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Technical Director
File Reference No. 2015-230
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Proposed Accounting Standards Update – *Presentation of Financial Statements of Not-for-Profit Entities*

CliftonLarsonAllen LLP (CLA) is pleased to comment on the FASB's proposed Accounting Standards Update of Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954), *Presentation of Financial Statements of Not-for-Profit Entities*.

We applaud the Board's efforts to improve the current not-for-profit reporting model to provide better information to donors, creditors, and other users of financial statements. Thank you for the opportunity to submit comments developed with the shared goal of improving the usefulness of the reporting model.

General Comments

Goals of the proposed amendments include enhanced comparability and understandability, improved usefulness, and/or reducing complexities of a not-for-profit organization's financial statements. CLA believes proposed changes that increase the differences between not-for-profit financial reporting and for-profit financial reporting are counter-productive to these goals. We suggest tabling such proposals until the time when similar issues are addressed for for-profit entities and proposed changes can be made for all entities in concert.

Our comments below address the extent to which we believe the proposed changes are likely to accomplish the Board's goals in a cost-effective way.

Understandability

Many stakeholders of not-for-profit organizations, including board members, creditors, and contributors, have for-profit backgrounds. The more that not-for-profit standards deviate from for-profit standards, the more difficult it will be for such stakeholders to understand the financial statements. Because of this, we do not support the proposed reporting of two intermediate measures of operations, changing the classification of elements contained in the statement of cash flows, and classification of interest expense outside of operations on the statement of activities. Likewise, we are not convinced that requiring the direct method of reporting operating activities on the statement of cash flows will increase the understandability of not-for-profit financial statements.

Comparability

We agree that improving comparability is an important goal. However, we believe improving comparability between not-for-profit and for-profit organizations within an industry may be more meaningful and realistic than attempting to drive comparability among not-for-profit organizations across a wide range of diverse industries. For example, in certain industries, such as health care, not-for-profit organizations find it useful to compare themselves to for-profit entities operating in the same industry. We are not convinced that there is a compelling need for stakeholders to compare not-for-profit organizations operating across a variety of widely differing industries. Accordingly, we suggest that the Board consider defining operating measures based on generally accepted reporting practices by industry. In addition, we suggest the Board consider limiting the activities that may be reported in operations to promote consistency, as a simple alternative to the proposed operating mission measure.

Usefulness

We agree with the concept that liquidity information is useful to not-for-profit stakeholders. We suggest the Board consider requiring a classified statement of financial position. Because of its simplicity and consistency with for-profit financial statements, we favor this approach over the proposed annotative disclosures related to liquidity. We believe such disclosures would increase the complexity of the notes to the financial statements and make comparisons between not-for-profits more difficult.

Reduce Complexity

To reduce the complexity of not-for-profit financial statements, the proposed standards decrease the net asset categories from three to two. While the proposed amendment may make the basic financial statements less complex, the notes to the financial statements would be expanded and thus more complex. Therefore, we are not convinced this change will achieve the goal. Since the current reporting model has been in use for over twenty years, users are generally familiar with the definitions and underlying external restrictions. Under the proposed amendments, users would have to find the relevant information within the notes to the financial statements—likely a more burdensome process. In addition, we have concerns that this change will make the basic financial statements less transparent.

Specific Comments***Statement of Financial Position and Liquidity***

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.)

Response: Fundamentally, we do not agree that presenting temporarily and permanently restricted classes of net assets into one combined donor restricted category in the statement of financial position is preferable because of the loss of a liquidity measure from this statement. For example, while under UPMIFA underwater spending is allowed, the majority of the endowment is not available for use in current or future operations. Therefore, combining permanent endowments with temporarily restricted net assets could

mask a lack of liquidity. Providing this information in the notes to the financial statements, lessens its prominence and thus increases the risk that users will misunderstand the liquidity situation. Additionally, for institutions of higher education, a composite score is also required to be submitted; eliminating the temporarily restricted column will add challenges in completing this calculation.

