The financial statement users’, investors’, donors’ and academic researchers’ understanding of current accounting recognition and reporting guidance affect their ability to compare financial information issued by nonprofit universities, hospitals, fund-raising organizations and government agencies. The financial results reported by public nonprofit organizations is different from that reported by private nonprofit organizations. This study discusses the events that brought about the divergence in nonprofit financial accounting recognition and reporting, and illustrates specific differences.

BACKGROUND

Beginning in 1973 formal guidance through the American Institute of Certified Public Accountants’ (AICPA), College and University Audit Guide (1973) gave institutions the fund-based reporting model. That model started to change in the 1980s when the Financial Accounting Standards Board (FASB) initiated a not-for-profit agenda that identified several projects. These projects resulted in the issuance of the following six financial reporting statements: 93 addressing depreciation (FASB 1987), 116 addressing contributions (FASB 1993a), 117 establishing the reporting model (FASB 1993b), 124 addressing investments (FASB 1995), 136 concerning funds held by others (FASB 1999) and 164 regarding mergers and combinations (FASB 2009).

The AICPA reacted to the issuance of Statement of Financial Accounting Standards (SFAS) No. 116 and No. 117, which fundamentally changed financial reporting for nongovernmental not-for-profit institutions, and issued a new audit guide in 1996. This guide marks the official departure from the fund-based model and the first introduction of entity-based reporting for not-for-profits. In 1984, the Government Accounting Standards Board (GASB) was created and began issuing standards affecting governmental not-for-profits. Some, like GASB Statement (GASBS) No. 8 (1988) on depreciation were a reaction to a standard issued by the FASB. GASBS No. 35 (1996b) was a landmark event in terms of higher education reporting. That is, the GASB abandoned the effort to develop a separate reporting model for higher education and chose to include public colleges and universities within the GASBS No. 34 (1996a) guidance. GASBS No. 34 identifies three options for reporting: business-type activities (BTA), governmental, and governmental with BTA. Most colleges and universities report as BTAs because (1) it is more straightforward and (2) it matches well—though not perfectly—the reporting followed by
nongovernmental not-for-profit institutions. The differences noted in this analysis are based on the GASB BTA reporting model.

Some differences being mentioned are not necessarily specific FASB action differences; they result from actions by the AICPA. For example, the AICPA proposes a Statement of Position; the FASB and/or the GASB reviews the statement and while they may not endorse it, unless they object, the statement becomes part of generally accepted accounting principles (GAAP). In that case, it is as if the FASB or the GASB issued the guidance. The statements have a different level of GAAP, but they must be followed when preparing financial statements in order to obtain an unqualified audit opinion. The capitalization of construction projects is an example in which non-action by the FASB resulted in the establishment of an AICPA standard. The AICPA issued Statement of Position 81-1 which allows non-governmental entities to capitalize a percentage of completion for construction projects (AICPA 1981 ¶23).

**PHILOSOPHY OF THE BOARDS**

To understand the various differences in standards issued by the two accounting boards, one needs to begin by examining the philosophical approaches the boards have taken. Those can be found in the board’s respective concepts statements. Concept statements are not GAAP to which preparers must adhere when issuing financial statements. Instead, taken as a whole, concepts statements form the framework used by the boards when developing accounting standards.

For the FASB, the overall focus is decision usefulness, attempting to provide the best information to influence decisions by investors, creditors, and others interested in commercial and not-for-profit activity. The FASB conceptual framework includes:

- Objectives of Financial Reporting by Business Enterprises
- Qualitative Characteristics of Accounting Information
- Objectives of Financial Reporting by Nonbusiness Organizations
- Recognition and Measurement in Financial Statements of Business Enterprises
- Elements of Financial Statements
- Using Cash Flow Information and Present Value in Accounting Measurement

The GASB’s primary focus is accountability as opposed to decision usefulness. This is a result of the heavy reliance on taxpayer support of governmental entities. The GASB conceptual framework includes:

- Objectives of Financial Reporting
- Service Efforts and Accomplishments Reporting
- Communication Methods

The GASB’s current agenda includes concepts projects related to elements and future projects will address recognition and measurement.

