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Proposed statement of position : accounting for costs of materials and activities of not-for-profit organizations and state and local governmental entities that include a fund-raising appeal : (a revision of SOP 87-2, Accounting for joint costs of informational materials and activities of not-for-profit organizations that include a fund-raising appeal); Accounting for costs of materials and activities of not-for-profit organizations and state and local governmental entities that include a fund-raising appeal : (a revision of SOP 87-2, Accounting for joint costs of informational materials and activities of not-for-profit organizations that include

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EXPOSURE DRAFT

PROPOSED STATEMENT OF POSITION

ACCOUNTING FOR COSTS OF MATERIALS AND ACTIVITIES OF NOT- FOR-PROFIT ORGANIZATIONS AND STATE AND LOCAL GOVERNMENTAL ENTITIES THAT INCLUDE A FUND-RAISING APPEAL

(A revision of SOP 87-2, Accounting for Joint Costs of Informational Materials and Activities of Not-for-Profit Organizations That Include a Fund-Raising Appeal)

SEPTEMBER 10, 1993

Prepared by the Not-for-Profit Organizations Committee
Accounting Standards Division
American Institute of Certified Public Accountants

Comments should be received by January 10, 1994, and addressed to
Joel Tanenbaum, Technical Manager, Accounting Standards Division, File 3605.JA
AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775

SUMMARY

This proposed statement of position (SOP) would supersede SOP 87-2, *Accounting for Joint Costs of Informational Materials and Activities of Not-for-Profit Organizations That Include a Fund-Raising Appeal*. The scope of this proposed SOP would be broader than the scope of SOP 87-2, because this proposed SOP would apply to all not-for-profit organizations (NPOs) and state and local governmental entities that report expenses or expenditures by function.

It would amend the following, which include guidance for accounting for the costs of informational materials and activities that include a fund-raising appeal:

- AICPA Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations*
- SOP 78-10, *Accounting Principles and Reporting Practices for Certain Nonprofit Organizations*
- AICPA Audit and Accounting Guide *Audits of Certain Nonprofit Organizations*

Also, it would be applied by all not-for-profit organizations and state and local governmental entities in determining fund-raising costs.

This proposed SOP sets forth the following:

- The costs of all materials and activities that include a fund-raising appeal should be reported as fund-raising costs, including costs that are otherwise clearly identifiable with program or management and general functions, unless a bona fide program or management and general function has been conducted in conjunction with the appeal for funds.
- If a bona fide program or management and general function has been conducted in conjunction with an appeal for funds, the joint costs of those activities should be allocated. Costs that are clearly identifiable with fund-raising, program, or management and general functions should be charged to that cost objective.
- Criteria of purpose, audience, and content must be met in order to conclude that a bona fide program or management and general function has been conducted in conjunction with the appeal for funds. (The flowchart in Appendix B on page 29 illustrates the decision-making process for applying the conclusions in the SOP.)
- Some commonly used and acceptable allocation methods are described and illustrated though no methods are prescribed or prohibited.
- Certain information must be disclosed if joint costs are allocated.

The proposed SOP would be effective for financial statements for years beginning on or after its issuance date. Earlier application would be encouraged in fiscal years for which financial statements have not been issued.

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September 10, 1993


Accompanying this letter is an exposure draft of a proposed statement of position (SOP), *Accounting for Costs of Materials and Activities of Not-for-Profit Organizations and State and Local Governmental Entities That Include a Fund-Raising Appeal*. This proposed SOP has been developed by the AICPA Not-for-Profit Organizations Committee.

Comments should be sent to Joel Tanenbaum, Technical Manager, Accounting Standards Division, File 3605.JA, AICPA, 1211 Avenue of the Americas, New York, NY 10036-8775, in time to be received by January 10, 1994.

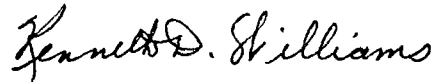
Comments will be reviewed by the Committee to determine whether any revisions should be made to the draft before it is sent to the Accounting Standards Executive Committee (AcSEC) for approval to issue a final SOP.

Written comments on the exposure draft will be available for public inspection at the AICPA library after February 11, 1994, for one year.

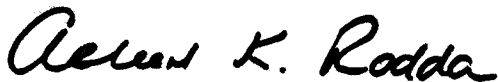
Yours truly,



Norman N. Strauss
Chairman
Accounting Standards Executive Committee



Kenneth D. Williams
Chairman
Not-for-Profit Organizations Committee



Arleen K. Rodda
Director
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PROPOSED STATEMENT OF POSITION

ACCOUNTING FOR COSTS OF MATERIALS AND ACTIVITIES OF NOT-FOR-PROFIT ORGANIZATIONS AND STATE AND LOCAL GOVERNMENTAL ENTITIES THAT INCLUDE A FUND-RAISING APPEAL

INTRODUCTION

1. Some not-for-profit organizations (NPOs) and state and local governmental entities (referred to as *entities* throughout this SOP), such as governmental colleges and universities and governmental hospitals and other health care providers, solicit support through a variety of fund-raising activities, including direct mail, telephone solicitation, door-to-door canvassing, telethons, and special events. Sometimes an activity serves more than one function, such as fund-raising, program, or management and general. Generally, on these occasions, a portion of the costs of the activity is clearly identifiable with a particular function. However, other costs, referred to as joint costs, also generally exist that are not clearly identifiable with any one particular function.

2. External users of financial statements, including contributors, creditors, accreditation agencies, and regulators, want assurance that the amounts entities spend to solicit contributions, as well as the amounts spent for the program and management and general functions, are fairly stated. NPOs subject to the AICPA Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations*, as well as those that follow SOP 78-10, *Accounting Principles and Reporting Practices for Certain Nonprofit Organizations*, and that receive significant amounts of contributions from the public are required to report separately the costs of the fund-raising, program, and management and general functions. Entities subject to the AICPA Audit and Accounting Guide *Audits of Providers of Health Care Services* are required to separately disclose fund-raising expenses. Entities subject to the AICPA Audit and Accounting Guide *Audits of Colleges and Universities*, as amended by SOP 74-8, *Financial Accounting and Reporting by Colleges and Universities*, are required to report fund-raising as part of the "Institutional Support" function.¹ Proper identification and allocation of joint costs may be a significant factor in measuring the costs of activities by function.

3. This SOP establishes financial accounting standards for identifying joint costs and determining the circumstances in which costs of materials and activities that include fund-raising appeals may be allocated. In addition, this SOP requires financial statement disclosures about the nature of the activities for which joint costs have been allocated and the amounts of joint costs, and provides explanations and illustrations of some acceptable allocation methods.

