EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: July 2, 2012
Comments Due: October 1, 2012

Presentation of Financial Statements (Topic 205)

The Liquidation Basis of Accounting

This Exposure Draft of a proposed Accounting Standards Update of Topic 205 is issued by the Board for public comment. Comments can be provided using the electronic feedback form available on the FASB website. Written comments should be addressed to:

Technical Director
File Reference No. 2012-210

Financial Accounting Standards Board
of the Financial Accounting Foundation

The *FASB Accounting Standards Codification*® is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft and is requesting comments by October 1, 2012. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at Exposure Documents Open for Comment
- Emailing a written letter to director@fasb.org, File Reference No. 2012-210
- Sending written comments to "Technical Director, File Reference No. 2012-210, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116."

Do not send responses by fax.

All comments received are part of the FASB's public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

An electronic copy of this Exposure Draft is available on the FASB's website.

Financial Accounting Standards Board
of the Financial Accounting Foundation
401 Merritt 7, PO Box 5116, Norwalk, Connecticut 06856-5116

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Summary and Questions for Respondents

Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

There is minimal guidance that addresses when it is appropriate to apply, or how to apply, the liquidation basis of accounting. Consequently, there is diversity in practice. The guidance in the proposed amendments is being issued to clarify when an entity should apply the liquidation basis of accounting and to provide principles for the measurement of assets and liabilities under the liquidation basis of accounting as well as any required disclosures.

Who Would Be Affected by the Amendments in This Proposed Update?

The proposed amendments would apply to all entities that issue financial statements that are presented in conformity with U.S. generally accepted accounting principles (GAAP). The specific provisions would apply when an entity determines that liquidation is imminent.

What Are the Main Provisions?

The proposed amendments would require an entity to prepare its financial statements using the liquidation basis of accounting when liquidation is imminent. The Board decided that liquidation would be considered imminent when either (a) a plan for liquidation has been approved by the person or persons with the authority to make such a plan effective and the likelihood is remote that the execution of the plan will be blocked by other parties or (b) a plan for liquidation is being imposed by other forces (for example, involuntary bankruptcy) and the likelihood is remote that the entity will subsequently return from liquidation. If a plan for liquidation was specified in the entity's governing documents at the entity's inception (for example, limited-life entities), liquidation would be considered imminent when significant management decisions about furthering the ongoing operations of the entity have ceased or they are substantially limited to those necessary to carry out a plan for liquidation other than the plan specified at inception.

The proposed amendments also would require financial statements prepared using the liquidation basis to reflect relevant information about an entity's resources and obligations in liquidation by measuring and presenting assets and liabilities in the entity's financial statements at the amount of cash or other consideration that the entity expects to collect or the amount of cash or other consideration that the entity expects to pay during the course of liquidation. An entity also would be required to accrue and separately present the costs that it expects to incur and the income that it expects to earn during the expected duration of the liquidation, including any costs associated with settlement of those assets and liabilities.

Additionally, the proposed amendments would require disclosures about the entity's plan for liquidation, the methods and significant assumptions used to measure assets and liabilities, the type and amount of costs and income accrued, and the expected duration of liquidation.

How Would the Main Provisions Differ from Current U.S. Generally Accepted Accounting Principles (GAAP) and Why Would They Be an Improvement?

U.S. GAAP provides minimal guidance on the application of the liquidation basis of accounting. The Board believes that the new guidance would improve the consistency and comparability of financial reporting.

When Would the Amendments Be Effective?

The effective date will be determined after the Board considers the feedback on the amendments in this proposed Update. The proposed amendments would be effective as of the beginning of the period of adoption and would be applied prospectively from the day that liquidation becomes imminent.

How Do the Proposed Provisions Compare with International Financial Reporting Standards (IFRS)?

IFRS currently does not provide explicit guidance on when or how to apply the liquidation basis of accounting. IFRS states that an entity should prepare financial statements on the going concern basis of accounting "unless management either intends to liquidate the entity or to cease trading, or has no realistic alternative but to do so" (paragraph 25 of IAS 1, *Presentation of Financial Statements*).

