

Proposed Accounting Standards Update

Issued: April 30, 2015
Comments Due: June 29, 2015

Liabilities—Extinguishments of Liabilities
(Subtopic 405-20)

Recognition of Breakage for Certain
Prepaid Stored-Value Cards

a consensus of the FASB Emerging Issues Task Force

The Board issued this Exposure Draft to solicit public comment on proposed changes to Topic 405 of the *FASB Accounting Standards Codification*®. Individuals can submit comments in one of three ways: using the electronic feedback form on the FASB website, emailing written comments to director@fasb.org, or sending a letter to “Technical Director, File Reference No. EITF-15B, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116.”

The *FASB Accounting Standards Codification*[®] is the source of authoritative generally accepted accounting principles (GAAP) recognized by the FASB to be applied by nongovernmental entities. An Accounting Standards Update is not authoritative; rather, it is a document that communicates how the Accounting Standards Codification is being amended. It also provides other information to help a user of GAAP understand how and why GAAP is changing and when the changes will be effective.

Notice to Recipients of This Exposure Draft of a Proposed Accounting Standards Update

The Board invites comments on all matters in this Exposure Draft and is requesting comments by June 29, 2015. Interested parties may submit comments in one of three ways:

- Using the electronic feedback form available on the FASB website at [Exposure Documents Open for Comment](#)
- Emailing a written letter to director@fasb.org, File Reference No. EITF-15B
- Sending written comments to “Technical Director, File Reference No. EITF-15B, FASB, 401 Merritt 7, PO Box 5116, Norwalk, CT 06856-5116.”

Do not send responses by fax.

All comments received are part of the FASB’s public file. The FASB will make all comments publicly available by posting them to the online public reference room portion of its website.

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Summary and Questions for Respondents

Why Is the FASB Issuing This Proposed Accounting Standards Update (Update)?

Prepaid stored-value cards are prepaid cards with monetary values redeemable for goods, services, and/or cash. When an entity sells a prepaid stored-value card that is redeemable at a third-party merchant (or merchants), it recognizes a liability for its obligation to provide the customer with the ability to purchase goods or services at that third-party merchant (or merchants). When the customer redeems the prepaid stored-value card, the liability (or part of that liability) between the entity and the customer is extinguished. At the same time, the entity incurs a liability to the merchant that provided the goods or services. This liability is typically extinguished with cash through a card-settlement process. However, in some cases, a prepaid stored-value card may be unused wholly or partially for an indefinite time period.

Some entities support the view that the liability that exists between an entity that sells a prepaid stored-value card and its customer prior to when the customer redeems the prepaid stored-value card (prepaid stored-value card liability) is a financial liability. Other entities support the view that a prepaid stored-value card liability is a nonfinancial liability. Although Subtopic 405-20, Liabilities—Extinguishments of Liabilities, currently includes derecognition guidance for both financial liabilities and nonfinancial liabilities, there currently is diversity in the methodology used to derecognize the portion of the nonrefundable dollar value of prepaid stored-value cards that ultimately is unredeemed (that is, breakage).

Topic 606, Revenue from Contracts with Customers, includes authoritative breakage guidance. However, financial liabilities are excluded from the scope of Topic 606. The guidance in Topic 606 is effective in fiscal years beginning after December 15, 2016, for public business entities, certain not-for-profit entities, and certain employee benefit plans or December 15, 2017, for all other entities. However, the Board also is issuing a proposed Update to defer each of those dates by one year.

Under current generally accepted accounting principles (GAAP), if an entity concludes that a prepaid stored-value card liability is either a financial liability or a nonfinancial liability, it should apply the derecognition guidance in Subtopic 405-20. That guidance typically would prohibit derecognition of the liability prior to when a customer redeems the card or when the card expires or becomes subject to unclaimed property laws. Upon the effective date of Topic 606, if an entity concludes that a prepaid stored-value card liability is a nonfinancial liability, it would apply the less restrictive breakage guidance in Topic 606. The objective of

this proposed Update is to address the current and potential future diversity in practice related to the derecognition of a prepaid stored-value card liability.

