

Statement of Financial Accounting Concepts No. 4

[CON4 Status Page](#)

Objectives of Financial Reporting by
Nonbusiness Organizations

December 1980



Financial Accounting Standards Board
of the Financial Accounting Foundation
401 MERRITT 7, P.O. BOX 5116, NORWALK, CONNECTICUT 06856-5116

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CON 4: Objectives of Financial Reporting by Nonbusiness Organizations

CON 4 HIGHLIGHTS

[Best understood in context of full Statement]

- This Statement establishes the objectives of general purpose external financial reporting by nonbusiness organizations.
 - Based on its review of those objectives and the objectives set forth in FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises*, the Board has concluded that it is not necessary to develop an independent conceptual framework for any particular category of entities.
 - The two sets of objectives will serve as the foundation of an integrated conceptual framework for financial accounting and reporting that, when completed, will have relevance to all entities while providing appropriate consideration of any different reporting objectives and concepts that may apply to only certain types of entities.
 - Pending resolution of the appropriate structure for setting financial accounting and reporting standards for state and local governmental units, the Board has deferred a final decision on whether the objectives in this Statement should apply to general purpose external financial reporting of those units. On the basis of its study to date, the Board is aware of no persuasive evidence that the objectives in this Statement are inappropriate for that type of financial reporting by state and local governmental units.
 - Based on its study, the Board believes that the objectives of general purpose external financial reporting for government-sponsored entities (for example, hospitals, universities, or utilities) engaged in activities that are not unique to government should be similar to those of business enterprises or other nonbusiness organizations engaged in similar activities.
- This Statement focuses on organizations that have predominantly nonbusiness characteristics that heavily influence the operations of the organization.

- The major distinguishing characteristics of nonbusiness organizations include: (a) receipts of significant amounts of resources from resource providers who do not expect to receive either repayment or economic benefits proportionate to resources provided, (b) operating purposes that are primarily other than to provide goods or services at a profit or profit equivalent, and (c) absence of defined ownership interests that can be sold, transferred, or redeemed, or that convey entitlement to a share of a residual distribution of resources in the event of liquidation of the organization.
 - These characteristics result in certain types of transactions that are infrequent in business enterprises, such as contributions and grants, and in the absence of transactions with owners.
 - The line between nonbusiness organizations and business enterprises is not always sharp since the incidence and relative importance of those characteristics in any organization are different. This suggests that, for purposes of developing financial reporting objectives, a spectrum of organizations exists ranging from those with clearly dominant nonbusiness characteristics to those with wholly business characteristics.
 - Examples of organizations that clearly fall outside the focus of this Statement include all investor-owned enterprises and other types of organizations, such as mutual insurance companies and other mutual cooperative entities that provide dividends, lower costs, or other economic benefits directly and proportionately to their owners, members, or participants.
 - Examples of organizations that clearly fall within the focus of this Statement include most human service organizations, churches, foundations, and some other organizations, such as those private nonprofit hospitals and nonprofit schools that receive a significant portion of their financial resources from sources other than the sale of goods and services.
 - Borderline cases may exist where organizations possess some of the distinguishing characteristics but not others. Examples are those private nonprofit hospitals and nonprofit schools that may receive relatively small amounts of contributions and grants but finance their capital needs largely from the proceeds of debt issues and their operating needs largely from service charges. As a result, the objectives of Concepts Statement 1 may be more appropriate for those organizations.
- The objectives in this Statement stem from the common interests of those who provide resources to nonbusiness organizations in the services those organizations provide and their continuing ability to provide services.
 - Nonbusiness organizations generally have no single indicator of performance comparable to a business enterprise's profit. Thus, other indicators of performance usually are needed.
 - The performance of nonbusiness organizations generally is not subject to the test of direct

competition in markets to the extent that business enterprises are.

—Other kinds of controls introduced to compensate for the lesser influence of markets are a major characteristic of their operations and affect the objectives of their financial reporting. Controls, such as formal budgets and donor restrictions on the use of resources, give managers a special responsibility to ensure compliance. Information about departures from those mandates is important in assessing how well managers have discharged their stewardship responsibilities.

- The objectives in this Statement apply to general purpose external financial reporting by nonbusiness organizations.

—The objectives stem primarily from the needs of external users who generally cannot prescribe the information they want from an organization.

—In addition to information provided by general purpose external financial reporting, managers and, to some extent, governing bodies need a great deal of internal accounting information to carry out their responsibilities in planning and controlling activities. That information and information directed at meeting the specialized needs of users having the power to obtain the information they need are beyond the scope of this Statement.

- The objectives of financial reporting are affected by the economic, legal, political, and social environment in which financial reporting takes place.

—The operating environments of nonbusiness organizations and business enterprises are similar in many ways. Both nonbusiness organizations and business enterprises produce and distribute goods and services and use scarce resources in doing so.

—Differences between nonbusiness organizations and business enterprises arise in the ways they obtain resources. Noneconomic reasons are commonly factors in decisions to provide resources to particular nonbusiness organizations.

- The objectives also are affected by the characteristics and limitations of the kind of information that financial reporting can provide.

—The information provided by financial reporting is primarily financial in nature: It is generally quantified and expressed in units of money. However, quantified information expressed in terms other than units of money and nonquantified information may be needed to understand the significance of information expressed in units of money or to help in assessing the performance of a nonbusiness organization.

—The information provided by financial reporting pertains to individual reporting entities, often results from approximate rather than exact measures, largely reflects the effects of transactions and events that have already happened, is but one source of information needed by those who make decisions about nonbusiness organizations, and is provided

and used at a cost.

- The objectives state that:
 - Financial reporting by nonbusiness organizations should provide information that is useful to present and potential resource providers and other users in making rational decisions about the allocation of resources to those organizations.
 - Financial reporting should provide information to help present and potential resource providers and other users in assessing the services that a nonbusiness organization provides and its ability to continue to provide those services.
 - Financial reporting should provide information that is useful to present and potential resource providers and other users in assessing how managers of a nonbusiness organization have discharged their stewardship responsibilities and about other aspects of their performance.
 - Financial reporting should provide information about the economic resources, obligations, and net resources of an organization, and the effects of transactions, events, and circumstances that change resources and interests in those resources.
 - Financial reporting should provide information about the performance of an organization during a period. Periodic measurement of the changes in the amount and nature of the net resources of a nonbusiness organization and information about the service efforts and accomplishments of an organization together represent the information most useful in assessing its performance.
 - Financial reporting should provide information about how an organization obtains and spends cash or other liquid resources, about its borrowing and repayment of borrowing, and about other factors that may affect an organization's liquidity.
 - Financial reporting should include explanations and interpretations to help users understand financial information provided.
- Background information relating to the development of this Statement is included in paragraphs 57-66. Paragraph 67 contains a comparison of the objectives in this Statement to those in Concepts Statement 1.

Statements of Financial Accounting Concepts

This Statement of Financial Accounting Concepts is one of a series of publications in the Board's conceptual framework for financial accounting and reporting. Statements in the series are intended to set forth objectives and fundamentals that will be the basis for development of financial accounting and reporting standards. The objectives identify the goals and purposes of financial reporting. The fundamentals are the underlying concepts of financial

accounting—concepts that guide the selection of transactions, events, and circumstances to be accounted for; their recognition and measurement; and the means of summarizing and communicating them to interested parties. Concepts of that type are fundamental in the sense that other concepts flow from them and repeated reference to them will be necessary in establishing, interpreting, and applying accounting and reporting standards.

The conceptual framework is a coherent system of interrelated objectives and fundamentals that is expected to lead to consistent standards and that prescribes the nature, function, and limits of financial accounting and reporting. It is expected to serve the public interest by providing structure and direction to financial accounting and reporting to facilitate the provision of evenhanded financial and related information that helps promote the efficient allocation of scarce resources in the economy and society, including assisting capital and other markets to function efficiently.

Establishment of objectives and identification of fundamental concepts will not directly solve financial accounting and reporting problems. Rather, objectives give direction and concepts are tools for solving problems.

The Board itself is likely to be the most direct beneficiary of the guidance provided by the Statements in this series. They will guide the Board in developing accounting and reporting standards by providing the Board with a common foundation and basic reasoning on which to consider merits of alternatives.

