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RELIGIOUS ORGANIZATION GUIDE: BEST PRACTICES & INSIGHTS

THE ESSENTIAL GUIDE FOR RELIGIOUS INSTITUTIONS

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We are thrilled to present our Financial and Governance Guide for Religious Nonprofit Organizations, created to address the key challenges that faith-based institutions often encounter. As a CPA firm with extensive experience in serving religious-oriented nonprofits, we've designed this guide to offer practical insights into financial management, compliance, and governance—issues we regularly see facing our clients.

This guide is organized to provide a clear and cohesive understanding of essential topics:

1. NET ASSETS

Delivers a comprehensive explanation of net asset classifications under FASB (*with and without donor restrictions*) and shares strategies to avoid common mistakes when tracking restricted funds.

2. UNDERSTANDING FUND ACCOUNTING: A KEY TO TRANSPARENT FINANCIAL MANAGEMENT

A deep dive into fund accounting principles, offering best practices to ensure transparency in managing restricted and designated funds.

3. NEW YORK RELIGIOUS CORPORATIONS FACE A DOUBLE-BARRELED LEGAL AND GOVERNANCE CHALLENGE (PLUS BONUS ROUND: ENDOWMENT BASICS)

Explores the complexities of governance under New York's Religious Corporations Law and Not-for-Profit Corporation Law, including an insightful look at endowment management.

4. REVENUE RECOGNITION UNDER ASC 606 AND ASC 958 FOR FAITH-BASED NONPROFIT ORGANIZATIONS

Clarifies the FASB standards for recognizing income from contributions and exchange transactions, including tithes, event fees, grants, and more.

5. 5 BEST PRACTICES YOU NEED TO KNOW ABOUT ACCOUNTING FOR YOUR RELIGIOUS ORGANIZATIONS

Highlights five critical strategies that will improve financial management, from leveraging outsourcing to adopting digital-age practices.

6. NAVIGATING U.S. GAAP VS. INTERNAL FINANCIAL REPORTING FOR RELIGIOUS NONPROFITS

Explores the key differences between GAAP financial reporting and internal budgeting tools in religious nonprofits, offering leaders practical strategies to bridge the gap for stronger financial stewardship and mission-driven decision-making.

7. PREPARING A STATEMENT OF FUNCTIONAL EXPENSES FOR FAITH-BASED NONPROFITS

Walks you through the process of classifying and allocating expenses to ensure clear and compliant financial reporting.

8. NAVIGATING FOREIGN OPERATIONS: PRACTICAL CONSIDERATIONS FOR RELIGIOUS NONPROFITS

Provides guidance on managing international operations, with practical considerations and a focus on IRS Form 990 and handling foreign currency translations.

This guide is designed to equip your organization with the knowledge and tools to enhance financial stewardship, mitigate risk, ensure compliance, and build donor trust. We encourage you to share this valuable resource with your leadership team and board members.

If you have any questions or would like personalized support, please reach out to our team at Cerini & Associates. We are committed to helping your organization achieve financial excellence and fulfill its mission-driven goals.

Matthew Burke, CPA
Partner





NET ASSETS

Under the **Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-14**, net assets of nonprofit organizations are required to be split into two main categories: net assets with donor restrictions and net assets without donor restrictions. These two main categories are further broken down as well. In this article, we will cover what these categories mean and certain things to look out for to ensure compliance with these net asset categories.

NET ASSETS WITH DONOR RESTRICTIONS

Net assets with donor restrictions are funds that are restricted by donors as to time or purpose. An example of funds that are restricted as to the passage of time would be a \$100,000 contribution where \$50,000 is for the year ended December 31, 2024 and \$50,000 is for the year ended December 31, 2025. Examples of funds that are restricted as to purpose could look like a \$100,000 contribution that must be spent on a specific program, a scholarship fund, or a building project, just to name a few. Once the donor-restricted funds have been spent according to those donors' stipulations, the funds can be "released" from restrictions. In the examples above, the time-restricted contribution would have \$50,000 of releases during the year ended December 31, 2024 and \$50,000 of releases during the year ended December 31, 2025. The purpose-restricted contribution would be released upon spending the funds (*i.e. incurring expenses or spending on capital projects*) on the specific program, scholarship fund, or building project.

The particular types of donor-restricted net assets mentioned above were formerly known as "**temporarily restricted**" because the funds are only restricted until the donor's stipulation is fulfilled. However, there are also donor-restricted contributions that can be maintained in perpetuity, formerly known as "**permanently restricted.**" These contributions typically consist of a principal portion that cannot be spent but are typically held in an income-generating account or investment whereby the interest and dividend income that is generated can be spent, albeit still in accordance with the donors' stipulations. Commonly, these perpetual contributions are classified as endowments. Please read the other piece in this guide written by David Goldstein for more useful information about endowment funds.

NET ASSETS WITHOUT DONOR RESTRICTIONS

Net assets without donor restrictions are funds of an organization that do not have donor-imposed restrictions on them. Generally speaking, these funds can be used for any purpose that is aligned with an organization's exempt mission and purpose. The Board of Directors of an organization may decide that it would be appropriate to set aside a portion of these funds, which would be referred to as Board-designated net assets. Oftentimes, these funds are set aside as reserves. Operating reserves typically serve as a rainy-day fund and may set aside 3-6 months of expenses. Capital reserves are typically designated for future building repairs, purchases of equipment, or expansion projects. The Board could designate funds with the intention of launching a new program. Boards can also designate funds for financial stability, including setting aside funds to pay off a particular debt or setting up a Board-designated endowment (*which is not a technical "endowment" for legal purposes*) or quasi-endowment to invest a principal amount that would generate future revenue to use in the organization's operations.

Similar to releases of donor-restricted net assets mentioned earlier, Board-designated net assets also maintain stipulations whereby only the Board of Directors has the ability to remove these designations. Sometimes, there are Board-designated net assets that were set aside so long ago that it may not make sense for the organization to have these funds tied up anymore, in which case, a Board may vote to remove the designation.



OVERCOMING COMMON ISSUES WITH DONOR RESTRICTIONS AND BOARD DESIGNATIONS

First and foremost, the organization needs to ensure that its opening net assets agree to the prior year-end balances for the purposes of its accounting records. This provides an accurate starting point for tracking the different categories of net assets.

It's imperative that donor-restricted and Board-designated net assets be tracked throughout the year for the most accurate financial reporting. Depending on the complexity of the organization, accounting software abilities, and management preferences, there are a few ways that these funds can be tracked. Some accounting systems offer classes or cost centers as a function. Every relevant transaction that is then entered into the accounting system is assigned a class or cost center so that when reports are generated from the system, it is easily distinguishable where donor-restricted or board-designated funds have received grants, contributions, or investment income, as well as the specific expenses incurred which allow the organization to see how the funds were spent. This tracking becomes important because sometimes donors who have restricted contributions require reporting back to them on how the funds were spent. It also helps the organization see when funds are fully spent. "Negative" balances in net assets with donor restrictions and Board-designated funds are not permissible. This would be indicative of the organization spending funds from its own general operations rather than showing that a donor-restricted or Board-designated fund was "overspent." Additionally, this tracking ensures that funds aren't being comingled or "double-dipped." If a donor contributes to an organization for a specific purpose, it's important (and a legal requirement) that the organization doesn't spend the donor's contribution on anything other than that purpose. Frequently, organizations will receive multiple contributions that are meant to fund the same purpose, such as a specific individual's salary. The organization should ensure that if multiple contributions are funding the same individual's salary, that the total of those contributions doesn't exceed that particular salary, otherwise it insinuates that multiple donors paid for the same salary, or that it was simply not spent in accordance with the donor's restriction.

