



April 10, 2020

Technical Director, File Reference No. 2020-100
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VIA EMAIL
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**Re: National Association of State Charity Officials' Comments to FASB
Exposure Draft for Topic 958**

The Board of Directors of the National Association of State Charity Officials (NASCO)¹ hereby submits comments to FASB Exposure Draft for Topic 958 regarding Presentation and Disclosures by Not-for-Profit Entities for Contributed Nonfinancial Assets.² The NASCO Board appreciates the inclusion of NASCO representatives in the Working Group and the consideration of our concerns regarding the lack of transparency in the reporting of contributed nonfinancial assets (or “gift-in-kind donations”).

As we have expressed, while gift-in-kind programs can provide for the distribution of much-needed goods, NASCO and its member agencies are all too familiar with such programs being used to inflate an organization’s revenue and expenditures, and to manipulate its efficiency rating.

¹ NASCO is an association of state charities officials, including state Attorney General offices, Secretaries of State offices, and other state offices charged with preventing the misuse of charitable assets, ensuring that trustees of charitable trusts fulfill their fiduciary duties, and enabling donors to make informed choices about which charitable causes to support. This letter reflects the views of the NASCO board. It does not necessarily reflect the views of any individual Attorney General, Secretary of State, or other state official.

² Responses to questions posed by FASB in the Exposure Draft are appended hereto as Rider 1.

The NASCO Board believes that the FASB proposal as presented will promote awareness and examination of reporting of gift-in-kind donations; however, we are disappointed that FASB chose not take up the issue of proper valuation standards, particularly in the field of pharmaceutical donations. Our hope is that not only will the disclosures provide readers of the financial statements with important information, but that the disclosure requirements will increase auditor scrutiny of a client entity's gift-in-kind program, including valuation, donor restrictions, and consistency with the charitable mission of the organization. That said, proper valuation, not just disclosures, is essential in preventing the misuse of gift-in-kind programs. Additionally, as explained below, we also recommend an additional disclosure regarding discretion, a key factor in proper gift-in-kind recognition under existing FASB standards.

FASB is in a unique position to provide better guidance and clarity on the proper pricing inputs nonprofits should be using, particularly in the pharmaceutical arena. The nonprofit sector needs clear guidance on what methodology should be used for pharmaceutical donations. As such, for the reasons detailed below, we urge FASB to use this opportunity to provide such guidance, or at the least to continue to work towards a solution that will provide more guidance on the proper valuation of nonfinancial donations, particularly pharmaceutical donations.

Pervasive Misuse of GIK Valuation

NASCO member states and our federal partners have been endeavoring to combat the abuse of gift-in-kind programs through our enforcement authority. We have filed actions against nonprofits that inflate the value of their nonfinancial donations because such misrepresentations can result in false reporting to regulators and misleading statements to the donating public. In 2015, all fifty states and the Federal Trade Commission (FTC) filed a multistate action against Cancer Fund of America and its affiliated charity Breast Cancer Society. A significant part of the lawsuit arose out of the way these sham charities valued nonfinancial donations. For example, in 2012 and 2013, Breast Cancer Society reported receiving \$23 and \$21 million in pharmaceutical donations from World Assist, a public benefit corporation. To arrive at these valuations, Breast Cancer Society used U.S. prices. At the same time, World Assist reported that its grants to Breast Cancer Society were worth only \$127,362 and \$123,459.

