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March 7, 2012

Mr. David R. Bean  
Director of Research and Technical Activities  
Governmental Accounting Standards Board (GASB)  
Project 13-3  
401 Merritt 7  
Norwalk, CT 06856-5116

Dear Mr. Bean:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments to the Governmental Accounting Standards Board (GASB or the Board) on the Preliminary Views (PV) document entitled *Economic Condition Reporting: Financial Projections*. The FMSB is comprised of 25 members (list attached) with accounting and auditing backgrounds in federal, state and local government, as well as academia and public accounting. The FMSB reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately.

#### General Comments

The FMSB agrees with the Board's fundamental proposition that decision makers require information with which to assess a government's fiscal sustainability. However, it is the consensus of the FMSB that we do not support the current views of the Board as contained in the PV document. The FMSB believes that requiring financial projections and a narrative discussion on major intergovernmental service interdependencies as Required Supplementary Information (RSI) is not an appropriate approach to this matter.

A fundamental concern of the FMSB is that the PV suggests an approach that is contrary to the precepts of Concepts Statement 3. GASB Concept Statement 3, paragraphs 42 thru 45, defines RSI and the criteria for presenting information in RSI. RSI is defined as supporting information that is essential for placing the basic financial statements and notes in an appropriate context. By their nature, the basic financial statements are historical and the information in the statements and notes are based upon known events. The approach suggested by GASB, in particular Components numbers 1 and 2 would, if adopted, allow RSI to include information that is forward looking in nature, more akin to a forecast. We recognize that current footnote disclosures already include forward looking information such as long term debt payments; however these are schedules of future transactions to which a government entity is bound by a current contract or law.



This is fundamentally different than what is suggested by Components 1 and 2 in the PV. Not all of the items to be “projected”, as included in these two Components, are covered by a contract or other legal obligation. We recognize that the PV asks for them to be developed using “known” facts or assumptions. But known facts or assumptions are different from items covered by long term contracts and debt obligations. This concern extends to the projection of Financial Obligations under Component 3, where one should anticipate issuance of debt and debt re-financings. Such debt-related events may not occur in a specific pattern and would be difficult to project.

We also believe that the current views are contrary to the tenets of Concepts Statement 3, paragraph 43, which states that “RSI has a clear and demonstrable relationship to information in the basic financial statements or notes to basic financial statements to which it pertains.” We believe that Components 1 and 2 fail to meet the criteria of having a “clear and demonstrable relationship” to the basic financial statements. Neither the current entity-wide nor fund statements include statements of cash inflows and cash outflows. If adopted, this approach would require cash flow statements for the future but none for the immediate past period. This is contrary to what RSI is defined as in our opinion.

Further, paragraph 44 of Concept Statement 3 speaks as to what RSI is not meant to include. Paragraph 44 excludes predictions about the effects of future events on future financial statements. We recognize that the PV states that projections are to be based upon known facts. However, this notion is effectively a prediction as to what, under the current state of affairs, will remain unchanged by future events.

The FMSB understands the value of and the need for users to have access to information relevant to fiscal sustainability and we believe that some of the parts of what the Board has suggested for RSI are currently included elsewhere in the financial statements, their footnotes or other schedules. For example, information on future debt payment requirements are included the footnotes. Similarly, information on long term contracts is also included in the footnotes. We would not object to the consolidation of existing information now within the notes into a more understandable format that would focus on fiscal sustainability. We believe that GASB needs to provide additional analysis of why existing information does not provide users with the information to meet these needs already.

Concerns were also expressed about the development and review of the information for total cash inflows and total cash outflows and the potential for conflicting information for the auditor. It is not uncommon in larger governments for the budget development and forecast function to be separated from the unit which prepares the financial statements. Often they will report to different elected officials. The budget unit may publish projections for budget purposes that would differ, in a key areas and assumptions, from those provided by the accounting unit under the methodology presented within the PV. This could prove difficult to reconcile. Members of the FMSB asked if these types of issues would ultimately lead to GASB having to address issues related to the development of budgets. The development of budgets is a matter that has always been under the purview of local laws and practices. We question how these matters would be resolved or whether it would result in some type of new qualification in an auditor’s report. This may not be helpful to users and may raise concerns by bond rating agencies.

It is because of these concerns that the FMSB does not support the Board’s current views of including Components 1 through 5 as RSI. Based upon these factors as well as others, the FMSB finds that our views are more closely aligned with those expressed in the Alternative Views. We have provided answers to the questions posed by GASB in the PV, however our answers are qualified based upon the concerns we have expressed so far.

