DATE: March 27, 2017

TO: Government Accounting Standards Board

FROM: Alan Skelton, State Accounting Officer

RE: Invitation to Comment (ITC FRM) - Financial Reporting Model Improvements—Governmental Funds

We are pleased to provide the following responses on the Governmental Accounting Standard Board’s (GASB’s) to this Invitation to Comment. This project could potentially have a profound impact on the overall financial statements produced by the State and we welcome this opportunity to provide comments to the Board. Consistent with the ITC FRM we have provided answers to questions as outlined in the document.

Chapter 2: Recognition Approaches for Governmental Fund Financial Statements

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

Assuming that the fund statements and the government-wide statements will continue to exist and any discussion to eliminate either one is NOT on the table, we believe the governmental fund statements should reflect a shorter time horizon. The State believes it is imperative that the two statement types provide two distinct purposes as to avoid confusion and provide the reader with a perspective of both the financial and economic resources of the state. If this time perspective is not maintained, the purpose for the two statements would become less clear and some may ask what would be the point. Some respondents may think elimination of the fund statements is actually preferable, but we do not believe that topic is open for discussion.

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

As acknowledged in the ITC, budgets are an integral part of managing a government and are based on a budgetary basis of accounting which in many cases is either cash or some other method which is not GAAP but easily reconciled to the current modified accrual basis of accounting. The more fund statements move away from this perspective the less relevant the numbers are to legislative and
executive branch leadership and harder for preparers to communicate the intended message. It is already difficult to engage certain stakeholders in substantive conversations about the CAFR. The further we move away from the budgetary basis the harder that will become.

Some may argue that budgetary statements are already required by their state and therefore this perspective is not warranted. We would suggest that governmental fund statements that are presented on a consistent basis provide for comparisons across government entities and mitigates the differences that may exist in budgetary practices across different governments. Given the importance of budgets we think this perspective is critically important.

We strongly believe that the governmental fund statements should reflect a shorter time horizon which is consistent with budgetary practices. The shorter time horizon can provide certain stakeholders with important information on the need to adjust tax revenues or reduce program expenditures from one year to the next. Fund statements need to occupy a space somewhere on the continuum between cash and full accrual.

2.3. Which of the three recognition approaches provides the most relevant information for assessing fiscal accountability\(^1\) of the government? Why do you consider that information most relevant?

We consider fiscal accountability to be the responsibility for government leaders to ensure that amounts expended do not exceed resources available as articulated in our constitution. As a result of that definition, the State believes that the near-term approach is the most relevant. It appropriately excludes liabilities which are not due while also excluding revenues that are not available.

On a side note, we also cannot help but note that the near-term recognition approach most closely mirrors the modified accrual approach used today. While the approach currently in place lacks a “conceptual foundation” it was developed over time by prepares and auditors and therefore does provide a starting point from which an informal framework does exist. We believe it makes sense to start with what we developed organically rather than throwing that out and starting over.

The short term approach is clearly closer to the near term approach and therefore also closer to the budgetary perspective. However, we believe the confusion this method could introduce relative to long term liabilities such as pension and OPEB does not warrant its selection over the near-term approach.

Finally, we also believe the long-term approach is the most divergent from budgetary reporting and from the State’s perspective provides little to no discernable linkage to our budgetary process. As such we do not understand why it should even be considered given the assumption articulated in our answer to question 2.1.

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. (See the discussion in Chapter 3.) Which approach to the reporting of these notes provides the most valuable information? Why?
The State does not issue tax anticipation notes and has deferred any judgement on this specific question.

2.5. Views vary on the definition of financial resources—a concept integral to all three recognition approaches. (See the discussion in paragraphs 38–40 of Chapter 2.) 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?

We believe financial resources should refer to cash, cash equivalents, items that are readily converted to cash, and resources that can be used in lieu of cash.

As for prepaids and inventory, the State does not directly consider these items as revenue to be used to balance the budget. However, these items could be considered when appropriating amounts for expenditure—resulting in a lower appropriation. So it does not need to be considered a resource (in terms of part of the revenue estimate) to have an impact on the budget. We believe these items should be considered financial resources in all approaches.

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 think the near-term approach is favorable for two main reasons—it is closest to budgetary basis and most similar to modified accrual basis which is used today. As such we are not sure we would change anything at this point.

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?

We are supportive of examples but would prefer flexibility. All governments are not created equal and we believe this is one area in flexibility regarding presentation which can be provided without any negative impact on reporting.

Chapter 3: Other Governmental Fund Financial Statement Issues

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?

Current format since the State prefers near-term approach and therefore discussion of long-term activity is not particularly relevant to that approach.

3.2. Should a statement of cash flows be required for governmental funds? Why?
Not for near-term but possibly yes for others. We believe the near-term approximates cash and do not believe significant additional information justifies the time and effort required to produce this statement. As for short-term and long-term approaches, a statement of cash flow MAY make more sense due to the divergence from cash.

However, we do find it interesting that after spending time on multiple bond rating agency calls, we have never heard a question about our Statement of Cash Flows. There are questions for treasury and cash flows but these are typically not related to the statements in the CAFR.

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

Time, effort, and complexity of doing it for all the funds for which a Statement of Cash Flow has never been prepared. For the State this would require preparing cash flow statements for over 60 trial balances in order to produce a consolidated cash flow statement.

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?

Yes

1Fiscal accountability reflects a shorter time perspective than that conveyed by the information in the government-wide financial statements and focuses on financial, rather than economic, resources.

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