Letter of Comment No. 24
File Reference: 13-3PV
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February 27, 2012

David Bean
Director of Research
Project No. 13-3
Governmental Accounting Standards Board
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Dear Mr. Bean:

On behalf of the Tennessee Department of Audit, we thank the GASB for the opportunity to comment on its proposed Preliminary Views (PV), *Economic Condition Reporting: Financial Projections*. We generally disagree with the requirements of the PV and support many of the views expressed in the alternative view.

General Comments

Generally, we agree that fiscal sustainability, conceptually, is important for the government financial statement user community, and we support efforts to reexamine the CAFR content in total to determine exactly what information users find essential for decision making and what information can be eliminated. However, we do not support the effort to pile on additional requirements without lessening other requirements, especially when information needed for fiscal sustainability may already exist in the voluminous reporting documents already prepared (e.g., CAFR or AFR).

Furthermore, we believe the board should first explain how information currently required to be reported in a financial report (e.g., CAFR or other external financial report) does not allow for user analysis (i.e., financial projections) that the board is requiring in this proposed PV. The GASB User Guides clearly educate users in how existing annual financial report information can be utilized to assist users in assessing to some degree a government's fiscal sustainability. Existing note disclosures and required supplementary information (RSI) requirements already address many of the components the board believes is necessary for a user to assess a government's fiscal sustainability (e.g., long-term debt, other long-term liabilities, pensions and OPEB). We are not convinced that GASB has made the case that the five components of information necessary to assist users in assessing a governmental entity's fiscal sustainability are absent from existing financially reported information.

Although we agree with the general concept of fiscal sustainability, we do not agree with the board's preliminary view that these financial projections should be RSI. Instead, we support the alternative view which states 1) that these financial projections are not essential for placing the basic financial statements and notes to the basic financial statements in an appropriate operational, economic, or historical context, and 2) that the financial projections do not meet the definition of RSI, which would "place the basic financial statements and notes in context." We agree with Concept Statement 3 ¶44 that RSI does not include "subjective assessments of the effects of reported information on the reporting unit's future financial position," which we believe describes financial projections.

As an alternative solution, a government-wide Statement of Cash Flows could be added as a basic financial statement if other reporting requirements were eliminated. This Statement over time could accumulate 10-year historical trend information as an additional schedule in the Statistical Section (financial trend section). Because the government-wide statements are presented on an accrual basis of accounting, a Statement of Cash Flows could be required as is already required for proprietary funds. This Statement would address components 1 and 2 by providing a foundational basis for a user to conduct his/her own financial projection analysis of historical cash inflows and cash outflows. Components 3 and 4 are already addressed in current note disclosures and RSI through existing standards. For Component 5, we recommend several options: 1) disaggregating the Statement of Activities' "operating grants and contributions" and "capital grants and contributions" columns, as applicable, to identify intergovernmental revenues as is currently displayed on the face of the governmental funds Statement of Revenues, Expenditures, and Changes in Fund Balances; disclosing this disaggregation in a note disclosure; or providing an analysis of intergovernmental resources as a percentage of total resources in the MD&A. In addition, a subsequent events note disclosure would address any currently known facts, decisions, or conditions that will materially impact the financial statements. MD&A already requires a description of currently known facts, decisions, or conditions that have a significant effect on financial position or results of operations.

Overall, we believe the existing CAFR information (in addition to our suggestions above) provides sufficient information for a user to assess a government's fiscal sustainability. We suggest that this information could be provided in a comprehensive schedule within the Statistical Section (i.e., SI rather than RSI) under a Fiscal Sustainability heading. However, requiring such schedule(s) would likely require an amendment to GASB 44. Thus, it appears to us that a sufficient framework is already in place to allow user analysis of historical information without requiring financial projections. We believe the proposed requirements will add complexity (e.g., mixed attribute model with cash basis and accrual basis) and result in additional delays in timely financial reporting.

In conclusion, we see the financial reporting requirements increasing year after year. In this case, it is understandable, since most of us can all agree that fiscal sustainability information is important to the user. However, before the board goes down this path and creates new

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financial reporting requirements for a unique government user viewpoint, it may be time to redefine the whole user concept and get rid of all the extra reporting we are doing that is not currently used.

Questions for Respondents

Our general comments above represent our overall view of the PV approach and should be considered in the context of our answers below. If the majority of the board's views carry forward, our answers to the specific respondent questions follow.

1. We agree with the board's preliminary view that the recommended five components of information are necessary to assist users in assessing a governmental entity's fiscal sustainability (Chapter 3, paragraph 2). We believe these components are encompassed within the fiscal sustainability definition in Chapter 2 ¶8. However, as noted above, we believe most of these components are already presented in a CAFR.

2. In general, we disagree with including financial projections with historical basic financial statements. However, if the board's preliminary view is carried forward, we agree that financial projections should be (a) based on current policy, (b) informed by historical information, and (c) adjusted for known events and conditions that affect the projection periods, for the reasons discussed in Chapter 4, paragraphs 2–7.

3. Ultimately, we believe the board's preliminary view that inflows and outflows projected on a cash basis of accounting and that financial obligations projected on an accrual basis of accounting (Chapter 4, ¶8–12) would inject a mixed attribute model notion and thus complexity. This could result in comparing "apples to oranges" (i.e., cash-basis resources vs. accrual-based obligations). We are not sure how material these differences might be.

4. We agree with the board's preliminary view in Chapter 4, ¶13–16 that the identification and development of assumptions for making financial projections should be guided by a principles-based approach. We agree that such an approach would set forth principles that require assumptions to be based on relevant historical information, as well as events and conditions that have occurred and affect the projection periods. Furthermore, we agree that these assumptions should be (a) consistent with each other (where appropriate) and with the information used as the basis for the assumptions and (b) comprehensive by considering significant trends, events, and conditions.

5. We agree with the board's preliminary view, if carried forward, that annual financial projections should be made for a minimum of five individual years beyond the reporting period for the purpose of external reporting for the reasons presented in Chapter 4, ¶19–23.

6. We disagree with the board's preliminary view that all of the components of fiscal sustainability information are essential for placing the basic financial statements and notes to the basic financial statements in an operational or economic context and therefore should be required and communicated as RSI (Chapter 5, paragraphs 7–12). We do not believe the board has

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sufficiently justified its reasoning for how fiscal sustainability information places the basic financial statements and notes to the basic financial statements in an operational or economic context. We do believe the fiscal sustainability information is useful for that purpose and should be presented as SI instead.

7. We agree that if the board's preliminary view is carried forward that all governmental entities should be required to report financial projections and related narrative discussions for the reasons discussed in Chapter 5, ¶13 and 14.

8. We disagree with a phase-in period for implementing the reporting requirements for financial projections and related narrative discussions. Instead of a phase-in period, we recommend delaying the effective date one more year in order to allow for implementation of other more important GASB standards. Thus, all governments would implement at the same time, but earlier implementation could be encouraged.

Should you have questions or need clarification on any of our comments, please contact Gerry Boaz or me at (615) 747-5262.

Sincerely,

Arthur A. Hayes, Director
Division of State Audit