

# Virginia GFOA Spring Conference

## A GASB Update

Presented by

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Virginia Beach, Virginia  
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The views expressed in this presentation are those of Mr. Mazur. Official positions of the GASB are determined only after extensive due process and deliberation.

# Topics

- ▶ GASB's Recent Standards and Its Current Technical Agenda
- ▶ Implementing OPEB Standards
- ▶ GASB's Research Agenda

## Section 1

# GASB's Recent Standards and Its Current Technical Agenda

- ▶ Statement 48—Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues (issued Sept. 06)
- ▶ Statement 49—Accounting and Financial Reporting for Pollution Remediation Obligations (issued Nov. 06)
- ▶ Statement 50—Pension Disclosures (to be issued May 07)

# GASB's Recent Standards and Its Current Technical Agenda Cont'd

- ▶ Statement 51—Accounting and Financial Reporting for Intangible Assets (planned for issuance June 07)
- ▶ Concept Statement on Elements of Financial Statements (to be issued June 07)\*
- ▶ Due Process Documents (3)

\*not covered in presentation

## Statement 48

# Sales and Pledges of Receivables and Future Revenues

- ▶ Scope of the project—Government receives proceeds in exchange for the rights to future cash flows from:
  - Receivables:
    - ▶ Delinquent property taxes
    - ▶ Uncollected fines
    - ▶ Mortgages
    - ▶ Student loans
  - Future revenues

# Sale or Borrowing?

- ▶ Borrowing by default, unless specific criteria are met
- ▶ Continuing involvement—control
  - Does the transferor government retain control, or is control relinquished?
    - ▶ Criteria for receivables
    - ▶ Criteria for future revenues

# Receivables

- ▶ Are receivables sold or pledged?
- ▶ Transferee's ability to sell or pledge
- ▶ Isolation from seller (and its creditors)
  - Legally separate
  - No access to cash
  - Source and timing of payments
  - Satisfaction of accounts
  - Bankruptcy protection
- ▶ No option or ability to replace or repurchase accounts

# Future Revenues and Transfers

Are *future revenues* sold or pledged?

- ▶ Transferee's ability to sell or pledge
- ▶ Transferor's continuing *active* involvement in the generation of the revenues
  - Excludes own-source revenues
    - ▶ Taxes
    - ▶ User charges
  - Grants, entitlements, shared revenues could be sold or pledged, depending on *active* involvement

Deferral and amortization required to promote interperiod equity

# Effective Date

- ▶ Periods beginning after December 15, 2006



# Statement 49

## Accounting and Financial Reporting for Pollution Remediation Obligations



# Types of Remediation Obligations

- ▶ Pre-cleanup activities: site assessment, feasibility study, design
- ▶ Cleanup activities: neutralization, containment, disposal activities
- ▶ Oversight and enforcement costs
- ▶ Operation and maintenance of the remedy and monitoring

# Recognition Threshold

- ▶ Determine whether one or more components of a pollution remediation obligation are recognizable as a liability when . . .
  - Government knows or reasonably believes that a site is polluted, and
  - Obligating event occurs

# Obligating Events

- ▶ Compelled to take remediation action because of pollution-caused imminent endangerment
- ▶ Violate pollution-prevention permit—for example, RCRA permit
- ▶ Named, or evidence indicates govt. will be named, as responsible party or PRP for remediation (or cost sharing)
- ▶ Named, or evidence indicates govt. will be named in lawsuit compelling remediation
- ▶ Govt. commences cleanup activities

# Recognition

- ▶ Recognize components of liability as they become reasonably estimable
- ▶ Recognition benchmarks
  - Receipt of an administrative order
  - Participation as a responsible party or PRP
  - Completion of corrective measure feasibility study
  - Issuance of authorization to proceed
  - Remediation design and implementation

