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Statement No. 80 of the Governmental Accounting Standards Board

Blending Requirements for Certain Component Units

an amendment of GASB Statement No. 14

GASB

GOVERNMENTAL ACCOUNTING STANDARDS BOARD
OF THE FINANCIAL ACCOUNTING FOUNDATION

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Summary

The objective of this Statement is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units. This Statement amends the blending requirements established in paragraph 53 of Statement No. 14, *The Financial Reporting Entity,* as amended.

This Statement amends the blending requirements for the financial statement presentation of component units of all state and local governments. The additional criterion requires blending of a component unit incorporated as a not-for-profit corporation in which the primary government is the sole corporate member. The additional criterion does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units.*

The requirements of this Statement are effective for reporting periods beginning after June 15, 2016. Earlier application is encouraged.

How the Changes in This Statement Will Improve Financial Reporting

The requirements of this Statement enhance the comparability of financial statements among governments. Greater comparability improves the decision-usefulness of information reported in financial statements and enhances its value for assessing government accountability.

Unless otherwise specified, pronouncements of the GASB apply to financial reports of all state and local governmental entities, including general purpose governments; public benefit corporations and authorities; public employee retirement systems; and public utilities, hospitals and other healthcare providers, and colleges and universities. Paragraph 2 discusses the applicability of this Statement.

Statement No. 80 of the
Governmental Accounting
Standards Board

Blending Requirements for Certain Component Units

an amendment of GASB Statement No. 14

January 2016

GOVERNMENTAL ACCOUNTING STANDARDS BOARD
of the Financial Accounting Foundation
401 Merritt 7, PO Box 5116, Norwalk, Connecticut 06856-5116

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January 2016

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January 2016

INTRODUCTION

1. The objective of this Statement is to improve financial reporting by clarifying the financial statement presentation requirements for certain component units.

STANDARDS OF GOVERNMENTAL ACCOUNTING AND FINANCIAL REPORTING

Scope and Applicability of This Statement

2. This Statement establishes an additional blending requirement for the financial statement presentation of component units. This Statement applies to all state and local governments.

3. This Statement applies to component units that are organized as not-for-profit corporations in which the primary government is the sole corporate member. This Statement does not apply to component units included in the financial reporting entity pursuant to the provisions of Statement No. 39, *Determining Whether Certain Organizations Are Component Units.*

4. This Statement amends Statement No. 14, *The Financial Reporting Entity,* paragraph 53, and *Implementation Guide No. 2015-1,* Question 4.30.1.

Additional Blending Requirement

5. A component unit should be included in the reporting entity financial statements using the blending method if the component unit is organized as a not-for-profit corporation in which the primary government is the sole corporate member,[1] as identified in the component unit's articles of incorporation or bylaws, and the component unit is included in the financial reporting entity pursuant to the provisions in paragraphs 21–37 of Statement 14, as amended.

EFFECTIVE DATE AND TRANSITION

6. The requirements of this Statement are effective for reporting periods beginning after June 15, 2016. Earlier application is encouraged.

7. Changes adopted to conform to the provisions of this Statement should be applied retroactively by restating financial statements, if practicable, for all prior periods presented. If restatement for prior periods is not practicable, the cumulative effect, if any, of applying this Statement should be reported as a restatement of beginning net position (or fund balance or fund net position, as applicable) for the earliest period restated. In the first period that this Statement is applied, the notes to the financial statements should disclose the nature of the restatement and its effect. Also, the reason for not restating prior periods presented should be disclosed.

The provisions of this Statement need not be applied to immaterial items.

[1]The sole corporate member requirement in this Statement should not be analogized to any other situations that may be considered similar to those in which the primary government is the sole corporate member, such as situations in which the primary government is the residual equity interest owner.

This Statement was issued by unanimous vote of the seven members of the Governmental Accounting Standards Board.

David A. Vaudt, *Chair*
Jan I. Sylvis, *Vice-Chair*
James E. Brown
Brian W. Caputo
William W. Fish
Michael H. Granof
David E. Sundstrom

Appendix A

BACKGROUND

A1. Statement 14, as amended, establishes financial reporting requirements for the financial reporting entity, such as criteria for inclusion of component units, and display and disclosure requirements. Statement 14 was reexamined in a project that resulted in the issuance of Statement No. 61, *The Financial Reporting Entity: Omnibus.* After the issuance of Statement 61 in 2010, questions were raised regarding the appropriate presentation of certain component units. For example, what should be the appropriate presentation of a component unit when a governmental healthcare entity acquires a legally separate not-for-profit organization (that remains legally separate) to expand services? Those questions have focused on whether those entities meet the blending requirements established in paragraph 53 of Statement 14, as amended.

