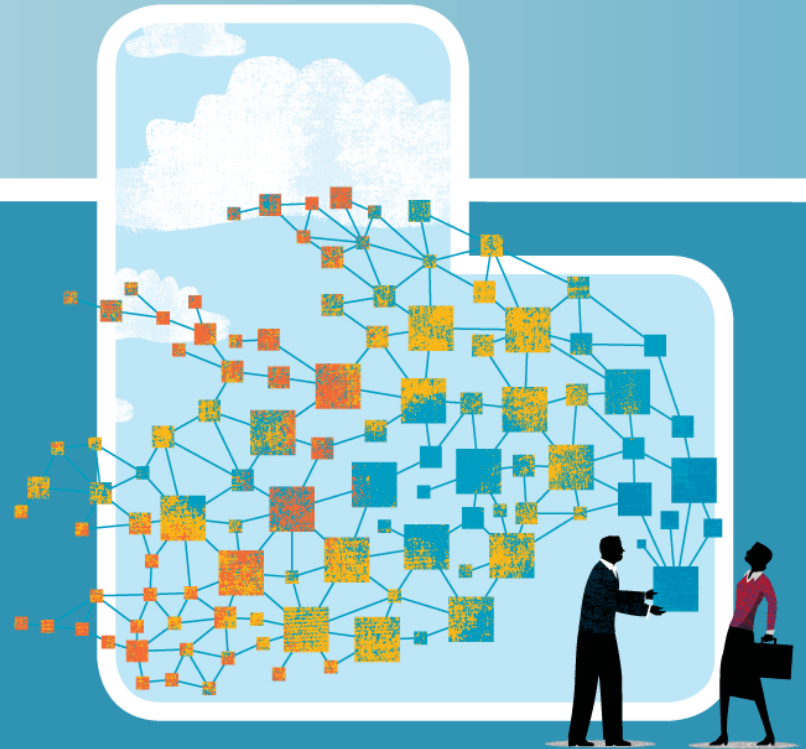


# ACCOUNTING AND FINANCIAL REPORTING UPDATE

HFMA Regional 11 Symposium  
January 2011



**MOSS-ADAMS** LLP  
Certified Public Accountants | Business Consultants

*Acumen. Agility. Answers.*

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# TODAY'S PRESENTERS



## **Brian Conner, CPA**

Assurance Partner with Moss Adams LLP  
Healthcare Industry Group



## **Erica Forhan, CPA**

Assurance Partner with Moss Adams LLP  
Professional Practice Group  
Focus on Healthcare, Not-for-Profit and Government entities

# AGENDA

- Healthcare EITF's
- FASB Activities
  - Fair value update
  - Subsequent events disclosure
  - Business combinations – not-for-profit organizations
- Other Healthcare accounting considerations
- FASB Convergence Projects
- GASB Activities
  - GASB Codification
  - Intangible assets
  - Derivatives and hedging
- California Hospital Fee update



# Healthcare: Emerging Issues

# HEALTHCARE EITF'S (AND ASU'S)

- Numerous healthcare specific standards recently
  - Revision of Audit and Accounting Guide (codification)
  - Elimination of industry specific “carve-outs”
- Multiple issues evaluated
  - Charity care
  - Revenue recognition (bad debt expense)
  - Claims obligations (insurance recoveries)
  - Long-lived asset contributions
  - Discounting of actuarially determined liabilities
  - Legal costs in medical malpractice
- A few issues addressed
  - Charity care
  - Revenue recognition (bad debt expense)
  - Claims obligations (insurance recoveries)

# MEASURING CHARITY CARE FOR DISCLOSURE (ASU 2010-23)

- **Issue:** Healthcare organizations disclose services to qualified charity patients in the notes to the financials statements.
  - Diversity exists on the basis for these disclosures
  - Update requires cost (both direct and indirect)
    - Disclose method used to identify or determine costs
    - Disclose funds received to offset or subsidize charity care
  - Effective for fiscal years beginning after December 15, 2010
    - Retrospective application required
    - Early application permitted

