NFP Interests in Other Entities
Whitepaper

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INTRODUCTION

Not-for-profit organizations (NFP)[1] have interests in various kinds of entities and for various purposes. This document describes requirements for reporting certain of such interests pursuant to existing GAAP, as well as what AcSEC believes are changes or clarifications that should be made to existing GAAP. (**Appendix C** of this whitepaper includes a top-level summary of the changes to financial reporting literature proposed in this draft white paper. Some of those changes or clarifications are such that they could be communicated by AcSEC via the NFP guide as non-authoritative "AcSEC believes" or interpretive guidance. Other of those changes or clarifications, however, would need to be promulgated by the FASB as authoritative GAAP. Guidance representing AcSEC's conclusions that go beyond existing authoritative GAAP are identified within this whitepaper via **bold notes** that clarify whether (a) AcSEC

[1] This document addresses only NFPs that are within the scope of the AICPA Audit and Accounting Guide *Not-for-Profit Organizations.* Accordingly, it does not address NFPs within the AICPA Audit and Accounting guide *Health Care Organizations*.

could communicate that guidance via the NFP guide, as non-authoritative "AcSEC believes" or interpretive guidance, or (b) that guidance would need to be promulgated by the FASB as authoritative GAAP.)

BACKGROUND

For purposes of this discussion, the kinds of entities and organizational structures in which NFPs have interests are grouped into three broad categories:[2]

For-profit (FP) with a corporate structure

FP with a non-corporate structure, such as a general partnership, LLP, LLC, or direct ownership interest in an entity.

NFP with a corporate structure[3]

[2] With the aim of advancing these issues, this document does not consider interests in trusts, including trusts related to split interest agreements and beneficial interests in perpetual trusts.

[3] As discussed in Appendix B to this document, AcSEC believes an entity with a non-corporate structure, in which an NFP has an interest, is not an

These categories are then broken down further depending on whether (a) the NFP is a general partner or limited partner (for interests in entities with a non-corporate structure) (b) the interest represents real estate or other than real estate. **[Though some of the discussion in this document distinguishes between interests in real estate and interests in other than real estate, ultimately this document includes the conclusion that AcSEC asks FASB to provide guidance at the authoritative level that NFPs should apply all the guidance in SOP 78-9 (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate interests.]**

NFP because it would not meet the characteristics of an NFP pursuant to the definition of an *NFP* under FAS 116. Specifically, it would not meet the characteristics of an NFP due to the existence of ownership interests and the provision of lower costs or other economic benefits directly and proportionally to the owners, members, or participants. **[Practice is diverse. Accordingly, AcSEC asks FASB to provide this guidance at the authoritative level. AcSEC could, however, also express this view as part of its NFP guide overhaul project, as "AcSEC believes" or interpretive guidance.]**

LITERATURE CONSIDERED

The following literature is relevant to the discussion in this document:

Consolidation and Equity Method Guidance

SOP 94-3*, Reporting of Related Entities by Not-for-Profit Organizations* (SOP 94-3)[4]

[4] Pursuant to FASB Statement No. 168, *The FASB Accounting Standards Codification ™ and the Hierarchy of Generally Accepted Accounting Principles*, the FASB Accounting Standards Codification (ASC) generally is effective for financial statements issued for interim and annual periods ending after September 15, 2009. To aid readers in using this white paper, as a drafting convention in referencing to (and quoting) sources of authoritative generally accepted accounting principles, this whitepaper sometimes references to pronouncements that were issued prior to the effective date of the ASC, and from which the ASC paragraphs are derived. In particular, this white paper tends to reference or quote guidance in pronouncements that were issued prior to the effective date of the ASC in circumstances in which the ASC disaggregates the guidance in those references or quotes into several sections of the ASC.

- FSP SOP 94-3-1, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations*
- FASB 94, *Consolidation of all Majority-Owned Subsidiaries* (FASB 94)
- ARB 51, *Consolidated Financial Statements* (ARB 51)
- FIN 35, *Criteria for Applying the Equity Method of Accounting for Investments in Common Stock*
- EITF No. 90-15, *Impact of Nonsubstantive Lessors, Residual Value Guarantees, and Other Provisions in Leasing Transactions*
- EITF 96-21, *Implementation Issues in Accounting for Leasing Transactions involving Special-Purpose Entities*
- EITF 97-1, *Implementation Issues in Accounting for Leasing Transactions, including Those involving Special-Purpose Entities*
- EITF No. 97-2, *Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain other Entities with Contractual Management Arrangements*.
- EITF 02-14, *Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock* (EITF 02-14)

- EITF 96-16, *Investment Accounting for Investee when the Investor has a Majority of the Voting Interest but the Minority Shareholders have Certain Approval/ Veto Rights* (EITF 96-16)
- FIN 46R, *Consolidation of Variable Interest Entities* (FIN 46R)
- FASB Statement No. 167, Amendments to FASB Interpretation No. 46R
- APB 18, *The Equity Method of Accounting for Investments in Common Stock* (APB 18).

Investment Guidance

- FASB 124, *Accounting for Certain Investments Held by Not-for-Profit Organizations* (FASB 124)
- AICPA Audit and Accounting Guide, *Not-for-Profit Organizations* (NFP Guide)
- FASB Staff Position FAS 115-1 and FAS 124-1, *The Meaning of Other-Than-Temporary Impairment and Its Application to Certain Investments* (FSP FAS 115-1 and 124-1)

Guidance Pertaining to Real Estate Investments and Non-Corporate Entities

- EITF 03-16, *Accounting for Investments in Limited Liability Corporations* (EITF 03-16)
- EITF Topic D-46, *Accounting for Limited Partner Investments* (Topic D-46)
- EITF 04-5, *Determining whether a General Partner Controls a Limited Partner or Similar Entity when the Limited Partner has Certain Rights* (EITF 04-5)
- SOP 78-9, *Accounting for Investments in Real Estate Ventures* (SOP 78-9)
- FSP SOP 78-9-1, *Interaction of AICPA SOP 78-9 and EITF Issue No. 04-5* (FSP 78-9-1)

Other guidance

- FASB Statement No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust that Raises or Holds Contributions for Others*

- FASB Statement No. 155, *Accounting for Certain Hybrid Financial Instruments*
- FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities*

CONCLUSIONS

Overall Approach

1. The model for reporting NFP interests in other entities should be as follows:

   Does GAAP require consolidation?

   If Yes—Consolidate

   If No—Does GAAP require the equity method of reporting?

   If Yes—Use the equity method

   If No - determine whether GAAP requires or permits fair value or cost

[This model differs from current GAAP and practice, which is diverse, and therefore would need to be promulgated by the FASB as authoritative GAAP.]

Paragraphs 36 to 46 illustrate the application of the guidance in this document.

Interest in a FP – Corporate Structure – Is Consolidation Appropriate?

2. Guidance for determining whether NFPs should consolidate an interest in a FP corporation should be the same as guidance for determining whether FPs should consolidate an interest in a FP corporation, except in circumstances in which authoritative GAAP includes scope exceptions pertaining to NFPs. Identified scope exceptions include (1) NFPs are explicitly scoped out of FIN 46R, *Consolidation of Variable Interest Entities* [ASC 810-10-15-17], except for certain limited exceptions, and (2) certain EITF consensus conclusions (such as 90-15 [ASC 958-810-25-8 pending and ASC 958-810-25-10 pending], 96-21 [ASC 958-810-25-9 pending], and 97-1 [ASC 958-840-55-4 pending] remain effective for NFPs and certain other entities [ASC 958-810-25 pending]. **[This guidance can be included in the guide as the application of existing GAAP.]**

3. In considering whether NFPs should consolidate investments[5] in FPs with corporate structures, NFPs should first consider paragraph 5 of SOP 94-3 [ASC 958-810-15-4]. Paragraph 5 of SOP 94-3 provides as follows:

> Not-for-profit organizations with a controlling financial interest in a for-profit entity through direct or indirect ownership of a majority voting interest in that entity should follow the guidance in ARB No. 51, as amended by FASB Statement Nos. 94, *Consolidation of All Majority-Owned Subsidiaries*, and 144, *Accounting for the Impairment or Disposal of Long-Lived Assets,* in determining whether the financial position, results of operations, and cash flows of the for-profit entity should be included in the not-for-profit organization's financial statements. [FN - EITF Issue No. 04-5 requires consolidation by a general partner of limited partnerships or similar entities (such as limited liability companies that have governing provisions that are the functional equivalent of a limited partnership) unless the rights of the limited partners overcome a presumption that the general partner controls a limited partnership. Paragraphs 6–19 and the examples in Exhibit 04-5A of EITF Issue No. 04-5 provide a framework to determine if a

[5] Throughout most of this document, the document refers to *interests* in other entities, rather than *investments* in other entities, to avoid a bias toward categorizing an interest as held for investment purposes versus mission-related purposes. In describing the requirements of SOP 94-3 [ASC 958-810-25], however, this document sometimes uses the word *investment*, because the ASC [SOP 94-3] sometimes uses the word *investment*.

general partner, or the general partners as a group, controls a limited partnership or similar entity when the limited partners have certain rights. If the presumption of control by the general partners is overcome, each of the general partners should account for its investment in the limited partnership using the equity method of accounting. **[Note: The two sentences following this bold note are as per SOP 94-3, which was conformed to reflect EITF 04-5. AcSEC asks FASB to revise the guidance at the authoritative level to reflect AcSEC's conclusion that the FV reporting per App A of chapter 8 of the NFP Guide should not trump consolidation per 04-5.]** The consensus does not apply to partnerships that are reported at fair value in conformity with paragraphs A.10–A.13 of this Guide. [ASC 958-810-15-4b, d and e] That is, if an organization is required to apply the consolidation guidance included in ARB No. 51 and FASB Statement No. 94 to its investment in a limited partnership, it is within the scope of EITF Issue No. 04-5. It also need not be applied in circumstances in which no single general partner in a group of general partners controls the limited partnership. The consensus opinion in this EITF Issue has been ratified by the FASB. EITF Consensus Opinions are category (c) GAAP as described in SAS No. 69, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles. The accounting conclusions in this SOP are category (b) GAAP as described in SAS No. 69. Including the EITF Consensus Opinions within this SOP does not change their position in the GAAP hierarchy. However, the guidance in this consensus opinion may be relevant in applying the guidance in this SOP and should be considered in conjunction with it. A more detailed summary of this consensus opinion is provided in the "Summary" of "Significant Matters Since the Issuance of this SOP." [FN 6 omitted]

That guidance (paragraph 5 of SOP 94-3 and ASC 958-810-15) generally provides that NFPs should report interests in FPs in the same manner in which FPs report interest in FPs,[6] with exceptions discussed in the following paragraphs.

