March 31, 2017

Mr. David Bean
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Project 3-25I — Invitation to Comment on Financial Reporting Model Improvements — Governmental Funds

Dear Mr. Bean:

Deloitte & Touche LLP is pleased to respond to the GASB’s invitation to comment (ITC) on Financial Reporting Model Improvements — Governmental Funds.

We commend the GASB for its continued efforts to improve the reporting model by undertaking a multi-phase project to reexamine it. There are a number of topics for consideration in the project that we believe could improve financial reporting for government financial statement stakeholders.

Government-wide financial statements contain information that is important to users such as bond-rating agencies, creditors, grantors, citizens, and elected officials as well as to others such as management and auditors. Fund-level financial statements, however, contain information that is narrow in scope and is not comparable between governments. It is therefore our strong belief that such information should be excluded from the basic financial statements because it does not provide sufficient incremental benefit to the broad user community. Instead, it should be provided separately in response to specific requests or as supplemental information.

As we previously commented before the issuance of GASB Statement 34, we believe that presenting financial information for the same activities by using two different bases of accounting increases the complexity of the basic financial statements without providing sufficient benefit to users. In addition, fund-level statements were created to demonstrate compliance (e.g., to note whether resources were used for their intended purposes) and to meet the needs of specific groups, not for general-purpose external financial reporting and basic financial statements, as discussed in GASB Concepts Statement No. 3. Further, compliance and fund-level reporting structures (such as the use of fund types and the aggregation or disaggregation of
activities into funds) differ between and within types of governments, leading to lack of comparability between them. Thus, we believe that fund-level financial statements should not be a part of the basic financial statements.

While we do not believe that fund-level financial statements are a necessary part of the basic financial statements, we recognize that the GASB may, on the basis of stakeholder feedback, decide that they should be retained or included as supplemental information. We have therefore evaluated the three recognition approaches proposed in the ITC for governmental funds and have concluded that the near-term approach has the most merit.

We appreciate the GASB’s efforts to align accounting for governmental funds with the more cohesive conceptual foundation. We agree with the GASB’s observation that certain accounting conventions under the current modified accrual model result in inconsistencies year over year and between entities. As the GASB acknowledges, none of the proposed approaches is perfect; however, since the near-term approach is most closely aligned with the current modified accrual reporting model, it would be the least disruptive and the most beneficial.

We encourage the GASB to consider making incremental revisions to the current model rather than adopting a new model. Doing so would retain familiar terminology and statement formatting as well as avoid unnecessary changes. Our recommendations are further discussed below and in the attached appendix, which contains our detailed responses to the ITC’s questions.

**Near-Term Approach**

As noted above, we believe that the near-term approach most closely aligns with the current modified accrual model. Accordingly, implementing this approach would be the least cost-prohibitive of the three approaches the GASB presented. In addition, because this approach is closely aligned with the budget basis of reporting (and similar to the cash basis), it offers a different perspective from that in the government-wide financial statements and therefore minimizes duplication of information presented in the report. In adopting this approach, we recommend that the GASB revise the current modified accrual model (keeping the format and terminology) and make incremental modifications to adapt for conceptual corrections.

**Short-Term Approach**

The short-term approach focuses on a government operating cycle of one year. We believe that certain reported amounts will be difficult and costly to measure under this method, which would lead to further inconsistencies in practice (related to “amounts normally due within the next operating cycle”). For example, under the
short-term approach, pension and other postemployment benefit (OPEB) liabilities would need to be recorded for the annual required contribution. Governments would therefore need to calculate their pension and OPEB liabilities in accordance with GASB Statements 27 and 68 and Statements 45 and 75, respectively, incurring significant costs related to both the calculations (actuarial valuations) and the related audits. We also believe that this approach duplicates information that is to some extent available in the government-wide financial statements, such as the subsequent operating cycle’s portion of bonded debt and lease obligations. Including such liabilities as well as the related outflows in the fund-level statements, and continuing to report the related current-period costs as expenditures, would only further complicate the statements for the average user.