# DISCLOSURE ABOUT NET REVENUE AND ALLOWANCE FOR DOUBTFUL ACCOUNTS (EITF ISSUE NO. 09-H)

- **Issue:** Healthcare organizations may recognize revenue for which the ultimate collection is not reasonably assured at the time services are rendered.
  - Classification will ultimately be addressed in step process
  - Proposed Update requires additional disclosure by major payor source:
    - Policy for assessing collectibility in the timing and amount of bad debt expense recognized
    - Tabular reconciliation of the activity in the allowance for doubtful accounts for the period
  - Major payor sources of revenue is entity-specific
  - Proposed effective for fiscal years beginning after December 15, 2010
    - Retrospective application required
    - Early application permitted

# PRESENTATION OF INSURANCE CLAIMS AND RELATED INSURANCE RECOVERIES (ASU 2010-24)

- **Issue:** Healthcare organizations have significant exposure to loss from malpractice and other claims
  - Healthcare organizations currently use “transfer of risk” model with net presentation
    - Other industries accrue claims liabilities and insurance recoveries on gross basis
  - Update requires gross presentation of claims liabilities and insurance recovery receivables
    - Liability should be determined without consideration of insurance recoveries
    - Disclose funds received to offset or subsidize charity care
  - Effective for fiscal years beginning after December 15, 2010
    - Retrospective application permitted (cumulative-effect)
    - Early application permitted



# FASB Activities

# FAIR VALUE UPDATE

- Changes in the last year related to fair value accounting and reporting:
  - Update No. 2009–05: Measuring Liabilities at Fair Value
  - Update No. 2009–12: Investments in Certain Entities That Calculate Net Asset Value per Share
  - Update No. 2010–06: Improving Disclosures about Fair Value Measurements
  - Proposed Update: Amendments for Disclosure Requirements in U.S. GAAP and IFRSs

# FAIR VALUE UPDATE

- Update No. 2009–05: Measuring Liabilities at Fair Value
  - Clarification of fair value measurements for liabilities
- Update No. 2009–12: Investments in Certain Entities That Calculate Net Asset Value per Share
  - Guidance on using net asset value to estimate fair value for alternative investments, hierarchy classification and certain disclosure requirements
  - Applicable for reporting periods **ending after December 15, 2010**
  - NAV = fair value if 1) investment company reporting used and 2) calculated at the measurement date
  - Redeemable at measurement date = Level 2; never redeemable = Level 3, redeemable in future = Level 2 or Level 3

# FAIR VALUE UPDATE

- Additional disclosure example for alternative investments:

	<u>Fair Value (in millions)</u>	<u>Unfunded Commitments</u>	<u>Redemption Frequency (If Currently Eligible)</u>	<u>Redemption Notice Period</u>
<u>Equity long/short hedge funds</u> <sup>(a)</sup>	\$ 55		quarterly	30–60 days
<u>Event driven hedge funds</u> <sup>(b)</sup>	45		quarterly, annually	30–60 days
<u>Global opportunities hedge funds</u> <sup>(c)</sup>	35		quarterly	30–45 days
<u>Multi-strategy hedge funds</u> <sup>(d)</sup>	40		quarterly	30–60 days
<u>Real estate funds</u> <sup>(e)</sup>	47	\$ 20		
<u>Private equity funds—international</u> <sup>(f)</sup>	43	15		
<u>Total</u>	<u>\$ 265</u>	<u>\$ 35</u>		

# FAIR VALUE UPDATE

- Update No. 2010-06: Improving Disclosures about Fair Value Measurements
  - Expanded disclosure requirements for fair value measurements
    - Transfers in and out of Levels 1 and 2
    - Level 3 activity disaggregation
    - Class of assets and liabilities disaggregation
    - Valuation techniques and inputs for recurring and non-recurring measurements in Level 2 and Level 3
    - Conforming amendments to employer disclosures for postretirement benefit plan assets (effective December 31, 2009)
    - Effective for periods **beginning after December 31, 2009** except for Level 3 disaggregation
    - Effective for periods **beginning after December 31, 2010** for Level 3 disaggregation