4. FASB Interpretation No. 46 (revised December 2003), [ASC 810-10], nullified EITF No. 90-15 [ASC 958-810-25-8 pending and ASC 958-810-25-10 pending], 96-21 [ASC 958-810-25-9 pending], and 97-1 [ASC 958-840-55-4 pending] for entities within the scope of FIN 46(R) [variable interest entities per ASC 810-10-15]. Per ASC 810-10-15-17, except in rare instances, NFPs are excluded from the scope of the guidance pertaining to variable interest entities [Interpretation 46(R)].[7,8] Thus, the otherwise nullified EITF guidance still applies to

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[6] For interests in FP entities, circumstances exist in which the owner of the majority voting interest does not control due to contractual arrangements or providing minority owners rights, as discussed in ASC 810-10-25-1 to ASC 810-10-25-14 [EITF 96-16.]

[7] The guidance pertaining to variable interest entities [Interpretation 46(R) in ASC 810 generally is not applicable to NFP parent entities. If a FP subsidiary of an NFP Parent has an interest in another FP entity, however, that interest held by the FP subsidiary should be reported pursuant to the guidance pertaining to variable interest entities in ASC

NFPs. Accordingly, NFPs that are engaged in leasing transactions with special purpose entity lessors should consider whether they should consolidate such lessors in conformity with the consensus guidance in Issues 90-15 [ASC 958-810-25-8 pending and ASC 958-810-25-10 pending], 96-21 [ASC 958-810-25-9 pending], and 97-1 [ASC 958-840-55-4 pending])

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810. For example, if NFP A owns FP B, and FP B owns FP C, NFP A should not apply the guidance pertaining to variable interest entities in ASC 810-10 in reporting its interest in FP B. FP B should, however, consider the guidance pertaining to variable interest entities in ASC 810 in reporting its interest in FP C. **[AcSEC could include this guidance in the NFP guide as implementation guidance.]**

[8] ASC 810-10-15-17a [Paragraph 4(a) of Interpretation 46(R)] states:

> Not-for-profit entities (NFPs) are not subject to the Variable Interest Entities Subsections, except that they may be related parties for purposes of applying paragraphs 810-10-25-42 through 25-44. In addition, if an NFP is used by business reporting entities in a manner similar to a VIE in an effort to circumvent the provisions of the Variable Interest Entities Subsections, that NFP shall be subject to the guidance in the Variable Interest Entities Subsections

Thus, except for abusive use of NFPs to avoid consolidation, the Interpretation does not apply to the consolidation **by** a NFP or **of** a NFP.

5. In addition, NFPs should consider the guidance in ASC 810-10-25 pertaining to physician practice management entities and certain other entities with contractual management arrangements. [EITF No. 97-2, *Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain Other Entities with Contractual Management Arrangements*.[9] ASC 810-10-25

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[9] Per ASC 810-10-15-20 [EITF 97-2], the guidance in the Consolidation of Entities Controlled by Contract Subsections of ASC 810-10-25 applies, in part, to contractual management arrangements with both of the following characteristics:

a. Relationships between entities that operate in the health care industry including the practices of medicine, dentistry, veterinary science, and chiropractic medicine (for convenience, entities engaging in these practices are collectively referred to as physician practices)

b.Relationships in which the physician practice management entity does not own the majority of the outstanding voting equity instruments of the physician practice, whether because the physician practice management entity is precluded by law from owning those equity instruments or because the physician practice management entity has elected not to own those equity instruments.

Further, ASC 810-10-15-20 provides that

> As stated in the preceding paragraph [ASC 810-10-15-19], there may be industries other than the health care industry in which a contractual management arrangement is established under circumstances similar to those addressed in the Consolidation of Entities Controlled by Contract Subsections”

provides that a PPM can establish a controlling financial interest in a physician practice through contractual management arrangements. Specifically, a controlling financial interest exists if, for a requisite period of time, the PPM has "control" over the physician practice and has a "financial interest" in the physician practice that meets certain requirements listed in ASC 810-10-15-22 [EITF 97-2]. **[AcSEC could include this guidance in the NFP guide as the application of existing GAAP.]**

6. SOP 78-9, *Accounting for Investments in Real Estate Ventures,*[10] provides guidance for investments in real estate. Paragraph 5 of SOP

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and as stated in ASC 810-10-15-19:

> [T]he guidance in the Consolidation of Entities Controlled by Contract Subsections applies to all entities that are not determined to be variable interest entities (VIEs)… if the circumstances are similar to those described in the Consolidation of Entities Controlled by Contract Subsections.

[This guidance can be included in the guide as the application of existing GAAP.]

[10] Footnote 2 of FSP No. SOP 94-3-1 and AAG HCO-1, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations*, which does not appear to be explicitly included in the ASC, provides that "[w]hile SOP 78-9 specifically addresses real estate partnerships and other ventures, in practice the guidance often is used for similar entities in other industries by analogy." This discussion document is prepared from the perspective that under current NFP GAAP, SOP 78-9

78-9 [ASC 970-323-25-10 and 970-323-25-11], which applies to real estate corporate joint ventures, provides as follows:

> .05 Paragraph 3 of APB Opinion 18 states that "an entity which is a subsidiary of one of the 'joint venturers' is not a corporate joint venture." A subsidiary, according to that opinion, refers to
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> > . . . a corporation which is controlled, directly or indirectly, by another corporation. The usual condition for control is ownership of a majority (over 50 percent) of the outstanding voting stock. The power to control may also exist with a lesser percentage of ownership, for example, by contract, lease, agreement with other stockholders, or by court decree.
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> Accordingly, an investment in a corporate subsidiary that is a real estate venture should be accounted for by the investor-parent using the principles applicable to investments in subsidiaries rather than those applicable to investments in corporate joint ventures. Minority shareholders in such a real estate venture should account for their investment using the principles applicable to investments in common stock set forth in APB Opinion 18

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applies only to investments in real estate ventures (and is limited to certain equity method guidance in SOP 78-9). **[This discussion document concludes, however, that AcSEC should ask FASB to provide guidance at the authoritative level that NFP's should apply all the guidance in SOP 78-9 (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate. AcSEC could consider, however, including this in the NFP guide as "AcSEC believes best practice is..." guidance.]**

or in FASB Statement No. 115, *Accounting for Certain Investments in Debt and Equity Securities*.

Accordingly, NFPs should consolidate ownership interests in corporate real estate ventures in circumstances in which those interests are over 50 percent pursuant to existing GAAP. **[AcSEC asks FASB to provide guidance at the authoritative level that NFP's should apply all the guidance in SOP 78-9 (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate interests. But perhaps AcSEC could say in the AICPA NFP Guide that "AcSEC believes best practice is..." if FASB does nothing and AcSEC wishes to narrow some choices.]**

7. If the interest is not consolidated, NFPs should consider whether the interest should be reported using the equity method, as discussed in **paragraphs 11 to 17**.

Interest in a FP - Corporate or Non-Corporate Structure - Is the Equity Method Appropriate?[11]

[11] ASC 958-605-25 [FASB Statement No. 136], establishes standards for transactions in which an entity—the donor—makes a contribution by transferring assets to a not-for-profit organization or charitable trust—the recipient organization—that accepts the assets from the donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to another entity—the beneficiary—that is specified by the donor. It also establishes standards for transactions that

[As noted in *paragraph 9*, AcSEC asks FASB to provide guidance at the authoritative level that NFPs should apply all the guidance in SOP 78-9 (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate interests.]

8. NFPs should report interests in FPs (that are not consolidated) held via (a) common stock or (b) noncontrolling interests in partnerships, limited liability companies, and similar entities using the equity method if required by ASC 958-810-15-4 [SOP 94-3]. That guidance generally provides that NFPs should report those interests in the same manner in which FPs report those interests, with exceptions for circumstances in which the interest is instead reported at fair value, as discussed in the following paragraphs.

9. Paragraphs 6, 6a, and 7 of SOP 94-3 (as revised per FASB FSP 94-3-1, *Omnibus Changes to Consolidation and Equity Method Guidance for Not-for-Profit Organizations*) [ASC 958-810-15-4], provide as follows:

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take place in a similar manner but are not contributions because the transfers are revocable, repayable, or reciprocal. Certain transactions that might otherwise appear to be advances to joint ventures, equity method investments, or other kinds of investments may instead be subject to the guidance in ASC 958-605-25 [FASB Statement 136]. **Appendix A** of this document discusses ASC 958-605-25 [FASB Statement 136] in more detail.

6. Investments in common stock of for-profit entities wherein the not-for-profit organization has 50 percent or less of the voting stock in the investee should be reported under the equity method in conformity with Accounting Principles Board (APB) Opinion No. 18, *The Equity Method of Accounting for Investments in Common Stock*, if the guidance in that Opinion requires use of the equity method, subject to the exception in paragraph .07 of this SOP. [**FN** - EITF Issue No. 02-14, *Whether an Investor Should Apply the Equity Method of Accounting to Investments Other Than Common Stock*, requires use of the equity method for investments that are deemed "in-substance common stock" (as defined in the consensus opinion). The consensus opinion in this EITF Issue has been ratified by the FASB. EITF Consensus Opinions are category (c) GAAP as described in AU section 411, *The Meaning of* Present Fairly in Conformity With Generally Accepted Accounting Principles. The accounting conclusions in this SOP are category (b) GAAP as described in AU section 411. Including the EITF Consensus Opinions within this SOP does not change their position in the GAAP hierarchy. However, the guidance in this consensus opinion may be relevant in applying the guidance in this SOP and should be considered in conjunction with it. A summary of this consensus opinion is provided in the "Summary" of "Significant Matters Since the Issuance of this SOP."] Also, not-for-profit organizations should make the financial statement disclosures required by APB Opinion No. 18 if the guidance in that Opinion requires them.

.06A Subject to the fair value exceptions in paragraph 7 of this SOP, noncontrolling interests in for-profit real estate partnerships, limited liability companies, and similar entities in which the not-for-profit organization has more than a minor interest shall be reported under the equity method in accordance with the guidance in AICPA Statement of Position 78-9, *Accounting for Investments in Real Estate Ventures*. [FN 6a - Paragraph 7 of SOP 78-9 indicates that noncontrolling general partners should account for their investments using the equity method. Paragraphs 8 and 10 of the SOP indicate that the equity method also should be used for noncontrolling limited partners unless such partner's interest is "so minor that the limited partner [has] virtually no influence over partnership operating and financial policies."] Not-for-profit organizations shall apply the guidance in FASB Staff Position SOP 78-9-1, *Interaction of AICPA Statement of Position 78-9 and EITF Issue No. 04-5,* to help determine whether their interests in for-profit partnerships, LLCs, and similar entities are controlling interests or noncontrolling interests. Not-for-Profit Organizations shall apply the guidance in EITF Issue No. 03-16, *Accounting for Investments in Limited Liability Companies*, to determine whether an LLC should be viewed as similar to a partnership, as opposed to a corporation, for purposes of determining whether noncontrolling interests in an LLC or a similar entity should be accounted for in accordance with SOP 78-9 and related guidance or Opinion 18.