However, knowledge of the objectives and concepts the Board will use in developing standards also should enable those who are affected by or interested in financial accounting standards to understand better the purposes, content, and characteristics of information provided by financial accounting and reporting. That knowledge is expected to enhance the usefulness of, and confidence in, financial accounting and reporting. The concepts also may provide some guidance in analyzing new or emerging problems of financial accounting and reporting in the absence of applicable authoritative pronouncements.

Statements of Financial Accounting Concepts do not establish standards prescribing accounting procedures or disclosure practices for particular items or events, which are issued by the Board as Statements of Financial Accounting Standards. Rather, Statements in this series describe concepts and relations that will underlie future financial accounting standards and practices and in due course serve as a basis for evaluating existing standards and practices.*

The Board recognizes that in certain respects current generally accepted accounting principles may be inconsistent with those that may derive from the objectives and concepts set forth in Statements in this series. However, a Statement of Financial Accounting Concepts does not (a) require a change in existing generally accepted accounting principles; (b) amend, modify, or interpret Statements of Financial Accounting Standards, Interpretations of the FASB, Opinions of the Accounting Principles Board, or Bulletins of the Committee on Accounting Procedure that are in effect; or (c) justify either changing existing generally accepted accounting and reporting practices or interpreting the pronouncements listed in item (b) based on personal interpretations of the objectives and concepts in the Statements of Financial Accounting Concepts.

Since a Statement of Financial Accounting Concepts does not establish generally accepted accounting principles or standards for the disclosure of financial information outside of

financial statements in published financial reports, it is not intended to invoke application of Rule 203 or 204 of the Rules of Conduct of the Code of Professional Ethics of the American Institute of Certified Public Accountants (or successor rules or arrangements of similar scope and intent). **

Like other pronouncements of the Board, a Statement of Financial Accounting Concepts may be amended, superseded, or withdrawn by appropriate action under the Board's *Rules of Procedure*.

FASB PUBLICATIONS ON CONCEPTUAL FRAMEWORK

Statements of Financial Accounting Concepts

No. 1, *Objectives of Financial Reporting by Business Enterprises* (November 1978)

No. 2, *Qualitative Characteristics of Accounting Information* (May 1980)

No. 3, *Elements of Financial Statements of Business Enterprises* (December 1980)

Discussion Memorandums and Invitations to Comment Having Issues Being (or Yet to Be) Considered by the Board

Elements of Financial Statements and Their Measurement (December 2, 1976)

Reporting Earnings (July 31, 1979)

Financial Statements and Other Means of Financial Reporting (May 12, 1980)

Reporting Funds Flows, Liquidity, and Financial Flexibility (December 15, 1980)

Other Projects in Process

Accounting Recognition Criteria

INTRODUCTION AND BACKGROUND

Scope

General

1. This Statement establishes the objectives of general purpose external financial reporting by nonbusiness organizations. Those objectives, together with the objectives set forth in FASB Concepts Statement No. 1, *Objectives of Financial Reporting by Business Enterprises*, will serve as the foundation of the conceptual framework the Board is developing for financial accounting and reporting. Based on its review of the similarities and differences between those two sets of objectives, the Board has concluded that it is not necessary to develop an independent conceptual framework for any particular category of entities (e.g., nonbusiness organizations or business enterprises). Rather, its goal is to develop an integrated conceptual framework that has relevance to all entities and that provides appropriate consideration of any different reporting objectives and concepts that may apply to only certain types of entities. Consideration of the differences between the objectives of financial reporting set forth in this Statement and those in Concepts Statement 1 will be most useful in helping to identify those areas that may require unique treatment. Appendix A to this Statement provides background information. Appendix B compares the objectives of this Statement and Concepts Statement 1, noting the many areas of similarity and the few, but important, areas of difference (paragraph 9).

2. This Statement uses terminology that has been chosen carefully to avoid prejudging issues that may be subjects of other conceptual framework projects. For example, it uses the terms *resource inflows* and *outflows* rather than *revenues*, *expenses*, and *expenditures*. The reasons for the Board's conclusions are included in the text rather than in a separate appendix.

State and Local Governmental Units

3. From its outset, the project leading to this Statement has included governmental units in its scope, and the Exposure Draft included governmental examples. On the basis of its study to date, the Board is aware of no persuasive evidence that the objectives in this Statement are inappropriate for general purpose external financial reports of governmental units. Nonetheless, the appropriate structure for setting financial accounting and reporting standards for state and local governmental units continues to be discussed.¹ Pending resolution of that issue, the Board has deferred a final decision on whether the objectives set forth in this Statement should apply to general purpose external financial reporting by state and local governmental units.

4. If the responsibility for standard setting was ultimately given to the Financial Accounting

Standards Board, the Board would expect to consider the findings of research in process by the National Council on Governmental Accounting (NCGA), the Council of State Governments (CSG) (paragraphs 65 and 66), and other intervening research. Before reaching a decision, it would also solicit additional views regarding the applicability of the conclusions in this Statement to general purpose external financial reporting of state and local governmental units.

5. Based on its study, the Board believes that the objectives of general purpose external financial reporting for government-sponsored entities (for example, hospitals, universities, or utilities) engaged in activities that are not unique to government should be similar to those of business enterprises or other nonbusiness organizations engaged in similar activities. Accordingly, examples of such government-sponsored organizations and activities are included in the sections of this Statement that discuss the environment in which nonbusiness organizations operate and the users of their financial reports.

Distinguishing Characteristics of Nonbusiness Organizations

6. The major distinguishing characteristics of nonbusiness organizations include:
- a. Receipts of significant amounts of resources from resource providers who do not expect to receive either repayment or economic benefits proportionate to resources provided
 - b. Operating purposes that are other than to provide goods or services at a profit or profit equivalent
 - c. Absence of defined ownership interests that can be sold, transferred, or redeemed, or that convey entitlement to a share of a residual distribution of resources in the event of liquidation of the organization.

These characteristics result in certain types of transactions that are largely, although not entirely, absent in business enterprises, such as contributions and grants,² and to the absence of transactions with owners, such as issuing and redeeming stock and paying dividends. Because the authoritative accounting literature has largely focused on problems commonly encountered in business enterprises, it has not dealt comprehensively with these unique areas in nonbusiness organizations.

7. This Statement focuses on organizations that have predominantly nonbusiness characteristics that heavily influence the operations of the organization. The line between nonbusiness organizations and business enterprises is not always sharp since the incidence and relative importance of those characteristics in any organization are different. This suggests that, for purposes of developing financial reporting objectives, a spectrum of organizations exists ranging from those with clearly dominant nonbusiness characteristics to those with wholly business characteristics. Examples of organizations that clearly fall outside the focus of this Statement include all investor-owned enterprises and other types of organizations, such as mutual insurance companies and other mutual cooperative entities that provide dividends, lower costs, or other economic benefits directly and proportionately to their owners, members, or participants. The objectives of financial reporting set forth in Concepts Statement 1 are

appropriate for those types of organizations. Examples of organizations that clearly fall within the focus of this Statement include most human service organizations, churches, foundations, and some other organizations, such as those private nonprofit hospitals and nonprofit schools that receive a significant portion of their financial resources from sources other than the sale of goods and services.³ As happens with any distinction, there will be borderline cases. This will be true especially for organizations that possess some of the distinguishing characteristics of nonbusiness organizations but not others.

