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Technical Director, FASB
File Reference No. 2015-230, FASB
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By email to director@fasb.org

Subject: *File Reference No. 2015-230*

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

We appreciate the opportunity to comment on the Proposed Accounting Standards Update on Presentation of Financial Statements of Not-For-Profit Entities, File Reference number 2015-230. CNA is a not-for-profit (NFP) Virginia-based corporation engaged in research and analysis and is the Federally Funded Research and Development Center (FFRDC) for the Navy and Marine Corps. With revenues exceeding $100 million, we have supported the Navy since 1942 in the areas of operations and systems analysis. We provide services primarily under cost reimbursable contracts and are subject to Federal Acquisition Regulations and Cost Accounting Standards, and audited under OMB Circular A-133 (revised "Uniform Guidance"). CNA has a complex accounting system designed for US Government contractors and which addresses various service centers, overhead pools, G&A allocations and other detailed complexities associated with doing cost reimbursable business with the US Government.

Although we are a not-for-profit, we do not have the characteristics associated with organizations soliciting charitable contributions. Accordingly, we do not have donor-imposed restrictions and we offer no opinion as to those proposed changes. We also do not support our current operations with investment income; therefore, our activities would all be operating activities (with the exception of realized/unrealized investment activity which is not material). As a result, we do not see any significant value for CNA in the proposed new model for the Statement of Activities.

We are concerned, however, with the proposed direct method for the cash flow statement for NFP organizations. Even though CNA agrees that the direct method is actually easier for the financial statement user to understand, we do not agree that the not-for-profit industry should be the first industry to be required to convert to the direct method. Furthermore, we have Trustees who serve or have served on both our board as well as the boards of for-profit entities and we think it would be confusing for Board members to see different types of cash flow statements. To the maximum extent possible, we support a common reporting framework for both for-profit and not-for-profit enterprises (taken to an extreme, the industries end up with specialized accounting talent which is not beneficial for the NFP enterprise or the individual).

Direct Method for Cash Flows:

Not-for-profit organizations have limited resources and the change to the direct method will require significant investment in system design and accounting architecture changes. This change will require a significant up-front investment, taking away available funds that should be used for programs which advance our mission. In addition, since we are a NFP government contractor we utilize an accounting platform primarily used by the for-profit government contractor community. Until the for-profit industry is required to report using the direct cash flow method (which will create sufficient demand), our accounting system software provider and associated consultants will require purchase of custom tool configuration and support versus development of a standard offering. CNA believes that any required change to the direct method should start with the for-profit industry since they have the people, processes, resources and ability to drive the systems changes in the industry. Given more limited scale and resources, the NFP organizations should follow, not lead, any implementation of the direct method of cash flows.

Information regarding liquidity:

CNA has neither donations nor limits on use of resources as described which may be common with NFPs soliciting charitable contributions. Also, CNA uses a classified balance sheet. Unique circumstances or characteristics should to the extent possible be addressed via footnotes rather than prescriptive designations for all NFPs. Accordingly, CNA agrees that providing more information regarding liquidity in the notes to the financial statements would be the most cost effective way to communicate any restrictions and the impact of these restrictions and how the organization manages liquidity. Although not-for-profit organizations can be difficult for creditors to understand, the footnote disclosure will allow the organization to disclose any restrictions on assets and their liquidity without imposing a significant burden. Furthermore, as a footnote, it will be subject to audit by the external accounting firm.

Adding intermediate measures:

Adding intermediate measures to assess operational performance may provide better insight for some NFP organizations, but our issues in presenting this information are related to other matters. Said differently, not all NFPs are alike. Since CNA is a NFP that is also subject to government contracting rules, the bigger impact in understanding our operational returns are the impacts of US GAAP required accounting entries (timing) that are non-reimbursable in our current allocation of costs. Items like the straight-line effect of deferred-rent create net asset (profit and loss) swings on the face of our financial statements as the US Government will only reimburse for the actual cash outlays for rent payments.

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These GAAP entries are included in the operating expenses and do not accurately reflect our actual performance from operations for the year. If the impact of these entries could be reflected in the "non-operating changes" on the Statement of Activities, it would allow our organization to more accurately reflect operational "income or loss" performance. We therefore think management judgment associated with classification of items as operating versus nonoperating is appropriate.