Sometimes things get a bit convoluted when reporting occurs. These donor-restricted or Board-designated funds generally come in the form of cash or investments, or sometimes they're reflected as receivables because a donor could pledge a contribution, but the actual funds haven't been received yet. So not only is it important to track the revenue and expenses of these donor-restricted or Board-designated funds, it's also important to track the related assets to ensure there's enough assets to cover those restrictions or designations. As a simple example, if a donor restricts a cash contribution of \$100,000 for the purpose of funding certain expenses, and those expenses totaled \$75,000 for the year, there should be \$25,000 of restricted cash within the assets of the organization at the end of the year. If there isn't enough cash on hand at the end of the year to cover the ending balance of net assets with donor restrictions (assuming it's all sitting in cash), then this says the organization spent donor-restricted funds on general operating expenses, which is not permissible, so this should be tracked carefully.


Additionally, the undesignated net assets without donor restrictions balance should be positive if there are any net assets with donor restrictions or Board-designated net assets. If the undesignated net assets without donor restrictions fall into a deficit position, this says that the organization has tapped into the donor-restricted or Board-designated funds for general operating purposes, which again, is not permissible.

In summary, without proper maintenance, internal controls, and financial reporting, funds may be used improperly, which could expose the organization to unwanted legal exposure. It can't be stressed enough that donor restricted funds and Board-designated funds need to be tracked and maintained carefully to ensure they are compliant with the specific intents of those funds.



Cystal is a member of Cerini & Associates' audit staff, where she focuses on serving nonprofit and religious organizations, as well as for-profit entities and employee benefit plans. She has experience performing assurance and outsourced accounting work, along with preparing tax returns. Crystal has extensive knowledge of the operations, internal controls, and financial environments specific to the sectors she serves. She brings her expertise, diverse background, and supportive approach to all of her engagements and understands the importance of being a year-round resource to her clients. Crystal stays current on industry trends, government regulations, and accounting standards, ensuring her clients are informed and prepared.

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UNDERSTANDING FUND ACCOUNTING: A KEY TO TRANSPARENT FINANCIAL MANAGEMENT

WHAT IS FUND ACCOUNTING?

Fund accounting is a specialized method of accounting used by nonprofit organizations, specifically religious institutions such as churches and synagogues, based on the principle that resources should be tracked separately according to their intended use. Organizations not only need to know how much money they have made, spent, and have left over, but also how much they have made, spent, and have left over for various purposes. Fund accounting streamlines the tracking and reporting of financial resources that are earmarked for specific purposes by donors and governing bodies to ensure that resources are being allocated and spent in line with the organization's mission and donor intentions.

WHAT ARE FUNDS?

A fund is an area of the organization that needs to be tracked separately from general operating activity. Examples of funds may include, but are not limited to, capital project funds, endowment funds, special project funds, grant funds, etc. Each fund has a self-balancing set of accounts comprised of its own assets, liabilities, net assets, revenue, and expenses. Funds can be thought of as mini organizations within the organization as a whole. When combined, the funds create the organization's financial statements. If you find yourself asking, "Do I need to know how much money is set aside for X purpose?" then you'll likely want to set up a fund to **(1) segregate the receipt of financial resources restricted or designated for X purpose from unrestricted or undesignated financial resources**, **(2) segregate the spending of restricted or designated resources from general operations**, and **(3) determine what is left to spend for X purpose**.

WHY USE FUND ACCOUNTING?

- ▶ **Ensures Accountability** – Fund accounting allows organizations to be transparent with donors, grantors, and the public regarding how their donations are being used in accordance with their intended purpose, as well as how the donations are benefitting the organization and the community. This is crucial for organizations that rely heavily on donations as transparency is a key factor in retaining major and recurring donors.
- ▶ **Facilitates Fund Management** – Many nonprofits receive restricted donations for which organizations are required to spend the donations in compliance with donor-imposed stipulations. Fund accounting assists organizations in complying with these restrictions by isolating restricted financial resources from financial resources available for spending on general operations. It also provides transparent reports to ensure that restricted funds are not accidentally used for other purposes.
- ▶ **Enhances Budgets and Promotes Discipline** – Fund accounting allows organizations to manage and allocate their financial resources effectively by ensuring expenditures align with the specific purpose of each fund. By tracking expenditures within each fund, organizations can ensure they do not overspend allocated budgets and will be able to track expenditures against levels of available financial resources.
- ▶ **Enhances Reporting** – By building funds into your chart of accounts, reports outlining the financial resources available for spending for various purposes can be generated by the click of a button in your accounting software.
- ▶ **Reduces the Need for Subsidiary Schedules Outside of the Accounting Software** – Nonprofits that have not implemented fund accounting typically use Excel or other spreadsheets to track additions and releases of donor restricted money. Fund accounting reduces the need for subsidiary and manual reports because all activity is already being captured in the fund's chart of accounts. This streamlines the accounting function and allows for real-time reporting.

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FUND ACCOUNTING BEST PRACTICES

1. USE ACCOUNTING SOFTWARE DESIGNED FOR FUND ACCOUNTING

Choosing an accounting software application that fits the needs of your organization is important to effectively implement fund accounting. Key features to look for in accounting software include fund segregation, grant management, detailed financial reporting, budgeting tools, donor management, integration with other systems, a user-friendly interface, and scalability. While general accounting software can be adapted to meet the needs of a nonprofit organization, such as using classes in QuickBooks to segregate fund activity, specialized nonprofit accounting software, such as Fund EZ and NetSuite, offer additional functionalities that are better suited for large organizations with various funds.

2. CATEGORIZE FUNDS BASED ON PURPOSE AND SOURCE

Separate funds should be created for each unique purpose. Activity not designated or restricted for a specific purpose should be recorded in a general fund. Keep in mind that too many funds with overlapping purposes can overcomplicate and add complexity to your chart of accounts. Clear documentation should be retained to support the receipt of restricted donations and their intended use.

3. AVOID PHYSICALLY SEGREGATING ASSETS BY FUND UNLESS LEGALLY REQUIRED

Although each fund has its own set of accounts with assets, liabilities, and a fund balance, creating a separate bank account for each fund is unnecessary (*unless required by donors restricting funds*) and adds complexity. For example, all cash can be maintained in the general fund checking account. Money collected for specific purposes will be captured as an asset in the restricted fund through an interfund journal entry to move financial resources between funds without having an impact on the organization's financial statements as a whole.

4. REGULARLY REVIEW FUND BALANCES

Accounting personnel should review fund balances and activity on a regular basis to ensure that what is being reported appears to be in line with the operations of the organization. For example, if the organization recently received a large donation to be spent on a specific project, but that project's fund balance does not reflect the donation, an interfund journal entry may be needed to move the financial resources from the general fund to the project's fund.