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: The proposed guidance would require an entity to prepare its financial statements using the liquidation basis of accounting when liquidation is imminent, as defined in the proposed guidance. Is the proposed guidance about when an entity should apply the liquidation basis of accounting appropriate and operational? If not, why?

Question 2: The proposed guidance includes a principle for measuring assets and liabilities, as well as related items of income and expense, using the liquidation basis of accounting. The proposed guidance would require supplemental disclosures about the methods and assumptions used in arriving at those measurements. This guidance is intentionally nonprescriptive in light of the specialized nature of liquidation basis financial statements and the impracticability of providing prescriptive guidance for the myriad of circumstances to which it might apply. Is the proposed guidance on how to prepare financial statements using the liquidation basis sufficient and operational? If not, why?

Question 3: The proposed guidance would apply to all entities that prepare financial statements in accordance with U.S. GAAP. Should the proposed guidance differ for any entities (for example, investment companies) whose primary measurement attribute is fair value? If so, why?

Question 4: The proposed guidance would apply to a limited-life entity when significant management activities are limited to those necessary to carry out a plan for liquidation other than that which was specified in the entity's governing documents. Indicators have been provided to help an entity determine whether a plan for liquidation differs from that which was specified in the governing documents. Do you agree with the proposed guidance about when a limited-life entity should use the liquidation basis of accounting? If not, why?

Question 5: The proposed guidance would apply to public and nonpublic entities (that is, private companies and not-for-profit organizations). Should any of the proposed amendments be different for nonpublic entities? If so, please identify those proposed amendments and describe how and why you think they should be different.

Amendments to the *FASB Accounting Standards Codification*®

Summary of Proposed Amendments to the Accounting Standards Codification

1. The following table provides a summary of the proposed amendments to the Accounting Standards Codification.

Codification Section	Description of Changes
Master Glossary	Added the terms *liquidation, statement of changes in net assets in liquidation,* and *statement of net assets in liquidation.*
Presentation of Financial Statements—Liquidation Basis (Subtopic 205-30)	Added proposed amendments that would establish guidance on the adoption and preparation of financial statements using the liquidation basis of accounting.
Reorganizations—Overall (Subtopic 852-10)	Amended paragraph 852-10-60-1 to reflect the addition of Subtopic 205-30.
Financial Services—Depository and Lending—Consolidation (Subtopic 942-810)	Amended paragraph 942-810-05-1 to reflect the addition of Subtopic 205-30. Superseded paragraph 942-810-45-2.
Plan Accounting—Defined Benefit Pension Plans—Terminating Plans (Subtopic 960-40)	Amended paragraphs 960-40-25-1 through 25-2 to reflect the addition of Subtopic 205-30. Superseded paragraph 960-40-35-1 and amended paragraph 960-40-35-2.
Plan Accounting—Defined Contribution Pension Plans—Terminating Plans (Subtopic 962-40)	Amended paragraphs 962-40-25-1 through 25-2 to reflect the addition of Subtopic 205-30. Superseded paragraph 962-40-35-1.
Plan Accounting—Health and Welfare Benefit Plans—Terminating Plans (Subtopic 965-40)	Amended paragraphs 965-40-25-1 through 25-2 and 965-40-35-2 to reflect the addition of Subtopic 205-30. Superseded paragraph 965-40-35-1.

Introduction

2. The Accounting Standards Codification is amended as described in paragraphs 3–12. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~. **[For ease of readability, the newly added Subtopic is not underlined.]**.

Amendments to Master Glossary

3. Add the following Master Glossary terms, with a link to transition paragraph 205-30-65-1, as follows:

Liquidation

The process by which an entity converts its assets to cash or other assets and partially or fully settles its obligations with creditors in anticipation of the entity ceasing its operations. Any remaining cash or other assets are distributed to the entity's owners. Liquidation may be compulsory or voluntary. Dissolutions via acquisition or merger do not qualify as liquidations.