Reporting operating expenses by both function and nature:

CNA does not agree that reporting operating expenses by both function and nature is necessary in the financial statements. This information is already provided in the IRS Form 990 ("Return of Organization Exempt from Income Tax"). The return provides extensive information and descriptions of the programs. This information is available to all financial statement users and available for public review by any requestor. Repeating this information on the financial statements would just add unnecessary complexity to the financial statements without clear value to the reader. Since our primary reader is our Board of Trustees (again, we do not solicit charitable contributions), they are already receiving this information through the preview of the IRS Form 990 before it is filed.

Reporting of investment activity and internal salaries for investment activity:

CNA agrees that reporting net investment income will be an effective way of obtaining comparability of performance without adding costly and time consuming processes. However, CNA does not agree that disclosure of internal salaries and benefits for investing activities is particularly relevant. We use an outside advisor as co-fiduciary for investment management; therefore, internal salaries and benefits for investment activities are minimal (our Investment Subcommittee membership has 4 Board Trustees plus the CEO and CFO). This information would not be costly to obtain but would be immaterial and irrelevant to the readers of our financial statements.

Reporting of interest expense as an operating activity:

CNA agrees that interest expense should be included as a nonoperating activity. Since CNA is a NFP that is also subject to government contracting rules, interest expense is not an allowable cost. Therefore, it is not an allocable cost to our programs. Due to this fact, showing interest expense in the nonoperating changes section of the Statement of Activities is the best reflection of our performance.

Overall Summary:

We understand and appreciate the Board's objective to improve the usefulness of the information provided to the users of the not-for-profit financial statements while reducing the costs and complexity in financial reporting. However, there are two significant changes that are being proposed that do not meet this objective and would require significant investment by the NFP community to accomplish. Both the direct cash flow method and the operating expense disclosure by nature and function would require significant system design and programming changes. The change to the direct cash flow method could potentially require a significant redesign of our chart of accounts to capture the required information. NFP organizations do not have the influence on software providers and/or the resources available to be a leader in a required change to the direct cash flow method. NFP organizations should be allowed flexibility to use the indirect cash flow method until the for-profit industries have made such a change and it is more institutionalized in systems and processes from which the NFP community can benefit.

Thank you for your consideration of the comments discussed in this letter. If you have any comments or questions about our assessment of the proposed standard, please do not hesitate to contact me at 703-824-2022 or debuckd@cna.org . Our responses to the electronic Q&A feedback are below.

Sincerely,

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File Reference No. 2015-230

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

Questions for Respondents

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.)

N/A for CNA as we are a NFP organization performing research and analysis services primarily under US Government contracts.

2. Do you agree that the aggregated amount by which endowment funds are underwater should be classified within n*et assets with donor restrictions* rather than *net assets without donor restrictions*? If not, why? (See paragraph BC24.)

N/A for CNA

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

N/A for CNA

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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 an NFP'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.)

CNA has neither donations nor limits on use of resources as described which may be common with NFPs soliciting charitable contributions. Also, CNA uses a classified balance sheet. Unique circumstances or characteristics should to the extent possible be addressed via footnotes rather than prescriptive designations for all NFPs. Accordingly, CNA agrees that providing more information regarding liquidity in the notes to the financial statements would be the most cost effective way to communicate any restrictions and the impact of these restrictions and how the organization manages liquidity. Although not-for-profit organizations can be difficult for creditors to understand, the footnote disclosure will allow the organization to disclose any restrictions on assets and their liquidity without imposing a significant burden. Furthermore, as a footnote, it will be subject to audit by the external accounting firm.

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

N/A for CNA

Statement of Activities, Including Financial Performance

6. Do you agree that requiring intermediate measures of operations would provide users of NFP 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.)

Adding intermediate measures to assess operational performance may provide better insight for some NFP organizations but our issues in presenting this information are related to other matters. Since CNA is a NFP that is also subject to government contracting rules (a Federally Funded Research and Development Center – FFRDC) the bigger impact in understanding our operational returns are the impacts of GAAP required accounting entries (timing) that are non-reimbursable in our allocation of costs. Items like the straight-line effect of deferred-rent, cause large profit and loss swings on the face of our financial statements. These GAAP entries are included in the operating expenses and do not accurately reflect our actual performance from operations for the year. If the impact of these entries could be reflected in the "non-operating changes" on the Statement of Activities, it would allow our organization to more accurately reflect operational income or loss.

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 an NFP'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.)

CNA would like to re-iterate the comment from question 6. Since CNA is a NFP that is also subject to government contracting rules (a Federally Funded Research and Development Center – FFRDC) the bigger impact in understanding our operational returns are the impacts of GAAP required accounting entries (timing) that are non-reimbursable in our allocation of costs. Items like the straight-line effect of deferred-rent, cause large profit and loss swings on the face of our financial statements. These GAAP entries are included in the operating expenses and do not accurately reflect our actual performance from operations for the year. If the impact of these entries could be reflected in the "non-operating changes" on the Statement of Activities, it would allow our organization to more accurately reflect operational inflows and outflows.