5. CONSIDER PROVIDING DONORS WITH A LIST OF PROJECTS TO SUPPORT

If a donor stipulates that their donation be used for a purpose for which there is not already a restricted fund set up, a new fund will need to be created. By providing donors with a list of projects to support, **(1)** *they may be more likely to donate due to awareness of how their donations will be spent* **(2)** *they will choose to donate to a fund that already exists and for a project that your organization is promoting, eliminating the requirement to create a new fund.*

Fund accounting is an essential tool for nonprofit organizations and specifically religious institutions that manage restricted and Board-designated funds. By categorizing funds based on their purposes and restrictions, fund accounting enhances transparency, accountability, and compliance, ensuring that funds are used as intended. While it can be complex and resource-intensive, with the right systems in place, fund accounting can greatly improve an organization's financial management and performance.



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aclyn is a member of Cerini & Associates' audit staff where she focuses primarily on serving nonprofit clientele. With a strong foundation in nonprofit accounting standards and a nuanced understanding of the operational and compliance challenges religious and faith-based organizations face, Jaclyn contributes technical expertise and has a deep respect for mission-driven work. She brings a detail-oriented yet mission-focused approach and partners with organizations to strengthen internal controls, ensure regulatory compliance, maintain transparency, and enhance financial stewardship.

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DOUBLE-BARRELED LEGAL AND GOVERNANCE CHALLENGE

(PLUS BONUS ROUND:
ENDOWMENT BASICS)



New York religious corporations face a double-barreled legal and governance challenge. That is because there are two separate New York statutes that deal with the governance fundamentals of religious corporations. First, and obviously, there is the Religious Corporations Law, under which New York religious corporations are incorporated and which has extensive governance provisions. But Section 2-b of the Religious Corporations Law makes the New York Not-for-Profit Corporation Law applicable to religious corporations with some limited exceptions and carve outs. So, while a New York not-for-profit corporation is governed by, and must comply with, the New York Not-for-Profit Corporation Law, a New York religious corporation is governed by, and must comply with, the provisions of both the New York Not-for-Profit Corporation Law and the Religious Corporations Law.

Many New York religious corporations are surprised to discover, for example, that the incredibly demanding provisions of the Not-for-Profit Corporation Law regarding a required conflict of interest policy, and also governing conflicts of interests and related party transactions, apply fully to religious corporations. So too, the incredibly demanding provisions of the Not-for-Profit Corporation Law regarding a required investment policy, and also governing the prudent management of institutional funds and investments (*also known as the New York Prudent Management of Institutional Funds Act, or by its acronym, NYPMIFA*), apply fully to religious corporations. And additionally, the incredibly demanding provisions of the Not-for-Profit Corporation Law regarding a required whistleblower policy for organizations of a certain size, and also governing whistleblower protections and procedures for those organizations, apply fully to religious corporations. And this is just the tip of the proverbial iceberg! The Not-for-Profit Corporation Law is jam-packed with detailed and demanding provisions that apply to, and govern, religious corporations.

A telling fact that many people, including lawyers, do not realize about the Religious Corporations Law is that it was written, and went into effect, in the first decade of the twentieth century. The Religious Corporations Law was enacted in 1909. That is almost 120 years ago. And the Religious Corporations Law has been very sparingly updated since then. Contrast this with the Not-for-Profit Corporation Law, which was enacted in 1969, has been regularly updated and amended, and had a major overhaul (*the Non-Profit Revitalization Act*) in 2013. The result is that the Religious Corporations Law is chock-full of archaic and outdated provisions that religious corporations need to be aware of and comply with. One striking example follows.

Under certain circumstances, certain religious corporations could be subject to the following provisions set forth in Section 194 of the Religious Corporations Law regarding notice of meetings. Note that these provisions apply to both annual meetings and to special meetings. Also, do not be misled by the references to churches. These provisions can apply to Jewish religious corporations, as well.

The trustees shall cause notice of the time and place of its annual corporate meeting, therein specifying the names of any trustees, whose successors are to be elected thereat, and, if a special meeting, specifying the business to be transacted thereat, to be given at a regular meeting of the church for public worship, at morning service, if such service be held, on each of the two successive Sundays next preceding such meeting, if Sunday be the regular day for such public worship, and public worship be had thereon, or otherwise at a regular meeting of such church for public worship on each of two days, at least one week apart, next preceding such meeting, or if no such public worship be held during such period, by conspicuously posting such notice, in writing, upon the outer entrance to the principal place of worship of such church. Such notice shall be given by the minister of the church, if there be one, or if not, by the officiating minister thereof, if there be one, or if not, or if any such minister refuse to give such notice, by any officer of such church.

It is not surprising to learn that these provisions were enacted in 1909. They clearly reflect what community and religious life was like 120 years ago. The only comfort to be taken is that these provisions are not applicable to all religious corporations. The lesson to be learned here is that it is imperative to understand whether your religious organization is about to step on a landmine like this if there are provisions in the Religious Corporations Law that you are not aware of that apply to your religious organization and/or apply to, and govern, some action that your religious organization is taking. The time to know is before you take an action, and to avoid being surprised and ambushed somewhere down the road.





Another challenging layer of complexity of the Religious Corporations Law is that the law has 2 general articles with provisions that apply across denominations, followed by 31 articles that apply to specific religious denominations.

All of the foregoing necessitates close coordination between religious corporations and legal counsel well-versed in both the Religious Corporations Law and the Not-for-Profit Corporation Law in order to assure compliance is achieved, and to avoid the adverse consequences of failure to comply with mandatory provisions of the law, because these consequences can be profound and severe.

Let's briefly turn to endowments, and a commonly misunderstood fundamental distinction. The common perception is that an endowment can be established by an agreement between the organization and a donor – but also that the Board can establish an endowment of its own accord. But when we look at the definition of endowment under New York law, we see that the law explicitly excludes a Board-designated fund from the definition of endowment. **The New York Prudent Management of Institutional Funds Act (NYPMIFA)**, specifically, Section 551(b) of the Not-for-Profit Corporation Law, provides as follows.

“Endowment fund” means an institutional fund or part thereof that, under the terms of a gift instrument, is not wholly expendable by the institution on a current basis. The term does not include assets that an institution may designate as an endowment fund for its own use, consistent with the terms of the applicable gift instrument.

Funds always need to be utilized consistent with any donor restrictions. That being said, if the Board designates certain funds as an *“endowment,”* these funds are not a true endowment, but rather constitute a *“Board-designated endowment,”* also known as a *“quasi-endowment.”* The principle here is that, in the case of a true endowment (*with certain extremely limited exceptions*), the organization is bound by the donor's restrictions as to the expendability of the funds (*a common structure being that while the earnings on the principal of the fund are expendable on a current basis, the principal of the fund itself is not expendable, and must be maintained in perpetuity*).

On the other hand, what is created by the Board can be changed by the Board, so that the Board can, at a later date, alter or remove the restrictions as to expendability that it had established for a *“Board-designated endowment”* or *“quasi-endowment.”* If the Board designates an endowment fund where only earnings can be expended currently, but principal must be maintained and may not be expended, the Board can, at a later date, remove this restriction of its own volition, and provide that all of the funds, both earnings and principal, are currently expendable. For this reason, organizations prefer a Board-designated endowment to a true endowment. Some donors may be flexible enough to allow an organization to establish a Board-designated endowment. This donor flexibility, in turn, provides the organization the flexibility to respond to changes over time in its priorities and plans, as well as the flexibility to respond to changing circumstances and exigent circumstances.

