NJCPA

Sent via email to director@fasb.org

August 19, 2015

Technical Director
File Reference No. 2015-230
FASB
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

Re: Proposed Exposure Draft of the Proposed Accounting Standards Update, Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954) - File Reference No. 2015-230

Dear Ms. Cosper:

The Nonprofit Interest Group of the New Jersey Society of Certified Public Accountants (NJCPA) is pleased to offer its comments on the above-referenced proposed Accounting Standards Update (Update). The NJCPA represents over 15,000 certified public accountants and prospective CPAs. The comments herein represent the views of some of the individuals of the Nonprofit Interest Group only and do not necessarily reflect the views of all members of the NJCPA.

We appreciate the efforts of the Financial Accounting Standards Board (FASB) to reexamine existing standards for financial statement presentation by not-for-profit entities (NFPs), focusing on improving 1) net asset classification requirements and 2) information provided in financial statements and notes about liquidity, financial performance, and cash flows. Our responses to the following specific questions are derived from CPAs, some of whom are auditors, users, and preparers of financial statements of NFPs.

Question 1 - *Do you agree that the disclosures about the nature of donor-imposed restrictions and their effects on liquidity in notes to financial statements would help ensure that necessary information is not lost by combining the temporarily and permanently restricted classes of net assets into one donor restricted category for purposes of presentation in the statement of financial position (balance sheet)? If not, please identify the information lost and why it is necessary. (See paragraphs BC22–BC23 and BC27–BC32.)*

We agree. The distinction between temporarily and permanently restricted is difficult for some NFPs, board members and other users to comprehend. Changing net asset classes to either “with” or “without” donor restrictions should provide a clearer distinction for NFPs, the board members and users of the financial statements. Disclosures would be needed to describe the restrictions and when and how the funds are available to be used. These disclosures will also assist in the liquidity assessment.

NFPs will continue to maintain endowments and their related accounting records for legal reasons, as well as the related enhanced disclosures. In addition, since liquidity is a key consideration, we request that NFPs be permitted to report subcategories on the Statement of Financial Position, e.g. “With Donor Restrictions – Held in Endowment” or “Without Donor Restrictions – Board Designated.”

Question 2 *- Do you agree that the aggregated amount by which endowment funds are underwater should be classified within net assets with donor restrictions rather than net assets without donor restrictions? If not, why? (See paragraph BC24.)*
Question 3 *- Do you agree that disclosures describing the NFP’s policy on spending from underwater endowment funds, together with the aggregated original gift amount or the amount that is required to be maintained by donor or by law, would provide creditors, donors, and other users with information useful in assessing an NFP’s liquidity and potential constraints on its ability to provide services without imposing undue costs? Why or why not? (See paragraph BC32.)*

We disagree with both questions 2 and 3. Historically, some NFPs have gone into corpus and are in underwater positions due to investment performance and when investment returns do not match or exceed spending policy. Having the underwater position classified as “without donor restrictions” may have a more impactful presentation for board members and other users. Showing the underwater amount as a deficit in operations on the face of the financial statements has the greater potential to create urgency around restoring the corpus.

Question 4 *-Do you agree that providing information in notes to financial statements about financial assets and liabilities and limits on the use of those assets is an effective way to clearly communicate information useful in assessing an NFP’s liquidity and how it manages liquidity without imposing undue costs? If not, why, and what alternative(s) would you suggest? (See paragraphs BC27–BC31.)*

We agree for most NFPs. However, a very small NFP (such as a PTA, first aid squad or firehouse) does not normally accumulate monies from year to year and some are required by their charters to spend donations within the same fiscal year. Therefore, we recommend a scope out for small NFPs. The definition of a small NFP may be problematic, but it was a recurring theme in our discussions of this exposure draft.

Question 5 *- Most business-oriented health care NFPs are required to present a classified balance sheet. Continuing care retirement communities and other NFPs may choose to sequence their assets and liabilities according to their nearness to cash as an alternative to using a classified balance sheet. As a result of the proposed requirement to provide enhanced disclosures of information useful in assessing liquidity, would there no longer be a need to hold business-oriented health care NFPs to the more stringent standard for their balance sheets? If not, why?*

Yes, we agree that business-oriented health care NFPs should not be held to a more stringent standard and should have the choice of a classified or non-classified balance sheet.

Question 6: *Do you agree that requiring intermediate measures of operations would provide users of NFP financial statements with more relevant and comparable information for purposes of (a) assessing whether the activities of a period have drawn upon, or have contributed to, past or future periods and (b) understanding the relationship of resources used in operations of a period to resource inflows available to fund those operations? Do you also agree that classifying and aggregating information in that way would not require major system changes? If not, why? (See paragraphs BC38–BC47.)*

We agree that intermediate measures of operations may provide users with more relevant and comparable information; however, it seems that more guidance is needed to assure consistency across the NFP sector. In addition, we suggest a scope out for small NFPs.