California, Michigan and Minnesota have also filed multiple actions against nonprofits that have used gift-in-kind donations to confuse donors with their efficiency ratings.³ For example, in January 2019, California reached a settlement with a charity and its principals to resolve claims that the charity misled the public by falsely claiming that 99% of contributions went to provide direct aid, when in fact that percentage relied on the use of vastly inflated valuation of gift-in-

³ See, e.g.:

<https://www.ftc.gov/news-events/press-releases/2018/07/ftc-states-combat-fraudulent-charities-falsely-claim-help>.
<https://oag.ca.gov/sites/all/files/agweb/pdfs/charities/pdf/food-poor-inc-appeal-request-hearing.pdf>?
<https://oag.ca.gov/sites/all/files/agweb/pdfs/charities/pdf/decision-map-intl.pdf>?
<https://oag.ca.gov/sites/all/files/agweb/pdfs/charities/pdf/decision-catholic-med-mission-board.pdf>?
https://www.michigan.gov/ag/0,4534,7-359-82915_82919_80762-479605--,00.html

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kind donations of pharmaceuticals. As part of the settlement, the charity, directors, officers and accountant paid \$410,000 to be used for state charity enforcement, will stop providing misleading reports, and the charity agreed to end its pharmaceutical gift-in-kind program.⁴ In another matter litigated by California, the judge noted that using U.S. prices to value pharmaceuticals that are restricted to distribution and use outside the United States is “counterintuitive” and allows charities to appear artificially large.⁵

The problem of overvaluation of pharmaceuticals is not new. Forbes reported in 2011 that some U.S.-based nonprofits distributed deworming pills that could be bought on world markets in Europe, China and India for 2 cents each. Using U.S. prices, nonprofits reported values ranging from \$1.54 to \$16.25 per pill, whereas other nonprofits valued the same deworming bills at 2.6 to 3.2 cents. The Forbes noted that the 2-cent medicine becomes a \$16.25 pill because nonprofits reporting the higher amount are using the Average Wholesale Price or Red Book, which are prices supplied by the manufacturer and there is no requirement that they be accurate or even real. The defenders of these high values interviewed by Forbes, justified their actions by stating that accounting rules are “flexible, confusing and in flux.”⁶

FASB allows nonprofits to use the “principal market” in valuing an asset or the “most advantageous market” in the absence of a principal market. (FASB ASC 820-10-35-5.) However, nonprofit organizations are using multiple methods to arrive at the “principal market” or the “most advantageous market” for pharmaceutical donations. In fact, a publication by InterAction, the largest alliance of U.S. based international nongovernmental organizations, gives its membership wide latitude on how best to value pharmaceuticals with its Pharmaceutical Pricing Inputs Catalog. This Catalog lists nine different pricing sources that nonprofits can use for valuing pharmaceutical donations.⁷ While some nonprofits may be conservative in their approach and use the Federal Upper Limit or International Prices, others may opt to use the Wholesale Acquisition Cost (WAC), Average Wholesale Price (AWP) or Average Manufacturer Price (AMP), none of which includes rebates or discounts available to market participants, and AWP often reflects a 20 percent markup compared to WAC.⁸

Relatedly, any guidance regarding nonfinancial assets should incorporate the legal principle that donor restrictions follow the donated asset. In many cases, pharmaceutical companies make donations with the restriction that the pharmaceuticals may not be distributed in the United States. The inability to legally use pharmaceutical donations in the United States due to a donor restriction is a material fact that nonprofits should consider when valuing the asset. If the donation cannot be used in the United States and the recipient does not have access to the U.S.

⁴ <https://oag.ca.gov/news/press-releases/attorney-general-becerra-announces-410000-settlement-giving-children-hope-after>

⁵ <https://oag.ca.gov/sites/all/files/agweb/pdfs/charities/pdf/decision-food-for-the-poor.pdf>? at 13.

⁶ <https://www.forbes.com/sites/williamparrett/2011/11/30/donated-pills-makes-some-charities-look-too-good-on-paper/#52632e182cf9>.

⁷ <http://www.interaction.org/documents/interactions-pharmaceutical-recommended-methodology-decision-tree-and-pricing-inputs-catalog/>

⁸ See InterAction pricing inputs catalog.

market, then the United States should not be considered the principal market for valuation purposes.