In addition, some Boards fall victim to the confusion around the meaning of the term *“endowment,”* and erroneously assume that because the Board had previously designated certain funds as an *“endowment,”* the Board is not now able to change the expendability of those funds and make those funds expendable on a current basis. This is not the case. As stated above, what is created by the Board can be changed by the Board. This flexibility of a Board-designated endowment can be most welcome news to a Board struggling with new priorities, changed circumstances, or unexpected exigencies.



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REVENUE RECOGNITION UNDER ASC 606 AND ASC 958 FOR FAITH-BASED NONPROFIT ORGANIZATIONS



Faith-based nonprofit organizations, such as churches, synagogues, religious charities, and ministries, often face unique challenges when it comes to financial reporting. Unlike for-profit entities, these organizations rely heavily on contributions, grants, and program-related income, which complicates revenue and contribution recognition. The **Financial Accounting Standards Board (FASB)** provides guidance through **Accounting Standards Codification (ASC) 606**, Revenue from Contracts with Customers, and **ASC 958**, Not-for-Profit Entities. Together, these standards establish a framework for recognizing revenue and contributions in a way that ensures transparency and consistency. This article explores revenue and contribution recognition under ASC 606 and ASC 958, with a focus on conditional revenue, restricted revenue, bequests, pledges, agency transactions, in-kind contributions, and grants.

OVERVIEW OF ASC 606: REVENUE FROM CONTRACTS WITH CUSTOMERS

ASC 606, effective for annual reporting periods beginning after December 15, 2018, introduced a five-step model for recognizing revenue from contracts with customers. While primarily designed for for-profit entities, this standard also applies to nonprofits when they engage in exchange transactions—situations where goods or services are provided in return for consideration of commensurate value. For faith-based organizations, this might include tuition for religious schools, membership, fees for retreats, or sales of religious materials.

THE FIVE-STEP MODEL UNDER ASC 606 IS AS FOLLOWS:

1. IDENTIFY THE CONTRACT WITH A CUSTOMER:

A contract exists when there's an agreement with enforceable rights and obligations. For example, a faith-based nonprofit hosting a paid conference would have a contract with attendees.

2. IDENTIFY PERFORMANCE OBLIGATIONS:

These are the promises to deliver distinct goods or services. For instance, a retreat fee might include lodging, meals, and spiritual sessions—each a separate performance obligation if distinct.

3. DETERMINE THE TRANSACTION PRICE:

This is the amount the organization expects to receive. Variable considerations (e.g., discounts or refunds) must be estimated.

4. ALLOCATE THE TRANSACTION PRICE:

If multiple performance obligations exist, the price is allocated based on their standalone selling prices.

5. RECOGNIZE REVENUE:

Revenue is recognized when (or as) each performance obligation is satisfied, either at a point in time (e.g., delivering a book) or over time (e.g., a year-long membership).

While ASC 606 primarily governs exchange transactions (e.g., tuition fees or bookstore sales), ASC 958 addresses contributions, which are common in nonprofits. ASC 958-605 distinguishes between contributions (*nonreciprocal transactions*) and exchange transactions (*covered by ASC 606*), requiring nonprofits to assess whether a resource provider receives commensurate value in return. For faith-based nonprofits, most revenue streams fall under ASC 958, though some activities (e.g., tuition, day care, membership, etc.) may trigger ASC 606.

OVERVIEW OF ASC 958: NOT-FOR-PROFIT ENTITIES

ASC 958 addresses recognition of contributions, which are vital to faith-based nonprofits. Updated through ASU 2018-08, Clarifying the Scope and Accounting Guidance for Contributions Received and Contributions Made, ASC 958 distinguishes between contributions (*nonreciprocal transactions*) and exchange transactions (*reciprocal transactions subject to ASC 606*).

Under ASC 958-605, contributions are recognized immediately when they are unconditional (meaning there are no barriers or conditions the nonprofit must overcome to be entitled to the funds). Key considerations include:

- ▶ **Donor-Imposed Conditions:** *If a gift is contingent on a specific action (e.g., raising matching funds or completing a project), it's conditional, and revenue recognition is deferred until the condition is met.*
- ▶ **Donor-Imposed Restrictions:** *Restrictions limit how funds can be used (e.g., for a specific ministry program) but don't delay recognition if the gift is otherwise unconditional. These are reported as net assets with donor restrictions. There is frequent confusion between what constitutes a condition as opposed to a restriction. Generally speaking, conditions are stricter and provide donors with more control over the use of funds (along with rights of return to the donor if conditions are not met). Restrictions are more directional, leaving the nonprofit with more latitude in the ultimate use of the funds.*

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- ▶ **Promises to Give:** *Unconditional pledges are recognized as revenue when promised, typically at their fair value, discounted to present value if payments span multiple years.*

For example, a church receiving a \$10,000 donation for its youth ministry recognizes the full amount immediately if no conditions exist, classifying it as a restricted contribution. However, if the donation is contingent on hosting a youth camp during a specific period of time, recognition waits until the camp occurs.

APPLYING ASC 606 AND ASC 958 TO FAITH-BASED NONPROFITS

Faith-based nonprofits often encounter funding streams that blur the lines between contributions and exchange transactions. To determine the appropriate standard, organizations must assess whether a transaction provides commensurate value to the payor (ASC 606) or is a voluntary transfer of assets (ASC 958). Below are common scenarios and their treatment:

1. TITHES AND OFFERINGS

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *These are voluntary contributions without an expectation of goods or services in return. Contributions are recognized upon receipt, with restrictions noted if specified by the donor (e.g., “for the building fund”).*

2. EVENT FEES (E.G., RETREATS OR CONFERENCES)

- ▶ **Guidance:** ASC 606
- ▶ **Treatment:** *Fees for events like retreats, conferences, or workshops are exchange transactions if attendees receive a distinct benefit (e.g., education or spiritual enrichment). Revenue is recognized when the event occurs, as this is when the performance obligation is satisfied. For multi-day events, revenue may be allocated over the event period if benefits are provided incrementally. If fees are prepaid, they are recorded as deferred revenue until the event takes place.*



3. BOOKSTORE OR GIFT SHOP SALES

- ▶ **Guidance:** ASC 606
- ▶ **Treatment:** *Sales of books, religious materials, or merchandise in a nonprofit's bookstore are exchange transactions. Revenue is recognized when control of the goods transfers to the customer—typically at the point of sale. The transaction price is the amount paid, net of discounts or refunds. For example, if a church bookstore sells Bibles for \$20 each, revenue is recognized upon sale, assuming no significant return obligations exist.*

4. MEMBERSHIP DUES

- ▶ **Guidance:** ASC 606 or ASC 958 (depending on nature)
- ▶ **Treatment:** *If membership provides specific benefits (e.g., access to exclusive events, publications, or facilities), it's an exchange transaction under ASC 606, with revenue recognized over the membership period as benefits are delivered. If dues are more akin to a donation without distinct benefits, they fall under ASC 958 and are recognized as contributions when received, unless conditional.*