.07. Chapter 8 of the AICPA Audit and Accounting Guide *Not-for-Profit Organizations*) permits investment portfolios to be reported at fair value in certain circumstances. FASB Statement No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities,—Including an amendment of FASB Statement No. 115,* permits common stock, "in-substance common stock," and other investments that are financial instruments to be reported at fair value. Not-for-profit organizations are permitted to report investment portfolios at fair value in conformity with that guide or make an election to report investments in common stock, "in-substance common stock," or other financial instruments at fair value pursuant to FASB Statement No. 159 instead of applying the equity method of accounting to investments covered by paragraphs 6 and 6A of this SOP.

10. Note that ASC 810-20-25-10 and 810-20-25-11 [EITF 04-5], and paragraph 5 of SOP 94-3 [958-810-15-4 and related guidance] provide that for a limited partnership, if the limited partners possess substantive kick-out rights or participating rights, presumption of control by the general partners is overcome and each of the general partners should account for its investment in the limited partnership using the equity method of accounting.

11. **As noted in paragraph 9, AcSEC asks FASB to provide guidance at the authoritative level that NFP's should apply all the guidance in SOP 78-9 (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate interests.**

12. In addition, NFPs should consider the guidance in ASC 323 and ASC 323-30-S99-1 [APB 18 and related guidance, including EITF Topic D-46 and FIN 35],[12] pertaining to determining

[12] ASC 323-30-S99-1 [Topic D-46] is an SEC staff position and therefore does not currently apply to NFPs that are not SEC registrants. ASC 323-30-S99-1 [Topic D-46] provides that investments in all limited partnerships should be accounted for pursuant to paragraph 8 of SOP 78-9. That guidance requires the use of the equity method [by limited partners] unless

whether the NFP has significant influence. **[The FASB should provide this guidance through authoritative GAAP. But perhaps AcSEC could say in the AICPA NFP Guide that "AcSEC believes best practice is..." if FASB does nothing and AcSEC wishes to narrow some choices.]**

13. ASC 825 [FASB Statement No. 159] provides that entities are permitted to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. (Among financial instruments that are excluded from the scope of ASC 825 [Statement 159], and therefore ineligible for the fair value option, are investments in a subsidiary that the entity is required to consolidate.)

14. If the interest is not consolidated or reported using the equity method, NFPs should consider whether the interest should be reported at cost or fair value, as discussed in **paragraph 35**.

Interest in a FP – Non-Corporate Structure - Is Consolidation Appropriate?

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the investor's interest "is so minor that the limited partner may have virtually no influence over partnership operating and financial policies." The SEC staff understands the practice generally has viewed investments of more than 3 to 5 percent to be more than minor.

15. Guidance for determining whether NFPs should consolidate an interest in an unincorporated FP entity should be the same as guidance for determining whether FPs should consolidate an interest in an unincorporated FP entity, except in circumstances in which authoritative GAAP includes scope exceptions pertaining to NFPs (no such exceptions are identified at this time), and except that NFPs should apply all the guidance in SOP 78-9 to both real estate and non-real estate interests. Certain issues specific to applying GAAP to interests in noncorporate FP entities are discussed in **paragraphs 19 to 23** of this document.

16. In practice, questions exist about whether the consolidation guidance in section 810 that is derived from ARB 51 applies to interests in unincorporated entities. Those questions stem in large part from the guidance in 810-10-15-8 [paragraph 2 of ARB 51], which provides, in part:

> The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, of more than 50 percent of the outstanding voting shares of another entity is a condition pointing toward consolidation.

17. Some believe that guidance infers that only entities with voting shares, such as corporations with voting shares of stock, are required

to be consolidated pursuant to the consolidation guidance in section 810 that is derived from ARB 51; and that entities without voting shares of stock, such as partnerships, are exempt from being consolidated pursuant to the consolidation guidance in section 810 that is derived from ARB 51. The ASC, in codifying the guidance in ARB 51 and other GAAP, provides as follows:

810-10-10-1 - The purpose of consolidated statements is to present, primarily for the benefit of the shareholders and creditors of the parent entity, the results of operations and the financial position of a parent entity and its subsidiaries [Glossary definition of subsidiary an entity that is controlled, directly or indirectly, by another entity. Open - the following is pending content; see transition guidance in a 10-10-65-1. An entity, including an unincorporated entity such as a partnership or trust, in which another entity, known as its parent, holds a controlling financial interest...] essentially as if the group were a single entity with one or more branches or divisions. There is a presumption that consolidated statements are more meaningful than separate statements and that they are usually necessary for a fair presentation when one of the entities in the group directly or indirectly has a controlling financial interest in the other entities. *(Derived from paragraph 1 of ARB 51.)*

810-10-15-8 - The usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one reporting entity, directly or indirectly, of more than 50 percent of the outstanding voting shares of another entity is a condition pointing toward consolidation. *(Derived from paragraph 1 of ARB 51.)* The power to control may also exist with a lesser percentage of ownership, for example, by contract, lease, agreement with other stockholders, or by court decree.

810-10-15-10 - A reporting entity shall apply consolidation guidance for entities that are not in the scope of the Variable Interest Entities Subsections (see the Variable Interest Entities Subsection of this Section) as follows:

a. All majority-owned subsidiaries—all entities in which a parent has a controlling financial interest through direct or indirect ownership of a majority voting interest—shall be consolidated. However, there are exceptions to this general rule.

1. A majority-owned subsidiary shall not be consolidated if control does not rest with the majority owner [Glossary - **Note**: The following definition is Pending Content; see Transition Guidance in 805-10-65-1 and 810-10-65-1. The term owners is used broadly to include holders of ownership interests (equity interests) of investor-owned or mutual entities. Owners include shareholders, partners, proprietors, or members or participants of mutual entities], for instance, if any of the following are present:

i. The subsidiary is in legal reorganization

ii. The subsidiary is in bankruptcy

iii. The subsidiary operates under foreign exchange restrictions, controls, or other governmentally imposed uncertainties so severe that they cast significant doubt on the parent's ability to control the subsidiary.

iv. In some instances, the powers of a shareholder with a majority voting interest to control the operations or assets of the investee are restricted in certain respects by approval or veto rights granted to the minority shareholder (hereafter referred to as minority rights). In paragraphs 810-10-25-2 through 25-14, the term *minority shareholder* refers to one or more minority shareholders. Those minority rights may have little or no impact on the ability of a shareholder with a majority voting interest to control the investee's operations or assets, or, alternatively, those rights may be so restrictive as to call into question whether control rests with the majority owner.

v. Control exists through means other than through ownership of a majority voting interest, for example as described in (b) through (e).

2. A majority-owned subsidiary in which a parent has a controlling financial interest shall not be consolidated if the parent is a broker-dealer within the scope of Topic 940 and control is likely to be temporary.

3. Except as discussed in paragraph 946-810-45-3, consolidation by an investment company within the scope of Topic 946 of a non-investment-company investee is not appropriate.

b. Subtopic 810-20 shall be applied to determine whether the rights of the limited partners in a limited partnership overcome the presumption that the general partner controls, and therefore should consolidate, the partnership.

c. Subtopic 810-30 shall be applied to determine the consolidation status of a research and development arrangement.

d. The Consolidation of Entities Controlled by Contract Subsections of this Subtopic shall be applied to determine whether a contractual management relationship represents a controlling financial interest.

e. Paragraph 710-10-45-1 addresses the circumstances in which the accounts of a rabbi trust that is not a VIE (see the Variable Interest Entities Subsections for guidance on VIEs) shall be consolidated with the accounts of the employer in the financial statements of the employer

> ASC 810-10-25-1 - Consolidation is appropriate if a reporting entity has a controlling financial interest in another entity and a specific scope exception does not apply (see Section 810-10-15). The usual condition for a controlling financial interest is ownership of a majority voting interest, but in some circumstances control does not rest with the majority owner.

Based on the above, AcSEC believes that the general principles of consolidation are applicable to all entity structures, including unincorporated entities, and not merely entities for which stock ownership exists. Accordingly, as stated in ASC 810-10-25-1, "consolidation is appropriate if a reporting entity has a controlling financial interest in another entity and a specific scope exception does not apply." **[AcSEC could consider explicitly clarifying this in the NFP guide.]**

18. Paragraph 3 of EITF 04-5 [ASC 958-810-15-4b and e],[13] in addressing limited partnerships and similar entities, should be read as excluding from the scope of EITF 04-5 limited partnership interests that are required to be reported at fair value pursuant to GAAP (such as investments in limited partnerships held by investment companies), rather than limited partnership interests that are permitted to be reported at fair value pursuant to GAAP (such as investments in limited partnerships reported at fair value pursuant to ASC 958-325-35 [Appendix A of chapter 8 of the NFP Guide]. **[As discussed in the note embedded in *__paragraph 6__* of this document, given that the**

[13] In circumstances in which the NFP is a GP in a limited partnership, the NFP should first consider the guidance in EITF 04-5. In circumstances in which EITF 04-5 requires consolidation, NFPs should consolidate the limited partnership in which they have an interest.

NFP Guide and practice, however, excludes from the scope of the EITF 04-5 limited partnership interests that are reported at fair value as permitted by ASC 958-325-35 [Appendix A of chapter 8 of the NFP Guide], AcSEC asks FASB to eliminate, through a change to authoritative GAAP, SOP 94-3's [ASC 958-810-15-4b and e] provision that reporting investments at fair value in conformity with ASC 958-325-35 [Appendix A of chapter 8 of the NFP Guide] qualifies for the fair value scope exclusion included in EITF 04-5. AcSEC concluded that it should ask FASB to revise the guidance at the authoritative level to reflect AcSEC's conclusion that the FV reporting per ASC 958-325-35 [Appendix A of chapter 8 of the NFP Guide] should not trump consolidation per 04-5.]

19. ASC 970-323-25-3 and 970-323-25-4 [Paragraph 6 of SOP 78-9], which apply to real estate general partnerships, discuss consolidation accounting, among other issues, and provide as follows:

> 25-3 Many provisions of Topic 323 are appropriate in accounting for investments in certain unincorporated entities. The principal difference, aside from income tax considerations, between corporate joint ventures and general partnerships is that the individual investors in general partnerships usually assume joint and several liability. The equity method, however, enables noncontrolling investors in general partnerships to reflect the underlying nature of their investments in those ventures as well as it does for investors in corporate joint ventures. Accordingly, investments in noncontrolled real estate

> general partnerships shall be accounted for and reported under the equity method.
>
> 25-4 An entity shall apply the one-line equity method of presentation in both the balance sheet and the statement of income. Pro rata consolidation is not appropriate except in the limited circumstances described in paragraph 810-10-45-14. Topic 323 shall be used as a guide in applying the equity method

ASC 970-810-25-1 and 970-810-25-2 [SOP 78-9, paragraph 7; and APB 18], which apply to interests in real estate general partnerships, provide as follows:

> 25-1 A general partnership that is controlled, directly or indirectly, by an investor is, in substance, a subsidiary of the investor. Paragraph 810-10-15-8 states that the usual condition for a controlling financial interest is ownership of a majority voting interest, and, therefore, as a general rule ownership by one entity, directly or indirectly, of over 50 percent of the outstanding voting shares of another entity is a condition pointing toward consolidation. However, if partnership voting interests are not clearly indicated, a condition that would usually indicate control is ownership of a majority (over 50 percent) of the financial interests in profits or losses (see paragraphs 970-323-35-16 through 35-17). Paragraph 810-10-15-8 states that the power to control may also exist with a lesser percentage of ownership, for example, by contract, lease, agreement with other stockholders, or by court decree. The power to control may also exist with a lesser percentage of ownership by agreement with other partners.
>
> 25-2 On the other hand, the majority interest holder may not control the entity if one or more of the other partners have substantive participating rights that permit those other partners to effectively participate in significant decisions that would be expected to be made in the ordinary course of business. The determination of whether the rights of the

other partners are substantive participating rights shall be evaluated in accordance with the guidance for substantive participating rights in Subtopic 810-20. If the other partners have substantive participating rights, the presumption of control by the majority interest holder is overcome. A controlling investor shall account for its investment under the principles of accounting applicable to investments in subsidiaries. Accordingly, interentity profits and losses on assets remaining within the group shall be eliminated. A noncontrolling investor in a general partnership shall account for its investment by the equity method and should be guided by the provisions of Topic 323.