¹ Paragraph 26 of Financial Accounting Standards Board (FASB) Statement of Financial Accounting Standards No. 117, *Financial Statements of Not-for-Profit Organizations*, requires NPOs to report expenses by function. FASB Statement No. 117 is effective for annual financial statements for years beginning after December 15, 1994, except for organizations with less than \$5 million in total assets and less than \$1 million in annual expenses, in which case it is effective for fiscal years beginning after December 15, 1995. Earlier application is encouraged.

SCOPE

4. This SOP establishes accounting standards for all NPOs and state and local governmental entities that report expenses or expenditures by function. (Footnote 3 on page 11 discusses the application of this SOP concerning entities that report expenses or expenditures by function but have a functional structure that does not include *fund-raising, program, or management and general.*) It amends the following:²

- AICPA Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations*
- SOP 78-10, *Accounting Principles and Reporting Practices for Certain Nonprofit Organizations*
- AICPA Audit and Accounting Guide *Audits of Certain Nonprofit Organizations*

This SOP supersedes SOP 87-2, *Accounting for Joint Costs of Informational Materials and Activities of Not-for-Profit Organizations That Include a Fund-Raising Appeal.*

5. This SOP applies only to costs of materials and activities that include a fund-raising appeal. Allocations of other costs are permitted under existing authoritative literature.

BACKGROUND

6. Paragraph 6.11 of Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations*, which is amended by SOP 87-2, states, in part:

The cost of printed material used should be charged to program service, management and general, or fund-raising on the basis of the use made of the material, determined from the content, the reasons for distribution, and the audience to whom it is addressed.

7. Paragraph 97 of SOP 78-10, which is amended by SOP 87-2, states:

If an organization combines the fund-raising function with a program function (for example, a piece of educational literature with a request for funds), the costs should be allocated to the program and fund-raising categories on the basis of the use made of the literature, as determined from its content, the reasons for its distribution, and the audience to whom it is addressed.

8. In 1987, the AICPA issued SOP 87-2. It provided more detailed guidance than did Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations* and SOP 78-10. SOP 87-2 required that all circumstances concerning informational materials and activities that include a fund-raising appeal be considered and that the following criteria be applied:

² As discussed in paragraph 2, certain AICPA pronouncements, such as Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations*, SOP 78-10, Industry Audit Guide *Audits of Providers of Health Care Services*, Audit and Accounting Guide *Audits of Colleges and Universities*, and SOP 74-8, include guidance for reporting fund-raising. Entities that are required to follow the guidance in those pronouncements should follow the guidance in this SOP for reporting the costs of materials and activities that include a fund-raising appeal.

- All...*joint costs*...should be reported as fund-raising expense if it *cannot be demonstrated that a program or a management and general function has been conducted* in conjunction with the appeal for funds (paragraph 15) (emphasis added)
- Demonstrating that a bona fide program or management and general function has been conducted...requires *verifiable indications* of the reasons for conducting the activity. *Such indications include the content* of the nonfund-raising portion of the activity; *the audience targeted; the action, if any, requested* of the recipients; *and other corroborating evidence*, such as written instructions to parties outside the organization who produce the activity, or documentation in minutes of the organization's board of the organization's reasons for the activity. (paragraph 16) (emphasis added)
- Most fund-raising appeals include descriptions of the causes for which the entities exist and the planned uses of the funds, to inform prospective donors why funds are needed and how they will be used. Unless an appeal is *designed to motivate its audience to action* other than providing financial support to the organization, all costs of the appeal should be charged to fund-raising. (paragraph 17) (emphasis added)
- In order to accomplish their basic missions, some organizations educate the public in the attainment of their missions by telling people what they can or should do about particular issues. Those organizations should allocate joint costs to program activities *if the informational materials or activities further those program goals*. (paragraph 18) (emphasis added)

Present Practice

9. The activities of some entities raise consciousness and stimulate action; others are primarily educational. Those activities are often done in conjunction with fund-raising. Many entities allocate the joint costs of those activities primarily to educational programs, based on the content of the materials distributed or the activities conducted. These entities believe that their primary programs are to educate the public or stimulate action and that such activities or the distribution of such materials helps accomplish those program goals.

10. Other entities allocate costs to fund-raising, program, or management and general based on the purpose of the material or activity, determined by the reason for its distribution, the audience to whom it is addressed, and its content.

11. Some believe the guidance in SOP 87-2 is inadequate to determine whether fund-raising appeals, such as those that also list the warning signs of a disease, are designed to motivate their audiences to action other than to provide support to the organization and whether appeals that merely repeat slogans are designed to help the entity attain its mission by educating the public in a meaningful manner. It is unclear what attributes the targeted audience should possess in order to conclude that an educational program function is being conducted.

12. SOP 87-2 has been difficult to implement and inconsistently applied in practice, because of the following:

- The second sentence of paragraph 1 of SOP 87-2 states that "some of the costs incurred by such organizations are clearly identifiable with fund-raising, such as the cost of fund-raising consulting services." It is unclear whether activities that would otherwise be considered program activities may continue to be characterized as program activities if they are performed or overseen by professional fund-raisers. It is unclear whether activities would be reported differently (for example, program versus fund-raising)

depending on whether the fund-raising consultant is compensated by a predetermined fee or by some other method, such as a percentage of funds raised.

- SOP 87-2 is unclear about whether allocation of costs to program expense is permitted if the activity for which the costs were incurred would not have been undertaken were the activity not intended to raise funds.
- SOP 87-2 defines joint costs through examples, and it is unclear what kinds of costs are covered by SOP 87-2.
- SOP 87-2 is unclear concerning whether salaries and indirect costs can be joint costs.

13. SOP 87-2 does not address the issue of how to allocate joint costs. Some believe that guidance should be provided on the subject, possibly through illustrations of the use of acceptable allocation methods.

DEFINITIONS

Joint Activities

14. For purposes of this SOP, joint activities are activities that are part of the fund-raising function and one or more of the following functions:

- Program
- Management and general

Joint Costs

15. For purposes of this SOP, joint costs are the costs of conducting, producing, and distributing materials and activities that include both a fund-raising appeal and a bona fide program or management and general component and that are not specifically attributable to a particular component. Joint conducting and producing costs may include the costs of salaries, facilities rental, contract labor, consultants, paper, and printing. Joint distribution costs may include costs of postage, telephones, airtime, and facility rentals. Some costs, such as utilities, rent, and insurance, commonly referred to as indirect costs, may be joint costs. However, for some entities, the portion of those costs that are joint costs are impracticable to measure and allocate.

16. Costs that are specifically attributable to a particular cost objective, such as fund-raising, program, or management and general, are not joint costs. For example, some costs incurred for printing, paper, professional fees, and salaries to produce donor cards, are not joint costs, though they may be incurred in connection with conducting a joint activity. However, as discussed in paragraphs 18 and 19, accounting for such costs is covered by this SOP if they are incurred for joint materials and activities even though the costs are not joint costs.

