Hot Topic: Coronavirus

Accounting and reporting impacts of the CARES Act for not-for-profit higher education institutions

May 21, 2020

KPMG addresses accounting and financial reporting effects of key aspects of the CARES Act on not-for-profit higher education institutions

Background

The Coronavirus Aid, Relief, and Economic Security (CARES) Act (the Act) was enacted into law on March 27, 2020 as a $2 trillion national economic rescue package. The Act contains several provisions that provide relief for educational institutions.

Most notably, the Act appropriated $30.75 billion for the Education Stabilization Fund (the Fund) to the Department of Education (ED) to prevent, prepare for and respond to the coronavirus. The Fund has been added to the US Assistance Listings as CFDA 84.425. Approximately $14 billion of the Fund is reserved for higher education institutions – both public and private – and the students they serve through the Higher Education Emergency Relief Fund (HEERF). The Act allocates the HEERF as follows.

— **General grants.** Approximately $12.56 billion is broadly available to institutions, based on two formula factors, heavily weighted toward full-time equivalent enrollment of Pell Grant recipients not enrolled exclusively in distance education.

— **Minority-serving and strengthening institutions grants.** Approximately $1.05 billion is reserved exclusively for minority-serving institutions and other institutions eligible for the Strengthening Institutions Program.

— **Unmet needs grants.** Approximately $350 million is reserved for certain institutions that are determined to have the most unmet needs related to the effects of the coronavirus.

In this Hot Topic, we address the primary accounting and reporting impacts of the HEERF on not-for-profit (NFP) higher education institutions reporting under US GAAP and applying standards of the Financial Accounting Standards Board (FASB).

The Act provides additional relief to higher education institutions by providing waivers and other regulatory flexibility. This Hot Topic does not address those provisions.

For higher education institutions with an academic medical center, see our Hot Topic, Healthcare entities' accounting for COVID-19 government aid.

Institutions are eligible for relief through provisions of the Act that are not specifically designated for higher education institutions, such as an employer payroll tax deferral and employer payroll tax credit. Some institutions may also be eligible for small business loans under the Paycheck Protection Program. See our Hot Topic, Accounting and reporting impacts of the CARES Act, for discussion of these and other provisions of the CARES Act and related accounting and reporting considerations.

Business interruption and event cancellation insurance could be another source of funding as a result of the pandemic. See our Hot Topic, Potential accounting and disclosure impacts of COVID-19 on insurance recoveries.

Key provisions of the Higher Education Emergency Relief Fund[1]

General grants

For the $12.56 billion of the HEERF that is broadly available to higher education institutions, ED has allocated 75% of these funds based on institutions' enrollment of Pell Grant recipients and the remaining 25% based on institutions' non-Pell Grant recipient enrollment. The enrollment is based on students who were not enrolled exclusively in distance education prior to the coronavirus emergency.

ED is awarding these funds in two portions. Institutions must apply for each portion separately and enter into a funding certification and agreement that sets forth the terms and conditions of each portion. To receive these HEERF grants, institutions must agree to the terms and conditions. ED has released Frequently Asked Questions (FAQ) documents that provide additional guidance on use of the general grants. These summaries of the two portions are based on the applicable agreement or FAQ document.

— **Student aid:** Fifty percent of the general HEERF funding is available to institutions for the sole and exclusive purpose of providing emergency financial aid grants to students for their expenses related to the disruption of campus operations due to the coronavirus such as food, housing, course materials, technology, health care and child-care expenses. Institutions retain discretion to determine the amount of each individual emergency financial aid grant consistent with all applicable laws, including non-discrimination laws. However, eligible students are limited to those that are or could be eligible to participate in Title IV programs and exclude those who were enrolled exclusively in an online program on March 13, 2020 (the date of the Proclamation of National Emergency). Institutions may not use the funds to reimburse any of their costs or expenses, including but not limited to any costs associated with significant changes to the delivery of instruction due to the coronavirus and/or any refunds or other benefits that the entity previously issued to students.

— **Institutional costs:** The remaining 50% of this funding is available to cover costs associated with significant changes to the delivery of instruction due to the coronavirus that were incurred on or after March 13, 2020 (e.g. refunds made to students for housing, food or other services that the institution could no longer provide). Institutions retain discretion in determining how to allocate and use the funds, provided that funds are spent only on those costs that have a clear nexus to significant changes to the delivery of instruction due to the coronavirus. These costs cannot include payment to contractors for the provision of pre-enrollment recruitment activities, including marketing and advertising, endowments, or capital outlays associated with facilities related to athletics, sectarian instruction or religious worship. In addition, the following would not be

[1] ED has posted various documents, including the certification and agreement documents, FAQs and allocations to institutions at https://www2.ed.gov/about/offices/list/ope/caresact.html. Summary of provisions herein is based on information posted by ED as of May 20, 2020.

considered allowable costs: senior administrative and/or executive salaries, benefits, bonuses, contracts, incentives and any other cash or other benefit for a senior administrator or executive.

