CPE

Not-for-Profit Accounting and Auditing Supplement No. 3—2016

Chapter 1

NOT-FOR-PROFIT ACCOUNTING AND AUDITING SUPPLEMENT NO. 3–2016

INTRODUCTION

This update includes the more significant accounting and auditing developments affecting the not-for-profit industry from July 2016 through September 2016. Included in this update are standard-setting and project activities of the Auditing Standards Board (ASB), Accounting and Review Services Committee (ARSC), Assurance Services Executive Committee, Professional Ethics Executive Committee, and FASB.

These developments, although believed to be complete at the date at which they were prepared for this course material, may not cover all areas within accounting and auditing relevant to all users of this material. Readers are encouraged to visit the AICPA's Financial Reporting Center for additional resources, including various "standards trackers" for the most recent standard-setting activity in the areas of accounting and financial reporting, audit and attest, and compilation, review and preparation.

This update may refer to other sources of information, in which case you are strongly encouraged to review that information if relevant to your needs.

After completing this course, you should be able to identify some of the more significant accounting and auditing developments from July through September 2016.

Audit and Accounting Final and Proposed Standards

Final Standards, Interpretations and Regulations

AICPA

Auditing Standards Board

Auditing, Attestation and Quality Control Standards and Interpretations

The Auditing Standards Board (ASB) did not issue any new auditing, attestation, or quality control standards or interpretations in this period.

Accounting and Review Standards Committee

Statement on Standards for Accounting and Review Services No. 22, *Compilation of Pro Forma Financial Information*

Issue Date

September 2016

Background

This standard supersedes Statement on Standards for Accounting and Review Services (SSARS) No. 14, *Compilation of Pro Forma Financial Information*, as amended (AICPA, *Professional Standards*, AR sec. 120) by putting the requirements and guidance in clarity format. The clarified standard, designed to make the standards easier to read, understand, and apply, will be codified as AR-C section 120.

Main Provisions

The clarified format, standardized for all SSARs, provides the scope, objectives, definition of pro forma financial information, requirements, application and other explanatory material, and exhibits (illustrative engagement letter and report).

- Pro forma financial information is defined as: a presentation that shows what the significant effects on historical financial information might have been had a consummated or proposed transaction (or event) occurred at an earlier date.
- An accountant is required to comply with AR-C section 60, *General Principles for Engagements Performed in Accordance With Statements on Standards for Accounting and Review Services,* adapted as necessary, in addition to complying with AR-C section 120.
- Requirements address independence, client acceptance and continuance, and the agreement on engagement terms.
- The accountant should obtain an understanding of the applicable financial reporting framework and the significant accounting policies intended to be used in the preparation of the pro forma financial information, including significant accounting policies of affiliates if the entity is part of a combined entity.
- Compilation procedures and reporting and documentation requirements are incorporated directly (that is, those pertaining to compiling pro forma information) or by reference to other SSARs.
- Application guidance contains the following regarding independence in paragraph .A6:

The interpretations of the "Independence Rule" (AICPA, *Professional Standards*, ET sec. 1.200.001) of the AICPA Code of Professional Conduct provide authoritative guidance on independence. It is in the public interest and, therefore, required by this section, that the accountant modify the accountant's compilation report when the accountant is not independent of the entity whose pro forma financial information is the subject of the compilation engagement. The AICPA Code of Professional Conduct also defines *independence* as consisting of two elements, independence of mind and independence in appearance. Independence enhances the accountant's ability to act with integrity and be objective. Independence implies an impartiality that recognizes an obligation to be fair not only to the responsible party but also to users of the pro forma financial information who may rely upon the accountant's compilation report. In the absence of an interpretation of the "Independence Rule" that addresses a particular relationship or circumstance, a member should apply the "Conceptual Framework for Independence" interpretation (AICPA, *Professional Standards*, ET sec. 1.210.010).

Effective Date

The clarified standard applies to compilation reports on pro forma financial information issued on or after May 1, 2017.

Professional Ethics Executive Committee

The PEEC did not issue any new or revised ethics interpretations in this period.

FASB

Accounting Standards Updates

FASB ASU No. 2016-14, Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities

Issue Date

August 2016

Background

At the urging of its Not-for-Profit Advisory Committee (NAC) and feedback from stakeholders of the Not-for-Profit (NFP) sector, FASB initiated a project in 2011 to update and improve the 20 plus-year-old standard, *FASB No. 117, Financial Statements of Not-for-Profit Organizations.* Considered to be sound but improvable, FASB's goal was to improve the information NFPs provide to their stakeholders, including donors, creditors, and other users of their financial statements. Conducting significant outreach prior to proposing the changes in 2015, FASB targeted the following areas for improvement and change:

- Net asset classifications, specifically their complexity and understandability
- Information about liquidity and availability of resources, specifically the transparency and completeness of the information available to users
- Investment return and expenses, specifically the lack of consistency across NFPs in the way these were being presented and disclosed
- Statement of cash flows, specifically the decision-usefulness of cash flow information

FASB sought to find the balance between incremental benefits to users versus the costs of obtaining, categorizing, presenting, and disclosing additional information, eliminating certain tasks and disclosures and adding others. To read FASB's rationale that the benefits to users exceed the costs to NFPs, see *FASB Understanding Costs and Benefits—ASU: Presentation of Financial Statements of Not-for-Profit Entities (Topic 958).*