Regarding concerns about major system changes see response to questions 7, 8 and 10 below.

Question 7 *- Do you agree that intermediate measures of operations should include only those (a) resource inflows and outflows that are from or directed at carrying out an NFP's purpose for existence and (b) resources that are available for current-period operating activities before and after the effects of internal governing board appropriations, designations, and similar actions? If not, why? (See paragraphs BC48–BC74.)*

Question 8: *Do you agree that all internal transfers (governing board appropriations, designations, and similar actions that make resources unavailable or available for operations of the current period) should be reflected on the statement of activities immediately after an intermediate measure of operations before transfers and immediately before an intermediate measure of operations after transfers? If not all internal transfers, on what basis would you distinguish between those transfers that should and should not be reflected and how would you make that distinction operable? Do you also agree that reflecting those internal decisions (or lack of them) on the face of the statement rather than in notes will help an NFP communicate how its operations are managed without adding undue complexities? Why or why not? (See paragraphs BC46–BC47 and BC67–BC74.)*

Question 10 *- Do you agree that gifts of, or for, property, plant, and equipment (long-lived assets) should be considered operating revenue and support when received (or when placed in service in the case of a gift to acquire a long-lived asset)? Do you also agree that because the long-lived asset is not immediately fully available to be utilized in the current period, an NFP should be required to present a transfer from operating activities to other activities for the amount of the gifted asset or portion of the asset funded by restricted gifts? If not, why? (See paragraphs BC72–BC74.)*

We disagree with items 7, 8 and 10. The new concept of all transactions flowing through operations and then being "restricted" as a "transfer out" is a difficult one. More categories of transfers will make the financial statement unduly complex, confusing, and less readable. We understand the concept and the reasoning for the transfers; however, we believe they are complicated for users of the financial statements to follow, especially in a two statement approach. The example of receiving a gift of cash for long-lived assets with donor restrictions in "with donor restrictions" and then releasing it to "without donor restrictions – operating" and then simultaneously recording a transfer to "without donor restrictions – nonoperating" at the time the long-lived assets are acquired/placed in service seems ineffective and inefficient. It is our belief that transactions such as these should be recorded in their final position on the statement of activities at the time of the transaction. Therefore, when the long-lived assets are acquired/placed in service they should be directly transferred to "without donor restrictions –nonoperating" in one journal entry.

We are also unclear as to the mechanics of the transfers. Are transfers financial statement preparation (top side) entries or are transfers mandated to be included in the reporting system (general ledger)? If transfers are required in the reporting system, this would place a financial burden on NFPs.

Should the concept of transfers go forward, we request that the FASB provide comprehensive examples in the final guidance as to the reporting of these transfers.

Question 9 *- Do you agree that to promote comparability, the Board should eliminate one of the two optional methods for reporting expirations of donor restrictions on gifts of cash or other assets to be used to acquire or construct long-lived assets? Do you also agree that requiring the expiration of those donor restrictions on the basis of the placed-in-service approach rather than the current option to present a release from restriction over the useful life of the acquired long-lived asset is most consistent with the underlying notions of the intermediate measures of operations? If not, why? (See paragraph BC66.)*

We agree that the FASB should eliminate one of the two optional methods for reporting expiration of donor restrictions on gifts of cash or other assets to be used to acquire or construct long-lived assets. We agree that the placed-in-service approach is the preferred choice.

Question 12 *- Do you think the flexibility currently allowed by GAAP to present a statement of activities as either a single statement or two articulating statements and to use either a single-column or a multicolumn format should be retained or narrowed? If narrowed, why and in what ways?*

We have no preference on single-column or multi-column format; however, we request that the FASB indicate a preferred format in the final Update. An indication of a preference would facilitate comparability as most NFPs (in particular smaller ones) and auditors look for guidance and an indication of "best practice" when faced with such a choice.

Question 13 *- Do you agree that reporting operating expenses by both their function and nature together with an analysis of all expenses (other than netted investment expenses) provides relevant and useful information in assessing how an NFP uses its resources and, thus, should be required? Why or why not? (See paragraphs BC87–BC93.)*

We agree that NFPs should be required to report operating expenses both by programs (functional activities) and nature with an analysis of all expenses. This format of reporting enhances accountability and understandability of expenses and assists with budgeting for future periods. We recommend that the statement of functional expenses be required for all NFPs; removing the option of a supplemental schedule or disclosure. With this recommendation, NFPs would have four basic financial statements: statement of financial position, statement of activities, statement of functional expenses and statement of cash flows.

