ACCOUNTING

Just Go with the Flow—Cash Flow Reporting

History of Statement No. 9

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When the Berlin Wall came down and while people were singing to Madonna's "Like a Prayer," the Governmental Accounting Standard Board (GASB), in its fifth year of existence, approved Statement No. 9 on cash flow reporting of proprietary funds and governmental entities that use proprietary fund accounting. While much has changed in the international and social environments, as well as in the world of governmental accounting, very little has changed regarding cash flow reporting. There continues to be no indications of major changes on the horizon. The challenge is that minimal authoritative guidance has been developed to specifically address newer transactions, such as how pensions, asset retirement obligations, and lease activity fit into the existing structure of the statement of cash flows. The consensus appears to be that Statement No. 9's guidance stands strong and sufficient, as is.

Relevant guidance subsequent to 1989 includes an amendment to remove the *indirect method* as an allowable method of reporting the cash flows from operating activities and periodic implementation to guide questions and answers to address specific issues. Overall, guidance on cash flows reporting has largely remained intact for over 33 years. The current standards and implementation guidance on cash flow reporting is found in GASB's current Codification of Governmental Accounting and Financial Reporting Standards (Cod.), Section (Sec.) 2450, "Cash Flows Statements."

The cash flow statement can help governments—and users of their financial statements—understand how their proprietary funds are meeting their cash needs in the four categories defined by GASB Cod. Sec. 2450.112:

- **OPERATING**
- **NONCAPITAL FINANCING**
- **CAPITAL AND RELATED FINANCING**
- **INVESTING**

How to fit in the *flows*

Asset Retirement Obligations (ARO). Many enterprise funds were impacted by Statement No. 83, Asset Retirement Obligations (as amended, in GASB Cod. Sec. A10, "Certain Asset Retirement Obligations"), which resulted in the reporting of a long-term liability and a related deferred outflow of resources. The annual activity for Asset Retirement Obligations (AROs), as well as for the similar landfill closure and postclosure (as amended, in Cod Sec. L10, "Landfill Closure and Postclosure Care Costs"), will likely result in both cash and noncash reporting on the statement of cash flows.

On the statement of cash flows, the actual cash paid for the ongoing retirement efforts of an asset (reduction of the liability) would likely meet the criteria of a cash outflow from operating activities and not be specifically identified as ARO related. While the annual recognition of the deferred outflow of resources over the expected life of an ARO is not directly impacted by cash activity, the change in this balance sheet line item should be reported on the reconciliation of operating income (loss) to net cash from (for) operating activities.

Liabilities for Leases and SBITAs. Efforts to implement leases and subscription-based information technology arrangements (SBITAs) (GASB Cod. Sec. L20, "Leases" and Cod. Sec. S80, "Subscription-Based Information Technology Arrangements," respectively), are well underway. The initiation of a lease (by a lessee government) or SBITA, and the resulting recognition of the intangible right-to-use asset, as well as remeasurement adjustments throughout the life of the lease, should be reflected in the schedule of noncash financing and investing activities.

Throughout the life of the lease or SBITA, the cash outflows for principal and interest payments should be reflected as a capital and related financing outflow, consistent with the concept that the associated intangible right-to-use asset is a capital asset. The annual amortization of the intangible right-to-use asset can be aggregated with depreciation of other capital assets in the reconciliation of operating income (loss) to net cash from (for) operating activities.

Lease receivable and other long-term notes receivable. As a reminder, when a government enterprise fund is the lessor in a lease of a capital asset, the proprietary fund statement of fund net position reports a long-term lease receivable and a related deferred inflow of resources. The government will continue to report the capital asset at historical cost and depreciate annually. The categorization of the cash receipts for principal and interest related to this lease are identified in authoritative implementation guidance (GASB Cod. Sec. 2540.707-16) as capital and related financing. The path to this conclusion is based on the principle that leases are financings with the categorization of proceeds analogized to a sale of capital assets. This categorization should be applied even when the ongoing operations of the government or proprietary fund is leasing property to third parties.

If a government proprietary fund is the lessor of an asset that is classified as an investment on its statement of fund net position, then the government should follow recognition, measurement, and reporting guidance applicable to the underlying asset (an investment) in GASB Cod. Secs. 3100, "Fair Value Measurement" and I50, "Investments"). Hence, this would not result in a lease receivable and deferred inflow of resources. Instead, since the cash flows receipts for principal and interest relate to an investment, the lessor would categorize them as cash flows from investing activities. This analysis takes us back to the implementation of GASB Statement No. 72, *Fair Value Measurement*, (GASB Cod. Secs. 3100 and I50) which required governments to identify assets as investments at the time of implementation.

Other long-term receivables may be the result of a sale of capital assets, such as a note receivable, or the result of cash lending, such as a loan receivable. Understanding the origin of the receivable is paramount to proper categorization on the statement of cash flows. For a note receivable, the cash inflow associated with a sale of a capital asset should be reported as a capital and related financing inflow. However, the cash inflow related to the loan receivable (principal and interest), would be reported as an investing activity.

American Rescue Plan Act Funding. With some governments allocating American Rescue Plan Act (ARPA) funding (unrestricted federal revenue) to proprietary funds for a variety of purposes, including pursuing capital projects, understanding the crosswalk between the government-wide statement of activities and the proprietary funds statements is important. These federal revenues are not restricted to a specific purpose. Even if a government chooses to use ARPA funds to complete capital projects, the cash inflow does not meet the criteria to be reported as a capital related financing activity. Cash receipts from grants that are not specifically restricted for capital purposes should be reported as a cash inflow from noncapital financing activities.

Reminders!

Always Double Check NICA—If the cash flow for principal and interest payments is reported as a cash flow for capital and related financing activities, then the amount of the related debt proceeds that have been spent on capital assets should be included in the calculation of the net investment in capital assets.

Mismatch—While operating revenues and expenses are defined by each government for reporting on the statement of revenues, expenses and changes in fund net position, cash flows from operating activities are considered the *catchall* group on the statement of cash flows. As such, the cash flows from nonoperating revenues and nonoperating expenses should not automatically be excluded from cash flows from operating activities.

Noncash items matter, too!—Capital contributions reported on the statement of revenues, expenses and changes in fund net position can be noncash (contribution of a capital asset) or cash (contribution or grant of cash restricted to fund a capital asset). Cash receipts from grants restricted for capital purposes should be reported as part of cash flows from capital and related financing activities, while noncash contributions should be included in the schedule of noncash financing and investing activities. The schedule of noncash activities should also include donated commodities, donated capital assets, debt refunding activity when an escrow agent is used, and issuances of other liabilities, including loans, leases, and SBITAs that directly result in a capital asset.

Keep your eyes on the flow of the Financial Reporting Model Project

GASB's major project on the Financial Reporting Model continues to move through deliberations. Tentative changes to the proprietary fund's statement of revenues, expenses and changes in fund net position may impact how operating revenues and expenses correspond to cash flows from operating activities in the statement of cash flows. And to all those who had their fingers crossed during this project's initial deliberations, there should be no government-wide statement of cash flows requirement coming. Stay tuned!

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