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Proposed statement of position : report on a financial feasibility study ;Report on a financial feasibility study; Exposure draft (American Institute of Certified Public Accountants), 1982, Feb. 15

American Institute of Certified Public Accountants. Financial Forecasts and Projections Task Force

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EXPOSURE DRAFT

PROPOSED STATEMENT OF POSITION

REPORT ON A FINANCIAL FEASIBILITY STUDY

FEBRUARY 15, 1982

Prepared by the AICPA Financial Forecasts and
Projections Task Force for comment from persons interested
in financial feasibility studies

Comments should be received by May 15, 1982, and addressed to the
AICPA Auditing Standards Division, File 2660F
AICPA, 1211 Avenue of the Americas, New York, NY 10036

M815130

SUMMARY

This proposed Statement of Position illustrates an expanded form of report that can be used for financial feasibility studies when the accountant has applied procedures that exceed those that would pertain solely to a review of a financial forecast. The report includes a description of the scope of the feasibility study and a statement of conclusions that result from the study.



American Institute of Certified Public Accountants

1211 Avenue of the Americas, New York, New York 10036 (212) 575-6200

February 15, 1982

Accompanying this letter is an exposure draft of a proposed Statement of Position entitled Report on a Financial Feasibility Study. It illustrates the form of report an independent accountant might issue on a financial feasibility study.

In October 1980, the American Institute of Certified Public Accountants (AICPA) published the Guide for a Review of a Financial Forecast (the Guide) setting forth the procedures a CPA should follow in reviewing a financial forecast and the form of report to be issued. The Guide is broadly applicable to forecasts, including those contained in financial feasibility studies. The Guide recognized that independent accountants may, in conjunction with a review of a forecast, assist management with various aspects of preparing the forecast. The Guide also recognized that the independent accountant could expand his report to discuss such extended services.

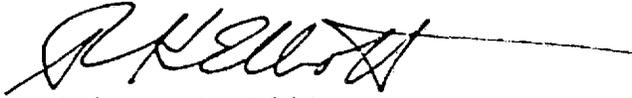
Since publication of the Guide, individuals and groups who prepare and use financial feasibility studies have indicated that guidance is needed as to the form and content of such an expanded report for an engagement to conduct a financial feasibility study. In studying the issue the task force obtained the opinions of parties interested in financial feasibility studies (e.g. health care authorities, attorneys, etc.). The illustrative report included in this exposure draft is the culmination of that process. We believe that greater uniformity in reporting on such engagements will result in the reports being more easily understood.

We believe the illustrative report in this exposure draft is responsive to the needs of those interested in financial feasibility studies. However, we want to be sure we have considered your views and those of other interested parties. Therefore we solicit your comments and invite you to call the draft to the attention of other reviewers, issuers, users, or regulators of forecast data. Consideration of responses will be helped if the comments refer to the specific paragraph numbers and include supporting reasons for any suggestions or comments. Responses should be addressed to the AICPA Auditing Standards Division, File 2660F in time to be received by May 15, 1982.

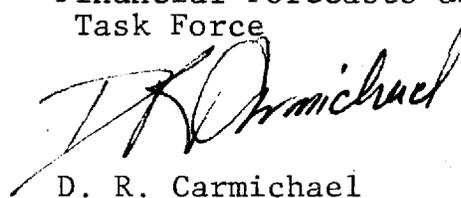
Written comments on the exposure draft will become part of the public record of the AICPA Auditing Standards Division and will be

available for public inspection at the offices of the American Institute of Certified Public Accountants after June 15, 1982, for one year.

Sincerely,

A handwritten signature in black ink, appearing to read "R. K. Elliott", with a long horizontal flourish extending to the right.

Robert K. Elliott
Chairman
Financial Forecasts and Projections
Task Force

A handwritten signature in black ink, appearing to read "D. R. Carmichael", with a long horizontal flourish extending to the right.

D. R. Carmichael
Vice President, Auditing

PROPOSED STATEMENT OF POSITION

Report on a Financial Feasibility Study

(This Statement of Position should be read and applied in conjunction with the Guide for a Review of a Financial Forecast.)

1. In 1980, the AICPA issued the Guide for a Review of a Financial Forecast (the Guide). Although the Guide was not intended to cover all aspects of performing feasibility studies that include financial forecasts, it does apply to the review of the forecast and report thereon.
2. Preparation of a financial feasibility study often includes such elements as the following:
 - analyzing and evaluating demand
 - assisting management to identify key factors on which future financial results will depend
 - assisting management to develop assumptions that form the basis for the forecast
 - assembling the forecast (i.e., performing the mechanical aspects of translating the assumptions into the forecast)
 - reviewing the financial forecast, which permits expressing conclusions on whether (a) the assumptions provide a reasonable basis for the forecast and (b) the forecast is presented in conformity with applicable presentation guidelines, and
 - concluding whether the forecast indicates that sufficient funds will be available to meet operating and debt service requirements.

When the financial feasibility study includes such procedures, the accountant's report on the study often describes the procedures and conclusions.

3. The Guide provides for such an expanded report (page 22) stating:

The report /on a review of a financial forecast/ may also present other information and comments the accountant wishes to include such as... explanatory comments or other informative material.