Statement of Changes in Net Assets in Liquidation

A statement that includes information about the changes during the period in net assets available for distribution to investors and other claimants during liquidation.

Statement of Net Assets in Liquidation

A statement that includes information about the net assets available for distribution to investors and other claimants during liquidation as of the end of the reporting period.

Addition of Subtopic 205-30

4. Add Subtopic 205-30, with a link to transition paragraph 205-30-65-1, as follows:

Presentation of Financial Statements—Liquidation Basis

Overview and Background

205-30-05-1 The Liquidation Basis Subtopic provides guidance on when and how an entity should prepare its financial statements using the liquidation basis of accounting and describes the related disclosures that should be made.

205-30-05-2 This Subtopic addresses the accounting and financial statement disclosure for entities that may have filed petitions with the **bankruptcy court** and expect to liquidate under Chapter 7 of the bankruptcy code. However, the material in this Subtopic should not be relied upon as a definitive interpretation of the law for any purpose.

205-30-05-3 The accounting and reporting guidance in this Subtopic is incremental to guidance that otherwise applies to an entity.

Scope and Scope Exceptions

205-30-15-1 The guidance in this Subtopic applies to all entities.

Recognition

205-30-25-1 An entity shall prepare financial statements in accordance with the requirements of this Subtopic when **liquidation** is imminent.

205-30-25-2 Liquidation is imminent when either of the following occurs:

a. A plan for liquidation has been approved by the person or persons with the authority to make such a plan effective and the likelihood is remote that the execution of the plan will be blocked by other parties (for example, those with **protective rights**).
b. A plan for liquidation is imposed by other forces (for example, involuntary bankruptcy) and the likelihood is remote that the entity will return from liquidation.

205-30-25-3 If a plan for liquidation was specified in an entity's governing documents at the entity's inception (for example, limited-life entities), then liquidation is imminent when significant management decisions about furthering the ongoing operations of the entity have ceased or they are substantially limited to those necessary to carry out a plan for liquidation other than the plan specified at inception. Indicators that a plan for liquidation might differ from that which was specified in the governing documents include the following:

a. The date that liquidation is expected to conclude is earlier or later than the contractually stated expiration date of the entity.
b. The entity is forced to dispose of its assets in a manner that is not orderly or in exchange for consideration that is not commensurate with the fair value of such assets.
c. The entity's governing documents were amended since inception.

Other circumstances may arise that indicate a plan for liquidation that differs from that which was specified in the entity's governing documents.

205-30-25-4 The liquidation basis of accounting shall be applied prospectively from the day that an entity meets the conditions of paragraph 205-30-25-1 with a cumulative-effect adjustment to the statement of changes in net assets in liquidation, as applicable.

Initial Measurement

205-30-30-1 Assets and liabilities shall be measured to reflect the estimated amount of cash or other consideration that an entity expects to collect or pay to carry out its plan for **liquidation**.

205-30-30-2 Estimated costs to dispose of assets or liabilities shall be accrued and presented in the aggregate separately from the measurement of those assets or liabilities.

205-30-30-3 Other costs and income that an entity expects to incur or earn (for example, payroll expense and interest income) shall be accrued through the date at which the entity expects to complete its liquidation. See paragraph 205-30-50-1 for related disclosure requirements.

Subsequent Measurement

205-30-35-1 At each reporting date, an entity shall remeasure its assets, liabilities, and the accruals of disposal or other costs or income to reflect the actual or estimated change in value since the previous reporting date in accordance with paragraphs 205-30-30-1 through 30-3.

Other Presentation Matters

205-30-45-1 At a minimum, liquidation basis financial statements shall consist of the following:

a. A **statement of net assets in liquidation**
b. A **statement of changes in net assets in liquidation.**

Disclosure

205-30-50-1 In addition to all other disclosures required by U.S. GAAP, an entity shall disclose all of the following when it prepares financial statements using the liquidation basis of accounting:

a. That the financial statements are prepared using the liquidation basis of accounting, including the facts and circumstances surrounding the adoption of the liquidation basis of accounting.
b. A description of the entity's plan for **liquidation**, including, at a minimum, a description of the manner by which the entity expects to dispose of its assets and liabilities and the expected duration of the liquidation.
c. The methods and significant assumptions used to measure assets and liabilities, including subsequent changes to those methods and assumptions. Significant methods and assumptions might include, for example, the nature and source of expected future cash flows and discount rates used.
d. The type and amount of costs and income accrued in the statement of changes in net assets in liquidation.