[In addition, as noted in paragraph 9 of this white paper, AcSEC asks FASB to provide guidance at the authoritative level that NFP's should apply all the consolidation and equity method guidance in ASC 970 [SOP 78-9] (corporate joint venture guidance, consolidation guidance and equity method guidance) to both real estate and non-real estate interests.]

20. ASC 970-323-25-5, which applies to real estate limited partnerships, provides as follows:

> 25-5 For guidance on determining whether a general partner shall consolidate a limited partnership or apply the equity method of accounting to its interests in the limited partnership, see paragraph 970-810-25-2. **[Note: 970-810-25-2 appears to be a bad reference, because it purports to reference to guidance on interests in limited partnerships, but 970-810-25-2 addresses interests in general partnerships. Staff submitted a comment on the ASC. Presumably, the reference**

should be to 970-810-25-3, which addresses interests in real estate limited partnerships.]

ASC 970-810-25-3 [paragraph 9 of SOP 78-9 and EITF 04-5], which addresses interests in real estate limited partnerships, provides as follows:

> The rights and obligations of the general partners in a limited partnership are different from those of the limited partners and, accordingly, the general partners shall be presumed to control the limited partnership. However, the rights of the limited partners may overcome that presumption of control. The guidance in Subtopic 810-20 shall be used to determine whether the rights of the limited partners overcome the presumption of control by the general partners:
>
> a. If the presumption of control by the general partners is overcome by the rights of the limited partners, the general partners shall apply the equity method of accounting to their interests.
>
> b. If the presumption of control by the general partners is not overcome by the rights of the limited partners and no single general partner controls the limited partnership, the general partners shall apply the equity method of accounting to their interests.
>
> c. If the presumption of control is not overcome by the rights of the limited partners and a single general partner controls the limited partnership, that general partner shall consolidate the limited partnership and apply the principles of accounting applicable for investments in subsidiaries.

> 25-8 If the substance of the partnership arrangement is such that the general partners are not in control of the major operating and financial policies of the partnership, a limited partner may be in control. An example could be a limited partner holding over 50 percent of the total partnership interest. A controlling limited partner shall be guided in accounting for its investment by the principles for investments in subsidiaries. Noncontrolling limited partners shall account for their investments by the equity method and shall be guided by the provisions of Topic 323, as discussed in the guidance beginning in paragraph 970-323-25-2, or by the cost method, as discussed in the guidance beginning in paragraph 970-323-25-5, as appropriate.

21. If the interest is not consolidated, NFPs should consider whether the interest should be reported using the equity method, **as discussed in paragraphs 11 to 17 of this document**.

Interest in an NFP - Is Consolidation Appropriate?

22. Guidance for determining whether NFPs should consolidate an interest in an NFP should be pursuant to ASC 958-810-25 [SOP 94-3].

23. NFPs may have an interest in one or more other NFPs through various means, including control[14] and economic interest. ASC 958-810-25 [SOP 94-3] is the applicable literature for reporting a relationship with another NFP. The guidance in ASC 958-810-25 [SOP 94-3] pertaining to interests in NFPs focuses on (1) various kinds of control and (b) economic interest. Certain kinds of control always result in consolidation, while other kinds of control result in consolidation only if coupled with an economic interest. Still other kinds of control result in consolidation being permitted but not required if coupled with an economic interest. The relevant sections of SOP 94-3 are summarized in the following paragraphs.

24. ASC 958-810-25-2 (pending content) [Paragraph 10 of SOP 94-3] provides that an NFP with a controlling financial interest in another NFP through direct or indirect ownership of a majority voting interest or sole corporate membership should consolidate[15] the other NFP.

[14] The Glossary of ASC 958-810-25 [SOP 94-3] defines *control* as "the direct or indirect ability to determine the direction of management and policies through ownership, contract, or otherwise."

[15] Unless control does not rest with the majority owner or sole corporate member (for example, if the subsidiary is in legal reorganization or bankruptcy), consolidation is prohibited, as discussed in paragraph 810-10-

25. ASC 958-810-25-3 [Paragraph 11 of SOP 94-3] provides as follows:

> In the case of control of a related but separate NFP through a majority voting interest in the board of the other NFP by means other than ownership or sole corporate membership and an economic interest in other such organizations, consolidation is required, unless control does not rest with the majority holder of the majority voting interest, in which case consolidation is prohibited. An NFP has a majority voting interest in the board of another entity if it has the direct or indirect ability to appoint individuals that together constitute a majority of the votes of the fully constituted board (that is, including any vacant board positions). Those individuals are not limited to the NFP's own board members, employees, or officers. For implementation guidance on a majority voting interest in the board of another entity, see paragraph 958-810-55-5.

15-8. Sole corporate membership in an NFP, like ownership of a majority voting interest in a for-profit entity, shall be considered a controlling financial interest, unless control does not rest with the sole corporate member (for instance, if the other [membership] entity is in bankruptcy or if other legal or contractual limitations are so severe that control does not rest with the sole corporate member). Also, supermajority voting requirements might overcome the presumption of control by the owner or holder of a majority voting interest.

[Note: The Master Glossary of the ASC [Paragraph 3 of APB 18] defines a *corporate joint venture* as follows:

> A corporation owned and operated by a small group of entities (the joint venturers) as a separate and specific business or project for the mutual benefit of the members of the group. A government may also be a member of the group. The purpose of a corporate joint venture frequently is to share risks and rewards in developing a new market, product or technology; to combine complementary technological knowledge; or to pool resources in developing production or other facilities. A corporate joint venture also usually provides an arrangement under which each joint venturer may participate, directly or indirectly, in the overall management of the joint venture. Joint venturers thus have an interest or relationship other than as passive investors. An entity that is a subsidiary of one of the joint venturers is not a corporate joint venture. The ownership of a corporate joint venture seldom changes, and its stock is usually not traded publicly. A minority public ownership, however, does not preclude a corporation from being a corporate joint venture

The ASC's Master Glossary definition of a *joint venture*, as opposed to a *corporate joint venture*, [EITF 01-2] provides that "…a joint venture is not limited to corporate entities."

26. 958-810-25-4 [Paragraph 12 of SOP 94-3] provides that an NFP is permitted but not required to consolidate a related but separate NFP

if the reporting NFP exercises control of the NFP in which it has an economic interest by means other than majority ownership interest, sole corporate membership, or a majority voting interest in the board of the other NFP. In other words, if control other than the kind of control described in ASC 958-810-25-2 and ASC 958-810-25-3 [paragraphs 10 and 11 of SOP 94-3] exists, such as control through contract or affiliation agreement, and an economic interest exists, consolidation is permitted but not required. (If the reporting NFP elects not to consolidate the other NFP, the reporting NFP should make certain financial statement disclosures.)

27. A controlling interest by an NFP in another NFP may be less than a complete interest. 958-810-25-6 provides that if the conditions for consolidation in ASC 958-810 [SOP 94-3] are met, the basis of that consolidation should not reflect a minority interest for that portion of the board that the reporting entity does not control.

28. In addition, as discussed in **paragraph 7** above, FASB Interpretation No. 46 (revised December 2003), *Consolidation of*

Variable Interest Entities [ASC 810], nullified EITF No. 90-15; 96-21*;* and 97-1 for entities within the scope of FIN 46(R). Except in rare instances, NFPs are excluded from the scope of the guidance pertaining to variable interest entities in ASC 810.[16] Thus, the otherwise nullified EITF guidance still applies to NFPs. Accordingly, NFPs that are engaged in leasing transactions with special purpose entity lessors, including lessors that are NFP's, should consider whether they should consolidate such lessors in conformity with the consensus guidance in Issues 90-15 [ASC 958-810-25-8 pending and ASC 958-810-25-10 pending], 96-21 [ASC 958-810-25-9 pending], and 97-1 [ASC 958-840-55-4 pending]**.**

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[16]ASC 810-10-15-17a [Paragraph 4(a) of Interpretation 46(R)] states:

> [NFPs] are not subject to the Variable Interest Entities Subsections, except that they may be related parties for purposes of applying paragraphs 810-10-25-42 through 25-44. In addition, if an NFP is used by business reporting entities in a manner similar to a VIE in an effort to circumvent the provisions of the Variable Interest Entities Subsections, that NFP shall be subject to the guidance in the Variable Interest Entities Subsections.

Thus, except for abusive use of NFPs to avoid consolidation, the guidance pertaining to variable interest entities in ASC 810 [FIN 46 ®] does not apply to the consolidation **by** a NFP or **of** a NFP.

29. As discussed in **paragraph 33** of this white paper, if that interest is not consolidated, NFPs should not report that interest using the equity method.

Interest in an NFP – Is the Equity Method Appropriate[17]

30. AcSEC considered whether NFPs with an interest in another NFP (that is not consolidated) should report that interest using the equity method. Specifically, AcSEC considered whether it is appropriate to report an interest in another NFP using the equity

[17] As discussed in **footnote 11** of this document, ASC 958-605-25 [FASB Statement 136] establishes standards for transactions in which an entity—the donor—makes a contribution by transferring assets to a not-for-profit organization or charitable trust—the recipient organization—that accepts the assets from the donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to another entity—the beneficiary—that is specified by the donor. It also establishes standards for transactions that take place in a similar manner but are not contributions because the transfers are revocable, repayable, or reciprocal. Certain transactions that might otherwise appear to be advances to joint ventures, equity method investments, or other kinds of investments may instead be transfers and subject to the guidance in ASC 958-605-25 [FASB Statement 136]. **Appendix A** of this document discusses ASC 958-605-25 [FASB Statement 136] in more detail.

method if the NFP has significant influence over the operating and financial policies, coupled with an economic interest. AcSEC believes interests in NFPs should not be reported using the equity method. The equity method implies an ownership interest, and the definition of an *NFP* excludes entities with ownership interests like those of a business enterprise, and all investor-owned enterprises or entities that provide various economic benefits directly and proportionately to their owners, members, or participants entities. In addition to the view that it's an oxymoron to have an equity interest in an NFP, AcSEC believes it would not be operational to determine the measurement of such equity interests. For example, NFP A may control 4 of 10 of NFP B's board seats, and have an economic interest. That equity interest may not necessarily equal 40 percent of the net assets of NFP B, and likely would not otherwise be quantifiable. Accordingly, it would not be operational to measure that economic interest.

