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Mr. David Bean
Director of Research and Technical Activities
Governmental Accounting Standards Board
401 Merritt 7
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Project Nos. 3-25 & 3-20

Dear Mr. Bean:

RSM US LLP is pleased to provide feedback on the Exposure Drafts ("ED"), *Financial Reporting Model Improvements* ("FRM ED") and *Recognition of Elements of Financial Statements* ("Elements ED"). We appreciate the opportunity to be involved with such an important initiative and the time the Board has provided stakeholders to evaluate and respond to the ED. In the remainder of this letter, we have included our comments for your consideration.

Short-Term Financial Resources Measurement Focus and Accrual Basis of Accounting

We understand the Board's desire to develop a conceptual foundation for the recognition of financial statement elements in the governmental funds financial statements. The proposed short-term financial resources measurement focus and accrual basis of accounting ("the model"), as defined in paragraph 13 of the FRM ED, will require governmental entities to report short-term transactions and other events ("transactions") in its governmental funds financial statements based on the contractual terms of a transaction. Short-term transactions are defined as transactions for which the period of time from the inception of the transaction to its conclusion is twelve months or less. We believe this transaction-based approach is significantly flawed and will result in a lack of comparability between government entities, potential manipulation of financial statement elements and decreased usefulness of interperiod equity. We also believe the proposed changes to the model, which will require an evaluation of each transaction, will create a significant burden for preparers.

The primary purpose of the governmental funds financial statements is to demonstrate accountability, which we believe the proposed model will make it more difficult to evaluate. Rather than creating consistency in reporting, we believe using the contract terms of a binding arrangement as the basis to determine if a transaction will be reported in the governmental funds financial statements increases the risk entities could negotiate terms to achieve desired reporting. Using negotiated contract terms as the basis to determine if a transaction is short term will also create inconsistencies within classes of transactions and will undermine and create more confusion in understanding the governmental funds financial statements. We believe the following classes of transactions are examples of those transactions that would be susceptible to these inconsistencies due to the complexity of the agreements and the entity's ability to negotiate the terms: grants, special assessments and liabilities. Furthermore, paragraph 18 of the FRM ED states that once a transaction is classified as either short-term or long-term, it should retain that classification for financial reporting purposes even when there are changes to the binding arrangement's terms or conditions that would otherwise suggest the classification should be changed. This provision exacerbates the potential risk of manipulation and prevents recognition based on the substance of the transaction.

We strongly recommend the Board redefine the short-term financial resources measurement focus and base recognition on the notion of when transactions are "normally due," similar to that proposed in the related Preliminary Views: *Financial Reporting Model Improvements* document. While "normally due" would require the Board to provide detailed guidance on which transactions are normally due within one year for similar classes of transactions, we believe this approach to recognition will facilitate consistent reporting among governments.

If the Board does not proceed with our recommendation, we believe the best path forward would be for the Board to maintain the current governmental funds reporting model and limit this project to addressing the specific concerns that stakeholders have with the current model, such as addressing the period of availability and the issuance of long-term debt for short-term purposes.

Operating Revenues and Expenses

Paragraph 31 states that revenues and expenses that would otherwise be classified as nonoperating in most proprietary fund financial statements be classified as operating revenues and expenses if those transactions constitute the proprietary fund's "principal ongoing operations." We recommend the Board define "principal ongoing operations" and provide additional examples illustrating the application of this definition.

Presentation of Transfers

Governmental Funds

While we are generally supportive of the separate reporting of resource flows from current and noncurrent activities in the governmental funds statement of short-term financial resource flows, we do not believe transfers should be reported as current or noncurrent. We believe that separating these internal activities does not provide value beyond current disclosure requirements. Separating transfers could result in governments making arbitrary decisions when determining the presentation. This point is reinforced in paragraph B55 of the FRM ED, which indicates that field participants found classifying transfers as current or noncurrent activities challenging, particularly when a single transfer has a current and noncurrent component. Therefore, we recommend transfers be reported in a separate section of the statement after "net flows from noncurrent activities."

