April 27, 2018

Mr. David R. Bean
Director of Research and Technical Activities
Project No. 4-6I
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Bean:

We are pleased to comment on the Governmental Accounting Standards Board’s (GASB or Board) Invitation to Comment, Revenue and Expense Recognition (ITC).

We are supportive of the GASB’s continued efforts to improve financial reporting for governmental entities. We agree that existing guidance for exchange revenue and expense transactions is limited and existing guidance for nonexchange revenue and expense transactions could be improved through clarification. Therefore we support the consideration of developing a comprehensive revenue and expense model with the goal of enhancing guidance surrounding various types of transactions and making financial information more consistent and useful for users of governmental financial reports in making decisions and assessing accountability.

Overall Comments

The ITC states that it is limited to the recognition of revenue and expense transactions for the economic resources measurement focus, thus the recognition of transactions for a financial resources measurement focus may need to be addressed based on future conclusions that the Board reaches in the Financial Reporting Model (FRM) project. The conclusions reached by the Board in the FRM project and how the recognition models described in this ITC impact those conclusions could potentially alter the comments we have provided in our response. To fully assess the suitability of each of the models presented and evaluate the potential benefits and challenges they each bring forth, we believe stakeholders would have to understand how each model impacts every component of a government's financial statements, not only the portions that follow the economic resources measurement focus.

In addition, although we appreciate the inclusion of the examples in Appendix A, we did not readily see significant benefit in the three basic examples provided. Each example included a description of how the example transaction would be classified differently under the exchange/nonexchange model and performance obligation/no performance obligation model, however the conclusions related to the recognition of revenue and expense for each example transaction was similar under each of the two recognition models. Therefore, it was difficult to assess the recognition impact each model would have since they ultimately resulted in the same recognition method. Additionally, we believe that existing guidance on each of these example transactions is clear and that governments have typically reported these transactions consistently. If the Board decides to move forward with this project, it would be beneficial if examples were provided with transactions that may have inconsistent application under the
current model along with additional examples that have varying recognition conclusions based on the proposed model chosen.

Our detailed responses to the questions proposed in the ITC are included in Attachment A.

Please contact Scott Lehman at (630) 574-1605 or scott.lehman@crowehorwath.com or Kevin Smith at (214) 777-5208 or kevin.w.smith@crowehorwath.com should you have any questions.

Cordially,

Crowe Horwath LLP
Exchange/Nonexchange Model

The exchange/nonexchange model would classify revenue and expense transactions based on whether a transaction is considered exchange or nonexchange. If the transaction is an exchange, revenue or expense would be recognized based on an earnings recognition approach. If the transaction is a nonexchange, revenue or expense would be recognized based on the provisions of Statement 33, as amended.

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?

Certainly, the terminology of exchange vs nonexchange would be familiar with current personnel in governmental entities. In addition, the post implementation review of GASB Statement No. 33 by the Financial Accounting Foundation found that the guidance generally was effective in achieving its stated objectives. Therefore maintaining this existing guidance along with expanding the guidance surrounding exchange transactions would appear to result in less implementation costs and challenges than implementing a new model with significantly more terminology and application changes.

Consequently, under the concept of an earnings approach, governmental fund-type funds typically do not have that many exchange revenues that fund the majority of operations, as many are funded by taxes or revenues that are non-exchange. The concept of an earnings approach might not be intuitive to some since many believe that governments don’t really “earn” the appropriate value of their services provided. In addition, the concept of “equal value” is subject to interpretation which presents disparity in the way different governments or even a single government would classify certain transactions. If this method is retained, we recommend a clearer definition of “equal value” be provided.

Performance Obligation/No Performance Obligation Model

The performance obligation/no performance obligation model would classify revenue and expense transactions on the basis of whether a binding agreement contains one or more performance obligations. If the transaction contains a performance obligation, revenue or expense would be recognized following the performance obligation recognition approach. If the transaction does not contain a performance obligation, revenue or expense would be based on the provisions of Statement 33, as amended.

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?

Although the principal revenue resource for most governments is taxation, which is a legally mandated involuntary transaction between individual citizens and business and their government, this does not change the government’s primary goal of enhancing or maintaining the well-being of citizens and the expectation of performance in return for the taxation. Therefore, the existence of a performance obligation to a specific party (as currently defined) or lack of a performance obligation conceptually best describes the nature of governmental revenues. In addition, the performance obligation guidance and terminology is largely consistent with both Topic 606 of the FASB Accounting Standards Codification and guidance from the International Public Sector Standards Board. This convergence with other standard setting bodies would likely result in greater understanding of governmental financial reporting by users outside of government. Also, with many governments hiring employees from outside the governmental space, a GASB standard that is more similar to FASB pronouncements may lessen the time and effort needed for implementation. Although the complexity of certain performance obligation assessments could be challenging at first, having a defined model to compare to as opposed to unclear authoritative guidance would lead to greater consistency amongst governments.
A potential challenge to this approach would be the introduction of the performance obligation would likely be a burden for units of governments as it would add a level of complexity for the determination of revenue recognition. Complexities already exist in the revenue recognition for non-exchange transactions such as grants and taxes on both the modified accrual and full accrual basis, and an additional level of consideration for revenue recognition will likely add to the existing complexities.

Alternative Models

Other alternative revenue and expense recognition models could be suitable for governments.

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?

Utilizing this model continues to follow the exchange/nonexchange concepts governments are familiar with and the model that appears to recognize and account for the distinct activity found within governments. The model then adds further guidance for exchange transactions that is currently lacking and bases this guidance on recognition concepts that more defined and consistent with other industries. Also, since this model mainly impacts exchanges transactions, and governments are predominately funded by nonexchange revenues, the implementation costs/burden would not seem to be as large.

This model also introduces the performance obligation/no performance obligation concepts which will lead to challenges as described in our response to Question 3.1. In addition, although this alternative model would address some of the current shortcomings, having two conceptual definitions could continue to cause confusion long after the challenges of implementation have passed.

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.

There is no other alternative model for distinguishing revenue and expense transactions that we would like to propose at this time.