The amendments in this ASU affect NFPs and the users of their general purpose financial statements. NFPs generally receive significant contributed resources and operate to further a public purpose rather than to achieve a profit objective, and their stakeholders, unlike those of business entities, generally do not have ownership interests. Those NFPs typically include nongovernmental entities such as charities, foundations, colleges and universities, health care providers, cultural institutions, religious organizations, and trade associations, among others. They generally do not include investor-owned entities or entities that provide dividends, lower costs, or other economic benefits directly and proportionately to their owners, members, or participants, such as mutual insurance entities, credit unions, farm and rural electric cooperatives, and employee benefit plans. Rather, NFPs seek resources from lenders, bondholders, donors, and grantors, including foundations and governmental agencies, that seek financial information in making their decisions to lend, donate, or grant resources to an NFP.

The ASU results from completion of phase 1 of FASB's project to improve the standard for NFPs. Phase 2 (the final phase) will address some of the more challenging issues being considered by FASB, such as

- requirement and definition of a measure of operations
- realignment of certain line items in the statement of cash flows to better match the required measure of operations
- consideration of segment reporting as an alternative to analyzing expenses by nature and function for NFPs that are business-oriented healthcare organizations

Research is currently underway for phase 2 of the project.

Main Provisions

The main provisions of FASB ASU 2016-14 are amendments to the requirements for financial statements and notes in FASB ASC 958, *Not-for-Profit Entities*, are captured below. Commentary regarding FASB's estimation of possible costs and benefits the NFP and its stakeholders may derive from amending the provision(s) follows the description of each provision under five general areas.

Net Asset Classes

- Present on the face of the statement of financial position amounts for two classes of net assets at the end of the period, rather than for the currently required three classes. That is, an NFP will report amounts for net assets with donor restrictions and net assets without donor restrictions, as well as the currently required amount for total net assets. Underwater endowment funds (also discussed below under *Liquidity and Availability of Resources)* should be classified as part of net assets with donor restrictions.
- Present on the face of the statement of activities the amount of the change in each of the two classes of net assets rather than that of the currently required three classes. An NFP would continue to report the currently required amount of the change in total net assets for the period.

Potential Costs and Benefits

Presenting fewer categories of net assets and the change in net assets each period (eliminating the distinction between temporary and permanent restrictions, which was partially driven by changes in state laws that have made the distinction less relevant) should reduce complexity and costs for NFPs.

Presentation of Operating Cash Flows

Continue to present on the face of the statement of cash flows the net amount for operating cash flows using either the direct or indirect method of reporting but no longer require the presentation or disclosure of the indirect method (reconciliation) if using the direct method.

Potential Costs and Benefits

For all NFPs, the continued ability to choose provides flexibility in approach. For NFPs using the direct method in preparing the statement of cash flows, elimination of the presentation, or disclosure of the indirect method via reconciliation should reduce complexity and costs.

Liquidity and Availability of Resources

Provide the following new, enhanced disclosures about the following:

- Amounts and purposes of governing board designations, appropriations, and similar actions that result in self-imposed limits on the use of resources without donor-imposed restrictions as of the end of the period.
- Composition of net assets with donor restrictions at the end of the period and how the restrictions affect the use of resources.
- Qualitative information that communicates how an NFP manages its liquid resources available to meet cash needs for general expenditures within one year of the balance sheet date.
- Quantitative information, either on the face of the balance sheet or in the notes, and additional qualitative information in the notes as necessary, that communicates the availability of an NFP's financial assets at the balance sheet date to meet cash needs for general expenditures within one year of the balance sheet date. Availability of a financial asset may be affected by (1) its nature, (2) external limits imposed by donors, grantors, laws, and contracts with others, and (3) internal limits imposed by governing board decisions.
- Underwater endowment funds, including disclosures of (1) an NFP's policy, and any actions taken during the period, concerning appropriation from underwater endowment funds, (2) the aggregate fair value of such funds, (3) the aggregate of the original gift amounts (or level required by donor or law) to be maintained, and (4) the aggregate amount by which funds are underwater (deficiencies).

Potential Costs and Benefits

The thrust of these new requirements enhances the relevance of information to users due to greater transparency regarding the way the NFP manages its resources, the nature and timing of self-imposed and externally imposed restriction on donations, and the impact of such restrictions and similar issues, such as underwater endowment funds, on the NFP's operations, and liquidity. The enhanced disclosures provide stakeholders a better gauge on the NFP's availability of resources to meet cash needs within one year of the balance sheet date and aspects of management's performance in optimizing the NFP's stewardship over resources.

> A new requirement to use, in the absence of explicit donor stipulations, the placed-in-service approach for reporting expirations of restrictions on gifts of cash or other assets to be used to acquire or construct a long-lived asset, and reclassify any amounts from net assets with donor restrictions to net assets without donor restrictions for such long-lived assets that have been placed in service as of the beginning of the period of adoption. This method eliminates the current option to release the donor-imposed restriction over the estimated useful life of the acquired asset.

Potential Costs and Benefits

Using the placed-in-service approach for reporting expirations or restrictions on gifts and other assets to be used in construction projects, rather than over the estimated life of the asset, should reduce complexity and costs for preparers. Stakeholders should benefit from enhanced comparability and greater decision-usefulness of the information.

