Letter of Comment No. 077
File Reference: REC
Project No. 3-20
Date Received: 02/26/2021

Plante & Moran, PLLC
27400 Northwestern Highway
P.O. Box 307
Southfield, MI 48037-0307
Tel: 248.352.2500
Fax: 248.352.0018
plantemoran.com

February 26, 2021

Director of Research and Technical Activities
Project No. 3-25 and Project No. 3-20
Governmental Accounting Standards Board
Via email: director@gasb.org

Plante Moran has reviewed the proposed concepts statement on *Recognition of Elements of Financial Statements*, dated June 17, 2020 along with the Exposure Draft on *Financial Reporting Model Improvements*, dated June 30, 2020 (collectively referred to in this letter as "FRM"). As a result, we offer the following comments for your consideration:

**Alignment between FRM and RER**

We strongly encourage GASB to consider aligning the issuance and the effective dates of FRM with those of the Revenue and Expense Recognition project (RER). We found that our understanding of FRM changed substantially after reading Chapter 7 of RER, even within the context of FRM as a stand-alone standard (excluding the impact of RER). Additionally, we anticipate that governments will be challenged to adopt these two major standards in a linear fashion (one before the other) given the mindset shift that likely is required once RER becomes effective. While normally we wouldn't encourage two such significant standards to be adopted simultaneously, we believe preparers and users will be better served by aligning the adoption of these standards. Not only will it reduce confusion that might be caused by eliminating the necessity for two shifts in thinking (once when FRM is effective, and again when RER comes out), but it also would result in great efficiencies for governments.

**Presentation of Governmental Fund Financial Statements**

While we appreciate GASB's desire to address the conceptual concerns with the current financial resources measurement focus and modified accrual basis of accounting, we do not support moving to the proposed short term financial resources measurement focus and accrual basis of accounting. We do not feel that the proposed model would result in a better measurement of fiscal accountability and would not provide for consistent application across governments as written. In addition, we believe that the proposed model would allow for significant manipulation by governments to achieve desired results within the fund statements.

By focusing the accounting on the length of a transaction from inception to conclusion, rather than the time to maturity as of the balance-sheet date, the result is a measurement of fund balance that is not comparable between governments, nor one that best reflects the concept of interperiod equity. The alternative views within the basis for conclusions of the FRM ED highlights this challenge through an example of debt which is due on the same day for each government, but given differing inception dates, one government will reflect this debt as a liability in the fund statements and the other government would not.

Another good example that highlights the challenges in measuring interperiod equity under this model would be a garbage service special assessment that is imposed on May 1, 2020. Assuming the service period is July 1, 2020 through June 30, 2021 and a payment due date of July 1, 2021, for a June year end government, the transaction would be considered long term and in the fund statements, the provision of garbage service would be reflected in the financial statements in the fiscal year prior to which the related revenues would be recorded. Additionally, if you change the fact pattern simply by altering the due date by one day to June 30th, you'd drastically change the measurement of fund balance as now, even though the transaction is still long term, the payment due date falls within the government's fiscal year, providing under the proposed model that revenue could be recorded as of fiscal year end.

While on the surface the proposed model appears to be simple by just measuring the period between inception to conclusion of a transaction, when you delve into the details, the model really becomes overly complex and therefore, subject to many inconsistencies in application. To illustrate, the manner in which inception and conclusion are defined doesn't align with the general concept of when an agreement begins and ends; rather, it is significantly nuanced. As an example, we struggled with defining the inception and conclusion of a transaction when considering the concept of component parts, such as would be applicable in a construction transaction where the agreement might span multiple years but the measurement under this proposed standard instead relates to the period between which the services are provided and the related payment is due.

We also believe it will be easy with the proposed model for governments to manipulate their agreements and contracts to achieve a desired financial result within the fund statements. Terms of the contract could be defined as just less than or just slightly greater than 12 months to either ensure a transaction is reflected in the fund statements or, alternatively, ensure that it would not be recorded until due. In addition, we find the provision within paragraph 18 which does not require a reassessment of the length of a transaction when the terms and conditions are changed, to be extremely problematic again due to the potential for manipulation.

For these reasons, we do not believe that the proposed short-term financial resources measurement method provides for a better model than the current financial resources measurement focus. We believe that the more significant shortcomings with the current financial resources measurement focus could be overcome with some additional guidance, such as requiring a fixed period of availability for all governments.

Should GASB decide to move forward with FRM as presented, we offer the following:

- The basis of accounting, as reiterated in the Concepts Statement relates to *when* an item should be reported in a government's financial statements. Despite having read paragraph B23 in the Concept Statement which attempts to describe the board's rational for associating the term "accrual basis of accounting" with what is being proposed, we disagree with the use of this terminology as it relates to the proposed recognition model. The board went to great lengths with this project to attempt to make the differences between the governmental fund financial statements and the governmental activities in the government-wide financial statement clear to

plante moran

Letter of Comment No. 077
File Reference: REC
Project No. 3-20
Date Received: 02/26/2021



the reader. By using the same terminology to refer to the basis of accounting on both perspectives, the board has taken a step backward in achieving this understanding.