# FAIR VALUE UPDATE

- Proposed ASU ( 6/29/2010)
  - Redefine certain terms used in fair value measurements
  - Clarifies measurement of fair value for certain instruments measured within a portfolio
  - Blockage factor use clarification
  - Additional disclosure requirements:
    - Measurement uncertainty for Level 3 category (quantify effect)
    - Use of an asset that differs from highest and best
    - Level categorization applicable for financial instrument disclosures (old FAS 107, new Topic 825)

# SUBSEQUENT EVENTS (TOPIC 855)

- ASU No. 2010-09 amends requirement to disclose date through which subsequent events are evaluated:
  - Eliminates “widely distributed” qualitative evaluation for issued vs. available to be issued
  - Explicitly scopes in “conduit debt obligors” to evaluate subsequent events through date financial statements are issued
  - Financial statements are issued when they are widely distributed to shareholders and other financial statement users
    - Filed with clearinghouse
    - Posted to website
    - Filed with Trustee
  - Not applicable to GASB reporters (GASB 56)
  - Effective for interim and annual periods ending after June 15, 2010

# NOT-FOR-PROFIT BUSINESS COMBINATIONS (ASC 958-805)

- Scope:
  - Applies to
    - Transactions or other events that result in a not-for-profit entity initially recognizing another NFP entity, business, or nonprofit activity in its financial statements
  - Does not apply to
    - Joint venture formation
    - Acquisition of assets not constituting a business or nonprofit activity
    - A combination between not-for-profit entities, businesses, or nonprofit activities under common control
    - Situations where a NFP obtains control but does not consolidate the entity

# NOT-FOR-PROFIT BUSINESS COMBINATIONS (ASC 958-805)

- Key Provisions:
  - Mergers are accounted for using the Carryover Method
    - *Merger – combination where 2 or more NFP's cede control and form new NFP*
  - Acquisitions are accounted for using the Acquisition Method
    - *Acquisition – combination where NFP obtains control of another NFP*

# NOT-FOR-PROFIT BUSINESS COMBINATIONS (ASC 958-805)

- Carryover Method – the combined entity carries forward the assets and liabilities of the individual combining entities at their prior book values
  - Similar to old pooling method
  - Combination date on effective date of merger
- Acquisition Method – applies guidance very similar to current for-profit business combination accounting (recording asset and liabilities at fair values) with some key differences
  - Goodwill is NOT recognized if the acquirer expects the operations of the acquiree to be predominantly supported by contributions and returns on investments
  - If otherwise (i.e. the acquiree is businesslike through charging fees to customers), recognize goodwill.
- Goodwill subsequently measured based on ASC Topic 350
  - No amortization; annual evaluation of impairment

# NOT-FOR-PROFIT BUSINESS COMBINATIONS (ASC 958-805)

- Important considerations
  - Acquisition method prevalent; merger accounting rare
  - Non-controlling interest guidance scoped in for NFP's
    - “Minority interest” reported in net assets
  - Transition guidance requires evaluation of existing goodwill at beginning of period of implementation
    - An NFP that is predominantly supported by contributions and returns on investments shall write off previously recognized goodwill by a separate charge in the statement of activities for the effect of the accounting change.
    - An NFP that is not predominantly supported by contributions and returns on investments shall subject previously recognized goodwill to impairment evaluation

# NOT-FOR-PROFIT BUSINESS COMBINATIONS (ASC 958-805)

- Effective Dates
  - Prospectively for mergers and acquisitions in periods beginning on or after December 15, 2009
    - For June 30 year ends, effective for acquisitions/mergers in FY 2011
    - For calendar year ends, effective in FY 2010
  - Early application prohibited

