FASB Proposes More Disclosures about Risks
For Non-Financial Institutions

As part of its ongoing financial instruments projects, the Financial Accounting Standards Board (FASB) has proposed an Accounting Standards Update (ASU) which requires additional disclosures by reporting entities regarding information about liquidity and interest rate risks arising from the entity's use of financial instruments. The incremental disclosures affect all entities regardless of the size or complexity of operations, but the specific requirements vary depending on the nature of the entity and its operations. The proposed ASU is a result of the FASB's outreach project regarding the classification and measurement of financial instruments and concerns by financial statement users regarding additional decision-useful information related to an entity's broad exposure to liquidity and interest rate risks associated with financial instruments. In issuing the proposed ASU, the FASB concluded that certain information relevant to financial statement users could not be achieved through classification and measurement, thus, additional disclosures were better designed to provide such information.

Overview of disclosures about liquidity and interest rate risks

The additional reporting requirements are designed to provide additional information regarding: (1) liquidity risk, meaning the risk that the reporting entity may encounter difficulty in meeting obligations to be settled by delivering cash or another financial asset, and (2) interest rate risk, defined as the exposure of a financial institution's financial instruments to fluctuations in market interest rates. The proposed requirements apply on a consolidated basis, but may apply to certain reportable segments for entities with diverse operations.

Certain disclosures regarding liquidity risks are applicable to all reporting entities, with expanded disclosures applicable to financial institutions. Interest rate risk disclosures are applicable only to financial institutions as defined in the proposed ASU. The definition of a financial institution excludes most broker-dealers and investment companies; however, it may still apply if such entities have individual reportable segments that meet the definition of a financial institution. This article summarizes the requirements for non-financial institutions, including the potential impact to reportable segments. The requirements for financial institutions and companies with subsidiaries or segments that are considered financial institutions are summarized in a tailored version of our MHM Messenger publication (MHM Messenger 13-12b).

How would non-financial institutions be affected?

The FASB's proposed requirements are contained in Proposed ASU, *Financial Instruments (Topic 825), Disclosures about Liquidity Risk and Interest Rate Risk*. Highlights are as follows.

1. **Definition.** Non-financial companies would be defined under the exposure draft as those that do not meet the following definition of a financial institution: An entity or reportable segment for which the primary business activity is to do either of the following: (a) earn, as a primary source

of income, the difference between interest income generated by earning assets and interest paid on borrowed funds, or (b) provide insurance. However, entities that are not considered financial institutions when considered as a whole may have subsidiaries or reportable segments that are considered financial institutions, and therefore, the disclosures applicable to such entities would apply to those subsidiaries and/or reporting segments. This may require nonpublic entities to include the expanded disclosures applicable to financial institutions for certain reporting segments and the less detailed liquidity risk disclosures for the remaining reporting segments that are not considered financial institutions. Multiple reportable segments may be consolidated when preparing such disclosures.

2. **Disclosures about expected cash flow obligations.** To help users of financial statements understand an entity's liquidity risks, a non-financial institution would be required to provide a table showing a detail of the expected maturities of its undiscounted financial liabilities and off-balance sheet obligations as of the reporting date. Public companies would be required to provide this information for both annual and interim reporting periods specified in the ASU. Nonpublic companies would be required to provide the information only for certain annual periods. Key aspects of the table include:

   - The line items of the table could be presented in one of several ways (e.g., on the basis of their nature, characteristics, or risks). These items would need to include the undiscounted amounts of the entity's financial liabilities and off-balance sheet obligations.
   - The columns of the table would represent the time intervals of the expected maturities. For a public company, the columns would display at least seven time intervals, including each of the next four quarters and other specified intervals. Nonpublic entities may combine the quarters into a single time interval. This table would also include a column presenting the adjustments necessary to reconcile the sums of the amounts shown in the table to the carrying amounts presented in the statement of financial position.
   - An entity would be required to disclose any significant expected differences between contractual maturities and expected maturities.
   - An illustrative example is shown in Table 1 on the last page of the PDF version of our MHM Messenger.

3. **Disclosures about available liquid funds.** All companies, including financial and non-financial institutions, would be required to provide a table showing their available liquid assets, including unencumbered cash and high-quality assets, as well as borrowing availability, which might include available lines of credit and other contractual commitments. Key points:

   - A tabular presentation would be required by class of asset (which typically would be more detailed than the captions presented in the balance sheet). An additional narrative discussion would be required to provide information about the effects of regulatory, tax, legal, repatriation, and other conditions that could limit the transferability of funds among entities.
   - Judgment would be required to determine which liquid assets are high-quality, and companies would need to disclose the characteristics considered in making this determination along with any changes in characteristics compared with prior reporting periods.
   - An illustrative example is shown in Table 2 on the last page of the PDF version of our MHM Messenger.

4. **Additional quantitative or narrative disclosures.** To supplement the tables related to liquidity risk, non-financial institutions would also need to discuss any significant changes in the timing and amounts of their cash flow obligations and available liquid funds in the tabular disclosures from the last reporting period to the current reporting period, including the reasons for the changes and actions taken, if any, during the current period to manage the exposure related to those changes.

5. **Effective date.** The exposure draft does not propose a specific effective date. But the FASB has indicated a desire to make the requirements effective as soon as possible. The FASB will determine the effective date after consideration of the comments letters and other feedback received on the proposed ASU.

Open questions

The Exposure Draft was open for comment through September 25, 2012. The FASB asked for comments on a number of open questions for users, preparers, and auditors, including operational concerns, how much lead time would be required to prepare for and implement the proposed amendments and whether the effective date should be delayed for nonpublic entities.

For more information

If you have any specific questions, comments or concerns, please share them with your CBIZ Tofias & Mayer Hoffman McCann advisor, or you may reach us at TheBottomLine@cbiztofias.com and 888.761.8835.

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