5. GRANTS

- ▶ **Guidance:** ASC 606 or ASC 958 (depending on nature)
- ▶ **Treatment:** *Grants are evaluated to determine if they are exchange transactions (ASC 606) or contributions (ASC 958). A grant to provide community services in return for funding is an exchange transaction, with revenue recognized as services are performed. A general support grant with no reciprocal benefit is a contribution, recognized when awarded unless conditional. Restricted or conditional grants follow the respective rules above, and are admittedly very confusing and subject to interpretation.*

6. CONDITIONAL REVENUE

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *Conditional contributions (e.g., a grant requiring a specific project milestone) are not recognized until the conditions are substantially met. Until then, amounts received are recorded as refundable advances (a liability). For example, if a donor pledges \$50,000 to build a chapel contingent on raising matching funds, revenue is deferred until the match is secured.*

7. RESTRICTED CONTRIBUTIONS

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *Donor-restricted contributions (e.g., funds designated for a capital project) are recognized when received or pledged, but classified as “with donor restrictions” in net assets. Contributions are released to “without donor restrictions” when the restriction is satisfied (e.g., when the qualifying capital expenditures are made). Time-restricted contributions are recognized similarly unless paired with a condition.*

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8. BEQUESTS

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *Bequests are contributions recognized when the organization has an irrevocable right to the assets, typically upon the donor's death and probate clearance. If restricted (e.g., for a specific ministry), they are recorded as part of restricted net assets. Uncertainty in amount or timing may delay recognition until resolved.*

9. PLEDGES

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *Unconditional pledges (promises to give) are recognized as when the pledges are made, at the present value of expected future cash flows, net of an allowance for uncollectible amounts. Conditional pledges are not recognized until conditions are met. For example, a \$10,000 pledge to support a mission trip is recorded as when promised, unless tied to a future event or milestone.*

10. AGENCY TRANSACTIONS

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *When a nonprofit acts as an intermediary (e.g., collecting funds for another charity), it does not recognize contributions for amounts it must pass through. Instead, it records a liability for funds held on behalf of others. For instance, if a church collects \$5,000 for a disaster relief fund to be remitted to a partner organization, no contribution is recognized—only the liability and subsequent disbursement, unless the church has some form of variance power or control over the use of the funds, in which case contributions would be recognized.*

11. IN-KIND CONTRIBUTIONS

- ▶ **Guidance:** ASC 958
- ▶ **Treatment:** *Noncash donations (e.g., food, clothing, or volunteer services) are recognized as at fair value when received, provided they can be used or sold by the organization. Specialized services (e.g., legal or accounting work) are recognized if they require specialized skills that the nonprofit would otherwise purchase. For example, donated hymnals valued at \$1,000 are recorded as in-kind contribution revenue and an asset or expense, depending on use.*

PRACTICAL CHALLENGES AND CONSIDERATIONS

Faith-based nonprofits often lack the accounting resources of larger entities, making compliance with ASC 606 and ASC 958 challenging. Key hurdles include:

- ▶ **Distinguishing Transaction Types:** *A donation with a “suggested amount” for a dinner event might require splitting the payment between contribution (ASC 958) and exchange (ASC 606) portions, based on the fair value of the meal.*
- ▶ **Tracking Restrictions and Conditions:** *Robust record-keeping is essential to differentiate between restricted, conditional, and unrestricted funds.*
- ▶ **Educating Stakeholders:** *Boards and donors may not understand why revenue recognition timing varies, necessitating clear communication.*

To address these, organizations can adopt accounting software tailored for nonprofits, train staff on ASC standards, and consult with accountants familiar with faith-based entities.

CONCLUSION

Revenue and contribution recognition under ASC 606 and ASC 958, respectively, provides faith-based nonprofits with a structured approach to financial reporting, ensuring accountability to donors, regulators, and their communities. By applying ASC 606 to exchange transactions and ASC 958 to contributions, these organizations can accurately reflect their financial position while adhering to GAAP. With ongoing updates to accounting practices, staying informed and seeking expert guidance remains critical for compliance and mission success. Through diligent application of these standards, faith-based nonprofits can maintain trust and transparency in their stewardship of resources. For matters of interpretation, which are very commonplace, lean on your trusted professionals (*like us!*).



Brianna is an Audit Supervisor at Cerini & Associates, where she specializes in serving nonprofit and religious organizations. She has experience performing assurance services, outsourced accounting, and tax planning and preparation. BriAnna brings a well-rounded skill set and a solutions-oriented approach to every engagement, helping mission-driven organizations meet their financial and compliance goals with confidence and clarity.

5 BEST PRACTICES YOU NEED TO KNOW ABOUT ACCOUNTING FOR YOUR RELIGIOUS ORGANIZATIONS



When it comes to finance and accounting, religious nonprofits face unique challenges balancing sustainability and donor engagement.

RELIGIOUS NONPROFIT ORGANIZATIONAL PILLARS

DONOR
RELATIONSHIP
MANAGEMENT

BUDGET
PLANNING AND
FORECASTING

FINANCIAL
REPORTING
TRANSPARENCY

Here are 5 best practices to know when balancing the financial pillars of your faith-based organization.

1. LEVERAGE EXPERTS: WHEN OUTSOURCING MAKES SENSE

The days of the “accidental bookkeeper” who is tasked with entering transactions into the accounting system because they are good with numbers are over. This approach exposes the board and religious leaders to risk. Volunteer board members and religious leaders should understand the importance of a technically knowledgeable expert. In fact, some situations of fraud and mismanagement can lead to boards and leadership being personally liable. The accounting profession as a whole is facing a talent shortage. Retiring professionals are not being replaced quickly enough by younger ones. Properly vetting, hiring, and retaining qualified bookkeepers, accountants, and finance professionals can be a lot like rolling dice. Outsourcing is becoming a popular option for religious institutions, as accounting firms now offer an array of outsourcing solutions with industry veterans who know the business of being a religious institution. Consider this the next time you’re looking to add to and/or replace any part of your accounting team.

2. EDUCATE: UNDERSTAND YOUR FINANCIAL PICTURE

Religious organization boards strengthen governance. Make sure your financial statements are presented in a way that allows your leadership to understand and make strategic decisions. Include both financial and non-financial key performance metrics that are aligned with your mission to tell the full story of your religious organization’s financial picture.

3. ORDER: BUILD A STRONG FINANCIAL FOUNDATION

Effective financial management is essential for advancing your mission and maintaining trust. Set up technology and systems to help you create a clear picture. To get an accurate picture of your religious organization’s financial health, first take a look at your financial structure.

By utilizing your accounting software’s built-in capabilities instead of creating unnecessary complexity, your religious organization can operate more efficiently allowing you to focus more on your time serving your congregation, supporting community outreach, and fulfilling your spiritual mission.

4. TRUST: UNDERSTAND OUR GREATEST VULNERABILITY IN THE DIGITAL AGE

We’re naturally trusting beings. We rarely question information from familiar sources as our brains prioritize efficiency over verification. During busy days, we make quick decisions, fearing delays more than deception. Protect yourself and your religious organization by creating detection perception; building defenses; implementing practical safeguards; and trusting your instincts. Trust but verify.

5. MONITOR: KEEP YOUR FINANCIAL HOUSE HEALTHY

After educating leadership, organizing your finances, and employing healthy skepticism, the next step is recognizing financial warning signs. Early detection can help your religious organization avoid financial crises. These red flags are a starting point. Each of these items could be a normal occurrence. The key is to use these red flags as a basis for asking more questions.

