

CHAPTER 2***Cash Flows Reporting***

Primary Pronouncement: GASB Statement 9

Primary Codification Section Reference: 2450

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QUESTIONS AND ANSWERS

2.1 Introduction

2.2 FASB Statement 95

2.2.1. [Not used in GASBIG 20XX-1]

2.3 Scope and Applicability of Statement 9

2.4 Reporting Entity Issues

2.4.1. Q—Paragraph 456 in the Basis for Conclusions of Statement No. 34, *Basic Financial Statements— and Management’s Discussion and Analysis—for State and Local Governments*, explains that users interested in cash flow information about a specific component unit should refer to the component unit’s separately issued financial statements. If a component unit does not issue separate financial statements, is cash flow information for the component unit required to be presented in the reporting entity’s comprehensive annual financial report (CAFR)?

A—Yes. If a component unit does not issue separate financial statements, fund financial statements for that component unit should be included in the reporting entity’s CAFR. Therefore, if the component unit has proprietary funds, cash flow statements for those funds would be included in the major component unit information in the reporting entity’s CAFR as supplementary information.

2.4.2. Q—Does Statement No. 9, *Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities That Use Proprietary Fund Accounting*, apply to component units when they are included in a governmental financial reporting entity? Does it matter if the component units are blended or discretely presented?

A—Generally, a statement of cash flows is not required for discretely presented component units. (See Questions 2.4.1 and 4.28.10.) Paragraph 125 of Statement 34, as amended, requires discrete presentation of component unit financial data in the reporting entity’s statement of net position and statement of activities—there is no “government-wide” cash flows statement. However, the balances and transactions of *blended* component units are included as if they were balances and transactions of the primary government itself. Therefore, if a component unit is “blended” as an enterprise fund, a statement of cash flows would be required for that fund, either presented separately as a major fund or aggregated with other nonmajor enterprise funds.

2.4.3. Q—A public university uses the business-type activities model and has a closely related fund-raising foundation that meets the component unit criteria in Statement No. 39, *Determining Whether Certain Organizations Are Component Units*. The foundation’s financial statements will be included through discrete presentation. Is the university required to include the foundation’s cash flow information in its statement of cash flows?

A—No. Paragraph 125 of Statement 34, as amended, states that the discrete presentation requirements are met by displaying component unit financial data in the statements of net position and activities. Even though that requirement is stated in terms that apply to reporting governmental activities, the standard should be comparably applied, in substance, to the business-type activities model. That is, component unit data should be included by discrete presentation in the statements of financial position (statement of net position/balance sheet) and changes in financial position

(statement of revenues, expenses, and changes in net position). Paragraph 125 does not include a requirement to display component unit cash flow information.

2.5 Public Employee Retirement Systems and Pension Trust Funds

2.5.1. Q—Are public employee retirement systems (PERS) prohibited from presenting a statement of cash flows? If a statement of cash flows is presented, should it conform to the Statement 9 requirements, as amended, or can the presentation be modified?

A—PERS are not required to present a statement of cash flows; however, they are not precluded from presenting it as supplementary information. Statement 9 establishes standards for the basic financial statements; it does not prescribe requirements for data presented as supplementary information. PERS that present a statement of cash flows as supplementary information may choose, but are not required, to present that statement in accordance with the provisions of Statement 9, as amended.

2.6 Colleges and Universities

2.6.1. [Not used in GASBIG 20XX-1]

2.6.2. [Not used in GASBIG 20XX-1]

2.6.3. [Not used in GASBIG 20XX-1]

2.7 Other Applicability Issues

2.7.1. Q—In the private sector, certain investment companies are exempted from presenting a statement of cash flows. Are public-sector investment pools similarly exempt?

A—Yes. Paragraph 17 of Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, as amended, states that “. . . annual financial reports for governmental external investment pools should include a statement of net position and a statement of changes in net position. . . . A statement of cash flows is not required to be presented.” Paragraph 18 of that Statement, as amended, requires sponsoring governments to use investment trust funds to report the external portions of their investment pools. It states that “. . . the sponsoring government should present for each investment trust fund a statement of fiduciary net position and a statement of changes in fiduciary net position.”

2.7.2. Q—Should agency cash flows be included in the statement of cash flows for a university that reports using the business-type activities model?

A—A statement of cash flows is required for proprietary funds and entities that use proprietary fund accounting. A statement of cash flows is not required for fiduciary funds. Therefore, if the university does not use fiduciary funds, and instead includes the agency cash and cash equivalent balances with the cash and cash equivalents reported on the university’s statement of net position, the receipts and disbursements pertaining to agency activity should be included.

2.7.3. Q—Should a proprietary fund that has no operating income or loss present a statement of cash flows?

A—Yes. A statement of cash flows should be presented for all proprietary funds even if operating income is zero. Transactions other than those resulting in operating income create cash flows that should be presented in the statement of cash flows. If there is no operating income or loss for the

period, the reconciliation of operating income to net cash flow from operating activities would begin with zero. Adjustments and reconciling items should be presented as additions to and deductions from zero to arrive at the amount of net cash flow from operating activities.

2.7.4. [Not used in GASBIG 20XX-1]

2.8 Financial Reporting of Cash Flows

2.9 Purpose of a Statement of Cash Flows

2.10 Focus on Cash and Cash Equivalents

2.11 Definition of Cash and Cash Equivalents

2.11.1. Q—Is the definition of cash equivalents limited to investments with an original maturity of three months or less?

A—Generally, the three-month criterion is the deciding factor. The definition of cash equivalents in Statement 9, paragraph 9, first refers to short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. Although this definition appears to be somewhat broad, the reference to “three months or less” provides more specific guidance.

Because the definition of cash equivalents is a vital part of a cash flow presentation, a uniform definition should be used by all governmental enterprises. Therefore, generally only investments with original maturities of three months or less meet the definition of cash equivalents.

2.11.2. Q—When should the term *original maturity* be applied to investment purchases?

A—Original maturity is based on the date the governmental enterprise purchases an investment. If, *on the purchase date*, a qualifying investment will mature in three months or less, it meets the definition of a cash equivalent. The evaluation should be made only once, as of the purchase date. (See footnote 6 of Statement 9, for further explanation.)

2.11.3. Q—How should a negative cash balance be presented in the statement of cash flows?

A—For purposes of the statement of cash flows, a negative cash balance should be assumed to be zero. This is consistent with traditional balance sheet reporting of zero cash and a liability for the negative amount. Because the accumulation of cash flows during the period results in a negative cash balance, an adjustment should be made to the cash flow amounts. An increase to zero in cash balance should be incorporated into the statement of cash flows by reporting an inflow in the noncapital financing activities category. This presentation reports the circumstances as if the banking system (or cash management pool) implicitly financed the negative cash situation. In the subsequent period, an assumption should be made that the “loan” was repaid, and a noncapital financing outflow should be reported.

The presentation of implicit financing contradicts the requirement that cash flows not be reported unless they actually occur. The alternatives to this solution, however, are impractical and also have their own inconsistencies and contradictions. The solution provided in the preceding paragraph is consistent with reporting demand deposit cash flows at the moment the demand deposits are

tendered, rather than when the withdrawals are debited by the bank. For example, cash outflows represented by outstanding checks are reported based on the assumption that instantaneous withdrawals are made from demand deposit accounts at the time a check is written. At the reporting date, there is no need to reverse the outstanding checks from reported cash outflows merely because the checks have not been fully negotiated by the banking system. This may seem inconsistent with the guidance in Question 2.15.1, which states that cash flows in a banking environment occur only when a debit or credit is made to an account. However, a requirement to measure demand deposit cash flows at the point they are recorded by the bank is impractical. (See Example B in nonauthoritative Appendix 2-1.)

2.12 Investments and Cash Equivalents Definition Policy

2.12.1. Q—What are the cash flow statement ramifications of opting to treat an investment instrument that meets the definition of a cash equivalent as an investment?

A—If an instrument is treated as a cash equivalent, its conversion to or from cash or another cash equivalent would not be reported on the statement of cash flows. The transaction is analogous to the transfer of cash between two checking accounts. If, on the other hand, an instrument is treated as an investment, its conversion to or from cash or a cash equivalent should be reported in the investing activities category of the statement of cash flows, and the cash flows usually should be presented gross.

2.12.2. Q—Can restricted cash equivalents be treated as investments if similar unrestricted cash equivalents are treated as cash equivalents?

A—Yes. Identifying restricted cash equivalents that are similar to unrestricted cash equivalents as investments is acceptable according to the provisions of paragraph 11 of Statement 9. As long as an entity formulates and discloses a specific policy for defining cash equivalents, it may elect to treat any type of cash equivalents as investments. For example, Treasury bills with 60-day maturities in a restricted portfolio may be treated as investments even if unrestricted Treasury bills with the same maturities are treated as cash equivalents. (Paragraph 52 of the Statement 9 Basis for Conclusions states that “. . . governmental enterprises may choose to treat their restricted cash equivalents or unrestricted cash equivalents as investments.”)

2.13 Cash Management and Investment Pools

2.13.1. Q—When attempting to determine whether a participant is using an internal cash management or investment pool as a demand deposit account, is it important to consider the pool’s liquidity?

A—Yes, to some extent. A participant’s equity in an internal cash management or investment pool should not be considered cash unless the participant is able to withdraw cash at any time without prior notice or penalty. (Footnote 5 of Statement 9 acknowledges that cash includes “deposits in other kinds of accounts or cash management pools that have the general characteristics of demand deposit accounts in that the governmental enterprise may deposit additional cash at any time and also effectively may withdraw cash at any time without prior notice or penalty.”) If the pool is not liquid enough to enable a participant to make such demands on the pool, the participant is not able to use its equity in the pool as a demand deposit account. Stated another way, an investment pool should be evaluated as if it were a mutual fund. To some extent, the pool’s investments affect the ability of participants to use the pool as a demand deposit account. Also important are the number of participants and the likelihood that their withdrawals could overburden the pool. For cash flow

reporting purposes, the equity in a pool that is not sufficiently liquid to enable withdrawal without prior notice or penalty should be treated as an investment.

- 2.13.2. Q—Can an internal investment pool that is not being used by some participants as a demand deposit account be treated as cash by those participants who do use their equity in the pool as a demand deposit account?

A—Yes. The determination of whether a pool is being used as a demand deposit account should be made by each participant, independently of how other participants use the pool. If the pool is managed in such a way as to allow the governmental enterprise making the evaluation to deposit and withdraw funds as if it were a demand deposit account, that governmental enterprise's equity in the pool could be considered cash.

- 2.13.3. Q—Does restricted cash that is pooled by a bond paying agent meet the definition of a cash management or investment pool?

A—For cash flow reporting purposes, a pool operated by a bond paying agent is very similar to a mutual fund or an internal cash management or investment pool. If the bond paying agent pools the assets it receives from various sources and allocates investment earnings to all participants, the assets should be viewed as equity in a pool. According to footnote 5 of Statement 9 (and explained in paragraph 50 of the Basis for Conclusions), equity in a pool should be treated as either cash or an investment. If the governmental enterprise is able to deposit additional cash at any time and also effectively may withdraw cash at any time without prior notice or penalty, the equity in the pool may be treated as cash. If not, it is an investment.