A2. After receiving feedback from members of the Governmental Accounting Standards Advisory Council (GASAC) in December 2013, the Board initiated pre-agenda research regarding the prevalence of component units and their organizational structures in governments primarily engaged in business-type activities. The pre-agenda research included archival research of governmental financial reports and a survey of users of those financial reports. The results of the research were discussed by the Board in July 2014. The pre-agenda archival research highlighted diversity in practice among governments primarily engaged in business-type activities in the application of the standards for component unit presentation.

A3. In August 2014, the Board initially added a project on blending requirements for certain governments engaged in business-type activities to the practice issues portion of the GASB's current technical agenda. Deliberations began in November 2014. During deliberations leading to the Exposure Draft, additional research was conducted regarding the prevalence and presentation of certain not-for-profit component units in general purpose governments. Based on this research, as noted in Appendix B, the project scope was expanded to encompass all state and local governments.

A4. In June 2015, the Board issued an Exposure Draft, *Blending Requirements for Certain Component Units*. The Board received 21 responses to the Exposure Draft from organizations and individuals. As discussed throughout Appendix B, comments and suggestions from those respondents contributed to the Board's deliberations in developing the requirements of this Statement. Feedback also was provided by GASAC members and subject matter experts throughout the Board's deliberations.

Appendix B

BASIS FOR CONCLUSIONS

Introduction

B1. This appendix discusses factors considered significant by Board members in reaching the conclusions in this Statement. It includes discussion of the alternatives considered and the Board's reasons for accepting some and rejecting others. Individual Board members may have given greater weight to some factors than to others.

Scope and Applicability of This Statement

Scope

B2. The scope of this Statement is limited to the presentation of certain component units, specifically not-for-profit corporations included in the financial reporting entity pursuant to the provisions of paragraphs 21–37 of Statement 14 and for which the primary government is the only corporate member. The Board considered whether blending is the appropriate presentation for those component units and, if so, whether this Statement should clarify the requirements for blending or establish an additional blending requirement.

B3. This Statement is not the result of the reexamination of Statement 14, as amended. Consequently, this Statement does not address fundamental reporting entity principles established in Statement 14, as amended, such as the criteria for inclusion of component units in the financial reporting entity or the provision that component units should be discretely presented unless the component unit meets established blending requirements.

B4. The Board specifically excluded component units that are included in the reporting entity pursuant to the provisions of Statement 39 from the application of the blending requirement established in this Statement. Statement 39 established provisions for component unit inclusion in the reporting entity for organizations that warrant inclusion in the financial reporting entity's financial statements because of the nature and significance of their relationship with the primary government but for which the primary government is not financially accountable. The Board believes that an explicit scope exclusion will avoid uncertainty in application because this Statement applies to component units organized as not-for-profit corporations, and the component units included in the financial reporting entity pursuant to the provisions of Statement 39 often are not-for-profit corporations.

B5. Respondents to the Exposure Draft commented on that scope exclusion. Some respondents described component unit relationships that they believe may be equivalent to those in which the primary government is the sole corporate member and requested clarification of whether the blending requirements in this Statement would apply to those component units (directly or by analogy). An example used by respondents involved a not-for-profit entity that is a component unit, pursuant to the provisions of Statement 39 that has no corporate members and for which the primary government has a residual interest in the entity's net assets upon dissolution. Statement 39 established that a legally separate entity included as a component unit under its provisions should be discretely presented, regardless of whether that component unit satisfies any of the blending criteria in paragraph 53 of Statement 14, as amended. In considering the respondents' request for clarification, the Board concluded that despite the similarities between component units included in the financial reporting entity pursuant to the provisions of Statement 39 and the component units that would be subject to the blending requirements of this Statement, the blending provisions of this Statement should not be applied to Statement 39 component units. The Board believes that this conclusion is consistent with existing reporting requirements and decided to provide clarification regarding the applicability of the blending requirements established in this Statement to component units included in the financial reporting entity pursuant to the provisions in paragraphs 21–37 of Statement 14 (as opposed to paragraph 5 of Statement 39). Moreover, the Board added footnote 1 to eliminate the possibility of applying the provisions of this Statement, by analogy, to Statement 39 component units.

Applicability

B6. Based on the original inquiries that ultimately resulted in this Statement, the Board considered the implications of limiting the application of this Statement to governments engaged only in business-type activities, but it determined that such an approach would result in inconsistencies in reporting by those governments and by governments engaged in both governmental and business-type activities that encounter the same facts and circumstances. Therefore, the Board concluded that this Statement should be applied to all state and local governments.