Expenses

- Present expenses both by their nature (new requirement) and function (existing requirement). Analyze expenses in one location, which could be on the face of the statement of activities, as a separate statement, or in notes to financial statements.
- Describe the method(s) used to allocate costs among program and support functions.

Potential Costs and Benefits

Enhanced disclosures should help stakeholders better assess the nature of an NFP's expenses and the way the NFP's management allocated costs among programs and support functions and enhance comparability among organizations.

Investment Return

Report investment return net of external and direct internal investment expenses and no longer require disclosure of expenses.

Potential Costs and Benefits

Removing the requirement to present and disclose investment-related expenses should reduce complexity and cost for NFPs, freeing NFP from identifying fees embedded in investment returns and providing a more comparable measure of investment returns across NFPs.

Effective Date

The amendments in this ASU are effective for annual financial statements issued for fiscal years beginning after December 15, 2017, and for interim periods within fiscal years beginning after December 15, 2018. Application to interim financial statements is permitted but not required in the initial year of application.

- Early application of the amendments in this ASU is permitted. The amendments in this ASU should be initially adopted only for an annual fiscal period or for the first interim period within the fiscal year of adoption.
- The amendments in this ASU should be applied on a retrospective basis in the year that the ASU is first applied. However, if presenting comparative financial statements, an NFP has the option to omit the following information for any periods presented before the period of adoption:
  - Analysis of expenses by nature and functional classification (previously only certain NFPs had to present this analysis); the separate presentation of expenses by functional classification and expenses by natural classification is still required. NFPs that previously were required to present a statement of functional expenses do not have the option to omit this analysis; however, they may present the comparative period information in any of the formats permitted in this update, consistent with the presentation in the period of adoption.
  - Disclosures about liquidity and availability of resources.

In the period that the amendments are first applied, an NFP should disclose the nature of any reclassifications or restatements and their effects, if any, on changes in the net asset classes for each period presented.

Practically Speaking

Preparers. NFPs should consider FASB ASU 2016-14 in light of their particular circumstances and discuss the ASU and its impact to the NFP with the board of directors and individual committees of the board, as applicable, and the NFP's auditors. Issues to consider include

- when to implement the ASU in light of the upcoming ASU on revenue recognition and lease accounting, which may significantly impact the NFP (that is, consider adopting the NFP standard early if the impact of the other standards, implemented later, will be significant).
- an implementation plan that includes consideration of possible changes to policies and procedures to implement this ASU.
- a plan for educating management, staff, the board of directors and users of the NFP's financial statements about the upcoming changes.

Auditors. Consider whether to include in an NFP's audit report an emphasis-of-matter paragraph to discuss the impact of the ASU on the NFP's financial statements.

Knowledge Check

1. Which statement best describes a significant change to NFP accounting under ASU No. 2016-14?

   a. Preparers no longer are required to analyze expenses by nature and function.
   b. Preparers will present net assets in two categories instead of three.
   c. Preparers now must use the indirect method for presenting the statement of cash flows.
   d. Preparers should classify underwater endowment funds as unrestricted cash.

FASB ASU No. 2016-15, *Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments*

Issue Date

August 2016

Background

This ASU resulted from a consensus of FASB Emerging Issues Task Force and addresses the diversity in practice regarding the presentation and classification of certain items in the Statement of Cash Flows, and related items. Eight issues are addressed. All the following items except the last one, provide guidance where none currently exists in GAAP. The last item clarifies existing GAAP.

Main Provisions

1 – Classify cash payments for debt prepayment or extinguishment costs

Classify cash payments for debt prepayment or extinguishment costs as cash outflows for financing activities.

2 – Classify cash payment made by a bond issuer when settling a zero-coupon bond

Classify portion of cash payment attributed to accreted interest related to the debt discount as cash outflow for operating activities; classify portion attributed to principal as financing activities.

3 – Classify cash payments made by acquirer after a business combination for the settlement of a contingent consideration liability

If cash payments are not made soon after the business combination, separate and classify as cash outflow for financing and operating activities. Recognize cash payments up to the amount of the contingent consideration liability at the acquisition date as financing activities, with any excess treated as operating activities. Classify cash payments made by an acquirer soon after the acquisition date of a business combination to settle a contingent consideration liability as cash outflows for investing activities.

4 – Proceeds from settling insurance claims

Classify on the basis of the related insurance coverage, that is, the nature of the loss. If proceeds result from a lump sum settlement, consider the basis of the nature of each loss included in the settlement.

5 – Proceeds from settling corporate insurance policies (including bank-owned policies)

Classify settlements (inflows) from corporate-owned policies as financing activities. Classify cash paid for premiums as investing and operating or a combination of investing and operating activities.

