

MINUTES



MEMORANDUM

To: Board Members

From: Not-for-Profit Team

Subject: September 21, 2015 Roundtable
Minutes: Financial Statements of
Not-for-Profit Entities, Norwalk AM
Session

Date: December 16, 2015

cc: Stacey Sutay

The Board meeting minutes are provided for the information and convenience of constituents who want to follow the Board's deliberations. All of the conclusions reported are tentative and may be changed at future Board meetings. Decisions become final only after a formal written ballot to issue an Accounting Standards Update or a Statement of Financial Accounting Concepts.

Topic: Proposed FASB Accounting Standards Update, *Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954): Presentation of Financial Statements of Not-for-Profit Entities*

Basis for Discussion: Proposed FASB Accounting Standards Update, *Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954): Presentation of Financial Statements of Not-for-Profit Entities*, Outreach Summary of proposed Update

Length of Discussion: 9:00 a.m.to 12:00 p.m.

Attendance:

External Participants

Jack Abdo
Kelly Frank
Jeffrey Haber
Jackson Day

Abdo, Eick & Meyers
CohnReznick
The Commonwealth Fund
Ernst & Young

Karen Kedem
John Bailey
Susan Menditto

Alice Antonelli
Candice Meth
Beth Lipson
Nancy Gunza
Joan Waggoner

Moody's
Museum of Modern Art
National Association of College and
University Board Officers (NACUBO)
Nonprofit Finance Fund
New York Society of CPAs
Opportunity Finance Network
Pennsylvania Institute of CPAs
Plante & Moran

FASB Participants

Russ Golden
Jim Kroeker
Daryl Buck
Tom Linsmeier
Marc Siegel
Larry Smith
Sue Cospers
Jeff Mechanick
Ron Bossio
Rick Cole
Chris Dickson
Ranee Wiley

Board Chairman
Board Vice-Chairman
Board Member
Board Member
Board Member
Board Member
Technical Director
Assistant Director
Senior Project Manager
Supervising Project Manager
Postgraduate Technical Assistant
Postgraduate Technical Assistant

1. Participants were provided an agenda and advance materials to facilitate the roundtable discussions ([click here](#)).

Topic 1: Operating Measures

2. Participants were generally supportive of requiring an intermediate measure of operations, but were generally unsupportive of the approach proposed.
3. Participants were generally unsupportive of the proposed section for internal transfers due to the complexity it adds to the face of the statement of activities and concern that users would not understand it.
4. A participant from the private foundation industry, a participant from the community development financial institution (CDFI) industry, and an auditor suggested allowing not-for-profit entities (NFPs) to choose their own measure of operations. Reasons for allowing NFPs to choose their measure of operations include (a) the definition of operating performance varies across industries and (b) it would be impossible to have a uniform definition of what is operating or nonoperating due to the diversity among NFPs.

5. A participant from the higher education industry expressed concern that transfers for board appropriations from quasi-endowment return and appropriations from true endowment would be presented in two separate areas when many organizations treat the appropriation from quasi and true endowment as one board action. This participant suggested expanding the availability dimension to show internal policies and board decisions with some general constraints around those decisions.
6. An auditor stated that it is important to stay principles-based in the area of internal transfers and that moving quasi-endowments out of transfers causes inconsistency in the principles.
7. A participant from the CDFI industry did not support including board designations on the face of the financial statements because, in that industry, board designations are often used as capital for lending and, in the participant's view, these board designations do not relate to operations, but instead relate to management's intentions on how to use resources. Therefore, such board designations could distort the operating measure by showing an operating loss when that is not the case. This participant would support disclosure of board designations in the notes rather than on the face of the financial statements.
8. An auditor suggested that, for private foundations, describing investment income as nonoperating is not meaningful. This participant also stated that there would not be manipulation of the operating measure because everything is shown on the face of the statement of activities.
9. An FASB Board member asked participants to give a broad sense of some of the objections to the project and if the Board should be doing a more fundamental consideration of FASB Statement No. 116, *Accounting for Contributions Received and Contributions Made*, FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations*, and what a contribution represents, as suggested by a few comment letters.
10. An auditor agreed with taking a more fundamental look at Statements 116 and 117, but stated that they do not necessarily need to be changed. This participant also suggested that there should be consistency among operating measures, but that the operating measures do not need to apply to the entire NFP population, particularly small NFPs.
11. Another auditor suggested that small NFPs will likely appreciate simplicity and that a higher level of transparency is needed for small NFPs to see how their mission is being fulfilled. This participant suggested that the proposed operating measures are helpful in illustrating how small NFPs are managed. This participant suggested that the Board should not revisit contribution revenue as, in their view, the current accounting is appropriate.