Blending Requirements for Not-for-Profit Corporations

B7. As noted in Appendix A, the GASB's initial research indicated that a significant number of component units included in the reporting entity of the governments studied were not-for-profit corporations. For example, as a primary government seeks to expand its operations, it may acquire legally separate entities to expand services or spin off operations to incorporate them into legally separate entities. Many of those legally separate entities that are reported as component units have governing bodies that are representative of the community, and the primary government is the sole corporate member. Generally, those types of component units would not meet the previous blending requirements established in paragraph 53 of Statement 14, as amended, for three reasons:

a. Previous standards do not equate being the sole corporate member to having substantively the same governing body.
b. The main purpose of those legally separate entities is to provide or expand services to the general public, or to entities or individuals other than the primary government and its employees.
c. Although it is possible that the primary government may have some responsibility for the total outstanding debt of the acquired or spun-off entities, it is generally expected that those entities will generate sufficient resources to meet some or all of their own obligations.

B8. The Board believes that being a sole corporate member of a not-for-profit corporation establishes a unique relationship, from the standpoint of financial accountability, between the primary government and the component unit. This relationship is established through articles of incorporation or bylaws and is not found in other component unit relationships in which the primary government appoints the component unit's governing body. Based on this unique relationship, the Board concluded that blending is the appropriate presentation of a component unit that is a not-for-profit corporation, in which the primary government is the sole corporate member.

B9. Some respondents to the Exposure Draft requested that the Board include in this Statement a definition of the term *sole corporate member.* The Board believes that the term *sole corporate member* is not an ambiguous term, nor is there a matter of professional judgment associated with the application of this term because the articles of incorporation or bylaws for the component unit (the not-for-profit corporation) specify corporate membership. Thus, the Board concluded that including a definition in this Statement is unnecessary.

Clarifying Guidance for Limited Liability Companies

B10. The GASB's research showed that some component units included in the financial statements of governments studied were limited liability companies (LLCs). Research regarding the governance models of those entities showed that LLC component units generally do not have separate governing boards. Some respondents requested that this Statement specifically address LLC component units. In considering this request, the Board observed that blending those component units would be consistent with existing financial reporting standards in certain circumstances. Therefore, the Board concluded that including additional blending requirements to address LLCs in this Statement was not necessary.

Equity Interest Ownership

B11. Consistent with decisions made during the development of Statement 61, the Board considered but decided not to establish blending requirements for component units for which a primary government has equity interest ownership of less than 100 percent. Paragraph 60 of the Basis for Conclusions of Statement 61 states, ". . . the Board considered requiring blending, in some or all circumstances, of majority-owned enterprises that are component units. However, that would result in blending of some component units that are not considered to be so intertwined with the primary government that blending is appropriate. Furthermore, that could involve determination of whether a primary government meets a control criterion, which is a conceptually different basis for blending than the financial accountability approach in Statement 14." Respondents to the Exposure Draft requested that the Board consider blending requirements for other corporate structures, such as majority-owned component units, non-member not-for-profit corporations, and partnerships (component units other than bodies corporate and public). The Board considered these requests but decided not to establish blending requirements for these entities because this project was narrowly defined to address a specific issue. Consideration of other component unit structures would require the reexamination of several provisions of Statement 14, including the provision that component units should be discretely presented, unless the component unit meets blending requirements.

Limited Partnerships and Limited Liability Partnerships

B12. The Board also considered whether blending requirements should be established for limited partnerships or limited liability partnerships. However, as noted in paragraph B11, the Board decided not to do so because both types of partnerships imply equity interest ownership of less than 100 percent.

Notes to Financial Statements

B13. The Board considered possible additional requirements for notes to the financial statements related to the blending requirement established in this Statement. Potential notes considered by the Board included a combining schedule for the entire financial reporting entity, which was suggested by respondents to the survey of users noted in Appendix A. The Board believes that existing requirements for notes to the financial statements adequately address the information needs of users. Thus, the Board concluded that this Statement should not require any additional notes to the financial statements.

Considerations Related to Benefits and Costs

B14. The overall objective of financial reporting by state and local governments is to provide information to assist users (the citizenry, legislative and oversight bodies, and investors and creditors) in assessing the accountability of governments and in making economic, social, and political decisions. One of the principles guiding the Board's setting of standards for financial reporting is the assessment of expected benefits and perceived costs. The Board strives to determine that its standards address significant user needs and that the costs incurred through the application of its standards, compared with possible alternatives, are justified when compared to the expected overall public benefit.