Because the equity in the pool is restricted, there may be a question about whether the governmental enterprise may withdraw cash at any time. Even though the governmental enterprise may not be able to access its equity in the pool because the assets are legally restricted, it is able to withdraw cash by directing the bond paying agent to pay bondholders or others for whom the assets are restricted. The legal restrictions affect the governmental enterprise's access to the assets and the timing of payment to bondholders, but the restrictions do not change the characteristics of the account in which the assets are held. Statement 9, paragraph 8, disregards restriction of use as a factor in determining whether an asset meets the definition of cash or a cash equivalent.

- 2.13.4. Q—Does the issuance of warrants reduce cash?

A—Yes. The issuance of warrants, rather than the subsequent acceptance by the treasurer of the warrants, effectively reduces cash. That reduction of cash creates a cash flow. The substance, rather than the legal form, of the warrants should prevail. In a warrant system, participants draw down an available cash balance by issuing warrants. The system operates essentially as an internal cash management pool. It is irrelevant whether a warrant has been redeemed, just as it is irrelevant whether a check has been cashed, for determining cash balance. (See Question 2.11.3 for further explanation of cash flow timing.)

- 2.13.5. Q—Is there a cash flow to be reported in the statement of cash flows if an internal cash management pool engages in reverse repurchase agreement transactions with a third party?

A—No. If a reverse repurchase agreement is transacted through an internal cash management or investment pool, there are *no cash flows* directly into or out of an individual fund participating in the pool. The *pool* receives the borrowed cash and is obligated to “repurchase” the instrument at a later date. Reverse repurchase agreement activity in an internal cash management or investment pool

should have no effect on the participants' statements of cash flows—neither on the cash flows reported nor on the beginning and ending balances of cash and cash equivalents.

Interpretation No. 3, *Financial Reporting for Reverse Repurchase Agreements*, as amended, explains that, when a *pool* engages in a reverse repurchase agreement, the participating funds should be allocated to the related asset and liability and the interest income and expense. An allocation, however, is not a cash transaction to be presented in the statement of cash flows.

2.14 Relationship with GASB Statements 3 and 40

2.14.1. Q—How does the definition of cash equivalents correspond with the definitions of deposits and investments in Statements No. 3, *Deposits with Financial Institutions, Investments (including Repurchase Agreements)*, and No. 40, *Deposit and Investment Risk Disclosures*?

A—Statements 3 and 40 distinguish between deposits with financial institutions and investments. The two are mutually exclusive. The Statement 9 definition of a cash equivalent overlaps the definitions of deposits and investments. A cash equivalent, when evaluated for Statement 3 and 40 purposes, is either a deposit or an investment. That is, a 60-day certificate of deposit is a deposit with a financial institution, and a Treasury bill purchased 60 days before its maturity is an investment. But for cash flow reporting purposes, both qualify as cash equivalents because their original maturities are three months or less. The fact that a cash equivalent is a deposit or an investment has no effect on the presentation of the statement of cash flows.

2.14.2. Q—How should differences between the Statement 9 definition of cash equivalents and the Statements 3 and 40 definitions of deposits and investments be reconciled?

A—The Statement 9 definition of cash equivalents affects reported cash flows and beginning and ending cash and cash equivalent balances, as well as presentation of the related assets on the statement of net position/balance sheet. Statements 3 and 40 primarily address disclosure in the notes to the financial statements. The financial statement presentation requirements of Statement 9, as they relate to the presentation of cash equivalents, take precedence over discussions of deposits and investments in Statements 3 and 40. There is no requirement to reconcile the disclosures required by Statement 3, as amended, or Statement 40, as amended, to the statement of cash flows or to the statement of net position/balance sheet; however, some believe a reconciliation provides useful information. (See Question 1.26.6. See also Questions 2.31.1 and 2.31.2 for a discussion of the Statement 9 requirements for articulation between the statement of cash flows and the statement of net position/balance sheet.)

2.15 Identifying a Cash Flow

2.15.1. Q—What constitutes a cash flow?

A—Sometimes there may be a question as to whether a *cash* transaction has occurred. It may be confusing to identify a cash flow in a banking environment. Generally, cash flows only if it changes hands; that is, ownership of cash legally changes. In an internal exchange transaction conducted totally within a bank, a cash transaction occurs only if a debit or credit is made to a governmental enterprise's bank account. For example, a service charge or interest income is considered to be a cash transaction on the date the bank posts the amount to the account. After that date, the interest amount is available for withdrawal or the amount posted for the service charge is no longer available for withdrawal. Another example is a loan granted by a bank. If the loan proceeds are credited to the borrower's bank account, a cash flow occurred. If the bank remitted the proceeds directly to the

vendor, a noncash financing activity occurred. (See Question 2.32.1 for a discussion of noncash transactions.)

2.15.2. Q—How should bond issuance costs and underwriter fees be presented in the statement of cash flows?

A—If bond issuance costs and underwriter fees were deducted from bond proceeds, the governmental enterprise experienced only one cash flow. The net amount of bond proceeds actually received should be presented as a cash inflow in the appropriate category (either capital and related financing or noncapital financing, depending on the purpose of the borrowing).

On the other hand, if a governmental enterprise receives the proceeds from the sale of bonds and pays bond issuance costs and underwriter fees separately, the following cash flows should be presented: The total amount of bond proceeds should be presented as a cash inflow in the appropriate category (either capital and related financing or noncapital financing, depending on the purpose of the borrowing). The costs and fees that are paid from the governmental enterprise's cash or cash equivalents should be presented as cash outflows in the same category. (See Examples A, C, E, and F in nonauthoritative Appendix 2-1.)

2.15.3. Q—Are there cash flows associated with bond refundings?

A—Cash flow reporting of a defeasance of debt is addressed in paragraph 29c of Statement 9 and in Question 2.19.3 of this chapter. Paragraph 29c presumes that the refunding transaction resulted in cash flows. If the proceeds from the new bond issue are not converted into cash or a cash equivalent of the governmental enterprise before being used to defease the obligations associated with the refunded debt, there would be no cash flows to present in the statement of cash flows. (There are cash flows resulting from bond proceeds' being placed in escrow if the escrow assets are reported on the balance sheet.) If the transaction does not affect cash or cash equivalents, it should be disclosed as a noncash financing activity. (See Questions 2.32.1 and 2.32.2 on noncash disclosures; see also Examples A and D in nonauthoritative Appendix 2-1.)

2.15.4. Q—Should a cash flow be presented if the proceeds of revenue bonds issued by a finance authority are remitted directly to another organization?

A—No. If bond proceeds are remitted directly to another organization, there are no cash flows to report. If, however, the proceeds are received by the governmental enterprise (deposited in a cash or cash equivalent of the governmental enterprise) for distribution to another organization, cash flows do occur. The governmental enterprise is operating as an intermediary. Because the cash inflow and the cash outflow do not meet the criteria of the capital and related financing, noncapital financing, or investing activities category, both should be presented in the operating activities category. The operating activities category is the residual category.

2.15.5. Q—If a certificate of deposit that does not meet the definition of a cash equivalent automatically rolls over at maturity, is there a cash flow?

A—No. A cash flow does not occur unless there is a deposit to or withdrawal from cash or a cash equivalent. Therefore, a rollover does not affect the statement of cash flows. The certificate of deposit is merely converted from one investment instrument to another.

- 2.15.6. Q—If a trustee is administering a restricted investment portfolio for a governmental enterprise, should the investing activities be presented in the governmental enterprise’s statement of cash flows?

A—Yes. The investing cash flows should be presented on the statement of cash flows as if the governmental enterprise were managing the investments. The trustee is managing investments that belong to the governmental enterprise and are held in the name of the governmental enterprise, even though they are restricted. The investment portfolio is presented in the governmental enterprise’s statement of net position/balance sheet, and its performance is presented in the governmental enterprise’s operating statement. This arrangement is different from a cash management or investment pool arrangement, in which a fund manager commingles the assets provided by others. In a pool, each participant owns a share of the pooled assets and their earnings, rather than specific securities. (See Question 2.13.3.)

- 2.15.7. Q—How should the statement of cash flows display the net increase (decrease) in the fair value of investments?

A—The increase (decrease) in the fair value of investments is not a cash flow. However, changes in fair value (or amortization) of investments that meet the definition of cash equivalents in paragraph 9 of Statement 9 should be reported as cash flows from investing activities. These changes are readily convertible to known amounts of cash and are so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. When the net increase (decrease) in the fair value of investments is reported in the change statement as part of operating income, the change is presented as an element in the reconciliation of operating income to net cash provided by operating activities. (See also Question 2.21.1.)

2.16 Gross versus Net Reporting

- 2.16.1. Q—Should a governmental enterprise that qualifies for netting its investing activities under paragraph 14 of Statement 9 test for qualification every year?

A—Statement 9 states that information about gross cash receipts and payments is generally more relevant than net cash flow information. Therefore, the provision allowing a governmental enterprise to report certain cash flows net is an exception that should be used only after careful consideration. A governmental enterprise that qualifies for netting in one year should not presume to qualify permanently because it is possible to meet the criteria in one reporting period but not in another. Paragraph 14 lists two criteria that should be met in order for a governmental enterprise to qualify for net reporting of investments, and both should be evaluated throughout the year: “(a) during the period, substantially all of the governmental enterprise’s assets were highly liquid investments (for example, marketable securities and other assets for which a market is readily available) and (b) the governmental enterprise had little or no debt, based on average debt outstanding during the period, in relation to average total assets.” The basic characteristics of a governmental enterprise that qualifies for this netting provision should be called into question if they are subject to change. Essentially, the exception was designed to facilitate the cash flow reporting of governmental enterprises engaged solely in managing a highly liquid investment portfolio. If high liquidity varied from year to year, the governmental enterprise would not meet the spirit of the exception in any year.

- 2.16.2. Q—Paragraph 19 of Statement No. 49, *Accounting and Financial Reporting for Pollution Remediation Obligations*, states that the measurement of a government’s pollution remediation expense should include all remediation work that the government expects to perform, *reduced* by expected recoveries from other parties and from policies that indemnify the government for its pollution

remediation obligations. Should receipts of recoveries also reduce outflows reported on the statement of cash flows?

A—No. All cash flows for pollution remediation activities should be reported gross, in accordance with the provisions of Statement 9.

2.17 Classification of Cash Flows

2.17.1. Q—Can governments “indirectly” determine direct method cash flows?

A—Yes. Generally, governments can estimate certain direct method cash flow amounts by adjusting for beginning and ending receivables and payables. Exercise 7 in nonauthoritative Appendix 7-3 illustrates how that can be done.

2.18 Operating Activities—General

2.18.1. Q—Does the nature of a fund’s “operations” determine which cash flows should be presented in the operating activities category?

A—No. As stated in paragraph 7 of Statement 9, “the primary purpose of a statement of cash flows is to provide relevant information about the cash receipts and cash payments of an entity during a period.” It was determined that the most useful presentation is to provide information about capital and related financing, noncapital financing, and investing activities, as well as cash flows from operating activities. The Statement defines the categories from a functional perspective. Although the operating activities category also is defined, it serves as the residual category. Therefore, cash flow transactions should be evaluated first according to the definitions of capital and related financing, noncapital financing, and investing activities before being included in the operating activities category.