31. In circumstances in which an NFP transfers resources to another NFP without obtaining an interest, the transfer is either:

- contribution expense
- another type of expense or reduction of a liability (If paying for goods or services received from that other NFP)
- loan receivable, or
- some other type of asset represented by contractual rights (rather than an interest).

[Practice is diverse. Accordingly, AcSEC asks FASB to provide this guidance at the authoritative level. AcSEC could, however, consider including this guidance in the NFP guide as implementation guidance.]

Interests in FP - Corporate or Non-Corporate Structure - if Neither Consolidation or Equity Method is Appropriate - Cost or FV[18]

32. In circumstances in which an interest in a FP exists and neither consolidation nor the equity method is appropriate, NFPs

[18] As discussed in **footnote 11** of this document, ASC 958-605-25 [FASB Statement 136] establishes standards for transactions in which an entity—the donor—makes a contribution by transferring assets to a not-for-profit organization or charitable trust—the recipient organization—that accepts the assets from the donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to another entity—the beneficiary—that is specified by the donor. It also establishes standards for transactions that take place in a similar manner but are not contributions because the transfers are revocable, repayable, or reciprocal. Certain transactions that might otherwise appear to be advances to joint ventures, equity method investments, or other kinds of investments may instead be transfers and subject to the guidance in ASC 958-605-25 [FASB Statement 136]. **Appendix A** of this document discusses ASC 958-605-25 [FASB Statement 136] in more detail.

should consider whether the interest is within the scope of ASC 958-320-35-1 [FASB Statement No. 124] or ASC 815 [FASB Statement No. 133]. If the interest is within the scope of ASC 958-320-35-1 [FASB Statement No. 124] or ASC 815 [FASB Statement No. 133], it should be reported in conformity with that guidance. If the interest is not within the scope of ASC 958-320-35-1 [FASB Statement No. 124] or ASC 815 [FASB Statement No. 133] (and not consolidated or reported pursuant to the equity method), it should be reported at cost, unless it is reported at fair value pursuant to authoritative GAAP, such as ASC 815-15-25 or ASC 825-10 [FASB Statement Nos.155 or 159. [Embedded in this conclusion is deleting ASC 958-325-35-1 to ASC 958-325-35-7 (Appendix A of chapter 8 of the NFP Guide, other than the guidance pertaining to equity securities accounted for under the cost method.)]. **AcSEC asks FASB to provide this guidance at the authoritative level.]**

ILLUSTRATIONS

Interest in a Unincorporated Joint Venture- Joint meeting of Two NFP's, with a 50/50 Split on the Interests

33. NFP A and NFP B hold their annual meetings at the same time and in the same city. In order to save costs, they merge their meetings via an unincorporated joint venture, negotiating better rates with the hotel and realizing other synergies. They share equally in the decision-making and net proceeds from the meeting.

This transaction is outside the scope of this document, because it is not a separate legal entity.

Ownership of a building by several NFPs, but one NFP has legal title

34. NFPs A, B, and C buy a building together. Title is held in the name of NFP A, but by agreement NFP's A, B, and C each share equally in the risks and rewards of ownership.

This transaction is outside the scope of this document, because it is not a separate legal entity.

<u>Interest in an NFP (significant influence) via the ability to appoint a minority of the board</u>

35. NFP A, whose mission is to help the homeless in City X, appoints 3 of the 10 board members of NFP B, a soup kitchen serving downtown City X.

This circumstance results in no balance sheet reporting for NFP A.

Interest in an FP - Joint meeting of two NFP’s, with a 70/30 split on the interests – general partnership -

36. NFP A and NFP B hold their annual meetings at the same time and in the same city. In order to save costs, they merge their meetings via a general partnership, negotiating better rates with the hotel and realizing other synergies. (They form a general partnership to handle the meeting.) Though they share equally in the decision-making, NFP A has a 70 percent ownership account and NFP B has a 30 percent ownership account.

Neither entity has control and therefore neither entity should consolidate its interest per ASC 958-810-15-4 [SOP 94-3] and ASC 970-810-25-1 and ASC 970-323-25-3 [SOP 78-9]. (SOP 78-9 is made applicable by **paragraph 9** to this document.)

Both entities should apply the equity method per **paragraphs 11 to 17** of this document. (As discussed in **paragraph 22** of this document, ASC 970-810-25-2 [paragraph 7 of SOP 78-9] provides that “a noncontrolling investor in a general partnership shall account for its investment by the equity method and should be guided by the provisions of Topic 323.") (Both entities are permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Interest in a FP with a non-corporate structure - limited partnership – 10 percent GP - RE

37. NFP A sets up a limited partnership with two other NFPs (NFP B and C) to buy a building in which they will house their R & D departments. NFP A is the general partner and has a 10 percent interest. NFP B and C each have 40 percent interests including a right to and responsibility for the partnership operating results, but do not have substantive kickout or participating rights.[19]

[19] General partner is also referred to as a managing member in an LLC.

NFP A should consolidate its interest per ASC 810-20-25-3 [EITF 04-5] and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], per the conclusion in **paragraph 9** of this document.

If NFP B and C have substantive kick-out or participating rights, the presumption of control is overcome and NFP A should report using the equity method per ASC 810-20-25-10 or ASC 810-20-25-11 (EITF 04-5), and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], as discussed in **paragraph 13** of this document.

NFPs B and C should apply the equity method of accounting per ASC 323-30-25-1 and ASC 970-323-25-6 (paragraph 8 of SOP 78-9).

(NFPs A, B, and C are permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Interest in a FP with a non-corporate structure - limited partnership - 80 percent GP - other than RE

38. NFP A sets up a limited partnership with two other NFPs (NFP B and C) to form a shared services entity. NFP A is the general partner and has an 80 percent interest. NFP B and C each have a 10 percent interest, including a right to or responsibility for the partnership's operating results.[20]

NFP A should consolidate its interest per ASC 810-20-25-3 [EITF 04-5] and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], per the conclusion in **paragraph 9** of this document unless the presumption of control by the general partner (NFP A) is overcome by the rights of the limited partners.

If NFP B and C have substantive kick-out or participating rights, the presumption of control is overcome and NFP A should report using the equity method per ASC 810-20-25-10 or ASC 810-20-25-11 [EITF 04-5], and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], as discussed in **paragraph 13** of this document.

[20] General partner is also referred to as a managing member in an LLC.

NFPs B and C should apply the equity method of accounting per ASC 323-30-25-1 and ASC 970-323-25-6 (paragraph 8 of SOP 78-9).

(NFPs A, B, and C are permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

<u>Interest in a FP with a non-corporate structure - general partnership – 40 percent GP - other than RE</u>

39. *NFP A sets up a general partnership with two other NFPs (NFP B and C) to form a shared services entity. NFP A is the general partner and has a 40 percent interest. NFP B and C each have a 30 percent interest including a right to or responsibility for the partnership's operating results.*

Do not consolidate.

Because its a non-controlling interest in a general partnership, use the equity method per ASC 970-810-25-2 and ASC 970-323-25-2 [paragraph 6a of SOP 94-3 and paragraph 6 of SOP 78-9.] (NFP A would be permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Interest in a FP with a non-corporate structure - general partnership – 50 percent GP - RE

40. NFP teams with another entity to create a FP general partnership to acquire a building in which the NFP is one of many tenants. NFP A and the other entity each have a 50 percent interest.

Assuming it is a non-controlling interest in a general partnership, use the equity method as per ASC 970-810-25-2 and ASC 970-323-25-2 [paragraph 6a of SOP 94-3 and paragraph 6 of SOP 78-9.] (NFP A would be permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Interest in an FP with a non-corporate structure - limited partnership - 40 percent LP - investing - RE

Interest in an FP with a non-corporate structure - limited partnership – 10 percent GP – investing RE

41. *NFP forms a FP limited partnership*[21] *with two other NFPs to acquire a building that none of the founding NFPs will use in a mission-related activity. Rather, the building will be used to generate current income and, eventually, capital appreciation. NFP is a 10 percent GP.*

[21] The legal structure could be a LLP or LLC.

NFP should consolidate its interest per ASC 810-20-25-3 [EITF 04-5] and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], per the conclusion in **footnote 12** of this document, unless the presumption of control by the general partner (NFP) is overcome by the rights of the limited partners.

If the other two NFPs have substantive kick-out or participating rights, the presumption of control is overcome and NFP should report using the equity method per ASC 810-20-25-10 or ASC 810-20-25-11 (EITF 04-5), and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], as discussed in **paragraph 13** of this document.

(NFP would be permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

The other two NFPs should apply the equity method of accounting per ASC 323-30-25-1 and ASC 970-323-25-6 (paragraph 8 of SOP 78-9 and paragraph 6a of SOP 94-3).

(The other two NFPs are permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Interest in a FP with a non-corporate structure - limited partnership - 10 percent GP - investing - other than RE

42. NFP invests in a FP private equity LLP. NFP is a 10 percent GP.

NFP should consolidate its interest per ASC 810-20-25-3 [EITF 04-5] and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], per the conclusion in **footnote 12** of this document, unless the presumption of control by the general partner (NFP) is overcome by the rights of the limited partners. If the presumption of control by the general partner (NFP) is overcome by the rights of the limited partners, NFP should report using the equity method per ASC 810-20-25-10 or ASC 810-20-25-11 [EITF 04-5], and ASC 970-810-25-

3 [paragraph 9 of SOP 78-9], as discussed in **paragraph 13** of this document.

If the other NFPs have substantive kick-out or participating rights, the presumption of control is overcome and NFP should report using the equity method per ASC 810-20-25-10 or ASC 810-20-25-11 (EITF 04-5), and ASC 970-810-25-3 [paragraph 9 of SOP 78-9], as discussed in **paragraph 13** of this document. (NFP would be permitted to report at fair value under FAS 159 [ASC 825-10], as an alternative to the equity method.)

Appendix A - ASC 958-605-25, *Transfers of Assets to a Not-for-Profit Entity or Charitable Trust that Raises or Holds Contributions for Others* [FASB Statement No. 136]

ASC 958-605-25-21 to ASC 958-605-25-33, *Transfers of Assets to a Not-for-Profit Entity or Charitable Trust that Raises or Holds Contributions for Others* [FASB Statement No. 136, *Transfers of Assets to a Not-for-Profit Organization or Charitable Trust that Raises or Holds Contributions for Others]*, provides standards for transactions in which an entity—the donor—makes a contribution by transferring assets to a not-for-profit organization or charitable trust—the recipient organization—that accepts the assets from the donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to another entity—the beneficiary—that is specified by the donor. It also provides standards for transactions that take place in a similar manner but are not contributions because the transfers are revocable, repayable, or reciprocal.