The line between decision usefulness and accountability is blurred and the boards’ propensity toward one does not make it exclusive of the other. Rather, it is a continuum on which the boards operate. For example, the FASB in issuing SFAS No. 136 (1999), Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others, was focused just as much on accountability as on decision usefulness. Similarly, the GASB’s efforts on other postemployment benefits, which resulted in GASBS No. 45 (2004), Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions, clearly is focused as much on decision-making as it is accountability.

**AREAS OF POTENTIAL DIFFERENCES**

**Major Types**

There are four major types of differences: recognition, measurement, display, and disclosure. Recognition differences deal with whether or not an item appears in a financial statement. An example is contributed services. SFAS No. 116 (1993a) addresses contributed services while GASBS No. 33 (1998) does not. Measurement differences refer to how items are included in the financial statements—at what
amount and based on which criteria. For example, both the FASB and the GASB require recognition of pension liabilities; however, they have established different standards for measuring the amount to be recognized. An example of a display difference is the GASB requirement for a classified balance sheet, separating assets and liabilities into current and noncurrent. The FASB requires listing assets and liabilities in order of liquidity. However, the FASB does allow an option of separating assets and liabilities into current and noncurrent based on ARB 43 (AICPA 1953). Finally, the boards have different requirements with respect to required disclosures. Disclosure differences are not addressed in this analysis.

**Restriction Definition**

The FASB’s definition of who can establish restrictions is much narrower than the GASB’s. Under the FASB, only donors can restrict whereas under the GASB any external party (donors, creditors, legislation, contracts) and constitutional provisions all can impose restrictions. This stems from the GASB’s philosophy toward accountability in that if any restrictions are imposed, the GASB wants those to be clearly identified. The effect is only on the categorization of net assets. Net assets reported as unrestricted under the FASB could be restricted expendable using GASB guidance. There is no difference for true endowments, which are restricted nonexpendable for governmental not-for-profits and permanently restricted for nongovernmental not-for-profit entities.

**Use of Restricted Funds**

The FASB’s guidance on the use of restricted funds is another area of difference and is considered one of the most controversial steps that the FASB has taken with respect to not-for-profit organizations. The FASB mandates the first dollar release method. Under first dollar release, restrictions are released if unrestricted resources are used for a purpose for which restricted resources are available. Although internal accounting and reporting may not be affected, the application of first dollar release converts previously restricted resources into unrestricted resources simply because they could have been expended.

The GASB considered this position but concluded that it should not be required in a governmental environment. However, they chose to recognize first dollar release as an acceptable method, making it optional. The GASB requires disclosure of the policy applied in situations when both restricted and unrestricted resources are available for the same purpose. Again, this results in a categorization of net assets difference.

**RECOGNITION AND RECORDING DIFFERENCES**

The following is a discussion of specific recognition and recording differences that result from different GASB and FASB guidance.

**Endowment Gift Pledges**

The difference in treatment of endowment pledges is quite noticeable. Endowment pledges that are recognized by nongovernmental not-for-profit entity will not be recognized by a comparable governmental not-for-profit institution. The FASB recognizes endowment pledges as permanently restricted. The GASB prohibits recognition of endowment pledges based on its conclusion that a promise cannot satisfy the restriction because resources have not been received. This difference affects recognition of assets, gift revenues, and net assets and results in nongovernmental not-for-profits reporting a larger total assets amount.

**Discounting of Pledges**

With regards to discounting of pledges, the FASB requires discounting if the pledge is collectible beyond one year. The GASB allows discounting, but does not require it. This results in assets, gift revenues and net assets differences.
The differences with regard to pledges do not preclude GASB institutions from recognizing all pledges, only those that meet certain eligibility criteria. That is, the institution could use the resources in a current activity. The logic for the difference in discounting is APB Opinion 20 (AICPA 1971), which drives the recognition of discounts and applies to exchange transactions. By defining pledges as non-exchange transactions, the GASB does not require discounting.