# OTHER HEALTHCARE CONSIDERATIONS

- New Audit and Accounting Guide
- Subjective acceleration clauses



# FASB Convergence Projects

# FASB/IASB CONVERGENCE PLAN

Project	Exposure Draft	Final Statement
Financial Instruments*	May 2010	Q2 2011
FV Measurements	June 2010	Q1 2011
Revenue Recognition*	June 2010	Q2 2011
Leases*	August 2010	Q2 2011
Insurance Contracts	September 2010 (discussion paper)	TBD
Consolidations: Voting Interests, Investment Companies	Roundtable in Q4 2010	TBD
Financial Statement presentation	TBD	TBD
Financial Instruments With Characteristics of Equity	TBD	TBD

# FASB/IASB CONVERGENCE

- Financial Instruments Project: simplify, improve and converge the accounting and reporting of financial instruments
  - Classification and measurement
  - Impairment accounting
  - Hedge accounting

# FASB/IASB CONVERGENCE: FINANCIAL INSTRUMENTS PROJECT

- Important for all not-for-profits:
  - Scope: all financial instruments, with certain exceptions
    - Contributions receivable, contributions payable by NFPs
  - On balance sheet at FV, except for:
    - ST receivables and payables (approx. 1 year or less)
    - Financial liabilities with an accounting mismatch (specific criteria to be met, based on contractual linkage and/or asset composition)
  - Areas of most significant impact: loans, some liabilities
    - 4-year deferral on loans receivable (and core deposits) for nonpublic entities with less than \$1B in assets

# FASB/IASB CONVERGENCE: FINANCIAL INSTRUMENTS PROJECT

- Important for healthcare not-for-profits:
  - FV/OCI option for assets and liabilities held for receipt or payment of contractual cash flows (e.g., loans and debt securities, financial liabilities)
  - Clarifications/improvements to incurred loss model for asset impairments (ASC 310/FAS 114)
    - Removes “probable” threshold for loss recognition
    - Focus on past events and current conditions rather than forecasting future conditions (expected loss model)
    - Consistent now for loans and debt securities (no more OTTI)

# FASB/IASB CONVERGENCE: FINANCIAL INSTRUMENTS PROJECT

- Important for healthcare not-for-profits (cont):
  - Simplifications/ improvements to hedge accounting
    - More qualitative, with lower effectiveness threshold (“reasonably effective” rate than “highly effective”)
  - Equity method accounting:
    - Must not only have significant influence, but the investments must be related to the investor’s consolidated business

# FASB/IASB CONVERGENCE: REVENUE RECOGNITION PROJECT

- Revenue Recognition Model:
  1. Identify the contact(s) with a customer
  2. Identify the separate performance obligations in the contract
  3. Determine the transaction price (credit risk affects measurement, not recognition)
  4. Allocate the transaction price to the separate performance obligations
  5. Recognize revenue when the entity satisfies each performance obligation

# FASB/IASB CONVERGENCE

- Leases Project – Issues
  - Off-balance sheet presentation of leased assets and related financing
  - Bright-line distinction between on- and off-balance sheet; structuring opportunities
  - Very detailed rules

# FASB/IASB CONVERGENCE: LEASES PROJECT

- Current – evaluate the transfer of underlying asset (“all of nothing”)
- Proposed – account for the value of the rights and obligations conveyed through the lease contract (“to the extent of”)
- Present value of cash flows
  - Estimate lease term, considering likelihood of renewal (must be more likely than not)
  - Discount lease payments and contingent rentals using probability-weighted cash flows
  - Exception for ST leases (simple accrual, no discounting)

# FASB/IASB CONVERGENCE: LEASES PROJECT

- Lessees:
  - Asset: right to use the leased item for the lease term
  - Liability: obligation for lease payments (at PV)
  - Expense: interest expense and amortization expenses in lieu of rent expense
- Lessors:
  - Asset: right to receive lease payments (at PV)
  - Liability: obligation to make leased item available for use during the lease term
  - Revenue: recognize as the obligation is met



