

DEPARTMENT OF ADMINISTRATION
STATE ACCOUNTING DIVISION



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Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
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My staff and I do not conceptually agree with the proposed reporting requirements contained in the Economic Condition Reporting: Financial Projections preliminary views document. While the five components discussed in the related questions may be useful to users in projecting the fiscal sustainability of a government, we do not believe the related information should be included in the financial reporting contained in a government's Comprehensive Annual Financial Report (CAFR). By definition this is an annual financial report, covering one year of time, and reporting on the financial activity relating to that period of time, along with other known financial information relating to a specific year. While it may be perceived these projections would assist the financial community, they go far beyond financial reporting, would be very expensive to both implement and apply into the future, and move us firmly into the financial forecasting arena, which we believe is well outside the scope of Governmental Financial Reporting as it should be defined by your board.

Admittedly current governmental financial reporting includes statistical information relating to previous fiscal years and some known financial information, such as payments on bonds currently issued, projected into the future. Because this is known information we agree that this is within the scope of what should be included in the CAFR. In other words, the financial projections contained in the exposure draft are not based on known financial information and it is our opinion these should not be reported in the CAFR as a result.

An example of a projected number now included in the CAFR is the inclusion of the projected spend down of General Fund balance, in the next fiscal year, as an assignment of fund balance. We do not agree that even this limited projection should be included in the CAFR because of the potential for a misleading impact on public perception and possible erroneous negative effect on governing body decision making. As an early implementer of Statement 54 we encountered a real life example of this was the impact of this projection on the fiscal year 2010 General Fund, fund balance. The projected Montana decreasing General Fund revenues for fiscal year 2011, as included in the 2010 CAFR, resulted in a \$70.3 million assignment of fund balance. Instead of encountering the assumed revenue shortfall we had an unanticipated increase in revenue and, as a result, fund balance during fiscal year 2011. Because the "projection" used in the 2010 CAFR process was not accurate (we encountered an unanticipated economic recovery), this resulted in a fund balance "swing" of over \$114.6 million. Without the incorporation of this one year financial projection in the fund balance for

fiscal year 2010, the fund balance increase for 2011 would have been a more reasonable \$44.6 million. This provides a real life example of how volatile some of our “projections”, even only one year out, can be.

Even though we do not conceptually agree with the reporting required in the exposure draft my staff and I are providing the following responses to the specific questions contained in the document.

Question 1

Comments on components 1, 2 and 3 – The state of Montana currently prepares a cash-flow for the State’s General Fund to determine whether we will need to issue “TRANS”, and at what point in time these would be needed. The Governor’s Office and Legislative Fiscal Division prepare a General Fund analysis on a budgetary basis for each biennium. These reports are only accurate if there are no major changes in the economy during the related timeframes. Based on our experience, the extended projections defined in these three components, would be very time consuming to prepare and would only be of value if the underlying assumptions were correct, and there were no material changes in the national and worldwide economies.

Component 4 – We do not always issue bonds that are authorized and some bonds are not issued until many years after authorization have passed. As a result, the fact that bonds are authorized should not drive the reporting. We believe the reporting currently provided in the CAFR, which includes schedules of known bond payments into the future, provides better financial information than that included in component 4.

Component 5 – It appears that we would be required to include the financial information relating to other separate legal entities, not considered component units of the State, if this were adopted. We believe this goes beyond what should be included in a CAFR.

Question 2

Not without significant changes to the existing State policy process. The estimates currently developed during the State policy process may lose their accuracy because of timing and other factors. For example, I do not use the Legislative revenue estimate (HJR-2) in the cash-flow process, discussed above, because it loses its accuracy over the biennium. By the end of the first fiscal year included in the estimate, the projected information is 15 months old and by the end of the second year of the biennium it is 27 months old. If this estimate were used as the State policy for this process it would need to be more flexible and adjusted to follow actual revenue trends during the biennium. Also, current State policy as used in the Legislative process only goes out two years. We do not currently carry these estimates out 5 years.

Question 3

We believe the modified accrual basis (using fund balance) should be used, rather than the cash basis approach, for determining liquidity because it is still important to understand what will be available to spend. The accrual basis is not a good measure of what is available and does not add value to a 5 year fiscal sustainability projection because some of the numbers go out much further than 5 years. We don’t see any value in abandoning our current modified accrual based fund balance approach.

Question 4

We do not believe these financial forecasts should be prepared whether they are on a principle based or other approach. We would need to either hire additional staff, i.e. and economist and actuary, or contract with professionals to provide this information. We do not have this expertise in our office.

Question 5

We believe the projections beyond one or two years will have no value based on our past experience in the biennial budget process. We also believe there is significant legal risk in forecasting information for any number of years in our CAFR. If these were materially incorrect, which in many cases they will be, and an investor purchased revenue bonds, we believe they would seek relief in the court system.

Question 6

The users of the basic financial statements can put these in context by looking at the State, national and worldwide economies. They can also look at past financial statements and use this information to build their own projections into the future. Other branches of the government can build financial forecasts using their internal assumptions/parameters and provide these to the public. We do not believe financial forecasts are needed in the CAFR to put the basic financial statements into context.

Question 7

We believe this would be too expensive and costly for the governments within the State of Montana, including the State, to implement. While this would be both difficult and costly for a state to implement, it would be even more so for smaller governmental entities, where there is probably the most risk. We do not believe the changes to the CAFR contained in this exposure draft are cost beneficial.

Question 8

If implemented a phase in period would definitely be needed.

We appreciate the opportunity to comment on this exposure draft and hope this is not issued as a Standard, in any form, by the Board.

Sincerely,

A handwritten signature in black ink that reads "Paul A. Christofferson". The signature is written in a cursive style with a large, sweeping initial "P".

Paul Christofferson, CPA