6 – Distributions received from equity method investees

When a reporting entity applies the equity method, it should make an accounting policy election to classify distributions received from equity method investees using either of the following approaches:

1. Cumulative earnings approach: Distributions received are considered returns on investment and classified as cash inflows from operating activities, unless the investor's cumulative distributions received less distributions received in prior periods that were determined to be returns of investment exceed cumulative equity in earnings recognized by the investor. When such an excess occurs, the current-period distribution up to this excess should be considered a return of investment and classified as cash inflows from investing activities.
2. Nature of the distribution approach: Classify distributions received on the basis of the nature of the activity or activities of the investee that generated the distribution as either a return on investment (classified as cash inflows from operating activities) or a return of investment (classified as cash inflows from investing activities) when such information is available to the investor. If an entity elects to apply the nature of the distribution approach and the information to apply that approach to distributions received from an individual equity method investee is not available to the investor, the entity should report a change in accounting Cash Flow Issue Summary of Amendments principle on a retrospective basis by applying the cumulative earnings approach in (1) for that investee. In such situations, an entity should disclose that a change in accounting principle has occurred with respect to the affected investee(s) due to the lack of available information and should provide the disclosures required in paragraphs 1b and 2 of FASB ASC 250-10-50, as applicable. This amendment does not address equity method investments measured using the fair value option.

7 – Beneficial interests in securitization transactions

Disclose a transferor's beneficial interest obtained in a securitization of financial assets as a noncash activity, and classify cash receipts from payments on a transferor's beneficial interests in securitized trade receivables as cash inflows from investing activities.

8 – Separately Identifiable Cash Flows and Application of the Predominance Principle

The classification of cash receipts and payments that have aspects of more than one class of cash flows should be determined first by applying specific guidance in GAAP. In the absence of specific guidance, an entity should determine each separately identifiable source or use within the cash receipts and cash payments on the basis of the nature of the underlying cash flows. An entity should then classify each separately identifiable source or use within the cash receipts and payments on the basis of their nature in financing, investing, or operating activities. In situations in which cash receipts and payments have aspects of more than one class of cash flows and cannot be separated by source or use, the appropriate classification should depend on the activity that is likely to be the predominant source or use of cash flows for the item.

Effective Date

Public Business Entities. The amendments in this ASU are effective for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years.

Other Entities. The amendments are effective for fiscal years beginning after December 15, 2018, and interim periods within fiscal years beginning after December 15, 2019. Early adoption is permitted, including adoption in an interim period. If an entity early adopts the amendments in an interim period, any adjustments should be reflected as of the beginning of the fiscal year that includes that interim period. An entity that elects early adoption must adopt all the amendments in the same period.

The amendments in this ASU should be applied using a retrospective transition method to each period presented. If it is impracticable to apply the amendments retrospectively for some of the issues, the amendments for those issues would be applied prospectively as of the earliest date practicable.

KNOWLEDGE CHECK

2. Which statement about SSARS No 22, *Compilation of Pro Forma Information,* is correct?

   a. The standard sets forth requirements and guidance for compiling pro forma information in the clarity format.
   b. The standard adds significant new requirements for practitioners compiling pro forma information.
   c. The standard eliminates most of the requirements for practitioners compiling pro forma information.
   d. The standard eliminates the requirement to disclose a lack of independence in the report.

Proposed Standards, Interpretations, and Regulations

AICPA

Proposed Auditing Standards

Proposed Statement on Auditing Standards: *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (Clarification and Recodification of Sections 800, 805, and 930)

Issue Date

July 5, 2016

Comment Due Date

September 5, 2016

Background

The proposed Statement on Auditing Standards (SAS) would supersede SAS No 126, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern.* The ASB revised the standard to incorporate elements that were not yet developed by FASB (management responsibilities) and GASB (application to government entities) when the standard was clarified in June 2012. The revision also converges SAS No 126 with international standard on auditing (ISA) 570, *Going Concern,* issued by the International Auditing and Assurance Standards Board (IAASB) (except for the IAASB's auditor reporting guidance, which the ASB plans to address in its auditor's report initiative).

The proposed SAS is intended to apply to any financial reporting framework. Because the SAS is a US standard, when terms needed explanation the proposed standard deferred to definitions used by FASB or GASB.

Main Provisions

The most significant changes to the existing SAS are

AU-C Section 930, *Interim Financial Information*

- Would require review procedures when the applicable financial reporting framework requires management to assess the entity's ability to continue as a going concern for a reasonable period of time in preparing interim financial information (no longer optional)
- New proposed requirement to include an emphasis of matter paragraph in the report when certain conditions related to the entity's viability exist, which makes annual and interim reporting requirements the same

AU-C Section 805, *Special Considerations—Audits of Single Financial Statements and Specific Elements, Accounts, or Items of a Financial Statement*

- AU-C section 570 would apply whenever the going concern basis of accounting is relevant in preparing financial statements in accordance with a special purpose framework
  - Proposed that the going concern basis is not relevant for single financial statements and specific elements, accounts or items of a financial statement because members should evaluate these matters at the entity level and not at the level of a single financial statement or specific items, and so on.

- Would require evaluation of whether disclosures are needed to describe risk and uncertainties in achieving fair presentation

AU-C section 580, *Written Representations*

- Would require an additional written representation that explicitly addresses management's completion of its evaluation to whether there is substantial doubt about the entity's ability to continue as a going concern, when applicable.

Proposed Effective Date

If approved, the proposed SAS will be effective for audits of financial statements for periods ending on or after December 15, 2017, and for interim periods after that date.