CONCLUSIONS

Flowchart

17. The flowchart in appendix B on page 29 of this SOP illustrates the decision-making process for applying the conclusions in this SOP to determine whether a bona fide program or management

and general function has been conducted and to which function costs of an activity should be charged. The flowchart is explained in paragraph 21.

Joint Materials and Activities

18. The cost of joint materials and activities may include both joint costs and costs that are clearly identifiable with a particular cost objective (function), such as fund-raising, program, or management and general.

19. All costs of materials and activities that include a fund-raising appeal should be reported as fund-raising costs, including costs that are otherwise clearly identifiable with program or management and general functions, unless it can be demonstrated that a bona fide program or management and general function has been conducted in conjunction with the appeal for funds. However, if this can be demonstrated, costs that are clearly identifiable with a particular cost objective should be charged to that cost objective and joint costs should be allocated between fund-raising and the appropriate program or management and general function.³ (Paragraphs 20 to 31 discuss the criteria for determining whether a bona fide program or management and general function has been conducted in conjunction with the appeal for funds.) For example, the costs of materials that otherwise accomplish program goals and that are unrelated to fund-raising, such as the costs of an educational pamphlet included in a joint activity, should be charged to program if it can be demonstrated that a bona fide program function has been conducted in conjunction with the appeal for funds. However, if the pamphlet is used in fund-raising packets and it cannot be demonstrated that a bona fide program or management and general function has been conducted in conjunction with the appeal for funds, the costs of the pamphlets should be charged to fund-raising.

Bona Fide Program or Management and General Function

20. In order to conclude that a bona fide program or management and general function has been conducted in conjunction with the appeal for funds, all of the following criteria, which are discussed in paragraphs 21 to 31 and illustrated in appendix A, must be met:

- Purpose
- Audience
- Content

21. The flowchart in appendix B on page 29 illustrates the decision-making process for determining whether the criteria in paragraph 20 have been met, as follows:⁴

³ Some entities that report expenses or expenditures by function have a functional structure that does not include fund-raising, program, or management and general. Paragraph 2 of this SOP discusses a number of such entities. Though this SOP applies to all entities that report expenses or expenditures by function, it is not intended to require reporting the functional classifications of fund-raising, program, and management and general. Rather, those functional classifications are discussed throughout this SOP for purposes of illustrating how the guidance in this SOP would be applied by entities that use those functional classifications. Entities that do not use those functional classifications should apply the guidance in this SOP for purposes of accounting for joint activities, using their reporting model.

⁴ Though the flowchart and the following description of it illustrate the general decision process for applying the conclusions in this SOP, they are not intended to be substitutes for the detailed conclusions.

- a. If substantially all compensation or fees for performing the activity are based on amounts raised, the purpose criterion is not met (paragraph 23) and all costs of the joint activity should be charged to fund-raising.
- b. If the method of compensation under item a does not lead to the conclusion that all costs of the joint activity should be charged to fund-raising, determine whether the program or management and general component is conducted on a similar scale using the same medium without the fund-raising appeal. If it is conducted on a similar scale using the same medium without the fund-raising appeal, the purpose criterion is met (paragraph 25) and the audience and content criteria should be considered to determine whether all three criteria in paragraph 20 have been met. If it is not conducted using the same medium without the fund-raising appeal, consider the indicators in item c to determine whether the purpose criterion has been met.
- c. If the purpose criterion is not met under item b, it may be met based on an evaluation of indicators (paragraph 26). If the purpose criterion is not met based on an evaluation of those indicators, all costs of the joint activity should be charged to fund-raising. If the purpose criterion is met based on an evaluation of those indicators, the audience and content criteria should be considered to determine whether all three criteria in paragraph 20 have been met.
- d. If the audience is selected principally on its ability or likelihood to contribute (paragraphs 27 to 29), the audience criterion is not met and all costs of the joint activity should be charged to fund-raising. If the audience is not selected principally on its ability or likelihood to contribute, but rather is selected because it can assist the entity in meeting its program goals other than by financial support provided to the entity, the audience criterion is met and the content criterion should be considered to determine whether all three criteria in paragraph 20 have been met.
- e. If the materials or activity motivate the audience to action in support of program goals, the content criterion is met and the costs of the joint activities should be allocated (paragraphs 30 and 31). However, if the fund-raising is incidental to the program activity, the joint costs need not be allocated and may instead be charged entirely to program (paragraph 32).
- f. If the content criterion is not met under item e, consider whether the materials or activity inform the public regarding the entity's stewardship function [paragraph 30(b)]. If they inform the public regarding the stewardship function, the content criterion is met and the joint costs of the activity should be allocated. However, if the fund-raising is incidental to the management and general activity, the joint costs need not be allocated and may instead be charged entirely to management and general (paragraph 30). If they do not inform the public regarding the stewardship function, the content criterion has not been met and all costs of the joint activity should be charged to fund-raising.

Purpose

22. In determining whether a bona fide program or management and general function has been conducted, the purpose for conducting the activity must be considered.

23. If substantially all compensation or fees for performing the activity are based on amounts raised, the purpose criterion is not met and all costs of the activity should be charged to fund-raising. Further, if the performance of the party performing the activity is evaluated substantially on the activity's effectiveness in raising funds, the purpose criterion is not met and all costs of the activity should be charged to fund-raising.

24. If the conditions in paragraph 23 have not resulted in all costs of the activity being charged to fund-raising, the purpose criterion may be met either by the conditions in paragraph 25 or the conditions in paragraph 26.

25. If a similar program or management and general component is conducted without the fund-raising appeal using the same medium, such as direct mail, direct response advertising, or television, and on a scale that is similar to or greater than the scale on which it is conducted with the appeal, the purpose criterion is met.

26. If the purpose criterion is not met based on the condition in paragraph 25, it may be met based on other factors. Those other factors are not universally applicable, and they should be considered based on the facts and circumstances concerning a particular joint activity. The relative importance of those factors should be weighed in determining whether the purpose of the activity includes conducting a bona fide program or management and general activity. Accordingly, the following indicators should be considered in determining whether the purpose criterion is met.

