FINANCIAL ACCOUNTING SERIES

EXPOSURE DRAFT

Proposed Accounting Standards Update

Issued: April 17, 2012
Comments Due: July 16, 2012

Statement of Cash Flows (Topic 230)

Not-for-Profit Entities: Classification of the Sale of Donated Securities in the Statement of Cash Flows

a consensus of the FASB Emerging Issues Task Force

This Exposure Draft of a proposed Accounting Standards Update of Topic 230 is issued by the Board for public comment. Written comments should be addressed to:

Technical Director
File Reference No. EITF-12A

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 July 16, 2012. Interested parties may submit comments in one of two ways:

- Emailing a written letter to director@fasb.org, File Reference No. EITF-12A
- Sending written comments to "Technical Director, File Reference No. EITF-12A, 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)?

The objective of this proposed Update is to address the diversity in practice about how to classify cash receipts arising from the sale of certain donated securities in the statement of cash flows of not-for-profit entities (NFPs). Some NFPs classify the cash receipts arising from the sale of donated securities in the statement of cash flows as investing cash inflows. Other entities classify the cash receipts from the sale of donated securities as either operating cash inflows or financing cash inflows, consistent with their treatment of inflows arising from cash contributions.

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

The amendments in this proposed Update would affect any entity within the scope of Topic 958, Not-for-Profit Entities, that accepts donated securities.

What Are the Main Provisions?

The amendments in this proposed Update would require an NFP to classify cash receipts from the sale of donated securities consistently with cash donations received in the statement of cash flows if those cash receipts were from the sale of donated securities (a) that upon receipt are directed for sale and (b) for which the NFP has the ability to avoid significant investment risks and rewards through near immediate conversion into cash. Accordingly, the cash receipts from the sale of those securities would be classified as cash inflows from operating activities, unless the donor restricted the use of the contributed resources to long-term purposes, in which case those cash receipts would be classified as cash flows from financing activities. Otherwise, receipts from the sale of donated securities would be classified as cash flows from investing activities by the NFP.

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

Currently, there is diversity in practice under U.S. GAAP about the presentation of the cash receipts from the sale of donated securities in the statement of cash flows as either an investing activity or a noninvesting (operating or financing) activity. The amendments in this proposed Update would eliminate the diversity in practice.

When Would the Amendments Be Effective?

The amendments in this proposed Update would be applied prospectively to cash receipts on or after the date of adoption from the sale of donated securities. The proposed amendments would permit retrospective application. Early adoption would be permitted. The effective date will be determined after the Task Force considers stakeholder feedback on the proposed Update.

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

The Preface of International Financial Reporting Standards states that IFRSs are designed to apply to general purpose financial statements and other financial reporting of all profit-oriented entities. Although IFRSs are not designed to apply to not-for-profit activities, entities with such activities may find them appropriate.

IAS 7, *Statement of Cash Flows*, presents a principles-based definition of the classifications of cash flows. Operating cash flows are those that are derived from the principal revenue-producing activities of the entity. Sales of debt and equity instruments are identified as examples of investing activities; however, IAS 7 does not explicitly state that sale of such securities should be classified as investing activities.

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: Do you agree that the scope of this proposed Update should be limited to cash receipts of NFPs resulting from the sale of donated securities (a) that upon receipt are directed for sale and (b) for which the NFP has the ability to avoid significant investment risks and rewards through near-immediate conversion into cash? If not, should the scope be expanded by including donated assets other than securities and/or removing criterion (b)? Do you have another recommendation as to scope?

Question 2: Do you agree that cash receipts of NFPs resulting from the sale of donated securities (a) that upon receipt are directed for sale and (b) for which the NFP has the ability to avoid significant investment risks and rewards through near-immediate conversion into cash should be classified as operating cash flows unless the cash receipts meeting conditions (a) and (b) must be classified as a financing activity because the donor restricted the use of the contributed resources to long-term purposes? Do you also agree that all other cash receipts of NFPs resulting from the sale of debt and equity securities not meeting those conditions would be classified as investing cash flows? If not, please explain why.

Question 3: If you are a user of the financial statements of NFPs, would the amendments in the proposed Update affect your analysis? If so, please explain how.

Question 4: Do you agree that the proposed amendments should be applied prospectively but permit retrospective application to all prior periods presented upon the date of adoption? If not, please explain why.

Question 5: How much time is needed to implement the proposed amendments?

Amendments to the *FASB Accounting Standards Codification*®

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–5. 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 <u>underlined</u> and deleted text is ~~struck out~~.