The operating activities category of the statement of cash flows is not intended to be a cash-basis operating statement. The format prescribed in Statement 9 is intended to complement the accrual-basis financial statements. In addition, the presentation is not intended to imply that one category is more desirable than any other category. Therefore, there should be no predilection for classifying cash flows in the operating activities category or any other category.

2.18.2. Q—Should all items reported as part of operating income be included in the operating activities category?

A—Not necessarily. Classification of a transaction for operating statement purposes should not dictate its classification in the statement of cash flows. As discussed in Question 2.18.1, the transaction should be evaluated first according to the definitions of the capital and related financing, noncapital financing, and investing activities categories.

Paragraph 16 of Statement 9 states that “cash flows from operating activities generally are the cash effects of transactions and other events that enter into the determination of operating income.” It was believed that most nonoperating income items would be classified in other than the operating activities category. The reconciliation of operating income to cash flows from operating activities would have fewer reconciling items if the operating activities category were highly correlated to operating income. However, paragraph 16 *definitively* states that the operating activities category includes “all transactions and other events that are not defined as capital and related financing,

noncapital financing, or investing activities.” Therefore, operating income should not be considered a criterion for classifying cash flows.

If a transaction is included in operating income and its resulting cash flow meets the definition of a category other than operating activities, the item should be presented as a reconciling item in the reconciliation of operating income to net cash flow from operating activities. For example, if a finance authority reports interest income as a component of operating income, the cash received from interest income should be presented in the investing activities category. The reconciliation of operating income to net cash flow from operating activities should begin with reported operating income, and the interest income amount should be deducted as a reconciling adjustment to operating income, similar to depreciation. (See Questions 7.73.1–7.73.5.)

2.19 Debt

2.19.1. Q—Should debt proceeds be classified in the capital and related financing activities category if the proceeds are distributed to component units for capital purposes?

A—No. The debt proceeds should be presented as a noncapital financing cash inflow, and subsequent debt service payments should be presented as noncapital financing cash outflows. Whether a financing activity meets the definition of capital depends on the use of the proceeds. If a governmental enterprise distributes the proceeds, it is not using the proceeds to acquire, construct, or improve its own capital assets. Therefore, the debt should not be considered capital debt for purposes of the statement of cash flows. Distribution of debt proceeds is similar to grant transactions. With regard to grant transactions, the grantor should classify all grants (except for certain operating-type grants) as *noncapital* financing activities, regardless of whether the grantee uses the grant for capital or noncapital purposes. To preserve classification symmetry, the proceeds of debt issued for the purpose of making grants for capital purposes should also be treated as *noncapital* financing activities.

2.19.2. Q—How should interest earnings on capital debt proceeds that are temporarily invested before being used for construction be classified?

A—Investment earnings should be considered an investing activity. Classification of cash flows usually should be based on the nature of the transaction.

2.19.3. Q—How should bond refunding transactions be presented?

A—Paragraph 29c of Statement 9 provides guidance for classifying bond refunding transactions:

In a defeasance of debt, the proceeds of a refunding debt issue used to refund capital debt should be reported as a cash inflow in the capital and related financing category and the payment to defease the existing capital debt should be reported as an outflow in that category. Similarly, subsequent principal and interest payments on the refunding debt should also be reported as cash outflows in the capital category. If the refunding issue is in excess of the amount needed to refund the existing capital debt, the total proceeds and the subsequent principal and interest payments should be allocated between the capital category and the noncapital financing category based on the amounts used for capital and noncapital purposes.

If the new bonds result in an in-substance defeasance and cash flows actually occur (see Question 2.15.3), there should be symmetry in reporting the cash flows related to the refunding. The outflow to a trustee or fiscal agent to defease the debt should be presented in the same category as the debt

service payment on the old debt. The proceeds should be classified as an inflow of the same category. The new debt assumes the characteristics of the old debt. Subsequently, the new debt issue should be classified in the same manner as the defeased debt. For example, if the original debt was for capital purposes, the new debt should be considered capital debt.

However, paragraph 29c explains that an entire refunding issue may not assume the characteristics of the old debt if the refunding debt exceeds the amount needed to defease the existing debt. If debt is issued for a dual purpose—to defease a noncapital debt issue and to finance new construction, for example—it should be allocated according to its purposes. The portion required to defease the old debt assumes the characteristics of the old debt. The remainder should be evaluated according to its purpose and is classified appropriately. (In this case, the remainder would be classified as a capital financing activity.) (See Example A in nonauthoritative Appendix 2-1.)

2.19.4. Q—Should a subsidy received to finance capital debt service be classified as capital or noncapital financing?

A—The subsidy should be reported by the recipient as an inflow in the capital and related financing activities category. A subsidy received specifically to finance capital debt service payments is an indirect way of financing capital acquisition, construction, or improvement. Therefore, it should be reported in the same way as a capital grant or other contribution received to defray capital costs. (See Example I in nonauthoritative Appendix 2-1.)

2.20 Nonoperating Income Items

2.20.1. Q—Rent income is an item often presented in the *nonoperating* income section of the operating statement. Should rent be classified as an operating activity or as some other activity?

A—As discussed in Question 2.18.1, the basic question is whether rent income meets the classification criteria of the noncapital financing, the capital and related financing, or the investing activities category. If not, the cash flows should be classified in the operating activities category because that is the residual category. Rent income is not specifically addressed in Statement 9; however, that should not necessarily lead one to categorize rent as an “operating activity.” The characteristics of the rent-generating asset should be examined.

The definition of the investing activities category does not specifically address the possibility of an investment being a tangible capital asset such as land; however, the list of investments described is not intended to be all-encompassing. If the land or other capital asset generating the rent is being held as an investment (because it is being held for appreciation or it is being held temporarily for resale), rent should be classified as an investing activity. Reporting the rent-generating asset on the statement of net position as an investment rather than a capital asset is evidence that the cash flows should be classified as investing activities.

If, however, the land or capital asset is being managed solely as a rent-generating operation, the cash inflows from rent should be classified with operating activities. (See Example C in nonauthoritative Appendix 2-1.)

2.20.2. Q—Should royalty income be evaluated in the same manner as rent income for statement of cash flows classification?

A—Yes. Royalty income is similar to rent income for cash flow reporting purposes. (See Question 2.20.1.) The asset underlying the royalties should be evaluated to determine whether it should be

treated as an investment for cash flow reporting purposes. If it should, the royalty income should be classified as an investing activity. If not, it should be classified in the residual category—operating activities.

- 2.20.3. Q—How should contributions received by an enterprise fund that are not intended for capital purposes be classified?

A—Paragraph 21b of Statement 9 defines “noncapital” grants and subsidies as noncapital financing activities. A noncapital contribution to an enterprise fund would normally be used the same as a grant or subsidy; therefore, it should be classified as a noncapital financing inflow. (See Example I in nonauthoritative Appendix 2-1.)

- 2.20.4. Q—How should commodities donated to a school lunch program be reported if they are recorded as both an *operating* expense and *nonoperating* revenue on the operating statement?

A—Commodities are noncash items that should not be presented in the statement of cash flows. However, the amount of the expense will appear as a reconciling adjustment in the reconciliation of operating income to net cash flow from operating activities. (See Illustration B, Exhibit 29, in nonauthoritative Appendix 7-1.)

- 2.20.5. Q—How should the cash flows resulting from miscellaneous income and expense be classified?

A—Miscellaneous cash flows should be included in the operating activities category even if the income or the expense is considered a nonoperating income item. The operating activities category is not limited to the cash flows resulting from operating income items. Unless the cash flows specifically meet the definition of the noncapital financing, capital and related financing, or investing activities category, they should be presented in the residual category—operating activities. If nonoperating income items, such as miscellaneous income or expense, are included in the operating activities category, an adjustment should be made to operating income in the reconciliation of operating income to net cash flow from operating activities. (See Example H in nonauthoritative Appendix 2-1.)

2.21 Investment Earnings

- 2.21.1. Q—Where should gains and losses on investments be presented?

A—Gains and losses, per se, should not be presented in the statement of cash flows. Rather, proceeds from the sale of the investments (including gains and net of losses) should be reported as a cash inflow in the investing activities category. (See also Question 2.15.7.)

- 2.21.2. Q—Investment earnings are sometimes (although rarely) included in operating income. Should the cash flows be classified as an operating activity?

A—No. Investment earnings should be classified in the investing activities category.

The statement of cash flows is not intended to replicate, on a cash basis, the operating statement. It is intended to complement the accrual-basis financial statements. The classification of cash flows provides functional information about financing and investing activities. This approach concentrates on the underlying nature of a transaction. Therefore, earnings on investments should be classified as investing activities, regardless of why the investments are made, what the earnings are used for, and where the income is reported on the operating statement. (Except that interest received on qualifying program loans should be classified as operating inflows. See Question 2.25.1.)

If investment earnings are included in operating income, the related cash flows should be presented as a deduction from operating income in the reconciliation of operating income to net cash flow from operating activities (just as depreciation is adjusted).

2.21.3. Q—How should interest on cash and cash equivalents be classified?

A—Interest earnings, by nature, are an investing activity; therefore, interest on cash and cash equivalents should be considered an investing activity. The discussion in the answer to Question 2.21.2 is relevant to this question. Even though cash and cash equivalents are not investments, the interest they earn should be classified the same as interest earned on investments. (See Examples A and H in nonauthoritative Appendix 2-1.)

2.21.4. Q—How should interest on customer deposits be classified?

A—Although customer deposit transactions are considered operating activities (see Question 2.24.1), interest earned on the deposits is an investing activity. As discussed in Question 2.21.2, regardless of whether the customer deposits are held as cash, investments, or restricted assets, the interest should be classified as investing activities. (However, distribution of the interest to customers is an operating activity because the cash flow does not meet the definition of any of the other categories.)

2.22 Taxes

2.22.1. Q—Should property taxes levied specifically for capital debt service requirements be classified as capital or noncapital financing?

A—Paragraph 24e of Statement 9 identifies property taxes received specifically to finance the acquisition, construction, or improvement of capital assets as a capital and related financing activities inflow. Property taxes levied specifically for capital debt service are indirectly financing the costs of capital acquisition, construction, or improvement by directly financing debt service. Therefore, the taxes received should be classified as capital and related financing activities. This link is necessary for symmetry in cash flow reporting.

2.22.2. Q—Would property taxes levied by a hospital district for care of indigent patients be classified as an operating activity?

A—No. Property taxes, unless levied for capital purposes, should be classified as a noncapital financing activity (Statement 9, paragraph 21d). Even if the amount levied is calculated to finance estimated costs of care of the indigent, it is not a charge for services. Instead, property tax payers are financing the care of the indigent. The nature of the receipt is a subsidy, which is defined in Statement 9 as a noncapital financing activities inflow. (See Example I in nonauthoritative Appendix 2-1.)

2.23 Investment Instruments

2.23.1. Q—How should transactions to provide for prize annuities be classified in a lottery's statement of cash flows?

A—The discussion of debt defeasance in Question 2.19.3 is relevant to the issue of lottery annuities. If, for example, a lottery purchases an annuity in a prize winner's name and the transaction meets the requirements for right of setoff, the purchase should be considered an operating activities cash outflow (as though it paid the prize winner directly). If, on the other hand, a lottery purchases a series

of investments, such as federal Treasury STRIPS, in its own name to allow it to service its prize awards as they come due, there are (at least) three cash flows to report. The purchase of the STRIPS and the proceeds received at maturity are investing activities cash flows. The cash payment to the prize winner is an operating activities cash flow. (See Example H in nonauthoritative Appendix 2-1.)

