The Association of Accountants and Financial Professionals in Business

July 27, 2015

Ms. Susan M. Cosper, Technical Director
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: File Reference No. 2015-230, Exposure Draft of Proposed Accounting Standards Update (ASU), *Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954), Presentation of Financial Statements of Not-for-Profit Entities*

Dear Ms. Cosper:

The Institute of Management Accountants (IMA), its Financial Reporting Committee (FRC) and its Small Business Financial and Regulatory Affairs Committee (SBFRC) are writing to share their views on the Financial Accounting Standards Board's (Board or FASB) Exposure Draft of Proposed ASU – *Not-for-Profit Entities (Topic 958) and Health Care Entities (Topic 954), Presentation of Financial Statements of Not-for-Profit Entities* (ED or Proposal).

The IMA is a global association representing over 75,000 accountants and finance team professionals. Our members work inside organizations of various sizes, industries and types, including manufacturing and services, public and private enterprises, not-for-profit organizations, academic institutions, government entities and multinational corporations. The IMA is a Section 501(c)(3) not-for-profit organization that presents its financial statements in accordance with Statement of Financial Accounting Standards (SFAS) No. 117 (Topic 958-205).

The FRC is the financial reporting technical committee of the IMA. The committee includes preparers of financial statements for some of the largest companies in the world, representatives from the world's largest accounting firms, valuation experts, accounting consultants, academics and analysts. The FRC reviews and responds to research studies, statements, pronouncements, pending legislation, proposals and other documents issued by domestic and international agencies and organizations.

The SBFRC addresses issues that impact small and medium-sized organizations. On behalf of IMA's members and all accounting professionals working within these organizations, SBFRC engages and suggests solutions to standard-setters and regulatory agencies such as the Financial Accounting Standards Board, Securities and Exchange Commission, International Accounting Standards Board, Small Business Administration, American Banking Association, Internal Revenue Service and others.

Additional information on the IMA can be found at www.imanet.org (information on both committees can be found in the Advocacy Activity section under the About IMA tab).

Overview

In general, we support efforts by the FASB to improve the fundamental financial reporting model for not-for-profit organizations (NFPs). As noted above, the IMA is a not-for-profit organization and

The Association of Accountants and Financial Professionals in Business

prepares its financial statements on that basis. In addition, several of the members of our committees participate as board members or volunteers for NFPs so we recognize the importance of these organizations having credible financial reports. Such reporting is vital for fund raising purposes, for certain compliance reporting, to inform members, and to provide useful information to board members overseeing activities, among other reasons. As noted, the fundamental financial reporting model for not-for-profit organizations was established by the FASB more than twenty years ago and it is certainly due for a fresh look.

A basic premise of the current GAAP for NFPs (SFAS No. 117) was that "Its requirements generally are no more stringent than requirements for business enterprises" (paragraph 7). This was reinforced in the Benefits and Costs section of the Basis for Conclusions with the statement, "The Board also believes that some of the costs this Statement imposes have been reduced in various ways: by limiting the provisions of this Statement to requirements that are generally no more stringent than those for business enterprises …." (paragraph 40). And in the Framework for Considering Issues on Financial Statement Display section of the Basis, "It concluded that the reporting standards in this Statement generally should focus on information that is essential in meeting the financial reporting objectives applicable to all not-for-profit organizations and should be no more stringent than requirements for business enterprises." Much the same as our support for there being no GAAP recognition and measurement differences between smaller and larger companies, we support this approach of having not-for-profit entities follow the accounting for business entities unless there are compelling reasons to do otherwise, such as different economic circumstances.

However, as noted in the Alternative Views of the ED, in certain major respects the Proposal would require changes for not-for-profit entities in areas for which the related accounting for businesses is either under active study (reporting an "operating" performance measure) or well established (cash flow reporting). We continue to support the SFAS No. 117 approach for these matters and do not believe the matters in question represent an improvement as further explained below.

Support

The FASB's News Release highlights five major improvements to the fundamental financial reporting model for NFPs and we support the following three of those improvements.

- Simplifying the existing net asset classification scheme by reducing it from three to two categories and enhancing related note disclosures.
- Making information about expenses more comparable and useful by requiring that all operating expenses be reported by both function and nature and investment return be reported net of related expenses.
- Enhancing information in the notes about liquidity, although we do not agree with one of the specific proposals.

However, as noted above, we do not agree with proposals dealing with measures of operating performance or with changes to cash flow reporting. Those matters are discussed in the next sections.

