Suggested Footnote Disclosure for Information Reported on the Statement of Revenues, Expenses, and Changes in Net Assets

POSITION PAPER PREPARED BY THE NACUBO ACCOUNTING PRINCIPLES COUNCIL

The position paper that follows was approved in December, 2000, by the NACUBO Accounting Principles Council. The paper represents preferred industry practice, and in the absence of any guidance from the Financial Accounting Standards Board (FASB), the Governmental Accounting Standards Board (GASB), or the American Institute of Certified Public Accountants (AICPA), this document should be followed by all higher education institutions.

Purpose: This document addresses NACUBO’s position pertaining to a footnote disclosure to display natural classification information for those public colleges and universities that display functional classifications on the face of their Statement of Revenues, Expenses, and Changes in Net Assets. In its review of this topic, NACUBO does not prescribes that public not-for-profit higher education institutions present their expenses on the face of their financial statements using either the functional classifications or the natural classifications. NACUBO recognizes that by institutional choice, or primary government mandate, public higher education institutions may report either functional or natural classifications on the face of their Statement of Revenues, Expenses, and Changes in Net Assets. NACUBO also recognizes, however, that traditional functional classification information has value to the industry for multiple comparative and reporting purposes among the NACUBO membership. To preclude the loss of information, this Advisory Report suggests a footnote disclosure be included in the financial statements to display a matrix of expenses by functional and natural classes.

Applicability: This position paper applies to all public higher education institutions reporting under guidance provided by Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments, as amended by GASB Statement No. 35, Basic Financial Statements—and Management’s Discussion and Analysis—for Public Colleges and Universities.

Scope: Given the latitude provided by Governmental Accounting Standards Board (GASB) Statement No. 34, Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments, as amended by GASB Statement No. 35, Basic Financial Statements—and Management’s Discussion and Analysis—for Public Colleges and Universities, public not-for-profit higher education institutions are authorized to provide an analysis of expenses by either functional designation or natural classification (object class).
**Significance:** Reporting an organization’s expenses by natural classification can be useful to the readers of the financial statements. However, presenting expenses by natural classification on the face of the financial statements would represent a major change to current financial statement composition and presentation. A natural classification presentation could improve comparability between institutions when considering the allocation of costs in the functional classifications. However, it is recognized that, without guidance from NACUBO, the functional classification data may be lost to the industry for those institutions that adopt the natural classification model, or natural class data is not available for those institutions that report their expenses by functional classifications. NACUBO believes that, at this time, functional classification data should not be lost to the industry when an institution chooses to report its expenses by natural classes. NACUBO also believes that expense information by natural class enables greater articulation with the statement of cash flows and thus serves an additional use to the myriad purposes that users now have for functional classification data. At some point in the future this position might be reviewed and possibly modified and reversed. Until such time, NACUBO suggests the presentation of an expense matrix footnote disclosure to the financial statements that compares the functional to natural classifications that details the expenses presented on the face of their Statement of Revenues, Expenses, and Changes in Net Assets.

**Effective Date:** The effective date of this suggested disclosure for public higher education institutions will coincide with the institution’s implementation date under GASB Statement 34, Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments, as amended by GASB Statement No. 35, Basic Financial Statements—and Management’s Discussion and Analysis—for Public Colleges and Universities.

---

**Background and Suggested Disclosure Format**

The use of natural classifications has been supported, in the past, by the *American Institute of Certified Public Accountants (AICPA) Industry Audit Guide, Audits of Colleges and Universities, With Conforming Changes as of May 1, 1993, Statement of Position 74.8*, in that: “Thus, expenditures and transfers may be classified in terms of programs, functions, organization units, projects, and object classes.”¹ The Financial Accounting Standards Board (FASB) has also supported natural classification presentation. In the Statement of Financial Accounting Standards No. 117, *Financial Statements of Not-for-Profit Organizations*, it is stated: “The Board concluded that information about an organization’s expenses by function may be meaningfully communicated either in a statement of activities or in notes to financial statements”; and, “The Board decided not to require not-for-profit organizations to provide an analysis of expenses by natural classification. . . . The Board agrees that information about expenses by natural classification often is useful and encourages organizations to provide that information. However, it also believes that information about expenses

---

² FASB SFAS No. 117, ¶57.
by natural classification may be essential in understanding the service efforts of all not-for-profit organizations or in assessing the ability of all organizations to continue to provide services.\(^3\) Currently, the Governmental Accounting Standards Board’s Statement No. 35, *Basic Financial Statements—and Management’s Discussion and Analysis—for Public Colleges and Universities* recognizes natural classification presentations in the illustrative financial statements provided in Appendix D. The text box included in Appendix D’s Statement of Revenues, Expenses, and Changes in Net Assets states: “Operating expense may be displayed using either object [natural] or functional classifications.”\(^4\)

Given that public not-for-profit higher education institutions have the choice to report expenses by functional or natural classification, it is encouraged that when the face of the Statement of Revenues, Expenses, and Changes in Net Assets contains expenses by one perspective [e.g., natural (object) classifications], the other perspective [e.g., functional classifications] should be included in the footnotes. It is suggested that the natural classifications be categorized the same as those categories presented as direct cash outflows in the statement of cash flows. For example, the following natural classes could be used for reporting the direct cash outflows.