- 2.23.2. Q—A state government authority received a cash payment in exchange for the future cash flows from the collections of significant delinquent accounts receivable. How should the cash payment received be reported in the statement of cash flows?

A—If the transaction meets the criteria in paragraph 6 of Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, the receivables are considered to have been sold and the cash flows from that sale should be reported as cash flows from operations. If those criteria are not met, the transaction is considered to be a borrowing, and the cash flows would be classified in the noncapital or capital and related financing category, depending on the nature of the receivables.

- 2.23.3. Q—How should hedging transactions be presented in the statement of cash flows?

A—Although Statement 9 does not specifically refer to hedging transactions, it does provide specific guidance for classifying the cash flows. A borrowing transaction should be considered a noncapital financing activity, and an investing transaction should be considered an investing activity.

2.24 Cash Flows Not Reported on the Operating Statement

- 2.24.1. Q—How should refundable customer deposits be classified?

A—Cash flows from deposits made by customers, and the eventual repayment of the deposits, should be classified as operating activities because the transactions do not meet the definitions of either the financing activities categories or the investing activities category. (The operating activities category is the residual category.) Although the deposits are refundable, they are not loans from customers. Therefore, these are not financing activities. And although the deposits may be invested or may otherwise earn interest (see Question 2.21.4), the receipts of the deposits are not investing activities. (See Example A in nonauthoritative Appendix 2-1.)

- 2.24.2. Q—How should a lender and a borrower present the cash flows resulting from interfund loans?

A—Statement 9 presumes that interfund cash flows are noncapital financing activities. The exceptions are specific: interfund services provided and used, interfund reimbursements, and receipts for capital purposes. Therefore, interfund loan activity should be classified as noncapital financing. However, if the loan is intended to finance capital acquisition, construction, or improvement, the borrower should classify the related cash flows in the capital and related financing activities category.

For example, an interfund loan to cover a temporary cash deficiency would be considered a noncapital financing activity; however, an interfund loan for the purchase of new vehicles would be considered a capital and related financing activity.

- 2.24.3. Q—How should capital contributed by developers and other individuals be classified?

A—Cash contributed specifically to defray the cost of acquiring, constructing, or improving capital assets should be presented in the capital and related financing activities category, as required by paragraph 24c of Statement 9. Noncash transactions (such as the contribution of water and sewer

lines by a developer) should be disclosed in a schedule to the statement of cash flows. (See Questions 2.32.1 and 2.32.2; see also Examples A–C and I in nonauthoritative Appendix 2-1.)

2.24.4. Q—How should tap fees be classified?

A—The portion of a fee (tap fee, system development fee, connection fee) that is received to defray the operating costs associated with connecting a customer with a utility system and that is reported in operating income should be presented in the operating activities category. Any portion of the fee that is to be used for the specific purpose of defraying the cost of acquiring, constructing, or improving capital assets should be presented in the capital and related financing activities category. (See Question 2.24.3; see also Example A in nonauthoritative Appendix 2-1.)

2.24.5. Q—How should transactions of an education trust that is reported as an enterprise fund be classified?

A—An education trust accepts deposits from parents or others. In return for the deposits, college tuition payments will be made for students sometime in the future. The receipts should be reported as cash inflows in the operating activities category, and subsequent tuition payments also should be reported in the operating activities category. Cash flows from purchases and sales of the related investments and earnings on the investments should be classified in the investing activities category.

2.25 Program Loans

2.25.1. Q—What type of governmental loan programs, other than those for low-income housing mortgages and student loans, meet the paragraph 19 conditions for treatment as operating activities? Would a finance authority created to finance state building projects meet the provisions of paragraph 19?

A—Except for low-income housing mortgage programs and student loan programs, few, if any, programs qualify for special treatment under paragraph 19. The presumption should be to classify the making and collecting of all loans as investing activities. Paragraph 19 of Statement 9 provides an *exception* to the classification scheme set forth in the Statement by allowing the cash flows associated with making and collecting *certain* program loans to be presented in the operating activities category rather than the investing activities category. Only the cash flows associated with making and collecting the loans are affected. The underlying financing transactions should be classified as noncapital financing activities, and the investment of idle cash should be classified as investing activities.

In deciding to provide the exception in paragraph 19, the Board concluded that it would be inappropriate, in some circumstances, to classify loan activities as investing activities. The Board evaluated the characteristics of governmental loan programs as it deliberated which programs meet the intent of the paragraph 19 exception. It concluded that certain “loan programs” are the operating activities of a governmental enterprise. The loans are not typical investments because they are not necessarily intended to earn a profit. However, the Board did not intend for *all* loan programs to be classified as operating activities. The loan programs that qualify for special treatment under paragraph 19 are distinguished from other governmental loan programs because they are undertaken to provide a *direct* benefit to *individual* constituents.

There are no specific criteria in paragraph 19 of Statement 9 for determining which loan activities should be classified as operating rather than investing activities, nor is there an explanation of “direct benefits” being provided to “individual constituents.” There are only two examples of qualifying loan programs in paragraph 19—low-income housing and student loan programs. In the low-income housing mortgage program example, loans are made to individuals who might not otherwise qualify

for a home mortgage. The program is intended to directly benefit the individuals receiving the loans. Usually, the interest rate on a loan provided by this type of program is below the market rate. A student loan program provides similar direct benefits to individuals—students in need of financing their education.

The Board expected few types of loan programs or finance authorities to meet the spirit of the exception provided in paragraph 19, even if making and collecting loans are the primary operations of the enterprise. A finance authority that facilitates financing by serving as an intermediary or conduit generally would not qualify even if the project to be financed indirectly benefits the government or its constituents. For example, an authority created to finance government building projects (such as state office buildings or public university dormitories) would not qualify because the direct beneficiary is the government rather than individual constituents. In the example of a public university dormitory authority, debt is issued by the authority and the proceeds are loaned to universities for their dormitory construction projects. Although the students who eventually live in the dorms will benefit from the activity, the direct beneficiary of the dormitory authority is the university itself, which is part of the governmental financial reporting entity. Such an arrangement merely facilitates the government's financing process. The substance of the arrangement is that the government issued bonds to serve its own needs.

It is unlikely that many finance authorities operate loan programs (other than low-income housing and student loans) that qualify for the exception provided in paragraph 19. An exception might be a loan program for elderly persons who are unable to pay their property taxes. (See Examples F and G in nonauthoritative Appendix 2-1.)

2.25.2. Q—How should the loan activity of a loan program that qualifies for inclusion in the operating activities category be presented in relationship to the cash flows of the other operating activities?

A—There are no provisions in Statement 9 detailing how program loan activities should be presented in the operating activities category. The minimum level of detail required is listed in paragraph 31 of Statement 9, as amended, and is discussed in Questions 2.29.1 and 2.29.2. For example, cash receipts from customers should be presented separately from other operating cash receipts, and cash payments to suppliers should be presented separately from other operating cash payments. Because borrowers in a qualifying loan program are neither suppliers nor customers (they are direct beneficiaries of the program), it would be appropriate to separately identify cash disbursements and collections of loans. It would also be useful to separate the collection of principal from interest received. The principal and interest components of normal loan collections are separately identified in the investing activities category. (See Example G in nonauthoritative Appendix 2-1.)

2.26 Interfund Activity

2.26.1. Q—How should interfund transfers be reported in the statement of cash flows?

A—The cash portion of an interfund transfer out should be presented in the noncapital financing activities category. A governmental enterprise fund *receiving* a transfer to be used for the specific purpose of defraying the cost of acquiring, constructing, or improving capital assets, however, should classify the cash inflow as a capital and related financing activity.

Noncash transfers should not be presented within the statement of cash flows. Instead, they should be presented in a separate schedule of noncash investing, capital, and financing activities. (See Questions 2.32.1 and 2.32.2 for a discussion of noncash disclosures; see also Example B in nonauthoritative Appendix 2-1.)

2.26.2. Q—Can interfund loan activity be netted?

A—No. The preference for gross cash flow information over net cash flow information applies to interfund loan activity. Loan activity may qualify for net reporting only if the turnover is quick, the amounts are large, and the maturities are short (three months or less), based on paragraph 13 of Statement 9.

2.27 Other

2.27.1. Q—If there are cash flows associated with conduit debt (such as industrial development bonds), how should they be classified?

A—If there are cash flows through the governmental enterprise related to debt for which the enterprise does not report a liability, related cash flows should not be presented in the investing activities category or either of the financing categories. Instead, the cash flows should be presented in the residual category—operating activities. (See Question 2.15.4 for a discussion of identifying when a cash flow occurs.)

2.27.2. [Not used in GASBIG 20XX-1]

2.27.3. Q—Where should insurance proceeds be presented?

A—Insurance proceeds are specifically identified in only one place in Statement 9. In accordance with paragraph 24d of the Statement, the capital and related financing activities category includes proceeds from insurance on capital assets that are stolen, damaged, or destroyed. Other insurance proceeds should be classified in the residual category—operating activities.

2.27.4. Q—What are the factors for determining whether a grant received meets the criteria for classification as an operating activity?

A—In Statement 9, the view was adopted that grants received generally should be treated as subsidies. Capital grants should be considered capital and related financing activities, and all other grants should be considered noncapital financing activities. However, it was recognized that certain arrangements that are called “grants” appear to be contracts for services. Grants of this type should be classified as operating activities. The determination of whether a grant is, in substance, a purchase of services requires the exercise of judgment. To be classified as an operating cash inflow, the grant should finance a program that the grantee would not otherwise undertake (for example, a senior citizens’ transportation service). Therefore, the grant is not subsidizing an existing program. It reimburses the costs of a new program, whose activity is inherently part of the operations of the *grantor*. A grant with these characteristics should be considered an “operating grant” as described in paragraph 17 of Statement 9. (See Example D in nonauthoritative Appendix 2-1.)

2.27.5. Q—How should lease activities be classified in the statement of cash flows?

A—Classification of leasing transactions depends on whether the lease is a capital lease or an operating lease. (See National Council on Governmental Accounting Statement 5, *Accounting and Financial Reporting Principles for Lease Agreements of State and Local Governments*, as amended, and Statement 62, paragraphs 211–271, as amended.) The capital and related financing activities category is directly affected by capitalization policies. (See paragraph 63 of the Basis for Conclusions of Statement 9.) If a lease is a capital lease, the cash flows (including the interest

portion) should be included in the capital and related financing activities category, as an inflow in the lessor's statement of cash flows and as an outflow in the lessee's statement of cash flows. The lease transaction is essentially treated as an installment sale of a capital asset. The timing of the cash flows does not coincide with the date of the "sale," but the cash flows are, nevertheless, payments for the purchase of a capital asset. (See the discussion of noncash disclosures in Question 2.32.1.)

Cash flows resulting from an operating lease, on the other hand, usually should be classified with operating activities. The lessee's cash payments always should be presented as an operating activities outflow. The lessor's cash receipts normally should be presented as an operating activities inflow; however, Question 2.20.1 discusses factors that should be evaluated to determine whether lease revenue may be classified as an investing activities inflow. (See Examples B, C, E, H, and I in nonauthoritative Appendix 2-1.)

