

BPM

A Comprehensive Guide to Alternative Investments

August 13, 2020

Presenters



Daniel Figueredo, Partner, Assurance, Nonprofit Industry Group Co-Leader, BPM LLP

Daniel co-leads BPM's Nonprofit industry group and he is also a leader in BPM's Financial Services group. His career started at BPM, and for nearly 20 years he has helped the Firm and his clients grow and succeed. Daniel's nonprofit experience includes working extensively with fair value and alternative investments. He serves investors in alternative investments (e.g. foundations, arts and culture, educational institutions, trade associations, social enterprises, etc.), as well as alternative investment funds directly (e.g. hedge funds, venture capital funds, private equity funds, fund of funds, crypto funds, etc.).

Daniel is an organizer of BPM's long-standing Nonprofit Education Series for Nonprofits and he is a regular presenter for industry groups and conferences. His experience in Nonprofit includes Arts and Culture, Environmental, Higher Education, Political and Advocacy Organizations, Private and Community Foundations, Private Schools, Religious Organizations, Social Enterprises, and Trade Associations.

His financial service experience includes FinTech, Hedge Funds, Impact Investing, Investment Banking, Marketplace Lending, Broker-Dealers, and Venture Capital. Daniel is a graduate of the University of San Francisco with a Bachelor's degree in Accounting and Finance. Daniel's community involvement includes serving as Audit Committee Chair for CalCPA, AICPA Governmental and Not-for-Profit Conference Committee, CalCPA Not-for-Profit Conference Co-Chair, Treasurer for The Guardsmen, Treasurer and Conference Committee for the Northern California Planned Giving Council, Board of Directors for Smith-Kettlewell Eye Research Institute, Treasurer for the Online Lending Policy Institute, University of San Francisco – Accounting Advisory Board, Finance Committee for SF Performances, and Leadership San Francisco Class of 2016.

Presenters



Elena Serebriakova, CPA, Director, Tax, BPM LLP

Elena has over 12 years in public accounting, with a focus on providing tax services to nonprofit and for-profit organizations. Her nonprofit experience includes community foundations, professional membership associations, education organizations, performing arts organizations, social welfare organizations and private foundations.



Su Rim, Manager, Assurance, BPM LLP

Su has more than 8 years of experience in public accounting. She serves a wide variety of nonprofit clients, primarily private foundations and environmental organizations. Her experience also includes federal compliance audits. Su is active in BPM's Nonprofit Industry Group, and she assists in developing and conducting internal nonprofit training sessions.

Presenters



Melodie Olson, CPA, Senior Manager, Assurance, BPM

Melodie has more than 10 years of professional public accounting experience, and she is a Senior Manager on BPM's Assurance and Business Enterprise Service Team (BEST). Her audit experience includes working with companies in a variety of industries – including education nonprofits, private foundations, religious organizations, professional service organizations, real estate firms and consumer products companies.

Melodie heads up BPM's Professional Services Industry Group, which provides services to clients who serve other companies. Melodie is also active in BPM's Nonprofit Industry Group, and she assists in developing and conducting nonprofit training sessions for staff.

Agenda

- I. Introduction to Alternative Investments
- II. Terminology and Fund Structures
- III. Tax Considerations
- IV. Operational Considerations
- V. Accounting and Disclosure

Disclaimer – Not Investment Advice

- We are not professional investment advisors and this content is for informational purposes only.
- You should not take this information as investment, financial, legal, tax, or other advice.
- We do not solicit, recommend, endorse, or offer to buy or sell any securities or other financial instruments.



Introduction to Alternative Investments

Pros and Cons

Cons and Risks

- ✗ More fees and costs
- ✗ Less liquid and can be difficult to exit
- ✗ Lack of transparency
- ✗ Some investing strategies are complex and volatile
- ✗ Possible unrelated business income tax
- ✗ Possible foreign filings and reporting
- ✗ More staff and board resources needed to evaluate, track, monitor, and report on alternatives
- ✗ Private foundations – special excise taxes

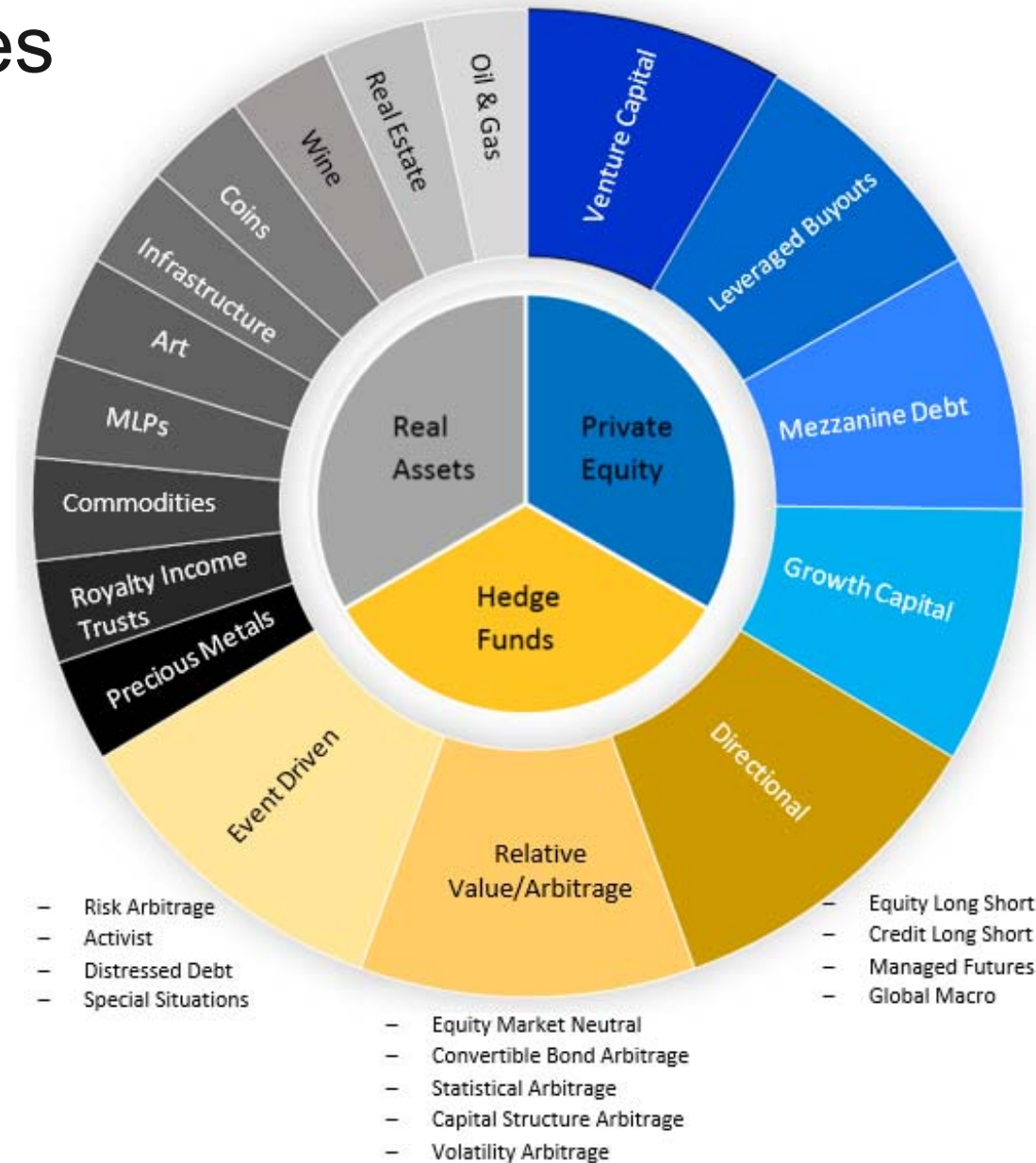
Pros and Upside

- ✓ Hedge against risk with non-correlated asset classes
- ✓ Diversification through access to more sophisticated investments and strategies
- ✓ Potentially higher returns
- ✓ Premiums often demanded for giving up short-term liquidity
- ✓ Expert advice
- ✓ Longer time horizon / less emphasis on current earnings
- ✓ Early access to hot companies (IPOs and unicorns)

