

Subject: **Disclosure of Board's Definition of Permanently Restricted Funds, in Accordance with FSP FAS 117-1**

Executive Summary

According to FASB Staff Position (FSP) FAS 117-1, *a non-profit organization shall disclose information to enable users of financial statements to understand policies related to its endowment funds*, and the annual financial statements shall include a description of the governing board's interpretation of the law that underlies the organization's net asset classification of donor-restricted endowment funds.

The recommended view under the guidance provided by the Financial Accounting Standards Board (FASB) for the new Uniform Act (UPMIFA) is to continue to define permanently restricted net assets as the historic-dollar-value of donor-restricted gifts to endowment. Historic-dollar-value is defined as the fair value of the original gift and subsequent gifts as of the gift dates, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor instrument. Under this definition, the remaining portion of the fund, i.e. reinvested returns on invested endowment funds, are booked on the financial records as temporarily restricted net assets. According to the FASB, this view *provides the most faithful representation of the organization's fiduciary duty for its donor-restricted endowment funds, and is both workable and appropriate*.

If this recommendation is adopted by the [board], our financial reporting methodology will remain the same as it has been in previous years. Since there is also a preference for the governing board's interpretation of the relevant law to be consistent from year-to-year going forward, it is our intention to make this a permanent decision, to be reviewed in the event of future changes in the law, relevant court activity and additional guidance from FASB.

Background

The [state] has enacted a version of UPMIFA, the Uniform Prudent Management of Institutional Funds Act, a model act approved by the Uniform Law Commission that serves as a guideline for states to use in enacting legislation. This replaces a previous law, UMIFA, the Uniform Management of Institutional Funds Act. Under UMIFA, spending below the historic-dollar-value of an endowment was not permitted; the accounting definition of permanently restricted funds was the historic-dollar-value of a donor-restricted gift to endowment. Under UPMIFA, the historic-dollar-value threshold is eliminated, and the governing board has discretion to determine appropriate expenditures of a donor-restricted endowment fund in accordance with a robust set of guidelines about what constitutes prudent spending. Although UPMIFA offers short-term spending flexibility, the explicit consideration of the preservation of funds among factors for prudent spending suggests that a donor-restricted endowment fund is still perpetual in nature.

As is the case in the current financial environment, there is no guarantee that the permanently restricted amount of an endowment will remain intact at all times. Under UPMIFA, the Board is permitted to determine and continue a prudent payout amount, even if the market value of the fund is below historic-dollar-value. There is an expectation that, over time, the permanently restricted amount will remain intact. This perspective is aligned with the accounting standards definition that permanently restricted funds are those that must be held in perpetuity even though the historic-dollar-value may be dipped into on a temporary basis.

Proposed Resolution

Whereas, FAS 117-1 requires the annual financial statements for non-profit organizations issued for years ending after December 15, 2008, to include a description of the governing board's interpretation of the law underlying the organization's net asset classification of donor-restricted endowment funds;

Whereas, UPMIFA was adopted by the [state] and became effective [date];

Whereas, the language of a specific endowment agreement is the primary determinant of the application of spending policy to a donor-restricted endowment;

Whereas, the standard endowment agreement between donors and the foundation agrees to follow the board approved spending policy, and the policy permits temporary use of historic-dollar-value and takes a long-term view towards protecting the principal;

Whereas, historic-dollar-value is defined as the fair value of the original gift and subsequent gifts as of the gift date, and accumulations to the permanent endowment made in accordance with the direction of the applicable donor instrument,

Whereas, this resolution is consistent with the recommended guidance provided by the FASB for FAS 117-1 and has been reviewed by legal counsel;

Resolved, that the [organization] has interpreted the [state law] as requiring the preservation of the fair value of the original gift as of the gift date of the donor restricted endowment funds absent explicit donor stipulations to the contrary. As a result of this interpretation, the [organization] classifies as permanently restricted net assets (a) the original value of gifts donated to the permanent endowment, (b) the original value of subsequent gifts to the permanent endowment, and (c) accumulations to the permanent endowment made in accordance with the direction of the applicable donor gift instrument at the time the accumulation is added to the fund. The remaining portion of the donor-restricted endowment fund that is not classified as permanently restricted net assets, is classified as temporarily restricted net assets.