Letter of Comment No. 010
File Reference: REC
Project No. 3-20
Date Received: 12/03/2020

Re: GASB Projects 3-20 and 3-25

To the Board and Staff:

This is a high-level reaction to the most recent exposures for Project No. 3-20 (Recognition of Elements of Financial Statements) and Project No. 3-25 (Financial Reporting Model Improvements).

In general, I am confused as to why these proposals are seen as improvements, especially when I contrast them to other accounting standards I've dealt with as they have been developed: IFRS, U.S. GAAP (from FASB), insurance statutory accounting, and federal income tax accounting. Each of the standards I mentioned were developed with specific goals in mind, such as protecting policyholders or providing accurate information to shareholders. These standards have been adjusted over time to support these goals as well as prevent behavior by entities that would thwart these goals.

The reason I say I'm confused by the GASB exposure drafts is that they seem to provide incentives for state or local governments to behave in ways deleterious to sustainable public fiscal positions. This is not a laudable goal for an accounting standard.

I recommend GASB members to look at the development of insurance accounting standards, which often has been reactive to insurer disasters, though more recent improvements have been pro-active. My own expertise is in life insurance and annuities, which are very long-term promises sometimes backed by short-term cash flows. However, some products had short-term optionality that were backed by long-term financing. A mismatch either way can and has led to insolvencies, which is why prior accounting and reserving standards have changed. With regards to insurance, standards-setters have been sensitive to making sure revenues from premiums and deposits have been appropriately matched up in timing with the promises being made.

To be sure, governments do not fail fiscally in the same way insurance companies do, so consider the multiple ways governments have come to grief: scoop-and-toss financing, pension obligation bonds, California's back-dating of pension benefit increases not fully recognized in accounting years later. The current proposals do not discourage such behavior, if anything, they reinforce the incentives leading to their adoption.

In particular, consider the fiscal stress some governments have come under in calendar year 2020 and in fiscal year 2021. Do we really want to encourage recognizing loan proceeds as revenue, given the liability generated? Do we want governments to report better funds positions in the short run by underfunding their actuarially required contributions to employee pension funds?

The current proposals do nothing to disincentivize governments from the same fiscal misbehavior that have caused so many governments to fall into a hole of leveraged fiscal failure. There is no merit in change for the sake of change, and the exposure drafts do not appropriately align the timing of promises with cash flows in terms of recognition, whether credit or debit. One may as well scrap the proposals if one is not going to appropriately match up promises and cash flows.

- Mary Pat Campbell, FSA, MAAA

Letter of Comment No. 010
File Reference: REC
Project No. 3-20
Date Received: 02/24/2021

24 February 2021

Re: GASB Projects 3-20 and 3-25

To the Director and Board:

I have written an earlier letter with high-level comments on exposures for Project No. 3-20 (Recognition of Elements of Financial Statements) and Project No. 3-25 (Financial Reporting Model Improvements). This letter adds to the previous one (sent 3 December 2020), and is in reaction to the Fact Sheet on Project No. 3-25 which is published here: https://www.gasb.org/cs/Satellite?c=Document_C&cid=1176176133242&pagename=GASB%2FDocument_C%2FDocumentPage and which I first read on receiving an email on 22 February 2021 telling me that such a fact sheet had been published.

Before more substantive remarks, it seems very odd to me that such a fact sheet has been published by GASB during a comment period on a proposed statement, much less one week before said comment period closed. I can see the need for a simplified document to explain the thrust of what are, after all, technical accounting statements. But if it were necessary to publish during the comment period, I would have thought publication of such a fact sheet earlier in the process would have been more appropriate.

Now onto the meat of the matter.

Let me start with the last Q&A in the fact sheet: “Would the GASB’s proposal treat borrowing as revenue?”.

What then follows, for something that is intending to be a clarifying, simplifying fact sheet, is quibbling over terminology. Yes, under current standards, such cash proceeds from such borrowing is not explicitly labeled “revenue”. It’s given another name. Under the proposed statement, it would still not be labeled “revenue”, but given yet another term. How very enlightening.

The current standards are the ones under which entities such as the state of Illinois can claim to have put forth a balanced budget, which is a laughable claim as it continues to sink deeper in debt, because it will have enough cash from borrowing to cover outgoing cash flows. It is not the only governmental entity following GASB standards to the letter and telling taxpayers and voters a very different fiscal message from their precarious financial reality.

To address another part of the fact sheet, I completely agree with the following: “To be clear, it is not the GASB’s mission to tell governments how to manage their finances. … The GASB does not, however, tell governments that their revenues must exceed their expenses.” GASB is not there to tell politicians, taxpayers, voters, rating agencies, and muni bond buyers how to decide to budget, react, vote, rate, or make investment decisions. However, it is GASB’s mission to “establish and improve standards … that will [g]uide and educate the public.”[i]

In short, the sophisticated users of public financial statements know how to adjust the statements in order to back out whatever clever maneuvers have been made to make state and local government budgets pass as “balanced”. These users make these adjustments in order to make their own assessments of items such as leverage, sustainability, and credit risk. They have been used to the prior standards and will not get much extra information from the proposed changes.

Taxpayers and voters are left out of that particular specialized realm of knowledge of such adjustments, and the GASB proposal is basically a wash for them as well. It will be just as easy for politicians to deceive them as before regarding “balanced” budgets, but now with the veneer than some sort of accounting standard update had been made. Taxpayers and voters should be at least as important as the muni bond buyers in considering financial reporting improvements, given that they will be the ones on the hook with increased costs and lost government services, while the bond buyers merely have to worry about the loss of the value of their investments.

The current exercise may as well be scrapped given it does not really provide any extra information to any of the interested parties, and may confuse the non-expert interested parties into thinking some substantive reform had occurred.

I request to testify at one of the upcoming hearings on these statements. Thank you.

- Mary Pat Campbell, FSA, MAAA

Croton Falls, NY

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[i] GASB’s Mission, Vision, and Core Values.
https://www.gasb.org/jsp/GASB/Page/GASBSectionPage&cid=1175804850352 Accessed 24 February 2021.