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Mr. Russell G. Golden
Director of Technical Application and Implementation Activities
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

*FSPFAS117A*

LETTER OF COMMENT NO. 38

**File Reference: Proposed FSP FAS 117-a**

Dear Mr. Golden:

PricewaterhouseCoopers LLP appreciates the opportunity to respond to the guidance that the Financial Accounting Standards Board has proposed in FASB Staff Position No. FAS 117-a, *Endowments of Not-for-Profit Organizations: Net Asset Classification of Funds Subject to an Enacted Version of the Uniform Prudent Management of Institutional Funds Act, and Enhanced Disclosures.*

Overall, we support issuance of the proposed FSP. Our responses to the specific issues on which the Board is seeking comments are provided below.

**Question 1** – *Is the guidance for net asset classification of donor-restricted endowment funds for not-for-profit organizations subject to UPMIFA appropriate, and can it be applied consistently? If not, why not?*

We agree with the proposed FSP's overall conclusion that a not-for-profit organization subject to UPMIFA should classify as permanently restricted the portion of an endowment fund that is explicitly restricted in perpetuity by donor stipulation or by law. However, we believe that a variety of interpretations exist regarding the Board's intent with respect to restriction of net appreciation. Unless the Board's intent is clarified in the final FSP, we believe the FSP will be inconsistently applied. Specifically, we believe interpretations will vary about whether:

- new responsibilities are being placed upon governing boards to make legal interpretations;
- UPMIFA's "prudent spending" guidelines (which explicitly reference maintaining purchasing power) create a legal restriction on net appreciation; and
- different governing boards subject to the same state laws have latitude to interpret differently whether they believe that law imposes restrictions.

Similar concerns were addressed by the Board in its deliberations of FASB Statement No. 117. We believe that much of the current confusion could be alleviated by explicitly aligning the proposed FSP with the relevant guidance in FAS 117 and its Basis for Conclusions. For example, with respect to legal interpretations made by governing boards, it appears that the proposed FSP is simply re-affirming the baseline rule regarding restriction of net appreciation that was established by FAS 117. Paragraph 22 of FAS 117 states, in part:

> ...If the governing board determines that the relevant law requires the organization to retain permanently some portion of gains on investment assets of endowment funds, that amount shall be reported as an increase in permanently restricted net assets.

We believe the proposed FSP is consistent with that guidance and is not intended to impose any new responsibilities on governing boards to interpret the law in a different way. We recommend that a reference to FAS 117, paragraph 22 be made in the body of the final FSP to clarify that the FSP is re-affirming that guidance.

With respect to whether laws related to "prudent spending" of endowment assets create additional restrictions on net appreciation, we note that this also is explicitly discussed in FAS 117's Basis for Conclusions. Those discussions explain that the Board determined that a state's adoption of UMIFA's "prudent spending" standard did not in and of itself create legal limitations that, for accounting purposes, would impose a permanent restriction on net assets. Paragraph 128 of FAS 117 indicates that unless a state adopts explicit provisions that fix more exacting standards or impose a greater constriction than the standard of ordinary business care and prudence established under UMIFA (e.g., Rhode Island's requirement to adjust the historic dollar value of an endowment fund to reflect the change, if any, in the purchasing power of the historic dollar value), a restriction has not been created. This appears to be directly on point with respect to the current questions surrounding enactment of UPMIFA laws and, specifically, its revision of the "prudent spending" standard. Therefore, we suggest that the final FSP incorporate relevant portions of those discussions in FAS 117. In particular, we believe it is important for the FSP to explicitly acknowledge that unless a state has adopted explicit provisions that fix more exacting standards or impose a greater constriction than the standard of prudence as defined under UPMIFA, restrictions on net assets are not created by a state's adoption of UPMIFA.

With respect to whether governing boards have latitude to interpret the law differently, paragraph A5 of the proposed FSP clearly articulates the Board's intent: If the governing board determines that a portion of a donor-restricted endowment fund **must** be retained permanently in accordance with the relevant law (as opposed to being simply good organizational policy to retain a portion of appreciation; for example, to maintain the purchasing power of the gift), then a permanent restriction exists. The FASB appears to be clearly differentiating between a governing board's spending policy with respect to endowment management (including purchasing power), which does not create restrictions, and laws that explicitly do create restrictions. To reduce confusion, we suggest that this statement be moved from paragraph A5 into the "FASB Staff Position" section of the FSP.

One significant difference between the situations addressed by the proposed FSP and the situations existing when FAS 117 was issued, is that unlike UMIFA (which had significant legislative and interpretive history at that time), the UPMIFA laws are newly enacted. Therefore, it is not known what interpretations will arise in various states as a result of state attorney general interpretations, enforcement actions, case law, etc. The proposed FSP's statement that a governing board's interpretation of the relevant law should be consistent from year to year might be interpreted as meaning that an organization cannot change its initial legal interpretation. We suggest that the final FSP clarify that, as additional interpretations of state law arise, organizations should determine the impact and, if necessary, adjust the amounts determined to be permanently restricted.

**Question 2** – *Are the proposed disclosures about an organization's endowment funds needed, and do they provide sufficient transparency in the new UPMIFA environment? If not, please explain which disclosures are not needed or what additional disclosures are needed.*

We agree with the Board's decision to require additional disclosures to provide greater transparency, but suggest eliminating certain of the proposed disclosures. The first is the requirement in paragraph 12(d) to disclose the "cumulative amount of investment return, if any, contained in the permanently restricted net asset class because of the organization's interpretation of relevant law, beyond that required by explicit donor stipulations." We disagree with requiring disclosure of amounts based on these distinctions because we believe the disclosure will not provide useful information. For similar reasons, we believe the last sentence in paragraph 12(e) should be deleted.

Additionally, we suggest the Board delete the proposed disclosure of planned appropriation (paragraph 13). This disclosure relates to forward-looking information that is generally outside the scope of general-purpose external financial statements.

In addition, we suggest the Board delete the amounts displayed as "temporarily restricted board-designated funds" in the illustrative tabular disclosures in paragraph C4, as we are not aware of situations in which board-designated funds could be classified as temporarily restricted.

**Question 3** – *Do you agree with the Board's decision to require that organizations provide the additional disclosures even if they are not yet subject to a version of UPMIFA? If not, why not?*

We agree with the Board's decision to require all organizations to provide the additional disclosures.

**Question 4** – *Do you agree with the Board's decision to make the provisions of the FSP effective for fiscal years ending after June 15, 2008, with early application permitted as long as the organization has not previously issued annual financial statements for that fiscal year? If not, why not?*

We believe that the FSP should be effective for fiscal years ending on or after December 15, 2008, with early application permitted as long as the organization has not previously issued financial statements for that fiscal year. Given the diversity in interpretations that have arisen regarding the intent of the proposed FSP, a six-month delay in the effective date will provide additional time for organizations to evaluate and appropriately implement the provisions of the final FSP. In addition, a deferred effective date allows additional time for states to provide interpretive legal guidance.

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We appreciate the opportunity to express our views on this FSP. If you have any questions about our comments, please contact John Mattie (646-471-4253) or Martha Garner (973-236-7294).

Sincerely,

PricewaterhouseCoopers LLP