- Further clarity is needed on defining the inception of and the conclusion of a transaction. Paragraphs 12-17 in the ED are very unclear and therefore ripe for inconsistent understanding and treatment. We spent significant time trying to decipher the concepts outlined within these paragraphs and believe we still likely don't have a full understanding of what is being proposed.

- Paragraph 20 and 21 provides for an exception to recognizing long term debt issued for short term purposes. Because the proposed standard provides no definition of "long term debt issued for short term purposes", we are unclear how this concept would be applied to various circumstances.

  To illustrate a current example we deliberated, the payroll tax deferral under the CARES Act allows employers to defer the payment of the employer portion of FICA taxes. Under the current financial resources and modified accrual basis of accounting, this deferral would result in a fund liability because those payments meet the definition of "normally due". On the contrary, under this proposal, because the inception to conclusion of the transaction is greater than a year, the transaction would not be recorded within the fund statements. As we discussed this example, however, some argued that this would be long-term debt issued for short term purposes, therefore requiring accrual. While we certainly see the merit of this exception, without better definition and guidance in the standard, we were left questioning this treatment.

- The examples in Appendix C offer fairly simple fact patterns. We encourage the GASB to provide examples of transactions requiring multiple actions (paragraph 14b and 14c) versus just a single action. We also encourage GASB to provide examples that illustrate the application of the concept of component parts.

**Presentation of the Proprietary Fund Statement of Revenues, Expenses and Changes in Fund Net Position**

We continue to agree with the self-sustaining or subsidized approach within proprietary funds. Given that, while we see merit for the additional intermediate measure for operating income (loss) and noncapital subsidies, we struggle with the value of including transfers as part of this subtotal. We believe governments do not generally segregate transfers between capital and non-capital purposes, therefore requiring this bifurcation may not be meaningful, and extremely problematic to determine. We also do not believe users of the financial statements benefit from this segregation. Therefore, we recommend all transfers be presented in the other nonoperating revenues and expenses section of the statement of revenues, expenses and changes in fund net position.

**Definition of Operating Revenues and Expenses and Description of Nonoperating Revenues and Expenses**

We agree with GASB's intent to provide better guidance that would achieve greater consistency among governments in the classification of transactions between operating and nonoperating. However, we are significantly challenged with applying the definition of a subsidy to various transactions. The definition

Letter of Comment No. 077
File Reference: REC
Project No. 3-20
Date Received: 02/26/2021



leaves room for significant interpretation, particularly when it comes to understanding the provision in the definition "to keep rates lower", as that seems to require a determination of intent, which is extremely subjective. For example, we debated whether an unrestricted donation met the definition of a subsidy, although we believe that is the desire outcome under this proposal. In this example, we were unsure that we could substantiate that those donations are received in order "to keep rates lower".

Additionally, we found ourselves attempting to connect the determination of operating/nonoperating back to the categorization model in the RER PV. For example, we believe all category A transactions would be operating, while many (not all) category B transactions would be nonoperating. If some type of connection could be made between the classification on the income statement and the categorization within RER, we believe the challenges we have with the proposed definition would likely be minimized.

**Remaining Sections**

We are generally supportive of the requirements outlined in the remaining sections of the financial reporting model exposure draft, which include the paragraphs pertaining to the MD&A, unusual or infrequent items, information about major component units and the budgetary comparison information. However, we do offer the following additional comments:

- Management's Discussion and Analysis:
  - Paragraph 8 indicates that the MD&A should avoid "boilerplate" discussion, but yet the information required by paragraph 8a seems to be nothing more than boilerplate.
  - The heading within paragraph 8d refers to capital asset and long-term debt activity; however, the scope of paragraph 8d(2) goes beyond long-term debt to included leases, PPPs and SBITA arrangements. We suggest, to avoid a lack of clarity, that the heading within this paragraph be revised to reflect the more encompassing nature of these requirements.
- Budgetary Comparison Information:
  - We disagree with the proposed additional column in the budgetary comparison schedules to compare the original and final budget amounts. We believe that adding this additional column will only obfuscate the readability of this statement, while not providing additional value to the reader.
  - The last sentence in paragraph 34 is extremely unclear; we suggest that the GASB rewrite this sentence to ensure any requirements stemming from this sentence are well understood.
- Example financial statements:
  - We greatly appreciate these visuals and examples. We strongly recommend that examples of BTA-only financial statements also be presented, which would greatly aid those who serve in the higher education or healthcare industries.

February 26, 2021

Thank you again for the opportunity to comment. If you'd like further clarification on our comments, please feel free to contact Michelle Watterworth at 248-223-3520 or michelle.watterworth@plantemoran.com.

Very truly yours,

Plante & Moran, PLLC

Plante & Moran, PLLC