2.28 Content and Format Issues

2.29 Presentation of Individual Line Items

2.29.1. Q—What level of detail should be provided for individual line items in the statement of cash flows?

A—Gross cash flow information generally is required. Therefore, related transactions should not be netted. For example, bond proceeds should be reported separately from capital purchases made with the proceeds. Beyond that, the level of detail in the descriptions of the categories (in paragraphs 17–28 of Statement 9, as amended) and illustrated in nonauthoritative Appendix 2-1 provides a guideline for determining the appropriate level of detail in the statement of cash flows. For example, separating the principal and interest portions of debt service payments is considered useful.

The most specific guidance in Statement 9 as to level of detail in reporting is provided in the guidance for reporting cash flows from operating activities (paragraph 31, as amended). The discussion provides seven classes of information that serve as a minimum level of required detail.

- a. Cash receipts from customers
- b. Cash receipts from interfund services provided
- c. Other operating cash receipts, if any
- d. Cash payments to other suppliers of goods or services
- e. Cash payments to employees for services
- f. Cash payments for interfund services used, including payments "in lieu of taxes" that are payments for, and reasonably equivalent in value to, services provided or received
- g. Other operating cash payments, if any.

In all cases, governmental enterprises should provide further detail if the information would be useful.

2.29.2. Q—Should the cash outflows for payroll taxes and employee-related costs, such as fringe benefits, be reported with either "cash payments to employees for services" or "cash payments to other suppliers of goods or services," or should they be reported separately?

A—Paragraph 31 of Statement 9, as amended, requires presentation of cash flows from operating activities by major class, and lists a minimum of seven classes. (See Question 2.29.1.) One of the major classes is "cash payments to employees for services." Statement 9 does not provide a definition for this or any other of the major classes referred to in paragraph 31, as amended. It is reasonable to group cash payments for payroll taxes and fringe benefits with cash payments to

employees, even though the cash is not paid directly to the employees. Payroll taxes and fringe benefits are paid on behalf of employees and are an integral part of employment costs.

On the other hand, further detail is encouraged if it would be useful. Therefore, it may be helpful to present cash flows for payroll taxes and fringe benefits *separately* from payments to employees if the amounts are significant.

- 2.29.3. Q—If an internal service fund purchases supplies from both vendors and other funds of the primary government, should it report its purchases from other funds separately from its purchases from vendors?

A—Paragraph 31 of Statement 9, as amended, states that interfund services provided and used should be presented separately from other operating transactions. The intent was to highlight interfund activity. Although the cash flows between the internal service fund and other funds of the government may seem identical to transactions with outside suppliers or vendors, the fact that the activity is “intra-entity” is noteworthy.

- 2.29.4. Q—If a state governmental enterprise (such as a workers’ compensation fund) has receipts from within the state’s entity and also from local government participants, should a distinction be made between “customers” inside and outside the entity?

A—Yes. Interfund activity should be distinguished from external operating transactions. As discussed in Question 2.29.3, paragraph 31 of Statement 9, as amended, states that cash flows from interfund services provided and used should be presented separately from other operating transactions. (See Example J in nonauthoritative Appendix 2-1.) However, there is no requirement to separate the cash flows with discretely presented component units from those involving external parties. Note, however, that paragraph 128 of Statement 34 requires disclosure of the nature and amount of significant transactions between the primary government and each major component unit.

- 2.29.5. Q—Should debt service interest payments that are capitalized be reported in the capital and related financing activities category as an outflow for interest on capital debt or as part of the capital acquisition outflow?

A—All interest payments associated with “capital debt” should be presented in the capital and related financing activities category as “cash payments to lenders and other creditors for interest.” The presentation of cash payments for interest should not be affected by the transaction’s presentation on the operating statement or the statement of net position/balance sheet. The fact that the amount of the cash flow is capitalized does not change the fact that the cash was paid to a lender for interest.

- 2.29.6. Q—Under the direct method for reporting cash flows from operating activities, are governments required to separately report transactions with discretely presented component units?

A—No. Paragraph 31 of Statement 9, as amended, requires separate reporting of cash flows from interfund services provided and used but does not require a similar distinction for transactions with component units. Governments may provide those additional details but are not required to do so. However, paragraph 128 of Statement 34 requires disclosure of the nature and amount of significant transactions between the primary government and each major component unit.

2.30 Reconciliation of Operating Income to Net Cash Flow from Operating Activities

2.30.1. Q—Can the reconciliation of operating income to net cash flow from operating activities be presented in notes to the financial statements?

A—No. The reconciliation is a requirement of cash flow reporting and should be presented as part of the statement of cash flows, as a separate schedule (preferably on the same page). Paragraph 67 of the Statement 9 Basis for Conclusions discusses this topic.

2.30.2. Q—In reconciling operating income to operating cash flows, should the changes in all asset and liability accounts and in deferred outflows of resources and deferred inflows of resources be reconciled?

A—Only those asset, deferred outflows of resources, liability, and deferred inflows of resources accounts that affect operating cash flow items should be included in the reconciliation of operating income to net cash flow from operating activities. For example, if a governmental enterprise holds a receivable related to grants from another government, that receivable should not affect cash flows from operating activities; therefore, it should not be a reconciling item. The receivable does, however, have an effect on the noncapital financing activities presentation (assuming the grant is an operating subsidy and not a capital grant). Grant revenues reported as nonoperating income in the flows statement should be adjusted by the receivable amount to arrive at the actual cash flows from the grant.

2.30.3. [Not used in GASBIG 20XX-1]

2.31 Articulation to the Statement of Net Position/Balance Sheet

2.31.1. Q—Do the requirements of Statements 3 and 40, as amended, affect the articulation of the statement of cash flows to the statement of net position/balance sheet?

A—No. As discussed in Question 2.14.2, because Statement 9, as amended, addresses financial statement display and Statements 3 and 40, as amended, address disclosure in the notes to the financial statements, Statement 9, as amended, takes precedence in issues of financial reporting display. Statement 9, as amended, mandates articulation between the statement of cash flows and the statement of net position/balance sheet, possibly requiring changes to certain statement of net position/balance sheet presentations. Paragraph 8 of Statement 9 states, “The total amounts of cash and cash equivalents at the beginning and end of the period shown in the statement of cash flows should be easily traceable to similarly titled line items or subtotals shown in the statements of financial position as of those dates.” Therefore, it would be inconsistent to include in the caption “cash and cash equivalents” items that do not meet the definition.

Statements 3 and 40, as amended, do not require articulation between the required disclosures and the statement of net position/balance sheet. However, some do trace the balances in the Statements 3 and 40 disclosures, as amended, to the statement of net position/balance sheet presentation. Because Statement 9, as amended, changes that presentation, a reconciliation may be necessary when tracing these disclosures to the statement of net position/balance sheet. (See Question 1.26.6.)

2.31.2. Q—Is it possible to trace cash and cash equivalent balances to the statement of net position/balance sheet if participation in a cash management pool is reported as “equity in pooled cash” rather than as “cash and cash equivalents”?

A—Yes. Rather than require cash and cash equivalents per the statement of cash flows to be the same as similarly titled line items in the statement of net position/balance sheet, paragraph 8 requires that cash and cash equivalents be *easily traceable* to similarly titled line items in the statements of financial position. This flexibility was provided to allow restricted cash and cash equivalents to be presented separately in the statement of net position/balance sheet. A reconciliation is not necessary if a reader is able to easily trace the statement of cash flows amounts to similarly titled line items in the statement of net position/balance sheet.

This flexibility also is useful for various other articulation problems, such as the labeling conflict in this question. Because the equity in the pooled cash meets the definition of cash, it may be included in the balance of cash and cash equivalents. If it is labeled as “equity in pooled cash” on the statement of net position/balance sheet, a reader may not be able to easily trace from the statement of cash flows to the statement of net position/balance sheet. Therefore, a reconciliation may be provided—for example, at the bottom of the statement of cash flows—tracing the amounts per the statement of cash flows to the appropriate statement of net position/balance sheet line items. (See Example A in nonauthoritative Appendix 2-1.)

2.31.3. [Not used in GASBIG 20XX-1]

2.32 Noncash Investing, Capital, and Financing Activities

2.32.1. Q—When is disclosure of noncash information required?

A—Paragraph 37 of Statement 9 requires that “information about all investing, capital, and financing activities of a governmental enterprise during a period that affect recognized assets or liabilities but do not result in cash receipts or cash payments in the period should be reported.” Disclosure of noncash information is required if a transaction meets *all* of these three characteristics:

- a. *Is the transaction noncash?* Questions 2.15.1–2.15.6 provide guidance on identifying a cash flow. Some transactions include cash and noncash components. Only the cash portion of the transaction should be presented in the statement of cash flows. The noncash portion should be evaluated further.
- b. *Does the transaction affect recognized assets or liabilities?* Noncash transactions that result in the recognition of assets and liabilities should be analyzed. Changes in the balance of an asset or a liability that are not attributable to cash transactions should be considered noncash transactions. For example, when an enterprise fund enters into a capital lease for a building, a noncash transaction occurs because a capital lease obligation and the building are recorded in the statement of net position. The inception of an *operating* lease, on the other hand, requires no disclosure because there is no effect on the statement of net position.
- c. *Is the transaction an investing, capital, or financing activity?* A noncash transaction should be disclosed only when it (had it been a cash transaction) meets the definition of the investing, capital and related financing, or noncapital financing activities category. For example, a capital lease transaction meets the definition of a capital and related financing activity. However, a customer account receivable balance that was used to offset an account payable to that customer is an operating activity and is not required to be disclosed. (See Examples A–D and G–I in nonauthoritative Appendix 2-1.)

Examples of noncash transactions include acquiring capital assets by assuming directly related liabilities, such as purchasing a building by incurring a mortgage to the seller or purchasing on credit and taking delivery of vehicles in the current period and paying for them in a future period, obtaining a capital asset by entering into a capital lease, refunding bond proceeds delivered directly to an

irrevocable trust, changes in fair value of investments or derivative instruments, receiving donated capital assets, and transfers of capital assets between funds.

2.32.2. Q—How should noncash transactions be reported?

A—Paragraph 37 of Statement 9 states that noncash information “should be presented in a separate schedule, which may be in either a narrative or a tabular format, and it should clearly describe the cash and noncash aspects of transactions involving similar items. The schedule may be presented, if space permits, on the same page as the statement of cash flows.” Therefore, the format for presenting the noncash disclosures is flexible. For example, a governmental enterprise with only one transaction to disclose may find it most effective to describe the transaction in a sentence or two. Another governmental enterprise, with several noncash financing activities, may find it useful to arrange the information in a column. Whatever format is chosen, the disclosures should be made in a schedule to the statement of cash flows (preferably on the same page). (See Examples A–D and G–I in nonauthoritative Appendix 2-1.) As discussed in paragraph 68 of the Basis for Conclusions of Statement 9, the disclosures should not be separated from the statement of cash flows by being presented in the notes to the financial statements.