- a. *The method of compensation for performing the activity.* If compensation or fees are based in part (but less than substantially) on amounts raised, the purpose criterion may not be met. Paragraph 23 discusses situations in which such compensation is based substantially on amounts raised.
- b. *The method of evaluating the performance of the activity.* The following should be considered:
 - Whether there is a process to identify and evaluate program results and accomplishments. Identification and, where practical, measurement of program results and accomplishments may indicate that a bona fide program has been conducted.
 - Whether evaluation of the effectiveness of the activity is skewed to the activity's effectiveness in raising funds or skewed to the accomplishment of program goals. The former may indicate that the purpose criterion is not met. The latter may indicate that it is met.
- c. *Different media for the program or management and general component and fund-raising.* Consider whether the program or management and general component is also conducted in a different medium without a significant fund-raising component.
- d. *Qualifications and duties of personnel.* The qualifications and duties of those performing the activity should be considered according to the following criteria.
 - If the entity employs a third party, such as a consultant or contractor, to perform part or all of the activity, the third party's experience and full range of available services should be considered in determining whether it is performing program activities.
 - If the entity's employees perform part or all of the activity, the full range of their job duties should be considered in determining whether those employees are performing program or management and general activities. For example, employees who are not members of the fund-raising department and those who perform other nonfund-raising activities are more likely to perform activities that include bona fide program or management and general functions than are employees who otherwise devote significant time to fund-raising.

e. *Tangible evidence of activities.* Consider whether tangible evidence supports the existence of a bona fide program or management and general component of the activity. Examples of such tangible evidence include the following:

- The organization's mission, as stated in its fund-raising material, bylaws, or annual report
- Minutes of board of directors, committees, or other meetings
- Restrictions imposed by donors (who are not related parties) on gifts intended to fund the activity
- Long-range plans or operating policies
- Job descriptions
- Written instructions to other entities, such as script writers, consultants, or list brokers, concerning the purpose of the activity, audience to be targeted, or method of conducting the activity
- Internal management memoranda

Audience

27. If the audience for the materials or activities is selected principally on its ability or likelihood to contribute, the audience criterion is not met and all the costs of the activity should be charged to fund-raising.

28. If the audience is selected principally based on its need for the program or because it can assist the entity in meeting its program goals other than by financial support provided to the entity, the audience criterion is met. The following are examples of the kinds of targeted audiences and the conditions under which they would or would not generally meet the audience criterion:

- a. *A broad segment of the population.* Appealing to a broad segment of the population to avoid heart disease, for example, by avoiding cholesterol or reducing dietary fat, may meet the audience criterion. However, an appeal to a broad segment of the population concerning a condition affecting only a small segment of the population or geographical area would indicate that the audience criterion had not been met.
- b. *A population specifically in need of the program services of the organization.* An appeal concerning urban poverty and including information about qualifying for food stamps and other assistance mailed to residents of a particular urban area in need of those programs would meet the audience criterion. However, such a solicitation targeted to specific high-income suburban neighborhoods would not meet the audience criterion.
- c. *A population that is able to perform actions to help achieve the program objectives.* An environmental appeal including advice to use mass transit mailed to an urban or suburban audience where mass transit exists would meet the audience criterion. However, such an appeal would not meet the audience criterion if mailed to rural areas where mass transit is unavailable.

29. The source of the names and the characteristics of the audience should be considered in determining whether the audience was selected principally on its ability or likelihood to contribute. For example, if the audience is made up of existing donors who have also participated in program activities in the past, it is likely that the audience criterion would be met. If the audience is made up of past donors with no such previous program participation, the audience criterion would likely not be met. Many entities use list rentals and exchanges to reach new audiences. The source of

such lists may indicate the purpose for which they were selected. For example, lists acquired from organizations with similar or related programs are more likely to meet the audience criterion than are lists based on consumer profiles.

Content

30. In order to meet the content criterion, the materials or activity must support bona fide program or management and general functions, as follows:

- a. *Program.* The materials or activity must call for specific action by the recipient that will help accomplish the entity's mission and that is unrelated to providing financial or other support to the entity itself by (1) benefiting the recipient (such as by improving the recipient's physical, mental, emotional, or spiritual health and well-being) or (2) benefiting society by addressing societal problems. Information must be provided explaining the need for and benefits of the action. Sufficient detail should be provided describing the action to be taken; merely providing a slogan is not sufficient.⁵
- b. *Management and General.* The materials and activities should report on mission accomplishments or inform supporters about the entity's stewardship performance.

31. Statements identifying and describing the entity or stating the needs or concerns to be met or how the funds provided will be used should be treated as in support of the fund-raising appeal. Educational materials and activities should be treated as support of fund-raising unless they motivate the audience to action other than providing financial support to the organization.⁶

⁵ Examples of calls to action that benefit the recipient or society include the following:

- a. Calls for action that benefit the recipient, such as the following.
 - *Stop smoking.* Specific methods, instructions, references, and available resources should be suggested; a simple admonition to stop smoking is too vague to be considered a motivating factor.
 - *Do not use alcohol or drugs.* The same conditions apply as with the stop smoking message.
 - *If you are suicidal, call this hotline.*
- b. Calls for action that benefit society, such as the following.
 - *Write or call your legislator or other public official.* The subject matter to be communicated should be specified.
 - *Volunteer to help out at your local nursing home.*
 - *Protest.* The object of protest and specific method of protest, such as a time and place to demonstrate or an entity to communicate with, must be described; a general call to protest against something is too vague to satisfy the criterion of *action*.
 - *Pray.* If what is to be prayed for, such as the occurrence of a particular event, is specifically stated; a general call to prayer is too vague to satisfy the criterion of *action*.
 - *Complete and return the enclosed questionnaire.* This applies only if the results of the questionnaire help the entity achieve its mission.
 - *Boycott a particular product or company.*

⁶ Some educational messages, for example, messages informing the public about lifesaving techniques, have an implied message to motivate the audience to action other than by providing financial support to the organization.

Incidental Costs

32. Many entities conduct fund-raising activities in conjunction with program or management and general activities that are incidental to such program or management and general activities. For example, the words, "Contributions to Organization X may be sent to [address]," may appear on a small area of a message that would otherwise be considered a program or management and general activity based on its purpose, content, and audience. The fund-raising activity described in the previous example would generally be considered incidental to the program or management and general activity being conducted. Similarly, entities may conduct program or management and general activities that are incidental to fund-raising activities, such as including a generic program message on all public communications. An example would be the inclusion of the words, "Continue to pray for [a particular cause]," with fund-raising materials. The program activity described in the previous example would generally be considered incidental to the fund-raising activity being conducted. In circumstances in which a fund-raising, program, or management and general activity is conducted in conjunction with another activity and is incidental to that other activity, joint costs are not required to be allocated and may therefore be charged to the other activity. However, the costs of the incidental activities may be charged to their respective functional classification if the conditions for charging those costs to that functional classification included in this SOP are met. However, if the program or management and general activities are incidental to the fund-raising activities, it is unlikely that the conditions required by this SOP to permit allocation of joint costs would be met.

