March 28, 2017

Mr. David R. Bean
Director of Research and Technical Activities
Project No. 24-16ED
Governmental Accounting Standards Board
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Mr. Bean:

Baker Tilly Virchow Krause, LLP (“Baker Tilly”) appreciates the opportunity to respond to the GASB Invitation to Comment (ITC), Financial Reporting Model Improvements—Governmental Funds.

Baker Tilly is a large accounting firm with approximately 300 partners and 2,700 team members, and is ranked in the top 15 of American CPA firms. Baker Tilly performs approximately 1,000 audits of governmental entities annually. We have drawn on this experience in preparing our response for your consideration.

The overall theme in our responses to the questions posed in the ITC is the importance of budgetary comparison information in the financial statements to promote financial accountability. We believe the information in the government-wide financial statements provides the needed information relevant to the long-term perspective. The near-term model supports the accountability of current government leadership in directing the use of current year revenue. The complementary balance of the government-wide statements with the fund financial statements paints the full picture.

Question 2.1: Do you believe that governmental fund financial statements should continue to present information that reflects a shorter time perspective than the information presented in the government-wide financial statements and that focuses on financial, rather than economic resources? Why?

Yes, the governmental fund financial statements should present information that reflects a shorter time perspective than the government-wide statements. The near-term approach properly focuses on the financial resources that are available to support current government services and obligations. This focus supports the government’s responsibility of operating within a legally enacted budget. Government officials have a responsibility to adhere to the government’s budget, and the near-term approach closely reflects the importance of that process. Most elected officials, and the public at large, can readily understand the near term approach to financial reporting; a movement away from this approach could result in information that is less useful and effective.

Additionally, the information provided in the governmental fund financial statements differs significantly from the government-wide statements providing users with multiple perspectives. The combination of the governmental fund financial statements and the government-wide statements present the necessary near-term and long-term perspective in a complementary way.
Question 2.2: Do you believe that governmental fund financial statements should continue to present information that facilitates comparisons with a government’s budgetary information? Why?

Yes, the governmental fund financial statements should continue to present information that facilitates comparisons with a government’s budgetary information. Users rely on budgetary information and the budget-to-actual comparison to hold the government financially accountable. Unlike the private sector, government budgets are legally enacted by elected officials after taxpayer input. These budgets are more than a management tool, they are used to assess the decision making of elected officials, offers transparency and holds them accountable for their financial decisions.

Question 2.3: Which of the three recognition approaches provides the most relevant information for assessing fiscal accountability of the government? Why do you consider that information most relevant?

A combination of a longer-term and shorter-term perspective provides valuable information for assessing fiscal accountability. Near-term is the best choice for the governmental fund financial statements because it focuses on the financial resources for the reporting year, which is highly relevant to current leadership decisions. Fund financial statements do not need to show long-term accrual information because that is available in the government-wide statements. Together, the fund financial statements and the government-wide statements provide the full picture necessary to assess fiscal accountability of the government.

Question 2.4: Transactions related to tax anticipation notes or revenue anticipation notes are presented differently under the three recognition approaches. In the near-term approach, borrowings on and repayments of these notes would be reported as inflows and outflows of resources on the statement of resource flows and in the reconciliation to the government-wide statement of net position. In the short-term and long-term approaches, outstanding balances of these notes would be reported as liabilities on the balance sheet, and borrowings on and repayments of these notes would be reported in the statement of cash flows. Which approach to the reporting of these notes provides the most valuable information? Why?

We generally support the provisions of the proposed near-term approach, however, we are least comfortable with the treatment of TANs and revenue anticipation notes under the proposed near-term approach. It may be misrepresenting the use of current financial resources if the short-term debt instruments which are expected to be paid back in the near-term are not reflected on the balance sheet.

Governments may use these instruments in different ways. When one government may regularly have outstanding TANS every year-end, another government may only periodically issue TANs, for example, when a local government issues TANs because the State is delayed in distributing taxes. We have concerns on the comparability aspect of government financial statements. A government could be showing a favorable fund balance when, in fact, they are borrowing against the next year’s revenue. If Government A chooses to issue TANs close to year-end, and comparable Government B chooses not to, Government A may appear to some readers to be in a more favorable financial position due to the higher fund balance. Although we acknowledge the effect of the short-term debt instrument would be reflected on the government-wide statements and in the notes to the financial statements, we believe some users may not fully understand the impact of that short-term debt on the governmental funds. Therefore, we recommend TAN and revenue anticipation notes be accounted for in a similar method as the existing reporting model.
Question 2.5: Views vary on the definition of the financial resources – a concept integral to all three recognition approaches. What definition of financial resources provides the most valuable information? Why? Do you consider prepaid items to be financial resources? Why? Do you consider inventory to be financial resources? Why?

