March 10, 2017

David R. Bean, Director of Research and Technical Activities
Governmental Accounting Standards Board
Project No. 3-25I
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

Re: Financial Reporting Model Improvements—Governmental Funds, Project No. 3-25I

Dear Mr. Bean:

The following is the response of the Government Accounting and Auditing Committee of the Washington Society of Certified Public Accountants (WSCPA). The views expressed are the views of the Committee and not necessarily the views of the individual members or the WSCPA as a whole. We are pleased to have the opportunity to respond to the Governmental Accounting Standards Board’s (GASB) Invitation to Comment (ITC) Financial Reporting Model Improvements—Governmental Funds.

We support the mission of GASB, to establish and improve standards of state and local governmental accounting and financial reporting.

**Background and Nature of Our Response:**

As noted in Chapter 1, Paragraph 2, we understand that this project does not represent a “clean slate” approach, rather specific improvements are provided. Paragraph 8 states “The current financial resources measurement focus, which is used at present for reporting governmental funds, does not have a cohesive, conceptual foundation. Rather, it is applied as a collection of accounting conventions intended primarily to present a shorter time perspective of the activities reported.” We agree with this statement. Furthermore, we agree with the analysis presented in Appendix C that the economic resources measurement approach most closely correlates to the Concepts Statement Number 1 objectives, except for budgetary and financial resource flows (the latter may be satisfied with a cash flow presentation). With current robust financial accounting systems, available to all governments, we believe that reporting financial information and budget information can be accomplished without the need to link financial reporting and budgetary reporting. In other words, we believe that budgetary reporting considerations should no longer drive sound accounting theory. However, there are some that believe that financial reporting should support the budget reporting objectives.
We expect that the GASB found in its pre-agenda research activities that there are divergent views on this matter and our committee is no exception. As such, we provide all comments, whether in agreement or not. In essence, our disagreements center on how important budgetary compliance is to external financial reporting and the cost/benefit of any suggested changes, including timeliness.

**Overview of Our Response:**

We encourage the GASB to include the economic measurement focus and basis of accounting for governmental funds as a fourth option in preparing its Preliminary Views Document. We believe this option better presents the underlying economic condition of a government and presents inter-period equity in a way that the current financial resources measurement focus cannot. This option would have the benefit of eliminating the need to reconcile the fund financial statements to the government-wide financial statements, and therefore, reduce the users’ confusion regarding differing measurement focus and basis of accounting. GAAP allows for differing basis and perspective in reporting budgetary information and that presentation is most properly included as required supplementary information.

Regarding certain users’ need to understand “spendable” resources, available to be used in the ensuing operating period, the current fund balance (net position) reporting will work. Capital assets, much like inventory, cannot be used to fund operating expenses in the ensuing operating period, and long-term debt is an obligation that must be met from future resources.

If the economic measurement focus and basis of accounting for governmental funds as a forth option is not considered, then we would support the long-term approach as it most closely resembles the economic measurement focus and then only capital assets and capital-related debt would be excluded from the fund presentation and be the only items included in a reconciliation to the government-wide financial statements. The prevailing attitude is that this type of change should ease the financial reporting burden and not add to it. Some thoughts expressed by our committee suggest that adding a cash flow statement without eliminating the budgetary statements/schedules and other changes would only add to the burden. Those that agree with this concept would argue that no change should be made. For those governments that use financial reporting as a means to present legal budget compliance, no change would be better than any change.

We also present the alternative views that recognize that financial reporting should assist in the reporting of budgetary information in a short-term or long term basis.

The following presents our answers to the specific questions:

**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?

Response: No, we believe fund financial statements should be based on economic resources as discussed in our overview provided above. This option would have the benefit of eliminating the need to reconcile the fund financial statements to the government-wide financial statements, and therefore, reduce the users’ confusion regarding differing measurement focus and basis of accounting.

An alternative view is that yes, the governmental financial statements should continue to present the information that reflects the shorter time perspective. The economic resource perspective is presented for governmental funds at the entity-wide level. Presenting economic resource perspective at the fund level would make it very difficult to demonstrate compliance with the budget.

The ITC does not address the impacts of the various approaches to the budgetary and fund statement presentation options. Changing from the current “near-term” to either the short-term, long-term or economic resources will involve various levels of added burden and those differing levels of burdens should be considered and explained in a future Preliminary Views document.

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?

Response: No, as noted above, we believe that budgetary presentations may be made as RSI and there is no need to link financial statements to budgetary presentations. GAAP allows for differing basis and perspective in reporting budgetary information and that presentation is most properly included as required supplementary information. We do not believe that it is necessary for governmental financial statements to facilitate budgetary information. There is also a view that if the burdens from budgetary reporting is not eliminated or reduced, when a cash flow requirement is added, then the current approach should not be changed.

The alternative view is that yes, governmental budgets are the primary method by which citizens and their elected representatives hold the government’s management financially accountable. Maintaining the relationship between the information provided by governmental fund financial statements and the budget is a major consideration when determining the appropriate measurement focus and basis of accounting for and presentation of governmental fund financial statements.
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?

Fiscal 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.

**Response:** We believe accountability should be based on the underlying economic condition of a government and methods to present inter-period equity in a way that the current financial resources measurement focus cannot. The ITC discusses ways in which the focus on current financial resources can obscure underlying economic condition. Accountability should be based on whether decisions positively or negatively impact the financial condition of a government. Prior to current pension standards, a legislative body could pass generous benefits enhancements, COLAs etc. (especially if the aggregate actuarial method were used) without any detriment to the current budget. As such, under the current financial resources approach, they wouldn’t be held accountable for the new liability created in the current period that must be paid from future resources for many years.