1. The Board's preliminary view is that there are five components of information that are necessary to assist users in assessing a governmental entity's fiscal sustainability (Chapter 3, paragraph 2):
  - Component 1—Projections of the total cash inflows and major individual cash inflows, in dollars and as a percentage of total cash inflows, with explanations of the known causes of fluctuations in cash inflows (Chapter 3, paragraphs 4–9)
  - Component 2—Projections of the total cash outflows and major individual cash outflows, in dollars and as a percentage of total cash outflows, with explanations of the known causes of fluctuations in cash outflows (Chapter 3, paragraphs 10–14)
  - Component 3—Projections of the total financial obligations and major individual financial obligations, including bonds, pensions, other postemployment benefits, and long-term contracts, with explanations of the known causes of fluctuations in financial obligations (Chapter 3, paragraphs 15–20)
  - Component 4—Projections of annual debt service payments (principal and interest) (Chapter 3, paragraphs 21–23)
  - Component 5—Narrative discussion of the major intergovernmental service interdependencies that exist and the nature of those service interdependencies (Chapter 3, paragraphs 24–26).

Do you agree with this view? Why or why not

**FMSB Response** - Recognizing our fundamental disagreement with GASB's current views of providing this information as RSI, the FMSB agrees that the five components would assist users in assessing a governmental entity's fiscal sustainability. However we believe additional information would also be needed to assist users in assessing a governmental entity's fiscal sustainability. For example, economic factors have a major impact on a government's fiscal sustainability and these factors are not addressed in these five components. For local governments, the elasticity of the tax base would also be a key piece of information. This type of information would prove valuable for users who are trying to assess fiscal sustainability.

We also have concerns about the construction of some of these components. In constructing the information for Component 4, as we read the PV, the entity would be required to include in the schedule not only information on existing debt obligations but also authorized and unissued debt obligations. The issuance, retirement, and replacement of debt through refinancing are not always done in accordance with a strict schedule and are often influenced by economic and political factors. We question whether this is possible and meaningful.

For Component 5, we do agree that disclosure of major intergovernmental interdependencies should be required and believe that it could be included in MD&A. As currently proposed, Component 5 is limited to only service interdependencies and not fiscal interdependencies because these matters would be presented as part of Components 1 and 2. As stated above, we do not believe that the PV approach is prudent. Therefore, we would suggest that the Board consider an alternative approach to providing information on these matters. An alternative might be that past and current fiscal interdependencies could be disclosed in some manner that would illustrate major recurring interdependencies and major one-time interdependencies (e.g., recurring revenues from entitlement programs versus one time grants). We believe that this information would prove valuable, allow users to assess future events for their own purposes and not violate any underlying concepts.

The PV also does not address the relationship between the government's current budget and the information in the five proposed Components. By the time the financial statements are released, governments may be two to three months into the current budget. Does GASB anticipate that the information in the five Components for year one should align with the entity's budget? If it does not, will this generate further confusion for the user?

2. The Board's preliminary view is 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. Current policy includes policy changes that have been formally adopted by the end of the reporting period but that will not be effective until future periods (Chapter 4, paragraphs 2–7). Do you agree with this view? Why or why not

**FMSB Response** - Recognizing our fundamental disagreement with GASB's current views of providing this information as RSI, the FMSB has concern with this proposal. The Board's proposal that the financial projections will be based all known information at the time of the fiscal period year end has merit as it would not be wise to ignore all known information. However we question how changes that are adopted subsequent to the end of the fiscal period, but have a major impact on the projections could likewise be ignored when the CAFR has not yet been issued. If this course is followed, the RSI could be outdated before the CAFR is issued. For example a state legislature may adopt a major change to its pension benefits and healthcare benefits for future employees subsequent to the year end, but prior to the issuance of the CAFR. Based on our reading of the Board's proposal, this change would not influence any of the RSI and thus it would be out of date before the CAFR is issued.

3. The Board's preliminary view is that inflows and outflows should be projected on a cash basis of accounting, and financial obligations should be projected on an accrual basis of accounting (Chapter 4, paragraphs 8–12). Do you agree with this view? Why or why not?

**FMSB Response** - We disagree with the approach of mixing cash and accrual basis projections as suggested by GASB. We believe that GASB should not proceed with the approach contemplated in the PV, but rather adopt a single approach to the development of projections. If the intent is to project fiscal sustainability, than it would be reasonable that the projections would be based on cash, since the lack of cash to pay the bills would be the major concern for users. However if the intent is to highlight issues of interperiod equity, than an accrual basis would be better suited for the projection.

