



August 14, 2015

Technical Director
File Reference No. 2015-230
Financial Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Re: Project 2015-230 – Presentation of Financial Statements of Not-for-Profit Entities

To Whom It May Concern,

Heffler, Radetich & Saitta, LLP is pleased to have the opportunity to comment on the *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*. As a regional public accounting firm based in Philadelphia, Pennsylvania, the firm has been providing audit, tax and consulting services for over 72 years, primarily within the not-for-profit, government and quasi-government industry sectors. Given our firm experience and background in these industries, we felt compelled to not only present our views on the aforementioned Exposure Draft, but to also solicit input from key stakeholders (primarily Chief Financial Officers and Controllers) within the non-profit industry in the Greater Philadelphia area. As a result, we have included their views and commentary herein.

As you will note below, commentary has been provided only to the questions that were of interest to our firm and the key stakeholders solicited.

QUESTIONS AND COMMENTS

Statement of Financial Position and Liquidity

- Question 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).

Response: We are in favor of this change in reporting the classes of net assets, but note that there will be less transparency on the face of the statement of financial position regarding the amount required to be held in perpetuity under this change. This lack of transparency may negatively impact non-profit entities in the analytical evaluation of the long term financial health of the entity often conducted by third party users (e.g. financial institutions and donors) of the financial statements. While the details regarding how and when the net asset resources can be used will be disclosed, many third party users do not necessarily read and understand the corresponding footnote disclosures. Further, it is suggested that the Board consider additional disclosures regarding spending “with donor restricted funds” (formerly, permanently restricted funds) when an entity is dissolved.

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

Response: We are in agreement with this treatment of underwater endowment funds. Ironically, UPMIFA has not been adopted in the Commonwealth of Pennsylvania, and thus the requirement to transfer the underwater amount to unrestricted net assets does not exist; however, many non-profit entities in the greater Philadelphia, PA area follow the general guidelines of UPMIFA as a “best practice”. With the issuance of the final FASB technical pronouncement, it will be a pleasure to have more authoritative guidance in this area that will require uniform application regardless of the location of the non-profit entity.

- Question 3:** Do you agree that disclosures describing the NFP’s policy on spending from underwater endowment funds, together with the aggregated original gift amount of the amount that is required to be maintained by the donor and 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)

Response: We are in agreement with this disclosure requirement. We believe that external users will be able to understand the organization’s liquidity more clearly with the expanded disclosure. As mentioned previously, we suggest that the Board consider additional disclosure requirements regarding spending donor restricted funds in preparation for the dissolution of an entity.

- Question 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)

Response: We understand the intent of the liquidity disclosures; however, we do not find the quantitative measure disclosure requirement to be useful. Given the time horizon suggested of 30, 60 or 90 days (90 days being the maximum) and in consideration of the report issuance date of many not-for-profit entities, the content of the disclosure even at the maximum time horizon of 90 days could be stale to third party users. Gathering this additional information would be time consuming and somewhat repetitive, since many not-for-profit entities present classified statements of financial position. The qualitative liquidity disclosure requirement appears to be valuable to all readers of the financial statements and provide decision useful information.

Question 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?

Response: No comment.

Statement of Activities, including Financial Performance

- Question 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 BC-38-BC47)

Response: We are not in agreement with this change and do not believe that mandating the use of the operating and non-operating categories on the statement of activities is useful, especially for the not-for-profit sector. Our concern is that the operating measures as defined may not accurately reflect the not-for-profit's stewardship of resources. Also, users of the financial statements may tend to focus more attention on one measure than on both measures.

Question 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 the internal governing board appropriations, designations, and similar actions? If not, why? (See paragraphs BC-48-BC74)

Response: Although we are not in favor of the requirement of an intermediate measure of operations on the statement of activities, we are in agreement with the definition of the intermediate measure of operations as stated above. Providing a clear definition of operating and non-operating activities is paramount to this requirement since the measure of operations will depend on each specific not-for-profit's business. For example, in the current guidance it is unclear as to whether the earnings from certain program related investment earnings from with donor restricted funds should be included in operating or non-operating activities. Another topic that appears vague in the Exposure Draft is the placement of the reclassification of net assets category. The Exposure Draft as written suggests that all reclassifications should be shown as operating items; however, there may be certain transactions that do not have purpose restrictions (i.e. not meeting the mission dimension) that are considered reclassifications. Transactions of this type appear to be included within the transfer category, which we are not in agreement with (see response to Question #8).