Summary

- Alternative investments are most associated with private investment partnerships, but can be structured in a variety of ways
- Alternatives are generally for investing strategies beyond trading long on stocks and bonds
- There is increasing competition for new investment offerings
 - Emerging endowment-like alternatives mutual funds and ETFs
 - Bitcoin and other digital assets
 - Decentralized finance (DeFi)
 - Direct investments in private companies
 - Reg CF (Equity Crowdfunding)
 - Reg A+ (IPO Lite)

Strategies



Topics Not Covered In Depth With Presentation

- Direct investments (i.e. program-related investments, private company investments, etc.)
- Basics of the fair value measurements framework (ASC 820)
 - Fair value approaches (market, income, and cost)
- Base terminology
 - Net asset value (NAV)
 - Partnership agreement (LP's)
 - Operating agreement (LLC's)
- Foreign tax filings
 - What is entailed in each foreign filing

Terminology and Fund Structures

Terminology

Terminology



Agreement outlining the terms that will govern the relationship between investors and the manager of an investment fund

Limited Partnership Agreement (for LPs)
Operating Agreement (for LLCs)
Articles of Association (for Offshore Funds)



Offering documents for potential investors outlining the fund's business plan and key provisions

Private Placement Memorandum (for Private Funds)
Offering Memorandum (for Private Funds)
Prospectus (for Public Funds)
Term Sheet



Investors application to join an investment partnership

Subscription Agreement

Terminology



Entity that makes all the investment decisions

General Partner (for LPs)
Managing Member (for LLCs)
Investment Manager (for Offshore Funds)



Service provider handling the accounting, investor reporting, and other key compliance needs of an investment fund

Fund Administrator



Financial institution that safeguards assets managed by an investment advisor

Custodian

Terminology



An investment fund that raises a fixed amount of capital, to be invested mostly in illiquid investments over a pre-determined number of years (i.e. 7-10 years), that an investor cannot take back out of the fund, and where investors ultimately receive distributions from liquidated investments

Closed-End Fund



An investment fund allowing investors to buy and sell their capital interests at defined intervals, often invested in more liquid investments strategies, and generally without a pre-determined life or with a much longer life than closed-end funds

Open-End Fund



A legal trust administered by a bank or trust company that combines assets of multiple investors, and is not regulated by the SEC, but instead by regulations of the OCC

Collective Investment Fund
Common Collective Trust
Common Funds
Commingled Trusts
Collective Trusts

Terminology



Making an investment of capital into an investment fund

Capital Contribution



The promise by an investor to make capital contributions over a specified period of time

Capital Commitment (for Closed-End Funds)



Legal right for the fund manager to demand money promised by an investor

Capital Call (for Closed-End Funds)

Terminology



A return of investor capital balances in an investment fund

Capital Withdrawal or Redemption (Open-End Funds)

Capital Distribution (Closed-End Funds)



A segregated account for an illiquid investment of an open-end fund, which investors cannot redeem and just wait for capital distributions

Side Pocket

Special Investment

Special Situation Account



A pre-defined % of a capital withdrawal/redemption balance to be distributed after a period of time after year-end or completion of the fund audit

Holdback

Terminology



A pre-defined period for which an investor's capital cannot be withdrawn or redeemed

Lockup



A fund manager's right to limit or halt capital withdrawals/redemptions, typically imposed to prevent a run on the fund

Gate



An annual % of the funds committed capital, contributed capital, or NAV used to pay overhead costs of the fund manager

Management Fee

Terminology



An allocation by the fund of a portion of its profits to the fund manager as a form of compensation, regardless of whether the fund manager contributes initial funds

Incentive Allocation (Open-End Funds)
Carried Interest (Closed-End Funds)



The right for limited partners to block or participate in the operating decisions of the fund

Participating Rights

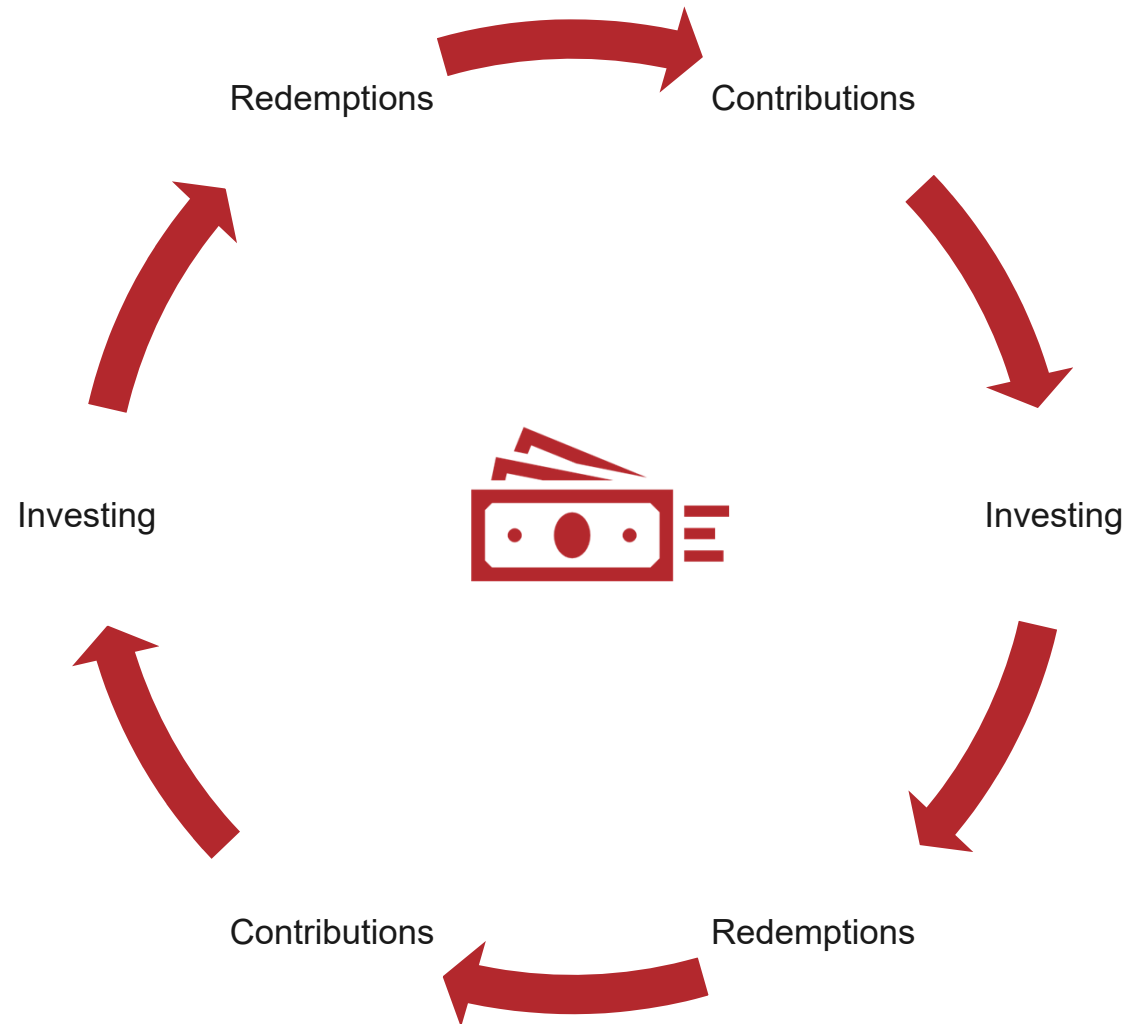


The ability of limited partners to remove the fund manager without cause or to liquidate or dissolve the fund without cause