The expanded liquidity disclosure information would be of greatest interest to creditors. However, creditors are typically able to obtain the specific liquidity information they want through existing contractual agreements. We believe the current presentation and disclosures provide adequate information to most readers of not-for-profit financial statements. Thus, in our opinion, removing detail from the statement of financial position and increasing the amount of disclosure information in the notes to the financial statements will increase the complexity of the information presented without increasing value to the readers of the financial statements.

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.)

Response: We agree that presenting amounts related to underwater endowments, as well as donor restricted unappropriated earnings, into a restricted net asset category, is appropriate.

Question 3: Do you agree that disclosures describing the not-for-profit'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 a not-for-profit's liquidity and potential constraints on its ability to provide services without imposing undue costs? Why or why not? (See paragraph BC32.)

Response: We agree that the disclosures described at BC32 a-c provide appropriate information on the current value of endowment funds, the current aggregate fair value of endowments, and management's intention with respect to future spending from the funds. We support the required disclosure of amounts that must be maintained by donor directive or by applicable state law, which is consistent with UPMIFA. However, we do not believe disclosure of the historical dollar value (original gift endowment amount) should be required, since its relevance diminishes over time.

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 a not-for-profit'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.)

Response: We do not believe that providing information in notes to financial statements about financial assets and liabilities and limits on the use of assets is an effective way to communicate information about liquidity. We believe this is better accomplished through a classified balance sheet and identification of restricted use assets on the face of the statement of financial position. The proposed additional disclosures appear complex and would likely not be presented in a consistent manner by the various not-for-profit organizations. We have concerns about the burden and cost for not-for-profit organizations to gather this

information, consult with their accountants, and ensure information is properly disclosed. Furthermore, increased auditing costs may occur, as additional procedures may need to be performed to ensure the disclosures are complete and accurate.

Question 5: Most business-oriented health care not-for-profits are required to present a classified balance sheet. Continuing care retirement communities and other not-for-profits 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 not-for-profits to the more stringent standard for their balance sheets? If not, why?

Response: Since for-profit health care providers are required to present classified balance sheets, we recommend that not-for-profit business-oriented health care organizations be required to follow the same requirements as for-profit organizations and present classified balance sheets to aid comparability within their unique industry. Overall, while enhanced disclosures around liquidity may provide additional detail to explain the information provided by a classified balance sheet, it would not be as direct or clear as presenting classified balance sheets. Please also see our response to question 4.

Statement of Activities, Including Financial Performance

Question 6: Do you agree that requiring intermediate measures of operations would provide users of not-for-profit 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.)

Response: We do not agree that requiring intermediate measures of operations would provide users of not-for-profit financial statements with more relevant comparable information. Creating intermediate measures for all not-for-profit sub-industries would not meet the objective of financial statement comparability as there are significant differences in operating activities between different not-for-profits.

We do believe that if comparability is desired by certain users, the measure should not be an operating measure. We believe it should be a defined measure that is analogous to the existing ASC 954 performance indicator. We understand that the FASB has a project in place relating to the income statement for all entities. If based on that project, a defined measure of operations for all entities is approved, that would alleviate some of our concern. Implementing a defined measure that excludes certain items would allow comparability without driving the not-for-profit reporting model further away from the for-profit reporting model.

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 a not-for-profit'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.)

Response: We agree that intermediate measures should only include resource inflows and outflows related to the not-for-profit's purpose for existence; nonetheless, determining which resources are for the purpose of the organization's existence will vary depending on each specific not-for-profit. Any transactions that are not related to operations (yet are in support of the not-for-profit's purpose) could be reflected in a section that includes any non-operating activity. We believe that not-for-profits should be able to have flexibility in determining the definition of their operations, similar to for-profit entities, and therefore what activities should be included or excluded from an intermediate measure of operations. An alternative approach could be defining what types of activities should not be included within a "performance" indicator, such as pension related charges.