# Recognition

- ▶ Cost accumulation, not fair value
- ▶ Current value, not present value
- ▶ Expected cash flow technique would be required
  - Not FASB Statement No. 5, *Accounting for Contingencies*

# Capitalization Permitted in Limited Circumstances

- a. Cleanup to prepare property for sale (limited to fair value)
  - b. Polluted property bought and cleaned for use (limited)
  - c. Asset impaired and cleanup restores lost service utility (limited)
  - d. Acquired capital assets have future alternative use. For example, land (limited to future service utility)
- For a. & b.—capitalize only if incurred within reasonable period

# Effective Date

- ▶ Fiscal periods beginning after December 15, 2007

# Statement 50

## Pension Disclosures



# Objective: Conforming Pension Disclosure Requirements to Those for OPEB

- ▶ Statements 43 and 45 for pensions followed the same overall approach as Statements 25 and 27 for pensions
- ▶ Note disclosure and RSI requirements are generally parallel; however, those for OPEB are stronger on some points
- ▶ The Pension Disclosure project would modify Statement 25 and 27 to conform on several points where that would strengthen pension disclosures

# Notable Changes

- ▶ **Note disclosure of funded status information** (most recent actuarial valuation) by plans and employers
- ▶ **Note disclosure of key methods and assumptions**—moved from RSI for plans
  - Funding progress trend information still required as RSI
- ▶ **Explanatory note disclosures about the actuarial measurement process** —estimates, assumptions, re-estimation over time taking into consideration additional history
- ▶ Presentation by plans and employers that use the **aggregate actuarial cost method** of funded-status note disclosure and funding-progress RSI using **entry age as a surrogate** (purpose: *fill information void left by the aggregate method*)

# Notable Changes (cont.)

- ▶ Note disclosure by a cost-sharing employer of **how the contractually required contribution was determined**
- ▶ If a cost-sharing plan *does not issue* a Statement 43 financial report, including RSI, and the plan is *not included in the report of another entity*, **presentation of plan RSI in a participating employer's financial report** (with disclosure to "size" the plan information relative to the employer)
- ▶ Note disclosure of **legal or contractual maximum employer contribution rates**, if applicable
- ▶ Additional note disclosure of **how the fair value of assets was determined**, if not based on market values

# Effective Date

- ▶ for periods beginning after June 15, 2007, with specific instructions for governments using entry age actuarial cost as a surrogate for aggregate cost method

Final Statement expected to be issued in  
June 2007

# Statement 51 (planned)

Accounting and Financial Reporting  
For Intangible Assets



# Definition

- ▶ An intangible asset as an asset that possesses all of the following characteristics:
  - Lack of physical substance
  - Nonfinancial nature
  - Initial useful life extending beyond a single reporting period.

# Types of Intangibles

- ▶ Computer software
  - Purchased
  - Internally developed
- ▶ Right-of-ways
- ▶ Easements
- ▶ Water rights
- ▶ Patents and copyrights

# Basic Guidance

- ▶ All intangible assets should be classified as capital assets, and all existing authoritative guidance related to capital assets should be applied to these intangible assets.

# Internally Generated

- ▶ Outlays incurred related to an internally generated intangible asset that is considered identifiable should be capitalized only upon the occurrence of all of the following:
  - Determination that an objective for the project is to create a specific internally generated intangible asset;
  - Determination of the nature of the service capacity that is expected to be provided by the asset upon its completion;
  - Demonstration of the technical or technological feasibility for completing the project so that the asset will provide its expected service capacity;
  - Demonstration of the current intention, ability, and presence of effort to complete or, in the case of a multiyear project, continue development of the intangible asset.

# Project Timetable

- ▶ December 2006—Exposure draft
- ▶ Comment Deadline—March 23, 2007
- ▶ Public hearings—April 2007
- ▶ Final statement—June 2007?