Proposed Auditing Standards

Statement on Auditing Standards: Auditor Involvement with Exempt Offering Documents

Issue Date

July 13, 2016

Comment Due Date

October 13, 2016

Background

Because of changes to the AICPA Audit and Accounting Guides, *State and Local Governments* and *Health Care Entities,* the ASB appointed a task force to address the topic of auditor involvement with exempt offerings under the Securities Act of 1933 (as amended) and franchise offerings regulated by the Federal Trade Commission (FTC).

Main Provisions

The SAS provides performance requirements when an auditor is deemed to be "involved" with an exempt offering, whether deliberately (triggered by the auditor's activities described in the proposal) or voluntarily through other means. The proposed performance requirements are consistent with those in

- AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*
- AU-C section 720, *Other Information in Documents Containing Audited Financial Statements*

As proposed, auditors are neither required to, nor precluded from, becoming involved in offering documents.

The ASB raised certain issues, requesting comment on whether the offering documents and trigger events included in the proposed scope were appropriate and whether auditors, when involved in exempt offering documents, should be required to apply AU-C section 560, *Subsequent Events and Subsequently Discovered Facts*.

Proposed Effective Date

If approved, the proposed SAS would be effective for exempt offering documents with which the auditor is involved that are initially distributed, circulated, or submitted on or after June 15, 2018. Early application, once issued, would be permitted.

Proposed Attestation or Quality Control Standards

The ASB did not issue any proposed attestation or quality control standards or interpretations in this period.

Accounting and Review Services Committee

Amendment to Statement on Standards for Accounting and Review Services No. 21 Section 90, *Review of Financial Statements*

Issue Date

July 6, 2016

Comment Deadline

September 2, 2016

Background

The proposed SSARS will amend AR-C section 90, *Review of Financial Statements* (AICPA, *Professional Standards*), to revise requirements and guidance that applies when an accountant's review report includes supplementary information in addition to the reviewed financial statements. The proposed SSARS reflects a technical correction of AR-C section 90. ARSC is not proposing any other modifications to SSARSs.

Amendment(s)

AR-C section 90 addresses the accountant's responsibilities when engaged to review financial statements. This amendment clarifies the definition of *supplementary information* and the accountant's reporting responsibilities in circumstances where the review report covers supplementary information.

Effective Date

The revisions will be effective upon issuance.

Professional Ethics Executive Committee

The PEEC did not issue any proposed ethics interpretations in this period.

FASB

Proposed ASU

Income Taxes (Topic 740): Disclosure Framework—Changes to the Disclosure Requirements for Income Taxes

Issue Date

July 26, 2016

Comment Deadline

September 30, 2106

Background

This proposal relates to FASB's disclosure framework project, which seeks to improve the consistency of FASB decisions about disclosure requirements and allowing an entity's management to exercise the appropriate level of discretion in developing the notes to the financial statements. The board used the guidance in the March 2014 proposed concepts statement, *Conceptual Framework for Financial Reporting—Chapter 8: Notes to the Financial Statements,* in developing this proposed ASU, which is also consistent with Proposed ASU, *Notes to the Financial Statements (Topic 235): Assessing whether Disclosures are Material.* (That ASU promotes the use of discretion when evaluating FASB disclosure requirements.)

Main Provisions

The proposed requirements apply to all entities that are subject to income taxes although some requirements only apply to public business entities.

Based on its cost and benefit analysis, FASB proposed that all entities provide the following additional disclosures:

- Description of an enacted change in tax law that is probable to have an effect on the reporting entity in a future period
- Income (or loss) from continuing operations before income tax expense (or benefit) disaggregated between domestic and foreign
- Income tax expense (or benefit) from continuing operations disaggregated between domestic and foreign
- Income taxes paid, disaggregated between domestic and foreign, and the amount of income taxes paid to any country that is significant to total income taxes paid
- An explanation of circumstances that caused a change in assertion about the indefinite reinvestment of undistributed foreign earnings and the corresponding amount of those earnings
- The aggregate of cash, cash equivalents, and marketable securities held by foreign subsidiaries

The following disclosures would be required for public business entities by Topic 740 based on the proposed Concepts Statement, which also includes cost and benefit considerations:

- Within the reconciliation of the total amounts of unrecognized tax benefits at the beginning and end of the period, settlements using existing deferred tax assets separate from those that have been or will be settled in cash.
- The line items in the statement of financial position in which the unrecognized tax benefits are presented and the related amounts of such unrecognized tax benefits. If the unrecognized tax benefits are not presented in the statement of financial position, those amounts should be disclosed separately.
- The amount and explanation of the valuation allowance recognized or released during the reporting period.
- The total amount of unrecognized tax benefits that offsets the deferred tax assets for carryforwards.

The proposed concept statement would limit the disclosure of future-oriented information to the information the entity used to determine amounts in the financial statements or the notes to the financial statements, eliminating for example disclosures related to unrecognized tax benefits.

The proposal would also modify the existing rate reconciliation requirement for public business entities to be consistent with SEC Reg. S-X.

The proposal would require an entity to describe any specific, legally-enforceable agreement with the government to reduce (or possibly reduce) taxes, including amount, commitments made, and duration of the agreement.

Effective Date

The proposed ASU calls for companies to apply the ASU prospectively. FASB will determine the effective date based on feedback from the proposal.