Create an environment where challenging questions are welcomed, as they often lead to better financial decisions and long-term sustainability. Implementing these best practices helps create a space for good people to do good things.



ASHA VAYAS
TRAINING CONTENT SPECIALIST
YPTC

YPTC provides specialized accounting and financial management services tailored to faith-based organizations. Our experts offer guidance in education, helping to train your staff to strengthen financial understanding. We ensure internal controls are in place to set your organization up for success. With extensive experience across various software platforms, we help you navigate the systems that best fit your organization’s unique needs. Backed by over 30 years of nonprofit expertise, YPTC is committed to supporting faith-based organizations with the financial insight and tools they need to thrive. [Learn more about our faith-based specialization here!](#)

NAVIGATING U.S. GAAP VS. INTERNAL FINANCIAL REPORTING FOR RELIGIOUS NONPROFITS



Religious nonprofit organizations, such as churches, ministries, and faith-based charities, operate with a mission-driven focus, often balancing spiritual goals with financial stewardship. For their leadership—CEOs, COOs, CFOs, Controllars, and board members—understanding financial reporting is critical. However, the financial statements prepared under **U.S. Generally Accepted Accounting Principles (GAAP)** often differ significantly from the internal budgeting, budget-to-actual reports, and cash flow statements used by management. These differences stem from distinct purposes, methodologies, and compliance requirements. This article explores how GAAP financial reports diverge from internal financial tools in religious nonprofits, offering clarity for leaders navigating these complexities.

UNDERSTANDING GAAP FOR NONPROFITS

GAAP, established by the **Financial Accounting Standards Board (FASB)**, provides a standardized framework for financial reporting to ensure transparency, consistency, and comparability. For nonprofits, including religious organizations, GAAP compliance is often mandatory to maintain tax-exempt status, secure grants, or meet donor requirements. GAAP-compliant financial statements—such as the Statement of Financial Position, Statement of Activities, Statement of Cash Flows, and Statement of Functional Expenses—focus on presenting a comprehensive, accrual-based view of an organization's financial health to external stakeholders like donors, regulators, and auditors. GAAP emphasizes several principles relevant to nonprofits:

Accrual Accounting: Revenue and expenses are recorded when earned or incurred, not when cash changes hands. For example, a pledge for future donations is recognized as revenue when the commitment is made, even if the cash is received later.

Net Asset Classification: Nonprofits must categorize net assets as without donor restrictions or with donor restrictions (*for time, perpetually, or for purpose*), reflecting how funds can be used based on donor stipulations.

Functional Expense Reporting: Expenses must be allocated to program services, management, and fundraising, providing transparency on how resources support the mission.

These requirements ensure that external stakeholders can assess the organization's financial position and accountability. However, they often present a more complex picture than the internal reports used by leadership for day-to-day management.

INTERNAL BUDGETING AND REPORTING: A MANAGEMENT PERSPECTIVE

In contrast, internal budgeting, budget-to-actual reports, and cash flow statements are designed for operational decision-making and oversight. These tools prioritize simplicity, flexibility, and cash-based insights to help leaders manage resources effectively. Here's how they typically function in religious nonprofits:

Budgets: Annual budgets outline projected revenues (*e.g., tithes, offerings, grants*) and expenses (*e.g., clergy salaries, facility costs, outreach programs*). They are often created in collaboration with board members and reflect strategic priorities, such as funding a new program or maintaining reserves. Budgets are forward-looking and focus on cash availability.

Budget-to-Actual Reports: These compare budgeted amounts to actual revenues and expenses over a period, highlighting variances. For example, if a church budgeted \$50,000 for a mission trip but spent \$60,000, the report flags the overrun for discussion. These reports are typically cash-based or modified accrual, focusing on immediate financial performance.

Cash Flow Statements (Internal): Unlike GAAP's formal Statement of Cash Flows, internal cash flow reports track actual cash inflows (*e.g., weekly offerings*) and outflows (*e.g., payroll*) to ensure liquidity. They help leaders anticipate cash shortages, such as during low-attendance months, and plan accordingly.

These internal tools are tailored to the organization's operational needs, offering a granular, cash-focused view that aligns with the practical realities of managing a religious nonprofit.

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KEY DIFFERENCES BETWEEN GAAP AND INTERNAL REPORTING

The divergence between GAAP financial reports and internal reporting creates challenges for nonprofit leaders, who must reconcile these perspectives. Below are the primary differences and their implications:

Accrual vs. Cash-Based Accounting: GAAP requires accrual accounting, recognizing revenues and expenses when they are earned or incurred. For instance, a multi-year grant pledged in 2025 is recorded as revenue in 2025, even if funds arrive in 2026. Internal budgets and cash flow reports, however, often use cash-basis accounting, recording transactions only when cash changes hands. This means a budget-to-actual report might show no revenue from the grant until cash is received, creating a disconnect. Leaders may see robust GAAP revenue due to pledges but face cash shortages in internal reports, requiring careful cash flow planning. For example, an organization might appear financially healthy on a GAAP Statement of Activities but struggle to pay bills if pledges are delayed.

Net Asset Restrictions: GAAP mandates classifying net assets based on donor restrictions, which is critical for transparency but complex. A donation restricted for a youth program must be tracked separately, and its use reported accordingly. Internal budgets, however, often aggregate funds for simplicity, focusing on total available cash rather than restrictions, or focus solely on the operating or general funds. Budget-to-actual reports may not distinguish restricted funds unless explicitly tracked. Board members reviewing GAAP statements might see significant restricted assets unavailable for general operations, while internal reports show a tighter cash position. This requires clear communication to avoid misinterpreting financial health.

Expense Allocation: GAAP requires expenses to be allocated across program, management, and fundraising categories in the Statement of Functional Expenses. For a religious nonprofit, this means parsing staff time (e.g., a pastor's salary) across preaching (program), administration (management), and donor outreach (fundraising). Internal budgets and reports rarely break down expenses this way, instead grouping costs by department or project (e.g., "Worship Services"). GAAP reports emphasize mission-driven spending for donors, but internal reports are more actionable for managing specific initiatives. Leaders must translate GAAP allocations into budget categories for operational decisions.

Cash Flow Presentation: GAAP's Statement of Cash Flows categorizes cash flows into operating, investing, and financing activities, with qualitative disclosures about liquidity management. Internal cash flow reports are simpler, often just a running tally of cash inflows and outflows. For example, a GAAP statement might show a positive cash flow from a loan (financing activity), while an internal report highlights the immediate burden of loan repayments. Internal reports provide a clearer picture of short-term liquidity, while GAAP statements offer a broader view for external stakeholders. Leaders must use both to balance immediate needs with long-term stability.

Timing and Frequency: GAAP financial statements are typically prepared annually or quarterly for external reporting, with a focus on historical accuracy. Internal budgets and budget-to-actual reports are often monthly or weekly, providing real-time insights. Cash flow projections may be updated daily during critical periods, such as a capital campaign. The lag in GAAP reporting can make it less relevant for immediate decisions, while internal reports drive ongoing management. Leaders must align these timelines for strategic planning.

BRIDGING THE GAP FOR EFFECTIVE LEADERSHIP

To navigate these differences, religious nonprofit leaders can adopt several strategies:

Education and Training: Ensure board members and management understand GAAP requirements and how they differ from internal reports. Regular training sessions with a nonprofit-focused CPA can clarify concepts like accrual accounting and net asset restrictions.