# GASB Activities

# EVOLUTION OF GASB STANDARDS

## Statement No. 20 (1993)

- Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities that use Proprietary Fund Accounting

## Statement No. 34 (1999)

- Basic Financial Statements—and MD&A—for State and Local Governments

## Statement No. 55 (2009)

- The Hierarchy of GAAP for State and Local Governments

## Statement No. 56 (2009)

- Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards

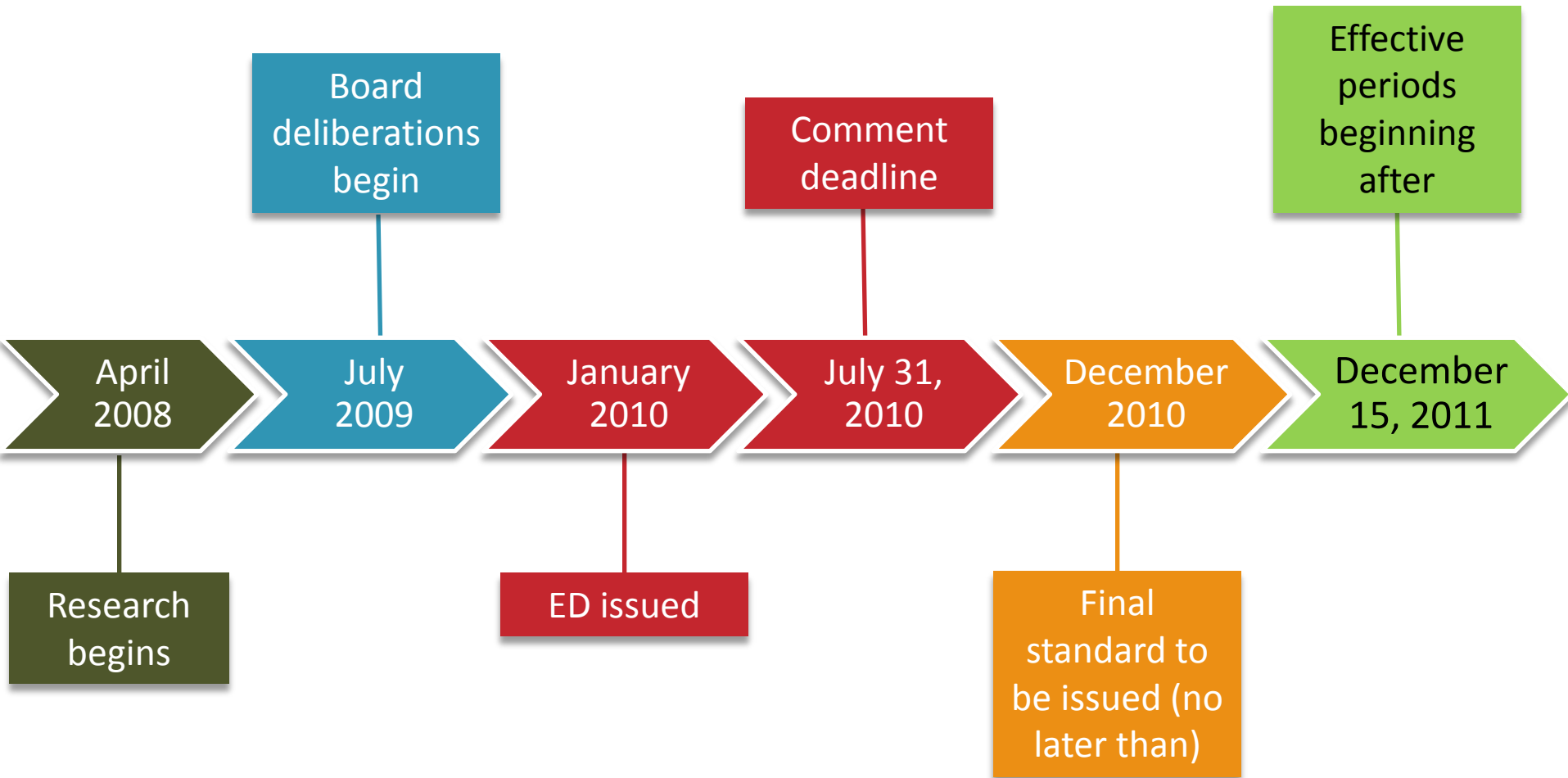
## Exposure Draft (2010)