We agree resources subject to donor imposed restrictions that are not available for current operations should be excluded from a defined performance measure. However, resources that are appropriated or designated by the governing body and do not have external limitations have the potential for use in the current period and therefore should be included.

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 a not-for-profit communicate how its operations are managed without adding undue complexities? Why or why not? (See paragraphs BC46–BC47 and BC67–BC74.)

Response: We do not agree that all internal transfers should be reflected on the statement of activities before an intermediate measure of operations that reflects transfers. Inclusion of a second operating indicator adds a level of complexity to the statement of activities that potentially could make the statement of activities more difficult to understand by users of the financial statements and further divides not-for-profit financial reporting from for-profit financial reporting. This information is currently required to be disclosed within the notes to the financial statements. Most not-for-profits use their internal software to prepare the financial statements, including the statement of activities. It could be cost prohibitive for a not-for-profit's internal accounting personnel to re-design how their current chart of accounts map would be used in the preparation of the proposed statement of activities. We believe these transactions should be separate from the presentation of a defined operating indicator. Please also see our response to question 6.

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.)

Response: We 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. A consistent approach would be preferable. The existing allowable approach of recognizing as capital assets are acquired and placed in service allows the recognition on a timelier basis that is consistent with the donor's intent.

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, a not-for-profit 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.)

Response: We do not agree that gifts of, or for, property, plant, and equipment should be considered operating revenue and support when received. Capital gifts more closely resemble investing activities as they expand an entity's capacity to provide future services and/or generate future revenues and therefore are not current year operating activities. An exception to this may be on the occasion where there is an arrangement to liquidate the asset in the near term authorized by the not-for-profit's board. Furthermore, reflecting these contributions in operations can create significant inconsistencies in an organization's operations between fiscal years and would not emulate a true reflection of operations.

Question 11: Do you agree that the addition of required intermediate measures of operations for all not-for-profits would make unnecessary the need for not-for-profit business-oriented health care entities to also present their currently required *performance indicator*? Why or why not? (See paragraph BC99.)

Response: We believe not-for-profit business oriented health care entities will prefer to leave their current operating indicators as defined unchanged. An overall performance measure for organizations, such as health care entities, is valuable in assessing the overall performance and allows the financial statements to be comparable to other organizations within its respective industry that are not organized as not-for-profits. The health care operating indicator is a good example for other industries to follow.

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?

Response: We believe continuing to allow not-for-profit organizations in different industries flexibility in how the statement of activities is presented makes the statement more meaningful within each industry. The current flexibility allows preparers of financial statements to make informed decisions related to which presentation appropriately addresses the needs of the users of their financial statements.

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 a not-for-profit uses its resources and, thus, should be required? Why or why not? (See paragraphs BC87–BC93.)

Response: Currently different not-for-profit sub-industries have already determined what stakeholders and users of their financial statements find useful in analyzing their financial statements. Examples include health care entities reporting natural expenses and colleges and universities reporting by functional expenses as defined by their national association. It is not clear what group of stakeholders would benefit from requiring all entities to report expenses by nature and function. Requiring both presentations for all not-for-profit organizations may not be cost effective for all not-for-profits, especially smaller organizations with limited administrative resources. Rather than requiring both presentations for all not-for-profit organizations, we would recommend modifying the scope of entities required to include the disclosure.

Currently the reporting of functional expenses in financial statements differs from the reporting of functional expenses in federal Form 990. Requiring a detailed reporting of functional expenses in the financial statements can cause an apparent lack of consistency, reduce clarity, and increased burden for preparers of financial statements. In addition, lack of standard definitions for functional categories within each industry will result in a lack of consistency and comparability between organizations.

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.)

Response: We 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.

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.)

Response: We agree that the disclosure of the amount of all investment expenses is unnecessary. We do not believe internal salaries and benefits that are netted against investment return should be required as it is irrelevant.

