To: GASB Director <director@gasb.org>
Subject: For GASB: Pennsylvania’s comments on GASB’s Invitation to Comment related to Revenue and Expense Recognition (Project No. 4-6I)

Dear Dave:

We are pleased to provide comments on the Governmental Accounting Standards Board’s (GASB) Invitation to Comment (ITC) regarding Revenue and Expense Recognition. We appreciate GASB’s ongoing efforts to provide transparency and consistency in our financial reporting for all our financial statement stakeholders.

Overall, we agree that having additional authoritative guidance addressing revenue and expense recognition will help to improve uniformity and consistency in the reporting of governmental entities. Additionally, centralizing the guidance into one standard will be more efficient when researching issues impacting revenue and expense recognition. We have a concern that the ITC only addresses the economic resources measurement focus and does not consider recognition for the financial resources measurement focus. We understand that GASB is waiting until a final determination is made regarding the new approach in the financial reporting model project, however making the exchange/nonexchange determination for recognition of revenue and expenses in the governmental fund financial statements is the basis we use for making the determination for recognition of revenue and expenses on the government-wide financial statements. As such, we agree that guidance should be developed to address the recognition of transactions for the financial resources measurement focus used in the governmental fund financial statements.

In assessing the revenue and expense recognition models presented in the ITC (exchange/nonexchange, performance obligation/no performance obligation, and the alternative model), we conclude that the exchange/nonexchange model would be the best model to utilize in developing a comprehensive revenue and expense recognition model. We will present our reasoning further in our responses to the questions provided below.

Question 2.1: Do you believe the exchange/nonexchange model would provide a suitable basis for classifying transactions and recognizing revenue and expense? Why or why not?

Yes. We believe that the exchange/nonexchange model provides the most suitable basis for classifying transactions and recognizing revenue and expense. While the ITC indicates that some challenges currently exist in practice with classifying exchange and nonexchange transactions due to the subjectivity of the assessment of value, as financial statement preparers we have not identified any significant issues with classifying exchange and nonexchange transactions for our financial statements. As such, we believe the current classifications being used are effective and we do not see any reason to change the classifications. We have, however, identified some issues surrounding recognition of certain exchange transactions such as revenue related to multi-year hunting licenses or driving licenses. Additional guidance surrounding recognition of such transactions could be included in the comprehensive model. Therefore, we believe that utilizing the current, more familiar classifications of exchange and nonexchange transactions, while also providing more robust guidance surrounding exchange transactions and the term equal value, as well as other problematic areas identified by GASB and the Financial Accounting Foundation, would be the most logical track to take in developing a comprehensive revenue and expense model.
Not only would implementing the exchange/nonexchange model be the least costly to implement, having the familiarity of the terminology and recognition methodology for nonexchange transactions would likely result in a more feasible and consistent implementation across entities. Additionally, with so many other changes being proposed by GASB currently or slated for the near future, having some continuity by maintaining the exchange/nonexchange classifications and recognition approaches would allow us to provide more focus and resources on implementing the more significant and time consuming changes to our accounting and financial reporting coming down the pipeline, such as leases and changes to the financial reporting model.

**Question 3.1: Do you believe the performance obligation/no performance obligation model would provide a suitable basis for classifying transactions and recognizing revenue and expense? Why or why not?**

No. The performance obligation/no performance obligation model introduces a list of all new complications to revenue and expense recognition and does not appear to provide much benefit in return. In the ITC, one of the benefits that GASB identified for this model is the intention to simplify the manner of classifying transactions by focusing on the existence or absence of a performance obligation. Although determining the existence or absence of a performance obligation may seem simple in theory, the definition of a performance obligation in the ITC uses new terminology that in practice, even with the further definition in the ITC, would be open to differing interpretations and subjectivity. The subjective nature of the terminology introduces new and significant challenges to classifying revenue and expense transactions. For example:

- The determination of whether an arrangement would be legally enforceable as a binding arrangement may often require the involvement of an attorney, as accountants may not have the training or expertise to make that judgment call. The involvement of an attorney would result in more time-consuming and expensive processes for classifying transactions, and potentially delayed preparation of financial statements.

