Financial Accounting Standards Board
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November 8, 2016

Dear Fellow Accountants:

I am enclosing a copy of an email I sent to Barron's letters to the editor in response to their article in the October 10, 2016 issue on the FASB reforms to non-profit accounting. It is encouraging that Barron's, primarily a publication for business people, published an article that might help business people in their services to non-profit organizations, but much more needs to be done. I also include a copy of my letter to the editor published in the October, 2015 issue of the Journal of Accountancy. I believe the FASB needs to seriously consider the points I made in those letters, and will expand below on my views.

These views come from my many years of serving non-profits as auditor, board member, Treasurer, Finance Committee, Audit Committee, Investment Committee, and other roles. Your view of the need for simplification on non-profit statements is in the view I have seen from many business people not experienced in non-profit accounting who take the business view that what we need to see is the real bottom line of all activities, and who see the various transfers between restricted categories as manipulative and confusing and the result of management making arbitrary transfers to make things look good. They simply do not understand that combining regular operations with gifts for endowment and other specific purposes, endowment market value change, unrestricted bequests, and changes in actuarial calculations of retirement plans does not result in a meaningful number.

One good thing about non-profit presentations is that it is considered appropriate for their financial statements and many provide a breakdown between operations and non-operating items that is essential for understanding. I find it very interesting that now many corporate business annual reports show an earnings number that is described as the GAAP number and then show what management believes they actually earned, removing non-operating and other items. I think this makes sense, but the FASB simply cannot afford the idea that this creates that GAAP accounting is wrong and misleading. I think that GAAP should be revised for both profits and non-profits to require the presentation of both normal operations and non-operating items. There needs to be clear description of what should be treated as non-operating. This will be difficult and controversial. I believe that some things which occur every year, like change in market value of investments, should be treated as non-operating. As an investor, and serving on investment committees, what I want to know is what a company earned from continuing operations so that I can make some projection of earnings for next year which will affect the stock price.

I continue to believe that combining Temporarily Restricted with Permanently Restricted creates a meaningless number that will result in the apparent net worth moving up and down with changes in amounts of grants and other restricted funds that happen to be on hand at a particular time. Clearly, gifts and grants restricted for short-term spending for particular purposes are different from endowment funds, and combining them impairs understanding. The more I think about it, the more I think that the concept of temporarily restricted contributions and grants should be done away with, and such receipts should be considered as liabilities, like a business treats an advance deposit on a contract or the unexpired portion on a three year subscription or fee. A basic accounting principle is to report expenses related to a particular revenue in the period the revenue is reported. Let us conform to that.

Maybe this is because I am so old, but I remember that in the distant past it seemed to me that board and other people had a better understanding of the financial situation of non-profits than they do today. I think that was because rather than using the restricted categories, fund presentations were grouped by nature and purpose. We had the Operating Fund, the Property Fund and the Endowment Fund. Equipment items that were expected to be replaced from operating funds were recorded in the Operating Fund, while buildings and other major property, generally purchased from a capital campaign, were recorded in the Property Fund, as was depreciation thereon as there was no expectation that operations would recover the building depreciation.

Now, with depreciation in operations what frequently results is an unreal operating loss. But what is often more seriously misleading is inclusion of buildings in unrestricted which in many cases results in a large unrestricted balance which makes donors think the organization is wealthy and does not need their support, when often when the building is taken out, there is a negative Operating Fund and the organization has to incur debt to pay its bills.

Spreading the endowment between Unrestricted, Temporarily Restricted and Permanently Restricted makes it almost impossible for a reader to determine what is actually working as an endowment. Whether it is donor restricted or board designated bequests or accumulated retained appreciation or unexpended earnings thereon is much less important than what is actually serving as endowment. I would have a column in the Statement of Operations that would include transactions in all funds acting as endowment. The restriction concept, which I believe is necessary to report, could be accomplished by showing that detail on the Balance Sheet in the Net Assets category.

We are now in a situation where many published non-profit annual financial statements combine the three restriction categories into one column. Others are way off from FASB standards. A recent extreme case I saw had only pie charts which had only percentage numbers as to income and expense categories with no dollars shown. Some annual reports no longer include any financial statements. We need to ask ourselves why this is happening. I think it is because many non-profits believe that the FASB model statements are simply not understandable and are misleading to most readers who are not accountants or who have only experience with accounting for businesses.

In conclusion, I believe that present FASB financial statements for non-profits are simply not understandable to many readers and that this must change. I think the FASB should seriously consider returning to the much more understandable format of reporting by Operating Fund, Property Fund, and Endowment Fund.

Sincerely,

Stanley F Dole

Stanley F. Dole, C. P. A.

