March 24, 2016

Project No. 3-13E
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, Connecticut 06856-5116

This letter is in response to GASB’s proposed standard that addresses certain changes in the accounting for fiduciary activities.

Suggested Changes to the Text

You might want to consider the following changes in the text of the proposed standard to improve its clarity:

1. A critical term used in paragraph seven is the term *beneficiary*. The GASB might want to consider defining this term. A possible definition might be “the party identified to receive outflows associated with assets held by the reporting government”. If this is not your intention, a more clear description of your intent as to the meaning of this term would be appreciated.

2. To improve clarity, you may want to add clarifying language (italized below) to paragraph 7(c) “the assets are to be provided to organizations or other governments that are neither part of the financial reporting entity nor recipients of the goods or services provided by the primary government or its component units.

3. The clarity of both paragraphs 7(b) and 7(c) might be improved if “for purposes unrelated to the programs of the reporting government” I are added as a required element of their application. Otherwise, some readers might inappropriately classify certain activity as fiduciary simply because they are paid to vendors that are not required to be residents, recipients of the government’s goods and services, or organizations that are not part of the financial reporting entity.

4. The distinction between own-source revenues and revenues that are not own-source is not clear. As the final statement becomes implemented in actual practice, there may be a certain amount of confusion as various forms of revenue are identified that may not clearly fall within the subtle distinction suggested by the proposed standard for these two broad classifications of revenue. For example, although intergovernmental aid is not an own source revenue, it is not clear how non-government contribution revenue should be classified. I am not sure what the intention is with respect to the distinction provided in the proposed statement for own-source revenue. Perhaps the statement should define more clearly the aspects of those revenues meant to be excluded from the scope of this statement rather than to use a term that has an ambiguous meaning.
Practical Situations for Which Application of the Proposed Standard is Not Clear

1. Some local governments have established a fiduciary fund to account for deposits that are refundable to the paying party once that party has satisfied certain requirements. Typically these are for contractor performance deposits for private construction to be performed by that contractor within the jurisdiction of the reporting government. Once the construction has been inspected and found to meet certain local requirements, the deposit is returned to the contractor. This activity appears to fall within the scope of paragraph 7(b). The parties receiving these assets are “not required to be residents or recipients of the government’s goods or services as a condition of being a beneficiary”. This activity may also fall within the scope of paragraph 7(c). If it is not your intent for this activity to fall within the scope of a fiduciary fund, you may want to consider clarifying criterion 7(b) to prevent a misapplication of this guidance to the situation described above.

2. If the above activity will continue to be reported in a fiduciary fund, it is unclear whether or not the language of paragraph 18 would require that this activity be reported as a liability upon receipt. Paragraph 18 says that “a government should “recognize a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources. Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action or condition is required to be met by the beneficiary to be entitled to receive the resources.” The words “entitled to receive the resources” might suggest to some readers that since the depositor has been identified as the party to receive the assets, the “entitled to receive” criterion has been met. This might suggest to some readers that the deposit should be recognized as a liability immediately upon receipt. Other readers might believe that “entitled to receive” means that all events have occurred to permit the immediate disbursement of the assets to the intended party. You may want to consider adding a sentence that states that “a recipient is not considered entitled to receive the assets if approval is required prior to release of the assets” or other language to avoid an inconsistent application of this guidance.

3. Some local governments have established a fiduciary fund to account for assets to be used for purposes understood by the government to be expenses of the paying party, rather than a payment to support a program of the reporting government. For example, the assets held by a local government may be required to be remitted to third parties to pay for certain services relating to a private development that is an obligation of the developer, such as an environmental impact review. Since the assets are paid to “organizations that are neither part of the financial reporting entity nor recipients of the government’s goods and services”, some local governments might believe that 7(c) applies to these situations. If that is not your intent, language should be added to avoid an inconsistent application of this guidance.

4. Some local governments use fiduciary funds to account for deposits paid by private construction contractors to be applied toward the payment of certain inspection and review services that are outsourced by the local government to private vendors. This appears to be inconsistent with your
intended use of the fiduciary fund type. However, some readers of the proposed statement may believe that this qualifies for fiduciary fund treatment because the “the assets are to be provided to organizations that are neither part of the financial reporting entity nor recipients of the government’s goods and services” [paragraph 7(c)].

5. On occasion, a local government will establish in its accounting system a fund to account for the cash activity of a nonprofit corporation (that is not a component unit) or a joint venture (for which it is a member). The local government issues the checks for the corporation or joint venture (“the other organization”) pursuant to a budget adopted by the governing board of the other organization. Some readers might believe that this qualifies as a fiduciary activity and meets the requirements of paragraph 7(c). If that is not your intent, clarifying language should be added to the proposed statement.

6. Same as Scenario 5, but in addition, the local government provides recordkeeping services for the other organization. In this situation, may the local government report all of the assets (receivables, capital assets, etc.) of the other organization, or only the cash that is held on behalf of the other organization?

7. A local government has a Section 457 deferred compensation plan. A committee of non-management employees selects a vendor that provides investment options (to be selected by each employee) for each employee’s account and that processes retiree requests for the disbursement of funds to the retiree. As presently worded, different local governments might reach different conclusions as to whether or not in this situation “the government has the ability to administer or direct the use, exchange, or employment of the present service capacity of the assets”. Additional clarifying language should be added to the standard to assure a consistent application of this new guidance for fiduciary funds.

8. Same as Scenario 7, except that the vendor is selected by management employees.

9. The governing board of a local government has selected a private company to hold its OPEB assets in an irrevocable trust that meets all of the requirements of paragraph 4 of GASB Statement No. 75. This private company invests the assets under a broad investment program strategy selected by the local government. The local government determines the amount of disbursements to be made to retirees. As presently worded, different readers might reach different conclusions as to whether or not the determination of benefits payments and the selection of a broad investment program is such that it constitutes “administering” or “directing the use”. It would be best for local governments to report similar situations in a similar manner. Language should be added to the statement to further define these terms.

10. The governing board of a local government has approved placement of its OPEB trust assets into an irrevocable trust administered by the state’s PERS system. This trust meets all of the requirements of paragraph 4 of GASB Statement No. 75. The investments of the trust will be determined and managed by the state PERS system. The local government will determine the amount of disbursements to be made to retirees. Some readers might believe that the role of the PERS system in managing the assets of the
trust and inclusion of this OPEB trust in the plan financial statements issued by the PERS system might allow for excluding this trust from the fiduciary funds reported by the local government. Adding language to address this fairly common situation will contribute toward uniform reporting of similar circumstances.

11. A state-run PERS agency has created separate irrevocable trusts for those local agencies that wish to advance fund their contributions to the state-administered pension program. The trusts meet all of the requirements of paragraph 4 of GASB Statement No. 68. At the discretion of the local government, the assets held in this separate trust, can be applied in any given year toward that agency’s required contribution to the pension system for that year. The local government controls and determines the timing and amount of such application of these funds towards its annual contribution requirement. The state-run pension system will administer this separate “prefunding trust” for that local employer and invest the monies held consistent with the PERS’ investment management practices. Clarifying language should be added to the proposed statement to ensure consistent application in practice by readers that might report this situation differently.

Sincerely,

Ken Al-Imam, CPA