- Whether the arrangement identifies rights and obligations of the parties that articulate in equivalent terms could be somewhat subjective in nature and confused with the term equal value used in classifying exchange transactions. Making such a determination may also require the involvement of an attorney.

- There may be differing opinions of whether goods or services have the ability to benefit a recipient individually or if the goods or services would need to be bundled to be considered distinct and specifically identifiable in the arrangement.

- The definition of specific beneficiary does not explicitly define how sufficiently distinguishable from the general public the specific beneficiary must be. For example, preparers would have to determine if citizens of Pennsylvania are considered distinguishable from the general public and should be identifiable as a specific beneficiary.

Without further substantial application guidance surrounding those terms, we believe that the subjective nature of the definition of a performance obligation would result in additional reporting inconsistencies and would not resolve the current issues identified regarding inconsistencies in classifying revenue and expense transactions.
As presented in the ITC, this model also involves allocating consideration to each performance obligation. Determining the value of the consideration to be allocated to each performance obligation would likely prove to be challenging, as all contracts may not be written to explicitly identify each performance obligation, and all contracts would need to be reviewed to see if they contain multiple performance obligations.

In addition, with the implementation of the performance obligation/no performance obligation model, the re-evaluation of transactions for proper classification and recognition would be time-consuming and costly, and tracking the extent that obligations have been satisfied to properly recognize the revenue/expense would be very burdensome. Financial statement preparation would likely take considerably longer due to requiring non-financial statement preparers to make judgment calls related to the various aspects of determining whether an arrangement is a performance obligation. There are numerous variations of arrangements that would need to be evaluated. After all this analysis has been completed, we are not convinced that revenue and expense recognition would be materially different than under the exchange/nonexchange model. From our standpoint, the performance obligation/no performance obligation model would likely involve an extensive amount of work for what appears to be very little added benefit, and we believe the costs of implementing this model would far outweigh any benefits identified.

Lastly, we are wondering whether the term “no performance obligation” could be negatively interpreted by our constituents. We consider the term “nonexchange transaction” to be more positively perceived that the term “no performance obligation.” Because the word performance implies an action, the term “no performance” seems to imply we don’t need to do anything beyond collecting the tax or revenue. We realize this is not the case in fact and that most users of our financial statements will also have this understanding, so it may not be a significant point in this discussion, but we wanted to bring it up for consideration, nonetheless.

**Question 4.1: Do you believe that the alternative model presented as an example in Chapter 4 could provide a suitable basis for classifying transactions and recognizing revenue and expense? If so, what are the potential benefits and challenges of that model?**

No. Although the exchange and nonexchange classifications would be familiar, the issues we identified with the performance obligation/no performance obligation model would still exist and would likely result in more inconsistencies in financial reporting. Thorough implementation guidance would be necessary, and the costs of implementing this alternative model would outweigh the benefits of implementing this model.

**Question 4.2: The models distinguish transactions on the basis of (a) exchange or nonexchange or (b) a performance obligation or no performance obligation. Do you believe there is another alternative for distinguishing revenue and expense transactions? If so, please describe that alternative and explain why you believe it would be suitable.**

As expressed above in our response to Question 2.1, we are in favor of the exchange/nonexchange model presented in the ITC. We do not believe there is a benefit to establishing another alternative model.

As you have read, we agree that developing a comprehensive revenue and expense model for state and local governments would be helpful in creating uniformity and consistency across government financial reporting. Additionally, we believe that guidance surrounding the recognition of transactions for a financial resources measurement focus would also need to be addressed before issuing further due process documents for revenue and expense recognition. We are in favor of the proposed
exchange/nonexchange model but have major concerns surrounding the complexity, time and costs of implementation regarding the performance obligation/no performance obligation model, as well as the alternative model presented in the ITC, especially when considering that any new model may not produce materially different results.

We appreciate your consideration of our comments.

Best Regards,

Anna Maria

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