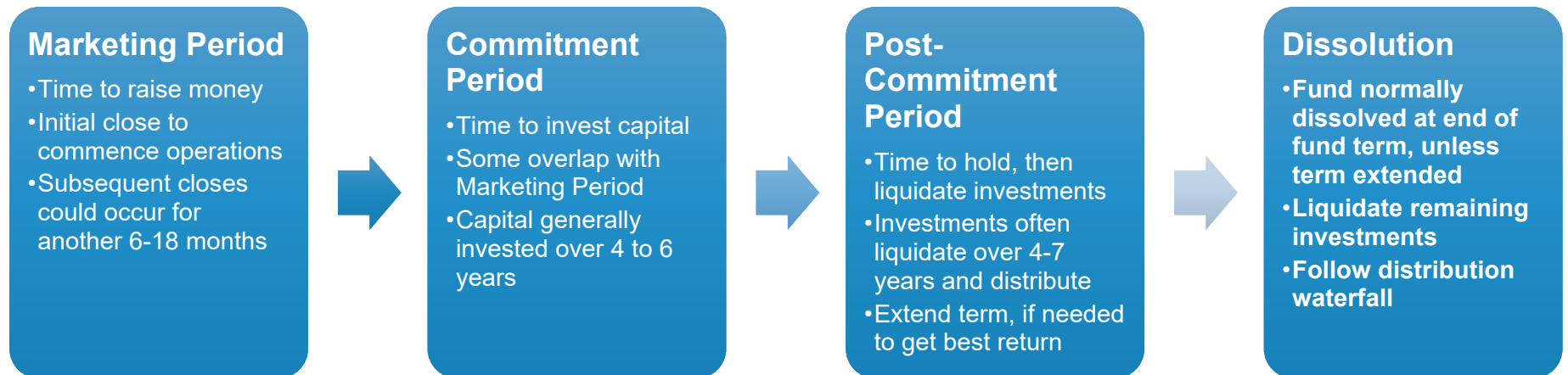
Kick-Out Rights

Open-End and Closed- End Funds

Open-End Funds



Closed-End Funds



Open-End vs. Closed-End Funds

Investment Fund Characteristics	Open-End	Closed-End
Raising Capital	Can continuously raise capital	Finite period for admissions
Fund Term	Potentially unlimited life	Limited life
Ability to Liquidate	Redemptions allowed with some regular frequency. However, illiquid side pocket investments could occur.	Illiquid and only receive distributions when portfolio company investments are liquidated
Investment Time Horizon	Short term and long term	Generally long term
Management Fees	Based on net asset value (NAV) (market value)	Based on committed or invested capital
Incentive Fees	Performance fees based on NAV	Carried interest based on realized gains