- Question 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 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 would 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).

Response: We are not in agreement with the additional category of transfers on the face of the statement of activities. We believe that transfers overall would distort the information presented, may be misunderstood by users of the financial statements and could present a situation for the financial statement amounts to be easily manipulated. From an auditors' perspective, these transactions would be quite challenging to audit and overall we do not believe that this new category will add any value to the users of the financial statements. As such, documentation related to these transactions would need to be maintained in sufficient detail as support for their financial reporting treatment. We also believe that aggregating the information in this way would require major accounting software changes to accommodate the new financial reporting model.

Question 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).

Response: We are in agreement with the proposed changes outlined and these changes appear to be consistent with the intermediate measure of operations.

- Question 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)

Response: We are in agreement with the proposed changes; however, the changes need to be defined more clearly (including more expansive examples) in the final technical pronouncement.

- Question 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)

Response: No comment.

- Question 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?

Response: We believe that the single column format of the statement of activities presentation should be phased out as this is no longer used by most of the not-for-profit entities that we serve or were polled in providing this commentary on the Exposure Draft. The multicolumn format, single statement should be the only presentation maintained prospectively.

- Question 13:** Do you agree that reporting operating expenses by both their function and nature together with an analysis or 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 paragraph BC87-BC93).

Response: We agree with reporting operating expenses by both their function and nature together provides relevant and useful information. Although, not currently required, many not-for-profit entities that we serve or that were polled for purposes of this commentary practice this type of reporting.

- Question 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)

Response: We agree; however the guidance is vague and does not seem to consider how alternative investments (e.g. partnerships, etc.) should be treated under this scenario.

- Question 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)

Response: We agree with the disclosure requirement.

- Question 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 in operating activities? If not, why? (See paragraphs BC59-BC60).

Response: We agree with this proposed change.

- Question 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)).
 - b) Immediate write-offs of goodwill generally should be presented within operating activities? (See paragraph BC62 (b)).
 - c) Immediate write-offs of acquisitions of non-capitalized 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)).

Response: No comment. The transactions outlined above are not frequent in nature and therefore we did not deem these a critical part of our review and related feedback.

Statement of Cash Flows, Including Financial Performance

- Question 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).

Response: We do not agree with the change to require the direct method of cash flows financial statement presentation. We believe that the costs will far outweigh the benefits of making this financial statement presentation change. While we believe the direct method cash flow aligns operating cash flows with measures of operations in the statement of activities, this method will not prove to be more useful to external users and it will not be more understandable. Further, this method differs significantly from the statement of cash flows prepared by for-profit entities, and as a result would prove to be confusing to external third party users of the financial statement, especially lending institutions. We also believe that the changes in classification introduced by the direct method will more likely reflect negatively on a typical not-for-profit entity's operation and cause the total operating activities to reflect cash "used in" instead of cash "provided by" operating activities (a more favorable indicator).

- Question 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).

Response: We recommend that the current indirect method of cash flow presentation remain in practice, reconciling to the overall change in net assets.

- Question 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).

Response: While we believe the direct method of cash flows aligns operating cash flows with measures of operations in the statement of activities, this method will not prove to be more useful to external users and it will not be more understandable. See our previous comments regarding the statement of activities recommendations.

Effective Date

- Question 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.

Response: We believe that more time will be needed for the restatement of the prior period financial statements. We propose that a single statement should be used in the year of implementation. In general, management of not-for-profit entities request adequate lead time before the final pronouncement becomes effective.

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

Response: We believe that the smaller NFPs will need more time to implement the final pronouncement given the number of proposed changes and the proposed retroactive implementation. We also believe that consideration should be given to the companies who provide accounting software systems to allow time to update accounting software packages for these changes.

We appreciate your attention to the commentary provided herein and we look forward to the distribution of the revised Exposure Draft document.

Very Truly Yours,