8. Some organizations have no ownership interests but are essentially self-sustaining from fees they charge for goods and services. Examples are those private nonprofit hospitals and nonprofit schools that may receive relatively small amounts of contributions and grants but finance their capital needs largely from the proceeds of debt issues and their operating needs largely from service charges rather than from private philanthropy or governmental grants. As a result, assessment of amounts, timing, and uncertainty of cash flows becomes the dominant interest of their creditors and other resource providers and profitability becomes an important indicator of performance. Consequently, the objectives of Concepts Statement 1 may be more appropriate for those organizations.⁴

9. The objectives in this Statement stem from the common interests of those who provide resources to nonbusiness organizations in the services those organizations provide and their continuing ability to provide services. In contrast, the objectives of financial reporting of Concepts Statement 1 stem from the interests of resource providers in the prospects of receiving cash as a return of and return on their investment.⁵ Despite different interests, resource providers of all entities look to information about economic resources, obligations, net resources, and changes in them for information that is useful in assessing their interests. All such resource providers focus on indicators of organization performance and information about management stewardship. Nonbusiness organizations generally have no single indicator of performance comparable to a business enterprise's profit. Thus, other indicators of performance are usually needed. This Statement sets forth two performance indicators for nonbusiness organizations: information about the nature of and relation between inflows and outflows of resources and information about service efforts and accomplishments. Moreover, the performance of nonbusiness organizations generally is not subject to the test of direct competition in markets to the extent that business enterprises are. Other kinds of controls introduced to compensate for the lesser influence of markets are a major characteristic of their operations and affect the objectives of their financial reporting. Controls, such as formal budgets and donor restrictions on the use of resources, give managers a special responsibility to ensure compliance. Information about departures from those mandates that may impinge upon an organization's financial performance or its ability to provide a satisfactory level of services is important in assessing how well managers have discharged their stewardship responsibilities. Paragraphs 13-22 compare the environments of nonbusiness organizations and business enterprises and provide a basis for the similarities and differences noted in this section and elsewhere in this Statement.

General Purpose External Financial Reporting

10. The objectives in this Statement apply to general purpose external financial reporting by nonbusiness organizations. The aim of that type of financial reporting is limited. It does not attempt to meet all informational needs of those interested in nonbusiness organizations nor to furnish all the types of information that financial reporting can provide. For example, although managers and governing bodies of nonbusiness organizations are interested in the information provided by general purpose external financial reporting, they also need additional information to help them carry out their planning, controlling, and other stewardship responsibilities (paragraph 32). Nor is general purpose external financial reporting intended to meet specialized needs of regulatory bodies, some donors or grantors, or others having the authority to obtain the information they need (paragraph 31). Rather, general purpose external financial reporting focuses on providing information to meet the common interests of external users who generally cannot prescribe the information they want from an organization. Those users must use the information that is communicated to them by the organization. The most obvious and important users fitting that description in the nonbusiness environment are resource providers, such as members, taxpayers, contributors, and creditors (paragraph 36).

11. The objectives in this Statement are not restricted to information communicated by financial statements. Financial reporting includes not only financial statements but also other means of communicating information that relates, directly or indirectly, to the information provided by the accounting system, that is, information about an organization's resources and obligations.⁶

12. For convenience, *financial reporting* is used in place of *general purpose external financial reporting by nonbusiness organizations* in the remainder of this Statement.

Environmental Context of Objectives

13. Financial reporting is not an end in itself but is intended to provide information that is useful in making economic decisions—for making reasoned choices among alternative uses of scarce resources.⁷ Thus, the objectives in this Statement stem largely from the needs of those for whom the information is intended. Those needs depend significantly on the activities of nonbusiness organizations and the decisions that users of the information make about them. Accordingly, the objectives in this Statement are affected by the economic, legal, political, and social environment within which those organizations function in the United States. The objectives are also affected by the characteristics and limitations of the information that financial reporting can provide (paragraphs 23-28).

14. The operating environments of nonbusiness organizations and business enterprises are similar in many ways. Both nonbusiness organizations and business enterprises produce and distribute goods or services and use scarce resources in doing so. They sometimes provide

essentially the same goods or services. For example, both municipal transportation systems significantly subsidized by general tax revenues and private bus lines may carry passengers within a large city, and both private nonprofit organizations supported by significant philanthropy and investor-owned enterprises may operate theatrical, dance, and musical organizations.⁸ Both nonbusiness organizations and business enterprises obtain resources from external sources and are accountable to those who provide resources or their representatives. Both are integral parts of the national economy and interrelate directly or indirectly with other organizations. Both own or control supplies of resources, some of which are used in current operations and some of which are held for use in future periods. Both incur obligations. Some nonbusiness organizations, as well as business enterprises, incur and pay taxes, and both are subject to governmental laws and regulations. Both must be financially viable: To achieve their operating objectives, they must, *in the long run*, receive at least as many resources as they need to provide goods and services at levels satisfactory to resource providers and other constituents.⁹ Both generally obtain resources from the same pool of resource providers, and the resources available for use by all organizations are limited.

15. Differences between nonbusiness organizations and business enterprises arise principally in the ways they obtain resources. The following descriptions begin with areas of greatest similarity between nonbusiness organizations and business enterprises and end with the areas of greatest difference.

16. Both nonbusiness organizations and business enterprises obtain resources in exchange transactions in markets. Both obtain labor, materials, and facilities or their use by paying for them or agreeing to pay for them in the future.¹⁰ Both may borrow funds through bank loans, mortgages, or other direct loans or through issuing debt securities to creditors who commonly may evaluate and compare the risks and returns of securities of both nonbusiness organizations and business enterprises.

17. Both nonbusiness organizations and business enterprises may obtain resources by charging a price or fee for goods or services they provide, but the purpose of sales of goods or services is different. Some nonbusiness organizations may sell goods or services at prices that equal or exceed costs, but many nonbusiness organizations commonly provide goods or services at prices less than costs. Nonbusiness organizations also commonly provide goods or services free of charge. Moreover, those that charge prices sufficient to cover costs often use resources from those sales to subsidize other activities within the organization. For example, the football or basketball program at a college or university may finance both intercollegiate and intramural athletic programs. Although sales of goods or services may be important sources of financing for some nonbusiness organizations, nonbusiness organizations generally are not expected to and do not need to cover all costs, and perhaps earn profits, by sales because they rely significantly on other continuing sources of financing (paragraph 18). For example, some nonbusiness organizations have the power to assess dues, taxes, or other compulsory contributions, and others depend significantly on voluntary contributions. In contrast, business enterprises attempt to sell goods or services at prices that enable them to repay or compensate all resource providers,

including owners and others who expect a monetary return for providing resources. Profit is the basis for compensating owners and others for providing resources, and expectations of profit are necessary to attract resources. Moreover, unprofitable business enterprises find it increasingly difficult to borrow or otherwise obtain resources. Sales of goods or services are not only significant sources of resources for business enterprises but also underlie their ability to obtain resources from other sources.

18. Members, contributors, taxpayers, and others who provide resources to nonbusiness organizations do so for reasons different from those of owners of business enterprises. All nonbusiness organizations obtain significant resources from resource providers who either expect no economic benefits or expect benefits received not to be proportionate to the resources provided. Those resources are often provided for charitable, humanitarian, religious, or other noneconomic reasons.¹¹ As a result, those who provide resources to a nonbusiness organization and those who benefit from the goods or services it provides may be different individuals or groups. Owners of business enterprises, in contrast, generally expect returns through dividends or price appreciation of their securities commensurate with the perceived risk.

19. As the preceding paragraphs indicate, noneconomic reasons are commonly factors in decisions to provide resources to particular nonbusiness organizations. For example, contributors ¹² to philanthropic organizations, such as charities, and to some membership organizations, such as churches, generally seek no direct economic benefits. Rather, their reasons for voluntarily providing resources relate to their interests in furthering the purpose and goals of the organization. The goals may involve a wide range of endeavors including those of a charitable, cultural, educational, economic, religious, scientific, social, or political nature. Some kinds of membership organizations, such as professional and trade associations, assess membership dues. Persons joining these organizations often seek noneconomic benefits, such as recognition or prestige, in addition to direct service benefits.

20. Nonbusiness organizations and business enterprises have different degrees of involvement with markets. Most transactions of business enterprises with other entities involve exchange prices in active markets; that market mechanism provides a measure of the utility and satisfaction of goods and services businesses buy and sell and of the overall performance of those enterprises. Nonbusiness organizations also borrow money and buy goods and services in markets and may or may not sell goods or services in markets. However, market transactions play a more limited role in the resource allocation process of nonbusiness organizations because those organizations do not finance their operations through equity markets and they commonly receive resources and provide goods or services in other than market transactions. Since market controls exist to a lesser degree for nonbusiness organizations than for business enterprises, other kinds of controls are introduced to compensate for their absence.