**Long-Term Approach**

This approach focuses on long-term results of the government and would cause duplication between fund-level and government-wide reporting. We do not believe that this approach would provide meaningful information that is not otherwise available in the government-wide financial statements. If specific user groups require individual fund information, they have the option to request it from the government. Requiring all governments to provide such information is overly burdensome given that the information may not be relevant or necessary.

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If you have any questions concerning our responses, please contact Mike Fritz at +1 614 229 4806.

Yours truly,

Deloitte & Touche LLP

Cc: Robert Uhl
Appendix — Responses to Questions in the ITC

This project was undertaken by the Board to obtain stakeholder feedback on potential improvements to the existing financial reporting model for governmental funds related to:

- Recognition approaches (measurement focus and basis of accounting).
- Format of the governmental funds statement of resource flows.
- Specific terminology.
- Reconciliation of the government-wide statements.
- For certain recognition approaches, a statement of cash flows.

We have provided below our detailed responses to the questions posed in the ITC.

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?

If, on the basis of its research, the Board considers governmental fund financial statements to be valuable to all users, the information presented in them should be based on a shorter term perspective than that presented in government-wide financial statements. It is important to differentiate fund-level information from government-wide data and to focus on financial resources rather than economic resources. Fund-level information should more closely align with the way a government operates on a daily basis and prepares its budget. It should not duplicate information presented at the government-wide level.

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?

We believe that governmental-fund financial statements should be prepared on an accounting basis that is similar to — or the same as — the accounting basis used to prepare the budget for those funds. In our experience, the most frequent users of the governmental-fund financial statements are members of management and the governing body, who use the statements as a management tool, often in conjunction with the budget document. While we do not believe that budget reporting should be a part of the basic financial statements, it is logical to facilitate a comparison of the budget to governmental financial statements by using the same or a similar basis of accounting.
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?

The near-term approach provides the most relevant information for governmental-fund financial statements. This approach is most closely aligned with the basis by which the majority of governments prepare their budgets. A basis of accounting that is closest to budget, cash, or both is the most relevant one for assessing performance relative to budget and accountability. Taxes, fees, and charges are set on the basis of expected (budgeted) expenditures, and grant revenues are derived from expenditures that must accord with the approved (awarded) budget. Similarly, we believe that the activities of debt service and capital project funds are best presented on a basis close to cash or budget because the focus is on current-period inflows and outflows of resources as well as on the available fund balance for future debt service and capital project needs.

The consistency issues identified in the current modified accrual model would potentially be corrected with the least amount of change under this approach. We believe that if the GASB decides that fund-level financial statements should continue to be included as part of the basic financial statements or as supplementary information, financial statement preparers will view this approach more favorably, and fund-level financial statement users will understand it more easily, than the other approaches and that it would promote more consistent application of fund-level financial reporting requirements between entities.

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?

We believe that under the near-term approach, if tax and revenue anticipation notes have not been repaid as of year-end, the amounts due should be reported as liabilities on the balance sheet so as not to distort fund balance in any given year. We believe that it is imperative that the face of the governmental fund financial statements display the economic effect of these transactions on a government’s financial position. While this is our preference and recommendation to the Board, we recognize that this could be viewed as an exception to the conceptual basis of near-term. If the Board prefers not to make such a specific exception, we strongly recommend that the Board instead require outstanding balances of tax and revenue
anticipation notes to be displayed as a classification other than unassigned fund balances to make it clear to users that a portion of fund balance has been borrowed from anticipated taxes or other revenues.

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 that financial resources are best defined as items that *can be or are expected to be converted to cash.* We do not consider inventory or prepaid assets to be financial resources. Such treatment in the financial statements will be consistent with that for the budget (items are generally treated as expenditures in the year budgeted). On the basis of the nature of government inventory and prepaid items, such items are not revenue-generating (sold for cash) and will never become financial resources. The nature of these items is such that they are consumed and expensed. We agree with the GASB’s treatment of these items under the near-term approach.

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 propose the following general changes:

- **Consistency** — We believe that the near-term approach provides the most relevant information but that it should be implemented through incremental revisions to the current modified accrual accounting model. We recommend that to ease implementation overload and improve acceptance and support, the GASB adjust the current model only for the modifications that will achieve the most consistency between entities and for necessary clarifications in the absence of current guidance.