Appendix 2-1

EXAMPLES OF STATEMENTS OF CASH FLOWS

This nonauthoritative appendix provides illustrations of how Statement 9, as amended, might be applied for a variety of proprietary funds or business-type activities. The examples are designed to illustrate specific issues addressed in the Questions and Answers section of this chapter. The questions may include references to particular examples that illustrate the issue addressed in the question. As a cross-reference, examples in this appendix include appropriate footnote references to specific questions in the chapter.

Examples A–J are not as comprehensive as the illustration provided in nonauthoritative Appendix B of Statement 9 (included as Example K in this appendix). That example includes a discussion of relevant transactions and the other basic financial statements. Examples A–J include only the statement of cash flows and supporting schedules.

The following examples are provided:

- A. Water and Sewer Utility Fund
- B. Gas Utility Fund
- C. Airport Authority
- D. Transit Authority
- E. State Offices Building Authority
- F. Development Finance Authority G. Student Loan Program
- H. Lottery Fund
- I. County Hospital Authority
- J. Workers' Compensation Insurance Fund
- K. Appendix B from Statement 9, as amended—Illustrative Statement of Cash Flows

Example A

**Water and Sewer Utility Fund
Statement of Cash Flows
for the Year Ended April 30, 200X**

Cash flows from operating activities:		
Cash received from customers	\$ 5,100	
Cash payments to employees for services	(1,900)	
Cash payments to suppliers for goods and services	(3,300)	
Cash paid to general fund for supplies	(130)	
Customer deposits received ^a	60	
Customer deposits returned ^a	(40)	
Cash received from operating portion of tap fees ^b	200	
Net cash used for operating activities	\$ (10)	
Cash flows from noncapital financing activities:		
Transfer from general fund	450	
Net cash provided by noncapital financing activities	450	
Cash flows from capital and related financing activities:		
Net proceeds from bonds issued to refund capital debt ^c	5,200	
Principal paid on capital debt	(4,300)	
Interest paid on capital debt	(800)	
Acquisition of capital assets	(2,300)	
Proceeds from sale of capital assets	900	
Tap fees in excess of connection costs ^b	200	
Cash received from developers for capital purposes ^d	1,000	
Net cash used for capital and related financing activities	(100)	
Cash flows from investing activities:		
Interest on cash and cash equivalents ^e	30	
Interest and dividends from investments	180	
Proceeds from sales and maturities of investments	3,000	
Purchases of investments	(2,500)	
Net cash provided by investing activities	710	
Net increase in cash and cash equivalents	1,050	
Cash and cash equivalents at beginning of year	1,200	
Cash and cash equivalents at end of year	\$2,250	

^aSee Question 2.24.1.

^bSee Question 2.24.4.

^cSee Questions 2.15.2, 2.15.3, and 2.19.3.

^dSee Question 2.24.3.

^eSee Question 2.21.3.

Reconciliation of cash and cash equivalents to the statement of net position:

Cash and cash equivalents in current assets	\$ 200
Equity in pooled cash ^f	1,000
Restricted cash and cash equivalents	1,050
Total cash and cash equivalents	<u>\$ 2,250</u>

[**Note:** This reconciliation is presented to trace beginning and ending cash and cash equivalents to similarly titled line items on the statement of net position.]

Reconciliation of operating loss to net cash used for operating activities:

Operating loss		\$ (740)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	\$ 950	
Revenue reduced for uncollectible accounts	10	
Change in assets and liabilities:		
Increase in accounts receivable	(25)	
Decrease in inventory	15	
Decrease in prepaid insurance	40	
Decrease in accounts payable	(60)	
Decrease in salaries and wages payable	(200)	
Decrease in accrued compensated absences	(20)	
Increase in customer deposits	20	
Total reconciling adjustments		<u>730</u>
Net cash used for operating activities		<u>\$ (10)</u>

Noncash capital and financing activities:⁹

In November, the Water and Sewer Utility Fund disposed of miscellaneous equipment as scrap. The undepreciated cost of the equipment was recorded as a loss—\$850.

^fSee Question 2.31.2.

⁹See Question 2.32.1 and 2.32.2.

Example B

**Gas Utility Fund
Statement of Cash Flows
for the Year Ended April 30, 200X**

Cash flows from operating activities:		
Cash received from customers	\$ 285,000	
Cash payments to employees for services	(66,200)	
Cash payments to suppliers for goods and services	(97,800)	
Cash payment to gas supplier for take-or-pay contract	(9,800)	
Cash payment to general fund for operating lease ^a	(700)	
Net cash provided by operating activities	\$ 110,500	
Cash flows from noncapital financing activities:		
Cash payment (subsidy) to city	(80,500)	
Transfer from the Water Utility Fund ^b	1,000	
Negative cash balance implicitly financed ^c	500	
Net cash used for noncapital financing activities	(79,000)	
Cash flows from capital and related financing activities:		
Construction and improvement of plant	(300,000)	
Debt principal payments	(54,000)	
Debt interest payments	(6,000)	
Contributions in aid of construction from developers ^d	40,000	
Net cash used for capital and related financing activities	(320,000)	
Cash flows from investing activities:		
Interest and dividends on investments	58,500	
Proceeds from sales and maturities of investments	725,000	
Purchases of investments	(500,000)	
Net cash provided by investing activities	283,500	
Net decrease in cash and cash equivalents	(5,000)	
Cash and cash equivalents at beginning of year	5,000	
Cash and cash equivalents at end of year	\$ 0	

^aSee Question 2.27.5.

^bSee Question 2.26.1.

^cSee Question 2.11.3.

^dSee Question 2.24.3.

**Gas Utility Fund
Statement of Cash Flows
for the Year Ended April 30, 200X
(continued)**

Reconciliation of operating income to net cash provided by operating activities:

Operating income		\$ 16,300
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	\$ 95,000	
Change in assets and liabilities:		
Increase in accounts receivable	(1,200)	
Decrease in inventory	800	
Increase in accounts payable	2,000	
Decrease in accrued wages	<u>(2,400)</u>	
Total reconciling adjustments		<u>94,200</u>
Net cash provided by operating activities		<u><u>\$ 110,500</u></u>

Noncash financing activities:^e

In addition to a cash transfer of \$1,000, the Gas Utility Fund received certain capital assets of the Water Utility Fund. The net book value of the assets at the time of the transfer was \$13,000.

The net increase in fair value of the Gas Utility Fund's investments was \$14,665.

^eSee Questions 2.32.1 and 2.32.2.

Example C

**Airport Authority
Statement of Cash Flows
for the Year Ended September 30, 200X**

Cash flows from operating activities:		
Cash received from tenants for rent ^a	\$ 98,900	
Cash received from customers	10,004	
Cash paid to suppliers for goods and services	(30,752)	
Cash paid to employees for services	(16,930)	
Net cash provided by operating activities		\$ 61,222
Cash flows from noncapital financing activities:		
Operating grants received	218	
Net cash provided by noncapital financing activities		218
Cash flows from capital and related financing activities:		
Net proceeds from issuance of long-term debt ^d	107,812	
Principal payments—bonds and notes	(48,605)	
Interest payments—bonds and notes	(12,962)	
Capital lease payments ^c	(46)	
Proceeds from sale of capital assets	303	
Purchases of capital assets	(6,404)	
Construction of runway	(274,536)	
Passenger facility charges	4,210	
Capital contributed by airlines and federal and state governments ^d	18,111	
Net cash used for capital and related financing activities		(212,117)
Cash flows from investing activities:		
Purchases of investment securities	(683,639)	
Proceeds from sales and maturities of investment securities	848,968	
Interest and dividends on investments	14,869	
Net cash provided by investing activities		180,198
Net increase in cash and cash equivalents		29,521
Cash and cash equivalents at beginning of year		13,084
Cash and cash equivalents at end of year		<u>\$ 42,605</u>

^aSee Question 2.20.1.

^bSee Question 2.15.2.

^cSee Question 2.27.5.

^dSee Question 2.24.3.

**Airport Authority
Statement of Cash Flows
for the Year Ended September 30, 200X
(continued)**

Reconciliation of cash and cash equivalents to the statement of net position:

Cash and cash equivalents—current assets	\$14,716
Cash and cash equivalents—restricted assets	<u>27,889</u>
Total cash and cash equivalents	<u>\$42,605</u>

[Note: This reconciliation is likely not necessary. A reader probably would be able to easily trace the beginning and ending cash and cash equivalents to similarly titled line items on the statement of net position.]

Reconciliation of operating income to net cash provided by operating activities:

Operating income	\$36,053
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	19,960
Change in assets and liabilities:	
Increase in accounts receivable	(3,261)
Decrease in prepaid expenses	288
Increase in accounts payable	1,921
Increase in accrued expenses	557
Increase in advances	4,968
Decrease in deposits from tenants	(211)
Increase in advance rent	947
Net cash provided by operating activities	<u>\$61,222</u>

Noncash investing, capital, and financing activities:^e

Capital lease obligations of \$2,179 were incurred when the Airport Authority entered into leases for new telephone equipment and motor vehicles.

The increase in the fair value of the Airport Authority's investments was \$17,291.

^eSee Questions 2.32.1 and 2.32.2.

Example D

**Transit Authority
Statement of Cash Flows
for the Year Ended December 31, 200X**

Cash flows from operating activities:		
Cash received from passengers and service contracts	\$ 20,700	
Operating grant received from Department of Transportation for ridership pattern study ^a	6,500	
Cash payments to employees for services	(62,600)	
Cash payments to suppliers for goods and services	<u>(36,500)</u>	
Net cash used for operating activities		\$(71,900)
Cash flows from noncapital financing activities:		
Subsidies received from federal grants	8,900	
Subsidies received from local government	56,850	
Property taxes received	<u>7,650</u>	
Net cash provided by noncapital financing activities		73,400
Cash flows from capital and related financing activities:		
Acquisition and construction of capital assets	(29,000)	
Proceeds from sale of capital assets	100	
Capital grants received	<u>20,680</u>	
Net cash used for capital and related financing activities		(8,220)
Cash flows from investing activities:		
Interest received	10,650	
Proceeds from sales and maturities of investments	15,000	
Purchases of investments	<u>(12,100)</u>	
Net cash provided by investing activities		<u>13,550</u>
Net increase in cash and cash equivalents		<u>6,830</u>
Cash and cash equivalents at beginning of year		10,470
Cash and cash equivalents at end of year		<u>\$ 17,300</u>

Reconciliation of operating loss to net cash used for operating activities:

Operating loss	\$(76,600)
Adjustments to reconcile operating loss to net cash used for operating activities:	
Depreciation	10,300
Change in assets and liabilities:	
Increase in accounts receivable	(440)
Increase in inventory of fuel	(3,160)
Decrease in accrued payroll	(3,200)
Increase in accrued compensated absences	1,200
Net cash used for operating activities	<u><u>\$(71,900)</u></u>

Noncash capital and financing activities:^b

The Transit Authority issued capital bonds to refund debt issued in 1996.^c The \$42,000 proceeds were deposited immediately into an irrevocable trust for the defeasance of \$40,000 of outstanding revenue bond principal and \$1,200 of interest.

^aSee Question 2.27.4.

^bSee Questions 2.32.1 and 2.32.2.

^cSee Question 2.15.3.