21. Resource providers or governing bodies may restrict or mandate the ways a nonbusiness organization may spend the resources provided. Spending mandates generally take one of two forms: specific budgetary appropriations or direct restrictions by donors or grantors. For

example, a budgetary appropriation may limit the amount that a church may spend for its educational program or that a governmental unit may spend to subsidize its public transportation system, a donor or grantor may specify that a gift to a museum must be used to construct a new wing, or an agency of the federal government may specify that its grant to a university must be used for medical research. Those mandates give managers of nonbusiness organizations a special responsibility to ensure compliance. Although spending mandates also may exist in business enterprises, they are less common. Their effects on the conduct and control of the activities of business enterprises are less pervasive than in nonbusiness organizations.

22. Budgets are particularly significant in the nonbusiness environment. Both business and nonbusiness organizations use budgets to allocate and control uses of resources. However, in nonbusiness organizations for which providing resources is compulsory (for example, many membership organizations and governmental units), budgets are significant factors not only in allocating resources within an organization but also in obtaining resources. For example, budgets in membership organizations and governmental units are often pivotal in establishing the level of dues, taxes, or fees to be imposed; the level of services to be provided; and the desired relation between the two. Members and taxpayers may have the opportunity, either by direct vote or through elected representatives, to participate in developing and approving budgets. Elections and referendums also offer opportunities to change policies and the amounts and uses of resources provided. In other kinds of nonbusiness organizations, budgets may be important to voluntary donors in deciding whether to provide resources to nonbusiness organizations and in establishing the level of their giving.

Characteristics and Limitations of Information Provided by Financial Reporting

23. The objectives of financial reporting by nonbusiness organizations are affected not only by the environment in which financial reporting takes place but also by the characteristics and limitations of the kind of information that financial reporting, and particularly financial statements, can provide. The information provided by financial reporting is primarily financial in nature: It is generally quantified and expressed in terms of units of money. Information that is to be incorporated formally in financial statements must be quantifiable in terms of units of money. Other information can be disclosed in financial statements (including notes) or by other means, but financial statements involve adding, subtracting, multiplying, and dividing numbers that depict economic things and events and require a common denominator. Quantified information expressed in terms other than units of money (such as number of employees or units of services or products provided) and nonquantified information (such as descriptions of operations or explanations of policies) that are reported normally relate to or underlie the financial information. Information that is not expressed in terms of units of money may be needed to understand the significance of information expressed in terms of units of money or to help in assessing the performance of a nonbusiness organization (paragraphs 47-53). Financial reporting by nonbusiness organizations, however, is limited in its ability to provide direct measures of the quality of goods and services provided in the absence of market-determined exchange prices or the degree to which they satisfy the needs of service beneficiaries and other

consumers.

24. The information provided by financial reporting pertains to individual nonbusiness reporting entities. This Statement, however, does not include criteria for determining the appropriate reporting entity for purposes of financial reporting by nonbusiness organizations. That matter will need to be addressed by other projects.¹³

25. The information provided by financial reporting often results from approximate, rather than exact, measures. The measures commonly involve numerous estimates, classifications, summarizations, judgments, and allocations. Thus, despite the aura of precision that may seem to surround financial reporting in general and financial statements in particular, with few exceptions the measures are approximations which may be based on rules and conventions rather than exact amounts.

26. The information provided by financial reporting largely reflects the effects of transactions and events that have already happened. Governing bodies and managers may use budgets to communicate information about plans or projections, but most of the information provided by financial reporting is historical, including comparisons of actual results with previously approved budgets. The acquisition price of land and the current market price of a marketable equity security are other examples of historical data included in financial reports. No future amounts or events are involved. Estimates resting on expectations of the future are often needed in financial reporting, but their major use, especially of those formally incorporated in financial statements, is to measure financial effects of past transactions or events or the present status of an asset or liability.

27. Financial reporting is but one source of information needed by those who make economic decisions about nonbusiness organizations. They need to combine information provided by financial reporting with relevant social, economic, and political information from other sources.

28. The information provided by financial reporting involves a cost to provide and use. The cost includes not only the resources directly expended to provide the information but also may include adverse effects on an organization from disclosing it. For example, comments about a pending lawsuit may jeopardize a successful defense. The collective time needed to understand and use information is also a cost. Generally, the benefits of information provided should be expected to at least equal the cost involved.¹⁴ However, the benefits and costs usually are difficult to measure. Different persons will honestly disagree about whether the benefits of the information justify its cost.

Types of Users and Their Interests

29. Many people base economic decisions on their relationships to and knowledge about nonbusiness organizations and, thus, are interested in the information provided by financial reporting. Among present and potential users are members, taxpayers, contributors, grantors,

lenders, suppliers, creditors, employees, managers, directors and trustees, service beneficiaries, financial analysts and advisors, brokers, underwriters, lawyers, economists, taxing authorities, regulatory authorities, legislators, the financial press and reporting agencies, labor unions, trade associations, researchers, teachers, and students. The following groups are especially interested in information provided by the financial reporting of a nonbusiness organization:

- a. *Resource providers.* Resource providers include those who are directly compensated for providing resources—lenders, suppliers, and employees (paragraph 16)—and those who are not directly and proportionately compensated—members, contributors, and taxpayers (paragraph 18).¹⁵
- b. *Constituents.* Constituents are those who use and benefit from the services rendered by the organization. In some nonbusiness organizations, constituents include resource providers (for example, members who pay dues or taxpayers), and distinguishing constituents from resource providers may serve no function. However, resource providers and service beneficiaries are largely different groups or individuals in some organizations. The degree to which service beneficiaries are a distinctive part of a constituency depends largely on the extent of separation between those providing the resources and those using and receiving the service benefits.
- c. *Governing and oversight bodies.* Governing and oversight bodies are those responsible for setting policies and for overseeing and appraising managers of nonbusiness organizations. Governing bodies include boards of trustees, boards of overseers or regents, legislatures, councils, and other bodies with similar responsibilities. Oversight bodies also are responsible for reviewing the organization's conformance with various laws, restrictions, guidelines, or other items of a similar nature. Oversight bodies include national headquarters of organizations with local chapters, accrediting agencies, agencies acting on behalf of contributors and constituents, oversight committees of legislatures, and governmental regulatory agencies. In some nonbusiness organizations, governing bodies commonly are elected representatives of a constituency that is largely comprised of resource providers. In other nonbusiness organizations, governing bodies may be self-perpetuating through election of their successors.
- d. *Managers.* Managers of an organization are responsible for carrying out the policy mandates of governing bodies and managing the day-to-day operations of an organization. Managers include certain elected officials; managing executives appointed by elected governing bodies, such as school superintendents, agency heads, and executive directors; and staff, such as fund-raising and program directors.

30. Present and potential users of the information provided by financial reporting by a particular nonbusiness organization share a common interest in information about the services provided by the nonbusiness organization, its efficiency and effectiveness in providing those services, and its ability to continue to provide those services. Resource providers, such as members and contributors, may be interested in that information as a basis for assessing how well the organization has met its objectives and whether to continue support. Taxpayers may need similar information to help them assess whether governmental units and

government-sponsored entities have achieved their operating objectives. In addition, they may want to know how the services provided by the governmental unit or government-sponsored entity are likely to affect the amount of taxes and fees they will be required to pay. Resource providers, such as lenders, suppliers, and employees, view a nonbusiness organization as a source of payment for the cash, goods, or services they supply. Their interest stems from concern about the organization's ability to generate cash flows for timely payment of the organization's obligations to them. Governing and oversight bodies also use information about services rendered to help them evaluate whether managers have carried out their policy mandates and to change or formulate new policies for the organization. That information also is important to managers in evaluating the accomplishment of the responsibilities for which they are accountable to governing bodies, resource providers, and other constituents. Constituents, including recipients and beneficiaries of services who as a group are distinct from resource providers, share a direct interest in similar information.

31. Some users have specialized needs but also have the power to obtain the information they need. For example, donors and grantors who restrict the use of resources they provide often stipulate that they be apprised periodically of the organization's compliance with the terms and conditions of the gift or grant. Creditors also may be able to stipulate that certain specialized types of information be provided. Special-purpose reports directed at those kinds of needs are beyond the scope of this Statement.