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

The amendments in this proposed Update would apply to entities that sell prepaid stored-value cards that have all of the following characteristics:

- a. The cards do not have an expiration date.
- b. The cards are not subject to unclaimed property laws.
- c. The cards are redeemable for any of the following:
 - i. Cash
 - ii. Goods or services only at third-party merchants (for example, only at a merchant that accepts prepaid stored-value cards on a specific card network)
 - iii. Both i and ii.
- d. The cards are not attached to a segregated bank account like a customer depository account.

What Are the Main Provisions?

Liabilities related to the sale of prepaid stored-value cards within the scope of this proposed Update are financial liabilities. The amendments in this proposed Update would provide a narrow scope exception to the guidance in Subtopic 405-20 to require that breakage be accounted for consistent with the breakage guidance in Topic 606 for those liabilities with the characteristics described above.

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

Neither current GAAP nor the pending guidance in Topic 606 contains specific guidance for the derecognition of prepaid stored-value card liabilities within the scope of the amendments in this proposed Update. The amendments in this proposed Update would be an improvement to GAAP because the amendments would specify how prepaid stored-value card liabilities within its scope should be derecognized, thereby eliminating the current and potential future diversity in practice described above.

When Would the Amendments Be Effective?

The amendments in this proposed Update would be applied using a modified retrospective basis of application by means of a cumulative-effect adjustment to retained earnings as of the beginning of the annual period in which the guidance is effective. The effective date and the ability to apply the amendments before the effective date will be determined after the Task Force considers stakeholder feedback on this proposed Update.

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

IFRS does not currently provide specific guidance for the derecognition of prepaid stored-value card liabilities. The IFRS Interpretations Committee is currently discussing this issue. However, the International Accounting Standards Board (IASB) has not proposed amendments to IFRS as a result of those discussions. As such, the proposed amendments currently differ from IFRS.

Questions for Respondents

The Board invites individuals and organizations to comment on all matters in this proposed Update, particularly on the issues and questions below. Comments are requested from those who agree with the proposed guidance as well as from those who do not agree. Comments are most helpful if they identify and clearly explain the issue or question to which they relate. Those who disagree with the proposed guidance are asked to describe their suggested alternatives, supported by specific reasoning.

Question 1: Should the scope of the proposed amendments be limited to prepaid stored-value card liabilities resulting from the sale of cards with the characteristics specified in this proposed Update? If not, what other liabilities should be included in the scope of this proposed Update?

Question 2: If an entity expects to be entitled to a breakage amount, should a prepaid stored-value card liability within the scope of the proposed amendments be derecognized in proportion to the pattern of rights expected to be exercised by the card holder only to the extent that it is probable that a significant reversal of the recognized breakage amount will not subsequently occur? If an entity does not expect to be entitled to a breakage amount, should the liability be derecognized when the likelihood of the customer exercising its remaining rights becomes remote? If not, what breakage model would be appropriate?

Question 3: Should an entity be required to provide the disclosures specified in this proposed Update? Should any other disclosures be required? If yes, please explain what disclosures should be provided.

Question 4: Should the proposed amendments be applied using a modified retrospective transition method (requiring a cumulative-effect adjustment as of the beginning of the annual period in which the guidance is effective)? If not, please explain why.

Question 5: How much time would be needed to implement the proposed amendments? Should early adoption be permitted?

Question 6: Do entities other than public business entities (that is, private companies and not-for-profit entities) need additional time to apply the proposed amendments? Why or why not?

Amendments to the *FASB Accounting Standards Codification*[®]

Introduction

1. The Accounting Standards Codification is amended as described in paragraphs 2–5. In some cases, to put the change in context, not only are the amended paragraphs shown but also the preceding and following paragraphs. Terms from the Master Glossary are in **bold** type. Added text is underlined, and deleted text is ~~struck out~~.

Amendments to Subtopic 405-20

2. Amend paragraph 405-20-15-2, with a link to transition paragraph 405-20-65-1, as follows:

Liabilities—Extinguishment of Liabilities

Scope and Scope Exceptions

405-20-15-2 The guidance in this Subtopic applies to extinguishments of all liabilities, including both financial liabilities and nonfinancial ~~liabilities~~liabilities, unless derecognition of a financial or nonfinancial liability is addressed in another Topic (for example, the derecognition guidance for gaming chips in Subtopic 924-405 or the guidance in Topic 606 for breakage). ~~For example, derivative~~Derivative instruments that are nonfinancial liabilities (for example, a written commodity option) are included in the scope of this Subtopic.