Hybrid Reporting: Develop internal reports that bridge GAAP and operational needs. For example, include a "GAAP-adjusted" budget column showing pledged revenues alongside cash receipts to align perspectives.

Clear Communication: When presenting GAAP financials to the board, provide a companion summary explaining key differences from internal reports. Highlight restricted funds or accrual adjustments to avoid confusion.

Leverage Technology: Use nonprofit accounting software to automate GAAP-compliant reporting while generating customized internal reports. Tools like QuickBooks Nonprofit or NetSuite can streamline both processes.

Engage Experts: Work with accountants specializing in nonprofit GAAP to ensure compliance and translate GAAP reports into actionable insights for management.

TO SUM IT UP

For leaders of religious nonprofits, mastering the interplay between GAAP financial reports and internal budgeting/cash flow reporting is essential for effective governance and stewardship. GAAP ensures transparency and accountability for external stakeholders, emphasizing accrual accounting, net asset restrictions, and functional expense reporting. Internal reports, conversely, provide a cash-focused, operational lens for managing day-to-day activities. By understanding these differences—accrual vs. cash, restricted vs. unrestricted funds, and formal vs. flexible reporting—nonprofit leaders can make informed decisions that honor their mission and financial responsibilities. With education, clear communication, and the right tools, leaders can bridge these frameworks to drive both compliance and operational success.



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PREPARING A STATEMENT OF FUNCTIONAL EXPENSES
FOR FAITH-BASED NONPROFITS
UNDERSTANDING EXPENSE CLASSIFICATIONS AND ALLOCATION METHODOLOGIES

INTRODUCTION

Faith-based nonprofits, like other nonprofit organizations, are required to present their expenses in a manner that provides meaningful information to their stakeholders. This involves creating a statement of functional expenses which categorizes costs according to their nature and function. Understanding the distinction between these classifications and employing appropriate allocation methodologies is essential for accurate and transparent financial reporting.

NATURAL VS. FUNCTIONAL CLASSIFICATION

NATURAL CLASSIFICATION

Natural classification groups expenses according to their inherent nature. Examples of natural expenses include salaries, rent, utilities, supplies, and travel. This classification provides a straightforward view of what types of costs the organization incurs. Avoid using broad categories such as “*program expense*” when creating natural classifications. That’s a functional label and is too vague to meet the definition of natural classification.

FUNCTIONAL CLASSIFICATION

Functional classification, on the other hand, groups expenses according to their purpose within the organization. Typically, these purposes are divided into program services and supporting services. Supporting services can be further broken down into management and general expenses, fundraising, and membership development activities, if applicable. Functional classification helps stakeholders understand how resources are being utilized to achieve the organization’s mission.

IMPORTANCE OF EXPENSE CLASSIFICATION

Properly classifying expenses is crucial for several reasons. It ensures that donors, grantors, creditors, and organizational leaders have a clear understanding of how funds are being used, which in turn supports transparency and accountability. Moreover, it enables better financial planning and decision-making by providing insights into cost structures and resource allocation.

TRACKING COSTS AND AVOIDING DOUBLE CHARGING

Accurate tracking of costs is imperative to avoid charging the same costs to multiple grants or programs, which can lead to compliance issues and potential loss of funding. Each cost should be allocated to the appropriate program or supporting service and documented to ensure accuracy.

ALLOCATION METHODOLOGIES FOR COMMON EXPENSE ITEMS

Allocating expenses involves determining a rational and systematic basis for distributing costs among various functional classifications. Below are common expense items and suggested allocation methodologies:

- ▶ **Salaries:** *Use timesheets or time studies to allocate salaries based on the actual time employees spend on different activities.*
- ▶ **Employee Benefits:** *Allocate benefits in proportion to salaries or through time studies.*
- ▶ **Payroll Taxes:** *Allocate based on salary dollars or use studies.*
- ▶ **Supplies:** *Allocate based on headcount or specific uses.*
- ▶ **Telephone:** *Use the number of extensions, use studies, or salary dollars to allocate telephone expenses.*

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- ▶ **Postage and Shipping:** *Allocate through use studies.*
- ▶ **Interest Expense:** *Allocate based on asset use or loan use.*
- ▶ **Rental and Maintenance of Equipment:** *Allocate based on equipment use.*
- ▶ **Printing and Publications:** *Use studies or specific uses.*
- ▶ **Travel and Transportation:** *Allocate based on employee use or salary dollars for those traveling.*
- ▶ **Insurance:** *Allocate using square footage, asset use, and/or salary dollars.*
- ▶ **Depreciation and Amortization:** *Use asset use and/or square footage for allocation.*
- ▶ **Website Hosting and Maintenance:** *Allocate through use studies.*
- ▶ **Other Expenses:** *Allocate using other reasonable bases.*

REVIEWING AND UPDATING ALLOCATION BASES

It is essential to review and update allocation bases regularly, especially when significant changes occur, such as acquiring new office space, incurring new debt, starting or discontinuing programs, or changing staff positions. Regular reviews ensure that the allocation methods remain reasonable and consistent over time.

DOCUMENTATION AND POLICY DEVELOPMENT

Having a documented policy for expense allocation is critical. It should outline the methodologies used, the rationale behind them, and how they are reviewed. This documentation should be shared with organizational leaders, auditors, and users of the financial statements to ensure transparency and compliance.

CONCLUSION

Preparing a statement of functional expenses is a crucial task for churches and synagogues, and it's required for compliance with US accounting standards. By understanding the difference between natural and functional classifications, accurately tracking costs, and employing appropriate allocation methodologies, these organizations can ensure transparent and meaningful financial reporting. Regular reviews and well-documented policies further support the accurate allocation of expenses, helping to maintain trust and accountability with stakeholders.



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NAVIGATING FOREIGN OPERATIONS: PRACTICAL CONSIDERATIONS FOR RELIGIOUS NONPROFITS

Religious nonprofit organizations increasingly engage in foreign operations to fulfill their missions. These activities—such as funding overseas programs, establishing partnerships, or maintaining offices abroad—offer significant opportunities but introduce complex legal, financial, and accounting challenges. For stakeholders of religious institutions or faith-based nonprofits, understanding these implications is critical to ensuring compliance, financial transparency, and mission success. As a CPA firm specializing in religious institutions, we explore key practical considerations, focusing on IRS Form 990 and other tax reporting obligations, and some accounting considerations.

UNDERSTANDING THE SCOPE OF FOREIGN OPERATIONS

Foreign operations for religious nonprofits encompass activities like direct program delivery (e.g., *humanitarian aid or religious education abroad*), grantmaking to foreign entities, or maintaining overseas offices or subsidiaries. This often involves supporting educational institutions, community centers, or social services. These operations may involve transferring funds, hiring local staff, or navigating foreign regulations, each adding complexity.

IRS FORM 990 AND TAX REPORTING OBLIGATIONS

IRS Form 990, the annual information return for tax-exempt organizations, is a cornerstone of transparency for nonprofits with foreign operations. Accurate and comprehensive reporting ensures compliance with U.S. tax laws and maintains public trust. Remember though that certain religious institutions are exempt from the filing rules for IRS Form 990.