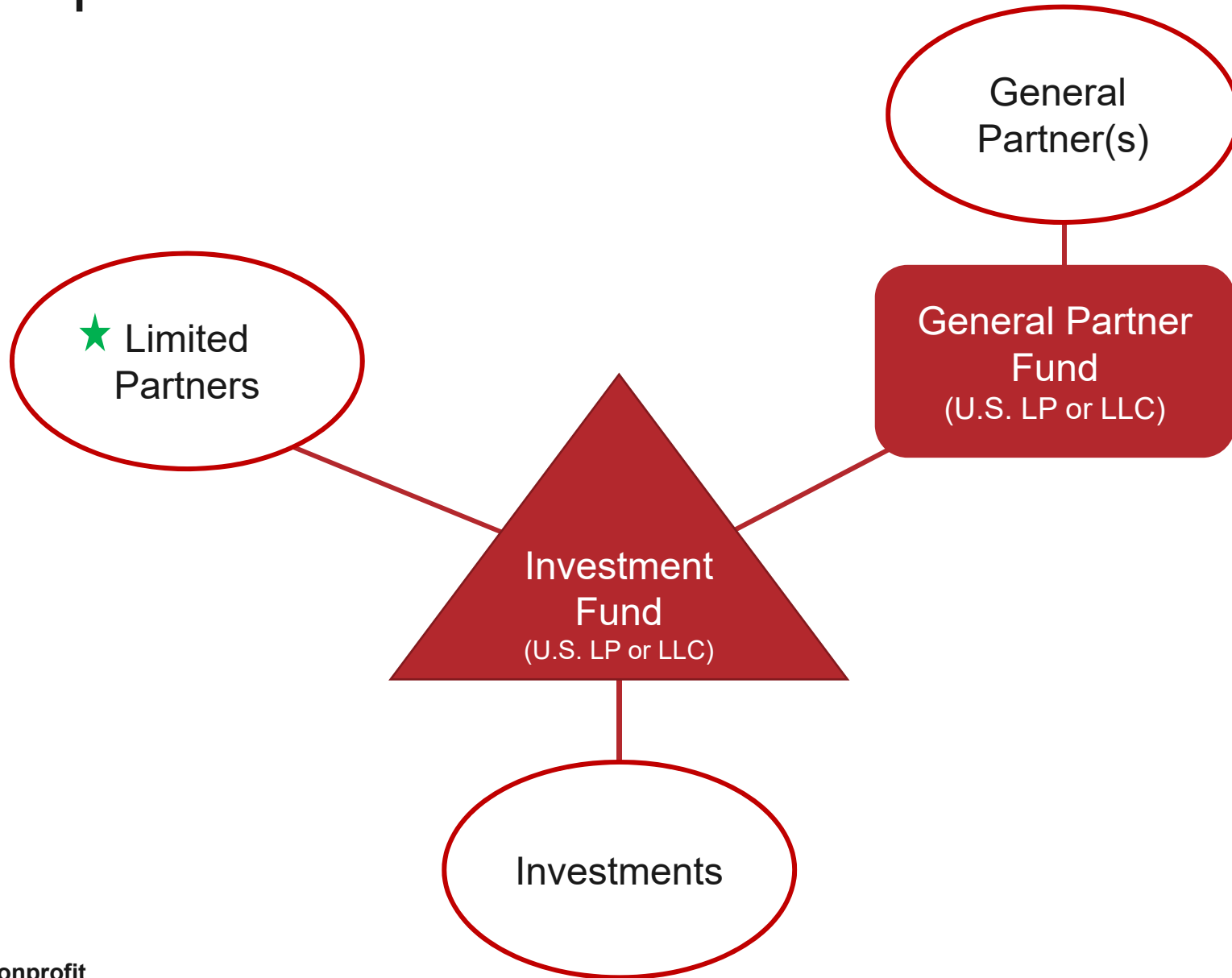


Fund Structures

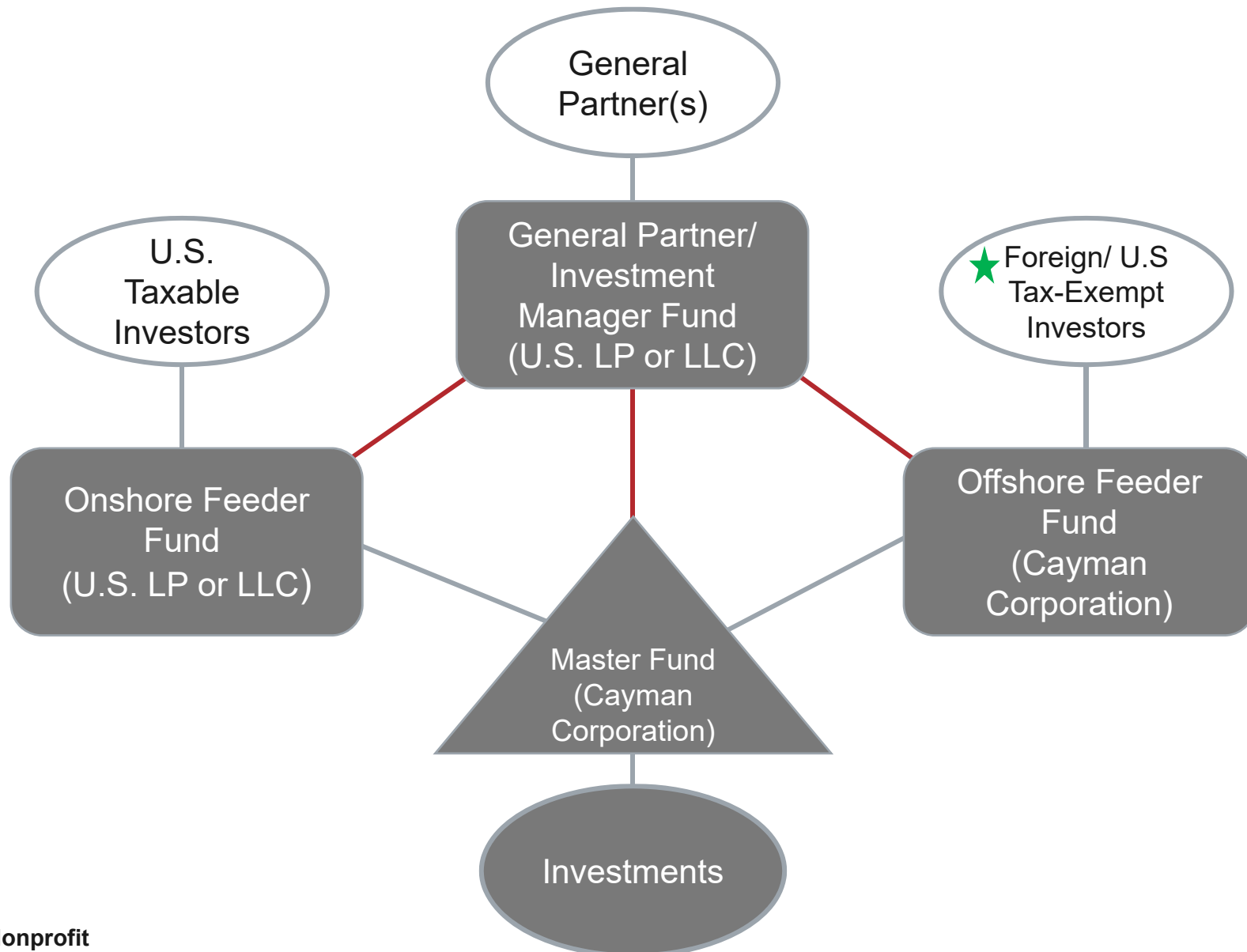
Overview

- Fund structures can be very simple
 - i.e. straightforward VC fund
- Fund structures can also be very complex
 - i.e. certain hedge funds or fund of funds
- An offshore blocker corporation is often used to address potential UBI
 - Covered later in the tax section
- Understanding where your investment falls in the fund structure helps you identify issues with costs, timeliness of information, transparency, and more

