

FINANCE DEPARTMENT

March 16, 2012

Director of Research and Technical Activities

Re: Project 13-3, Preliminary View of the GASB on Economic Condition Reporting: Financial Projections

The Town of Cary embraces the preparation of financial projections as a key component of our strong financial management program, however we strongly oppose the mandatory inclusion of financial projections in required supplementary information to the historical financial statements. We prepare financial projections as a part of our budget process and also in association with bond sales. These projections and subsequent comparison to actual results are a key component in the recognition of our prudent financial management through AAA bond ratings from all three rating agencies. Our financial reporting for both budgets and historical information earn recognition from our peers at the Government Finance Officers Association.

The Town of Cary demonstrated leadership in governmental accounting through participation in both the GASB 34 field test and the preliminary view field test on financial projections. We have significant concerns about this project both in concept and execution. Regarding the underlying concept that projections should be included in historical financial statements we believe that projections in the historical financial statements would:

- 1. Not be comparable. A key value in our current regulatory framework for financial reporting is comparability. Reporting of historical events can be controlled to ensure comparability through accounting, auditing and reporting standards. Projections cannot be reliably consistent or comparable because we cannot control, or even imagine, future significant political decisions, financial markets or environmental changes that will materially affect financial outcomes. Each preparer of projections reaches different conclusions simply depending on an inherently optimistic or pessimistic outlook.
- 2. <u>Illustrate invalid results.</u> Financial projections are based on innumerable assumptions. Knowing these assumptions will be subject to the scrutiny of every financial statement reader, the projection preparers will be overly cautious and conservative to the point that the projections will be invalid or will succumb to political pressure to report an excessively positive outlook that will also result in projections that are invalid. Readers would make invalid conclusions about either projected distress or success in a government's financial future.
- 3. <u>Establish unreasonable expectations for revenues and spending.</u> Projections published along with historical financial statements send a very different message than internally prepared projections for planning purposes.

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Published projections could create expectations for taxes or expenditures that could result in legal challenges from employees, vendors, bond holders and/or taxpayers.

In addition to our firm position against the inclusion of projections in the historical financial statements we have very serious concerns about the preliminary view guidance for developing the projections. The only possible outcome is a lose-lose situation. If the proposed standards are implemented, government officials, and particularly government financial managers, will lose credibility and our citizens' faith in government will be unfairly damaged. In particular, we believe that:

- 1. Results are inflammatory and grossly inaccurate. In contrast with GASB's mission to establish and improve standards of financial reporting that will result in useful information and educate the public, the definition of "known" events and the prescription for preparation of the projections results in reports of figures that are inflammatory and grossly inaccurate. In the Town of Cary, a AAA rated government, the field test resulted in financial projections that would lead a reader to have significant concerns about the financial management of the Town. The definition of "known" and other standards for preparation of the data result in projections that vary significantly from our internal planning documents. In North Carolina where state law requires a balanced budget, the deficits in our projection results are in conflict with those laws.
- Credibility will be damaged. There will be a miniscule percentage of readers who 2. understand the projection standards, and we believe they will disregard the projections, but all other readers will be misled. That vast majority of readers will either lose faith in the credible remainder of the report or worse yet, believe the inaccurate projections, regardless of the disclaimers. The inflammatory and inaccurate reports will create opportunity for politicians and the media to "expose" a negative picture of government. When, not if, questions arise from the inflammatory reports, government officials will have to contrast the inflammatory reports with fairly prepared projections that are based on realistic expectations. By preparing two sets of projections, akin to "keeping two sets of books", our credibility will be inherently damaged and our ethics will be at question. Some small percentage of the interested parties will lose respect for GASB for establishing invalid projection standards, and the remainder will not believe in the realistic projections and will lose trust in government staff and officials.
- 3. <u>Bond markets will be unfairly impacted.</u> Inflammatory and inaccurate reports will create concern in the government bond marketplace and could unfairly impact both initial bond sales and the secondary market. Investors could lose value and governments could experience higher interest rates because of an inaccurate perception of risk. This risk and potential liability alone could incent governments to manipulate their projections even within the GASB standards.

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4. We will incur unreasonable costs in time and expense. Burdensome costs of staff time to prepare a second set of projections, the related out of pocket cost for auditor review and then the cost of time spent to explain why the projections are invalid is a legitimate concern, but a secondary concern compared to the risk of damage to our credibility.

As government financial managers we are sorely disappointed to see financial management failures result in government bankruptcy and/or defaults on local government debt, but we do not believe that requiring the publication of projections would have prevented these failures or would prevent even one single future failure. Many other factors play a role in those type financial events.

Liabilities, potential liabilities and future risks are best reported as defined in the current standards. Any enhancements to risk reporting should be restricted to *historical* reporting and belong in the notes to the financial statements and/or expanded requirements in management's discussion and analysis. Existing historical trend data could move from statistical sections of the Comprehensive Annual Financial Report into the required supplementary information section of the financial statements to alert readers to trends they may deem noteworthy.

The Town of Cary has demonstrated responsible financial management for our citizens, tax and rate payers, vendors and employees, bond holders and other stakeholders. Our ten year capital plans, ten year general fund operating projections as well as 15 year operating projections for our utility fund are used throughout the year to guide organizational decision making and are crucial components to short term and long term financial and operational success. However, we do not believe that publication of those projections will add meaningful value to financial statement users or governmental financial management. We respectfully recommend that GASB not pursue standards of financial projections in historical annual financial reports.

Thank you for your work on our behalf and the opportunity to participate in this valuable process. Please contact us if we need to clarify or expand on our comments.

Sincerely,

Karen Mills, CPA

Finance Director

Michelle Price, CPA

Controller