

**Second  
Edition**

**Not-for-Profit  
*Accounting*  
*Made Easy***

**Warren Ruppel**

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John Wiley & Sons, Inc.



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# Preface

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*Not-for-Profit Accounting Made Easy* is a plain-language, easy to understand explanation of the various accounting and financial reporting practices of not-for-profit organizations. It is designed for all those individuals who have contact with these organizations—management and staff, board members (particularly audit committee members), consultants, donors, creditors—who should understand not-for-profit accounting but often do not. It is written for the nonaccountant, but those accountants who are unfamiliar with the nuances of not-for-profit accounting (or those who have grown a little rusty in the latest accounting pronouncements) and do not need an in-depth technical volume will also find it useful.

There are over one million not-for-profit organizations in the United States. They exist in all sizes and for many purposes. They range from homeless shelters to country clubs, from child day care centers to colleges and universities, from local to international. One thing these organizations all have in common is that their finances are subject to a great deal of scrutiny.

Since the publication of the first edition of this book, the accounting “industry” has undergone dramatic changes. Well-publicized accounting failures and frauds in large public companies led to the passage of the Sarbanes-Oxley Act of 2002. Although not applicable directly to not-for-profit organizations (except for some specific provisions that apply to all organizations with respect to protecting the rights of “whistle-blowers”), it is the trickle-down effect of these changes that have indirectly affected not-for-profit organizations. These changes will be discussed where applicable in this newly revised edition of this book, but there is no doubt that overall, not-for-profit organizations face increased scrutiny of their accounting and financial practices.

Effective accounting and financial reporting is a key ingredient in withstanding this increased scrutiny and ensuring accountability. Having a basic understanding of not-for-profit accounting and financial reporting can be a real asset for the many people who have contact with not-for-profit organizations in many different ways. This book is particularly important for a not-for-profit organization’s management and governing board who need a basic level of understanding of accounting and financial reporting to fulfill their fiduciary responsibilities. This book may not make you love not-for-profit accounting, but it will teach you the basics and help you read and understand a set of not-for-profit financial statements.

My thanks to all those at John Wiley & Sons, Inc., who helped make this book a reality, particularly John DeRemigis who supported and nurtured the concept and Judy Howarth and Pam Reh for making sure that the book is a quality product. Thanks also to my family, my wife Marie and sons Christopher and Gregory, for their continued support.

Warren Ruppel  
Woodcliff Lake, New Jersey  
January 2007

# About the Author

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**Warren Ruppel, CPA**, has over 25 years of expertise in not-for-profit and governmental accounting. He is currently the Director of Government Services at Marks Paneth & Shron LLP where he is also a key member of the firm's quality assurance team. He previously was the assistant comptroller for accounting of the City of New York, where he was responsible for all aspects of the City's accounting and financial reporting. He began his career at KPMG after graduating from St. John's University, New York. He later joined Deloitte & Touche to specialize in audits of not-for-profit organizations and governments. Mr. Ruppel has also served as the chief financial officer of an international not-for-profit organization and as a partner in a small CPA practice.

Mr. Ruppel has served as instructor for many training courses, including specialized governmental and not-for-profit programs and seminars. He has also been an adjunct lecturer of accounting at the Bernard M. Baruch College of the City University of New York. He is the author of five other books, *OMB Circular A-133 Audits*, *Not-for-Profit Organization Audits*, and Wiley's *Not-for-Profit Audit Committee Best Practices*, *GAAP for Governments*, and *Governmental Accounting Made Easy*.

Mr. Ruppel is a member of the American Institute of Certified Public Accountants as well as the New York State Society of Certified Public Accountants, where he serves on the Governmental Accounting and Auditing Committee and as a member of the Not-for-Profit Organizations Committee. He has also served as chair of the Society's Audit Committee. He is also a past president of the New York Chapter of the Institute of Management Accountants. Mr. Ruppel is a member of the Government Finance Officers Association and serves on its Special Review Committee.