32. Managers and, to some extent, governing bodies commonly are described as "internal users." In addition to the information provided by financial reporting, they need a great deal of internal accounting information to carry out their responsibilities in planning and controlling activities. Much of that information relates to particular decisions or to managers' exercise of their stewardship responsibility to ensure that resources are used for their intended purposes. For example, governing bodies and managers need information to evaluate properly the competing requests for funding of capital projects. They also need information to assist them in complying or overseeing compliance with spending mandates established by budgetary appropriations or donor or grantor restrictions. They need to know how much of a budgetary appropriation or restricted grant is unspent or uncommitted. They need to know that restricted resources were expended or committed in compliance with related mandates. Generally, both the number of spending mandates and the detail about them required to meet the informational needs of managers are so great that the usefulness of general purpose external financial reports would be reduced significantly if they reported the status of compliance with each mandate (paragraph 41). Since the type of reporting described in this paragraph needs to be tailored to meet the specialized needs of managers and governing bodies of particular organizations, it is beyond the scope of this Statement.

OBJECTIVES OF FINANCIAL REPORTING

33. The following objectives of financial reporting flow from the preceding paragraphs and proceed from the general to the specific. The objectives begin with a broad focus on information that is useful to resource providers and other users in making rational decisions about allocating resources to nonbusiness organizations. The focus is then narrowed to the needs of resource providers and other users for information about the services an organization provides and its ability to continue to provide those services. That directs their attention to information about the organization's performance and how its managers have discharged their stewardship responsibility. Finally, the objectives focus on the types of information financial reporting can provide to meet those needs. The reasons for focusing the objectives of financial reporting on decisions generally made by resource providers are given in paragraph 36. That focus and wording do not mean that the objectives apply to only resource providers. On the contrary, information that satisfies the objectives should be useful to all who are interested in a nonbusiness organization's present and future capacity to render service and achieve its operating goals.

34. The objectives are those of financial reporting rather than goals for resource providers or others who use the information or for the economy or society as a whole. The role of financial reporting in the economy and society is to provide information that is useful in making decisions about allocating scarce resources, not to determine what those decisions should be. For example, information that tries to indicate that a relatively inefficient user of resources is efficient or information that is directed toward a particular goal, such as encouraging the reallocation of resources in favor of certain programs or activities of nonbusiness organizations, is likely to fail to serve the broader objectives that financial reporting is intended to serve. The role of financial reporting requires it to provide neutral information.

Information Useful in Making Resource Allocation Decisions

35. Financial reporting by nonbusiness organizations should provide information that is useful to present and potential resource providers and other users in making rational decisions about the allocation of resources to those organizations. The information should be comprehensible to those who have a reasonable understanding of an organization's activities and are willing to study the information with reasonable diligence.

36. Resource providers are important users of information provided by financial reporting who generally cannot prescribe the information they want. Their decisions significantly affect both nonbusiness organizations and the allocation of resources in society generally. In addition, information provided to meet the needs of present and potential resource providers is likely to be useful to others who are interested in essentially the same aspects of nonbusiness organizations

as resource providers.

37. The potential users listed in paragraph 29 understand, to varying degrees, the environment within which a nonbusiness organization operates, the nature of its activities, and related matters. Their understanding of information provided by financial reporting and the extent to which they use and rely on it also varies greatly. Financial reporting information is a tool and, like most tools, cannot be of much direct help to those who are unable or unwilling to use it or who misuse it. Its use can be learned, however, and financial reporting should provide information that can be used by all who are willing to learn to use it properly. Efforts may be needed to increase the understandability of information provided by financial reporting. Cost/benefit considerations may indicate that information understood or used by only a few should not be provided.¹⁶ Conversely, financial reporting should not exclude relevant information merely because it is difficult for some to understand or because some choose not to use it.

Information Useful in Assessing Services and Ability to Provide Services

38. Financial reporting should provide information to help present and potential resource providers and other users in assessing the services¹⁷ that a nonbusiness organization provides and its ability to continue to provide those services.¹⁸ They are interested in that information because the services are the end for which the resources are provided. The relation of the services provided to the resources used to provide them helps resource providers and others assess the extent to which the organization is successful in carrying out its service objectives.

39. Resources are the lifeblood of an organization in the sense that it uses resources to provide services. A nonbusiness organization cannot, in the long run, continue to achieve its operating objectives unless the resources made available to it at least equal the resources needed to provide services at levels satisfactory to resource providers and other constituents. Although decisions of potential and present resource providers to provide or continue to provide resources involve expectations about future services of an organization, those expectations commonly are based at least partly on evaluations of past performance. Thus, resource providers tend to direct their interest to information about the organization's resources and how it acquires and uses resources. The focus of that interest is information about the organization's performance and how its managers have discharged their stewardship responsibility during a period.

Information Useful in Assessing Management Stewardship and Performance

40. Financial reporting should provide information that is useful to present and potential resource providers and other users in assessing how managers of a nonbusiness organization have discharged their stewardship responsibilities and about other aspects of their performance. Managers of an organization are accountable to resource providers and others, not only for the custody and safekeeping of organization resources, but also for their efficient and effective use. Those who provide resources to nonbusiness organizations do not have a profit indicator to guide

their resource allocation decisions and may not have an immediate choice about the amounts of their contributions. They must look to managers to represent their interests and to make operating cost/benefit judgments that achieve the objectives of the organizations with minimum use of resources. Managers also are accountable for compliance with statutory, contractual, or other limitations.

41. Information about an organization's performance (paragraphs 47-53) should be the focus for assessing the stewardship or accountability of managers of a nonbusiness organization. Users also need assurance that managers have exercised their special responsibilities to ensure that an organization uses resources in the manner specifically designated by resource providers. General purpose external financial reporting can best meet that need by disclosing failures to comply with spending mandates that may impinge on an organization's financial performance or on its ability to continue to provide a satisfactory level of services.

42. Financial reporting is limited in its ability to distinguish the performance of managers from that of the organization itself. Nonbusiness organizations are often highly complex institutions, and the processes by which they acquire resources and render services often are long and intricate. Organizational successes and failures are the result of numerous factors. The ability and performance of managers are contributing factors, as are events and circumstances that often are beyond the control of managers. It is usually not possible to determine the degree to which managers, or any other specific factors, have affected the result. Actions of past managers affect current periods' performance, and actions of present managers affect future periods' performance.

Information about Economic Resources, Obligations, Net Resources, and Changes in Them

43. Financial reporting should provide information about the economic resources, obligations, and net resources of an organization and the effects of transactions, events, and circumstances that change resources and interests in those resources.¹⁹ That type of information is useful in achieving each of the above objectives.

Economic Resources, Obligations, and Net Resources

44. Financial reporting should provide information about an organization's economic resources, obligations, and net resources. That information helps resource providers and others identify the organization's financial strengths and weaknesses, evaluate information about the organization's performance during a period (paragraphs 47-53), and assess its ability to continue to render services.

45. Information about an organization's economic resources, obligations, and net resources also provides direct indications of the cash flow potential of some resources and of the cash needed to satisfy many, if not most, obligations. The assessment of cash flow potential is important because it relates directly to the organization's ability to provide the goods and

services for which it exists.

46. Resources provided to nonbusiness organizations often are restricted by providers as to time and for particular purposes (paragraph 21). Accordingly, information about restrictions on the use of resources is important for assessing the types and levels of services an organization is able to provide. That information is also important to creditors in assessing their prospects for receiving cash.²⁰

Organization Performance

47. Financial reporting should provide information about the performance of an organization during a period. Periodic measurement of the changes in the amount and nature of the net resources of a nonbusiness organization and information about the service efforts and accomplishments of an organization together represent the information most useful in assessing its performance.

Nature of and Relation between Inflows and Outflows

48. Financial reporting should provide information about the amounts and kinds of inflows and outflows of resources during a period. It should distinguish resource flows that change net resources, such as inflows of fees or contributions and outflows for wages and salaries, from those that do not change net resources, such as borrowings or purchases of buildings. It also should identify inflows and outflows of restricted resources.

49. Financial reporting should provide information about the relation between inflows and outflows of resources during a period. Those who provide resources to a nonbusiness organization and others want to know how and why net resources changed during a period. To meet that need, financial reporting must distinguish between resource flows that are related to operations and those that are not.²¹ In this way, financial reporting may provide information that is useful in assessing whether the activities of a nonbusiness organization during a particular period have drawn upon, or have contributed to, past or future periods. Thus, it should show the relation of resources used in operations of a period to resource inflows available to finance those operations. Similarly, it should provide information about changes in resources that are not related to operations. For example, resource providers to colleges or universities need information about changes in an organization's endowment and plant to understand more fully the changes in its net resources during a period.

