April 2, 2015

Get Ready - Changes Ahead for Not-for-Profit Financial Reporting

AUDIT, NOT-FOR-PROFIT
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As we have written before, the Financial Accounting Standards Board (FASB) has been contemplating making significant changes to the ways that Not-for-Profits (NFP) present their financial statements. In early March, the FASB directed its Not-for-Profit Advisory Committee to proceed with completing the Exposure Draft on the proposed accounting standards update, *Not-for-Profit Entities (ASC Topic 958) – Presentation of Financial Statements for Not-for-Profit Entities*. Pending FASB approval, we should expect an Exposure Draft, available for public comment, to be issued by mid-April.

Overall, the financial reporting project to date has been primarily focused on simplifying the net asset classification requirements and improving the information provided in the financial statements and notes about liquidity, financial performance, and cash flows. The ultimate aim of the FASB's actions includes improving the comparability of financial information between NFPs. One significant change that could impact operating results is the elimination of the option to release donor-imposed restrictions over an asset's estimated useful life, a common practice among Not-for-Profits. While we anxiously await the issuance of the exposure draft, the FASB has issued a fairly comprehensive list of tentative board decisions that have been reached to date, which include:

1. Net Asset Classes – Move from three classes of net assets (unrestricted, temporarily restricted and permanently restricted) to two classes of net assets (with donor-imposed restrictions and without donor-imposed restrictions). In addition, additional disclosures will be updated to emphasize how and when resources can be used.

2. Intermediate Measure of Operations – A NFP will be required to present an intermediate measure of current operations that is defined on the basis of two dimensions: a mission dimension and an availability dimension.

3. Expiration of Restrictions – NFPs will be required to use the placed-in-service approach for the treatment of expiration of restrictions related to long-lived assets, thus eliminating the option to release the donor-imposed restriction over an asset's estimated useful life.

4. Reporting of Expenditures – NFPs will be required to report expenses by both their nature and function, but be allowed flexibility to present expenses by either function or nature (or both) on the face of the statement of activities or within the notes.NFPs will also be required to provide an analysis of expenses by function and by nature in one location.In addition, NFPs will be required to disclose a description of the method used to allocate costs among program and support functions.The Board will also refine the definition of management and general activities and include illustrative guidance to better depict which costs should be allocated among program and/or support functions.

5. Investment Return – NFPs will be required to have a net presentation of investment expenses against investment return on the face of the statement of activities.

6. Statement of Cash Flows – NFPs will be required to use the direct method of reporting cash flows by operating activities.

7. Note Disclosures – NFPs will also be required to enhance various footnote disclosures, including disclosures related to liquidity and underwater endowments.

Ultimately, Not-for-Profits need to be aware that significant changes are coming – the most significant since FASB’s SFAS 116 and 117 were issued more than 20 years ago. Organizations should be proactive in reviewing the exposure draft when issued, and provide feedback to the FASB as appropriate. While change isn’t always easy, NFPs should take solace in that these changes will ultimately increase comparability among their peers, and allow for more meaningful financial statements.

Follow the tentative board decisions reached to date.

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