- Salaries and wages
- Benefits
- Scholarships and fellowships
- Utilities
- Supplies and other services
- Depreciation

In some instances, institutions may wish to present additional sub-classification data to provide further details of the natural expense classes.

It is encouraged that the footnote disclosure to the financial statements include a matrix that compares the functional information with the natural class information. The functional classifications should include, as appropriate, the following.

**Functional Program Classifications**
- Instruction
- Research
- Public Service
- Academic Support
- Student Services
- Institutional Support
- Operations and Maintenance of Plant
- Auxiliary, Auxiliary-Other and Other Self-supporting Enterprises
- Hospitals
- Independent Operations

---

\(^3\) FASB SFAS No. 117, ¶62.

\(^4\) GASBS 35, Appendix D.
Depreciation expenses may be allocated to the various functional program classifications, included as part of the operations and maintenance of plant, or it can be identified as a separate program classification.

Should institutions, for materiality or information reporting purposes, desire to further breakout a functional classification to create a more readable footnote, such breakouts should be displayed under the major classification. Should an institution not have a major functional classification, such as Hospitals, it should not be included.

Materiality should be considered for any natural, or functional, classification. Should the amount associated with a classification not be material, and consolidation with another classification not be misleading, the amounts may be consolidated with an appropriate material classified amount. For example, if an institution had a non-material amount of Public Service, and the amount recorded represents primarily instructional activity, Public Service could be consolidated with Instruction and not listed separately.

A footnote disclosure to a Statement of Revenues, Expenses, and Changes in Net Assets is attached for illustrative purposes (ATTACHMENT A).
### NATURAL CLASSIFICATIONS WITH FUNCTIONAL CLASSIFICATIONS

<table>
<thead>
<tr>
<th></th>
<th>Compensation</th>
<th>Scholarships and Fellowships</th>
<th>Utilities</th>
<th>Supplies and Other Services</th>
<th>Depreciation</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Faculty</td>
<td>Exempt Staff</td>
<td>Nonexempt Wages</td>
<td>Benefits</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Instruction</td>
<td>$24,895,472</td>
<td>$1,294,743</td>
<td>$464,842</td>
<td>$5,876,423</td>
<td>$1,760,615</td>
<td>$681,548</td>
</tr>
<tr>
<td>Research</td>
<td>$9,656,498</td>
<td>$1,576,988</td>
<td>$1,640,164</td>
<td>$2,829,954</td>
<td>$287,281</td>
<td>$1,533,431</td>
</tr>
<tr>
<td>Public Service</td>
<td>$277,529</td>
<td>$42,306</td>
<td>$23,744</td>
<td>$99,206</td>
<td>$7,022</td>
<td>$17,970</td>
</tr>
<tr>
<td>Academic Support</td>
<td>$4,285,086</td>
<td>$202,027</td>
<td>$1,733,832</td>
<td>$37,325</td>
<td>$3,276,558</td>
<td>$574,735</td>
</tr>
<tr>
<td>Student Services</td>
<td>$1,974,634</td>
<td>$246,922</td>
<td>$749,406</td>
<td>$50,939</td>
<td>$402,130</td>
<td>$410,525</td>
</tr>
<tr>
<td>Institutional Support</td>
<td>$7,334,354</td>
<td>$628,528</td>
<td>$2,349,651</td>
<td>$189,204</td>
<td>$402,716</td>
<td>$985,259</td>
</tr>
<tr>
<td>Operations and</td>
<td>$510,453</td>
<td>$1,167,267</td>
<td>$688,622</td>
<td>$36,385</td>
<td>$4,740,553</td>
<td>$2,134,728</td>
</tr>
<tr>
<td>Maintenance of Plant</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$9,278,008</td>
</tr>
<tr>
<td>Depreciation</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$3,369,585</td>
</tr>
<tr>
<td>Student Aid</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$495,683</td>
</tr>
<tr>
<td>Other Expenditures</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td>$28,417</td>
</tr>
<tr>
<td>Auxiliary Enterprises</td>
<td>$12,579,112</td>
<td>$1,540,288</td>
<td>$4,189,465</td>
<td>$894,920</td>
<td>$5,408,596</td>
<td>$3,778,510</td>
</tr>
<tr>
<td>Total</td>
<td>$34,829,499</td>
<td>$29,597,676</td>
<td>$5,913,762</td>
<td>$18,486,559</td>
<td>$3,809,374</td>
<td>$12,451,064</td>
</tr>
</tbody>
</table>

Advisory Report 2000-08final edited.doc