Example E

State Offices Building Authority
Statement of Cash Flows
for the Year Ended June 30, 200X

Cash flows from operating activities:		
Cash received from fees	\$ 450	
Cash payments to employees for services	(1,100)	
Cash payments to suppliers for goods and services	<u>(980)</u>	
Net cash used for operating activities		\$ (1,630)
Cash flows from capital and related financing activities:		
Proceeds from bonds ^a	90,000	
Bond issuance costs paid ^a	(1,000)	
Principal paid on capital debt	(12,900)	
Interest paid on capital debt	(900)	
Capital lease payments received (including \$1,000 interest) ^b	13,800	
Construction of capital assets	<u>(27,550)</u>	
Net cash provided by capital and related financing activities		61,450
Cash flows from investing activities:		
Interest and dividends received	10,100	
Proceeds from sales of investments	35,000	
Purchases of investments	<u>(130,000)</u>	
Net cash used for investing activities		(84,900)
Net decrease in cash and cash equivalents		<u>(25,080)</u>
Cash and cash equivalents at beginning of year		93,300
Cash and cash equivalents at end of year		<u><u>\$ 68,220</u></u>
Reconciliation of operating loss to net cash used for operating activities:		
Operating loss	\$ (1,025)	
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	500	
Interest on lease receivable	(1,100)	
Change in assets and liabilities:		
Increase in fees receivable	(50)	
Increase in accounts payable	45	
Net cash used for operating activities	<u><u>\$ (1,630)</u></u>	

^aSee Question 2.15.2.

^bSee Question 2.27.5.

Example F

**Development Finance Authority
Statement of Cash Flows
for the Year Ended June 30, 200X**

Cash flows from operating activities:		
Cash received from fees	\$ 1,500	
Cash payments to employees for services	(1,420)	
Cash payments to suppliers for goods and services	<u>(200)</u>	
Net cash used for operating activities		\$ (120)
Cash flows from noncapital financing activities:		
Net bond proceeds received ^a	30,000	
Principal payment on debt	(3,000)	
Interest paid	<u>(200)</u>	
Net cash provided by noncapital financing activities		26,800
Cash flows from investing activities:		
Loans issued ^b	(30,000)	
Collections of loan principal ^b	4,000	
Interest received on loans ^b	750	
Purchases of investments	(5,000)	
Proceeds from sales and maturities of investments	5,500	
Interest and dividends on investments	<u>540</u>	
Net cash used for investing activities		<u>(24,210)</u>
Net increase in cash and cash equivalents		2,470
Cash and cash equivalents at beginning of year		180
Cash and cash equivalents at end of year		<u><u>\$ 2,650</u></u>

Reconciliation of operating income to net cash used for operating activities:

Operating income	\$ 810
Adjustments to reconcile operating income to net cash used for operating activities:	
Interest income from loans	(750)
Change in assets and liabilities:	
Increase in accounts receivable	(80)
Decrease in accounts payable	<u>(100)</u>
Net cash used for operating activities	<u><u>\$ (120)</u></u>

^aSee Question 2.15.2.

^bSee Question 2.25.1; this loan program does not qualify for classification in the operating activities category because it does not directly benefit individual constituents.

Example G

**Student Loan Program
Statement of Cash Flows
for the Year Ended June 30, 200X**

Cash flows from operating activities:		
Collections of student loan principal ^a	\$ 28,820	
Interest received from borrowers ^a	6,430	
Student loans issued ^a	(18,000)	
Fees and miscellaneous receipts	1,000	
Cash payments to suppliers for goods and services	(2,070)	
Cash payments to employees for services	(6,420)	
Net cash provided by operating activities		\$ 9,760
Cash flows from noncapital financing activities:		
Principal paid on long-term debt	(8,890)	
Interest paid on long-term debt	(740)	
Net cash used for noncapital financing activities		(9,630)
Cash flows from investing activities:		
Interest and dividends on investments	29,500	
Proceeds from sales of investments	85,400	
Purchases of investments	(93,000)	
Net cash provided by investing activities		<u>21,900</u>
Net increase in cash and cash equivalents		<u>22,030</u>
Cash and cash equivalents at beginning of year		<u>78,540</u>
Cash and cash equivalents at end of year		<u><u>\$ 100,570</u></u>
 Reconciliation of operating loss to net cash provided by operating activities:		
Operating loss		\$ (240)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	\$ 800	
Change in assets and liabilities:		
Decrease in loans receivable	10,820	
Increase in interest receivable	(1,000)	
Decrease in accrued wages payable	(620)	
Total adjustments		<u>10,000</u>
Net cash provided by operating activities		<u><u>\$ 9,760</u></u>

Noncash investing, capital, and financing activities:^b

Five personal computers with a fair value of \$8,750 were donated to the Student Loan Program at the end of the fiscal year.^c

The decrease in the fair value of the Student Loan Program's investments was \$1,234.

^aSee Questions 2.25.1 and 2.25.2; this loan program qualifies for classification in the operating activities category because it provides student loans.

^bSee Questions 2.32.1 and 2.32.2.

^cThe fair value of the donated assets exceeds the loan program's capitalization threshold.

Example H

**Lottery Fund
Statement of Cash Flows
for the Year Ended June 30, 200X**

Cash flows from operating activities:		
Cash received from players and agents (net of \$18,060 commissions retained by agents and \$13,590 instant winner cash prizes paid by agents)	\$ 77,155	
Cash received from multi-state lottery for grand prize winners	6,245	
Cash from other sources ^a	39	
Cash payments for prizes	(39,177)	
Cash paid to multi-state lottery grand prize winners	(6,245)	
Cash payments to employees for services	(7,905)	
Cash payments to suppliers for goods and services	<u>(3,440)</u>	
Net cash provided by operating activities		\$ 26,672
Cash flows from noncapital financing activities:		
Cash payments to general fund	<u>(26,238)</u>	
Net cash used for noncapital financing activities		(26,238)
Cash flows from capital and related financing activities:		
Acquisition of equipment	(7)	
Capital lease payment ^b	<u>(36)</u>	
Net cash used for capital and related financing activities		(43)
Cash flows from investing activities:		
Interest income on cash and cash equivalents ^c	4	
Annuity payments received from insurance companies ^d	1,093	
Purchases of annuities in the lottery's name ^d	<u>(1,212)</u>	
Net cash used for investing activities		<u>(115)</u>
Net increase in cash and cash equivalents		276
Cash and cash equivalents at beginning of year		<u>109</u>
Cash and cash equivalents at end of year		<u><u>\$ 385</u></u>

^aSee Question 2.20.5.

^bSee Question 2.27.5.

^cSee Question 2.21.3.

^dSee Question 2.23.1.

Lottery Fund
Statement of Cash Flows
for the Year Ended June 30, 200X
(continued)

Reconciliation of operating income to net cash provided by operating activities:

Operating income		\$ 26,686
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation	\$ 154	
Miscellaneous income ^e	39	
Changes in assets and liabilities:		
Decrease in accounts receivable	212	
Increase in inventory	(114)	
Increase in prepaid expenses	(88)	
Decrease in unpaid prize liability	(219)	
Increase in accounts payable	56	
Increase in accrued liabilities	6	
Decrease in advances	(60)	
Total adjustments	<u>(14)</u>	
Net cash provided by operating activities		<u>\$ 26,672</u>

Noncash capital and financing activities:^f

The Lottery Fund entered into a \$378,000 capital lease for ticket-issuing equipment.

^eSee Question 2.20.5.

^fSee Questions 2.32.1 and 2.32.2.

Example I

**County Hospital Authority
Statement of Cash Flows
for the Year Ended December 31, 200X**

Cash flows from operating activities:		
Cash received from patients and third-party payors	\$ 7,612	
Cash payments to employees for services	(3,799)	
Cash payments to suppliers for goods and services	(2,991)	
Other cash received	400	
Net cash provided by operating activities		\$ 1,222
Cash flows from noncapital financing activities:		
Property taxes received ^a	180	
Unrestricted gifts received ^b	200	
Net cash provided by noncapital financing activities		380
Cash flows from capital and related financing activities:		
Acquisition of capital assets	(2,296)	
Principal paid on long-term debt	(150)	
Interest paid on long-term debt	(6)	
Capital debt service subsidy from county ^c	156	
Gifts restricted for capital purposes ^d	1,120	
Capital lease payment ^e	(354)	
Net cash used for capital and related financing activities		(1,530)
Cash flows from investing activities:		
Purchases of investments	(500)	
Proceeds from sales of investments	400	
Interest and dividends received	130	
Net cash provided by investing activities		30
Net increase in cash and cash equivalents		102
Cash and cash equivalents at beginning of year		833
Cash and cash equivalents at end of year		\$ 935

^aSee Question 2.22.2.

^bSee Question 2.20.3.

^cSee Question 2.19.4.

^dSee Question 2.24.3.

^eSee Question 2.27.5.

**County Hospital Authority
Statement of Cash Flows
for the Year Ended December 31, 200X
(continued)**

Reconciliation of operating income to net cash provided by operating activities:

Operating income	\$ 1,170
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	585
Revenue reduced for uncollectible accounts	765
Changes in assets and liabilities:	
Increase in accounts receivable	(1,047)
Increase in inventory and prepaid expenses	(63)
Decrease in accounts payable	(126)
Decrease in wages and payroll taxes payable	(5)
Increase in accrued compensated absences	23
Decrease in estimated third-party settlements and Medicare advances	(80)
Net cash provided by operating activities	<u>\$ 1,222</u>

Noncash investing, capital, and financing activities:^f

In March, the County Hospital Authority acquired all of the assets of a small medical laboratory adjacent to the hospital in exchange for assuming the mortgage on the building and providing \$1,000 cash. The principal balance of the mortgage assumed was \$39,000.

The decrease in the fair value of the County Hospital Authority's investments was \$100.

^fSee Questions 2.32.1 and 2.32.2.

Example J

**Workers' Compensation Insurance Fund
Statement of Cash Flows
for the Year Ended June 30, 200X**

Cash flows from operating activities:		
Cash received for premiums within the state's entity ^a	\$ 24,876	
Cash received from others for premiums ^a	78,426	
Cash payments to suppliers for goods and services	(3,331)	
Cash payments to employees for services	(5,102)	
Cash payments for claims	(115,543)	
Other cash received	96	
Net cash used for operating activities		\$ (20,578)
Cash flows from noncapital financing activities:		
Transfers to other funds	(2,577)	
Transfers from other funds	13,410	
Net cash provided by noncapital financing activities		10,833
Cash flows from capital and related financing activities:		
Proceeds from sale of capital assets	782	
Acquisition of capital assets	(1,046)	
Net cash used for capital and related financing activities		(264)
Cash flows from investing activities:		
Purchases of investments	(11,004)	
Proceeds from sales and maturities of investments	27,912	
Interest and dividends on investments	4,622	
Net cash provided by investing activities		21,530
Net increase in cash and cash equivalents		11,521
Cash and cash equivalents at beginning of year		37,074
Cash and cash equivalents at end of year		\$ 48,595
 Reconciliation of operating loss to net cash used for operating activities:		
Operating loss		\$ (251,285)
Adjustments to reconcile operating loss to net cash used for operating activities:		
Depreciation	\$ 121	
Changes in assets and liabilities:		
Increase in accounts receivable	(2,262)	
Decrease in amounts due from other funds	2,633	
Increase in estimated claims	230,215	
Total adjustments		230,707
Net cash used for operating activities		\$ (20,578)

^aSee Question 2.29.4.

