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David Bean
Director of Research
Project No. 3-25
Governmental Accounting Standards Board
401 Merritt 7
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Dear Mr. Bean:

On behalf of the Tennessee Department of Audit, we thank the GASB for the opportunity to comment on its proposed Preliminary Views (PV), *Financial Reporting Model Improvements*. We believe the board's proposals generally represent meaningful improvements in financial reporting over the provisions of the current financial reporting model standard for both government-wide and governmental fund financial statements. We agree that the current financial resources measurement focus is based on accounting conventions, not a conceptual foundation; and thus, results in inconsistencies and misunderstanding by users. Unless otherwise stated, we generally agree with the board's proposals. However, we agree with the alternative view proposals (short-term financial resources measurement focus, normally, and government-wide cash flows statement) for the reasons presented and their purpose to improve the overall short-term financial resources measurement approach.

Our comments for the board's consideration to help improve the document are as follows:

Chapter 2:

1. For ¶2, we believe the board should include.
2. For ¶3, we believe the alternative view provides a more consistent conceptual basis. For example, if long-term receivables (long-term prepaid insurance or rent for a three-year period) is expected to be recognized as an asset in accordance with the short-term financial resources measurement focus, the current portion of long-term liabilities also should be recognized. On the contrary, if long-term liabilities are recognized only when due, why would prepaid assets that are also long-term in nature not also be excluded from recognition. Thus, it would appear that only the current portion (within one year of the balance sheet date) of a prepaid rent or insurance asset or long-term liability should be recognized as receivable or payable, rather than recognizing all of one and none of the other, respectively.

Chapter 3:

3. For ¶8 and ¶10, we disagree with the new titles of the governmental fund financial statements. We prefer to keep the titles as currently presented; however, we agree the additional explanation either following the titles or in the summary of significant accounting policies (SSAP) note disclosure is necessary for users to understand the relationship between the governmental funds and government-wide financial statements and differences in measurement focuses. On the other hand, any knowledgeable user or one willing to become knowledgeable about governmental accounting and financial reporting knows there are differences between the government-wide and governmental funds financial statements. Thus, making changes to the titles and element labels adds to the complexity and confusion, as well as makes the statements too “busy.” If the proposal was to go forward for the title and element labels, it would be very evident from the statement title that the focus is on short-term activities. Adding “short-term” throughout the financial statement is repetitive, confusing, and unnecessary. Instead of changing established practice and understanding in this area, the additional explanation (¶13) after the titles or in the SSAP can provide the education to users on the different perspectives and recognition differences.

Chapter 4:

4. For ¶3, the title of the section presents a definition for operating and description of nonoperating revenues and expenses. We believe an actual conceptual definition of nonoperating should be provided, especially if the *operating* definition is based on defining/describing *nonoperating*. We believe a description is insufficient for the conceptual underpinning. An example definition for nonoperating could be “activities not related to the entity’s/fund’s core operations.” Also, does the board intend that the description of nonoperating items will be limited only to items *a-d*? If so, a future basis for conclusions or the standard itself should clarify that the items are all-inclusive. In general though, we agree with the board’s proposal to eliminate the requirement for defining operating and nonoperating in the SSAP.
5. For ¶7, we agree with the board’s proposal.

Chapter 5:

6. For ¶3, we agree with the board’s proposal because the focus of general purpose external financial reporting should be on the historical basic financial statements, not budgetary information, in the hierarchy of communication. However, we disagree with the premise in ¶6 that budgetary information in the annual financial report is historical information. Only the actual results are historical information, not the forecasted revenues and expenditures for the budgetary reporting. Because there is no GAAP for budgetary reporting, we prefer keeping the focus on historical information (i.e., actual results). On the other hand, in order to strengthen the board’s argument, including language that budgetary information meets the objectives of general purpose external financial reporting in Concepts Statement 1 should be considered.

7. For ¶7, we agree with the board's proposal because most governments are likely already presenting in this manner as specified in ¶9.
8. For ¶10, we believe the board should clarify that the uncommon or nonrecurring events to highlight should be significant at a minimum.

Chapter 6:

9. For ¶2, we agree with the board's proposals and reasoning therefor.
10. For ¶5, we do not believe the threshold of "may provide insight for users" in ¶7 provides a sufficient reason to require a presentation by natural classification. We are not certain the costs of preparation exceed the benefits. We do not believe the board has made the case for the requirement as a basic financial statement (¶9) because of essentiality of the information. As stand-alone BTAs, our colleges and universities present expenses by natural classification, but only presents a statement of activities format by function for State CAFR purposes only. Thus, if the State did not require the function format for reporting entity purposes, those entities would not prepare the function format presentation. Therefore, we do not believe the natural classification presentation should be required; however, presenting the schedule in SI may be allowed based on professional judgment.

Appendices:

11. On page 51 for transaction #8 and #10, it would appear to be a more faithful representation to users if the current portion of the long-term transaction was recognized as an asset or liability, respectively, (i.e., receivable or compensated absences liability) since that portion of the payment is due to or from the entity. Thus, we agree with the alternative views proposal in this area and believe it would be an improvement to the short-term approach. In addition, #11 recognizes the accrued interest payable but not the current portion of the long-term debt due within 12 months after year end. The accounting and recognition for these types of long-term transactions (as well as other transactions in Appendix C) present an inconsistency in the conceptual foundation of the short-term approach. We believe the board should consider the alternative view as a solution to this inconsistency.

Should you have questions or need clarification on any of our comments, please contact Gerry Boaz or me at (615) 747-5262.

Sincerely,

Deborah V. Loveless, CPA
Director, Division of State Audit