Allocation Methods

33. The allocation of joint costs should be based on the degree to which the cost element was incurred for the benefit of the activity or activities undertaken (that is, fund-raising, program, or management and general). The cost allocation methodology used should be rational and systematic, it should result in an allocation of joint costs that is reasonable and not misleading, and it should be applied consistently, given similar facts and circumstances. However, that requirement is not intended to prohibit entities from using more than one allocation method. The reasonableness of the joint cost allocation should be evaluated based on whether it reflects the degree to which costs have been incurred for the benefit of fund-raising, bona fide program, or management and general activities. In making that evaluation, the purpose, audience, and content criteria should be considered.

34. Some commonly used cost allocation methods follow.

- *Physical Units Method.* Joint costs are allocated to activities in proportion to the number of units of output that can be attributed to each of the activities. Examples of units of output are lines, square inches, and physical content measures. This method assumes that the benefits received by the fund-raising, program, or management and general component activity from the joint costs incurred are directly proportional to the lines, square inches, or other physical output measures attributed to each component. This method may result in an unreasonable allocation of joint costs if the units of output, for example, line counts, do not reflect the degree to which costs are incurred for the joint activities. For example, a joint cost allocation based on line counts may not reflect the purpose for which the activity was undertaken or the reasons the audience was selected. Use of the physical units method may also result in an unreasonable allocation if the physical units cannot be clearly ascribed to fund-raising, program, or management and general. For example, direct mail and telephone solicitations sometimes include content that is not clearly identifiable with either fund-raising, program, or management and general; or the physical units of such content are inseparable.

- *Illustration:* Assume a direct mail campaign is used to educate the public about programs of the entity and to solicit funds to support the entity and its programs. Further, assume that the appeal meets the criteria for allocation of joint costs to more than one cost objective.

The letter and reply card includes a total of one hundred lines. Forty-five lines pertain to program because they educate the recipient about the entity’s program and include a call to action, while fifty-five lines pertain to the fund-raising appeal. Accordingly, 45 percent of the costs are allocated to program and 55 percent to fund-raising.

- *Relative Direct Cost Method.* Joint costs are allocated to each of the components on the basis of their respective direct costs. Direct costs are those costs that are incurred in connection with the multipurpose materials or activities and that are specifically identifiable with a cost objective (program, fund-raising, or management and general). This method may result in an unreasonable allocation of joint costs if the joint costs of the materials or activities are not incurred in approximately the same proportion and for the same reasons as the direct costs of those activities. For example, if a relatively costly booklet informing the reader about the entity’s mission (including a call to action) is included with a relatively inexpensive fund-raising letter, the allocation of joint costs based on the cost of these pieces may be unreasonable.

- *Illustration:* The costs of a direct mail campaign that can be specifically identified with program services are the costs of separate program materials and a postcard with a call to action. They total \$20,000. The direct costs of the fund-raising component of the direct mail campaign consist of the costs to develop and produce the fund-raising letter. They total \$80,000. Joint costs associated with the direct mail campaign total \$40,000 and would be allocated as follows under the relative direct cost method:

Program	$\$20,000/\$100,000 \times \$40,000 = \$8,000$
Fund-Raising	$\$80,000/\$100,000 \times \$40,000 = \$32,000$

- *Stand-Alone Joint-Cost-Allocation Method.* Joint costs are allocated to each component based on the ratio that the cost of conducting each component would have borne to the total costs of conducting each of the joint components had each component been conducted independently. This method assumes that efforts for each component in the stand-alone situation are proportionate to the efforts actually undertaken in the joint-cost situation. This method may result in an unreasonable allocation because it ignores the effect of each function, that is performed jointly with other functions, on other such functions. For example, the programmatic impact of a direct mail campaign or a telemarketing phone message may be significantly lessened when performed in conjunction with a fund-raising appeal.

- *Illustration:* Assume that the joint costs associated with a direct mail campaign are the costs of stationery, postage, and envelopes at a total of \$100,000. The costs of stationery, postage, and envelopes to produce and distribute the program component separately from the fund-raising component would have been \$90,000 for the program component and \$70,000 for the fund-raising component. Under the stand-alone joint-cost-allocation method, the \$100,000 in joint costs would be allocated as follows: $\$90,000/\$160,000 \times \$100,000 = \$56,250$ to program services and $\$70,000/\$160,000 \times \$100,000 = \$43,750$ to fund-raising.

Disclosure of Joint Costs

35. Entities that allocate joint costs should disclose the following in the notes to their financial statements:

- The types of materials and activities for which joint costs have been incurred
- A statement that such costs have been allocated
- The allocation method
- The total amount allocated during the period
- The portion allocated to each functional expense category

36. This SOP recommends, but does not require, that, in addition to disclosure of the total joint costs and the portion allocated to each functional expense category, the amount of joint costs for each activity be disclosed, if practical.

37. The following illustrates the disclosures discussed in paragraphs 35 and 36:

Note X. Allocation of Joint Costs

In 19XX, the organization conducted four activities that included appeals for funds and incurred joint costs of \$310,000. These activities included direct mail campaigns, two special events, and a telethon. [*Note to reader: The following sentence is recommended but not required.*] Joint costs for each activity were \$50,000, \$150,000, and \$110,000 respectively.] Joint costs were allocated using the physical units method for the direct mail campaigns, based on the number of lines of output for each component, and the relative direct cost method, based on the direct costs of each component, for the two special events and the telethon. Joint costs of \$180,000 were allocated to fund-raising, \$80,000 to Program A, \$40,000 to Program B, and \$10,000 to management and general.

EFFECTIVE DATE

38. The SOP is effective for financial statements for years beginning on or after its issuance date. Earlier application is encouraged in fiscal years for which financial statements have not been issued. If comparative financial statements are presented, retroactive application is permitted but not required.

DISCUSSION OF CONCLUSIONS

Rationale for Not Including the Word Joint in the Title

39. The title of SOP 87-2 included the word *joint* to reflect the focus on joint-cost disclosures. The AICPA Accounting Standards Executive Committee (AcSEC) believes that the SOP should provide guidance for more costs than merely joint costs. Therefore, the SOP covers all costs of materials and activities that include a fund-raising appeal.

Rationale for Not Including the Word Informational in the Title

40. The title of SOP 87-2 included the word *informational* due to concerns at the time the SOP was issued about abuses in reporting the costs of public information and education. AcSEC believes that this SOP provides accounting guidance that applies broadly to all materials and activities of entities that include a fund-raising appeal, including those made in conjunction with program or management and general functions that include no informational materials, such as annual dinners. Therefore, AcSEC believes that including the word *informational* in the title would imply a more limited scope than is intended and the word *informational* is excluded from the title of this SOP.

Allocation Criteria

41. Determining whether the costs of joint activities should be classified as fund-raising, program, or management and general sometimes is difficult, and such distinctions sometimes are subject to a high degree of judgment. Practice indicates that some entities prefer to report costs as program or management and general rather than as fund-raising. For practical reasons, AcSEC concluded that costs of activities that include a fund-raising appeal should be presumed to be fund-raising costs unless there is a bona fide program or management and general function. AcSEC believes that such a rebuttable presumption is necessary to prevent potential abuses in financial reporting.