Implementation Guidance and Illustrations

> Illustrations

205-30-55-1 The following Examples illustrate how an entity would determine when it should apply the liquidation basis of accounting. The Examples are not intended to capture every scenario under which an entity might have to apply the liquidation basis of accounting.

> > Example 1: Normal Operating Entity

205-30-55-2 Entity A is a manufacturer of goods. In 20X2, Entity A began experiencing financial difficulty because of declining market demand for its goods. On September 19, 20X2, Entity A's board of directors approved a plan for **liquidation**. The board of directors had the legal authority to make this plan effective, and there were no parties with protective rights that could block the execution of this plan. Entity A should begin preparing its financial statements using the liquidation basis of accounting as of September 19, 20X2, which is the date that Entity A's board of directors approved the plan for liquidation.

> > Example 2: Limited-Life Entity with Unplanned Liquidation

205-30-55-3 Entity B is a limited-life entity with a contractual life of 10 years. Entity B purchased various real estate properties in Years 1 through 3 with the intention of selling those properties on or before its contractual expiration date. On March 11 of Year 6, Entity B began disposing of its real estate properties because it was no longer solvent. Entity B's operating decisions were limited to decisions related to the maintenance of its properties pending their sale. All other operating decisions were insignificant. Entity B should begin preparing its financial statements using the liquidation basis of accounting as of March 11 of Year 6, which is the date that Entity B's significant management activities became limited to those related to carrying out a plan for liquidation in a manner different from that which was specified in Entity B's governing documents.

> > Example 3: Limited-Life Entity That Liquidates as Planned at Inception

205-30-55-4 Entity C is a limited-life entity with a contractual life of 10 years. Entity C purchased various real estate properties in Years 1 through 8. Management continued to actively make decisions related to managing and increasing the value of its investments through Year 8. In Year 9, as planned in Entity C's governing documents, management began to sell the properties as it wound down the entity. Entity C did not experience financial difficulty and was able to complete its planned cycle. In this case, Entity C should not prepare its financial statements using the liquidation basis of accounting at any time because its actual liquidation was consistent with the plan specified in Entity C's governing documents.

Transition and Open Effective Date Information

> Transition Related to Accounting Standards Update No. 2012-XX, *Presentation of Financial Statements (Topic 205): The Liquidation Basis of Accounting*

205-30-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 2012-XX, *Presentation of Financial Statements (Topic 205): The Liquidation Basis of Accounting*. The pending content that links to this paragraph shall be effective as of the beginning of a reporting entity's first annual reporting period that begins after **[date to be inserted after exposure]** and for interim and annual periods thereafter. Earlier application is permitted.

Amendments to Subtopic 852-10

5. Amend paragraph 852-10-60-1, with a link to transition paragraph 205-30-65-1, as follows:

Reorganizations—Overall

Relationships

> Financial Services—Depository and Lending

852-10-60-1 For the required financial statement reporting of a **liquidating bank**, see ~~Section 942-810-45~~ Subtopic 205-30.

Amendments to Subtopic 942-810

6. Amend paragraph 942-810-05-1 and supersede paragraph 942-810-45-2 and its related heading, with a link to transition paragraph 205-30-65-1, as follows:

Financial Services—Depository and Lending—Consolidation

Overview and Background

942-810-05-1 This Subtopic provides presentation and disclosure guidance concerning ~~**liquidating banks** and~~ trust-preferred securities.