The IRS considers any activity outside the U.S.—including financial transactions, partnerships, or physical presence—as a foreign operation, triggering specific reporting requirements. Board members and executives must ensure international activities align with the organization’s mission and resources, as missteps can lead to regulatory scrutiny or reputational risks. Key sections include:

Schedule F (Statement of Activities Outside the United States): Nonprofits must report foreign expenditures, including grants, program services, and investments. For example, a nonprofit funding a school in Israel must itemize the grant amount, recipient, and program description. Incomplete reporting can trigger IRS audits.

Schedule I (Grants and Other Assistance): Grants to foreign organizations or individuals require detailed documentation, including the recipient’s name, address, and tax status. Foreign charities often lack U.S. 501(c)(3) status, complicating compliance. Understanding the local regulatory environment and nonprofit classification system/requirements is essential for any organization with foreign business.

Foreign Bank Account Reporting (FBAR): Nonprofits with signature authority over foreign accounts exceeding \$10,000 must file FinCEN Form 114. Noncompliance carries severe penalties.

Schedule R (Related Organizations): Relationships with foreign entities, such as subsidiaries, affiliates, or partners, must be disclosed.

Additionally, the **Foreign Account Tax Compliance Act (FATCA)** mandates reporting on foreign financial assets. CFOs and controllers must track international transactions meticulously, and engaging a CPA firm with expertise in nonprofit compliance can prevent costly errors.

ACCOUNTING DIFFERENCES BETWEEN THE U.S. AND ELSEWHERE

Religious nonprofits operating in both the U.S. and overseas must navigate distinct accounting standards, impacting financial reporting, revenue recognition, expense allocation, compliance, and foreign currency translations. These differences are critical for ensuring accurate financial statements and regulatory adherence, particularly for organizations consolidating cross-border financials. These accounting differences necessitate robust systems and expertise. A CPA firm can standardize charts of accounts, reconcile cross-border transactions, manage currency translations, and ensure compliance with U.S. and other standards, minimizing errors in Form 990 and local filings. See below for some more specific considerations with regard to these reporting differences and challenges.

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Financial Reporting Standards: In the U.S., nonprofits follow **Financial Accounting Standards Board (FASB)** guidelines, specifically Accounting Standards Codification (ASC) 958, which governs nonprofit accounting. Financial statements classify net assets as “with donor restrictions” or “without donor restrictions,” reflecting donor-imposed limitations. This is critical for reporting funds received for specific international programs, such as aid to Israeli communities.

Most foreign nonprofits adhere to **International Financial Reporting Standards (IFRS)**, or some derivation of them, which are less fully-formed than their U.S. counterparts, **Generally Accepted Accounting Principles (GAAP)**. Financial statements often use some form of cash-based or modified accrual accounting, with less emphasis on donor restrictions. These standards typically prioritize compliance with local tax laws over detailed net asset classifications, creating challenges for U.S.-based nonprofits consolidating financials.

Revenue Recognition: The U.S.’s FASB’s ASC 606 and ASC 958 dictate recognition for contributions, grants, and service fees. Contributions are recognized when received or pledged, with conditional pledges deferred until conditions are met. For instance, a pledge for a program tied to specific milestones is recognized only when those milestones are achieved. Outside of the U.S., income recognition often follows a cash-based approach, especially for smaller nonprofits. Contributions are typically recognized when funds are received, not when pledged, creating timing differences. CFOs and controllers must reconcile U.S. and foreign records for accurate internal, Form 990, and GAAP reporting.

Expense Allocation: GAAP stipulates that nonprofits must allocate expenses across program, administrative, and fundraising categories, as reported on statements of activities and functional expenses and the IRS Form 990. This ensures transparency but can be complex for foreign operations, where expenses like overseas staff salaries or program costs in another country must be categorized accurately. Non-U.S. expense classification rules are simpler, often focusing on operational versus administrative costs. Program-specific allocations are less rigid, complicating U.S. compliance. CFOs and controllers must standardize expense tracking to meet both jurisdictions’ requirements.

Compliance and Audits: U.S. nonprofits with significant revenue or federal funding may require audits under **Generally Accepted Auditing Standards (GAAS)**. The IRS scrutinizes foreign transactions, necessitating robust internal controls. State charities officers normally set overall funding thresholds, over which nonprofits will be subject to independent audits. The IRS, contrary to popular belief, does not mandate such auditing. Auditing requirements may be mandatory for foreign nonprofits depending on the local regulatory environment in place. Care must be taken to fully understand the impact of all local laws and compliance requirements, which may be significantly different from the U.S.’s.

Foreign Currency Translations: Nonprofits with foreign operations or subsidiaries, such as an Israeli office, must follow FASB’s ASC 830 for foreign currency matters. Transactions in foreign currencies (e.g., *Israeli shekels*) are translated into U.S. dollars using the exchange rate at the transaction dates. For financial statement consolidation, assets and liabilities of foreign operations are translated at the exchange rate on the reporting date, while revenues and expenses are translated at the average rate for the period. Translation adjustments—gains or losses from exchange rate fluctuations—are typically recorded in net assets as a separate income or expense line item (*gain or loss on foreign currency exchange, respectively*).

NAVIGATING U.S. AND FOREIGN REGULATIONS

Foreign operations expose nonprofits to dual regulatory frameworks. In the U.S., the **Office of Foreign Assets Control (OFAC)** enforces sanctions that may restrict transactions with certain entities. In other countries where nonprofits may conduct business, there may be other equivalent offices that perform similar functions. Key executives and board members should establish policies for vetting foreign partners and documenting transactions, such as obtaining equivalency determinations or exercising expenditure responsibility.

This may be repetitive, but truly and fully understanding the regulatory landscapes of where you’re operating are absolutely essential for ensuring compliance and mitigating risk.

FINANCIAL AND OPERATIONAL CHALLENGES

Foreign operations can strain financial and operational capacity. Currency fluctuations, such as a weakening shekel, can reduce the value of grants to Israel, requiring CFOs and controllers to consider hedging strategies, multi-currency accounts, or frequent exchange rate monitoring to stabilize budgets. Banking fees for international transfers also add costs, necessitating careful planning.

Operationally, managing foreign staff or offices demands cultural and legal awareness. Foreign labor laws may have stricter rules on benefits and termination and usually differ from U.S. standards. Nonprofit leaders must ensure compliance while aligning activities with the nonprofit’s mission.

RISK MANAGEMENT AND GOVERNANCE

Effective governance ensures alignment with the organization’s mission and compliance with regulations. Boards should oversee international budgets, review Form 990 disclosures, and monitor risks like fraud or fund misuse. For Jewish nonprofits, geopolitical tensions in Israel can attract scrutiny, necessitating transparency and robust public relations. Insurance, such as foreign liability or political risk coverage, protects against unforeseen challenges. CFOs and controllers should consult brokers familiar with international nonprofit risks.

CONCLUSION

Foreign operations enable religious nonprofits to advance their missions globally. However, these activities demand careful attention to IRS Form 990, U.S. and other jurisdictional regulations, accounting differences, and foreign currency matters. By prioritizing compliance, transparency, and strategic planning, CEOs, CFOs, COOs, controllers, and board members can ensure operational excellence and mission-driven impact. Your organization’s global success depends on mastering these complexities and avoiding major regulatory pitfalls.



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