12. An FASB Board member clarified that by “stewardship,” the Board means how an NFP board decides to use its money. Otherwise, with an availability notion, effectively, quasi-endowment funds would not be presented in the financial statements because there are no restrictions on the money.
13. Another FASB Board member observed that some participants seemingly used the word “comparability” when they meant “uniformity.” This Board member stated that generally for for-profits, programmatic revenues cover programmatic expenses but, for many NFPs, programmatic revenues do not cover programmatic expenses, so NFPs turn to other sources. The proposal indicates programmatic revenues generated in the first subtotal and the portion that is set aside is illustrated above the second subtotal. This Board member questioned whether fixing the uniformity and flexibility issue would still allow for a structure that tells the story of an NFP in a productive way.
14. Another auditor preferred one set of standards for all NFPs to follow. This participant also supported being consistent with business entities.
15. A user of NFP financial statements stated that they work with whatever is presented to get to the measures that they feel are appropriate to evaluate the credit-worthiness of an organization. This participant also stated that having a measure of stewardship is an interesting concept and that, although transfers may be difficult for some readers to understand, it is good to see some of the intention that goes into the operating measure without looking at the notes.
16. An auditor suggested that the proposed format for the statement of activities would help a donor decide what sort of a donation to give.
17. A participant from the private foundation industry did not support the mission dimension. This participant also did not support the availability dimension because, in their view, internal transfers do not relate to the current period and suggested that the transfers section is similar to income smoothing for for-profit entities.
18. An FASB Board member noted that it was not the intent of the Board for the second measure, which includes the effects of internal governing board actions, to be comparable between organizations.
19. A participant from the higher education industry preferred a simplified statement of activities, such as an operating statement based on rules of legality and board decisions, and income based on availability. This participant was also supportive of a two-statement approach to the statement of activities, possibly with note disclosures, but also noted that sometimes the face of the statements is more powerful than the notes.

20. An FASB Board member asked if participants were concerned that small and mid-sized NFPs would have additional difficulty in actually preparing the financial statements.
21. Two participants from the CDFI industry, one who works with small to mid-sized NFPs, agreed that such NFPs would have additional difficulty in preparing the financial statements.
22. A participant from the CDFI industry did not support interest income, interest expense, and investment income being excluded from the operating measure. This participant supported more flexibility for NFPs and agreed with other participants that the statement of activities is too complex and the suggested changes would require more education of NFP board members.
23. A participant from the CDFI industry stated that there is a distinction between operating and nonoperating and core to the mission and not core to the mission.
24. An FASB Board member stated that it is interesting to hear that users want flexibility and asked the two CDFI participants, who also could be considered users of NFP financial statements, if having flexibility for preparers is most useful.
25. A participant from the CDFI industry stated that comparability between NFP industries is desirable. This participant also stated that they use the Form 990 to make comparisons between NFPs, so they would prefer flexibility for the statement of activities.
26. An FASB Board member stated that more flexibility in presentation reduces comparability between NFPs and will increase the time spent educating NFP board members. This Board member also noted that the arguments of some participants are contradictory in that they suggest reporting standards to be both (a) similar to for-profits and (b) sufficiently flexible to accommodate differences among different types of NFPs.
27. An auditor suggested that perhaps simplicity, rather than flexibility, is needed because the population of NFPs is diverse.
28. An auditor noted that the proposed model for operating measures shows where an NFP is vulnerable and the NFP's plans to address that vulnerability.

Topic 2: Presentation of Operating Cash Flows

29. A participant who is a user of NFP financial statements uses select data points from the statement of cash flows rather than the entire statement and has some trouble reconciling from some entities. Some data points

- this participant looks at are depreciation, principal and interest paid, and purchases of property, plant, and equipment.
30. A participant from the private foundation industry whose organization utilizes the direct method stated that, in their view, the indirect method does not provide any informative value that they cannot calculate themselves. This participant suggested that based on their experience, the direct method is as simple to present as the indirect method and that donors and other stakeholders generally do not understand the indirect method.
 31. An auditor stated that many boards they work with budget on a cash basis and looking at the change in net income and change in net assets on the statement of cash flows helps the boards to better understand. This participant further stated that a lot of information from the direct method can be taken from the statement of activities. This participant questioned why the direct method should be mandated for the NFP sector but not for other industries.
 32. An FASB Board member stated that for-profit entities have told the Board that issues on mergers and acquisitions, such as different systems, different countries, and so forth, cause the direct method information to be too costly to obtain. However, it is our understanding that most NFPs do not have these issues.
 33. An auditor stated that the direct method would be beneficial for an extremely complicated commercial entity, but the direct method may not make the financial statements more useful for an NFP that is more simplistic in nature or when the information can be gathered in other places. This participant expressed concern that the direct method would be a difficult change for NFPs in Year 1 and some NFPs are too heavily reliant on auditors to prepare their financial statements such that those NFPs may not have the expertise to understand the direct method statement of cash flows.
 34. Another auditor suggested that after Year 1, the difficulties associated with the direct method may lessen. This participant also suggested that the direct method is easier follow; however, they questioned how meaningful the direct method is to the governing board. This participant suggested that the indirect method's reconciliation is unnecessary because you can calculate that information from the balance sheet in a clear way. However, you cannot calculate the direct method's information from the statement of activities.
 35. A participant from the higher education industry stated that public institutions have been using the direct method for a while and that both preparers and users like the direct method statement of cash flows and find the indirect reconciliation to be of no value and more burdensome.