Amendments to Subtopic 230-10

2. Amend paragraph 230-10-45-12, with a link to transition paragraph 230-10-65-1, as follows:

Statement of Cash Flows—Overall

Other Presentation Matters

230-10-45-12 All of the following are cash inflows from investing activities:

a. Receipts from collections or sales of loans made by the entity and of other entities' debt instruments (other than cash ~~equivalents and~~ <u>equivalents,</u> certain debt instruments that are acquired specifically for resale as discussed in paragraph 230-10-45-21<u>, and certain donated debt instruments received by not-for-profit entities (NFPs) as discussed in paragraph 230-10-45-21A</u>) ~~that were purchased by the entity~~
b. Receipts from sales of equity instruments of other entities (other than certain equity instruments carried in a trading account as described in paragraph 230-10-45-19 <u>and certain donated equity instruments received by NFPs as discussed in paragraph 230-10-45-21A</u>) and from returns of investment in those instruments
c. Receipts from sales of property, plant, and equipment and other productive assets
d. not used
e. Receipts from sales of loans that were not specifically acquired for resale. That is, if loans were acquired as investments, cash receipts from sales of those loans shall be classified as investing cash inflows regardless of a change in the purpose for holding those loans.

For purposes of this paragraph, receipts from disposing of loans, debt or equity instruments, or property, plant, and equipment include directly related proceeds of insurance settlements, such as the proceeds of insurance on a building that is damaged or destroyed.

3. Add paragraph 230-10-45-21A, with a link to transition paragraph 230-10-65-1, as follows:

230-10-45-21A Cash receipts resulting from the sale of donated securities by NFPs that upon receipt are directed for sale and for which the NFP has the ability to avoid significant investment risks and rewards through near immediate conversion into cash shall be classified as operating cash flows. If, however, the donor restricted the use of the contributed resource to a long-term purpose of the nature of those described in paragraph 230-10-45-14(c), then those cash receipts meeting all the conditions in this paragraph shall be classified as a financing activity.

Amendments to Subtopic 958-230

4. Amend paragraph 958-230-55-3, with a link to transition paragraph 230-10-65-1, as follows:

Not-for-Profit Entities—Statement of Cash Flows

Implementation Guidance and Illustrations

> > Cash Received with a Donor-Imposed Restriction that Limits Its Use to Long-Term Purposes

958-230-55-3 When an NFP reports cash received (or cash receipts from the sale of donated securities that were directed upon receipt for sale and for which the NFP had the ability to avoid significant investment risks and rewards through near immediate conversion into cash as discussed in paragraph 230-10-45-21A) with a **donor-imposed restriction** that limits its use to long-term purposes in conformity with paragraph 958-210-45-6, an adjustment is necessary for the statement of cash flows to reconcile beginning and ending cash and cash equivalents. ~~To report in conformity~~In accordance with Topic 230, such a cash~~the~~ receipt ~~of a cash **contribution** that is restricted for the purchase of equipment~~ shall be reported as a cash flow from financing activities (using a caption such as contributions restricted for purchasing equipment), and it shall be simultaneously reported as a cash outflow from investing activities (using a caption such as purchase of assets restricted to investment in property and equipment or, if the equipment was purchased in the same period, purchase of equipment). An adjustment to reconcile the change in net assets to net cash used or provided by operating activities would also be needed if the contributed asset is not classified as cash or cash equivalents on the statement of financial position. When the equipment is purchased in a subsequent period, both the proceeds from the sale of assets restricted to investment in the equipment and the purchase of the equipment shall be reported as cash flows from investing activities.

5. Add paragraph 230-10-65-1 and its related heading as follows:

> Transition Related to Accounting Standards Update No. 2012-XX, *Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification of the Sale of Donated Securities in the Statement of Cash Flows*

230-10-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 2012-XX, *Statement of Cash Flows (Topic 230): Not-for-Profit Entities: Classification of the Sale of Donated Securities in the Statement of Cash Flows:*

a. The pending content that links to this paragraph shall be applied prospectively to cash receipts on or after the date of adoption from the sale of donated securities for fiscal years, and interim periods within those years, beginning after [date to be inserted after exposure]. Retrospective application to all prior periods presented upon the date of adoption also shall be permitted but not required.
b. Earlier adoption of the pending content that links to this paragraph is permitted.
c. An entity shall provide the disclosures in paragraphs 250-10-50-1 through 50-2 in the period the entity adopts the pending content that links to this paragraph.

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 Task Force's considerations in reaching the conclusions in this proposed Update. It includes the Board's basis for ratifying the Task Force conclusions when needed to supplement the Task Force's considerations. It also includes reasons for accepting certain approaches and rejecting others. Individual Task Force and Board members gave greater weight to some factors than to others.

BC2. This proposed Update would clarify the guidance on classification in the statement of cash flows of cash receipts from the sale of donated securities that upon receipt are directed for sale and for which the NFP has the ability to avoid significant investment risks and rewards through near immediate conversion into cash. The proposed Update would require that those cash receipts be classified consistently with cash donations received. Accordingly, the cash receipts from the sale of those securities would be classified as cash inflows from operating activities. However, if the donor restricted the use of the contributed resource to a long-term purpose (for example, the acquisition, construction, or improvement of long-lived assets or to establish or increase a permanent or term endowment), then those cash receipts would be classified as cash flows from financing activities. Otherwise, receipts from the sale of donated securities would be classified as cash flows from investing activities by the NFP.