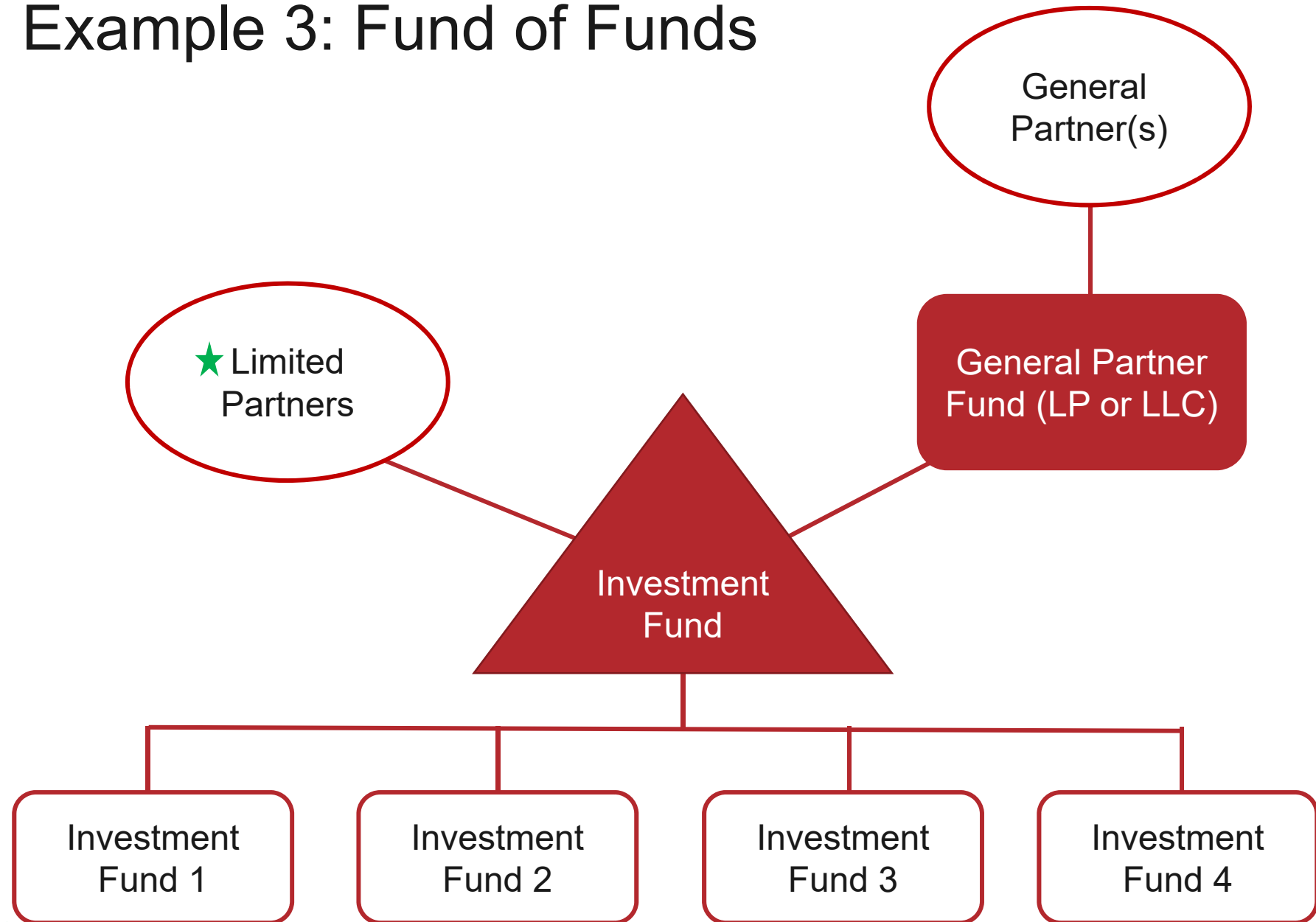
Example 1: Traditional U.S. Fund



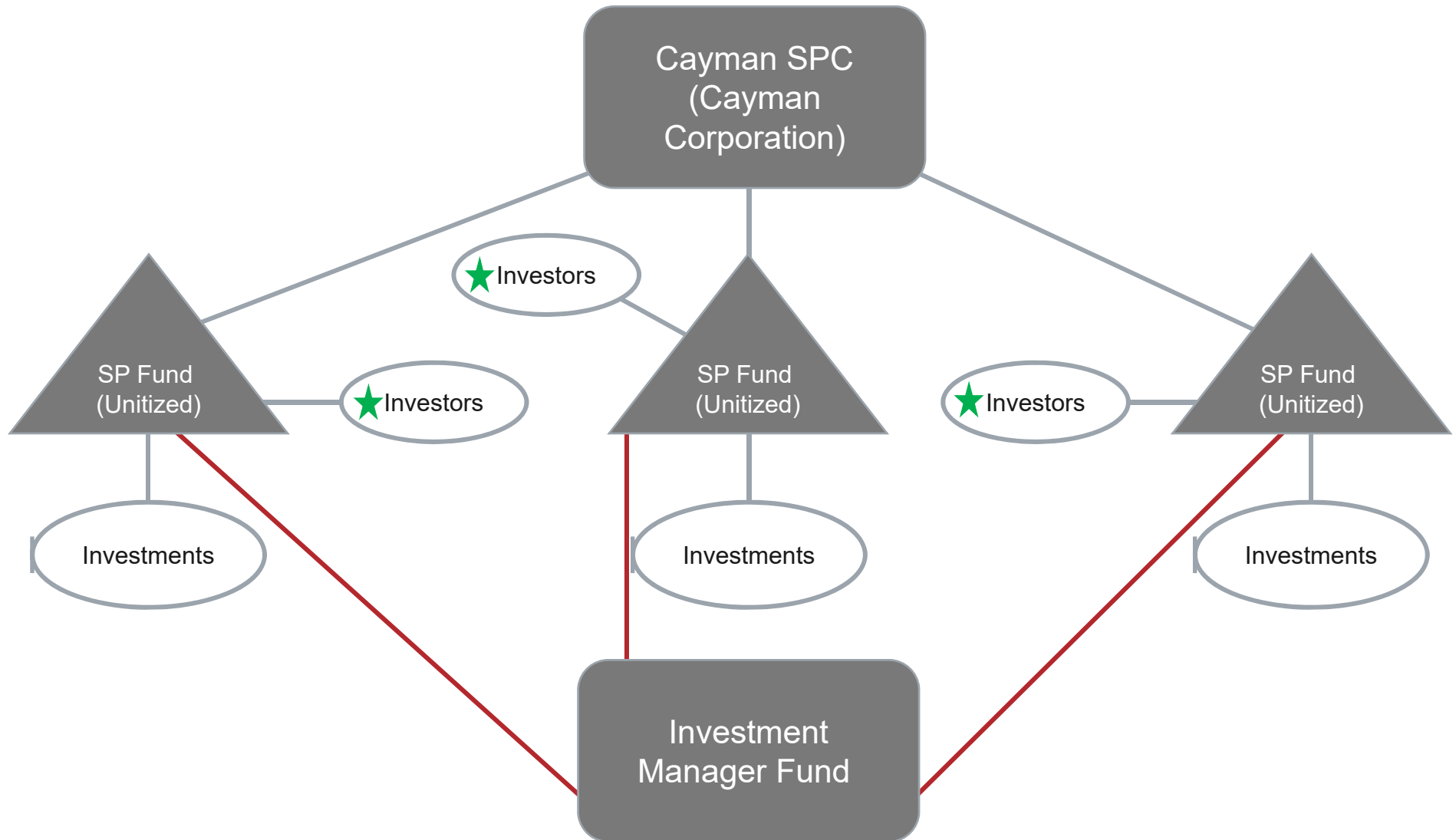
Example 2: Cayman Master-Feeder Fund



Example 3: Fund of Funds



Example 4: Cayman Segregated Portfolio Co. (SPC)



Alternative Investment Fund Agreements

Length of Term

Key Terms	What to Look Out For or Consider?	What is Typical?
<p>Fund Term</p>	<ul style="list-style-type: none"> • Closed-end funds <ul style="list-style-type: none"> • The fund's life and how long capital will be locked up • Over how many years does the fund manager expect to deploy capital and make capital calls? • Expected process for extending the fund's life for illiquid investments taking more time to distribute • Open-end funds <ul style="list-style-type: none"> • Typically deploy capital quickly • The planned use of any side pockets/special investments for less liquid investments 	<ul style="list-style-type: none"> • Closed-end funds <ul style="list-style-type: none"> • 10 years (general range is 7-15 years) • Open-end funds <ul style="list-style-type: none"> • Generally no set term

Capital Contributions

Key Terms	What to Look Out For or Consider?	What is Typical?
Capital Contributions	<ul style="list-style-type: none"> • Closed-end funds <ul style="list-style-type: none"> • Expected time period for capital to be called • Open-end funds <ul style="list-style-type: none"> • Minimum initial contributions and subsequent contributions • How often are capital 	<ul style="list-style-type: none"> • Closed-end funds <ul style="list-style-type: none"> • Generally 4-6 years • Open-end funds <ul style="list-style-type: none"> • Varies depending on the target capital raise
Capital Allocations	<ul style="list-style-type: none"> • What type of expense are covered by the fund vs. fund manager? • How are net income/loss allocated to partners and the frequency? • For closed-end funds, are allocations based on committed or contributed capital? 	

Investment Manager Compensation

Key Terms	What Should I Look Out For or Consider?	What is Typical?
Management Fees	<ul style="list-style-type: none"> • Is it based on contributed capital, committed capital, or NAV? • If a fund of funds, what management fees are already passed through from sub-funds? • Look out for the way the management fee is calculated regarding any side pockets/special investments 	2% (general range is .1%-4%)
Incentive Allocation/ Carried Interest	<ul style="list-style-type: none"> • Any hurdle rates of return to be achieved before the fund manager is eligible for their allocation • The frequency a fund manager gets to take a distribution for their allocation • Whether or not the fund manager has loss carryforwards on any subsequent allocations for any subsequent losses • Determine how the allocation works regarding any side pockets/special investments 	20% (general range is 10%-50%)

Distributions and Withdrawals

Key Terms	What to Look Out For or Consider?	What is Typical?
Rights of Fund Manager	<ul style="list-style-type: none"> • What rights are granted to the fund manager to use discretion with requests for special distributions or withdrawal? • What is the process for approving? 	<ul style="list-style-type: none"> • Fund managers often have free discretion to make special approvals beyond the terms of the fund
Tax Distributions	<ul style="list-style-type: none"> • Often specific provisions for needing to make distributions to investors when realized events trigger passthrough taxable income to investors 	<ul style="list-style-type: none"> • Provisions generally allow such that investors get enough distributions to pay tax on income
Lockup Periods <i>(Open-End Funds)</i>	<ul style="list-style-type: none"> • Is it after every contribution to the fund or just your initial contribution? • If the fund has different shares/series classes, which apply to you? 	<ul style="list-style-type: none"> • Varies on fund strategy (general range is 0-3 years)
Notice Periods <i>(Open-End Funds)</i>	<ul style="list-style-type: none"> • How many days/months advance notice needed • Can you elect a standing annual distribution? 	<ul style="list-style-type: none"> • Varies on fund strategy (general range is 10 days-6 months) • Certain funds allow a draw for endowments up to 7%
Gates <i>(Open-End Funds)</i>	<ul style="list-style-type: none"> • Can the fund manager cease withdrawals all together? • Are there limits on annual withdrawals 	<ul style="list-style-type: none"> • Often allowed • Only allow every M, Q, or Y • Could cap annual % allowed
Holdbacks <i>(Open-End Funds)</i>	<ul style="list-style-type: none"> • What % of your funds will be held back and for how long? • Is it subject to completion of the audit or time-based? 	<ul style="list-style-type: none"> • 10% (general range is 5%-10%) • Generally based on audit completion

Tax Considerations

Summary of Key Issues

Corporation, Partnership, or Trust

Questions to ask:

- Is it a domestic or foreign investment?
- Is it a trust, partnership, or a corporation (for U.S. tax purposes)? Will the organization receive a K-1?
- If no K-1 is issued, is the organization required to pick up its share of fund's taxable income?
- How and when will the organization be notified of its share of income?

The Fund Is a Partnership

- When will the K-1 be issued?
- Is unrelated business income expected?
- Is it a fund of funds? How is the state reporting handled?
- Will the organization receive the information needed for estimated tax payments?
- Will the partnership withhold tax on organization's behalf?

The Fund Is a Domestic Partnership

- The organization received a K-1 – now what?
- For PFs K-1 income needs to be added to net investment income
- For most of other organizations – see box 20 code V and footnotes
- Box 20 code V – unrelated business income
- Footnotes – various disclosures (UBTI, Form 926, Form 8865, Form 8886, Form 8621)

Reading a K-1

K-1 Example

Schedule K-1
(Form 1065)
Department of the Treasury
Internal Revenue Service

2019

For calendar year 2019, or tax year

beginning 01 / 01 / 2019 ending 12 / 31 / 2019

Partner's Share of Income, Deductions, Credits, etc.
▶ See back of form and separate instructions.