ASC 958-605-25-21 to ASC 958-605-25-33 require a recipient organization that accepts cash or other financial assets from a donor and agrees to use those assets on behalf of or transfer those assets, the return on investment of those assets, or both to a specified unaffiliated beneficiary to recognize the fair value of those assets as a liability to the specified beneficiary concurrent with recognition of the assets received from the donor. However, if the donor explicitly grants the recipient organization variance power or if the recipient organization and the specified beneficiary are financially interrelated organizations, the recipient organization is required to recognize the fair value of any assets it receives as a contribution received. Not-for-profit organizations are financially interrelated if (a) one organization has the ability to influence the operating and financial decisions of the other and (b) one organization has an ongoing economic interest in the net assets of the other.

ASC 958-605-25-21 to ASC 958-605-25-33 do not provide standards for a trustee's reporting of assets held on behalf of specified beneficiaries, but do provide standards for a beneficiary's reporting of its rights to assets held in a charitable trust.

ASC 958-605-25-21 to ASC 958-605-25-33 require that a specified beneficiary recognize its rights to the assets held by a recipient organization as an asset unless the donor has explicitly granted the recipient organization variance power. Those rights are either an interest in the net assets of the recipient organization, a beneficial interest, or a receivable. If the beneficiary and the recipient organization are financially interrelated organizations, the beneficiary is required to recognize its interest in the net assets of the recipient organization and adjust that interest for its share of the change in net assets of the recipient organization. If the beneficiary has an unconditional right to receive all or a portion of the specified cash flows from a charitable trust or other identifiable pool of assets, the beneficiary is required to recognize that beneficial interest, measuring and subsequently remeasuring it at fair value, using a valuation technique such as the present value of the estimated expected future cash flows. If the recipient organization is explicitly granted variance power, the specified beneficiary does not recognize its potential for future distributions from the assets held by the recipient organization. In all other cases, a beneficiary recognizes its rights as a receivable.

ASC 958-605-25-33 describes four circumstances in which a transfer of assets to a recipient organization is accounted for as a liability by the recipient organization and as an asset by the resource provider because the transfer is revocable or reciprocal. Those four circumstances are if (a) the transfer is subject to the resource provider's unilateral right to redirect the use of the assets to another beneficiary, (b) the transfer is accompanied by the resource provider's conditional promise to give or is otherwise revocable or repayable, (c) the resource provider controls the recipient organization and specifies an unaffiliated beneficiary, or (d) the resource provider specifies itself or its affiliate as the beneficiary and the transfer is not an equity transaction. If the transfer is an equity transaction and the resource provider specifies itself as beneficiary, it records an interest in the net assets of the recipient organization (or an increase in a previously recognized interest). If the resource provider specifies an affiliate as beneficiary, the resource provider records an equity transaction as a separate line item in its statement of activities, and the affiliate named as beneficiary records an interest in the net assets of the recipient organization. The recipient organization records an equity transaction as a separate line item in its statement of activities.

APPENDIX B – Determining whether an entity is an NFP or a FP

To determine whether an entity is an NFP, NFPs should apply the definition of an Not-for-Profit Entity in the ASC Glossary [Appendix D to FASB 116], which is as follows:

An entity that possesses the following characteristics, in varying degrees, that distinguish it from a business entity:

a. Contributions of significant amounts of resources from resource providers who do not expect commensurate or proportionate pecuniary return

1. Operating purposes other than to provide goods or services at a profit
2. Absence of ownership interests like those of business entities.

Entities that clearly fall outside this definition include the following:

1. All investor-owned entities
2. 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.

AcSEC believes an entity with a non-corporate structure, in which an NFP has an interest, is not an NFP because it would not meet the characteristics of an NFP pursuant to the definition of an *NFP* under the ASC [FAS 116].

Specifically, it would not meet the characteristics of an NFP due to the existence of ownership interests and the provision of lower costs or other economic benefits directly and proportionally to the owners, members, or participants.

Diversity in practice exists, however, in concluding about whether such entities are NFPs. If an NFP takes a portion of its mission-related activities and houses them in an entity that the NFP owns and controls, corporate or otherwise, some believe it is counterintuitive to call that owned and controlled entity anything other than an NFP, merely because a portion of the NFP's activities are carved out and housed in that separate entity. For example, assume a college or university owns real estate and houses students. In circumstances in which that real estate is owned directly by the college or university, its activities would be considered NFP activities of the college or university. If the college or university takes that real estate and houses it in a separate entity that it owns and controls, corporate or otherwise, some believe it is counterintuitive to call that separate entity anything other than an NFP, merely because its activities are carved out and held in a separate entity in which the NFP had an ownership interest. Similarly, if an NFP takes a portion of its investing activities and houses them in an entity in which the NFP has a less than complete interest, corporate or otherwise, some believe it is counterintuitive to call that entity in which the NFP has an interest anything other than an NFP, merely because a portion of the NFP's activities are carved out and housed in that separate entity. For example, assume Museum A has an investment portfolio that holds equity securities. In circumstances in which those equity securities are owned directly by Museum A, activities pertaining to those equity securities would be considered NFP activities of Museum A and accounted for pursuant to NFP GAAP. If Museum A takes those investments and houses them in a separate entity, corporate or otherwise, that it establishes with three other NFP to house all their investments, some believe it is counterintuitive to call that entity housing that investment activity anything other than an NFP, merely because the investments are carved out and held in a separate entity in which the NFP has an ownership interest.

APPENDIX C – Summary of Proposed Changes to Literature

The following is a top-level summary of the changes to financial reporting literature proposed in the draft white paper, *NFP Interests in Other Entities.* This summary is intended to be read in conjunction with and in the context of the draft white paper.

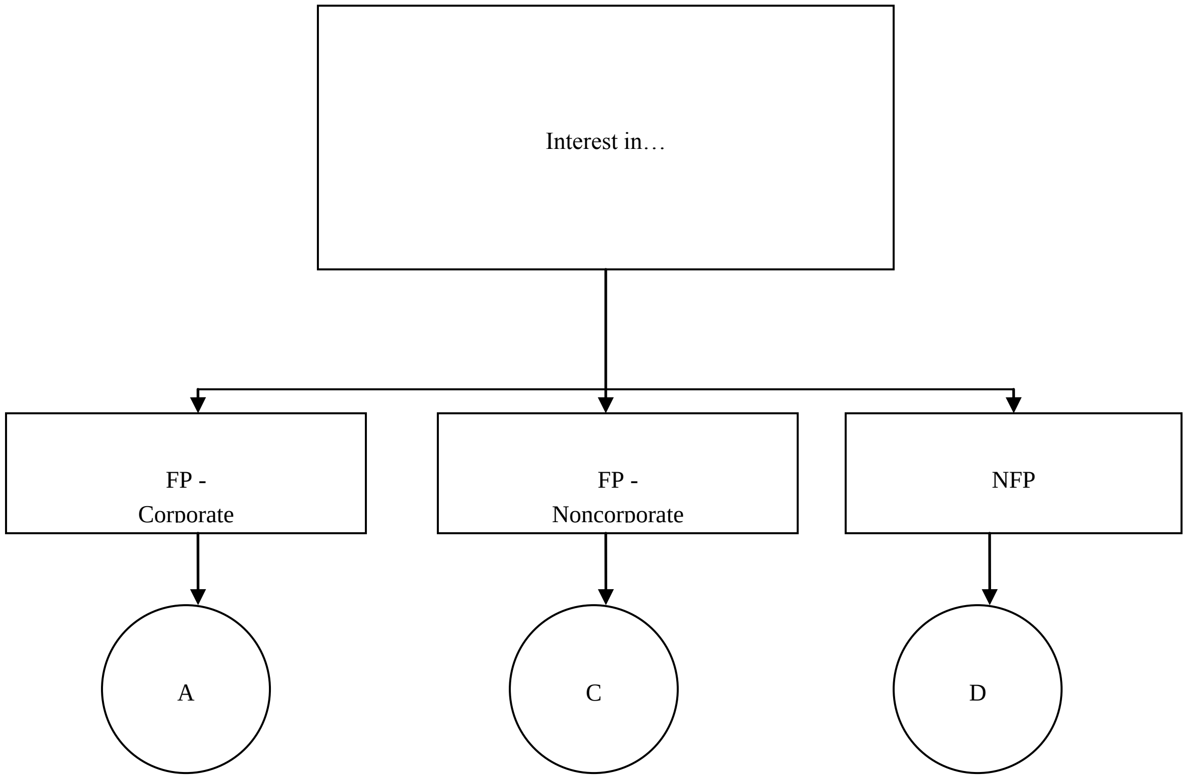
Description of proposed change	*Within the purview of*	*Example of page number or other reference within white paper doc*
Waterfall approach for the overall model: Consolidation? Equity method accounting? Fair value or cost?	FASB literature	4
Articulate the applicability of SPE EITF 90-15, 96-21, and 97-1	AcSEC in AICPA NFP Guide (articulation of existing GAAP)	5
Revise the guidance in the NFP Guide so that the FV option per Appendix A of Chapter 8 does not trump consolidation per EITF 04-5	FASB	6
Clarify that if a FP sub of an NFP parent has an interest in another FP entity, that interest held by the FP sub should be reported pursuant to FIN 46R.	AcSEC in AICPA NFP Guide (implementation guidance)	FN 6 to par 7