Other Presentation Matters

~~**> Liquidating Bank**~~

942-810-45-2 Paragraph superseded by Accounting Standards Update 2012-XX. ~~A **liquidating bank** shall report assets and liabilities at fair values at the date of the financial statements and shall recognize in the results of each current period subsequent decreases and increases in those values. In the absence of a change in facts and circumstances as to the anticipated timing and manner of disposition, the method used to develop the initial fair values shall continue to be used for subsequent valuations. Fair values provide users of financial statements with the most relevant information for a liquidating entity.~~

Amendments to Subtopic 960-40

7. Amend paragraphs 960-40-25-1 through 25-2, with a link to transition paragraph 205-30-65-1, as follows:

Plan Accounting—Defined Benefit Pension Plans—Terminating Plans

Recognition

960-40-25-1 If the decision to terminate a plan is made before the end of the plan year, the plan's year-end financial statements shall be prepared ~~on~~ using the liquidation basis of accounting~~, as described in paragraphs 962-40-35-1 through 35-2~~ in accordance with Section 205-30-45.

960-40-25-2 Plan financial statements for periods ending after the termination decision are prepared ~~on~~ using the liquidation basis of accounting.

8. Supersede paragraph 960-40-35-1 and amend paragraph 960-40-35-2, with a link to transition paragraph 205-30-65-1, as follows:

Subsequent Measurement

960-40-35-1 Paragraph superseded by Accounting Standards Update 2012-XX. ~~For **terminating plan** assets, changing to the liquidation basis will usually cause little or no change in values, most of which are current market values. Assets that may not be carried at market values include all of the following:~~

~~a. Operating assets~~
~~b. Insurance and certain investment contracts carried at contract values~~
~~c. Large blocks of stock or other assets that cannot be readily disposed of at their quoted market prices.~~

960-40-35-2 For **terminating plan** assets, accumulated ~~Accumulated~~ plan benefits shall be determined ~~on a~~ using the liquidation basis of accounting (see Subtopic 205-30), and their value may differ from the actuarial present value of accumulated plan benefits reported for an ongoing plan. In general, upon termination all benefits should be reported as vested.

Amendments to Subtopic 962-40

9. Amend paragraphs 962-40-25-1 through 25-2, with a link to transition paragraph 205-30-65-1, as follows:

Plan Accounting—Defined Contribution Pension Plans—Terminating Plans

Recognition

962-40-25-1 If the decision to terminate a plan is made before the end of the plan year, the plan's year-end financial statements shall be prepared ~~on~~ using the liquidation basis of accounting~~, as described in paragraph 962-40-35-1~~ in accordance with Section 205-30-45.

962-40-25-2 Plan financial statements for periods ending after the termination decision are prepared ~~on~~ using the liquidation basis of accounting.

10. Supersede paragraph 962-40-35-1, with a link to transition paragraph 205-30-65-1, as follows:

Subsequent Measurement

962-40-35-1 Paragraph superseded by Accounting Standards Update 2012-XX. ~~For **terminating plan** assets, changing to the liquidation basis will usually cause little or no change in values, most of which are current market values. Assets that may not be carried at market values include all of the following:~~

- ~~a. Operating assets~~
- ~~b. Insurance and certain investment contracts carried at contract values~~
- ~~c. Large blocks of stock or other assets that cannot be readily disposed of at their quoted market prices.~~

Amendments to Subtopic 965-40

11. Amend paragraphs 965-40-25-1 through 25-2, with a link to transition paragraph 205-30-65-1, as follows:

Plan Accounting—Health and Welfare Benefit Plans—Terminating Plans

Recognition

965-40-25-1 If the decision to terminate a plan is made before the end of the plan year, the plan's year-end financial statements shall be prepared ~~on~~ using the liquidation basis of accounting~~, as described in paragraphs 965-40-35-1 through 35-2~~ in accordance with Section 205-30-45.

965-40-25-2 Plan financial statements for periods ending after the termination decision are prepared ~~on~~ using the liquidation basis of accounting.