The Association of Accountants and Financial Professionals in Business

Measures of operating performance

The FASB's News Release states that the ED's proposed requirements in this area are intended to "Better reflect financial performance in the statement of activities by showing – in two measures of operating performance – available amounts that have been generated by or directed at carrying out the mission of a not-for-profit in the current period, both before and after any governing board actions affecting that availability." This was a topic actively debated when SFAS No. 117 was issued and, according to SFAS No. 117, "Present standards neither require nor preclude a business enterprise from classifying its revenues, expenses, gains and losses in that way, and the Board found no compelling reason to prescribe more specific display standards for not-for-profit organizations" (paragraph 67). Over time the FASB has considered whether to propose additional standards for business enterprises on this topic and, in fact, presently has an active project on its research agenda on Financial Performance Reporting. We note that, while there have been recent Board meetings on this project, it was added to the agenda in 2001.

We agree with the Alternative Views that given an active and ongoing project to address the same issues for business enterprises, it would be at best premature to require new accounting for NFPs. There would be a considerable likelihood of establishing different conclusions when evidence may suggest an aligned approach is warranted. We noted with favor paragraph BC20 that states in part that the Board "… is committed to considering the interaction of the projects before proceeding to finalize the proposed guidance for NFPs." We hope that this means the Board will not take a final position on the matter in the NFP project until it has made a similar final decision for business enterprises.

We further agree with the Alternative Views with respect to reporting an operating measure that reflects internally imposed limits. This would seem to provide the opportunity for an entity to determine what it wishes to report as its "bottom line" of the operating statement through equity transfers. That is inconsistent with our notion of how "operations" should be defined and also leads to reduced credibility of financial reporting overall.

Cash flow reporting

We disagree with the proposed requirement that NFPs should use the direct method of reporting operating cash flows. Again, we agree with the Board's approach to this issue in SFAS No. 117 to allow NFPs the same flexibility as business enterprises in reporting operating cash flows. Further, we agree with the Alternative Views "… that the indirect method can provide a useful link between the statement of cash flows, the statement of activities, and the statement of financial position, which is a benefit that could be eliminated by the proposed Update."

The Board argues (BC77-78) that developing information for the direct method of reporting operating cash flows should not involve significant costs as that has been the experience of governmental colleges and universities required to adopt that method. And the Board states that most private colleges and universities as well as other NFPs which voluntarily adopted that method, have had similar experiences. Further, the Board notes that NFPs generally are different than business enterprises in that (1) they do not have foreign translation issues, (2) they do not engage in significant M&A activities, and (3) they are not subject to accelerated SEC filing deadlines.

The Association of Accountants and Financial Professionals in Business

Notwithstanding those arguments, we believe that most NFPs that prepare GAAP financial statements keep their accounting records on an accrual basis and would need to make significant changes to current systems to comply with a direct method of reporting operating cash flows requirement. Specifically, IMA financial statements include a statement of cash flows using the indirect method, which is prepared in a relatively straight-forward basis from its general ledger accounts. Reporting under the direct method for operating cash flows would necessitate new systems to separate and aggregate cash transactions in a way that is not used for management reporting or other purposes. We believe the users of IMA's financial statements would receive little, if any, incremental benefits from having this direct method information. Further, we believe many informed readers of IMA's financial statements are accustomed to reading financial statements of business enterprises and would see no significant advantage in having the cash flow statement presented in a different format.

In addition to the proposal to change the format of reporting operating cash flows, the ED would require a number of changes in how particular cash inflows or outflows are reported to be more compatible with the mission dimension of the proposed intermediate measures of operations. More specifically, the ED proposes the following.

- Purchases of long-lived assets, contributions restricted to acquire long-lived assets, and sales of long-lived assets classified as operating rather than investing cash flows.
- Payments of interest on borrowings classified as financing rather than operating cash flows.
- Receipts of interest on loans and dividends on investments other than those made for programmatic purposes classified as investing rather than operating cash flows.

There is a certain amount of logic to each of these proposals but the Board debated the major points in great detail when developing SFAS No. 95, the original pronouncement requiring the statement of cash flows for business enterprises. Reasonable arguments can be (and were) made for both the original classification required for each of these cash flows and the classification now being proposed. We see no economic reason for having such differences in the reporting between NFPs and business enterprises and, therefore, do not support these changes. Further, we agree with the Alternative Views that the proposed changes fail to fully achieve the suggested alignment between the intermediate measures of operations and reporting of cash flows from operations.