- **Format** — We recommend that the terminology, format, titles of statements, et cetera be retained from the modified accrual accounting model wherever possible. We do not believe that revising the format or terminology of the statement of revenues, expenditures, and changes in fund balances will benefit users.

- **Placement** — As we previously stated, we consider the government-wide financial statements to be the most valuable financial statements, and we believe that fund-level financial statements should be excluded from the basic
financial statements. If the GASB concludes that they continue to be important to financial statement users, we recommend that they be placed in supplementary information.

- **Reconciliation** — We do not believe that the reconciliation between government-wide financial statements and fund-level financial statements should be included as a schedule in the report because the narrative disclosure in the footnotes that explains the nature of the statements provides sufficient information for educated users to understand the statements. Our response to question 2.7 provides additional information related to this topic.

We propose the following specific changes:

- **Near-term defined** — We believe that the GASB needs to define the “within the near-term” period to clarify that it refers to a set number of days that cannot be left open to individual interpretation. We recommend a 60-day period, which is consistent with current guidance on property tax revenues and generally the number of days governments select for other revenue streams. Further, defining the period will promote consistency, which is one of the key objectives of reexamining existing guidance for the modified accrual basis of accounting.

- **TANs/RANs** — As previously mentioned, we believe that tax and revenue anticipation notes (TANs/RANs) with balances as of year-end should be reported as liabilities in the near-term financial statements so as not to distort fund balance in any given year. These liabilities are short term in nature, very often repaid in the near term, and many times do not cross fiscal years. However, TANs/RANs that do cross fiscal years and are not recorded as liabilities provide an opportunity to manipulate fund balance when they are issued but not repaid by year-end.

- **Accrued interest on long-term debt** — We believe that the treatment of accrued interest on long-term debt is inconsistent with the treatment of the related debt under the near-term approach. We do not believe that this amount should be accrued unless it is past due if such debt is only accrued when past due. While we understand the conceptual basis in near-term for including this liability, such a practice is not consistent with how governments budget interest payments and is also inconsistent with how accrued interest is treated under modified accrual.

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?

When GASB Statement No. 34 was first issued, government-wide and fund-level financial statements were new and difficult concepts for preparers and users to understand. The reconciliation between the two different bases of accounting served as a method of educating everyone and helping to implement the new standard. Once users and preparers became better acquainted with the statements, the reconciliation became less valuable and was redundant with the narrative provided in the notes to the financial statements. The reconciliation has, in essence, become a working paper for financial statement preparers and auditors that is not an essential part of the basic financial statements if the notes adequately disclose the nature of the government-wide and fund-level financial statements. We do not believe that the GASB should require the reconciliation to be included in the basic financial statements.

**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?

We believe that the current format of the statement of revenues, expenditures, and changes in fund balances is less flawed than that described in either of the approaches (existing or current and long-term approach) presented in the ITC. We do not believe that a change in presentation that uses "inflows" and "outflows" is necessary or provides any additional information to the user. The GASB should evaluate the cost and benefits of implementing the proposed changes.

**Questions Related to Cash Flows**

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

We support the ITC’s proposal to exclude a cash flow statement from the near-term approach. Because the near-term approach is similar to a cash basis, information about cash flows is not needed, and no value would be added in providing this
statement. We point out that the nature of governmental funds is such that no matter the approach, the value of a cash flow statement is virtually nonexistent for the vast majority of individual governmental funds. While amounts reported in the statement of long-term financial resource flows and the related statement of cash flows may differ, preparing such statements for a debt service or capital project fund, for example, is not a meaningful exercise because it offers the reader no additional useful information. One of the purposes of the cash flow statement is to provide insight into activities of the entity that may be obscured by noncash amounts such as depreciation and capitalized interest. These amounts are not reported in governmental funds. These are just two such examples, and many others could be identified. We do not believe that there are sufficient indicators that a cash flow statement and the additional incremental information it contains — regardless of the approach adopted — would provide measurable benefit to the user.