Proposed ASU

Plan Accounting (Topics 960, 962, and 965): Employee Benefit Plan Master Trust Reporting

Issue Date

July 28, 2016

Comment Deadline

September 26, 2016

Background

To improve the usefulness of information reported to users of employee benefit plan (plan) financial statements, FASB issued this proposal which addresses a current gap in the guidance for plans that have an interest in a master trust (stakeholders believe they are limited and incomplete). A master trust is a trust for which a regulated financial institution (bank, trust company, or similar financial institution that is regulated, supervised, and subject to periodic examination by a state or federal agency) serves as a trustee or custodian and in which assets of more than one plan sponsored by a single employer or by a group of employers under common control are held.

The proposed ASU seeks to clarify presentation requirements for a plan's interest in a master trust and requires more detailed disclosures of the plan's interest in the trust.

Main Provisions

Under FASB ASC 960, a plan reports its interests in master trusts as a single line item in the statement of net assets available for benefits; FASB ASC 962 and FASB ASC 965 do not contain similar guidance, which has resulted in diversity in practice. The proposed ASU adds a requirement to disclose the interest in a master trust and any changes to the interest in the statement of changes in net assets for benefits.

FASB ASC 960 and FASB ASC 962 require plans to disclose their percentage interest in the master trust and a list of the investments held by the master trust, presented by general type, within the plan's financial statements. Stakeholders have said that the disclosure can be misleading when the plan has a divided interest in the individual investments of the master trust (that is, when the plan has a specific, rather than a proportionate, interest in the master trust). The amendments in this proposed ASU would require all plans with a divided interest to disclose both a list of the general types of investments held by the master trust and the dollar amount of their interest in each of those general types of investments.

The amendments in this proposed ASU would require all plans to disclose (1) their master trust's other asset and liability balances and (2) the dollar amount of the plan's interest in each of those balances.

FASB opted not to include in this proposal a requirement to provide other GAAP disclosures, such as for fair value or hedging activities, for the investments held in the master trust.

The proposal eliminates a redundancy related to disclosures related to 401(h) account assets. That is, health and welfare plans disclose the same information in their defined benefit and health and welfare plan financial statements; this proposal would require those plans include the disclosure in their defined benefit plan with a reference in the entity's health and welfare plan to the defined benefit plan).

Effective Date

To be determined once feedback on the proposal is considered. Otherwise, the ASU calls for companies to apply the ASU retrospectively to all prior periods presented.

Proposed ASU

Not-For-Profit Entities-Consolidation (Subtopic 958-810): Clarifying When a Not-for-Profit Entity That Is a General Partner Should Consolidate a For-Profit Limited Partnership or Similar Entity

Issue Date

August 3, 2016

Comment Deadline

October 3, 2016

Background

This proposed ASU amends the consolidation guidance in FASB ASC 958-810, *Not-for-Profit Entities—Consolidation*, to clarify when a NFP should consolidate a for-profit limited partnership or similar legal entity once the amendments in FASB ASU No. 2015-02, *Consolidation (Topic 810): Amendments to the Consolidation Analysis,* become effective.

Current GAAP requires an NFP that is a general partner of a for-profit limited partnership or similar legal entity to apply the consolidation guidance in FASB ASC 810-20*, Consolidation—Control of Partnerships and Similar Entities*, unless that partnership interest is reported at fair value. However, once the amendments in FASB ASU 2015-02 are effective, the guidance in FASB ASC 810-20 no longer will exist, creating uncertainty about when an NFP that is a general partner should consolidate a for-profit limited partnership. GAAP will require an NFP that is a general partner of a for-profit limited partnership to apply the general consolidation guidance in FASB ASC 810-10, however certain aspects of the new guidance (consideration of variable interest entities) are not relevant to NFPs, leaving a gap in the guidance that this proposal seeks to fill.

Main Provisions

The amendments in this proposed ASU would retain the consolidation guidance that existed in FASB ASC 810-20 by including it within FASB ASC 958-810 and would enhance GAAP by clarifying the consolidation guidance for NFPs and helping avoid diversity in practice.

The amendments in this proposed ASU would apply to an NFP that is a general partner of a for-profit limited partnership or a similar legal entity. A *similar legal entity* is an entity such as a limited liability company that has governing provisions that are the functional equivalent of a limited partnership. In such entities, a managing member is the functional equivalent of a general partner, and a nonmanaging member is the functional equivalent of a limited partner. Throughout this proposed ASU, any reference to a limited partnership includes limited partnerships and similar legal entities.

Under the proposed amendments, NFPs that are general partners would continue to be presumed to control a for-profit limited partnership, regardless of the extent of their ownership interest, unless that presumption is overcome. The presumption would be overcome if the limited partners have either substantive kick-out rights or substantive participating rights. To be substantive, the kick-out rights would have to be exercisable by a simple majority vote of the limited partners' voting interests or a lower threshold. For purposes of evaluating that threshold, the limited partners' voting interests would exclude voting interests held by the general partners, parties under common control with the general partners, and other parties acting on behalf of the general partners.

The ASU also would add guidance to FASB ASC 958-810 on when an NFP limited partner should consolidate a for-profit limited partnership. For ease of reference, FASB ASU 2015-02 adds new guidance to the general consolidation guidance in FASB ASC 810-10 on when limited partners should consolidate limited partnerships that are not VIEs (or not within scope of the VIE guidance).