50. The information described in paragraphs 47-49 measured by accrual accounting generally provides a better indication of an organization's performance than does information about cash receipts and payments.²² Accrual accounting attempts to record the financial effects of transactions, events, and circumstances that have cash consequences for an organization in the periods in which those transactions, events, and circumstances occur rather than in only the periods in which cash is received or paid by the organization. Accrual accounting is concerned

with the process by which cash is obtained and used, not with just the beginning and end of that process. It recognizes that the acquisition of resources needed to provide services and the rendering of services by an organization during a period often do not coincide with the cash receipts and payments of the period.²³

Service Efforts and Accomplishments

51. Information about an organization's service efforts and accomplishments is useful to resource providers and others in assessing the performance of a nonbusiness organization and in making resource allocation decisions, particularly because:

- a. The accomplishments of nonbusiness organizations generally cannot be measured in terms of sales, profit, or return on investment.
- b. Resource providers often are not in a position to have direct knowledge of the goods or services provided when they also are not users or beneficiaries of those goods and services.

52. Financial reporting should provide information about the service efforts of a nonbusiness organization. Information about service efforts should focus on how the organization's resources (inputs such as money, personnel, and materials) are used in providing different programs or services. Techniques for measuring the costs of significant programs or services are well developed and this information normally should be included in financial statements.

53. Ideally, financial reporting also should provide information about the service accomplishments of a nonbusiness organization. Information about service accomplishments in terms of goods or services produced (outputs) and of program results²⁴ may enhance significantly the value of information provided about service efforts. However, the ability to measure service accomplishments, particularly program results, is generally undeveloped. At present, such measures may not satisfy the qualitative characteristics of accounting information identified in Concepts Statement 2. Research should be conducted to determine if measures of service accomplishments with the requisite characteristics of relevance, reliability, comparability, verifiability, and neutrality can be developed. If such measures are developed, they should be included in financial reports. In the absence of measures suitable for financial reporting, information about service accomplishments may be furnished by managers' explanations and sources other than financial reporting.

Liquidity

54. Financial reporting should provide information about how an organization obtains and spends cash or other liquid resources, about its borrowing and repayment of borrowing, and about other factors that may affect its liquidity. Information about those resource flows may be useful in understanding the operations of an enterprise, evaluating its financing activities, assessing its liquidity, or interpreting performance information provided. Information about performance and economic resources, obligations, and net resources also may be useful in assessing an enterprise's liquidity.

Managers' Explanations and Interpretations

55. Financial reporting should include explanations and interpretations to help users understand financial information provided. For example, the usefulness of financial information to resource providers and others may be enhanced by managers' explanations of the information. Since managers usually know more about the organization and its affairs than do resource providers or others outside the organization, they often can increase the usefulness of information provided by financial reporting by identifying certain transactions, events, and circumstances that affect the organization and by explaining their financial impact.²⁵ In addition, dividing continuous operations into accounting periods is a convention and may have arbitrary effects. Managers can enhance the usefulness of information contained in financial reports by identifying arbitrary results caused by allocations between periods and by describing the effects of those allocations on reported information. Moreover, financial reporting often provides information that depends on, or is affected by, managers' estimates and judgments. Users are aided in evaluating estimates and judgments by explanations of underlying assumptions and methods used, including disclosure of significant uncertainties about principal underlying assumptions or estimates.

THE NONBUSINESS OBJECTIVES PROJECT—A PERSPECTIVE

56. Paragraphs 43-54 focus on information that assists resource providers and other users in assessing an organization's financial viability, its performance, and how the organization's managers have discharged their stewardship responsibilities. Those paragraphs emphasize information about an organization's economic resources, obligations, and net resources and its performance during a period. The objectives lead to, but leave unanswered, questions such as the identity, number, and form of financial statements; elements of financial statements and their recognition, measurement, and display; and criteria for determining the reporting entity. The Board's approach to resolving those questions will be to integrate consideration of nonbusiness organizations into its series of conceptual framework projects. That integration may involve initiating new projects to deal with issues that may be more prevalent in or unique to nonbusiness organizations.

This Statement was adopted by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Donald J. Kirk, *Chairman*
Frank E. Block
John W. March
Robert A. Morgan
David Mosso
Robert T. Sprouse
Ralph E. Walters

Appendix A: BACKGROUND INFORMATION

Brief History of FASB Nonbusiness Objectives Project

57. The Board's project on objectives of financial reporting by nonbusiness organizations is related to and part of its effort to develop a conceptual framework for financial reporting. The Board began its work on a conceptual framework in 1973 and used as a point of departure the Report of the Study Group on the Objectives of Financial Statements, *Objectives of Financial Statements* (Trueblood Report), published by the American Institute of Certified Public Accountants in October 1973. That report included governmental and not-for-profit organizations in its scope.

58. As more fully discussed in paragraphs 57-62 of Concepts Statement 1, the Board initially considered the 12 objectives of financial statements in the Trueblood Report but decided to concentrate its initial efforts on formulating objectives of financial reporting by business enterprises. Initially, therefore, the Board did not attempt to reach conclusions on the objectives of financial reporting for governmental and not-for-profit organizations.

59. The need to consider the objectives of general purpose external financial reporting by nonbusiness organizations generally is recognized. An increasing number of public officials and private citizens are questioning the relevance and reliability of financial accounting and reporting by nonbusiness organizations. That concern has been reflected in legislative initiatives and well-publicized allegations of serious deficiencies in the financial reporting of various types of nonbusiness organizations.

60. In response to those concerns, the Board, in August 1977, engaged Professor Robert N. Anthony of the Harvard Business School to prepare a research report aimed at identifying the objectives of financial reporting by organizations other than business enterprises. A 53-member advisory group was appointed to assist in that effort. When the Board began consideration of objectives of financial reporting by nonbusiness organizations in August 1977, significant

progress already had been made on the objectives of financial reporting by business enterprises. Rather than delay progress on that project to include nonbusiness organizations in its scope, and to explore thoroughly the issues in the nonbusiness area, the Board proceeded with two separate objectives projects. The Board issued Concepts Statement 1 in November 1978. Paragraph 1 of Concepts Statement 1 states:

This Statement establishes the objectives of general purpose external financial reporting by business enterprises. Its concentration on business enterprises is not intended to imply that the Board has concluded that the uses and objectives of financial reporting by other kinds of entities are, or should be, the same as or different from those of business enterprises. Those and related matters, including whether and, if so, how business enterprises and other organizations should be distinguished for the purpose of establishing objectives of and basic concepts underlying financial reporting, are issues in another phase of the Board's conceptual framework project.

61. In May 1978, the Board published the FASB Research Report, *Financial Accounting in Nonbusiness Organizations*, prepared by Professor Anthony. The Board added the nonbusiness objectives project to its technical agenda on May 11, 1978 and directed the staff to prepare a Discussion Memorandum to solicit public comment. The Discussion Memorandum was issued on June 15, 1978. It focused on specific issues discussed in the Research Report and identified those on which the Board sought comments.

62. The Board held public hearings in Washington, D.C. on October 12 and 13, 1978; in San Francisco on October 19 and 20, 1978; and in Chicago on November 3, 1978. The Board received 87 written responses to the Discussion Memorandum, and 48 oral presentations were made at the public hearings.

63. The Board issued an Exposure Draft, *Objectives of Financial Reporting by Nonbusiness Organizations*, on March 14, 1980. In preparing the Exposure Draft, the Board deliberated the issues at meetings which were open to public observation. FASB Board and staff members have met with and maintained close liaison with various groups and individuals in the community of nonbusiness organizations since the outset of this project. In addition, persons from academe, public accounting, and various nonbusiness organizations provided counsel to the Board and its staff in preparing the Exposure Draft. The Board received 77 letters of comment on the Exposure Draft and considered the issues raised by respondents in those comment letters at meetings which were open to public observation.