Part I Information About the Partnership

A Partnership's employer identification number

B Partnership's name, address, city, state, and ZIP code
The best investment LLP
3409 California Street #100
San Francisco, CA

C IRS Center where partnership filed return ▶

D Check if this is a publicly traded partnership (PTP)

Part II Information About the Partner

E Partner's SSN or TIN (Do not use TIN of a disregarded entity. See inst.)

F Name, address, city, state, and ZIP code for partner entered in E. See instructions.
Support our Pets
6500 Main Street
Paso Robles, CA

G General partner or LLC member-manager Limited partner or other LLC member

H1 Domestic partner Foreign partner

H2 If the partner is a disregarded entity (DE), enter the partner's TIN _____ Name _____

I1 What type of entity is this partner? Tax-exempt organization

I2 If this partner is a retirement plan (IRA/SEP/Keogh/etc.), check here

J Partner's share of profit, loss, and capital (see instructions):

	Beginning	Ending
Profit	0 %	15 %
Loss	0 %	15 %
Capital	0 %	15 %

Check if decrease is due to sale or exchange of partnership interest

K Partner's share of liabilities:

	Beginning	Ending
Nonrecourse	\$ 0	\$ 250,000
Qualified nonrecourse financing	\$ 0	\$ 0
Recourse	\$ 0	\$ 550,000

Check this box if item K includes liability amounts from lower tier partnerships.

L Partner's Capital Account Analysis

Beginning capital account	\$ 0
Capital contributed during the year	\$ 10,000,000
Current year net income (loss)	\$ 125,000
Other increase (decrease) (attach explanation)	\$ 0
Withdrawals & distributions	\$ 500,000
Ending capital account	\$ 9,625,000

Final K-1 Amended K-1

OMB No. 1545-0123

Part III Partner's Share of Current Year Income, Deductions, Credits, and Other Items

1 Ordinary business income (loss)	25,000	15 Credits
2 Net rental real estate income (loss)	10,000	
3 Other net rental income (loss)		16 Foreign transactions
4a Guaranteed payments for services		
4b Guaranteed payments for capital		
4c Total guaranteed payments		
5 Interest income	45,000	
6a Ordinary dividends	55,000	
6b Qualified dividends		
6c Dividend equivalents		17 Alternative minimum tax (AMT) items
7 Royalties	2,000	
8 Net short-term capital gain (loss)	254,000	
9a Net long-term capital gain (loss)	-85,000	18 Tax-exempt income and nondeductible expenses
9b Collectibles (28%) gain (loss)		
9c Unrecaptured section 1250 gain		
10 Net section 1231 gain (loss)		
11 Other income (loss)	10,000	19 Distributions
F		500,000
12 Section 179 deduction		20 Other information
13 Other deductions	280,000	V
W		65,000
14 Self-employment earnings (loss)		
21 <input type="checkbox"/> More than one activity for at-risk purposes*		
22 <input type="checkbox"/> More than one activity for passive activity purposes*		

*See attached statement for additional information.

Reading the K-1

- Check the ownership % - important for UBTI, excess business holdings, foreign reporting
- Does the K-1 show ordinary income (box 1)? If yes, ask about UBTI
- Does K-1 show debt allocated to the partner (lines K)? If yes, ask about UBTI
- Debt – financed income can trigger UBTI
- Read the K-1 footnotes

Box 20V and Form 990T

- Unrelated business income needs to be reported on Form 990T
- Summarize all K-1s to determine UBTI from investments
- Consider ownership % - silos
- Certain types of investments can be grouped in one SILO
 - De minimis test – owners % is 2% or less for capital and profit interests
 - Control test – ownership % is no more than 20% of capital interest and does not control or has influence over partnership
- There is transition rule for partnership interests bought before August 21, 2018 which do not meet the two tests above

Why Footnotes Are Important

- The organization might have to file various forms – disclosure only
- No tax associated with disclosure forms
- Penalties usually start from \$10,000 per form
- Footnotes have information for federal UBI, state UBI, taxes withheld
- UBTI, silos, and footnotes – tax-exempt organizations might need additional information to prepare 990T correctly

Foreign Filing Requirements

Form 926 – Return by a U.S. Transferor of Property to a Foreign Corporation

- Not all-inclusive information, usually what we see on K-1s
- Due with the organization's return
- Usually required when a U.S. person transfers more than \$100,000 during the twelve months period ending on the date of the transfer. The transfer amount is per foreign corporation.
- Penalty for non-filing 10% of the FMV of the property at the time of transfer. It is limited to \$100,000 unless the failure to comply was intentional.

Form 8865 – Return of U.S. Persons with Respect to Certain Foreign Partnerships

- Due with the organization's return
- The organization owned directly or constructively at least 10% after the contribution or contributed more than \$100,000 (FMV of the property) in 12 months period ending on the date of the transfer
- If the domestic partnership files Form 8865 (correctly), the partners will not be required to report the transfer
- Penalties \$10,000 - \$50,000 per form

The Fund is a Foreign Partnership

- Will the organization receive the K-1?
- If yes, the process is similar to domestic partnership except that Form 8865 might be required without footnotes disclosure
- No K-1 – the organization needs to request the information from foreign partnership
- Financial information, transfers to other foreign partnerships, corporations, any additional disclosures
- Allow enough time for information request

The Fund is a Foreign Corporation – Form 5471

- Due with the organization's return
- Usually 10% ownership requirement
- If directly investing in a foreign corporation – talk to your tax advisor!
- The investor can accidentally become 50% + owner. 50%+ is applied to ANY time during the year
- If the organization is one of the first investors, might be a 50%+ owner for one day
- Penalties - \$10,000 - \$50,000 per form

Footnote Example – Form 926

- U.S. persons, domestic corporations or domestic estates or trusts must file form 926, return by a U.S. transferor of property to a foreign corporation, to report any exchanges or transfers of property described in section 6038b(a)(1)(a) to a foreign corporation. The amounts shown below represent the total amount at the fund level. To calculate your allocable share, multiply the amounts below by your capital percentage

Form 926 Part I - US Transferor information

XXX Partnership, LLP

EIN 99-9999999

Form 926 Part II and III

- 1) Name, address – YYY LTD, 349 Main street, Dublin, Ireland
- 2) Date and amount transferred – 5/20/2020, \$1,400,400, cash
- 3) % of ownership before and after the transfer

Foreign Filings and Public Disclosure

- Most foreign filings can be filed with 990, 990-T, or 990-PF
- Notice 2008-49 states that foreign filings attached to 990-T are not open to public disclosure
- Form 5713, 3520, 3520-A must be filed with 990-T. Check instructions to see if a separate copy needs to be mail separately as well
- There is no explicit guidance whether filings attached to 990 or 990-PF are open to public disclosure

State Filing Considerations

State Considerations - UBTI

- Fund has activity in multiple states or underlying investments have activities in multiple states
- State income v. state unrelated business income
- Withholdings usually are based on state income
- Some states do not tax UBTI. If tax is withheld it is very hard to get it back
- Partnerships should provide forms which show withholdings (592-B for California)
- Some states do not have UBI forms, organizations need to file corporate or trust state returns

State UBTI Footnote Disclosure

- K-1s might show detail or summary information for state source income
- Usually K-1s show summary information for state UBTI

State	Source income (Loss)	Taxes paid on your behalf	UBTI
Alabama	(3,500)	-	2,200
California	15,000	1,200	3,000
North Carolina	4,500	300	(1,100)

Private Foundation Considerations

K-1s and Private Foundations

- Different reporting for Financial statements and Net Investment income (NII) on 990PF
- Different basis for Financial statement and NII
- When the investment is sold, the tax basis must be used for NII
- Use K-1 for all years to calculate basis (contributions, income, expenses, distributions)
- 20% ownership might trigger excess business holdings

Operational Considerations

Organizational Needs and Policies



Liquidity Needs



Investment Policies

Asset allocation

Endowment spending

Screening criteria (ESG, socially responsible, impact investing, faith-based, etc.)