As noted earlier, the IMA is a NFP organization and several of the members of the committees participate as Board members or Trustees for NFPs. And those who do not are commonly solicited for donations by NFPs. In reading the financial statements for these entities, it is easier and better facilitates understanding to see cash flow information in the same customary format as business enterprises.

Liquidity

According to the Board's News Release, one of the major objectives of the ED is to, "Enhance information in the notes to help financial statement users better assess a not-for-profit's liquidity and how it is being managed." In the Basis for Conclusions, the Board notes that some of the possible liquidity information is of a type that would go beyond the boundaries of financial reporting and generally is only provided outside of audited financial statements. Given that caveat, the ED proposes the following four disclosures about liquidity.

The Association of Accountants and Financial Professionals in Business

- The amount of financial assets at the end of the period.
- The amount, because of limitations, that is not available to meet cash needs in the near term.
- The amount of financial liabilities that require cash in the near term.
- The way an entity manages its liquidity, including the time horizon it uses in its management of liquidity.

We concur that improved information about a NFP's liquidity would be a useful change to the fundamental financial reporting model. The first three items listed above would assist in meeting that objective and are relatively straight forward. For the most part, we believe that NFPs would have little difficulty in developing the information and it would be beneficial to users. However, we do not support the last item.

First, we believe that the way in which an entity manages its liquidity goes well beyond the boundaries of financial reporting and, thus, fails the FASB's apparent limitation mentioned above. Second, the information is normally of a confidential nature that an entity does not wish to share with those outside the organization for many reasons. Finally, the many different ways in which this could be reported is likely to lead to little or no comparability from entity to entity. And that variability would almost certainly add to audit costs as well. In summary, there are many reasons why this particular proposed disclosure fails a cost/benefit test.

Other matters

Paragraph BC62b under Operating Activities states the following.

> "Goodwill write-offs upon an acquisition of an entity − For similar reasons, the Board decided to require presentation of the immediate write-off of goodwill within the operating activity section. That write-off is, for cost-benefit reasons, required when an NFP acquires another entity and the operations of the acquiree as part of the combined entity are expected to be supported predominately by contributions and returns on investments. Under those circumstances, the Board believes it is reasonable to assume that the purpose of acquiring the entity is to carry out the NFP's purpose for existence. Thus, although the write-off is an accounting accommodation rather than a current-period expense, it is a current-period event − an acquisition − that generally is undertaken to further the NFP's mission."

As stated in the April 17, 2015 letter from the FRC regarding the Three-Year Review of the Private Company Council, the FRC believes that there should be no differences between recognition and measurement differences for private and public companies. In particular, we believe that:

- differences in core recognition and measurement underpinnings dilute GAAP and
- public and private companies should not have different accounting for the same economic transactions.

We believe this same reasoning applies to the immediate write-off of goodwill as a practical "accounting accommodation" in appropriate circumstances. We recognize that NFP organizations often have fewer and less sophisticated accounting resources so an accommodation makes more sense for those

The Association of Accountants and Financial Professionals in Business

organizations. We trust this accommodation is debated as part of the Accounting for Goodwill for Public Entities and Not-for-Profit Entities project and believe that no changes should be made to SFAS No. 117 regarding the classification of the write-off in this Proposal.

We noted that on page 1 of the ED in describing why the FASB is issuing this Proposal, the first sentence states, "The FASB added a project to its agenda to improve the current net asset classification requirements and the information presented in financial statements and notes about a not-for-profit entity's liquidity, financial performance, and cash flows." Concepts Statement No. 4, Objectives of Financial Reporting by Nonbusiness Organizations, includes the following statement, "Financial reporting should provide information about the economic resources, obligations, and net resources of an organization and the effects of transactions, events, and circumstances that change resources and interests in those resources." In comparing those two statements, we note that the former is broader, particularly with respect to liquidity and cash flows. However, we could not find any comment in the current ED about balance sheet information (economic resources, obligations, etc.). We are sure that this was not a deliberate exclusion but suggest that in any final standard the Board be clear about the matter.

****

We would be pleased to discuss our comments with the Board or the FASB staff at your convenience.

Sincerely,

Jeffrey C. Thomson

Jeffrey C. Thomson, CMA, CAE
President and CEO
Institute of Management Accountants
jthomson@imanet.org

Schroeder

Nancy J. Schroeder, CPA
Chair, Financial Reporting Committee
Institute of Management Accountants
nancy@beaconfinancialconsulting.com

Gerald S. Silberstein

Gerald S. Silberstein, PhD, CPA, MBA, CMA
Chair, Small Business Financial and Regulatory Affairs Committee
Institute of Management Accountants
silbeg@sage.edu