12. Supersede paragraph 965-40-35-1 and amend paragraph 965-40-35-2, with a link to transition paragraph 205-30-65-1, as follows:

Subsequent Measurement

965-40-35-1 Paragraph superseded by Accounting Standards Update 2012-XX. ~~For **terminating plan** assets, changing to the liquidation basis will usually cause little or no change in values, most of which are current market values. Assets that may not be carried at market values include all of the following:~~

- ~~a. Operating assets~~
- ~~b. Insurance and certain investment contracts carried at contract values~~
- ~~c. Large blocks of stock or other assets that cannot be readily disposed of at their quoted market prices.~~

965-40-35-2 For **terminating plan** assets, benefit ~~Benefit~~ obligations shall be determined ~~on a~~ using the liquidation basis of accounting (see Subtopic 205-30), and their value may differ from the actuarial present value of benefit obligations reported for an ongoing plan. Consideration shall be given upon termination to whether any or all benefits become vested.

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Leslie F. Seidman, *Chairman*
Daryl E. Buck
Russell G. Golden
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Board's considerations in reaching the conclusions in this proposed Update. It includes reasons for accepting certain approaches and rejecting others. Individual Board members gave greater weight to some factors than to others.

Background Information

BC2. The Board originally undertook this project to incorporate the AICPA's Codification of Statements on Auditing Standards AU Section 341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AU 341), into U.S. GAAP. AU 341 provides guidance that requires an entity's auditors to assess whether there is substantial doubt about the entity's ability to continue as a going concern. During initial deliberations, the Board decided to develop guidance that would require an entity's management to evaluate the entity's ability to continue as a going concern and require disclosures when either financial statements are not prepared on a going concern basis or there is substantial doubt about the entity's ability to continue as a going concern.

BC3. In October 2008, the Board issued an Exposure Draft, *Going Concern,* covering the items set out in paragraph BC2. The Board received 29 comment letters in response to that Exposure Draft and considered respondents' comments during its redeliberations of the project. The Board decided that the following matters warranted further deliberations:

a. Reconsideration of defining and incorporating the terms *going concern* and *substantial doubt* into U.S. GAAP
b. The time horizon over which management would evaluate an entity's ability to meet its obligations
c. The type of information that management should consider in evaluating an entity's ability to meet its obligations
d. The effect of subsequent events on management's evaluation of an entity's ability to meet its obligations
e. Whether to provide guidance on the liquidation basis of accounting.

BC4. The Board then modified the objective of the project to include guidance that would require an entity to provide earlier disclosures (as it became increasingly likely that the entity would be unable to meet its obligations as they become due. This objective replaced the project's initial objective of incorporating AU 341 into U.S. GAAP because the Board came to believe that users of financial statements would benefit more from ongoing and incremental disclosures about risk than from disclosures only required when management concluded that there was substantial doubt about the entity's ability to continue as a going concern. Because of stakeholders' comments that the guidance about when and how an entity should apply the liquidation basis of accounting was inadequate, the Board also added a separate objective to provide guidance related to that topic.

Reasons for the Proposed Changes

BC5. The liquidation basis of accounting was not addressed in the 2008 Exposure Draft; however, several respondents indicated that there was a need for guidance about when and how to prepare financial statements using the liquidation basis of accounting. Separately, in discussions with a private company resource group, the group members indicated that guidance on the liquidation basis of accounting would be helpful to private company preparers and users of financial statements. Research performed during development of this proposed Update indicated that there is diversity in practice about the measurements and disclosures required when using the liquidation basis of accounting. Recognizing this diversity in practice, the Board decided to provide guidance on when and how to prepare financial statements using the liquidation basis of accounting.