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## CHAPTER 1

# **Understanding the Basics of Not-for-Profit Accounting**

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This chapter provides some very basic information about not-for-profit accounting to provide a basis for understanding the principles and standards that are discussed in greater detail throughout the remainder of this book. A lack of understanding or misunderstanding of these fundamentals will cause the reader to be lost when trying to understand more complex principles. Specifically, this chapter will

- Identify generally accepted accounting principles.
- Define and give examples of assets, liabilities, net assets, revenues, and expenses usually found in not-for-profit organizations' financial statements.
- Explain what is meant by the accrual basis of accounting. How does this differ from the cash basis of accounting, and which is better?
- Describe what happened to fund accounting.

### **WHAT ARE GENERALLY ACCEPTED ACCOUNTING PRINCIPLES?**

Nonaccountants sometimes ask the question, “Well, if these accounting principles are only generally accepted, that must mean that there are other perfectly good accounting principles that have

less than general acceptance that are fine to use.” Unfortunately for those desiring creativity and uniqueness in their accounting principles, this is not the case. Generally accepted accounting principles (GAAP) are the rules of road that need to be followed by not-for-profit organizations if they want to proclaim that their financial statements are prepared in accordance with GAAP.

### **WHY IS PREPARING GAAP FINANCIAL STATEMENTS IMPORTANT?**

Sometimes not-for-profit organizations are required by law or regulation to prepare financial statements in accordance with GAAP. Most states require that not-for-profit organizations that are organized within a state (or raise funds within that state) file an annual report with the state charities bureau (or its equivalent) and, for all but the smallest not-for-profit organizations, the annual reports usually require that financial statements prepared in accordance with GAAP be included with the annual report.

Several other groups are also important users of financial statements prepared in accordance with GAAP. Large, sophisticated donors often request copies of an organization’s financial statements, and having these financial statements prepared in accordance with GAAP lends a high degree of credibility to the financial statements. Creditors that loan money or provide credit lines to not-for-profit organizations also like to see GAAP financial statements. Sometimes a significant vendor or contractor will also request financial statements of the organization, particularly when a long-term lease or equipment-financing contract is being executed. Having financial statements prepared in accordance with GAAP makes them more understandable, comparable with other not-for-profit organizations, and provides a better representation of the financial affairs of the not-for-profit organization. Additionally, if the not-for-profit organization provides services to a governmental organization (federal, state, city, school district, county, etc.), the contract with the governmental entity often requires that financial statements prepared in accordance with GAAP be submitted to the government every year.

## **Who Sets the Laws of GAAP?**

Generally accepted accounting principles for not-for-profit organizations are basically set by the Financial Accounting Standards Board (FASB). The FASB is a private organization that is overseen by the Financial Accounting Foundation (FAF), itself a not-for-profit organization. The FASB issues GAAP accounting pronouncements that relate to commercial entities (both public and private) as well as not-for-profit organizations. The FAF also oversees the Governmental Accounting Standards Board (GASB), which sets GAAP for governmental entities. The American Institute of Certified Public Accountants (AICPA) has also issued accounting guidance in the past that is part of the accounting principles that comprise GAAP for not-for-profit organizations.

## **Who Makes Sure the Not-For-Profit Organization's Financial Statements Conform with GAAP?**

The answer may surprise the nonaccountant, but the fair presentation of a not-for-profit organization's financial position and activities in its financial statements prepared in accordance with GAAP is the responsibility of the not-for-profit organization's management. For those who would have guessed this responsibility was that of the not-for-profit organization's independent auditor, a serious change in paradigm needs to be made. Independent auditors are hired to perform an audit and issue an opinion as to whether the financial statements *prepared by management* are presented in accordance with GAAP. Not-for-profit organizations often rely on the independent auditors to help them meet their responsibility for preparing financial statements. The common reason for doing this, particularly in smaller organizations, is that the not-for-profit organization may not have individuals with the technical expertise on staff to take full responsibility for preparing the financial statements. While it is understandable how this happens, the management of the organization is, in fact, responsible for the financial statements. If assistance is needed of the independent auditor, management should at least understand how the financial statements are ultimately prepared