In the Exposure Draft on page 64, fire loss and actuarial loss on annuity obligations are excluded from nonoperating expenses in the disclosure on page 79, while interest expense is included. We suggest adding to the example impairment loss, changes in OBEP liability and other items to bolster an understanding of how to classify these items between "operating expenses and losses" and "nonoperating changes" in the statement of activities. We also suggest more guidance on whether or not to include such nonoperating expenses when presenting operating expenses by nature and function.

Question 14 *- Do you agree that requiring investment income to be reported net of external and direct internal investment expenses will increase comparability and avoid imposing undue costs to obtain information about all investment fees (for example, embedded fees of hedge funds, mutual funds, and funds of funds)? If not, why? (See paragraph BC100.)*

Question 15: *Do you agree that the disclosure of the amount of all investment expenses is unnecessary but that disclosure of internal salaries and benefits that are netted against investment return is of sufficient relevance, not too costly to obtain, and thus should be required? Why or why not? (See paragraph BC101.)*

Yes, we agree that investment expenses should be netted with investment return for the reason that it is costly to calculate all investment expenses and netting will increase comparability.

With regard to question 15, we agree that if internal salaries and benefits are netted with investment returns, it warrants disclosure. As to the definition of "direct internal investment expenses", we appreciated the information in the June FAQ document and think there is still some gray area as to which personnel and how much of their time should be included. To ensure the desired outcome of increased comparability, we request additional clarification to avoid inconsistent application.

Question 18 *- Do you agree that the direct method of presenting operating cash flows is more understandable and useful than the indirect method? Do you also agree that the expected benefits of presenting operating cash flows in that way would justify the one-time and ongoing costs that may be incurred to implement that method of reporting? If not, please explain why and suggest an alternative that might increase the benefits or reduce any operational concerns or costs. (See paragraphs BC75–BC80.)*
Question 19 *- Does the indirect method's reconciliation of cash flows from operations to the total change in net assets provide any particular type of necessary information that would be lost if, as proposed, that method is no longer required? If so, please identify the potentially omitted information and explain why it is useful and whether it should be provided through disclosure rather than requiring use of the indirect method. If you suggest that requiring the indirect method is necessary, would you require that the amount for cash flows from operations be reconciled to the amount of the (a) change in net assets, (b) change in net assets without donor restrictions, or (c) proposed intermediate measure of operations before or after transfers? Why? (See paragraphs BC75–BC80.)*
Question 20 *- Do you agree that although operating activities is defined differently for the statement of cash flows than for the statement of activities, more closely aligning line items presented in the statement of cash flows with the proposed operating classification for the statement of activities will increase understandability even though that reporting would be somewhat different from current requirements for business entities? If you believe that operating items in the two financial statements would not be sufficiently aligned, please indicate how their alignment might be further improved. (See paragraphs BC81–BC86.)*

We agree that the direct method of presenting operating cash flows is more understandable and useful. However, we disagree with making the change to the direct method until such time as it can be implemented across all industries. We do not believe that the NFP sector should be the only industry required to present in the direct format. After considerable discussion among our Interest Group members, we believe the changes in the statement of cash flows should be entirely removed from the final Update for NFP financial reporting.

Implementing the direct method of cash flows requires changes in systems and reporting and will impose a cost burden to implement. Most NFPs, in particular smaller organizations, will have difficulty implementing such changes.

We kindly request that the FASB consider the direct method of cash flows for all industries, as a separate project, for a later date.

Question 21: *Are there any particular proposed amendments in this Update that would require a longer period to implement than other amendments? If so, please explain.*
Question 22 *- Are there reasons for any particular size or type of NFP to need a longer time frame to implement the proposed amendments in this Update? If so, please explain.*

We believe that the final Update will take time for NFPs to understand and implement. It is our best estimate that a minimum of three years would be needed. Based upon our experience with SFAS 116 and 117, it will take several years for users to fully understand the changes.

With regard to timing, we offer the following suggestions:

- The implementation date should be certain and easy to follow (e.g. periods beginning January 1, 20XX).
- Early adoption should **not** be permitted.
- The initial implementation date should be at least one year later then the implementation of the revenue recognition standard. Implementing both standards simultaneously would be overwhelming.
- Smaller NFPs (e.g. less than five million dollars in gross revenue) should be given an additional one year to implement.

The above timing does not take into account restatement of prior years in the year the final Update is first applied. For those required to issue comparative statements, it appears that restatements would be required and, in that case, additional time from what was previously noted may be needed for implementation.

We would like to express our appreciation to the FASB and the Not-for-Profit Advisory Committee for the considerable efforts that culminated in this exposure draft. We applaud the thoughtful approach taken and the manner in which stakeholders were incorporated into the process. Thank you also for the opportunity to comment. We are available to discuss our comments with FASB members or staff at your convenience.

Respectfully submitted,

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