As a condition to receiving the funding available for institutional costs, institutions must have entered into the student aid funding certification and agreement. Further, ED has urged institutions to devote the maximum amount of funds possible to the student aid grants, including some or all of the funds earmarked for institutional costs. If an institution chooses to use funds designated for institutional costs to provide such emergency financial aid grants to students, those funds are subject to the requirements in the student aid funding certification and agreement.

Minority-serving, strengthening and unmet needs grants

ED has released information allowing eligible institutions to access allocations of the $1.05 billion of the HEERF that is reserved exclusively for Historically Black Colleges and Universities, Tribally-Controlled Colleges and Universities, other Minority Serving Institutions and institutions eligible for the Strengthening Institutions Program. The $350 million of the HEERF that is reserved for institutions with the greatest unmet needs has also been allocated to eligible institutions. To access these funds, eligible institutions must enter into a funding and certification agreement specific to these payments by August 1, 2020 agreeing to certain terms and conditions.

These grants are to be used to defray expenses (including lost revenue, reimbursement for expenses already incurred, technology costs associated with a transition to distance education, faculty and staff trainings, and payroll) incurred on or after March 13, 2020. The funds may also be used for grants to students. While there is no requirement to use any portion of these funds for that purpose, ED has encouraged the institutions eligible for these funds to devote the maximum amount possible to student aid grants.

Additional terms and conditions that apply to all HEERF funds

Institutions receiving HEERF funds agree to comply with all applicable federal regulations, including the False Claims Act; the Single Audit Act; and the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance). Institutions are required to promptly, and to the greatest extent practicable, use or distribute all of the advanced funds by one year from the date of the applicable certification and document their efforts to do so. There are also reporting requirements outlined in each of the agreements. Additionally, institutions are required, to the greatest extent practicable, to pay all employees and contractors during the period of disruptions or closures related to the coronavirus. The student aid certification specifies that institutions should document this and explain in detail all specific actions and decisions related thereto.

Section 18004(c) of the CARES Act establishes the requirements for the use of the HEERF funds. It states that higher education institutions receiving funds "may use the funds received to cover any costs associated with significant changes to the delivery of instruction due to the coronavirus" with certain exceptions, but that institutions "shall use no less than 50 percent of such funds to provide emergency financial aid grants to students for expenses related to the disruption of campus operations due to coronavirus." While the Act does not specify whether this section applies to all or only some of the HEERF funds, the April 30, 2020 ED cover letter and the certification and agreement for the minority-serving and strengthening grants indicate that these funds are not subject to the Section 18004(c) requirement and that institutions are not required to use at least 50% of these funds for grants to students. ED's May 6, 2020 Electronic Announcement outlining certain HEERF reporting requirements also limits the requirement to the student aid and institutional costs portion of the HEERF funds.

Institutions should carefully review the terms and conditions and monitor for further guidance released by ED.

Accounting considerations

NFP higher education institutions

Are the HEERF funds exchange transactions, contributions or another type of transaction?

Under Subtopic 958-605, as amended by ASU 2018-08[2], a transfer of assets from a governmental agency may be an exchange transaction, a contribution or another type of transaction. In analyzing the HEERF grants, the following considerations are made.

— Are the payments a tax exemption, tax incentive or tax abatement?

  No, the HEERF payments are from funds allocated by ED to assist higher education institutions and are not related to taxes.

— Are the transactions exchange transactions?

  No. An exchange transaction is a reciprocal transaction where each party receives and sacrifices commensurate value; the public benefit of a government grant or the execution of the grantor's mission do not represent commensurate value. ED receives no commensurate value.

— Are the payments transfers of assets that are part of an existing exchange transaction between the recipient and an identified customer?

  No. The HEERF payments are to provide aid to students and cover certain institutional costs and do not represent payments to satisfy student receivables. ED specifically states in its student aid FAQ that institutions may not use the emergency financial aid grants to satisfy outstanding or overdue student bills.

— Are the payments agency transactions (i.e. where the institution acts as an agent, trustee or intermediary for another entity)?

  No. For the student aid portion, each institution is required to certify and agree that it "holds those funds in trust for students and acts in the nature of a fiduciary". However, while ED has established certain eligibility requirements for selecting students, ED has also indicated in the certification that the "recipient retains discretion to determine the amount of each individual emergency financial aid grant consistent with all applicable laws…" ED provides recommendations for institutions to consider in allocating the aid to students but strongly encourages financial aid administrators to use professional judgment in selecting eligible students and calculating the individual student awards. Since the institution has discretion (variance power) to choose the beneficiaries and calculate the awards, this transaction is not considered an agency transaction.

— Are the transactions contributions?

  Yes. The transactions are voluntary nonreciprocal transfers from ED and as described above, the institution has discretion sufficient to recognize a contribution received.

Are the HEERF funds conditional contributions?