Question 16: Do you agree that interest expense, whether incurred on short-term or long-term borrowing, and fees and related expenses incurred for access to lines of credit and similar cash management and treasury activities are not directed at carrying out a not-for-profit's purpose and, thus, should not be classified as operating activities? If not, why? (See paragraphs BC59–BC60.)

Response: We do not agree that interest expense, fees, and related expenses should be classified as non-operating activities. The proposed treatment pushes not-for-profit accounting further away from that of a

for-profit reporting model, which can make not-for-profit financial statements more arduous to understand for stakeholders and board members with for-profit backgrounds. The financial statements would also be harder to compare in sub-industries that include both for-profit and not-for-profit entities.

Question 17: Do you agree with the following implementation guidance:

- a. Equity transfers between not-for-profits that are under common control and are eliminated in a parent entity's consolidated financial statements and equity transactions between financially interrelated entities should be presented within operating activities unless they are not available for current-period use in carrying out the purpose for the reporting entity's existence? If not, why? (See paragraph BC62(a).)
- b. Immediate write-offs of goodwill generally should be presented within operating activities? If not, why? (See paragraph BC62(b).)
- c. Immediate write-offs of acquisitions of noncapitalized items for a permanent collection should be presented within the operating activity section if acquired with net assets without donor restrictions? If not, why? (See paragraph BC62(c).)

Response: We do not agree that equity transfers between not-for-profits that are under common control and are eliminated in a parent entity's consolidated financial statements and equity transactions between financially interrelated entities should be required to be presented within operating activities. We believe the classification of such transactions should be consistent with management's intent of the transfer, for example, if the intent of a transfer is to support operations, the transaction should be classified within the operating activities.

We agree with the provisions noted above in b.

We do not agree that immediate write-offs of acquisitions of noncapitalized items for permanent collection should be presented within the operating activity section. Under the definition of a collection, these are assets which cannot be liquidated and made available for operations.

Statement of Cash Flows, Including Financial Performance

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.)

Response: We recommend overarching changes to the statement of cash flows for topics not unique to non-profits be deliberated congruently with for-profit entities. In order to avoid divergence of practice, CLA recommends the direct method of presenting operating cash flows not be required, but instead continue providing an option for not-for-profits to use the indirect method. This option promotes understandability

and consistency for users as the change in net assets is a relevant metric for many not-for-profits and their board members, who many times operate in a for-profit environment.

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.)

Response: If the Board continues with the proposal to require the direct method of cash flows, we believe that the indirect method's reconciliation should continue to be required, as noted in Question 18, to avoid relevant information being lost for some users until such a time as the topic is researched for all entities. Should a not-for-profit decide to utilize the indirect method of cash flows, we would recommend requiring cash flows from operations to be reconciled to the amount of the change in net assets. The change in net assets should be utilized as it captures all activity of the not-for-profit.

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.)

Response: As noted in our opening statements and in question 18, we have a concern regarding the timing of this requirement and its applicability to only not-for-profit entities. We believe changes which are not specifically unique to not-for-profits (such as appropriated endowment return) should be part of a global revision to cash flow presentation requirements for all entities, not just not-for-profit entities, to promote a universal understanding of the new required presentation format. To require changes for issues which impact for-profits and not-for-profits alike to only not-for-profits would result in confusion for financial statement users, such as lenders and board members, many of whom operate in a for-profit environment. Therefore, CLA recommends any changes to operating, investing, or financing cash flow classifications be limited to those items unique to not-for-profits. This will also ensure operating activities as defined on the statement of cash flows align with the concepts of operating activities on the statement of activities.

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.

Response: We do not believe any particular proposed amendment would take longer to implement than others.

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Question 22: Are there reasons for any particular size or type of not-for-profit to need a longer time frame to implement the proposed amendments in this Update? If so, please explain.

Response: We believe all not-for-profits should implement the proposed amendments at the same time.

Sincerely,

A handwritten signature in black ink that reads "CliftonLarsonAllen LLP". The signature is written in a cursive, flowing style.

CliftonLarsonAllen LLP