**Restricted Cash Contributions**

For FASB institutions, restricted cash contributions are recognized as either temporarily or permanently restricted. For GASB institutions, time restricted contributions are recognized as deferred revenue. This produces liabilities and gift revenues and thereby net assets differences between FASB and GASB not-for-profit entities.

**Restricted Non-Endowment Pledges**

The FASB recognizes restricted non-endowment pledges as temporarily restricted revenue. The GASB prohibits recognition if for future period use, under the same concept as with endowment pledges – one cannot recognize the gift before it is available. Again, this recognition results in assets, gift revenues, and net assets differences.

**Investment Income**

GASBS No. 31 (1997) establishes prescriptive treatment for investment income. Investment income and realized investment gains/losses must be reported as a single net amount. When looking at most governmental not-for-profit institutions' financial statements, one will see investment income which includes current yield, net realized gains and losses, and net unrealized gains and losses.

Net unrealized gains and losses can be displayed separately from investment income using a prescribed label: net increase (decrease) in the fair value of investments. Investment income cannot be reported as operating revenue by governmental not-for-profit higher education institutions unless it results from loans to students, which are classified as program loans. In fact, the only governmental entities that can report investment income as operating revenue are pooled-investment entities and fundraising foundations whose mission includes investment activities. The FASB does not have similar requirements related to investment income display or classification as non-operating.

**Pell Grants**

Funds received for Pell Grants are not counted as revenue by FASB institutions. This is a balance sheet rather than activities statement transaction. For GASB institutions Pell Grants are included as revenue as directed by GASBS 24 (1994) that requires all grant revenue to be reported as revenue. Whether the revenue is considered operating or non-operating is somewhat controversial. The differing treatment affects grants and contracts revenue, which will be higher for governmental not-for-profit institutions, while net tuition and auxiliaries revenue will be higher for nongovernmental not-for-profit institutions. In addition, liabilities and net assets will vary between the two types of institutions.

**Perkins Loan Program**

For FASB institutions, federal advances for Perkins loans are reflected as liabilities on the balance sheet. GASB institutions have an option to reflect Perkins loan receipts as liabilities on the balance sheet or revenues on the activities statement. Both are acceptable under current GAAP standards. The determination entails whether Perkins loan funds are treated as a net asset or a liability. Some believe it is a liability because the federal government can compel its return. Others believe this possibility to be so remote that the Perkins loan funds should be reported as revenues and net assets. National Association of College and Business Officers (NACUBO) raised the issue with the GASB, suggesting that it is inappropriate to treat something as a net asset when an external party can compel it to be returned. The GASB recognizes that different rules apply to different types of loans and added the issue to their agenda. The GASB project agenda plans to consider guidance about the treatment of federal loans. Until then,
either approach is considered GAAP. If governmental not-for-profit institutions reflect Perkins awards on the activities statement, it results in differences from nongovernmental not-for-profit institutions for grants and contracts revenue, liabilities, and net assets.

**Contributed Services**

The FASB has specific criteria for how to identify and recognize contributed services provided to a not-for-profit entity. The GASB does not have criteria for recognizing contributed services; however, there may be a GASB project to address contributed services in the future. Currently, nongovernmental not-for-profit organizations recognize contributed services that meet certain criteria established in SFAS No. 116 (1993a). Governmental not-for-profit organizations currently are not required to recognize contributed services. The effect of this difference is on gift revenues and expenses reported by the two different organizations. In most cases, there is no impact on net revenues because the contribution revenues usually are offset by an equal expense. An exception occurs when the contributed services create or enhance nonfinancial assets. In those cases, net assets increase by the value of the services.

**OPEB and Pension Obligations**

The GASB uses the term OPEB when referring to other postemployment benefits, which consist primarily of health care for retirees. The comparable term in the FASB literature is other postretirement benefits.

While the GASB and the FASB have different approaches to calculating pension and other postemployment liabilities, they are consistent within their own methodologies for calculating these types of liabilities. This affects the measurement and recognition of those liabilities which impacts expense, liability, and net assets. The GASB considered the FASB methodology during its deliberation of the OPEB standard, but concluded that it was more important to be consistent with the standards it previously established for pensions.

