

FASB Understanding Costs and Benefits

ASU: Presentation of Financial Statements of Not-for-Profit Entities (Topic 958)

This document summarizes how the Financial Accounting Standards Board (FASB) considered the expected benefits and costs of its new Accounting Standards Update (ASU) No. 2016-14, *Presentation of Financial Statements of Not-for-Profit Entities (Topic 958)*, and the process the FASB undertook in concluding that the expected benefits of the amendments in the ASU justify the anticipated costs.

The FASB concluded that the expected benefits of the amendments in this ASU justify the anticipated costs.

The FASB issues new financial accounting and reporting standards only when the benefits of a standard—which include improvements in the relevance and neutrality of reported financial information—justify the costs it imposes on financial statement preparers to implement the new standard, and on users to consider and respond to the new information.

The FASB concluded that the expected benefits of the amendments in this ASU justify the anticipated costs.

The new standard responds to a need for improvement in several areas of not-for-profit financial reporting including:

- The current net asset classification scheme, and
- Information provided in financial statements and notes about an

organization's liquidity, financial performance, and cash flows.

To address these areas, the new standard will improve how not-for-profits communicate their financial performance and condition to stakeholders, while also reducing certain costs and complexities in preparing financial statements.

While not-for-profits are likely to incur some costs associated with implementing the new requirements, those costs generally are not expected to be significant. Not-for-profits applying the new standard will be able to leverage many of their existing financial reporting processes, reducing costs associated with implementing it. Many requirements in the new standard are already permitted under current Generally Accepted Accounting Principles (GAAP), and the FASB has sought to minimize the cost of implementation and complexity based on preparer feedback. Additionally, the new requirements will provide users of not-for-profit financial statements with more useful information about a not-for-profit's availability of resources, liquidity and financial flexibility, and financial performance.

Not-for-profit organizations that will be affected include charities, foundations, colleges and universities, health care providers, religious organizations, trade associations, and cultural institutions, among others.

The ASU on not-for-profit financial reporting will take effect for most not-for-profits for their fiscal years

beginning in 2018. Early application will be permitted.

Background

The current reporting guidance in Topic 958 (Not-for-Profit Entities) was established in 1993 when the Board issued FASB Statement No. 117, *Financial Statements of Not-for-Profit Organizations*. While the FASB believes the financial reporting model established in Statement 117 is still sound, stakeholders expressed concerns that several areas needed to be revisited and improved.

The FASB's Not-for-Profit Advisory Committee (NAC) was established in 2009 to ensure that the perspectives from the not-for-profit sector are effectively communicated to the FASB on a timely basis in connection with the development of financial accounting and reporting guidance. The NAC consists of 18 current members (and 3 participating observers) who are active in and have experience with not-for-profits, including preparers, auditors, and users of financial statements.

In 2011, the FASB added the Not-for-Profit Financial Reporting project to its agenda as a result of recommendations from the NAC. The project's objectives encompassed

suggestions from the NAC as well as specific financial reporting suggestions received from other stakeholders.

In April 2015, the FASB issued for public comment the Exposure Draft, *Presentation of Financial Statements of Not-for-Profit Entities*. As a result of the feedback received on the Exposure Draft, the Board decided to split the redeliberations on the project into two phases. The issuance of this standard is the culmination of Phase 1.

The main objective of the new standard is to improve presentation and disclosures to help not-for-profits provide more relevant information about their resources (and the changes in those resources) to donors, grantors, creditors, and other users.

These include qualitative and quantitative requirements in the following areas:

- Net Asset Classes
- Investment Return
- Expenses

- Liquidity and Availability of Resources
- Presentation of Operating Cash Flows.

Outreach with Stakeholders

Since the project's inception in 2011, the FASB has requested and received significant input from stakeholders on the application of the proposed guidance. This input includes stakeholder responses to the proposed amendments in the 2015 Exposure Draft as well as public roundtables, workshops, and other outreach meetings. When developing the guidance in the new ASU, the FASB participated in extensive outreach activities and received significant input from a wide variety of stakeholders (including users, practitioners, preparers, academics, and others).

The Board also consulted with the NAC on a semi-annual basis throughout the development of the new ASU. NAC members provided valuable feedback on the operability and usefulness of many of the new requirements.

Considerable outreach was performed throughout all stages of the project. Throughout redeliberations, the Board addressed stakeholders' concerns about implementation and audit costs while still achieving many of the project's objectives for improving financial reporting for not-for-profits.

Stakeholder Concerns

The new ASU addresses many of the concerns raised by stakeholders about the costs and complexity of the proposal in the 2015 Exposure Draft.

Largely in response to those concerns, the Board:

- Divided the redeliberations of the project into two phases, leaving for Phase 2 certain issues that are more challenging and potentially path-dependent on a related research project on financial performance reporting by business entities.
- Modified the proposed disclosures on liquidity and availability of resources to address stakeholder concerns about the lack of comparability of some of the information and the difficulty in providing or auditing it
- Decided to continue to allow an option to use either the direct method and the indirect method of reporting operating cash flows, as opposed to mandating the direct method
- Provided relief for transition costs in implementing the new standard by allowing certain new requirements to be omitted in the comparative financial statements in the year of adoption.



Costs: Applying the New ASU

The FASB understands that some reporting organizations will incur additional costs as a result of the new ASU. For example, not-for-profits may need to gather and/or obtain incremental data relevant to the new disclosure requirements as well as consider any incremental effects the new presentation requirements will have on financial reporting processes and controls. Not-for-profits may also incur costs in explaining to users the effects of the changes in the presentation of financial statements.

Costs of Applying the New ASU

- Costs to obtain incremental data relevant to new disclosures
- Costs to consider effects on financial reporting processes and controls
- Costs in explaining to users the effects of the changes

However, although the new ASU adds and modifies certain presentation and disclosure requirements (potential cost increases), other current requirements are being streamlined or eliminated under the new ASU (potential cost savings). Once implementation activities related to the new ASU are complete and a not-for-profit's processes have been fully updated, the ongoing incremental costs for most not-for-profits of preparing financial statements under the new ASU are likely to be insignificant.

Benefits: Applying the New ASU

The FASB observed that the new ASU will provide benefits to users of not-for-profit financial statements by increasing the transparency and usefulness of information, as well as by promoting comparability. More specifically, the new ASU accomplishes the following:

- Better allows a not-for-profit to “tell its story” through flexibility in the new requirements
- Results in reduced cost and complexity for preparers in relation to net asset classification
- Provides users with more relevant information about how both externally and internally imposed limits on resources affect the availability of those resources
- Results in better comparability across organizations in reporting of expenses and investment return
- Provides users with more transparent information about a not-for-profit's service efforts and ability to continue providing services
- Reduces costs for those not-for-profits that choose to present the direct method of operating cash flows by eliminating the requirement of an indirect reconciliation.

Benefits of Applying the New ASU

- Reduces cost and complexity for preparers in classifying net assets
- Provides more relevant information about how imposed limits on resources affect availability of those resources
- Results in better comparability across preparers in reporting expenses and investment return
- Provides more transparency about a preparer's service efforts and ability to continue providing services
- Reduces costs for preparers that choose to present the direct method of operating cash flows

Conclusion

The FASB's assessment of the costs and benefits of issuing this ASU is unavoidably more qualitative than quantitative because there is no identified method to objectively quantify all costs to implement the new guidance or to quantify the value of improved information in financial statements.

Overall, the FASB concluded that the expected benefits of the amendments in the new ASU justify the anticipated costs.

More information on the ASU, including a press release, *FASB In Focus*, and a video, can be found on the FASB website.