The other information and comments may describe the nature of the work performed and conclusions reached with regard to other aspects of the financial feasibility study.

4. Following is an illustration of a report that might be issued when an accountant is engaged to conduct a financial feasibility study. Although the entity in the illustrative report is a hospital, the form of report, revised as appropriate, is applicable to other entities, such as a hotel or sports stadium.
5. The language used to expand the report on a review of a forecast should be tailored to fit the circumstances. The procedures listed in (paragraph e) of the illustrative report are merely examples and may not apply to all engagements.
6. In some circumstances, the accountant may wish to emphasize a matter in the report but not modify his conclusion. The accompanying illustrative report contains two examples of emphasis-of-a-matter paragraphs to illustrate the matters that are sometimes discussed by accountants. The first such paragraph

relates to legislation and regulation and illustrates how an accountant might refer to general conditions that could affect the forecast (paragraph j). The second such paragraph relates to the interest rate and other terms of the specific bond issue and illustrates how an accountant might refer to specific conditions that could affect the forecast (paragraph k).

Illustrative Report

- a. The Board of Directors
Example Hospital
Example, Texas
- b. We have prepared a financial feasibility study of the Example Hospital's plans to expand and renovate its facilities. The study was undertaken to evaluate the ability of the Example Hospital (the Hospital) to meet the Hospital's operating expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed \$25,000,000 [legal title of bonds] issue, at an assumed average annual interest rate of 10.0 percent, during the five years ending December 31, 1986.
- c. The proposed capital improvements program (the Program) consists of a new two-level addition which is to provide 50 additional medical-surgical beds, increasing the complement to 275 beds. In addition, various administrative and support service areas in the present facilities are to be remodeled. The Hospital administration anticipates that construction is to begin June 30, 1982, and to be completed by December 31, 1983.
- d. The estimated total cost of the Program is approximately \$30,000,000. It is assumed that the Example Hospital Finance Authority would issue \$25,000,000 of revenue bonds as the primary source of funds for the Program. Payment of debt service on the bonds is to be the sole responsibility of the Hospital. Other necessary funds to finance the Program are assumed to be provided from Hospital funds, from a local fund drive, and from interest earned on funds held by the bond trustee during the construction period.
- e. Our procedures included analysis and evaluation of:
 - Program history, objectives, timing and financing;
 - The future demand for the Hospital's services, including consideration of:
 - Economic and demographic characteristics of the Hospital's defined service area;
 - Locations, capacities and competitive information pertaining to other existing and planned area hospitals;
 - Physician support for the Hospital and its programs;
 - Historical utilization levels;
 - Planning agency applications and approvals;
 - Construction and equipment costs, debt service requirements and estimated financing costs;
 - Staffing patterns and other operating considerations;

- Third-party reimbursement policy and history; and
 - Revenue/expense/volume relationships.
- f. We also participated in gathering other information, assisted management in identifying and formulating its assumptions, and assembled the accompanying financial forecast based upon those assumptions.
- g. The accompanying financial forecast is based upon assumptions that were provided by or reviewed with and approved by management. The financial forecast for the annual periods ending December 31, 1982 through 1986 includes:
- Balance sheets,
 - Statements of revenues and expenses,
 - Statements of changes in financial position, and
 - Statements of changes in fund balance.
- h. The financial forecast presents management's estimate of the most probable financial position, results of operations, and changes in financial position and fund balance for the forecast periods. Accordingly, the forecast reflects its judgment, based on present circumstances, of the most likely set of conditions and its most likely course of action.
- i. We have made a review of the financial forecast in accordance with applicable guidelines for a review of a financial forecast established by the American Institute of Certified Public Accountants. Our review included those procedures we considered necessary to evaluate both the assumptions used by management and the preparation and presentation of the forecast.
- j. Legislation and regulations at all levels of government have affected and may continue to affect revenues and expenses of hospitals. The financial forecast is based upon legislation and regulations currently in effect. If future legislation or regulations related to hospital operations are enacted, such legislation or regulations could have a material effect on future operations.
- k. The interest rate, principal payments, Program costs, and other financing assumptions are described in the section entitled "Summary of Significant Forecast Assumptions and Rationale." If actual interest rates, principal payments, and funding requirements are different from those assumed, the amount of the bond issue and debt service requirements would need to be adjusted accordingly from those indicated in the forecast. If such interest rates, principal payments, and funding requirements are lower than those assumed, then such adjustments would not adversely affect the forecast.

1. Our conclusions are presented below:

- We believe that the accompanying financial forecast is presented in conformity with applicable guidelines for presentation of a financial forecast established by the American Institute of Certified Public Accountants.
 - We believe that the underlying assumptions provide a reasonable basis for management's forecast. However, some assumptions inevitably will not materialize and unanticipated events and circumstances may occur; therefore, the actual results achieved during the forecast periods will vary from the forecast, and the variations may be material.
 - The accompanying financial forecast indicates that sufficient funds will be available to meet the Hospital's operating expenses, working capital needs, and other financial requirements, including the debt service requirements associated with the proposed \$25,000,000 bond issue, during the forecast periods. However, the achievement of any financial forecast is dependent upon future events, the occurrence of which cannot be assured.
- m. We have no responsibility to update this report for events and circumstances occurring after the date of this report.
- n. (Date)