**Software Acquisitions**

The FASB has a requirement to capitalize software investments that meet specified criteria. The GASB does not have a similar requirement, although it has an intangible assets project on its current agenda. NACUBO issued an advisory report (AR 1999-7) encouraging governmental not-for-profit higher education institutions to capitalize software. This difference affects assets, expenses, and net assets. GASB institutions that do not follow NACUBO’s guidance will treat software purchases as a current period expense that also results in a reporting difference between the two types of institutions.

**Asset Impairment**

The FASB requires a cash flow approach for determining impairment loss (loss based on measurement of expected cash flows). The GASB considered the cash flow approach but opted instead for a service utility approach. The different methods for measuring an impairment loss results in assets, expenses and losses, and net assets differences.

**FINANCIAL STATEMENTS AND REPORTS**

The following is a discussion of specific differences found in the financial statements that result from GASB and FASB guidance.

**Disaggregation (Columns on Financial Statements)**

The FASB allows line of business (e.g. academic, auxiliaries, patient care, charity, etc.) or net asset class (i.e., unrestricted, temporarily restricted, permanently restricted) disaggregation. The GASB allows only line of business disaggregation. Net asset class disaggregation is prohibited by the GASB (1999a, ¶37).
Funds Held in Trust by Others

Funds held in trust by others are different in terms of both recognition and display. FASB institutions include these as assets, and the Not-for-Profit Organization Audit and Accounting Guide (AICPA 1996) prescribes the method for determining the amount to be recognized in the financial statements. Governmental not-for-profit organizations do not treat funds held in trust by others as an asset. However, under GASBS No. 39 (2002), if an entity meets specified criteria, it will be reported as a component unit using discrete display. That is, the entities’ financial statements will be presented with those of the governmental not-for-profit institution.

Technically, governmental not-for-profits could also have blended component units already holding assets in its name. Those assets would show up as well, but not be labeled as funds held in trust by others. The effect of this difference is that funds held in trust by others will appear on nongovernmental not-for-profit organizations’ statements, but not on those of governmental not-for-profit organization (unless they qualify as component units). In addition, nongovernmental not-for-profit institutions will show revenue as a result of a change in the value of the funds held in trust, resulting in a change in net assets.

Endowment Investment Losses

The FASB requires that permanently restricted net assets remain intact—insulated from reductions caused by the recognition of losses. Therefore, endowment losses reduce temporarily restricted net assets to the extent of unspent appreciation. If losses exceed such amounts, the excess is reflected in the unrestricted net assets category. The GASB has no similar requirement. Losses attributable to restricted nonexpendable net assets reduce the restricted nonexpendable net assets.

Management Discussion and Analysis

The GASB has a prescriptive requirement for management’s discussion and analysis (MD&A) and specifies what should be addressed (GASB 1999a, 11). The FASB has no similar requirement. There is no substantive effect of this difference. However, there is a benefit for governmental not-for-profits with respect to concerns regarding financial transparency.

Balance Sheet Display

The GASB (1999a) requires a classified balance sheet (i.e., current, noncurrent) and defines three net asset classes (capital assets net of related debt [designated as unrestricted in FASB statements], restricted and unrestricted). If an institution has permanent endowments, the resources must be classified within restricted net assets as expendable or nonexpendable. The GASB restricted expendable net asset class is very similar to the FASB temporarily restricted net asset class. It does not match exactly because the GASB’s broader definition of restriction results in some net assets being classified as restricted expendable by governmental not-for-profit entities when the same net assets would be classified as unrestricted by nongovernmental not-for-profit organizations.

The GASB prohibits display of unrestricted net asset designations, although disclosure in the notes to the financial statements is allowed. When a government has a significant amount of non-depreciable capital assets the GASB requires that they be reported separately from depreciable capital assets.

The FASB does not have a classification requirement. The FASB net asset classes are unrestricted, temporarily restricted, and permanently restricted. The FASB has no specific requirements related to the display of capital assets, although they are considered part of unrestricted net assets.