BC6. The Board decided that unless liquidation is imminent, an entity would be required to prepare financial statements under the assumption that the entity will continue to operate. If liquidation is imminent, the entity's financial statements would be prepared in accordance with the proposed guidance on the liquidation basis of accounting. The Board chose to use the term *imminent* because it is consistent with the guidance on the liquidation basis of accounting that currently exists in the AICPA's Codification of Statements on Auditing Standards Section AU 9508, *Reports on Audited Financial Statements: Auditing Interpretations of Section 508,* and Statement of Position 93-3, *Rescission of Accounting Principles Board Statements.*

BC7. The Board initially defined the term *imminent* in a manner similar to the definition in IFRS, which focuses on whether management intends to liquidate an entity or to cease trading, or has no realistic alternative but to do so. However, while the Board agreed with the overall principle behind this language, it chose not to pursue this definition. Instead, the Board considered language that more clearly stated when and how an entity should apply the liquidation basis of accounting. The Board's revised definition focused solely on whether an entity's decision makers had approved a plan for liquidation. However, this definition would have been problematic for the limited-life entity because the guidance could have been interpreted to mean that a limited-life entity would apply the liquidation basis from its inception. The Board indicated that this was undesirable from a cost-benefit standpoint primarily because investors in these entities understand at inception the limited-life nature of these entities and they often interact freely with management. Furthermore, because many limited-life entities already measure their assets at fair value, the incremental benefit of the liquidation basis of accounting would be limited for these entities. Specifically, while the measurement of some assets and liabilities might be reported at current amounts (fair value), an entity also would be required to accrue and separately present the estimated costs and income related to disposal of assets and liabilities, in addition to other costs and income that the entity expects to incur to complete its liquidation. The Board indicated that a switch to the liquidation basis should be required only when an entity's plan for liquidation changes from that which was communicated to investors as part of the entity's governing documents. To address implementation issues for limited-life entities, the Board specified that these entities should use the liquidation basis when significant management decisions about furthering the ongoing operations of the entity have ceased or they are limited to those necessary to carry out a plan for liquidation that differs from that which was specified in the governing documents at inception.

BC8. The Board recognizes that requiring an entity to prepare its financial statements using the liquidation basis of accounting may be inconsistent with the measurement of assets and liabilities presented for general purpose financial reporting in accordance with FASB Concepts Statement No. 8, *Conceptual Framework for Financial Reporting—Chapter 1,* The Objective of General Purpose Financial Reporting, *and Chapter 3,* Qualitative Characteristics of Useful Financial Information. However, Concepts Statement 8 states that general purpose financial reports are not designed to meet all specialized needs. The Board believes that financial statements that are prepared using the liquidation basis of accounting provide users of those financial statements with specialized information because the emphasis shifts from reporting about the entity's economic performance and position to reporting about the amount of cash that would be available to investors after liquidation. The Board decided that it would require, at a minimum, a statement of net assets and a statement of changes in net assets. The Board decided that it would require a statement of changes in net assets instead of a statement of comprehensive income because it considers it to be more relevant to users of the financial statements of an entity that is in liquidation. Financial statements that are prepared using the liquidation basis of accounting should convey information about the amount of cash or other consideration that an entity expects to collect or the amount of obligations that the entity expects to pay during the course of liquidation. The Board also decided that estimated costs to dispose of assets or liabilities would be presented separately from the measurement of those assets or liabilities.

BC9. Under the proposed guidance, assets and liabilities would be measured at the estimated amount of cash expected to be collected or paid. This measurement differs from fair value because it does not assume that the related dispositions would be conducted in an orderly manner; in fact, they likely would not. An entity that measures its assets primarily at fair value would record adjustments that reconcile fair value to the amount of expected recoverable cash as part of its accrual of estimated costs to dispose of assets and liabilities. Because expectations about the amount to be collected or paid may require significant estimation, the Board determined that an entity whose financial statements are prepared using the liquidation basis of accounting would disclose the methods and significant assumptions used to measure assets and liabilities, and the type and amount of costs and income accrued, including the time horizon of accrual.

Benefits and Costs

BC10. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Board's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC11. The guidance about when and how to apply the liquidation basis of accounting addresses an area in which there is currently minimal guidance. The Board believes that the primary benefit of this guidance is that it will improve consistency because under its proposals an entity would transition to the liquidation basis of accounting only when liquidation is imminent. Additionally, this guidance would improve consistency on how an entity uses the liquidation basis of accounting by including a principle for measurement and related disclosures. The resulting financial statements would allow investors and other claimants to estimate more precisely how much they can reasonably expect to recover during liquidation. The Board also believes that this guidance will lead to financial reporting practices that are more comparable to those under IFRS.