3. Amend paragraph 405-20-40-1 and add paragraphs 405-20-40-3 through 40-4 and their related heading, with a link to transition paragraph 405-20-65-1, as follows:

Derecognition

405-20-40-1 Unless addressed by other guidance (for example, paragraphs 405-20-40-3 through 40-4 or paragraphs 606-10-55-46 through 55-49), aA debtor shall derecognize a liability if and only if it has been extinguished. A liability has been extinguished if either of the following conditions is met:

- a. The debtor pays the creditor and is relieved of its obligation for the liability. Paying the creditor includes the following:
 1. Delivery of cash
 2. Delivery of other financial assets
 3. Delivery of goods or services
 4. Reacquisition by the debtor of its outstanding debt securities whether the securities are cancelled or held as so-called treasury bonds.
- b. The debtor is legally released from being the primary obligor under the liability, either judicially or by the creditor. For purposes of applying this Subtopic, a sale and related assumption effectively accomplish a legal release if nonrecourse debt (such as certain mortgage loans) is assumed by a third party in conjunction with the sale of an asset that serves as sole collateral for that debt.

> Prepaid Stored-Value Cards

405-20-40-3 Liabilities resulting from the sale of prepaid stored-value cards with the characteristics described in paragraph 405-20-40-4 are financial liabilities. The portion of the dollar value of prepaid-stored value cards that ultimately is not redeemed by customers for cash or used to purchase goods and/or services is referred to as breakage. If an entity expects to be entitled to a breakage amount for a liability resulting from the sale of a prepaid stored-value card that has all of the characteristics in paragraph 405-20-40-4, the entity shall derecognize the amount related to the expected breakage in proportion to the pattern of rights expected to be exercised by the card holder only to the extent that it is probable that a significant reversal of the recognized breakage amount will not subsequently occur. If an entity does not expect to be entitled to a breakage amount for prepaid stored-value cards that have all of the characteristics in paragraph 405-20-40-4, the entity shall derecognize the amount related to breakage when the likelihood of the customer exercising its remaining rights becomes remote.

405-20-40-4 The derecognition guidance in paragraph 405-20-40-3 shall apply only to liabilities resulting from the sale of prepaid stored-value cards that have all of the following characteristics:

- a. The cards do not have an expiration date.
- b. The cards are not subject to unclaimed property laws.
- c. The cards are redeemable for any of the following:
 - i. Cash
 - ii. Goods or services only at third-party merchants (for example, only at a merchant that accepts prepaid stored-value cards on a specific card network)
 - iii. Both i and ii.
- d. The cards are not attached to a segregated bank account like a customer depository account.

4. Add paragraph 405-20-50-2 and its related heading, with a link to transition paragraph 405-20-65-1, as follows:

Disclosure

> Prepaid Stored-Value Cards

405-20-50-2 An entity that recognizes a breakage amount in accordance with paragraph 405-20-40-3 shall disclose the methodology used to recognize breakage and significant judgments made in applying the breakage methodology.

5. Add paragraph 405-20-65-1 and its related heading as follows:

Transition Related to Accounting Standards Update No. 2015-XX, Liabilities—Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Cards

405-20-65-1 The following represents the transition and effective date information related to Accounting Standards Update No. 2015-XX, *Liabilities—Extinguishments of Liabilities (Subtopic 405-20): Recognition of Breakage for Certain Prepaid Stored-Value Cards*:

- a. The pending content that links to this paragraph shall be effective for fiscal years and interim periods within those years beginning after [date to be inserted after exposure].
- b. An entity shall apply the pending content that links to this paragraph using a modified retrospective transition method by means of a cumulative-effect adjustment to retained earnings as of the beginning of the annual period in which the pending content that links to this paragraph is effective.
- c. An entity shall provide the disclosures in paragraphs 250-10-50-1(a), 50-1(b)(3), and 50-2, as applicable, in the period the entity adopts the pending content that links to this paragraph.