Generally, we agree that financial resources are cash or assets that can be easily converted to cash. We agree with the near-term’s approach to expense the cost of inventory in the year it is purchased. We believe it is a management decision if a government purchases multiple periods of inventory, and by reflecting that full purchase in the current year properly reports how management is expending resources.

However, we believe prepaid items are often a result of a minor timing difference that should be accommodated in the same way as the accounts payable provisions. These items should be reported as expenditures in the proper fiscal year. Additionally, prepaid items are sometimes refundable and can be converted back to cash. Without reporting prepaid items in the fund financial statements as a financial resource, minor timing differences could have significant impacts on fund balance.

Question 2.6: For the recognition approach that you believe provides the most valuable information, how would you change that recognition approach to provide information that is more valuable? How would those changes make the information more valuable?

We believe the near-term approach is preferred for governmental funds.

Changes to consider to the near-term approach:
1) TANS should be reported as fund level liabilities as discussed in our response to Question 2.4.
2) Prepaid items should be reported as a fund level asset as discussed in our response to Question 2.5.

Question 2.7: Paragraph 6 of Chapter 2 discusses a same page reconciliation to government-wide information and the use of specific terminology to more clearly communicate that the information in governmental fund financial statements is of a shorter time perspective than information in the government-wide financial statements and focuses on financial, rather than economic, resources. Are these changes effective in communicating that the information in governmental fund financial statements is different from the information in government-wide financial statements? How could those differences be communicated more effectively?

A separate reconciliation is more valuable than a highly summarized same page reconciliation. Although showing a condensed reconciliation on the face of the governmental funds statement does highlight that there is a difference to financial statement users, it requires users to search the notes of the financial statements to obtain the full picture. One of the purposes of the current research on notes to the financial statements is to identify information that is not necessary to be reported in the notes to the financial statements. Requiring the notes to house the details on the reconciliation is counter to that goal. We believe a reconciliation containing sufficient detail within the basic financial statements is preferable.
Question 3.1: Which format for the governmental funds resource flows statement – existing format or current and long-term activity format – provides the most valuable information about governmental funds? Why do you consider the information to be more valuable?

The existing format of the governmental funds resource flows statement provides the most value because it does not disaggregate line items such as debt service payments, capital outlay and transfers, which are all common fund level activities. It would be difficult for users of the financial statements to visualize the full effect of these items under the disaggregated approach of the current and long-term activity format. It would also take more time to prepare and audit the current and long-term activity format and would not provide additional benefit to users.

Question 3.2: Should a statement of cash flows be required for governmental funds? Why?

No. We support the near-term approach for reporting governmental activities and believe no statement of cash flows should be required because the flows statement provides sufficient information about near-term changes in financial resources.

Question 3.3: What difficulties, if any, would arise in presenting a statement of cash flows for governmental funds?

Preparing and auditing a statement of cash flows for governmental funds would be time consuming and not add much value for users under the near-term approach.

Question 3.4: Are the four classifications for the statement of cash flows from Statement No. 9, Reporting Cash Flows of Proprietary and Nonexpendable Trust Funds and Governmental Entities that Use Proprietary Fund Accounting, the most appropriate for governmental funds? If not, what classifications would be most appropriate?

If the Board determines a cash flow statement is essential, the classifications for the statement of cash flows should be as consistent with Statement 9 as possible. Unless there is a good reason to move away from Statement 9, we support the existing four classifications. However, certain items will need to be reevaluated, including the classification of property taxes and sales taxes in governmental funds which may not fit within the current guidance in Statement 9. Implementation guidance would likely be needed if the Board moves forward with a required statement of cash flows for governmental funds.

We appreciate the opportunity to provide comments on this exposure draft. Should you wish to discuss any of these comments, please contact Heather Acker at heather.acker@bakertilly.com or 608 240 2374.

Sincerely,

BAKER TILLY VIRCHOW KRAUSE, LLP