This participant further stated that the direct method is not easily implemented in the first year, but it is not difficult after the first year.

36. A participant from the CDFI industry expressed concern that NFPs with for-profit subsidiaries would not have comparable cash flow statements or that the for-profit subsidiaries would still need to use the indirect method. This participant also stated that most CDFIs use the indirect method and it is not useful; however, this participant suggested that the direct method still would not be useful and would not justify the incremental cost when they can gather the direct method information from the statement of activities.
37. A user of NFP financial statements stated that their analysis is usually more accrual-based versus operating performance based and that they can usually find some noncash items in the notes.
38. A participant from the private foundation industry stated a preference for free choice of either the direct or indirect method and being required to only present one method.
39. A participant from the CDFI industry stated that, in their view, the utility of the statement of cash flows to board members is low, regardless of whether indirect or direct presentation is used. This participant still preferred to require the statement of cash flows, but stated that there is more important information for boards to discuss before cash flows.
40. A participant from the cultural arts industry supported requiring the direct method, suggested that the statement of cash flows is important, and noted that in the currently required statement of cash flows, investing and financing activities are already presented using the direct method.
41. An auditor suggested requiring both the direct method and the indirect method's reconciliation.
42. An FASB Board member asked whether the Board should consider eliminating the statement of cash flows if a statement of activities shown both on a cash and accrual basis was required instead.
43. A participant from the CDFI industry and an auditor both noted that showing a cash and accrual basis statement of activities would be an interesting thought.

Topic 3: Information Useful for Assessing Liquidity

44. A participant from the CDFI industry supported the proposed disclosures and thought the proposed disclosures would push users to think more about liquidity.
45. An auditor preferred a classified balance sheet with note disclosures.

46. A participant from the private foundation industry preferred notes around portfolio investment, but noted that it does not help with contributions.
47. An auditor and a participant who is a user of NFP financial statements expressed concern with a self-defined time horizon and would prefer a prescribed time horizon to aid in comparability.
48. A participant from the CDFI industry supported the quantitative disclosures but not the qualitative disclosures and, in their view, the qualitative disclosures are more appropriate for management discussion and analysis than the financial statements.
49. An auditor expressed concern that the timing of the issuance of the financial statements affects the utility of the liquidity disclosures and classified balance sheets and that the forward-looking information aspect is more appropriate for management discussion and analysis.
50. A participant who is a user of NFP financial statements and a participant from the CDFI industry noted that although the liquidity disclosures may be “stale” by the time financial statements are issued, there is value in the trend analysis over time.
51. An auditor and a participant from the higher education industry were not supportive of a classified balance sheet in place of the proposed liquidity disclosures. The higher education industry participant noted that off-balance sheet commitments may cause trouble.
52. Two participants from the audit industry suggested including a simpler example that would be more understandable to small and mid-sized NFPs.

Topic 4: Other Topics

Expenses by Function and Nature

53. An auditor expressed concern about the cost of determining allocation bases and additional audit costs for small NFPs.
54. A participant from the CDFI industry expressed concern that NFPs may over-allocate expenses to program expenses and hire more program staff than infrastructure staff due to the perception that most expenses should be programmatic expenses. This participant supports natural classification of expenses, but does not support functional classification.
55. A participant from the cultural arts industry requested guidance for the various categories due to wide variations within the participant’s industry.

Investment Return

56. A participant from the cultural arts industry expressed concern for the proposed disclosure of internal salaries and benefits because Schedule J on the Form 990 already tells the reader how salaries are managed. This participant also did not see value in disclosing internal salaries.
57. A participant from the higher education industry expressed concern about limiting the netting to only “direct” expenses because that would exclude certain related functions that are netted today. This participant prefers the current requirements to net “related” expenses. This participant also questioned the value of disclosing internal salaries and benefits because, in their view, it is not pertinent to cost structure.
58. An auditor and a participant from the private foundation industry supported netting investment income and direct investment expenses, but expressed concern that some organizations that do not net salaries in practice today would be reluctant to do so because it would put those salaries in the nonoperating section of the statement of activities.
59. A participant from the private foundation industry suggested using the term “internal” rather than “direct” and suggested netting unused fees on lines of credit against investment return because fees on unused lines of credit, in their view, are an investment expense rather than an operating expense.