Fiduciary Considerations



Investment Advisor Selection

Outsourced Chief Investment Officer (OCIO)

Investment Advisor
Multi-Strategy Funds



Governance

Board and Committee Oversight
Uniform Prudent Management of Institutional Funds Act (UPMIFA)

Timing Issues

Tax Estimates

- Determine what is the estimated timing for receiving final K-1's, estimated K-1's, or other estimates
- When is it appropriate to just use the prior year K-1's to timely file estimated tax payments?

Audit Completion

- Understand the expected timing for completion of audited financials from your alternative investments
- Determine whether to rely on preliminary information for your audit vs. final audits, K-1's, etc.
- Possibly separate audit fieldwork for alternative investments later in the year
- Evaluate significant variances of final information to preliminary estimates

Tax Returns









- How close to the 9/15 deadline (for calendar year funds) do you expect final K-1's?
- Fund of funds tend to report later, since they are gathering information from multiple funds

Due Diligence and Monitoring

Initial Due Diligence



Ongoing Monitoring

	Conduct regular check-ins with investment firm
	Attend annual meeting, site visits, or routine questionnaires
	Search for any relevant press
	Review fund communications
	Review SOC audit reports (custodian and fund admin)
	Key changes (management, valuation policies, legal, audit, custodian, fund admin)
	Update understanding of fund's operational due diligence performed on investments
	Review latest Form ADV
	Inquire about SEC examinations

Financial Reporting and Valuation

- Board and investment committee ongoing review of performance
- Track capital commitments
- Track tax estimates (K-1's or other tax information)
- Review most recent fund audit
- Monitor ownership level
- Compare investment balances (K-1, statements, audit)
- Rollforward activity if different year-end than the fund

Audited Financials Review – What to Look For

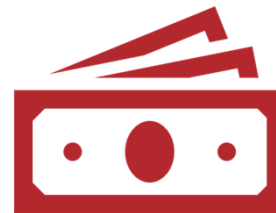


Audit Opinion

Type of opinion (unmodified, qualified, emphasis of matter, etc.)

Audit firm and reputation

Basis of accounting (U.S. GAAP, IFRS, other countries)



Statement of Financial Condition (i.e. Balance Sheet)

Debt – possible indicator of debt-financed UBI

Partners' Capital – agrees to totals in fund statements and evaluate your % ownership

Audited Financials Review – What to Look For



Schedule of Investments

Types, nature, and transparency of investments

Geographies – possible foreign filings needed

Costs and Fair Value - significant unrealized gains/losses

Investments in Funds - What are they invested in? What is the additional layer of fees and costs?



Statement of Changes in Partners' Capital

General Partner – reasonableness of incentive allocation (e.g. 20%)

Capital Contributions – Is it in line with your % committed? Is your % ownership going up or down?

Distributions or Withdrawals – How much activity? Are they allowed per the partnership agreement? How much is the GP getting vs. LPs?

Audited Financials Review – What to Look For in the Footnotes

Organization Note

- Description of the fund, manager, strategy, term, location, and more

Valuation Policy

- Describes policies and methods used to value investments and recognize gains/losses

Fair Value Disclosures

- Level 1, 2, & 3
- NAV practical expedient
- Breakdown of investments
- Level 3 valuation inputs

Capital Share Transactions

- Applicable to offshore corporations
- Shows activities and NAVs of different classes or series of shares

Capital Contributions and Withdrawals

- Details on contributions and withdrawals policies and distribution waterfall
- Special actions taken during the period
- % of capital called

Incentive Allocation/ Carried Interest

- Describes allocation methodology
- Describes side pockets/ special investments

Related Party Transactions

- Describes relationship with fund manager
- Describes any other significant relationships

Financial Highlights

- Shows rates of return
- Expense ratios
- % for incentive allocations/ carried interest

Accounting and Disclosure Framework

Nonprofit Investments Guidance

Nonprofit Investments Guidance

- **FASB ASC 958, *Not-for-Profit Entities***

- 958-320 *Investments- Debt Securities*

- 958-321 *Investments- Equity Securities*

- 958-323 *Investments- Equity Method*

- 958-325 *Investments- Other*

- **ASC 958-325**, Not-for-profit entities that are not colleges, universities, voluntary health and welfare entities, or health care entities (see chapter 954 *Health Care Entities*) should report other investments using either fair value or the lower of cost or fair value.

Nonprofit Investments Guidance

- **FASB ASC 820, *Fair Value Measurement***

Topic 820 allows reporting entities, as a practical expedient, to measure certain investments at their net asset value (NAV) per share (or equivalent).

If the reporting entity elects to use the practical expedient for the fair value measurement of certain investments, then the reporting entity is no longer required to categorize these investments within the fair value hierarchy. Instead, the reporting entity discloses its use of the NAV per share practical expedient for fair value measurement and that the investments aren't included in the fair value hierarchy.

- **Accounting Standards Update 2018-13**, *effective for all entities with fiscal years beginning after December 15, 2019. Primary focus is to improve the effectiveness of disclosures in the notes to financial statements.*

Fair Value – NAV
Practical Expedient

Net Asset Value (NAV) Practical Expedient

- NAV per share is the amount of net assets attributable to each share of capital stock (or its equivalent, e.g. member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed)

- In order to use NAV, must meet both of the following criteria as of the reporting entity's measurement date:
 - The investment does not have a readily determinable fair value
 - The investment is in an investment company within the scope of Topic 964 or is an investment in a real estate fund for which it is industry practice to measure investment assets at fair value on a recurring basis and to issue financial statements that are consistent with the measurement principles in Topic 946

Exception: A reporting entity is not permitted to estimate the fair value of an investment using the NAV per share of the investment as a practical expedient, if it's probable that the reporting entity will sell the investment for an amount difference from the NAV per share at measurement date

What is an Investment Company?

Fundamental Characteristics (must meet both)

Obtains funds from investors and provides investment management services, and

Commits to investors that their business purpose and only substantive activities are investing funds solely for returns from capital appreciation, investment income, or both.

Typical Characteristics

Multiple investments

Multiple investors

Investment by unrelated parties

Ownership in the form of equity or partnership interests

Investments managed on a fair-value basis

Financial Statement Disclosures

Financial Statement Disclosures

Assets Measured at Fair Value

- The valuation techniques and inputs
- The valuation processes used
- Sufficient information must be provided to permit reconciliation of the fair value of assets categorized within the fair value hierarchy to the amounts presented in the statement of financial position.

(\$ in millions)

Description	Fair Value Measurements at the End of the Reporting Period Using				Total Gains (Losses)
	12/31/09	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
Recurring fair value measurements					
Trading securities ^(a)					
Equity securities—real estate industry	\$ 93	\$ 70	\$ 23		
Equity securities—oil and gas industry	45	45			
Equity securities—other	15	15			
Total trading securities	\$ 153	\$ 130	\$ 23		
Available-for-sale debt securities					
Residential mortgage-backed securities	\$ 149		\$ 24	\$ 125	
Commercial mortgage-backed securities	50			50	
Collateralized debt obligations	35			35	
U.S. Treasury securities	85	\$ 85			
Corporate bonds	93	9	84		
Total available-for-sale debt securities	\$ 412	\$ 94	\$ 108	\$ 210	
Available-for-sale equity securities ^(a)					
Financial services industry	\$ 150	\$ 150			
Healthcare industry	110	110			
Other	15	15			
Total available-for-sale equity securities	\$ 275	\$ 275			
Total available-for-sale securities	\$ 687	\$ 369	\$ 108	\$ 210	
Hedge fund investments					
Equity long/short	\$ 55		\$ 55		
Global opportunities	35		35		
High-yield debt securities	90			\$ 90	
Hedge fund investments measured at net asset value ^(b)	30				
Total hedge fund investments	\$ 210		\$ 90	\$ 90	
Other investments					
Private equity fund investments ^(b)	\$ 25			\$ 25	
Direct venture capital: healthcare ^(a)	53			53	
Direct venture capital: energy ^(a)	32			32	
Other investments measured at net asset value ^(b)	45				
Total other investments	\$ 155			\$ 110	
Derivatives					
Interest rate contracts	\$ 57		\$ 57		
Foreign exchange contracts	43		43		
Credit contracts	38			\$ 38	
Commodity futures contracts	78	\$ 78			
Commodity forward contracts	20		20		
Total derivatives	\$ 236	\$ 78	\$ 120	\$ 38	
Total recurring fair value measurements	\$ 1,441	\$ 577	\$ 341	\$ 448	
Nonrecurring fair value measurements					
Long-lived assets held and used ^(c)	\$ 75		\$ 75		\$ (25)
Goodwill ^(a)	30			\$ 30	(35)
Long-lived assets held for sale ^(a)	26		26		(15)
Total nonrecurring fair value measurements	\$ 131		\$ 101	\$ 30	\$ (75)