If a nonprofit can increase efficiency rating by using the WAC or AMP, instead of the Federal Upper Limit or International Prices, this leads not only to unfair reporting of higher revenue and program expenses but also opens the door to donor deception. Donors deserve to know the fair value of nonfinancial assets based on the realities of the transaction, including any restrictions that may impact where the pharmaceutical donations are actually being used.

Allowing nonprofits wide latitude in valuing pharmaceutical donations also puts charities that predominantly rely on cash donations at a significant competitive disadvantage. The cash-based charities do not look as efficient on paper as the charities that have significant pharmaceutical programs.

In summary, FASB's failure to address the valuation methodology in its Accounting Standards will lead to inconsistent reporting by nonprofits depending on the different valuation approaches. As regulators we believe nonprofits should be transparent and accurate in their public filings and the values reported should be consistent and not inflated.

Disclosure is Necessary but not Sufficient

Additionally, while the proposed disclosure provisions are a marked improvement from the current opacity regarding gift in kind; disclosure alone is not sufficient when the information will not be provided by and available to all relevant stakeholders. Not all nonprofits provide financial statements to the public or even to regulators. Very few nonprofit organizations post their financial statements on their website but they are quick to report their efficiency ratios or their ratings which are often determined solely based on information gleaned from the nonprofit's IRS Form 990.

Even if the average donor were savvy enough to locate the financial statements, many donors will not be able to interpret the disclosures and how they impact the nonprofit's efficiency ratio or rating.

Discretion is Key

Finally, with respect to the proposed substance of the disclosures, NASCO suggests mandating an affirmative representation in the notes to the financial statements that the entity has discretion over the donated assets, a factor required for proper recognition of the transaction as a contribution under FASB standards. The recommendation arises out of the multiple instances we have seen in which entities serve merely as pass-throughs for donations but nevertheless (improperly) report them as gift-in-kind donations. There is consensus that this type of "daisy chain" arrangement, in which goods pass through several organizations, each of which records them as revenue and expenditures, is likely improper. Additional disclosure regarding discretion would hopefully increase auditor scrutiny and application of the existing inquiries in AICPA guidance.

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In summary, as state regulators, we are concerned about protecting donors from deceptive solicitation and reporting practices. When the value of nonfinancial assets is inflated, the nonprofit not only looks larger and more impactful, but inflated revenue and program services also leads to better efficiency ratings by organizations such as Charity Navigator which rely on the total revenue reported by the nonprofits. As such we urge FASB to provide additional guidance on valuations for nonfinancial donations.

We thank FASB for the opportunity to provide comments and to participate in the Working Group, and look forward to our continued collaboration.

Sincerely,

Yael Fuchs /s/

Yael Fuchs
President, NASCO

RIDER 1

Responses to questions posed by FASB on pages 2-3:

Question 1: Are the amendments in this proposed Update operable? If not, which proposed amendment or amendments pose operability issues and why?

Answer: Yes

Question 2: Should the scope of the presentation and disclosure requirements apply to all contributed nonfinancial assets? If not, what types of nonfinancial contributions should be excluded from the scope and why? Should the scope of the presentation and disclosure requirements be extended to business entities? If yes, why?

Answer: Yes to the first part of the question. No comment on whether it should be extended to other for-profit business entities.

Question 3: Should the disclosure requirements in paragraph 958-605-50-1A(c) be required for each category of contributed nonfinancial assets? If not, please explain why.

Answer: Yes

Question 4: Would retrospective application of the proposed amendments be operable and would that application provide decision-useful information? If not, please explain why and what would you recommend.

Answer: Yes

Question 5: How much time would be needed to adopt the proposed amendments? Should early adoption be permitted?

Answer: Adoption should be implemented early.

Question 6: Is education or implementation guidance needed on the valuation of contributed nonfinancial assets? If yes, what type of guidance or additional education should be developed.

Answer: Yes, FASB should play a role in providing guidance on the proper valuation of pharmaceutical donations, particularly if a donor restriction limits the donated goods from being used in the U.S.