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

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

N/A for CNA

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.)

N/A for CNA

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, an NFP 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.)

N/A for CNA

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

N/A for CNA

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?

N/A for CNA

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 an NFP uses its resources and, thus, should be required? Why or why not? (See paragraphs BC87–BC93.)

CNA does not agree that reporting operating expenses by both function and nature is necessary in the financial statements. This information is already provided in the IRS Form 990 ("Return of Organization Exempt from Income Tax"). The return provides extensive information and descriptions of the programs. This information is available to all financial statement users and available for public review by any requestor. Repeating this information on the financial statements would just add unnecessary complexity to the financial statements without clear value to the reader. Since our primary reader is our Board of Trustees (we do not solicit charitable contributions), they are already receiving this information through the preview of the IRS Form 990 before it is filed.

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.)

CNA agrees that reporting net investment income will be an effective way of obtaining comparability of performance without adding costly and time consuming processes.

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.)

CNA does not agree that disclosure of internal salaries and benefits for investing activities is particularly relevant. We us an outside advisor as co-fiduciary for investment management; therefore, internal salaries and benefits for investment activities are minimal. This information would not be costly to obtain but would be immaterial and irrelevant to the readers of our financial statements.

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 an NFP's purposes and, thus, should not be classified as operating activities? If not, why? (See paragraphs BC59–BC60.)

CNA agrees that interest expense should not be included as an operating activity. Since CNA is a NFP that is also subject to government contracting rules (a Federally Funded Research and Development Center – FFRDC), interest expense is not an allowable cost. Therefore, it is not an allocable cost to our programs. Due to this fact, showing interest expense in the non-operating changes section of the Statement of Activities is the best reflection of CNA's performance.

17. Do you agree with the following implementation guidance:

a. Equity transfers between NFPs 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).)

N/A for CNA

b. Immediate writeoffs of goodwill generally should be presented within operating activities? If not, why? (See paragraph BC62(b).)

N/A for CNA

c. Immediate writeoffs 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).)

N/A for CNA

Statement of Cash Flows, Including Financial Performance

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.)

CNA agrees that the direct method is actually easier to understand. However, we do not agree that the not-for-profit industry should be the first industry to be required to convert to the direct method.

Not-for-profit organizations have limited resources and the change to the direct method will require significant investment in system design and accounting architecture changes. This change will require a significant up-front investment, taking away available funds that should be used for programs which advance our mission. In addition, since we are a NFP government contractor we utilize an accounting platform primarily used by the for-profit government contractor community. Until the for-profit industry is required to report using the direct cash flow method (which will create sufficient demand), our accounting system software provider and associated consultants will require purchase of custom tool configuration and support versus development of a standard offering. CNA believes that any required change to the direct method should start with the for-profit industry since they have the people, processes, resources and ability to drive the systems changes in the industry. Given more limited scale and resources, the NFP organizations should follow, not lead, any implementation of the direct method of cash flows.

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.)

As indicated in our response to Question 18, CNA's issue with requiring the direct cash flow method is the NFP industry leading this change. Use of the indirect method is not always intuitive but it is the predominant method designed in systems and charts of account.

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.)

In general, CNA supports alignment across the financial statements to enable meaningful use by the user. However, making changes to the current institutionalization in systems and processes of current methodologies is not to be taken lightly, particularly for NFP entities which are unlikely to have the scale or resources to execute the changes without adversely impacting funds available for their mission.

Effective Date

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.

The two changes that would require additional time to implement would be the direct cash flows and the operating expense disclosure by nature and function. Both of these changes would require significant system design and programming changes. The change to the direct cash flow method could potentially require a significant redesign of our chart of accounts to capture the required information.

22. Are there reasons for any particular size or type of NFP to need a longer time frame to implement the proposed amendments in this Update? If so, please explain.

While the proposed changes are likely to impact the entire industry, we expect size and scale matter with respect to resources. Similarly, a $500 million US domestic NFP on a single accounting platform will have an easier transition than a global $500 million NFP using multiple accounting platforms across the globe with a separate consolidation tool for financial reporting.

Other Comments on the Proposed Update

CNA appreciates the opportunity to comment and welcomes FASB's outreach programs including the use of roundtables.

Electronic Feedback Process Comments