Slogans

42. Paragraph 30, footnote 5, states that certain calls to action are too vague to be considered motivating factors and therefore do not satisfy the criteria in the SOP that requires "...specific action by the recipient that will help accomplish the entity's mission...." The last sentence of paragraph 30 (a) states that "[s]ufficient detail should be provided describing the action to be taken; merely providing a slogan is not sufficient." The SOP does not conclude whether slogans benefit society. Rather, it provides accounting guidance for considering how, for purposes of this SOP, accounting for the costs of activities that include a fund-raising appeal should be affected by the use of slogans in those appeals.

Incidental Activities

43. Many entities include incidental fund-raising efforts with bona fide program or management and general activities. Such efforts may be a practical, efficient means for entities to raise funds, though the principal purpose of the activity may be to fulfill program or management and general functions. AcSEC believes that in those circumstances, the existence of such incidental activities should not affect the determination of whether the activity is a program or management and general activity. Similarly, the existence of incidental program or management and general activities should not affect the determination of whether the activity is a fund-raising activity. Therefore, this SOP states that the existence of incidental activities does not lead to the conclusion that joint costs are required to be allocated between fund-raising and the appropriate program or management and general activity.

Allocation Methods

44. AcSEC believes that no particular allocation method or methods are necessarily more desirable than other methods in all circumstances. Therefore, this SOP neither prescribes nor prohibits any particular allocation methods. AcSEC believes that entities should apply the

allocation methods that result in the most reasonable cost allocations for the activities of those entities. This SOP illustrates several cost allocation methods, any one of which may result in a reasonable or unreasonable allocation of costs in certain circumstances. The methods illustrated are not the only acceptable methods, but are merely intended to illustrate some methods that may be acceptable in some circumstances. However, AcSEC believes that, generally, the methods illustrated in this SOP are among those most likely to result in meaningful cost allocations.

Disclosures

45. Paragraph 36 includes disclosures that are recommended but not required. AcSEC believes those disclosures provide useful information, but that the benefits of providing that information may not be justified by the costs in all cases.

**ILLUSTRATIONS OF APPLYING THE CRITERIA OF PURPOSE, AUDIENCE,
AND CONTENT TO DETERMINE WHETHER A BONA FIDE PROGRAM OR
MANAGEMENT AND GENERAL ACTIVITY HAS BEEN CONDUCTED**

Illustration 1

Facts

A.1 Entity A's mission is to prevent drug abuse. Entity A's annual report states that one of its objectives in fulfilling that mission is to assist parents in preventing their children from abusing drugs.

A.2 Entity A mails informational materials to the parents of all junior high school students to help and encourage parents to counsel children about the dangers of drug abuse and to detect drug abuse, and includes an appeal for funds. Entity A conducts other activities that inform the public about the dangers of drug abuse that do not include appeals for funds.

Conclusion

A.3 The purpose criterion is met because (1) Entity A's mission is to perform such programs and (2) it otherwise conducts the program activity in this illustration without a fund-raising appeal.

A.4 The audience and content criteria are met.

A.5 The costs of the paper including an appeal for funds should be charged to fund-raising, and the costs of the informational materials should be charged to program.

A.6 Joint costs should be allocated based upon a reasonable method.

Illustration 2

Facts

A.7 Entity B's mission is to reduce the incidence of illness from XYZ disease, which afflicts a broad segment of the population. One of Entity B's objectives in fulfilling that mission is to inform the public about the early warning signs of the disease and specific action that should be taken to prevent the disease.

A.8 Entity B maintains a list of its prior contributors and sends them donor renewal mailings. The mailings include a separate piece of paper containing messages about the early warning signs of the disease and specific action that should be taken to prevent it. The information on that separate piece of paper is also sent to a similar-sized audience, but without the fund-raising appeal. Prior donors are deleted from the mailing list if they have not contributed to Entity B during the last three years.

Conclusion

A.9 The purpose and content criteria are met.

A.10 The audience criterion is not met, because Entity B selects individuals to be added to or deleted from the mailing list based on their likelihood to contribute.

A.11 Therefore, all costs, including those of the separate program piece should be charged to fund-raising.

Illustration 3

Facts

A.12 Entity C's mission is to reduce the incidence of illness from XYZ disease, which afflicts a broad segment of the population. One of Entity C's objectives in fulfilling that mission is to increase government funding for research about the disease.

A.13 Entity C maintains a list of its prior contributors and calls them on the telephone asking for donations and encouraging them to contact their elected officials to urge increased government funding for research about the disease. Entity C's research indicates that its donors are twice as likely as nondonors to contact their elected officials about such funding. When prior donors have not given for three years, they are deleted from the calling list.

Conclusion

A.14 The purpose, audience, and content criteria are met.

A.15 Though the activity is directed primarily at those who previously contributed, as in Illustration 2, the audience's program involvement and ability to perform actions to help achieve the mission demonstrate that the audience was selected based on its ability to assist Entity C in meeting its program goals.

Illustration 4

Facts

A.16 Entity D conducts an annual fund-raising mailing that includes information on a separate piece of paper telling recipients what kind of action to take concerning a particular environmental problem. Mailing labels in zip codes with average household incomes above \$45,000 are purchased from a list supplier.

Conclusion

A.17 The purpose criterion may be met depending on an evaluation of the indicators in paragraph 26. The content criterion would be met.

A.18 The criterion of audience would generally not be met. Because the audience selection is based principally on the ability or likelihood to contribute, and not on its being a broad segment of the population, its need of the program services, or its ability to perform actions to help achieve

the mission, all costs including the specific costs of the separate program piece would generally be charged to fund-raising.

Illustration 5

Facts

A.19 Entity E is a membership organization whose mission is to improve the quality of life for senior citizens. One of Entity E's objectives included in that mission is to increase the physical activity of senior citizens. Entity E also sends representatives to speak to groups about the importance of exercise and also to conduct exercise classes.

A.20 Entity E mails a brochure on the importance of exercise that encourages exercise in later years to residents over the age of 58 in three ZIP code areas. The last two pages of the four-page brochure include a perforated contribution remittance form on which Entity E explains its program and makes an appeal for funds. The content of the first two pages of the brochure is primarily educational; it explains how seniors can undertake a self-supervised exercise program and urges them to do so.

A.21 The leaflet is distributed to educate people in this age group about the importance of exercising, to encourage them to exercise, and to raise funds for Entity E. These objectives are documented in a letter to the public relations firm that developed the piece and are supported by a medical advisory board's approval of the exercise program. The audience is selected based on age, without regard to ability to contribute. Entity E believes that most of the recipients would benefit from the information about exercise.