The amendments in this proposed Update were approved for publication by the unanimous vote of the seven members of the Financial Accounting Standards Board:

Russell G. Golden, *Chairman*
James L. Kroeker, *Vice Chairman*
Daryl E. Buck
Thomas J. Linsmeier
R. Harold Schroeder
Marc A. Siegel
Lawrence W. Smith

Background Information and Basis for Conclusions

Introduction

BC1. The following summarizes the Task Force's considerations in reaching the conclusions in this proposed Update. It includes the Board's basis for ratifying the Task Force conclusions when needed to supplement the Task Force's considerations. It also includes reasons for accepting certain approaches and rejecting others. Individual Task Force and Board members gave greater weight to some factors than to others.

Background Information

BC2. Common examples of prepaid stored-value cards include prepaid gift and telecom cards, in both physical and digital forms. Current GAAP does not contain specific guidance for the derecognition of liabilities resulting from the sale of prepaid stored-value cards. In the absence of specific guidance, there has been diversity in practice on how prepaid stored-value card liabilities are derecognized. The FASB received an unsolicited comment letter from a stakeholder requesting that the Task Force clarify how (and whether) a prepaid stored-value card liability should be derecognized.

BC3. The stakeholder questioned whether a prepaid stored-value card liability meets the definition of a financial liability. Some stakeholders stated that the determination of whether a financial liability exists depends on whether the transaction between the entity that sells the prepaid stored-value card and the customer is viewed as a separate transaction from the transaction between the entity and the merchant. That is, the obligation the entity has to the merchant is settled in cash and would meet the definition of a financial liability, while the obligation the entity has to the customer is settled through the delivery of goods and services by the merchant and would not meet the definition of a financial liability.

BC4. However, other stakeholders view the substance of prepaid stored-value card sales as a single transaction between the entity and the customer that is settled in cash through the merchant. Accordingly, in their view, the liability recognized upon sale of a prepaid stored-value card meets the definition of a financial liability.

BC5. Many entities, but not all entities, currently apply the views expressed in a speech given by a U.S. Securities and Exchange Commission (SEC) staff member and recognize breakage for a prepaid stored-value card liability prior to when the

card is redeemed regardless of whether the liability is considered a financial liability. Topic 606 establishes breakage guidance for transactions within its scope. However, financial liabilities are excluded from the scope of that breakage guidance.

BC6. The objective of the amendments in this proposed Update is to provide specific guidance on the derecognition of prepaid stored-value card liabilities to eliminate the diversity in accounting treatment.

Scope

BC7. The Task Force reached a consensus-for-exposure that the guidance in this proposed Update should apply only to liabilities resulting from the sale of prepaid stored-value cards that have all of the following characteristics:

- a. The cards do not have an expiration date.
- b. The cards are not subject to unclaimed property laws.
- c. The cards are redeemable for any of the following:
 - i. Cash
 - ii. Goods or services only at third-party merchants (for example, only at a merchant that accepts prepaid stored-value cards on a specific card network)
 - iii. Both i and ii.
- d. The cards are not attached to a segregated bank account like a customer depository account.

BC8. The scope of the proposed amendments is primarily based on the characteristics of the prepaid stored-value cards described in the original stakeholder submission. The Task Force decided that the scope also should include prepaid stored-value cards that may be redeemed for cash because the Task Force believes that the economics of those cards are similar to the economics of prepaid stored-value cards that are only redeemable for goods and services. That is, the Task Force does not believe that the derecognition guidance for prepaid stored-value cards that are redeemable for cash should differ from the derecognition guidance for prepaid cards that are redeemable for goods and services. Several Task Force members suggested that the scope of the proposed amendments be broadened further to include liabilities similar to those included in the scope of this proposed Update (for example, certain customer loyalty programs). The Task Force determined that the scope of this proposed Update should include only liabilities resulting from the sale of prepaid stored-value cards with the characteristics described in paragraph BC7. However, the Task Force recommended that this proposed Update solicit feedback from stakeholders on the appropriateness of the scope of the proposed amendments.

