Nonprofit Financial Reporting

A brief overview of the upcoming changes to nonprofit financial statements as a result of ASU 2016-14

Overview

Background: The Financial Accounting Standards Board (FASB) sets accounting rules for nonprofit and for-profit entities. The FASB has been discussing changes to nonprofit financial reporting for several years and issued a new standard in August 2016. The main provisions are in the following boxes.

Timing of Implementation: The new standard is effective in 2018 for entities with a December 31 year end and in 2019 for entities with a different year end (such as June 30).

Statement of Financial Position and Statement of Activites

What is Changing: The statement of financial position and statement of activities and changes in net assets will be presented using only 2 classes of net assets (net assets with donor restrictions and net assets without donor restrictions) instead of the current 3 classes of net assets (unrestricted, temporarily restricted, and permanently restricted).

Additional Considerations: The new standard effectively merges temporarily and permanently restricted net assets into one category. However, the enhanced disclosures noted below mean that much of the same information, if not more, will still be available though it might be in a different place than you are used to looking.

Statement of Cash Flows

What is Changing: Organizations will continue to have the option of using either the direct method or the indirect method when preparing the statement of cash flows. Previously, a reconcilation between the two methods was required for organizations electing to use the direct method. That requirement has been removed.

Additional Considerations: One of the main points of discussion during the years leading up to the new standard was whether or not the indirect method of presenting the statement of cash flows should continue to be allowed. The FASB decided to keep this as an option which will be seen as a win by many financial statement preparers since the majority of nonprofits use the indirect method.

Expenses by Natural and Functional Classification

What is Changing: Previously, only voluntary health and welfare organizations had to present a statement of fuctional expenses. Now, all organizations have to present expenses by the natural classification (rent, salaries, utilities, etc) as well as by function (program, management and general, and fundraising). The information can be presented in the statement of activities, in a separate financial statement, or in the notes to the financial statements.

Additional Considerations: This is usually key information for donors who don't want to fund an organization that is all back office and no program work since it shows what percentage is being spent on programs.

Enhanced Disclosures

What is changing: The notes to the financial statements will change somewhat to include additional information about restricted net assets, board-designated net assets , and underwater endowment funds as well as qualitative information about liquidity.

Additional Considerations: Much of the additional information will be qualitative rather than quantitative since the numbers behind restrictions and endowments were already required to be disclosed. One of the new requirements will also change the way net assets are reported: for underwater endowment funds, the underwater portion was previously reported as unrestricted. That amount will now be included in net assets with donor restrictions.

Release of Restrictions on Long-Lived Assets

What is Changing: Restricted assets used to aquire or construct long-lived assets (such as property and equipment) are to be released from restriction when the asset is placed in service. Organizations no longer have the option of releasing the net assets from restriction over the useful life of the asset.

Additional Considerations: The impact of this change is that certain organizations will report a larger amount of unrestricted net assets and a lower amount of restricted net assets. However, the actual number of organizations impacted by this specific change is likely to be low since many organizations previously elected to follow the option which is now required.