Example K

Appendix B from Statement 9, as Amended—Illustrative Statement of Cash Flows

This example provides sample financial statements to illustrate the preparation of a statement of cash flows for a hypothetical water and sewer enterprise fund. Also included in this example are a comparative statement of net position for the water and sewer fund; a statement of revenues, expenses, and changes in fund net position; and two paragraphs with explanatory details coded for easy reference. The changes in the statement of net position amounts for the year are explained and coded¹ in Schedule I to provide a crosswalk to the statement of cash flows. Schedule II reconciles certain change statement amounts with corresponding amounts in the statement of cash flows. These illustrative statements are intended as examples only and may provide more or less detail than is most useful for a particular governmental enterprise.

¹The letters (A–M) correspond to the coding on the statement of cash flows and the reconciliation of operating income to net cash provided by operating activities; the numbers (1–14) correspond to the coding on the statement of net position.

**Water and Sewer Fund
Statement of Cash Flows
for the Year Ended June 30, 20X2**

Cash flows from operating activities:		
Cash received from customers	\$ 912,000	
Cash payments to suppliers for goods and services	(450,000)	
Cash payments to employees for services	(300,575)	
Other operating revenues	<u>15,075</u>	
Net cash provided by operating activities		\$ 176,500
Cash flows from noncapital financing activities:		
Net borrowings (repayments) under revolving loan arrangement	(20,000) ^J	
Interest paid on revolving loan	(1,500) ^I	
Operating grants received	100,000	
Payment in lieu of taxes to the general fund	(50,000)	
Transfers out to other funds	<u>(75,000)</u>	
Net cash used for noncapital financing activities		(46,500)
Cash flows from capital and related financing activities:		
Proceeds from sale of revenue bonds	250,000 ^L	
Acquisition and construction of capital assets	(350,000) ^F	
Principal paid on revenue bond maturities and equipment contracts	(75,000) ^{K,M}	
Interest paid on revenue bonds and equipment contracts	(33,500) ^H	
Proceeds from sale of equipment	10,000	
Capital contributed by subdividers	<u>60,000</u>	
Net cash used for capital and related financing activities		(138,500)
Cash flows from investing activities:		
Purchase of investment securities	(125,000) ^C	
Proceeds from sale and maturities of investment securities	75,000 ^D	
Interest and dividends on investments	<u>9,000^E</u>	
Net cash used in investing activities		(41,000)
Net decrease in cash and cash equivalents		(49,500)
Cash and cash equivalents at beginning of year		<u>175,600</u>
Cash and cash equivalents at end of year		<u>\$ 126,100</u>
Reconciliation of operating income to net cash provided by operating activities:		
Operating income (loss)		\$ (60,500)
Adjustments to reconcile operating loss to net cash provided by operating activities:		
Depreciation	\$ 245,000 ^G	
Revenue reduced for uncollectible accounts	2,000 ^B	
Change in assets and liabilities:		
Increase in accounts receivable	(15,000) ^A	
Decrease in inventory	2,000	
Decrease in prepaid expenses	500	
Increase in accounts payable	<u>2,500</u>	
Total adjustments		<u>237,000</u>
Net cash provided by operating activities		<u>\$ 176,500</u>

Noncash capital and financing activities:

Shortly before the end of the fiscal year, the government entered into a time-pay agreement to purchase office equipment costing \$7,500 for the Water and Sewer Fund. There was no down payment, and no monthly installments were made before year-end.

Disclosure of accounting policy:

For purposes of the Water and Sewer Fund statement of cash flows, the government considers all highly liquid investments (including restricted assets) with a maturity of three months or less when purchased to be cash equivalents. (*Note:* This disclosure should be included in the summary of significant accounting policies.)

**Water and Sewer Fund
Statement of Net Position
June 30, 20X2 and 20X1**

	<u>6/30/X2</u>	<u>6/30/X1</u>	Change (See Schedule I)
Assets:			
<i>Current assets:</i>			
Cash and cash equivalents	\$ 125,100	\$ 173,100	\$ (48,000) ¹
Customer accounts receivable (net of allowance for uncollectibles of \$7,500 and \$5,500)	96,500	83,500	13,000 ²
Inventory	46,000	48,000	(2,000) ³
Prepaid expenses	600	1,100	(500) ³
Total current assets	<u>268,200</u>	<u>305,700</u>	<u>(37,500)</u>
<i>Noncurrent assets:</i>			
Restricted assets:			
Cash and cash equivalents	1,000	2,500	(1,500) ¹
Investments	110,000	60,000	50,000 ⁴
Interest receivable	1,000	1,500	(500) ⁵
Property, plant, and equipment, at cost	7,066,200	6,714,200	352,000 ⁶
Less accumulated depreciation	<u>(3,238,000)</u>	<u>(2,995,000)</u>	<u>(243,000)⁷</u>
Property, plant, and equipment, net	<u>3,828,200</u>	<u>3,719,200</u>	<u>109,000</u>
Total noncurrent assets	<u>3,940,200</u>	<u>3,783,200</u>	<u>157,000</u>
Total assets	<u>4,208,400</u>	<u>4,088,900</u>	<u>119,500</u>
Liabilities:			
<i>Current liabilities:</i>			
Accounts payable and accrued expenses	68,000	65,500	2,500 ³
Accrued interest payable	1,250	750	500 ⁸
Revolving loan	3,000	23,000	(20,000) ⁹
Equipment contracts payable	2,500	2,500	0 ¹⁰
Revenue bonds	195,000	185,000	10,000 ¹¹
Total current liabilities	<u>269,750</u>	<u>276,750</u>	<u>(7,000)</u>
<i>Noncurrent liabilities:</i>			
Equipment contracts payable	5,000	7,500	(2,500) ¹⁰
Revenue bonds	380,000	205,000	175,000 ¹¹
Total noncurrent liabilities	<u>385,000</u>	<u>212,500</u>	<u>172,500</u>
Total liabilities	<u>654,750</u>	<u>489,250</u>	<u>165,500</u>
Net position:			
Net investment in capital assets	3,245,700	3,319,200	(73,500) ¹²
Restricted for capital construction	112,000	64,000	48,000 ¹³
Unrestricted	195,950	216,450	(20,500) ¹⁴
Total net position	<u>\$ 3,553,650</u>	<u>\$ 3,599,650</u>	<u>\$ (46,000)</u>

Water and Sewer Fund
Statement of Revenues, Expenses, and Changes
in Fund Net Position
for the Year Ended June 30, 20X2

Operating revenues:		
Water sales	\$695,250	
Sewer charges	231,750	
Other operating revenues	<u>15,075</u>	
Total operating revenues		\$ 942,075
Operating expenses:		
Costs of sales and services	507,300	
Administration	250,275	
Depreciation	<u>245,000</u>	
Total operating expenses		<u>1,002,575</u>
Operating income (loss)		(60,500)
Nonoperating revenues (expenses):		
Interest income	6,500	
Interest expense	(28,000)	
Gain on sale of equipment	1,000	
Operating grants	<u>100,000</u>	
Total nonoperating revenues (expenses)		<u>79,500</u>
Income before contributions and transfers		19,000
Capital contributions		60,000
Transfers to other funds		<u>(125,000)</u>
Change in net position		(46,000)
Net position—beginning of year		<u>3,599,650</u>
Net position—end of year		<u><u>\$3,553,650</u></u>

Schedule I

The following information provides the details to the changes in balances in the statement of net position. The letters (A–M) to the right correspond to the coding on the statement of cash flows and the reconciliation of operating income to net cash provided by operating activities; the numbers (1–14) on the left correspond to the coding on the statement of net position.

1. Net changes in cash and cash equivalents		
2. Increase in customer receivables	\$ 15,000 ^A	
Increase in allowance for uncollectibles	(2,000) ^B	
	<u>\$ 13,000</u>	
3. Simple increase (decrease)—traces directly to the reconciliation of operating income to net cash provided by operating activities		
4. Purchase of investments	\$ 125,000 ^C	
Sales and maturities	(75,000) ^D	
	<u>\$ 50,000</u>	
5. Interest earned	\$ 8,500	(\$6,500 revenue, \$2,000 capitalized)
Interest received	(9,000) ^E	
	<u>\$ (500)</u>	
6. Acquisition and construction	\$ 357,500	(\$350,000 cash paid, ^F \$7,500 time-pay)
Cost of equipment sold	(11,000)	
Net construction period interest:		
Expense	\$ 7,500	
Income	<u>(2,000)</u>	
	5,500	
	<u>\$ 352,000</u>	
7. Depreciation expense	\$ 245,000 ^G	
Accumulated depreciation on equipment sold	(2,000)	
	<u>\$(243,000)</u>	
8. Interest accrued	\$ 35,500	(\$28,000 expense, \$7,500 capitalized)
Interest paid	(35,000)	(\$33,500 ^H capital, \$1,500 ^I noncapital)
	<u>\$ 500</u>	
9. Short-term borrowing	\$ 5,000	
Repayments	(25,000)	
	<u>\$ (20,000)^J</u> (qualifies for “net” reporting)	

10. New contracts	\$ 7,500
Installments on old contracts	<u>(10,000)^K</u>
	<u>\$ (2,500)</u>
11. New bonds sold	\$ 250,000 ^L
Principal payments made	<u>(65,000)^M</u>
	<u>\$ 185,000</u>
12. Net increase—cost of capital assets (see 6)	\$ 352,000
Net change in accumulated depreciation (see 7)	(243,000)
Net reduction in equipment contracts (see 10)	2,500
Net increase in capital-related revenue bonds (see 11)	<u>(185,000)</u>
	<u>\$ (73,500)</u>
13. Decrease in restricted cash and cash equivalents	\$ (1,500)
Increase in restricted investments (see 4)	50,000
Decrease in restricted interest receivable (see 5)	<u>(500)</u>
	<u>\$ 48,000</u>
14. Total change in net position	\$ (46,000)
Less:	
Change in net investment in capital assets (see 12)	73,500
Increase in restricted net position (see 13)	<u>(48,000)</u>
	<u>\$ (20,500)</u>

Schedule II

The following calculations are provided to demonstrate how to “indirectly” determine certain cash flows from operating activities. See Exercise 7 in Chapter 7, nonauthoritative Appendix 7-3, for a more complete illustration.

Water sales	\$ 695,250
Sewer charges	231,750
Plus beginning receivables	89,000
Less ending receivables	<u>(104,000)</u>
Cash received from customers	<u>\$ 912,000</u>
Cost of sales and services	\$ 507,300
Administration	250,275
Plus:	
Allowance for uncollectibles, 6/30/X1	5,500
Inventory, 6/30/X2	46,000
Prepays, 6/30/X2	600
Accounts payable, 6/30/X1	65,500
Less:	
Allowance for uncollectibles, 6/30/X2	(7,500)
Inventory, 6/30/X1	(48,000)
Prepays, 6/30/X1	(1,100)
Accounts payable, 6/30/X2	<u>(68,000)</u>
Cash paid to suppliers and employees	750,575
Less cash paid to employees	<u>(300,575)</u>
Cash paid to suppliers	<u>\$ 450,000</u>