If the Preliminary Views document does not include the economic resources measurement as an option, then we would support the long-term approach as it most closely resembles the economic measurement focus. However, we believe that all assets and deferred outflows and all liabilities and deferred inflows should be presented in fund financial statements.

The alternative view is that Short-term financial resources is the best method. This approach would provide conceptually consistent recognition principles for governmental fund financial statements. Using a consistent 12-month measurement period would be vastly better than having each government decide its own criteria. It would provide a better basis for assessing inter-period equity than the current financial resources measurement focus.

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?

**Response:** Borrowings do not improve the financial condition of an entity (i.e., debit cash, credit liability, no equity improvement). Inflows from debt to pay for current expenses/expenditures obscure the fact that future resources to pay for future services are reduced in that the debt must be repaid. The long-term approach to place the liability on the
statement of net position and then reflect the resource flows in the statement of cash flows is preferable and provides the most valuable information. Once again, we note that some on our committee would not add a cash flow requirement unless other burdens are reduced.

The alternative view is consistent with our primary response. This is an example of how some governments are able to manipulate their fund balances. An approach reporting these anticipation notes as liabilities on the balance sheet would eliminate these practices.

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?

Response: If the GASB follows our suggestion to use the economic resources measurement for governmental funds then this question becomes mute. The focus will be on assets + deferred outflows minus liabilities+ deferred inflows. Taken literally, neither prepaid items nor inventory is a financial resource, yet they provide “resources” to satisfy the next year’s operating cycle. Once again, the focus on assets and liabilities should help in determining the theory on this issue. If an asset is an asset, then it should help to accomplish the next years’ operating goals. Whether it is a “financial” resource should not matter. Prepaid items, depending on the nature of the item should benefit the ensuing operating period. Likewise, inventory is expected to benefit the ensuing operating period. We believe that neither of these items are “financial” in nature but both are assets that should be reported in fund financial statements.

The alternative view states that financial resources are items that can be or are expected to be converted to cash or are consumable in lieu of financial resources, including prepaid items and inventory. Prepaid items are financial resources because they are consumable in lieu of financial resources. Inventory is a financial resource because inventories are consumable in lieu of financial resources.

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?

Response: It is time for GASB to disregard “old” thoughts of preparing financial information inappropriately encumbered by budgetary considerations and move to a paradigm that reports “true” economic reality. Fund financial statements should be prepared on the same basis as the government-wide statement, and in fact, should present all assets and liabilities as in the government-wide basis. In effect, there would be no need to present fund financial information as the government-wide financial presentation would suffice. This would eliminate the need for any reconciliation between the fund financial
statements and the government-wide financial statements. We believe users will understand this reporting paradigm much better than the current reporting model.

The alternative view states that the short-term approach is based on the concept of symmetry for assets and liabilities. This approach would recognize all of the obligations that are payable and normally due within the subsequent operating cycle, along with the existing resources that are available in the same period to satisfy these obligations.

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?

**Response:** Consistent with our overall response, we believe the fund financial statements should not require any reconciliation. If difficulties are identified consistent with the “long-term” approach, then just two reconciling items should be necessary: capital assets and capital-related debt and no other.

The alternative view states that the reconciliation more prominently identifies the recognition differences between the governmental fund information and governmental activities information in the government-wide financial statements, and may serve to draw users to the government-wide financial statements if they want to better understand the items not recognized in governmental funds.

**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?

**Response:** Consistent with our overview comments, we believe that all revenues and expenses using the economic resources measurement focus and accrual basis of accounting should be used for the resource flow statement for governmental funds. It is acceptable to separately present program revenues from general revenues. If capital assets are allocated to the funds, then we believe that depreciation should be captured in the funds flow statement.

The alternative view states that the current and long-term activity format of the governmental funds resource flows statement provides the most valuable information about governmental funds because it reports inflows and outflows of resources related to the
purchase and disposal of capital assets and the payment and issuance of long-term debt separately from other current-period activities of a governmental fund.

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

**Response:** If GASB adopts our recommendation to use the economic measurement focus and accrual basis of accounting for governmental funds, then we believe a “consolidated” cash flow statement is warranted because it will present the cash paid for capital items and payments on long term debt that won’t be captured in the operating statements.

The alternative view states that yes, as we move further away from cash based accounting using either the short-term approach or the long-term approach, governmental fund financial statements should include a statement of cash flows.

Once again, there is a view that adding a cash flows statement should be offset by a commensurate reduction in other reporting areas.

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

**Response:** Allocating capital assets among governmental funds would be the most difficult. If this could be accomplished, then governments could report just like any business enterprise. The alternative view supports cash flow statements and doesn’t see any difficulties.

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?

**Response:** The current classification seems to work well, and we suggest no changes. Perhaps this could be subject to future deliberation.

**Summary of Specific ED Comments:**

While we have expressed divergent views, the majority committee response is for GASB to consider the economic resources measurement flow and full accrual basis of accounting for governmental funds. If a “budgetary-basis” of accounting is to be followed, then we support the long-term or short-term approach and not the current financial resources model.

The main conflict within our committee is whether financial statements need to support budgetary accounting. Some see no need to support budgetary reporting, while others see a continuing need to support budgetary reporting. Any change should reduce the effort to prepare financial statements and not add to the burden.
Thank you for the opportunity to respond. If you have any questions or need additional information regarding this response, please contact Steve Miller at (206) 281-0281 or he prefers email at mandmps@comcast.net.

Sincerely,

SENT VIA E-MAIL to director@gasb.org

Mary Ann Hardy, Chair
Government Accounting and Auditing Committee
Washington Society of Certified Public Accountants