Background Information and Basis for Conclusions

BC3. NFPs receive donations to operate their programs. Many donations are made in the form of cash, but some donations are made in the form of securities. Although NFPs typically accept donations in the form of securities, many have institutional policies to immediately sell them to convert the securities to cash to be available for immediate use. Some NFPs that have such a policy consider those donated securities to be essentially equivalent to cash.

BC4. Topic 230 requires entities to classify cash receipts as operating, investing, or financing activities. There is diversity in practice on the presentation of cash receipts from the sale of donated securities in the statement of cash flows. Some NFPs classify the cash receipts arising from the sale of donated securities in the statement of cash flows as investing cash inflows. Other entities classify the cash receipts from the sale of donated securities as either operating cash inflows or financing cash inflows, consistent with their treatment of inflows arising from cash contributions. Some constituents have raised concerns with this diversity in practice.

BC5. The Task Force concluded that the receipt of a donated security and its near immediate conversion into cash is economically similar to the receipt of cash donations. Accordingly, the Task Force also concluded that characterizing the cash receipts from the sale of such securities as an investing activity would not provide relevant information about how an NFP obtains cash. Rather, characterizing those receipts as an investing activity might inappropriately suggest a degree of reliance on investing results and investment risks and rewards, which are not present. Because the securities in the scope of this proposed Update generally are accepted by the NFP to accommodate the donor's objectives rather than as a result of a strategic decision to invest in a particular entity or asset class, the Task Force does not consider the cash resulting from those transactions to be investing activities in the way that the statement of cash flows characterizes such activities. The Task Force concluded that determining whether the cash receipts from the sale of such donated securities are classified as an operating activity or instead are classified as a financing activity should be consistent with classifying receipts of cash donations.

Scope

BC6. The Task Force decided that the scope of this proposed Update would be limited to the statement of cash flows classification of cash receipts of NFPs resulting from the sale of donated securities that upon receipt are directed for sale and for which the NFP has the ability to avoid significant investment risks and rewards through near immediate conversion into cash. Task Force members discussed broadening the scope of this proposed Update to include cash flows resulting from the near immediate sale of other donated assets, such as cars and works of art, but concluded that since they are not aware of significant diversity in practice related to classification of cash flows from sale of other assets, the scope of this proposed Update should be limited to cash flows from donated securities.

BC7. The Task Force discussed whether the ability to avoid significant investment risks and rewards through near immediate conversion into cash should be one of the criteria for applying the proposed guidance or whether the intent to avoid the investment risks and rewards, as evidenced by direction upon receipt of the security for sale, should be the only basis for classifying the cash receipt as an operating or financing activity. The Task Force concluded that an entity's ability to avoid significant investment risks and rewards through near immediate conversion into cash (combined with the intent criterion) is significant in determining whether the cash flows are not reflective of investing activities of the NFP, since the volatility in the fair value is a common characteristic of investing activities. Furthermore, the Task Force concluded that classifying cash receipts for which an NFP is subject to a significant amount of investment risks and rewards as anything other than investing activities might impair a user's ability to assess the uncertainty in prospective cash receipts associated with future sales of donated securities.

Transition and Early Adoption

BC8. The Task Force reached a consensus-for-exposure that entities should apply the amendments in this proposed Update prospectively to cash receipts on or after the date of adoption from the sale of donated securities. Retrospective application to all prior periods presented upon the date of adoption also would be permitted but not required. The Task Force concluded that the costs of retrospectively applying the guidance may exceed the benefits of having comparable financial information. However, because comparability of financial information of an entity across periods is useful and the information required for retrospective application may be available to some NFPs, the Task Force decided to permit retrospective application of the proposed amendments. The transition guidance is based on the cash receipts from the sale of donated securities to ensure consistent treatment of cash receipts from those sales in the period of adoption.

BC9. The Task Force decided that early adoption of the proposed amendments should be permitted to allow for the elimination of existing diversity as soon as is practicable.

Benefits and Costs

BC10. The objective of financial reporting is to provide information that is useful to present and potential donors, creditors, investors, 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 donors, creditors, investors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by those that presently provide resources to the reporting NFP. 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 amendments in this proposed Update may be applied prospectively, and no additional recurring disclosures are required. As such, the Task Force does not anticipate that NFPs will incur significant costs as a result of the proposed amendments. The proposed amendments would provide the benefit of eliminating diversity in practice and increasing the consistency of the classification of the cash receipts from the sale of qualifying donated securities and cash donations received in the statement of cash flows.

Proposed 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 are finalized as proposed. The proposed changes to the UGT 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
EITF12A Member	EITF 12-A [Member]	EITF 12-A: Not-for-Profit Entities: Classification of the Sale of Donated Securities in the Statement of Cash Flows