Activities Statement

Reclassifications

The FASB (1993a) treats all expenses as unrestricted. To the extent that temporarily restricted resources are used to finance an expense, they must be reclassified from temporarily restricted to unrestricted net assets. The GASB has no similar concept—expenses can be reported as unrestricted, restricted, operating, or non-operating.
**Operating Measure**

The GASB (1999a) requires a somewhat prescriptive operating measure be reported in the activity statement. State appropriations, gifts, and investment income (except for interest on program loans) must be reported as non-operating activities. Institutions are allowed to decide how to treat other items. For example, gains and losses resulting from the disposition of capitalized equipment can be either operating or non-operating. In entities in which they occur frequently and are a routine part of doing business, the gains and losses might be classified as operating. If occurring infrequently they likely will be reported as non-operating activities.

There has been a great deal of discussion with regards to an operating measure for nongovernmental not-for-profit institutions. The FASB allows for a self-defined operating measure and requires disclosure of the methodology for determining the measure if it is not obvious.

**Expense Classification**

The FASB (1993a) allows natural classification of expenses but requires functional classification, either on the face of the activity statement display or in the financial statement notes. The GASB (1999a) also allows natural or functional expense classification. NACUBO, however, encourages all colleges and universities whether governmental or nongovernmental to report a matrix reconciling functional and natural expense classification in the financial statement notes.

**Specific Expenses**

The FASB (1993b) requires allocation of certain expenses, such as operations and maintenance of plant, depreciation, and interest to an appropriate functional designation. The GASB (1999a) allows, but does not require, an allocation of depreciation to some other expense designation. The GASB requires bad debts to be offset against the corresponding revenue source. The exception to this general rule is for bad debts resulting from loans because there is no revenue source.

**Extraordinary Items**

The FASB defines extraordinary items as those that are unusual and infrequent. The GASB has the same definition for extraordinary items and goes on to specify an additional category—special items. Special items are unusual or infrequent and within management’s control. For example, if a governmental not-for-profit institution elects to abandon a software implementation in which significant dollars have been invested (and capitalized), it would report this as a special item because it is within management’s control. A comparable nongovernmental not-for-profit institution might feel that this transaction is neither unusual nor infrequent and, therefore, record it as part of operating expenses.

**Cash Flow Statement**

There are major differences in the cash flow statement. The FASB (1993b) allows the indirect method and specifies three categories for reporting cash flows: operating, investing, and financing. The GASB (1999a) mandates the direct method, which requires that operating cash flows be reported by type of flow, and the presentation of a reconciliation of operating cash to operating income as reported on the Statement of Revenues, Expenses, and Changes in Net Assets. In addition, the GASB specifies the use of four categories for presenting cash flows: operating, investing, capital and related financing, and noncapital financing.

**CONCLUSION**

As evidenced by the discussion of specific differences in accounting between governmental not-for-profit organizations and nongovernmental not-for-profit organizations, a comparison between comparable entities can lead to very different conclusions.

Nongovernmental not-for-profits report a larger total asset amount due to the recognition of pledges and funds held in trust by others. Government not-for-profits report a greater amount of total liabilities...
due to the recognition of deferred time restricted cash contributions. Governmental not-for-profits separately display the capital asset’s equity while nongovernment not-for-profits include the capital assets’ ‘brick and mortar equity’ as part of the unrestricted net assets. In addition to these differences, the governmental not-for-profit presents a classified statement of net assets whereas the nongovernmental not-for-profit presents a statement in liquidity order.

The activity statement of the two types of not-for-profits is also quite different. Each recognize and report various revenues and expenses using criteria leading to a significantly different change in net assets amount. A nongovernmental not-for-profit entity compared to a comparable governmental not-for-profit will report a larger amount of revenues due to their ability to recognize all gift contributions and pledges.

The cash flow statement presentation of the two types of not-for-profits is so different a user must have special expertise to be able to make any comparison. The GASB cash flow statement has four categories versus the FASB three. Contents within categories are significantly different. The GASB presentation uses the direct method for the cash flows from operating activities as compared to the FASB indirect method.

Given these extensive differences, financial statement users, investors, donors and academic researchers must have more than a basic understanding of the underlying accounting differences to compare the financial statements of governmental not-for-profit organizations and nongovernmental not-for-profit organizations.

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