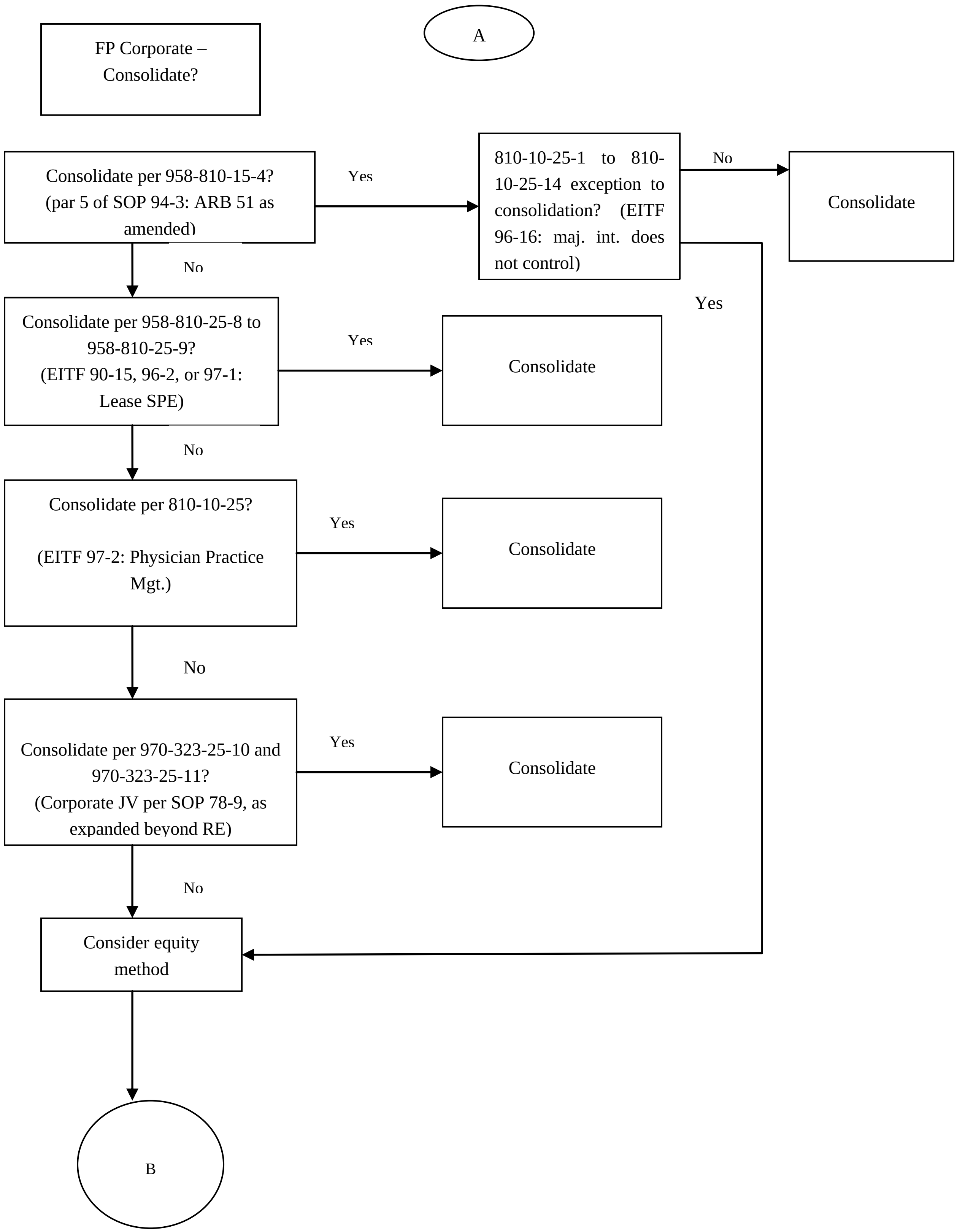
Description of proposed change	*Within the purview of*	*Example of page number or other reference within white paper doc*
NFPs should consider the guidance in EITF 97-2, *Application of FASB Statement No. 94 and APB Opinion No. 16 to Physician Practice Management Entities and Certain other Entities with Contractual Management Arrangements*.	In the AICPA NFP Guide, as the application of existing GAAP	Par 8
Clarify that current GAAP does not require the application of SOP 78-9 beyond real estate equity method accounting (note that AcSEC is also asking to change current GAAP).	AcSEC clarification in AICPA NFP Guide	FN 10
NFPs should apply all the guidance in SOP 78-9 to both real estate and non real estate interests.	FASB (but perhaps some room in AICPA NFP Guide for "AcSEC believes best practice..." if FASB does nothing and AcSEC wishes to reduce diversity in practice)	9
Apply EITF D-46 in determining whether the NFP has significant influence (3 to 5 percent)	FASB (but perhaps some room in AICPA NFP Guide for "AcSEC believes best practice..." if FASB does nothing and AcSEC wishes to reduce diversity in practice)	16

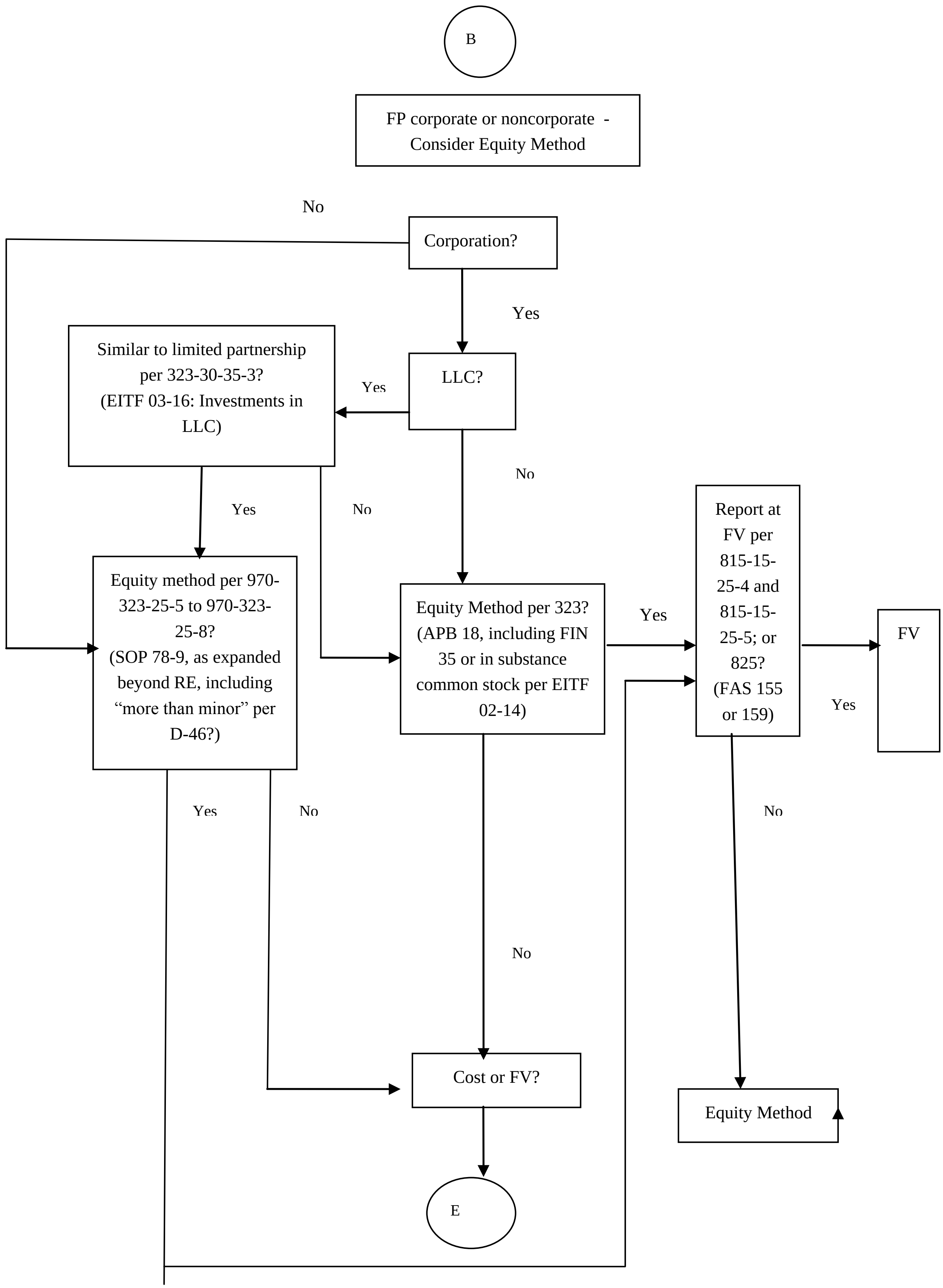
Description of proposed change	*Within the purview of*	*Example of page number or other reference within white paper doc*
The general principles of consolidation are applicable to all entity structures, including unincorporated entities, and not merely entities for which stock ownership exists. Accordingly, as stated in ASC 810-10-25-1, "consolidation is appropriate if a reporting entity has a controlling financial interest in another entity and a specific scope exception does not apply."	AcSEC clarify in AICPA NFP Guide	20
In circumstances in which an NFP transfers resources to another NFP without obtaining an interest, the transfer is either: • contribution expense • another type of expense or reduction of a liability (If paying for goods or services received from that other NFP) • loan receivable, or • some other type of asset represented by contractual rights (rather than an interest).	FASB (but perhaps some room in AICPA NFP Guide for AcSEC implementation guidance if FASB does nothing and AcSEC wishes to reduce diversity in practice)	34
Eliminate the "all or nothing" provisions off Appendix A of the NFP Guide	FASB	35

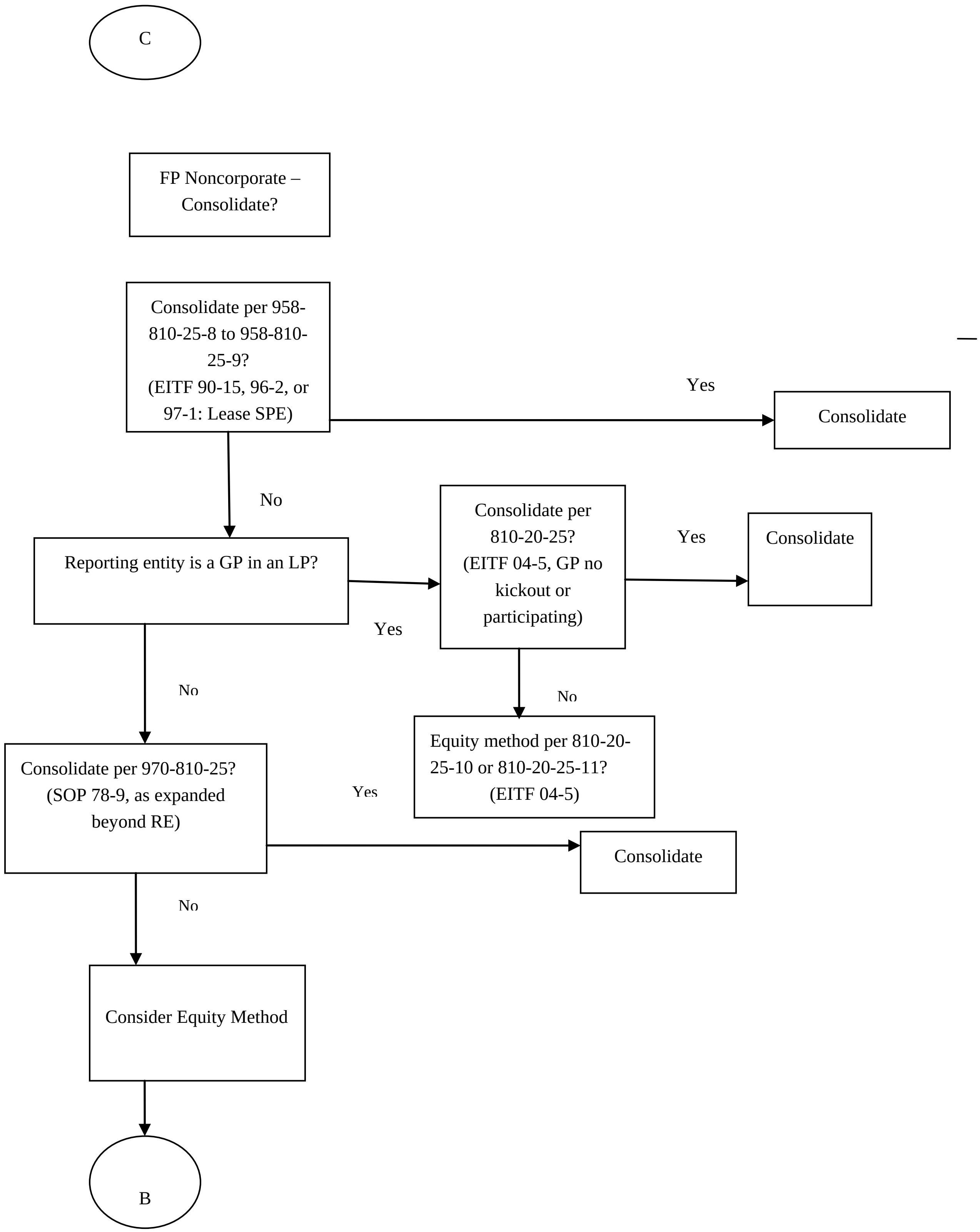
Description of proposed change	*Within the purview of*	*Example of page number or other reference within white paper doc*