The definitions of the terms *kick-out rights*, *participating rights*, and *protective rights* that were included in FASB ASC 810-20 for limited partnerships were amended by FASB ASU 2015-02. Those amended terms have been added to the glossary section of FASB ASC 958-810, and conforming revisions have been made to the application guidance. As stated in the basis for conclusions document, FASB amended the definitions to increase the consistency and accuracy of the terms but there was no intent to change their meanings or how they were interpreted under FASB ASC 810-20.

Due to recent standard-setting (creating FASB ASC 321, *Investments—Equity Securities,* and FASB ASC 958-321), the board felt it should make consequential amendments to FASB ASC 958-810 to clarify the board's intent not to affect current applications of the fair value elections in that subtopic for NFPs. To emphasize that intent, the board has proposed additional clarifications to FASB ASC 958-810 in this proposed update.

Effective Date and Transition Provisions

Early Adopters. Apply the amendments in this proposed ASU using either (1) a modified retrospective approach by recording a cumulative-effect adjustment to equity as of the beginning of the fiscal year of adoption or (2) a retrospective approach.

Other Entities. Adopt the amendments in this proposed ASU while it adopts the amendments in FASB ASU 2015-02 and to apply the same transition method elected for the application of update 2015-02.

The board will determine the effective date for entities that elected to early adopt the amendments in FASB ASU 2015-02 after it considers stakeholders' feedback on the proposed amendments.

Exposure Drafts

Proposed ASUs

Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities

Issue Date

September 8, 2016

Comment Deadline

November 22, 2016

Background

The proposed ASU seeks to improve the hedge accounting model by aligning it more closely to entities' risk management activities which should also help users better understand an entity's risk exposures and risk management strategies and simplifying the application of GAAP to hedging activities.

Main Provisions

In summary, the proposal would

- expand and refine hedge accounting for both nonfinancial and financial risk components, and
- align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements.

At a slightly more detailed level, the proposal would

- permit hedge accounting for risk components in hedging relationships involving nonfinancial risk and interest rate risk.
- change the guidance for measuring changes in fair value when hedging interest rate risk.

- align the recognition and presentation of the effects of the hedging instrument and the hedged item in the financial statements to increase the understandability of the results of an entity's intended hedging strategies.
- report the entire effect of the hedging instrument in the same income statement line item in which the earnings effect of the hedged item is reported in the period(s) that the hedged item affects earnings.
- no longer require entities to separately measure and report hedge ineffectiveness.
- improve current guidance related to the assessment of hedge effectiveness, for example, allow an entity more time to perform the initial prospective quantitative assessment of hedge effectiveness.
- modify disclosures (eliminate the requirement to disclose the ineffective portion of the change in fair value of hedging instruments) while adding new disclosures (enhanced qualitative disclosures related to hedging goals).

Effective Date and Transition Provisions

To be determined once feedback on the proposal is considered. Earlier application of the proposed amendments would be permitted at the beginning of any fiscal year before the effective date.

Transition provisions vary based on the entity's circumstances.

Proposed ASUs

Receivables—Nonrefundable Fees and Other Costs (Subtopic 310-20): Premium Amortization on Purchased Callable Debt Securities

Issue Date

September 22, 2016

Comment Deadline

November 28, 2016

Background

This proposed ASU would amend the amortization period for callable debt securities purchased at a premium. The board is proposing to shorten the amortization period for the premium to the earliest call date. Under current GAAP, entities generally amortize the premium as an adjustment of yield over the contractual life of the instrument.

Stakeholders have raised concerns that current GAAP excludes callable debt securities from consideration of early repayment of principal even if the holder is certain that the call will be exercised. As a result, upon the exercise of a call on a callable debt security purchased at a premium, the unamortized premium is recorded as a loss in earnings. Additionally, stakeholders have told the board that there is diversity in practice (1) in the amortization period for premiums of callable debt securities and (2) in how the potential for exercise of a call is factored into current impairment assessments.

Main Provisions

The ASU would require an entity to amortize the premium to the earliest call date. The proposal would not change GAAP for callable debt securities purchased at a discount; an entity would continue to amortize to the maturity date the discount associated with the purchase of a callable debt security.

Effective Date

To be determined once feedback on the proposal is considered. An entity would apply the proposed amendments through a cumulative-effect adjustment to retained earnings as of the beginning of the first reporting period in which the guidance is effective (that is, a modified retrospective approach). Additionally, in the period of adoption, an entity would provide disclosures about a change in accounting principle.

Proposed ASUs

Financial Services—Insurance (Topic 944): Targeted Improvements to the Accounting for Long-Duration Contracts

Issue Date

September 29, 2016

Comment Deadline

December 15, 2016

Background

Initially proposing more sweeping changes to GAAP for insurance entities' long-duration contracts, FASB changed course, deciding instead to target improvements to existing recognition, measurement, presentation, and disclosure requirements to simplify and improve GAAP in this area.

Main Provisions

The proposed amendments would apply to all insurance entities that issue long-duration contracts as defined in FASB ASC 944. The proposed amendments would not apply to (1) holders (that is, policyholders) of long-duration contracts and (2) noninsurance entities.

