

TIS Section 1100

Statement of Financial Position

.15 Liquidity Restrictions

Inquiry—Entities may invest in assets such as money market funds or other short term investment vehicles from which they generally may withdraw funds at any time without prior notice or penalty, but for which the fund (or its trustee) may restrict the ability of an entity to withdraw its balance in the fund or other short term investment vehicle. In some circumstances, with little or no notice, the fund (or its trustee) may impose such withdrawal restrictions. For example, the fund (or its trustee), in accordance with the terms of the fund, may, with little or no notice, stipulate that up to 20 percent of the fund balance can be withdrawn immediately, an additional 30 percent can be withdrawn in 6 months, and the remaining balance can be withdrawn in 2 years.

What are the potential accounting and auditing implications of such an event for a nongovernmental entity (the event being restrictions on the ability of an entity to withdraw its balance in the money market fund or other short term investment vehicle)?

Reply—The following are examples of potential accounting and auditing issues that may be relevant if such an event exists. Each situation is different and should be evaluated based on its specific facts and circumstances:

Balance Sheet Classification. Such withdrawal restrictions should be considered in determining whether such assets meet the definition of *cash equivalents*. (This technical question and answer does not address

whether such assets met the definition of *cash equivalents* prior to the imposition of such withdrawal restrictions.)

Paragraph 8 of Financial Accounting Standards Board (FASB) Statement No. 95, *Statement of Cash Flows*, provides a definition of *cash equivalents* for the purposes of applying that statement.

Such withdrawal restrictions should be considered in determining whether such assets meet the definition of *current assets*.

Accounting Research Bulletin (ARB) No. 43, *Restatement and Revision of Accounting Research Bulletins*, chapter 3A, "Current Assets and Current Liabilities," defines *current assets* for balance sheet classification purposes.

For entities that do not prepare a classified balance sheet, such withdrawal restrictions should be considered in determining the sequencing of assets on the balance sheet or disclosures in the notes to financial statements providing relevant information about the liquidity or maturity of assets.

Disclosures. The entity may be required to provide financial statement disclosures about such events. For example, such events may create or lead to risks and uncertainties pertaining to certain significant estimates, such as measurement, liquidity, and violation of debt covenants, and vulnerability from concentrations of investments in volatile markets. Entities should consider whether they should make disclosures in their financial statements (beyond those required or generally made in financial statements) about the risks and uncertainties resulting from such events and existing as of the date of the financial statements. In addition, auditors

should consider whether such disclosures include forward-looking statements that are not required by generally accepted accounting principles and therefore may not be audited.

Statement of Position 94-6, *Disclosure of Certain Significant Risks and Uncertainties* (AICPA, *Technical Practice Aids*, ACC sec. 10,640), provides guidance pertaining to disclosures about risks and uncertainties.

Debt Covenants. Such events may result in balance sheet classifications (balance sheet classifications are previously discussed) and other events that may trigger violations of debt covenants. If a covenant violation occurs, issuers of debt should consider whether that covenant violation triggers classification of the debt liability as current (or otherwise affects reported information about liquidity) or cross covenant violations in other arrangements.

ARB No. 43 defines *current assets* and *current liabilities* for balance sheet classification purposes. FASB Statement No. 78, *Classification of Obligations That Are Callable by the Creditor—an amendment of ARB No. 43, Chapter 3A*, clarifies how the debtor should present obligations that are callable by the creditor in a balance sheet in which liabilities are classified as current or noncurrent.

ARB No. 43 and FASB Statement No. 6, *Classification of Short-Term Obligations Expected to Be Refinanced—an amendment of ARB No. 43, Chapter 3A*, provide guidance for the classification of short-term obligations that are expected to be refinanced on a long-term basis.

Emerging Issues Task Force (EITF) Issue No. 86-30, “Classification of Obligations When a Violation is Waived by the Creditor,” addresses the classification of obligations at the balance sheet date that are not callable at the balance sheet date, but that become callable by violation of a debt agreement provision after the balance sheet date but before the financial statements are issued.

EITF Topic No. D-23, “Subjective Acceleration Clauses and Debt Classification;” FASB Technical Bulletin No. 79-3, *Subjective Acceleration Clauses in Long-Term Debt Agreements*; and FASB Statement No. 6 provide guidance pertaining to balance sheet classification in circumstances in which debt agreements include subjective acceleration clauses.

Events Occurring Subsequent to the Balance Sheet Date. Events occurring subsequent to the balance sheet date, but prior to the issuance of the financial statements, such as significant changes in fair value or changes in liquidity leading to violation of debt covenants, may need to be reflected in the financial statements (either through adjustment to or disclosure in the financial statements).

Paragraphs .02–.09 of AU section 560, *Subsequent Events* (AICPA, *Professional Standards*, vol. 1), provide guidance pertaining to subsequent events. EITF Topic D-11, “Impact of Stock Market Decline,” discusses matters pertaining to certain subsequent events.

Going Concern. Certain events (some interrelated) could call into question the entity’s ability to continue as a going concern. For example:

- The inability to withdraw funds can pose significant challenges to the entity's liquidity.
- As discussed earlier, balance sheet reclassifications or other events may trigger violations of debt covenants.

Entities and auditors should consider such events and circumstances in evaluating an entity's ability to continue as a going concern.

AU section 341, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern* (AICPA, *Professional Standards*, vol. 1), provides guidance with respect to evaluating whether there is substantial doubt about the entity's ability to continue as a going concern, as well as the impact on the auditor's report.

Auditor Communication With Those Charged With Governance. Auditors should consider whether such events and any matters related to such events should be communicated to those charged with governance.

AU section 380, *The Auditor's Communication With Those Charged With Governance* (AICPA, *Professional Standards*, vol. 1), establishes standards and provides guidance to an auditor on matters to be communicated with those charged with governance.

Auditor's Report—Emphasis of a Matter. Auditors should consider whether they wish to emphasize a matter pertaining to such events and regarding the financial statements in the auditor's report. For example, the auditor may wish to refer, in the auditor's report, to financial statement disclosures about restrictions on liquidity pertaining to such events.

AU section 508, *Reports on Audited Financial Statements*, paragraph .19 (AICPA, *Professional Standards*, vol. 1) discusses an emphasis of a matter in the auditor's report.