# Due Process Documents

- ▶ Derivatives
- ▶ Fund balance and fund definitions
- ▶ Land and other real estate in endowment funds\*

\*Not covered in presentation

# Derivatives

The Road to an ED

The background of the slide is a dark blue-grey color. It features a faint, light-colored topographic map with contour lines. In the lower-left corner, there is a faint compass rose with a needle pointing towards the top-left. The compass rose has letters 'N', 'E', 'S', and 'W' indicating the cardinal directions. The overall aesthetic is technical and navigational.

# Examples of Derivatives

- ▶ Interest rate swap
  - Variable-rate to fixed-rate
  - Fixed-rate to variable-rate
- ▶ Basis swap
  - Exchange payments based on the changes of two variable rates (i.e. BMI to Libor)
- ▶ Swaption
  - Gives the purchaser of the option the right, but not the obligation, to enter into an interest rate swap
- ▶ Commodity swap
  - Reduce exposure to a commodity's price risk

# PV Proposal

- ▶ Fair value all derivatives--with hedge accounting required
  - Changes in fair value of derivative are deferred for qualifying hedge transactions
  - Changes in fair value of derivative would not be deferred if the related asset (for example, an investment) is reported at fair value

# Hedge Effectiveness Testing Required at Year End

- ▶ Consistent critical terms
- ▶ Synthetic instrument
- ▶ Quantitative techniques
  - Regression analysis
  - Dollar offset
- ▶ Other equivalent quantitative method

# Disclosures

- ▶ Application of TB-2003 disclosures to all hedging derivatives
- ▶ Investment derivatives to conform to Statement 40 plus additional credit risk disclosures
- ▶ Summary of derivative activities by type
  - Beginning fair values
  - Fair value of derivatives acquired during the period (at time of acquisition)
  - Fair value of derivatives that matured or terminated
  - Changes in fair value during the period
  - Ending fair values
  - Ending notional amount

# Project Timetable

- ▶ Exposure Draft—June 2007
- ▶ Final statement—2008

# Fund Balance and Governmental Fund Definitions

## ▶ Clarify Fund Definitions:

- Special revenue—current Board position—no changes will be proposed at this time
- Capital projects
  - ▶ Financial resources to be used for. . .
- Debt service
  - ▶ Accumulation of resources for. . .

# Alternatives

- ▶ Current classifications—clarify definitions
- ▶ Restricted and unrestricted
- ▶ Amounts that are not available for appropriation and amounts that are available for appropriation

# Project Timetable

- ▶ Invitation to Comment—October 2006
- ▶ Public Hearing—February 2007
- ▶ Exposure Draft—November 2007
- ▶ Final Statement— 2008

## Section 2

# Implementing OPEB Standards

- ▶ Staggered Statement 45 implementation based on a government's phase for implementing GASB 34:
  - First fiscal year beginning after:
    - ▶ Phase 1 (\$100M+ revenue): December 15, 2006
    - ▶ Phase 2 (\$10M to \$100M revenue): December 15, 2007
    - ▶ Phase 3 (< \$10M revenue): December 15, 2008
  - Companion Statement (No. 43) relates to OPEB plan reporting
    - ▶ Applies to plans administered as trusts and to multiple-employer plans that are not administered as trusts
    - ▶ Effective one year prior to Statement 45 for largest participating employer

# Implementation Considerations

- ▶ Analyzing & classifying benefits offered
- ▶ Gathering information about plan terms & covered group
- ▶ Obtaining an initial actuarial valuation & absorbing the new information it provides
- ▶ Considering how OPEB will be managed and accounted for going forward:
  - Initiating discussions and decision processes re: variables that can be managed to make or keep benefits sustainable
  - If planning to fund, establishing a qualifying OPEB plan trust
  - Coming to grips with implicit rate subsidies
  - Working out issues related to fund structure, funds flows, and accounting and financial report preparation