Enclosures

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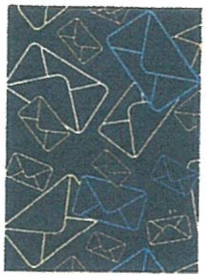
LETTER TO THE EDITOR



FASB should look again at not-for-profits reporting

I was pleased to see the article in the July *JofA* ("Not-for-Profit Financial Reporting Headed for a Change," page 42) about FASB considering changes in the model for not-for-profit accounting and reporting. However, I am concerned that the approach of having only two categories, unrestricted and restricted, in the financial statements would be a step in the wrong direction, making it more difficult for readers to understand the situation. Revision to the present not-for-profit model is essential but needs much more discussion and debate, particularly by users of not-for-profits' financial statements.

I am a retired CPA who had 25 years in the audit division of a major CPA firm and then 20 years with my small firm, which specialized in audits of not-for-profits. I have served and presently serve as board member, treasurer, and member of finance and investment committees for not-for-profits. It is my considered opinion that the understanding of the operations and financial status of not-for-profits by board members, staff, and donors is much less than in the old days when the reporting was by funds with specific purposes—operating, restricted, property, and endowment—rather than by legalistic restrictions. I believe FASB should seriously consider returning to the fund accounting model. If it is felt that restriction categories must be reported, that could be detailed in the net asset section of the balance sheet.

One of my earliest memories is a grade school teacher telling us that you cannot add apples and oranges and get a meaningful result. I see our present model as just that. When the endowment comprises all three restriction categories, nobody can figure what it is without reading all the notes. Unfortunately, few do. I believe it is important to have the basic statements provide as much information as possible. FASB needs to ask what information readers need and see that the financial statements provide it. I believe what is needed are the following:

1. The results of ongoing operations, without inclusion of nonoperating items like market value change in investments, bequests, legal settlements, gains on property sales, and gift annuity transactions. While these are frequent, they should be shown in a nonoperating separate section, so readers can evaluate regular operations. It should be very clear what the earnings on endowment were and what additional draw was taken.
2. Transactions in temporarily restricted net assets, with clear distinction between amounts currently expendable, and endowment appreciation, likely a permanent growing amount.
3. Transactions in the endowment funds, both donor restricted and board designated, in one place, with clear separation of income from market value change.
4. Transactions in fixed assets, clearly showing if they are included in the operating fund, and if so, how much is left in the operating fund for regular operations. Often that is negative. People need to see that property purchased from operations depletes money available for operations.
5. A major capital campaign needs reporting in a separate column so people can see it easily.

In summary, if FASB will consider and ask readers what they need to know and do their best to make required reporting tell it, not-for-profit reporting will be much improved.

—Stanley F. Dole, CPA
Grand Rapids, Mich.

The *JofA* welcomes letters commenting on the magazine's content. Letters should be no more than 500 words and may be edited for length and clarity. Please include your telephone number, city and state of residence, and email address. Letters can be sent to joaed@aicpa.org.

ILLUSTRATION BY MARK MURPHY/ISTOCK

NFP-UNS
Comment Letter No. 1

Gmail

Stanley Dole <stanley.dole@gmail.com>

Letter to Editor on article on FASB

1 message

Stanley Dole <stanley.dole@gmail.com> Fri, Oct 21, 2016 at 11:26 PM
To: Mail@barrons.com

I was pleased to see the October 10 article called Charity Reforms Don't Go Far Enough, about new FASB statements on non-profits. I hope Barron's can have more on non-profits as many business people serve on their boards but lack understanding of their accounting because it is different from business accounting. I was disappointed that the FASB combination of Permanently Restricted and Temporarily Restricted in the interest of simplification was not really discussed. I think that is a major error that needs discussion and change before it becomes effective.

I am a retired CPA whose main practice was auditing nor-for-profit entities, and have dealt with 30 years of evolving accounting standards for non-profits. It is my experience that if boards, executives, staff, donors and members are to have a good understanding of the financial position and operations of non-profits they need to know what is donor restricted endowment, retained appreciation and income on it, if any, and other funds such as unrestricted bequests that the Board has designated as endowment as separate from grants and contribution that donors have restricted for spending for specific purposed. These are significantly different funds and must show separately

A much better way to simplify and to avoid the transfers that are puzzling to non accountants would be to do away with Temporarily Restricted, and treat these amounts as a liability, like a business does for an advance payment on a contract before the services are rendered. It would be like an advance payment on a three year subscription to a publication, which is deferred revenue taken into income over the three year period.. Presently endowment funds are split between Unrestricted, Temporarily Restricted, and Permanently Restricted.This is almost impossible to understand. I would get away from the restricted concept and go back to the old time approach of having an Operating Fund, an Endowment Fund, and a Property Fund. That would be much clearer to most readers. I encourage business people to send comments to the FASB on these matters.

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