64. The major differences between this Statement and the Exposure Draft are revisions to the scope of the document. The types of organizations to which the objectives in this document apply have been clarified (paragraph 1 of the Exposure Draft), and a discussion has been added concerning the relationship of this Statement to Concepts Statement 1. Other significant changes are (a) the addition of examples of various types of nonbusiness organizations in the

environment section (paragraphs 13-22); (b) greater emphasis on distinguishing flows that affect operations from those that do not (paragraph 49); (c) greater emphasis on the need for research to determine if measures of service accomplishments with the requisite characteristics of relevance, reliability, comparability, verifiability, and neutrality can be developed; and (d) acknowledgement that, in the absence of that financial reporting capability, information about service accomplishments may be furnished by managers' explanations and sources other than financial reporting.

State and Local Governmental Units

65. Others have been studying the objectives of financial reporting by governmental units during the period that the Board has been deliberating the issues and preparing this concepts Statement. The National Council on Governmental Accounting is sponsoring research in the broad area of a conceptual framework for governmental accounting, which includes the objectives of external financial reporting by state and local governmental units. A state accounting project that was commissioned by the Council of State Governments includes a study of objectives of accounting and financial reporting by state governments. The U.S. General Accounting Office is developing a statement of the objectives of financial reporting by the federal government and its agencies.

66. Since the publication of the Exposure Draft of this concepts Statement, the Board and its staff have monitored developments on the three projects discussed above. This monitoring has consisted of reviewing and analyzing working drafts of certain materials made available to the FASB by the NCGA and other researchers. On the basis of its study to date, the Board is aware of no persuasive evidence that the objectives in this Statement are inappropriate for general purpose external financial reports of governmental units.

Appendix B: COMPARISON OF OBJECTIVES IN THIS STATEMENT TO THOSE IN CONCEPTS STATEMENT 1

67. This Statement follows the *structure* of Concepts Statement 1. Both sets of objectives are based on the fundamental notion that financial accounting and reporting concepts and standards should be based on their decision usefulness. Thus, the objectives in this Statement and in Concepts Statement 1 focus on:

- a. Types of users of the information provided by financial reporting and the types of decisions they make
- b. The broad interests of the users identified and the information they need to assist them in making decisions
- c. The type of information financial reporting can provide to help satisfy their informational needs.

The following chart compares the similarities and differences of this Statement and Concepts Statement 1 in each of those areas.

<u>Purpose of Objectives</u>	<u>Nonbusiness Organizations Concepts Statement 4</u>	<u>Business Enterprises Concepts Statement 1</u>	<u>Comparison of Objectives</u>
a. Identifies (1) the types of users that financial reporting should focus on in providing information and (2) the types of decisions those users make.	a. Financial reporting by nonbusiness organizations should provide information that is useful to present and potential resource providers and other users in making rational decisions about the allocation of resources to those organizations (paragraph 35).	a. Financial reporting should provide information that is useful to present and potential investors and creditors and other users in making rational investment, credit, and similar decisions (paragraph 34).	a(1) Investors and creditors are major resource providers to business enterprises. Thus, resource providers, as a type of user, include investors and creditors as well as other groups identified in Concepts Statement 4. a(2) Both Statements focus on providing information useful in deciding whether to provide resources to an entity. The reasons for providing the resources, in each case, are quite different. Investors and creditors of business enterprises seek monetary repayment of and a return on resources they provide. Nonbusiness organizations, in contrast, obtain significant resources from resource providers who either expect no economic benefits or expect benefits that are not proportionate to the resources provided.

b. Identifies the broad interests of the users identified and the information they need to assist them in making the type of decisions described above.

b(1) Financial reporting should provide information to help present and potential resource providers and other users in assessing the services that a nonbusiness organization provides and its ability to continue to provide those services (paragraph 38).

b(2) Financial reporting should provide information that is useful to present and potential resource providers and other users in assessing how managers of a nonbusiness organization have discharged their stewardship responsibilities and about other aspects of their performance (paragraph 40).

b(1) Financial reporting should provide information to help present and potential help present and potential investors and creditors and other users in assessing the amounts, timing, and uncertainty of prospective cash receipts from dividends or interest and the proceeds from the sale, redemption, or maturity of securities or loans (paragraph 37).

b(2) Financial reporting should provide information about how management of an enterprise has discharged its stewardship responsibility to owners (stockholders) for the use of enterprise resources entrusted to it (paragraph 50).

b(1) These two objectives reflect the different interests of the respective resource providers. Those different interests lead to the other major area of difference in the objectives: the types of information financial reporting should provide about performance.

b(2) The substance of these two objectives is similar but their placement within the two Statements is different. In this Concepts Statement, the objective is viewed as a basic information need of users. In Concepts Statement 1, it was viewed as information financial reporting could provide to satisfy other basic information needs. That difference in placement arises from the importance of stewardship information in the environment of nonbusiness organizations. It is more important because the organization often is not self-sustaining (not profit oriented) and is dependent upon the continuing support of its resource providers. Consequently, there often is a more direct relationship between resource providers and the entity than for a business enterprise.

c. Identifies the type of information financial reporting can provide to help satisfy users' informational needs.	c. Financial reporting should provide information about the economic resources, obligations, and net resources of an organization and the effects of transactions, events, and circumstances that change resources and interests in those resources (paragraph 43).	c. Financial reporting should provide information about the economic resources, of an enterprise, the claims to those resources (obligations of the enterprise to transfer resources to other entities and owners' equity), and the effects of transactions, events, and circumstances that change resources and claims to those resources (paragraph 40).	c. The objectives are similar except for differences in terminology that reflect one of the distinguishing characteristics of nonbusiness organizations—the lack of ownership interests entitled to a residual distribution in the event of liquidation.
	(1) Financial reporting should provide information about an organization's economic resources, obligations, and net resources (paragraph 44).	(1) Financial reporting should provide information about an enterprise's economic resources, obligations, and owners' equity (paragraph 41).	(1) Except for differences in terminology, these objectives are the same.
	(2) Financial reporting should provide information about the performance of an organization during a period. Periodic measurement of the changes in the amount and nature of the net resources of a nonbusiness organization and information about the service efforts and accomplishments of an organization together represent the information most useful in assessing its performance (paragraph 47).	(2) Financial reporting should provide information about the enterprise's financial performance during a period. The primary focus of financial reporting is information about an enterprise's performance provided by measures of earnings and its components (paragraphs 42 and 43).	(2) The goals of the two objectives are the same but, because of the distinguishing characteristics of nonbusiness organizations, somewhat different information is required to satisfy those goals. Both seek to measure the efforts and accomplishments of the entity but assessment of performance in nonbusiness lacks earnings as a focal measure. This creates the need for information on service efforts and accomplishments.

(3) Financial reporting should provide information about how an organization obtains and spends cash or other liquid resources, about its borrowing and repayment of borrowing, and about other factors that may affect its liquidity (paragraph 54).

(4) Financial reporting should include explanations and interpretations to help users understand financial information provided (paragraph 55).

(3) Financial reporting should provide information about how an enterprise obtains and spends cash, about its borrowing and repayment of borrowing, about its capital transactions, including cash dividends and other distributions of enterprise resources to owners, and about other factors that may affect an enterprise's liquidity or solvency (paragraph 49).

(4) Financial reporting should include explanations and interpretations to help users understand financial information provided (paragraph 54).

(3) Except for differences in terminology and circumstances that reflect the lack of ownership interests entitled to receive cash dividends and other distributions of entity resources in nonbusiness organizations, these objectives are the same.

(4) These objectives are the same.

Footnotes

CON4, Footnote *-- Generally accepted accounting principles for nonbusiness organizations are primarily set forth in publications of the American Institute of Certified Public Accountants (AICPA) and other bodies, such as the National Council on Governmental Accounting (NCGA). The Board has agreed to exercise responsibility, except as noted below, for all the specialized accounting and reporting principles and practices in AICPA Statements of Position and Guides that are neither superseded by nor contained in Accounting Research Bulletins, Accounting Principles Board Opinions, FASB Statements, and FASB Interpretations. The Board deferred similar action with regard to those specialized accounting and reporting principles and practices contained in the AICPA Industry Audit Guide, *Audits of State and Local Governmental Units*, and the three Statements of Position (75-3, *Accruals of Revenues and Expenditures by State and Local Governmental Units*; 77-2, *Accounting for Interfund Transfers of State and Local Governmental Units*; and 80-2, *Accounting and Financial Reporting by Governmental Units*) that supplement that Guide. In so doing, the Board noted that at the present time the accounting and reporting by such governmental units is addressed by the AICPA and the NCGA. The Board also noted that discussions are continuing among interested parties, including the AICPA, the Financial Accounting Foundation (FAF), and NCGA, as to what the appropriate structure for accounting standard setting for such governmental units should be. Until the matter is resolved, the FASB proposes no changes with respect to its involvement with pronouncements in that area (paragraphs 3-5).