Proprietary Funds

We are supportive of the separate reporting of noncapital subsidies and other nonoperating revenues (expenses) in the proprietary fund statement of revenues, expenses and changes in fund net position. Similar to the reasons previously discussed for governmental funds, we do not believe transfers should be reported within "noncapital subsidies" and "other nonoperating revenues (expenses)" sections. Accordingly, we recommend transfers be reported in a separate section of the statement after "other nonoperating revenues (expenses)."

Noncapital Subsidies

We are supportive of the new intermediate operating measure "operating income (loss) and noncapital subsidies" in the proprietary fund statements of revenues, expenses and changes in fund net position, and we believe it will be a helpful benchmark for certain governments (e.g., higher education, health care) when being compared to their nongovernmental counterparts. These types of governments often levy property taxes and receive other forms of intergovernmental revenue to subsidize the cost of operations; however, users are often confused by the significant loss from operations and misinterpret these losses as an indicator of the financial health of the entity.

We recommend the Board clarify what types of revenues should be considered a subsidy (e.g., derived tax revenue, imposed nonexchange transactions). Some types of governments, such as housing authorities, have historically shown intergovernmental revenue as operating revenue. Guidance should be provided to determine whether intergovernmental revenue received is the result of a services contract and may be shown as operating revenue rather than a subsidy.

Inflows and Outflows

While we understand the Board's underlying reasoning for suggesting the terminology "inflows" and "outflows" to replace "revenue" and "expenditures," we believe the existing terminology should be retained. We are concerned that moving away from terminology that is well understood by users and preparers of governmental financial statements will introduce unnecessary complexity.

Management's Discussion and Analysis (MD&A)

We recommend that MD&A exclude discussion of discretely presented component units, rather than management of the primary government using professional judgment to determine whether MD&A should include discussion of the individual component units' performance based on the nature and significance of their relationship to the primary government. Because these are legally separate entities, management of the primary government is not typically in a position to provide meaningful explanations for significant changes in financial performance. We believe reference to the separate report for the discretely presented component unit is sufficient.

The FRM ED has added a requirement to analyze nonmajor funds in the aggregate, in a manner previously limited to major funds. We believe such an analysis could be lengthy and complex for many governmental entities that have large numbers of nonmajor funds. Also, addressing restrictions, commitments and assignments for major and nonmajor funds is duplicative of information contained in the notes to the financial statements. We believe it would be preferable to add a reference to the applicable footnote in lieu of duplicating the information in MD&A.

Budgetary Comparison Information

We support requiring budgetary comparison information to be presented as Required Supplementary Information (RSI). However, we question the usefulness of including an analysis of significant variations between the original and final budget amounts and the final budget amounts and actual results in the notes to the RSI. While we understand the budgetary comparison information assists with evaluating accountability, we believe the usefulness of this information is diminished due to the timing of when governments typically release their financial statements.

Effective Date

We highly recommend the Board recombine the financial reporting model and concepts statement project with the revenue and expense recognition project. While we generally agree that providing time between the implementation of two significant standards can provide relief to preparers, we believe the projects are inherently interrelated to such an extent that they should have the same effective date. We found studying Chapter 7 in the Preliminary Views, *Revenue and Expense Recognition*, provided further clarification and understanding of the application of the Short-Term Financial Resources Measurement Focus and Accrual Basis of Accounting as outlined in the FRM ED. Both projects will require governments to make significant changes to their recognition of transactions, general ledger systems, policies, procedures and internal controls. In addition, extensive training will be required to assist users and preparers in understanding both the categorization model and related recognition guidance, as well as the new terminology and changes to the presentation of the financial statements. We believe implementing the standards separately will increase the costs associated with the implementation.

In addition, if the Board moves forward with a phased-in approach for implementation, we recommend increasing the phased-in threshold. The threshold proposed is less than the threshold used with the implementation of GASB Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, which was issued over 20 years ago.

We appreciate this opportunity to provide feedback on the FRM ED and Elements ED and would be pleased to respond to any questions the Board or its staff may have concerning our comments. Please direct any questions to Michelle Horaney, Partner – State & Local Government, Education and Gaming Industry Audit Technical Leader, at 563.888.4038.

Sincerely,

RSM US LLP

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