BC12. The amendments in the proposed Update would establish a principles-based approach for applying the standard; therefore, an entity will need to use judgment based on facts and circumstances to determine when it is appropriate to apply the liquidation basis of accounting. The Board anticipates that the costs to comply with the proposed amendments will be substantially limited to the costs required to perform the remeasurements of the cash expected to be collected or paid by an entity during liquidation. In many cases (for example, when there is an observable market price), estimating these amounts is anticipated to be straightforward. In some cases, the Board acknowledges that management might have to devote a significant amount of time to reliably estimate these figures. However, the Board believes that the benefit of such data will justify those costs. Currently, the liquidation basis is used in practice very infrequently. Based on the high hurdle for applying the liquidation basis, the Board expects that this will continue to be true. Another expected cost of implementation would be the time required to evaluate whether an entity meets the definition of *imminent*.

Amendments to the XBRL Taxonomy

The following proposed changes to the U.S. GAAP Financial Reporting Taxonomy (UGT) would be required if the provisions of this Exposure Draft were finalized as proposed. These proposed changes to the taxonomy are available for public comment in the development UGT throughout the year at www.fasb.org. Changes to the UGT for final Accounting Standards Updates will be formally exposed for public comment as part of the annual release process starting in September of each year.

Element Name	Standard Label	Documentation
LiquidationBasisOfAccountingMember	Liquidation Basis of Accounting [Member]	Accounting basis under which assets and liabilities are measured to reflect the estimated amount of cash or other consideration that an entity expects to collect or pay to carry out its plan of liquidation.
LiquidationBasisOfAccountingTextBlock	Liquidation Basis of Accounting [Text Block]	Disclosure of information when an entity's financial statements are prepared using the liquidation basis of accounting.
LiquidationBasisOfAccountingAdoption	Liquidation Basis of Accounting, Adoption	Description of the fact that the financial statements are prepared using the liquidation basis of accounting, including the facts and circumstances surrounding the adoption of the liquidation basis of accounting.

Element Name	Standard Label	Documentation
LiquidationBasisOfAccountingLiquidationPlan	Liquidation Basis of Accounting, Liquidation Plan	Description of the entity's plan of liquidation, including the manner by which the entity expects to dispose of its assets and liabilities and the expected duration of the liquidation.
LiquidationBasisOfAccountingMethodsAndAssumptions	Liquidation Basis of Accounting, Methods and Assumptions	Description of the methods and significant assumptions used to measure assets and liabilities, including subsequent changes. Significant methods and assumptions might include, for example, the nature and source of expected future cash flows and discount rates used.
LiquidationBasisOfAccountingCostsAndIncomes	Liquidation Basis of Accounting, Costs and Incomes	Description of type of costs and incomes accrued in the statement of changes in net assets in liquidation.
LiquidationBasisOfAccountingAccruedCostsToDisposeOfAssetsAndLiabilities	Liquidation Basis of Accounting, Accrued Costs to Dispose of Assets and Liabilities	Amount of estimated accrued costs to dispose of assets and liabilities during the process of an entity carrying out its plan of liquidation.
LiquidationBasisOfAccountingCostsAndExpensesToDisposeOfAssetsAndLiabilities	Liquidation Basis of Accounting, Costs and Expenses to Dispose of Assets and Liabilities	Amount of estimated costs and expenses to dispose of assets and liabilities during the process of an entity carrying out its plan of liquidation.

Element Name	Standard Label	Documentation
NetAssets	Net Assets	Amount of assets net of liabilities.
NetAssetsAdjustedBalance	Net Assets, Adjusted Balance	Amount of assets net of liabilities, net of the cumulative effect of prospective application of a new accounting principle on the beginning balance.
AccountingStandardsUpdate2012XXMember	Accounting Standards Update 2012-XX [Member]	Accounting Standards Update 2012-XX, Presentation of Financial Statements (Topic 205): The Liquidation Basis of Accounting.