CON4, Footnote **-- Rule 203 prohibits a member of the American Institute of Certified Public Accountants from expressing an opinion that financial statements conform with generally accepted accounting principles if those statements contain a material departure from an accounting principle promulgated by the Financial Accounting Standards Board, unless the member can demonstrate that because of unusual circumstances the financial statements otherwise would have been misleading. Rule 204 requires members of the Institute to justify departures from standards promulgated by the Financial Accounting Standards Board for the disclosure of information outside of financial statements in published financial reports.

CON4, Footnote 1--The Board recognizes that standard setting for the federal government is not in question. Although the Board sees no conceptual reasons why the objectives in this Statement could not be applied to general purpose external financial reporting by the federal government, the Board acknowledges that determination is the responsibility of others.

CON4, Footnote 2--These types of transactions are classified in APB Statement No. 4, *Basic Concepts and Accounting Principles Underlying Financial Statements of Business Enterprises*, as nonreciprocal transfers. Nonreciprocal transfers are therein defined as "transfers in one direction of resources or obligations, either from the enterprise to other entities or from other entities to the enterprise" (paragraphs 62 and 182). Two types of such transfers noted are: (a) transfers between the enterprise and its owners and (b) transfers between the enterprise and

entities other than owners. Transactions of the second type frequently are found in nonbusiness organizations.

CON4, Footnote 3--The FASB Research Report, *Financial Accounting in Nonbusiness Organizations*, distinguishes two types of nonprofit organizations based "on a difference in the source of the financial resources" (page 161). A Type A nonprofit organization is therein defined as "a nonprofit organization whose financial resources are obtained, entirely, or almost entirely, from revenues from the sale of goods and services" (page 162). A Type B nonprofit organization, in contrast, is defined as "a nonprofit organization that obtains a significant amount of financial resources from sources other than the sale of goods and services" (page 162). The Type B category corresponds to the type of organizations that clearly falls within the focus of this Statement.

CON4, Footnote 4--The organizations described in this paragraph correspond to the Type A category described in the preceding footnote. To the extent, however, that Type A organizations have the unique transactions described in paragraph 6, they naturally will be impacted by standards promulgated by the Board in those areas.

CON4, Footnote 5--Creditors of nonbusiness organizations are also interested in receiving cash. Because of the differences in environment (principally the motivations of other resource providers) and different indicators of the performance of a nonbusiness organization, creditors also look to information useful in assessing the services that type of organization provides and its ability to continue to provide services to satisfy their basic interest in the prospect for cash flows.

CON4, Footnote 6--Distinctions between financial reporting and financial statements are discussed at more length in Concepts Statement 1 (paragraphs 5-8), and are the subject of another phase of the Board's conceptual framework project.

CON4, Footnote 7--Economic decisions about nonbusiness organizations may take different forms depending on the factors that are evident in the resource allocation process affecting an organization. For example, if an element of compulsion is present as it is with members paying dues or taxpayers paying taxes, this Statement describes processes, such as approval of budgets, elections, referendums, and involvement in legislative processes, through which resource providers decide or influence decisions about matters that affect the amount and use of resources allocated to organizations. A member may discontinue membership or a taxpayer may choose to locate in one governmental jurisdiction rather than another as a result of assessment of their respective policies. That kind of action also represents, in part, the result of an economic decision.

CON4, Footnote 8--Other nonprofit organizations (paragraph 8) lacking all the distinguishing characteristics of nonbusiness organizations also may provide the services described in this sentence.

CON4, Footnote 9--Some nonbusiness organizations are established for short-term purposes and are not intended to survive after completing their operating objectives, such as an organization established to erect a memorial.

CON4, Footnote 10--Nonbusiness organizations also may receive significant donations of labor, materials, and facilities or their use from resource providers.

CON4, Footnote 11--Contributors to nonbusiness organizations often provide resources, such as property, materials, and uncompensated volunteer labor, in addition to financial resources. In many nonbusiness organizations, such as charities and youth groups, these donated materials and services are significant factors in the organization's operations. In other nonbusiness organizations, especially those operated by religious bodies, services contributed by personnel at far less than their market value are equally significant. Such donated or contributed services and materials are rarely found in business enterprises.

CON4, Footnote 12--Contributors include donors and prospective donors, grantors and prospective grantors, and federated fund-raising organizations that solicit contributions and then redistribute those contributions to nonbusiness organizations after deducting fund-raising and other costs.

CON4, Footnote 13--A discussion of the reporting entity issue can be found in the FASB Research Report on financial accounting in nonbusiness organizations, pages 18-21.

CON4, Footnote 14--Paragraphs 133-144 of FASB Concepts Statement No. 2, *Qualitative Characteristics of Accounting Information*, expand on the cost/benefit considerations discussed in this paragraph. The Board intends to solicit views regarding its tentative conclusion that the qualities of information set forth in Concepts Statement 2 also apply to accounting information of nonbusiness organizations.

CON4, Footnote 15--Taxpayers provide resources to nonbusiness organizations both directly and indirectly. They pay taxes to all levels of government. Governments (especially federal and state), in turn, provide funding to other levels of government, government-sponsored entities, and private nonbusiness organizations.

CON4, Footnote 16--See footnote 14.

CON4, Footnote 17--The term *services* in this context encompasses the goods as well as the services a nonbusiness organization may provide.

CON4, Footnote 18--An organization's ability to continue to provide services ultimately depends on its ability to obtain resources from resource providers. The ability to obtain sufficient resources normally is not discussed in general purpose external financial reports unless that ability is in doubt. Paragraphs 43-55 discuss the type of information financial reporting can

provide to meet the objective in paragraph 38.

CON4, Footnote 19--In FASB Concepts Statement No. 3, *Elements of Financial Statements of Business Enterprises*, the Board has attempted to define many elements (for example, assets and liabilities) in a way that they could apply to all types of entities. In the near future, the Board expects to consider and solicit views about which, if any, of the definitions are inappropriate or may require modification for nonbusiness organizations and whether other elements are needed for financial statements of nonbusiness organizations.

CON4, Footnote 20--Issues that affect how, if at all, restricted resources are displayed in financial statements, for example, by using multi-column presentations or disclosure in the notes, are outside the scope of this Statement and may be the subject of future Board projects.

CON4, Footnote 21--Resource flows that are not related to operations have been described in various ways, for example, as "nonexpendable," "capital," or "restricted" flows. The Board's endorsement of distinguishing these types of flows is not intended to prejudge future determinations of (a) the criteria that should be used in making this distinction and (b) how and in what financial statements different types of flows might be displayed.

CON4, Footnote 22--In some relatively small organizations, the benefits of the better information obtained from accrual accounting may not justify the costs of obtaining that information (footnote 14).

CON4, Footnote 23--Accrual accounting is concerned with the timing of recognizing transactions, events, and circumstances that have financial effects on an organization. This paragraph is not intended to prejudge specific recognition and measurement issues involved in applying accrual accounting in the nonbusiness area. For example, whether certain inflows of financial resources, such as taxes, grants, and contributions, should be recognized in the period when a claim arises, when they are received, when they are appropriated for use, when they are used, or when other events occur, is beyond the scope of this Statement.

CON4, Footnote 24--Service accomplishments generally may be viewed as the results of service efforts. The FASB Research Report, *Reporting of Service Efforts and Accomplishments*, distinguishes two possible measures of accomplishments, outputs and results. "*Outputs* usually are observable directly as a result of service delivery; they describe goods and services provided by service delivery but do not measure impact upon clients or problems. . . . *Results*. . . represent impact upon clients or problem situations" (page 7). In discussing this latter measure, this Statement uses the term *program results*.

CON4, Footnote 25--These discussions may include information about service efforts and accomplishments as described in paragraphs 51-53.