Financial Statement Disclosures

Nature, Characteristic and Risks of the Investments

- Election of NAV practical expedient
- The FVM of the investments in the class at reporting date and description of the significant investment strategies
- Investment strategies
- For investments that cannot be redeemed, estimate of period over which the underlying assets are expected to be liquidated [*Changes in ASU 2018-13*]
- The circumstances in which an otherwise redeemable investment in the class might not be redeemable (e.g. investments subject to a lockup, gate, holdback)
- Unfunded commitments
- A general description of the terms and conditions of redemption (e.g. quarterly redemption with 60 days' notice)
- Any other significant restriction on the ability to sell investments

Financial Statement Disclosures

Example 8: Disclosure of Fair Value Measurements of Investments That Are Measured at Net Asset Value per Share (or Its Equivalent, Such as Member Units) As a Practical Expedient—Illustration Applicable Based on Guidance in ASU No. 2018-13

<u>Description</u>	<u>Fair Value</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency</u> <u>(If Currently Eligible)</u>	<u>Redemption</u> <u>Notice Period</u>
Equity long/short hedge funds ^(a)	\$550,000	\$-	Quarterly	30-60 days
Event driven hedge funds ^(b)	450,000	-	Quarterly, Annually	30-60 days
Global opportunities hedge funds ^(c)	350,000	-	Quarterly	30-45 days
Multiple-strategy hedge funds ^(d)	400,000	-	Quarterly	30-60 days
Real estate funds ^(e)	<u>470,000</u>	<u>200,000</u>		
Total	\$2,220,000	\$200,000		
	=====	=====		

^(a) This class includes investments in hedge funds that invest both long and short primarily in U.S. common stocks. Management of the hedge funds has the ability to shift investments from value to growth strategies, from small to large capitalization stocks, and from a net long position to a net short position. The fair values of the investments in this class have been estimated using the net asset value per share of the investments. Investments representing approximately 25 percent of the value of the investments in this class cannot be redeemed because the investments include restrictions that do not allow for redemption in the first 12 to 18 months after acquisition. The remaining restriction period for these investments ranged from three to seven months at December 31, 20X2.

Financial Statement Disclosures

Investment Fees

- Investment return presented net of related investment expenses on the statement of activities
 - External investment expenses
 - Direct internal investment expenses- direct conduct or supervision of activities that generate investment returns
 - Employee costs- Salaries, benefits, travel for personnel responsible for developing and executing investment strategy
 - Costs related to internal investment management- supervision, selection and monitoring of investment management firms

Accounting Best Practices

Accounting Best Practices

- Important to maintain all investment agreements, not just the subscription agreement
- Review the LPAs and Operating Agreements closely and confirm liquidity restrictions with the Investment Administrator
- Understand investments in multiple classes of shares with different redemption period and frequency
- Investments with liquidity restrictions are properly reflected on the liquidity footnote on the AFS

Questions?

Contact Information

Daniel Figueredo, CPA, CGMA – Partner, Assurance, Nonprofit Industry Group Co-Leader

600 California St., Suite 600, San Francisco, CA 94108

Tel: 415-288-6284

Email: dfigueredo@bpmcpa.com

Su Rim – Manager, Assurance

600 California St., Suite 600, San Francisco, CA 94108

Tel: 415-677-3311

Email: srim@bpmcpa.com

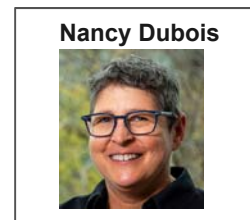
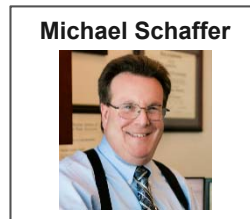
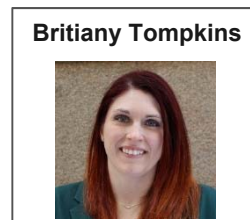
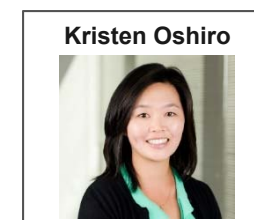
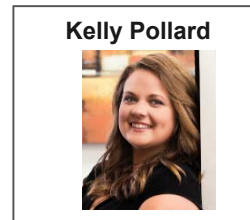
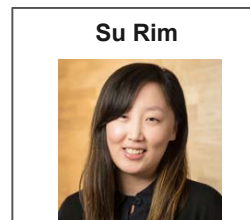
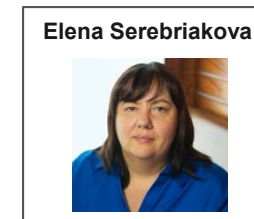
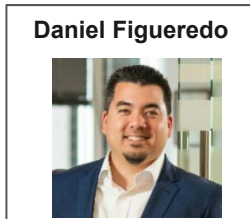
Elena Serebriakova, CPA – Director, Tax

2001 North Main Street, Ste. 360, Walnut Creek, CA 94596

Tel: 415-671-7616

Email: eserebriakova@bpmcpa.com

BPM's Nonprofit Partners, Directors and Managers



For more information on BPM's Nonprofit services, visit www.bpmcpa.com/nonprofits

BPM Offices

San Francisco

600 California Street, Suite 600
San Francisco, CA 94108
Phone: 415-421-5757
Fax: 415-288-6288

San Jose

10 Almaden Blvd., Suite 1000
San Jose, CA 95113
Phone: 408-961-6300
Fax: 408-961-6324

Stockton

3247 W. March Lane, Suite 200
Stockton, CA 95219
Phone: 209-943-2222
Fax: 209-943-2220

Eugene

184 East 11th Avenue, Suite 10
Eugene, OR 97402
Phone: 541-687-5222

Menlo Park

4200 Bohannon Drive, Suite 250
Menlo Park, CA 94025
Phone: 650-855-6800
Fax: 650-855-6899

Santa Rosa

110 Stony Point Road, Suite 210
Santa Rosa, CA 95401
Phone: 707-544-4078
Fax: 707-544-2190

Fairfield

5030 Business Center Drive, Suite 125
Fairfield, CA 94534
Phone: 408-333-9824

Seattle

12600SE 38th Street, Suite 245
Bellevue, WA 98015
Phone: 425-401-5061
Fax: 425-401-6306

Walnut Creek

2001 North Main Street, Suite 360
Walnut Creek, CA 94596
Phone: 925-296-1040
Fax: 925-296-1099

Saint Helena

1432A Main Street
St. Helena, CA 94574
Phone: 707-968-5207
Fax: 707-544-2190

Orange County- Santa Ana

2010 N. Tustin Avenue
Santa Ana, CA 92705
Phone: 714-558-3236
Fax: 714-558-2652

Orange County- Irvine

2875 Michelle Drive, Suite 200
Irvine, CA 92606

BPM Offices

Cayman Islands

19 Tarpon Island Drive
Sunrise Landing
Newlands, Grand Cayman
Cayman Islands KY1-1109
Phone: 345-769-6001
Fax: 345-945-0249

Bengaluru

Quest Offices, CWZ-1
10th Upper Floor, (10 UF)
Raheja Towers, M.G. Road
Bangalore- 560 001
Phone: +91 (725) 991-4444

Thank You!