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Liquidity Takes the Spotlight at Institutions of Higher Education

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As many colleges, universities and their related foundations gear up to implement *Accounting Standards Update (ASU) 2016-14 – Not-for-Profit Entities (Topic 958): Presentation of Financial Statements of Not-for-Profit Entities,* one thing has become clear: liquidity is now a significant new disclosure which deserves important consideration.

As many early adopters of the ASU have discovered, restrictions from both external and internal sources will affect the entity's presentation of liquidity in the financial statement. Institutions of higher education will need to include in their financial statements disclosures that provide more relevant information to donors, grantors, creditors and other users about resources available.

Financial Statement Considerations and Disclosures

Private colleges, universities and foundations of state colleges that follow FASB rules will now be required to disclose restrictions that affect the availability of liquid resources in their financial statements. In order to provide more transparency, the guidance includes requirements aimed at improving the ability of financial statement users to assess liquidity and availability of financial resources by requiring both quantitative and qualitative information about the availability of resources and how the institution manages those resources to meet cash needs for general expenditures within one year of the balance sheet date.

These requirements are further explained below:

- Quantitative disclosure requirements will communicate the availability of financial assets at the balance sheet date to meet cash needs for general expenditures over the next year. Institutions will need to identify all financial assets and any limitations on their use in the next twelve months. The ASU clarifies that the nature of an asset is not the only factor that affects its availability. There are external limits, such as donor restrictions, granting agencies requirements, laws and contracts as well as restrictions related to assets such as alternative investments with lock-up provisions, restrictions for endowments or capital projects, annuity reserves required by state law, or restricted cash held as a minimum balance threshold for debt, that need to be considered as well. In addition, internal limits imposed by the governing board on quasi-endowment funds also need to be addressed. Financial liabilities will need to be identified to compare against available assets to gain an understanding of future liquidity needs.

- Qualitative disclosure requirements include explaining how liquid resources are managed to meet cash needs for general expenditures within one year of the balance sheet date. Institutions might decide to develop a liquidity management plan to determine how liquid assets are managed Items to consider include strategies for addressing institution-wide risks, access to lines of credit or long-term financing, liquidity reserves established, and the time horizon used to manage liquidity. Liquidity reserves are not required under GAAP; however, if the decision to establish a liquidity reserve is made and approved by the board, disclosure is required under the new standards.

Summary

The disclosures related to liquidity should particularly assist creditors, donors, and other financial statement users in assessing the near-term availability of and requirements for cash. In prior practice, resources may have appeared to be available for short-term cash needs, but in fact may not have been available because of limitations on their use. Also, resources invested as quasi-endowment funds may appear to have been unavailable for near-term cash needs, but in fact can generally be liquidated by action of the governing board if cash needs arise. Thus, the new liquidity disclosures will provide significant new insight into an institution's available assets.

Contact Us

If you have any questions conerning implementation considerations required under ASU 2016-14 regarding liquidity disclosures or other prvisions, please contact your PKF O'Connor Davies engagement partner or either of the individuals listed below:

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