

Accounting Standards Update 2016-14 (ASU 2016-14), *Presentation of Financial Statements of Not-for-Profit Entities*

HEALTHCARE ENTITY CONSIDERATIONS

ISSUES ANALYSIS – NATURAL AND FUNCTIONAL CLASS PRESENTATION

Background – ASU 2016-14, among other provisions, requires all not-for-profit entities, including health care entities, to report expenses by nature and function in one location (face of statement of activities/operations, separate statement or footnote disclosure). This requirement is not necessarily drastically different than current functional expense reporting requirements but is different than what is seen in prevailing industry practice. A common health care entity presentation would provide expenses by natural classification on the face of the statement of activities or operations and a footnoted presentation of expenses by the functional classification:

Common current natural classification presentation:

Unrestricted net assets:

Operating revenues:

Patient service revenues	\$ 9,025	\$ 8,771
Provision for bad debts	(189)	(410)
Patient service revenues less provision for bad debts	<u>8,836</u>	<u>8,361</u>
Capitation revenues	922	939
Contributions	9	8
Other	394	341
Total operating revenues	<u>10,161</u>	<u>9,649</u>

Operating expenses:

Salaries and employee benefits	4,585	4,470
Purchased services	2,329	2,354
Supplies	1,125	1,056
Depreciation and amortization	564	603
Capitated purchased services	246	250
Rentals and leases	151	140
Interest	93	78
Insurance	14	30
Other	635	690
Total operating expenses	<u>9,742</u>	<u>9,671</u>

Income (loss) from operations	419	(22)
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Common current functional classification presentation in notes:



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	Year ended December 31,	
	2014	2013
Health services	\$ 8,834	\$ 8,819
General and administrative	908	852
	\$ 9,742	\$ 9,671

Issue – As noted, health care entities have historically not reported expenses by functional and natural classification in one place. Additionally, ASU 2016-14 raises the question about whether the historical reporting of functional expense categories is robust enough to meet the new standards update. Included below are examples of disclosures options that could meet the requirements of ASU 2016-14. The functional categories used are not prescribed by the standards update and thus each organization would have the flexibility to determine how best to report their expense activity. This type of disclosure could include significant additional work for the preparer to categorize and allocate expenses to functions appropriately. Materiality applies to inclusion of and content in disclosures to financial statements as well as measured amounts in the financial statements so preparers will need to determine the extent to which such disclosures are material to their financial statements:

	Health Care Services						Support Services		Total
	Acute	Ambulatory	Physician	Post Acute	Health Plan	Research	MG&A	Fundraising	
Salaries and benefits	\$ 1,742	\$ 321	\$ 688	\$ 459	\$ 229	\$ 229	\$ 688	\$ 229	\$ 4,585
Purchased services	885	163	349	233	116	116	349	116	2,329
Supplies	428	79	169	113	56	56	169	56	1,125
Depreciation and amortization	214	39	85	56	28	28	85	28	564
Capitated purchased services	-	-	-	-	246	-	-	-	246
Rentals and leases	57	11	23	15	8	8	23	8	151
Interest	35	7	14	9	5	5	14	5	93
Insurance	5	1	2	1	1	1	2	1	14
Other	241	44	95	64	32	32	95	32	635
	\$ 3,608	\$ 665	\$ 1,424	\$ 950	\$ 721	\$ 475	\$ 1,424	\$ 475	\$ 9,742

The financial statements report certain expense categories that are attributable to more than one health care service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation, amortization, interest and other occupancy costs, are allocated to a function based on a square footage or units of service basis. Allocated health care services cost not allocated on a units of service basis are otherwise allocated based on revenue.

	Health Care Services			Support Services		Total
	North Region	Central Region	South Region	MG&A	Fundraising	
Salaries and benefits	\$ 1,376	\$ 917	\$ 1,376	\$ 688	\$ 229	\$ 4,585
Purchased services	699	466	699	349	116	2,329
Supplies	338	225	338	169	56	1,125
Depreciation and amortization	169	113	169	85	28	564
Capitated purchased services	74	49	74	37	12	246
Rentals and leases	45	30	45	23	8	151
Interest	28	19	28	14	5	93
Insurance	4	3	4	2	1	14
Other	191	127	191	95	32	635
	<u>\$ 2,923</u>	<u>\$ 1,948</u>	<u>\$ 2,923</u>	<u>\$ 1,461</u>	<u>\$ 487</u>	<u>\$ 9,742</u>

The financial statements report certain expense categories that are attributable to more than one health care service or support function. Therefore, these expenses require an allocation on a reasonable basis that is consistently applied. Costs not directly attributable to a function, including depreciation, amortization, interest and other occupancy costs, are allocated to a functional region based on a square footage or units of service basis. Allocated health care services cost not allocated on a units of service basis are otherwise allocated based on revenue.