- Pre-November 30, 1989 AICPA and FASB literature (2010)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Project Overview:
  - With FASB Codification, original pronouncements are nonauthoritative
  - GASB 34 par. 17 requires application of pre-November 30, 1989 FASB pronouncements unless they conflict with or contradict GASB pronouncements
  - Goal: Specifically identify applicable provisions in FASB Statements and Interpretations, APB Opinions, ARBs, and AICPA Accounting Interpretations and incorporate into GASB literature

# PROJECT TIMELINE



# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Categories:
  - Conflict with or contradict GASB Standards (excluded)
  - Not applicable to governments (excluded)
  - Rarely applicable (excluded)
  - Applicable to governments (included and “governmentalized”)
  - Will be addressed in GASB projects (applicable, but excluded)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Accounting Research Bulletins
  - ARB 43 – Source of current standards (1939-1953)
    - Current assets, depreciation, inventory
  - ARB 44-51
    - Only ARB 45 is applicable (long-term construction contracts)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- AICPA Accounting Principles Board (1962-1973)
  - 31 Opinions issued (11 superseded by pre-November 30, 1989 literature)
  - Key Opinions
    - APB 20 – Accounting changes
    - APB 21 – Interest on receivables and payables
    - APB 22 – Disclosure of accounting policies
    - APB 29 – Nonmonetary transactions

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Financial Accounting Standards Board (From 1973)
  - 102 Statements issued before November 30, 1989 (19 superseded by pre-November 30, 1989 literature)
  - Many Statements rarely, if ever, apply to governments

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Key FASB Statements
  - FASB 13, as amended - leases
  - FASB 5 – Contingencies
    - NCGA Statement 4 and GASB 10 do not cover completely
  - FASB 57 – Related party transactions
  - FASB 6 – Classifying ST obligations
  - FASB 71 – Regulated industries
  - FASB 34 and 62 – Capitalization of interest

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- FASB Interpretations
  - 38 Interpretations issued before November 30, 1989 (10 superseded by pre-November 30, 1989 literature)
  - Key Interpretations
    - Interpretation 14 – reasonable estimates when applying FASB 5
    - Lease interpretations

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Tentative Decision: Statement 20 would be superseded
  - All applicable pre-11/30/89 standards would be contained in the GASB's codification
  - All potentially applicable post-11/30/89 non-GASB standards would be “other accounting literature”

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Tentative Decision: Guidance on 29 topics would be established in the GASB Codification
  - Capitalization of interest cost (FAS 34)
  - Revenue recognition for exchange transactions
  - Revenue recognition when right of return exists
  - Statement of net asset classifications (AR43, APB 12, FAS 6)
  - Special and extraordinary items (APB 30)
  - Comparative financial statements (ARB 43)
  - Related parties (FAS 57)
  - Prior-period adjustments (FAS 16, APB 9)
  - Accounting changes & error corrections (APB 20, FIN 20)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Topics in the GASB Codification(cont.):
  - Disclosure of accounting policies
  - Contingencies (FAS 5, FIN 14)
  - Construction-type contracts—long-term
  - Extinguishments of debt (APB 26, FAS 76)
  - Troubled debt restructuring (FAS 15)
  - Foreign currency transactions
  - Interest costs - Imputation
  - Inventory (ARB 43)
  - Investments in common stock
  - Leases (FAS 13, 22, 98; FIN 23, 26, 27)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Topics in the GASB Codification(cont.):
  - Nonmonetary transactions
  - Sales of real estate (FAS 66)
  - Real estate projects (FAS 67)
  - Research and development arrangements (FAS 68)
  - Broadcasters (FAS 63)
  - Cable television systems (FAS 51)
  - Insurance enterprises (FAS 60)
  - Lending activities (FAS 91)
  - Mortgage banking activities (FAS 65)
  - Regulated operations (FAS 71, 90, 101)