Conclusion

A.22 The purpose, audience, and content criteria are met, and the joint costs should be allocated.

Illustration 6

Facts

A.23 The facts are the same as those in Illustration 5, except that Entity F employs a fund-raising consultant to develop the brochure and pays that consultant 30 percent of funds raised.

Conclusion

A.24 The content and audience criteria are met.

A.25 The purpose criterion is not met, however, because the party performing the activity is compensated based on a percentage of funds raised. Therefore, all costs of the activity should be charged to fund-raising.

Illustration 7

Facts

A.26 Entity G's mission is to protect the environment. One of Entity G's objectives included in that mission is to take action that will increase the portion of waste recycled by the public.

A.27 Entity G conducts a door-to-door canvass of a community that recycles a low portion of its waste. The canvassers inform the residents about the environmental problems created by not recycling, recommend actions residents could take to help increase recycling, and ask for donations. The ability or likelihood of the residents to contribute is not a basis for selection, and all neighborhoods in this geographic area are covered if their recycling falls below a predetermined rate.

Conclusion

A.28 The purpose, audience, and content criteria are met, and the joint costs should be allocated.

A.29 The audience is selected based on presumed need for the program messages without regard to the ability to provide financial support. Therefore, the direct costs clearly identifiable with including a request for funds during the canvass, such as the cost of collection canisters, should be charged to fund-raising. Other costs should be charged to the program function. The joint costs would generally include the costs of the canvassers that Entity G reimburses.

Illustration 8

Facts

A.30 Entity H's mission is to provide summer camps for economically disadvantaged youths. Educating the families of ineligible youths about the camps is not one of the objectives included in that mission.

A.31 Entity H conducts a door-to-door solicitation campaign for its camp programs. In the campaign, volunteers with canisters visit homes in middle-class neighborhoods to collect contributions. Entity H believes that people in those neighborhoods would not need the camp's programs, but may contribute. The volunteers explain the camp's programs, including why the disadvantaged children benefit from the program, and distribute leaflets to the residents regardless of whether they contribute to the camp. The leaflets describe the camp, its activities, who can attend, and the benefits to attendees. Requests for contributions are not included in the leaflets.

Conclusion

A.32 The content criterion is not met because there is no call to action. Further, the audience criterion is not met because the audience does not need the program and cannot assist the entity in meeting its program goals other than by providing support. The purpose criterion may be met depending on an evaluation of the indicators in paragraph 26.

A.33 All costs of this activity should be charged to fund-raising. (There are no direct program costs because no program was performed.)

A.34 If the activity were conducted in a disadvantaged neighborhood and residents were also given a telephone number to call or an address to write to for more information, the conclusion may be different. In those circumstances, the audience and content criteria would be met and the purpose criterion may be met based on an evaluation of the indicators in paragraph 26. Only the cost of the canvassers would likely be charged to fund-raising because the fund-raising would be incidental to the program purpose. The information about the program and how to take advantage of it would be charged to program. The joint costs would generally include the costs of the canvassers that Entity H reimburses.

Illustration 9

Facts

A.35 Entity I's mission is to give the public lifesaving educational messages. One of Entity I's objectives in fulfilling that mission, as stated in the minutes of the board's meetings, is to produce and show television broadcasts including information about lifesaving techniques.

A.36 Entity I conducts an annual national telethon to raise funds and to reach the American public with lifesaving educational messages. The broadcast includes segments on personal health care and other segments describing Entity I's services. Entity I broadcasts the telethon to the entire country, not merely to areas selected on the basis of giving potential or prior fund-raising results.

Conclusion

A.37 The audience and content criteria are met.

A.38 In assessing whether the purpose criterion is met, a determination should be made as to whether or not the activity is or would be conducted without the fund-raising appeal using the same medium. If Entity I uses television broadcasts devoted entirely to lifesaving educational messages to conduct program activities without fund-raising, the purpose criterion would be met. If Entity I does not use such television programs to conduct program activities without fund-raising, and the purpose criterion is not met based on the indicators in paragraph 26, the purpose criteria would not be met and all costs of the telethon should be charged to fund-raising.

A.39 If the purpose criterion is met, joint costs such as television time, overall planning, and production should be allocated between program and fund-raising. One method of allocation may be based on the relative amounts of time each was on the air. The direct costs clearly identifiable with the lifesaving educational messages are not joint costs and should be charged to the program function. The costs of the service description messages that inform the audience about the organization and the related appeal for funds are not joint costs and should be charged to fund-raising.

Illustration 10

Facts

A.40 Entity J's mission is to provide food, clothing, and medical care to children in developing countries.

A.41 Entity J conducts television broadcasts ranging from 30 minutes to one hour in length that describe Entity J's programs, show the needy children, and then end with an appeal for funds.

Conclusion

A.42 The purpose, audience, and content criteria are not met. There is no call to action other than supporting Entity J, the audience's need for or ability to assist any programs is not a significant factor in selecting the audience, and all descriptions of Entity J's activities are in support of fund-raising.

A.43 All costs should be charged to fund-raising.

Illustration 11

Facts

A.44 Entity K is a University that distributes its annual report, which includes reports on mission accomplishments, to those who have contributed over the three preceding years, its board of trustees and its employees. Included in the package containing the annual report are educational materials about Entity K's mission, requests for funds, and donor reply cards.

Conclusion

A.45 The purpose, audience, and content criteria are met.

A.46 Though the activity is directed primarily at those who previously contributed, the audience was selected based on its presumed interest in Entity K's reporting on its financial position, results of operations, mission accomplishments, and fulfillment of its fiduciary responsibilities.

A.47 The costs clearly attributable to the annual report should be charged to management and general. The costs of the educational materials and donor reply cards should be charged to fund-raising. The joint costs should be allocated between management and general and fund-raising.

Illustration 12

Facts

A.48 Entity L is an animal rights organization. It mails a package of material to individuals included in lists rented from various environmental and other organizations that support causes that Entity L believes are congruent with its own. In addition to donor response cards and return envelopes, the package includes postcards addressed to legislators and bumper stickers urging support for legislation restricting the use of animal testing for cosmetic products. It also includes a letter instructing the reader to take specific actions to further Entity L's goals. The mail campaign is part of an overall strategy that includes magazine advertisements and the distribution of similar materials at various community events.

Conclusion

A.49 The purpose, audience, and content criteria are met. A bona fide program function is performed, the audience is not limited to potential donors; it also includes individuals who can assist Entity L in achieving its program goals, and the content includes a request for action in support of the program.