B15. Present and potential users are the primary beneficiaries of improvements in financial reporting. Persons within governments who are responsible for keeping accounting records and preparing financial statements, as well as managers of public services, also benefit from the information that is collected and reported in conformity with GASB standards. The costs to implement the standards are borne primarily by governments and, by extension, their citizens and taxpayers. Users also incur costs associated with the time and effort required to obtain and analyze new information to meaningfully inform their assessments and decisions.

B16. The Board's assessment of the expected benefits and perceived costs of issuing new standards is unavoidably more qualitative than quantitative because no reliable and objective method has been identified for quantifying the value of improved information in financial statements. Furthermore, it is difficult to accurately measure the costs of implementing new standards until implementation has actually taken place. Nonetheless, the Board undertakes this assessment based on the available evidence regarding expected benefits and perceived costs with the objective of achieving an appropriate balance between maximizing benefits and minimizing costs.

B17. The Board considered the expected benefits and perceived costs associated with implementation and application of this Statement. The Board believes that implementation costs for the additional blending requirement established in this Statement will be minimal because the Statement will affect only the presentation of certain component units, without impacting the organizations that comprise the financial reporting entity. Specifically, governments will consider whether certain not-for-profit component units should be blended. Because governments will have concluded that the legally separate entity is a component unit, governments already will have all of the necessary financial information for reporting purposes; however, the Board is aware that additional reclassifications may be required for certain component units. Finally, the Statement will not require any additional notes to the financial statements. Considering the expected benefit of increased comparability of financial statements and the anticipated minimal incremental implementation costs, the Board believes that the expected benefits of this Statement will outweigh the perceived costs.

Effective Date and Transition

B18. The provisions of this Statement are effective for reporting periods beginning after June 15, 2016. The Board concluded that this effective date is appropriate because governments implementing the guidance in this Statement already have determined that the legally separate entities affected are component units of the government. Consequently, the primary government should have sufficient information regarding those entities. Some governments may wish to implement the guidance earlier than the effective date, which this Statement encourages.

B19. The phrase *if practicable* has been used in other GASB standards in a similar context as used in this Statement with respect to transition provisions that require restating the financial statements for all prior periods presented. The Board believes that reasonable efforts should be deployed before a government determines that restatement of all prior periods presented is not practicable. In other words, *inconvenient* should not be considered equivalent to *not practicable.*

Appendix C

CODIFICATION INSTRUCTIONS

C1. The instructions that follow update the June 30, 2015 *Codification of Governmental Accounting and Financial Reporting Standards* (Codification) for the effects of this Statement. Only the paragraph number of this Statement is listed if the paragraph will be cited in full in the Codification.

* * *

REPORTING ENTITY AND COMPONENT UNIT PRESENTATION AND DISCLOSURE **SECTION 2600**

Sources: [Add GASB Statement 80.]

.113 [Add new subparagraph (d), including footnote, as follows:] The component unit is organized as a not-for-profit corporation in which the primary government is the sole corporate member,[6] as identified in the component unit's articles of incorporation or bylaws, and the component unit is included in the financial reporting entity pursuant to the provisions in paragraphs .120–.136 of Section 2100. [GASBS 14, ¶53, as amended by GASBS 61, ¶8 and GASBS 80, ¶5; GASBS 80, ¶5]

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[6][GASBS 80, fn1]

.706-1 [In the answer, insert new subparagraph (d):]

d. The component unit is organized as a not-for-profit corporation in which the primary government is the sole corporate member, as identified in the component unit's articles of incorporation or bylaws, and the component unit is included in the financial reporting entity pursuant to the provisions in paragraphs .120–.136 of Section 2100 (footnote omitted).

However, organizations that meet the criteria in paragraph .140 of Section 2100 should be discretely presented, even if they also meet the criterion in paragraph .113b or paragraph .113c of Section 2600.

[GASBIG 2015-1, Q4.30.1, as amended by GASBS 80, ¶5]

* * *

C2. The instructions that follow update *Implementation Guide No. 2015-1* for the effects of this Statement. That Guide, as modified, will be incorporated into the *Comprehensive Implementation Guide.*

* * *

4.30.1. [In the answer, insert new subparagraph (d) and revise the last sentence as follows:]

d. The component unit is organized as a not-for-profit corporation in which the primary government is the sole corporate member, as identified in the component unit's articles of incorporation or bylaws, and the component unit is included in the financial reporting entity pursuant to the provisions in paragraphs 21–37 of Statement 14, as amended (footnote omitted).

However, organizations that meet the criteria in paragraph 5 of Statement 39 should be discretely presented, even if they also meet the criterion in paragraph 53b or paragraph 53c of Statement 14, as amended, or paragraph 4 of Statement 80.

[GASBIG 2015-1, Q4.30.1, as amended by GASBS 80, ¶5]