofits—a deduction for expenses paid or incurred for employee parking after December 17, 2017.

To create parity between for-profit and nonprofit entities, a new Section 512(a)(7) requires nonprofits to increase their UBTI by the amount of employee parking expenses that would not be deductible if they were subject to the same deduction disallowances as for-profit companies. Now, nonprofit entities must pay tax of up to 21 percent on the amount of any disallowed parking expenses.

Calculating the Taxable Benefit

In December 2018, the IRS released Notice 2018-99 outlining the process to calculate this additional tax based on the “total parking expenses” paid to provide employee parking. These expenses include repairs and maintenance, rent or lease payments, interest, insurance, property taxes, landscape costs, utilities, parking attendant and security expenses, cleaning, and maintenance such as snow, leaf, and trash removal.

If your organization pays a third party for employee parking spots, the deduction and increase to UBTI is calculated as the total annual cost for parking paid to the third party.

If your organization owns or leases a parking facility, the IRS provides a four-step methodology for calculating the expense:

1. Calculate the disallowance for reserved employee parking. Any spots specifically reserved for employees are automatically disallowed and therefore taxable.
2. Determine the primary use of the remaining spots during normal working hours. If the “primary use” of 50 percent or more of the remaining spots is public usage, then the remaining total parking expense is excluded from the calculation. If your facility has greater than 50 percent public usage, your organization can skip the next two steps.
3. Calculate the allowance for reserved nonemployee spots, such as customers, patients, visitors, or congregants. These expenses continue to be an allowable expense.
4. Determine remaining use and allocable expenses. Allocate the remaining expenses not accounted for in steps 1–3 and add them to the amount in step 1 to determine the total taxable expense.

Stay Tuned

Until the IRS provides further guidance, nonprofits might want to consider changing their employee parking arrangements and determining how to reduce total parking expenses.

Let’s talk about ways to reduce your UBTI related to employee parking.

Tax Effects on Giving

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What Can You Do?

The good news is that donations increased in two major funding sources—corporations and foundations. Part of your strategy should be to follow the money.

Engage with corporate donors to ask how the new tax law is affecting their philanthropy strategy. With this insight, create a path to help them achieve their goals. Revisit corporate donors who declined in the past and update their awareness of your mission.

The same strategy can be applied to foundations. Perhaps they are now in a position to increase funding levels.

For individual donors, think high and low. Lower tax rates and a strong market mean high net-worth individuals are likely to have more disposable income and may be ready to contribute a larger first-time gift or increase from prior giving levels. The increased standard deduction has less of an effect on this level of donor.

Lower-level donors give because of your mission, not the tax benefit. Consider ramping up your direct appeals—direct mail and annual outreach—to these donors and make the case for why you need their help now more than ever. This new tax environment could provide good support for your message.

The Forecast

Despite gloomy predictions, 2018 turned out to be a good year for many nonprofits. For the time being, while unfavorable tax rules may depress individual giving, the economy has people feeling positive and generous.

Knowing your donors and how they react to economic changes is a good long-term strategy. Armed with this insight, you can adjust your message and your outreach to make the most of the current economic and tax climates.
COSO Provides Framework for Internal Controls

In 1992, the Committee of Sponsoring Organizations of the Treadway Commission (COSO) developed a flexible framework for designing, implementing, and evaluating internal controls. Internal controls help reduce fraud, improve accuracy and financial reporting, and maintain consistent practices across an organization.

Updated in 2013, the COSO framework isn’t a legal requirement but is considered a best practice and is widely adopted in the U.S. The framework is built around five core concepts, further broken down into 17 principles that provide guidelines on how to achieve the goals of the corresponding concept.

COSO’s core concepts include the following:

- **Control environment**—the set of standards, processes, and structures that provide the basis for carrying out internal controls
- **Risk assessment**—the process for identifying and assessing organizational risks
- **Control activities**—actions that help ensure that management’s risk management directives are carried out
- **Information and communication**—the flow of information necessary to support the internal control function, including communication between internal and external stakeholders
- **Monitoring**—ongoing performance evaluation and reporting of any deficiencies found

COSO emphasizes that all five components must be in place and functioning in order to be effective. This doesn’t mean your executive team can’t determine which controls are most appropriate. As a principle-based framework, COSO is designed to provide flexibility.

Remember, the ability to achieve your mission is sometimes based on your most valuable asset—your reputation. Adopting COSO conveys to regulators, volunteers, and donors that your organization is committed to good governance and accountability.

As with any framework, it can be difficult to turn abstract concepts into operational outcomes. Understanding the cost-benefit relationship for certain controls and quantifying the organization’s risk tolerance may require outside expertise.