Recognizing Breakage for Prepaid Stored-Value Cards

BC9. The Task Force reached a consensus-for-exposure that because an entity's liability for a prepaid stored-value card ultimately will be settled in cash to either the customer or a third party, that liability is a financial liability within the scope of Subtopic 405-20. However, the Task Force agreed that it is appropriate to provide a narrow scope exception to the derecognition guidance in Subtopic 405-20 to require breakage to be accounted for in a manner consistent with Topic 606 for liabilities resulting from the sale of prepaid stored-value cards within the scope of this proposed Update. The Task Force believes that providing a means for those financial liabilities to be derecognized provides better information to users than potentially recognizing those liabilities in perpetuity. For example, if a prepaid stored-value card is lost and never used, the liability related to the card may never meet the derecognition criteria in Subtopic 405-20. The Task Force concluded that the breakage guidance for those prepaid stored-value cards should be similar to the breakage guidance in Topic 606 because the economics of those prepaid stored-value card transactions are similar to the economics of prepaid stored-value card transactions that are expected to be within the scope of Topic 606. The Task Force also considered that the guidance in this proposed Update is similar to the way in which many entities with prepaid stored-value card liabilities within the scope of this proposed Update recognize breakage today.

Technical Correction

BC10. The Task Force observed that the guidance in Subtopic 405-20 applies to both financial and nonfinancial liabilities. However, the guidance in Subtopic 405-20 does not acknowledge the existence of other derecognition guidance in GAAP (for example, Topic 606 and Subtopic 924-405, Entertainment—Casinos—Liabilities). Accordingly, the Task Force recommended that a technical correction to the guidance in Subtopic 405-20 be made to acknowledge the existence of other derecognition guidance in GAAP.

Disclosure

BC11. The Task Force reached a consensus-for-exposure that an entity should be required to disclose the methodology used for calculating breakage. This disclosure would be similar to the disclosures required for entities that will apply the breakage guidance in Topic 606. The Task Force observed that a prepaid stored-value card liability also would be subject to the disclosure requirements for financial liabilities in Topic 825, Financial Instruments.

Effective Date and Transition

BC12. The Task Force reached a consensus-for-exposure that the amendments in this proposed Update would be applied using a modified retrospective transition method by means of a cumulative-effect adjustment to retained earnings as of the beginning of the annual period in which the guidance is effective.

BC13. The Task Force will determine the effective date after it considers stakeholder feedback on this proposed Update including feedback on the effective date for nonpublic entities based on the Private Company Decision-Making Framework. That framework states that based on private company resource limitations and the learning cycle, generally the amendments in an Accounting Standards Update should be effective for private entities one year after the first annual period in which public companies are required to adopt them and for interim periods after the first annual period.

Benefits and Costs

BC14. The objective of financial reporting is to provide information that is useful to present and potential investors, creditors, donors, and other capital market participants in making rational investment, credit, and similar resource allocation decisions. However, the benefits of providing information for that purpose should justify the related costs. Present and potential investors, creditors, donors, and other users of financial information benefit from improvements in financial reporting, while the costs to implement new guidance are borne primarily by present investors. The Task Force's assessment of the costs and benefits of issuing new guidance is unavoidably more qualitative than quantitative because there is no method to objectively measure the costs to implement new guidance or to quantify the value of improved information in financial statements.

BC15. The Task Force does not anticipate that entities would incur significant costs as a result of the amendments in this proposed Update because the proposed amendments would not represent a significant change in practice for most entities offering prepaid stored-value cards. Furthermore, the Task Force does not believe that the incremental disclosures required by this proposed Update would be costly. The Task Force agreed that derecognition of those liabilities would benefit users because there would be a means to recognize breakage for the prepaid stored-value cards within the scope of this proposed Update, rather than potentially recognizing a liability in perpetuity. Thus, on balance, the Task Force concluded that those benefits would justify the limited costs that entities are expected to incur as a result of the application of the amendments in this proposed Update.

Amendments to the XBRL Taxonomy

The provisions of this Exposure Draft, if finalized as proposed, would require changes to the U.S. GAAP Financial Reporting Taxonomy (Taxonomy). We welcome comments on these proposed changes to the Taxonomy through [ASU Taxonomy Changes](#) provided at www.fasb.org. After the FASB has completed its deliberations and issued a final Accounting Standards Update, proposed amendments to the Taxonomy will be made available for public comment at www.fasb.org and finalized as part of the annual release process.