Assumptions used to measure the liability for future policy benefits

The amendments in this proposed ASU would require an insurance entity to update (1) the assumptions used to measure future cash flows at least annually (or more frequently) and (2) the discount rate assumption at each reporting date.

The proposed changes would also require an insurance entity to discount expected future cash flows using a high-quality fixed income instrument yield that maximizes the use of market observable inputs.

Measurement of market risk benefits

The amendments in this proposed ASU would require an insurance entity to measure all market risk benefits at fair value. The portion of any change in fair value attributable to a change in the instrument-specific credit risk would be recognized in other comprehensive income.

Amortization of deferred acquisition costs

The amendments in this proposed ASU would simplify the amortization of deferred acquisition costs.

Deferred acquisition costs would not be subject to impairment testing.

Disclosures

The amendments in this proposed ASU would require an insurance entity to provide disaggregated roll-forwards of beginning to ending balances of the liability for future policy benefits, policyholder account balances, market risk benefits, separate account liabilities, and deferred acquisition costs.

The amendments in this proposed ASU also would require an insurance entity to disclose quantitative and qualitative information about significant inputs, judgments, and assumptions used in measurement, including changes in those inputs, judgments, and assumptions and the effect of those changes on the measurement.

Effective Date and Transition Provisions

To be determined once feedback on the proposal is considered.

Liability for future policyholder benefits. Apply the proposed amendments on the liability for future policyholder benefits retrospectively as of the beginning of the earliest period presented. If it is impracticable to apply the proposed amendments retrospectively, an insurance entity would apply the proposed amendments to in-force contracts based on their existing carrying amounts at the transition date, adjusted for the removal of any related amounts in accumulated other comprehensive income.

Measuring market risk benefits at fair value. Measure market risk benefits at fair value at the beginning of the earliest period presented. The cumulative effect of changes in the instrument-specific credit risk between contract inception date and transition date would be recognized in the opening balance of accumulated other comprehensive income. The difference between fair value and carrying value at the transition date, excluding the effect of changes in the instrument-specific credit risk, would require an adjustment to the opening balance of retained earnings.

Amortizing deferred acquisition costs. Apply the proposed amendments on amortizing deferred acquisition costs as of the transition date to the existing carrying amounts at that date, adjusted for the removal of any related amounts in accumulated other comprehensive income.

Note

On September 19, 2016, FASB issued "Technical Corrections and Improvements to ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*—Additional Corrections." Comments were due October 4, 2016.

Knowledge Check

3. Which statement best describes a provision in the 2016 FASB proposal on Not-For-Profit Entities Consolidation?

    a. The proposed ASU would change the meaning of the definition of *kick-out rights*.
    b. The proposed ASU would amend how an entity elects its fair value methodology.
    c. The proposed ASU would apply to all types of entities, including NFPs.
    d. The proposed ASU would apply to an NFP's investment in entities similar to for-profit limited partnerships.

NOT-FOR-PROFIT ACCOUNTING AND AUDITING SUPPLEMENT NO. 3–2016

Solutions

The AICPA offers a free, daily, e-mailed newsletter covering the day’s top business and financial articles as well as video content, research and analysis concerning CPAs and those who work with the accounting profession. Visit the CPA Letter Daily news box on the www.aicpa.org home page to sign up. You can opt out at any time, and only the AICPA can use your e-mail address or personal information.

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SOLUTIONS

CHAPTER 1

Solutions to Knowledge Check Questions

1.

a. Incorrect. The reverse is true, that is, preparers are required to provide such analysis under the ASU. Expenses should also be analyzed in one location, which could be on the face of the statement of activities, as a separate statement, or in notes to financial statements.
b. Correct. The net asset categories have been reduced by one to exclude a separate category for temporarily restricted assets.
c. Incorrect. The preparer may continue to choose between the two methods under the ASU (no change). The change is preparers are no longer required to reconcile to the indirect method if they choose the direct method.
d. Incorrect. Underwater endowment should be classified as part of net assets with donor restrictions.

2.

a. Correct. The standard adopted the clarity formatting, which should make the standard easier to read, understand, and apply.
b. Incorrect. The standard does not impose new requirements on practitioners. The clarified standard will make the standards easier to read, understand, and apply.
c. Incorrect. The standard does not eliminate most of the requirements in the superseded standard. The requirements in the standards address independence, client acceptance and continuance, and the agreement on engagement terms.
d. Incorrect. The standard does not eliminate the requirement to disclose a lack of independence in the report when warranted. The requirements in the standards address independence, client acceptance and continuance, and the agreement on engagement terms.

3.

a. Incorrect. The definitions of the terms *kick-out rights*, *participating rights*, and *protective rights* that were included in FASB ASC 810-20 for limited partnerships were amended by FASB ASU 2015-02. As stated in the basis for conclusions document, FASB amended the definitions to increase the consistency and accuracy of the terms but there was no intent to change their meanings or how they were interpreted under FASB ASC 810-20.
b. Incorrect. The board amended FASB ASC 958-810 to clarify the board's intent not to affect current applications of the fair value elections in that subtopic for NFPs.
c. Incorrect. The update would apply to NFPs exclusively.
d. Correct. The update would apply to limited partnership and similar interests such as in a limited liability company in which an NFP has an interest.