Yes. Contributions are considered conditional if:

— the contributor has a right of return for the transferred assets (or reduced, settled or cancelled liabilities), or the promisor has a right of release from its obligation to transfer assets (or reduce, settle or cancel liabilities); and

[2] ASU No 2018-08, Clarifying the Scope and the Accounting Guidance for Contributions Received and Contributions Made

— one or more barriers must be overcome before the recipient is entitled to the resources transferred or promised.

Subtopic 958-605 provides indicators that an agreement contains a barrier that must be overcome for the recipient to be entitled to the resources. Agreements may contain multiple barriers that must be overcome before the entity is entitled to the contribution. Although administrative tasks and trivial stipulations (e.g. a requirement to provide a report that serves only administrative purposes) are not considered barriers to entitlement, the ease with which a barrier may be met, or the entity's historical experience with meeting the barrier, are not factors to consider when determining whether the contribution is conditional.

Like other federal grants subject to the Uniform Guidance, an institution is entitled to the HEERF funds only if it complies with the terms and conditions (i.e. barriers) and the funds are subject to return otherwise. As such, we believe the funding represents conditional contributions that are recognized when the conditions on which the contributions depend are substantially met.

The HEERF funds include a *limited discretion* barrier in that ED is limiting the institution's discretion by prescribing how it may spend the funds (i.e. by incurring allowable and reasonable qualifying expenses in accordance with the terms of the agreements and underlying federal regulations, including the Uniform Guidance).

Are there additional barriers for the general grants?

In addition, as discussed above, the Act specifies that institutions are required to use no less than 50% of the HEERF general grants to provide emergency financial aid grants to students. ED requires separate certification agreements for each portion of the general grants and only required institutions to certify the student aid portion before they could certify and receive funds to cover institutional costs. Since the ED certifications for the general grants do not link the spending of the two portions, it may appear that institutions need to consider only the terms and conditions specified for each portion independently of the other portion.

However, the wording in the Act and in subsequent ED communications appears to link the spending on the two portions of the general grants. This linkage would impose an additional barrier whereby institutions are not entitled to the portion allocated for institutional costs unless at least the same amount is spent on student aid. An institution would recognize revenue related to the institutional costs portion only to the extent that the institution has provided grants to students from the HEERF funds. For example, assume an institution receives $500,000 to provide student aid and $500,000 to cover institutional costs. The institution has identified costs that qualify for the entire institutional costs portion of funding but has recorded student aid expense related to the HEERF funds of only $300,000. In this example, assuming the institution has complied with all other terms and conditions, the institution would recognize revenue of $600,000 (i.e. the revenue for the institutional portion would be limited to the amount recognized for the student aid portion). This is similar to the *at-risk* concept discussed in the FASB's Staff Q&A document[3] that analyzed grant cost-sharing provisions and amounts subject to return. ED has not specifically addressed the question of what portion of the institutional costs award would be at risk of return if an institution does not distribute all of the portion allocated for student aid awards. Our analysis herein is based on our interpretation of information provided by ED to date.

Are there special considerations if an institution does not expect to overcome the barriers?

An institution may receive HEERF funding for which it does not believe it will ultimately meet the conditions. This could occur because the funding allocations were pre-determined by ED and an institution may decide to return all or a portion of the funds. Entities that do not expect to earn grant revenue, i.e. meet the conditions, on amounts that are unexpended by period-end should evaluate how

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[3] FASB Staff Q&A, Subtopic 958-605, Application of the Limited Discretion Indicator and Accounting for Cost-Sharing Provisions in a Grant Agreement

these amounts are presented in the financial statements and consider disclosing information about the nature and potential disposition of these amounts.

Are the HEERF funds restricted?

Yes. When the conditions are met and revenue recorded, it will be donor-restricted by purpose due to the qualifying expenses. If the institution follows the *simultaneous release option* for conditional contributions that is permitted under paragraphs 958-605-45-4A and 45-4B, it may report these contributions as without donor restrictions since the conditions and restrictions are met simultaneously.

Internal processes and controls considerations

Higher education institutions that receive HEERF funding will be required to document certain items and periodically report to ED information about use of the funds, including how the amounts of individual emergency financial aid grants were determined. Institutions should note that while certain reporting requirements have been specified in ED communications, ED has indicated that the reporting requirements may also include "such information as the Secretary may reasonably require" in the future. Additionally, as discussed above, these grants are subject to single audit. To support accounting conclusions and compliance with the Act, we recommend that higher education institutions develop and document internal processes and controls for managing and allocating funds, including any metrics relied on to determine student need and factors used to determine costs considered to be associated with significant changes to the delivery of instruction due to the coronavirus.

Evolving information

The potential global and economic impacts of the coronavirus continue to evolve rapidly, and higher education institutions should monitor the situation. Questions remain about the process and conditions related to these funds. Higher education institutions should monitor federal communications regularly for additional guidance on the current and any future funding. The conclusions discussed herein are based on our current understanding of the federal requirements. Entities are encouraged to maintain close communications with their board of trustees, external auditors, legal counsel and other service providers as the circumstances progress. Stay informed at read.kpmg.us/coronavirus

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