A.50 Entity L accounts for the costs of the activity as follows:

Costs Charged Directly to Fund-Raising

Donor response card	\$ 14,000
Return envelope for contribution	18,000
Return postage	<u>8,000</u>
	\$ 40,000

Costs Charged Directly to Program

Bumper sticker	\$ 41,000
Postcard to legislator	<u>19,000</u>
	\$ 60,000

Joint Costs

Consulting and design costs	\$ 24,000
List rentals	182,000
Letter	52,000
Envelope (outgoing)	40,000
Postage (outgoing)	160,000
Mail handling costs	<u>42,000</u>
	\$ 500,000

A.51 Entity L uses the relative direct-cost-method to allocate joint costs. As a result, \$300,000 ($\$60,000/\$100,000 \times \$500,000$) of the joint costs are charged to program and \$200,000 ($\$40,000/\$100,000 \times \$500,000$) of the joint costs to fund-raising. Direct costs of \$60,000 and \$40,000 are charged to program and fund-raising, respectively.

A.52 In reviewing the purpose of the activity, Entity L concludes that though the fund-raising component is important, the activity was conducted primarily for program purposes. Passing the proposed legislation was highlighted as a major goal in Entity L's three-year program plan, and Entity L believes the mail campaign is essential for achieving this goal. Accordingly, the allocations resulting from the methodology used by Entity L are reasonable.

Illustration 13

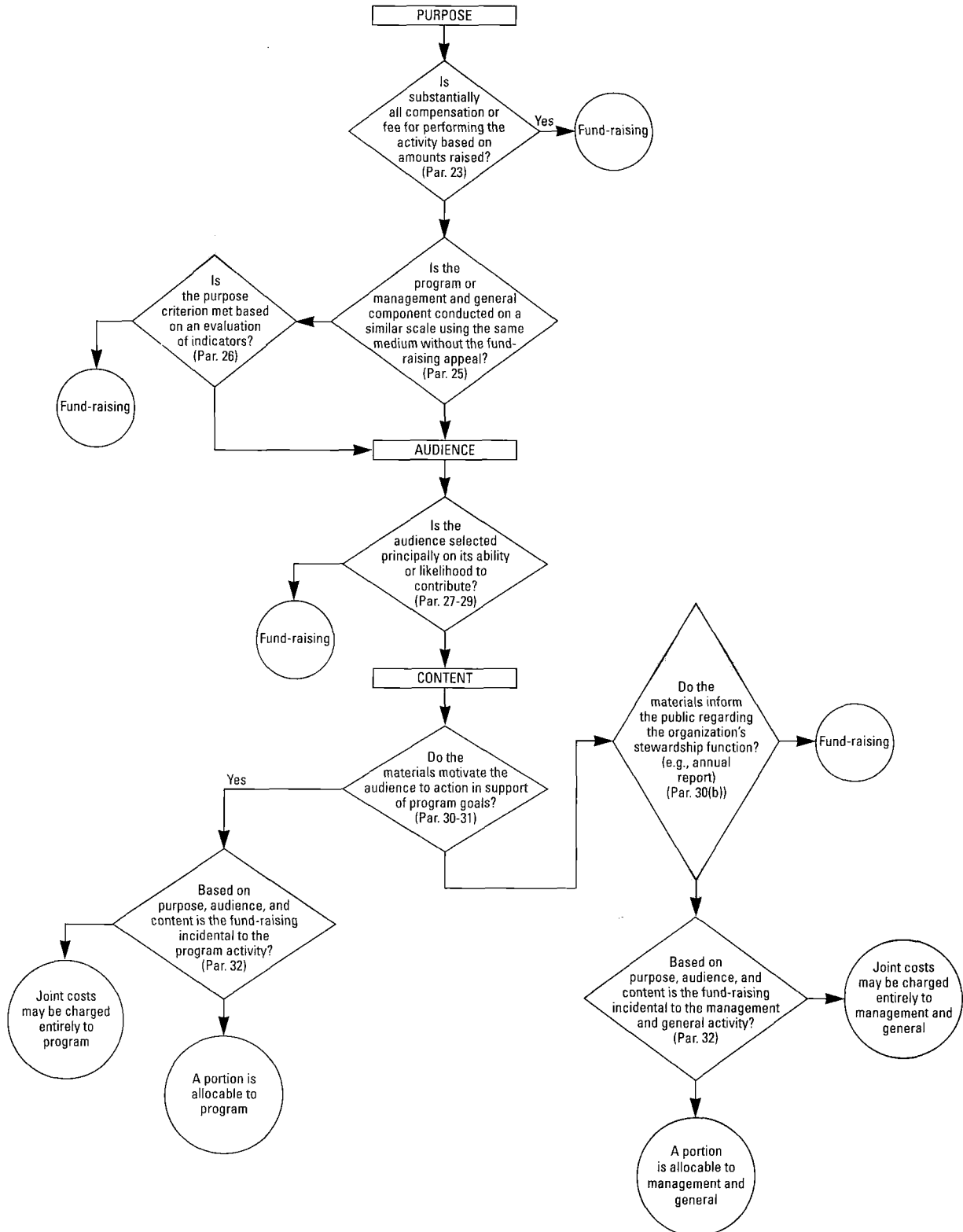
Facts

A.53 Entity M is a community hospital. Entity M's mission includes a requirement to educate the public about health maintenance and disease prevention. Twice a year, brochures are sent to all residents in the hospital's service area. These brochures discuss the importance of exercise and good nutrition and how to detect certain diseases, and encourage recipients to exercise, eat right, and practice self-detection. Once each year, Entity M includes an envelope with a request for contributions with the brochure.

Conclusion

A.54 The purpose, audience, and content criteria are met and the joint costs should be allocated.

ACCOUNTING FOR JOINT ACTIVITIES *



* Note: This flow chart summarizes certain guidance in this SOP and is not intended as a substitute for the SOP.

CONTRASTING THE GUIDANCE IN SOP 87-2 WITH THE GUIDANCE IN THIS SOP

This SOP

SOP 87-2

Applies to all entities, including state and local governments, that report expenses or expenditures by function.

Applies to entities that follow the AICPA Industry Audit Guide *Audits of Voluntary Health and Welfare Organizations* or SOP 78-10.

Covers *all* costs of joint activities, with costs otherwise clearly identifiable with program or management and general charged to fund-raising unless a bona fide program or management and general activity is conducted.

Covers only joint costs of joint activities.

Criteria of purpose, audience, and content must all be met in order to charge costs of the activity to program or management and general.

Unclear concerning whether all criteria must be met in order to charge costs of the activity to program or management and general.

Neither prescribes nor prohibits any allocation methods. Includes a discussion to help users determine whether an allocation is reasonable, and some illustrations are provided.

Neither prescribes nor prohibits any allocations methods. No illustrations.

Requires note disclosures about the types of materials and activities for which joint costs have been incurred, allocation methods, amounts allocated during the period, and portions allocated to each functional expense or expenditure category.

Requires less extensive note disclosures: total amount allocated during the period and amounts allocated to each functional expense category.