4. The Board's preliminary view is that the identification and development of assumptions for making financial projections should be guided by a principles-based approach. 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, 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 (Chapter 4, paragraphs 13–16). Do you agree with this view? Why or why not?

**FMSB Response** - Recognizing our fundamental disagreement with GASB's current views of providing this information as RSI, the FMSB has concerns that this proposal could result in GASB addressing issues of budgeting that may conflict with current practice and law in the governmental entity. Further, as stated in our opening comments, the development of budgets and budget projections, in larger units of government, will be made by different parts of the government. This may results in conflicting information and may confuse users.

5. The Board's preliminary view is that annual financial projections should be made for a minimum of five individual years beyond the reporting period for the purpose of external reporting (Chapters 4, paragraphs 19-23). Do you agree with this view? Why or why not?

**FMSB Response** - Recognizing our disagreement with GASB's current views of providing this information as RSI, a five year period would be a maximum.

6. The Board's preliminary view is 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 required supplementary information (Chapter 5, paragraphs 7-12). Do you agree with this view? Why or why not?

**FMSB Response**- As stated in our opening comments, we disagree that the information included in the PV under the five components properly belongs in RSI. As cited in our general comments, we believe that this information should not be included in RSI as it conflicts with the definitions provided in Concept Statement 3. The reasons for our disagreement have already been stated.

7. The Board's preliminary view is that all governmental entities should be required to report financial projections and related narrative discussions (Chapter 5, paragraphs 13 and 14). Do you agree with this view? Why or why not?

**FMSB Response** - As stated in our general comments; we disagree with the current views of the GASB on these issues. We agree that preparing the types of information related to fiscal sustainability contemplated by the Board may be useful, and should be considered by governmental entities. However we disagree that it should be included as RSI. GASB Concept Statement 1, paragraph 4 states, among other things that financial statements are the end products of the reporting process and certain information should be provided via the financial statements and other information is better provided outside of the reporting process. We believe that the information suggested for RSI by the current views should be presented outside of the financial statements. We believe it is not consistent with Concept Statement 3.

8. Do you believe that a phase-in period for implementing the reporting requirements for financial projections and related narrative discussions would be appropriate (for example, requiring governmental entities over certain dollar thresholds to implement first)? If so, what phase-in criteria would you recommend (Chapter 5, paragraph 14).

**FMSB Response** - We appreciate the approach afforded in the past, particularly with Statement No. 34. However, we believe that a stepped approach will be lengthy as most of the governments in America are small and not as sophisticated as states and large municipal governments. We recommend that should the Board approve the project in the future, that it would be initially for states and large non-state governments (those with over \$100 million in revenues) as a first phase of implementation. And then perhaps wait a number of years – even as long as five years for the procedures and information to be stabilized. We would then recommend that the remaining governments comply with any final standard, only if they prepare comprehensive annual financial reports. The remainder governments that do not prepare comprehensive annual financial reports would be exempted.

**Other Items** - We also noticed that a large segment of governments and governmental activity are not addressed in the preliminary views. Fiduciary governments (stand alone plans) which are at the forefront of sustainability discussions due to post-employment benefits sustainability are not mentioned. Furthermore the relationship between component unit reporting of this information and the primary government are not ideal. We would recommend that should the provisions of the preliminary views be eventually adopted that the focus would be emphasized for the primary government and blended

component units. Discretely presented component unit information would not be presented with a primary government's financial reports.

**Testimony Notification** - I am also pleased to inform you that I shall testify in Los Angeles on March 29<sup>th</sup>. I will provide my testimony by March 16<sup>th</sup>.

We appreciate the opportunity to comment on this document and would be pleased to discuss this letter with you at your convenience. This letter represents the consensus view of the FMSB members and they have approved the issuance of this letter of comments. If there are any questions regarding the comments in this letter, please contact Steven E. Sossei, CPA, and AGA staff liaison for the FMSB, at [ssossei@agacgfm.org](mailto:ssossei@agacgfm.org) or at 518-522-9968.

Sincerely,

A handwritten signature in black ink, appearing to read 'Eric S. Berman', with a long horizontal flourish extending to the right.

Eric S. Berman, CPA, Chair  
AGA Financial Management Standards Board

cc: Richard O. Bunce, Jr., CGFM, CPA  
AGA National President

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