# CODIFICATION OF PRE-NOVEMBER 30, 1989 FASB PRONOUNCEMENTS

- Expected to be effective for financial statements for periods beginning after December 15, 2011
- Earlier application encouraged
- Apply accounting changes retroactively by restating financial statements, if practical, for all periods presented

# GASB STATEMENT NO. 51: INTANGIBLE ASSETS

- An intangible asset is an assets that possesses all of the following characteristics:
  - Lack of physical substance
  - Nonfinancial nature
  - Initial useful life beyond a single reporting period
- Scope exception
  - Intangible assets acquired or created primarily for directly obtaining income or profit
  - Capital leases
  - Goodwill from a combination transaction

# GASB STATEMENT NO. 51: INTANGIBLE ASSETS

- Classify as capital assets
  - Apply all existing authoritative guidance related to capital assets to intangible assets
  - Because they are considered capital assets, not reported as assets in governmental fund financial statements
- Measure like a capital asset
  - Historical cost
  - If donated, estimated fair value at date of donation

# GASB STATEMENT NO. 51: INTANGIBLE ASSETS

- Examples
  - Bundled rights
  - Internally generated computer software
  - Right-of-way easement

# GASB STATEMENT NO. 51: INTANGIBLE ASSETS

- Amortization
  - Generally, apply existing guidance for capital assets depreciation to amortize intangible assets
  - Exception for intangible assets with indefinite useful lives:
    - No factors currently exist that limit the useful life of the asset
    - Estimating a useful life does not mean indefinite useful life
  - Intangible assets with indefinite useful lives should not be amortized

# GASB STATEMENT NO. 51: INTANGIBLE ASSETS

- Effective date: Fiscal periods beginning after June 15, 2009 (earlier application encouraged)
- Generally, apply provisions retroactively
- Exceptions for retroactively reporting intangible assets:
  - Permitted but not required for internally generated intangible assets and intangible assets with indefinite useful lives at transition
  - Required for all other intangible assets acquired in fiscal years ended after June 30, 1980 by phase 1 or 2 governments
  - Encouraged but not required for all other intangible assets of phase 3 governments

# GASB STATEMENT NO. 53: DERIVATIVE INSTRUMENTS

- A derivative instrument has:
  - One or more reference rates (underlyings) and one or more notional amounts (settlement factors)
  - Leverage
  - Net settlement

# GASB STATEMENT NO. 53: DERIVATIVE INSTRUMENTS

- Accounting Guidance - Fair value with hedge accounting
  - Derivative instruments would be measured on the statement of net assets at fair value
  - Fair value changes would be reported on the “change statement” as investment income
  - Exception: HEDGES
    - Changes in fair value of derivative instruments would be reported on the balance sheet as deferrals— either deferred charges or deferred credits
    - Swap asset, deferred inflows
    - Swap liability, deferred outflows

# GASB STATEMENT NO. 53: DERIVATIVE INSTRUMENTS

- Implementation issues
  - Normal purchases and normal sales
  - Hybrid instruments
  - Assessing effectiveness



# California Hospital Fee Update

# CALIFORNIA HOSPITAL FEE

- California Quality Assurance Fee Act:
  - QA Fees and Supplemental Revenues are operating expenses and net patient service revenue (reductions in Medi-Cal contractals), respectively
  - Retrospectively approved quarters are recorded at the time the legislation is approved by CMS
  - Prospectively approved quarters are recognized as the quarter elapses
  - Managed care revenue recorded when estimable and measurable (based on timing of receipt)
  - Direct Grant Revenue to designated public hospitals is non-operating for GASB reporters
  - California Health Foundation and Trust agreements depends on the nature of the individually executed agreements



Questions?