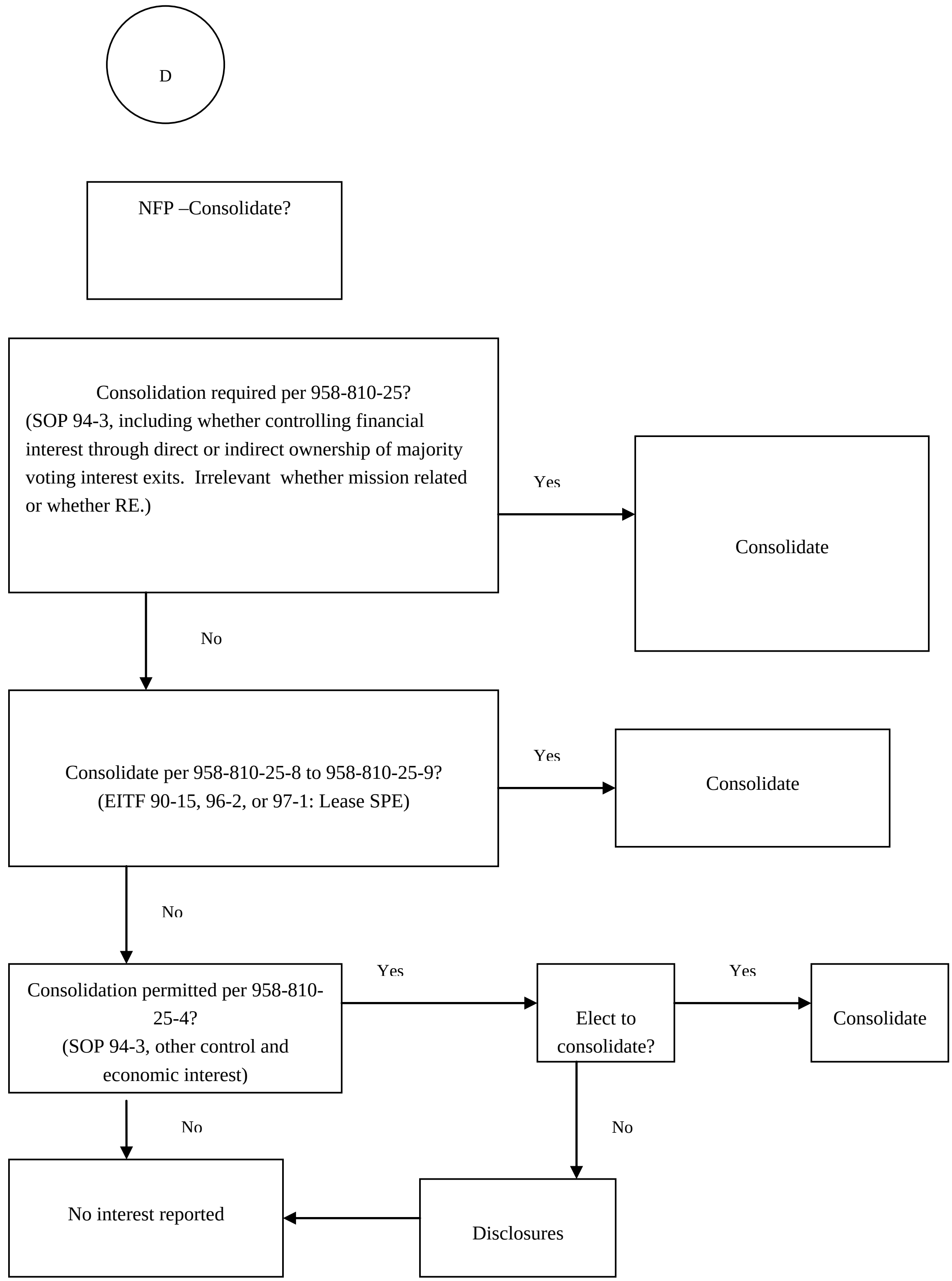
APPENDIX D – Decision Tree

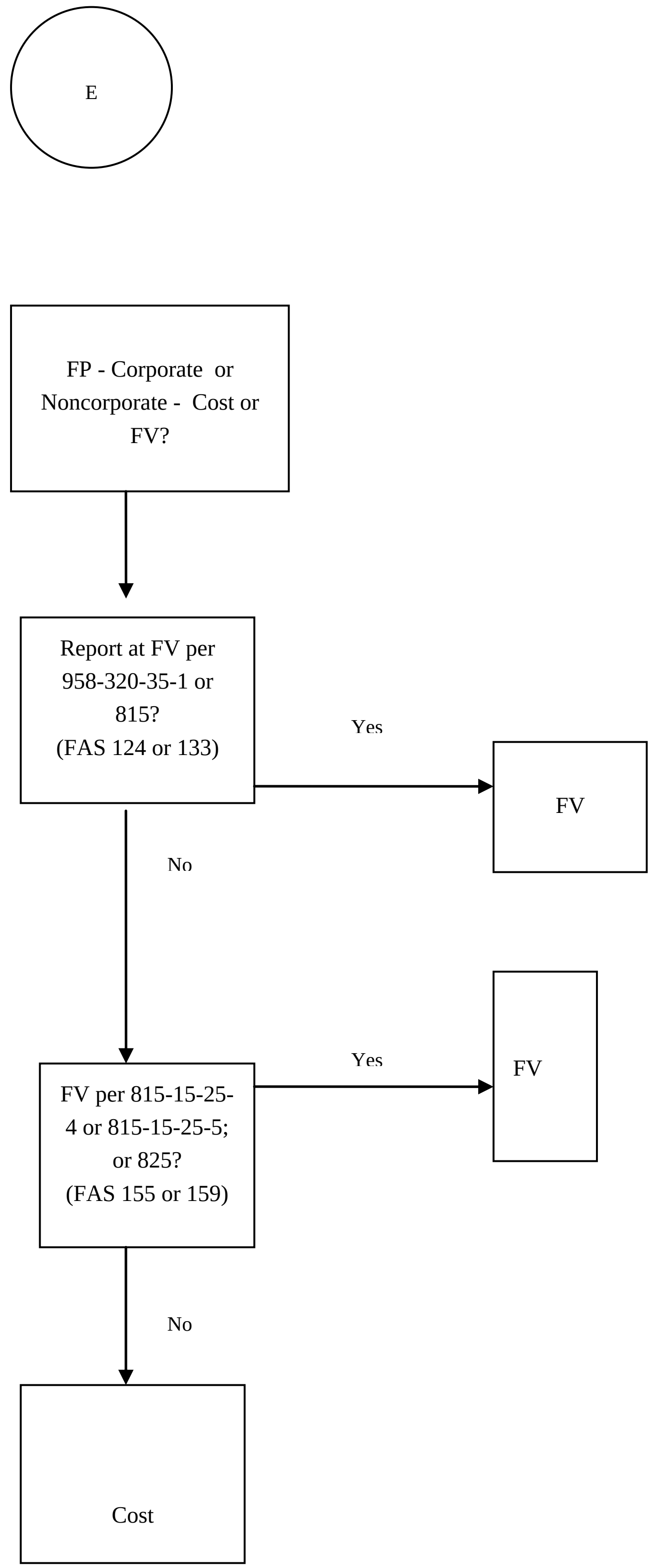



FP Corporate – Consolidate?
A
Consolidate per 958-810-15-4? (par 5 of SOP 94-3: ARB 51 as amended)
Yes
810-10-25-1 to 810-10-25-14 exception to consolidation? (EITF 96-16: maj. int. does not control)
No
Consolidate
Yes
No
Consolidate per 958-810-25-8 to 958-810-25-9? (EITF 90-15, 96-2, or 97-1: Lease SPE)
Yes
Consolidate
No
Consolidate per 810-10-25?
(EITF 97-2: Physician Practice Mgt.)
Yes
Consolidate
No
Consolidate per 970-323-25-10 and 970-323-25-11? (Corporate JV per SOP 78-9, as expanded beyond RE)
Yes
Consolidate
No
Consider equity method
B


B
FP corporate or noncorporate - Consider Equity Method
No
Corporation?
Yes
Similar to limited partnership per 323-30-35-3? (EITF 03-16: Investments in LLC)
Yes
LLC?
No
Yes
No
Equity method per 970-323-25-5 to 970-323-25-8? (SOP 78-9, as expanded beyond RE, including "more than minor" per D-46?)
Equity Method per 323? (APB 18, including FIN 35 or in substance common stock per EITF 02-14)
Yes
Report at FV per 815-15-25-4 and 815-15-25-5; or 825? (FAS 155 or 159)
FV
Yes
Yes
No
No
No
Cost or FV?
Equity Method
E


C
FP Noncorporate – Consolidate?
Consolidate per 958-810-25-8 to 958-810-25-9? (EITF 90-15, 96-2, or 97-1: Lease SPE)
Yes
Consolidate
No
Reporting entity is a GP in an LP?
Yes
Consolidate per 810-20-25? (EITF 04-5, GP no kickout or participating)
Yes
Consolidate
No
Equity method per 810-20-25-10 or 810-20-25-11? (EITF 04-5)
No
Consolidate per 970-810-25? (SOP 78-9, as expanded beyond RE)
Yes
Consolidate
No
Consider Equity Method
B


D
NFP –Consolidate?
Consolidation required per 958-810-25?
(SOP 94-3, including whether controlling financial interest through direct or indirect ownership of majority voting interest exits. Irrelevant whether mission related or whether RE.)
Yes
Consolidate
No
Consolidate per 958-810-25-8 to 958-810-25-9?
(EITF 90-15, 96-2, or 97-1: Lease SPE)
Yes
Consolidate
No
Consolidation permitted per 958-810-25-4?
(SOP 94-3, other control and economic interest)
Yes
Elect to consolidate?
Yes
Consolidate
No
No
No interest reported
Disclosures


E
FP - Corporate or Noncorporate - Cost or FV?
Report at FV per 958-320-35-1 or 815?
(FAS 124 or 133)
Yes
FV
No
FV per 815-15-25-4 or 815-15-25-5; or 825?
(FAS 155 or 159)
Yes
FV
No
Cost