Good morning. I am Mark Page, the Director Management and Budget of the City of New York.

Members and staff of the Governmental Accounting Standards Board, I want to thank you for the opportunity to testify before you today on what I perceive to be a serious problem for New York City’s financial future, as well as for the future value of all governmental financial statements prepared in accordance with your Board’s standards.

I recognize that there are different objectives of budgeting and financial reporting. However, I believe that in a government environment the linkage between the two is important. Enacted budgets represent legal mandates for many governmental entities, and also the culmination of the democratic process with regard to how scarce public resources are allocated.

As most of you are aware, in the mid-1970s the city experienced a singular financial crisis. A loss of access to public credit markets blocked the city’s ability to refinance its short-term notes as they come due. The immediate consequences were a failure to pay outstanding notes in accordance with their terms, very nearly the bankruptcy of the largest city in the United States, and extraordinary rescue efforts by the State of New York and the United States government, among others.

At the time financial information about the city’s financial condition was obscure, available only long after the reporting period, and of uncertain accuracy. When confidence failed, the lack of clear, timely and accurate financial information was a very serious problem. Starting with an automated city-wide budgeting and accounting system first implemented in 1978, the city has since earned a solid reputation for the clarity, timeliness and accuracy of its financial information.

However, much of the structural financial problem in New York City which gave rise to its fiscal crisis relates directly to the Board’s current proposal to replace “current financial resources” with “near-term financial resources” as a measurement focus.

New York City’s budget practices leading up to its 1975 crisis built a growing financial weakness stemming from a continuous failure to align genuine current resources with current expenditures in each fiscal year, the fiscal year being the unit of expenditure and resource planning on which the whole political process of budget development and resource allocation rests.

As a practical matter, prior to 1975 the city demonstrated that funding for current
spending needs could be met by the expedient of borrowing against the future, selling revenue or tax anticipation notes against next year's resources. The current period works fine on that basis. The next period may not work so well when the notes are due and resources are still needed for current expenses, but as long as credit is available, the problem can be met by again borrowing from the future; effectively accelerating future period revenues to meet current expenses.

A different version of much the same pattern is a failure to respect a capital versus operating distinction for the use of the proceeds of long term bonds. Again, resources naturally available in the future can be skimmed off early through obligations to pay future debt and spent on current services.

The long term recovery of the City's fiscal management, and the slow re-growth of confidence in its creditworthiness over many years, has rested heavily on a painstaking adherence to the current principals of accrual accounting applicable to governments. The statutory mandate for annual fiscal balance, combined with those accounting principles, has ended the practice in New York City of resorting to borrowing against the future to maintain an otherwise unsustainable level of spending on services in the current fiscal period.

The mechanism has forced the city to continuously restrain current spending to an amount not exceeding revenues attributable to the same fiscal year period. Along with clear, timely and accurate fiscal information, this discipline has given the city 30 years of currently balanced audited operating results. This discipline and performance has been a vital part of the city's success at regaining a reputation for fiscal integrity and credit worthiness.

A standard for resource or expenditure recognition that relates to the timing of the cash flows, rather than the period to which those flows relate, would not be helpful. Thus, upon learning of the Board's proposal to trade its current standards for just such a measurement focus, I must point out what role the existing body of governmental generally accepted accounting principles as promulgated by GASB and its predecessors has played in the City's evolution to financial transparency and resiliency.

As I've tried to illustrate, the solid financial foundation upon which the City now rests includes the heavy reliance on governmental GAAP noted in the opening paragraph of this letter. Obviously, the true financial health of New York City and every other public entity is dependent on the responsible budgeting and management of public resources. However, the enforced reliance on GAAP has given NYC officials, both elected and appointed, a robust framework to work within and a yardstick by which we know the credit markets and others will judge us.

Under current governmental GAAP, readers of all governments' financial statements can rely on audited governmental-fund financial statements prepared on a basis which is generally informative and useful from a budgetary perspective, regardless of what budgetary basis the individual entities might use. By including all revenues of the period which are available to finance current expenditures, and
all expenditures of the period normally expected to be paid from those resources, the current financial resources measurement focus provides a standardized proxy of what a responsible approach to budgeting might look like. Discarding this measurement approach in favor of a more “symmetrical” measurement focus dedicated exclusively to liquidity would be a disservice to users of financial statements and greatly diminish the value of fund statements prepared in accordance with GAAP. The presentation of a cash-flow statement would arguably better allow readers to assess liquidity, if that is really the overriding objective.

I am also concerned about the proposed use of “remeasured values” in governmental funds. For example, when reporting an interest rate swap which fails to qualify (or to continue to qualify) as a hedging derivative instrument, recognition of gains or losses from changes in market interest rates over time are not, as a practical matter, changes in current (or near-term) financial resources if the swap is not expected to terminate and the government is going to continue to pay interest at the amount determined by the swap agreement. Because this “revaluation” amount will never be “monetized,” it does not substantively meet the Board’s conceptual criterion that “remeasured amounts are more appropriate for assets that will be converted to cash” because the fair value changes will not actually be converted to cash, despite falling into the category of financial assets. Similar issues arise when considering other financial assets, such as investments that will be held to maturity. If the Board were to require such assets to be revalued in a governmental fund, it would force fund accounting further afield from a budgetary basis, as governments could not rationally be expected to budget for changes in market values of assets (or liabilities) which will never ultimately impact cash receipts or payments. I believe the concept statement should be explicit in stating that only those financial assets whose market value fluctuations would reasonably be expected to impact a government’s future cash flows would be candidates for remeasurement in a governmental fund.

Again, I thank you for the opportunity to comment on the PV, and I would be pleased to answer any questions.