# What Can a Government Do to Manage Its OPEB Obligations?

- ▶ Policy issues that the GASB cannot answer
- ▶ Information required by Statement 45 will provide basis for informed decision-making
- ▶ Elements to work with to manage for sustainable retiree healthcare benefits (and other forms of OPEB):
  - The actuarial accrued liability & factors that drive it
  - The amount of assets contributed to the plan
    - ▶ Whether or to what extent to fund
    - ▶ Whether or not to establish a qualifying OPEB plan trust to enable accumulation of plan assets
  - The allocation of the total cost of retiree healthcare coverage between the employer and plan members

# Common Implementation Questions

- ▶ Classification of benefits for accounting purposes (distinguishing between pensions, OPEB, compensated absences, termination benefits, etc.)
- ▶ Effects of various administrative arrangements on the accounting and reporting requirements. For example,
  - Qualifying trust vs. no qualifying trust
    - ▶ *Note:* Even if no trust is established, if an employer is sponsoring (administering) a plan that includes more than one employer, Statement 43 applies for plan reporting
  - Coordination of accounting for active employee and retiree healthcare costs when both are administered jointly as part of a self-insured arrangement
    - ▶ Costs for active employees and retirees are required to be accounted for separately
    - ▶ Self-insurance for active employee healthcare continues to be accounted for using Statement 10, retiree healthcare using Statements 43/45

# GASB Resources

- ▶ Statement 43/45 Implementation Guide (Q&A)
- ▶ 2006–2007 *Comprehensive Implementation Guide* (includes the Statement 43/45 Implementation Guide, plus additional questions & answers)
- ▶ GASB website ([www.gasb.org](http://www.gasb.org))
  - OPEB fact sheet
  - Plain language summary
  - Summaries of standards
  - Publication Ordering Information (Statements, Implementation Guides, Technical Bulletins, etc.)
  - Method of submitting technical accounting and financial reporting questions to GASB's professional staff

# Where are States in Implementing OPEB?

- ▶ Of the Implementation Group (37 states):
  - 23 have done either actuarial valuations or preliminary valuation
  - 12 have either submitted trust legislation or have already enacted trusts
  - 8 anticipate funding part or all of ARC in FY08

## Of the Implementation Group (37 states):

- Funding Mechanisms being considered include:
  - ▶ % of Tobacco Settlement Payments (Massachusetts)
  - ▶ Appropriations (Many states)
  - ▶ % of payroll (Delaware, Florida, Georgia, Nevada, South Carolina)
  - ▶ % of Lottery Net Revenues (North Carolina)
  - ▶ Other Funds and Predecessor Trusts

# Excellent Reference on Funding Strategies Being Considered by Selected States and Other Governments

*GASB 45 – Where are States in Implementing the Standards, a March 21, 2007 presentation to the National Association of State Comptrollers, by Eric Berman, Deputy State Comptroller of Massachusetts*

*Accessible through:*

[http://www.nasact.org/onlineresources/downloads/2007\\_NASC/2007\\_NASC.html](http://www.nasact.org/onlineresources/downloads/2007_NASC/2007_NASC.html)

Note: Eric Berman was a member of the GASB's OPEB Implementation Guide Advisory Committee

## Section 3

# GASB's Research Agenda

1. Economic condition reporting
2. Electronic financial reporting
3. Intergovernmental financial dependency and related risks
4. Pension accounting and reporting
5. Public/private partnerships
6. Reporting objectives and requirements for entities within governments
7. Reporting of service efforts and accomplishments\* (\*not included)

# Economic Condition Reporting

- ▶ To map information required to assess economic condition
- ▶ To compare such information with that received under current standards
- ▶ Key issue:
  - should additional information be "required" or "encouraged?"

# Electronic Financial Reporting

- ▶ To monitor effect of electronic media on information delivery and user needs
- ▶ To conduct extensive research into electronic financial reporting by governments
- ▶ To develop a prototype electronic financial reporting demonstration model

# Intergovernmental Financial Dependency and Related Risks

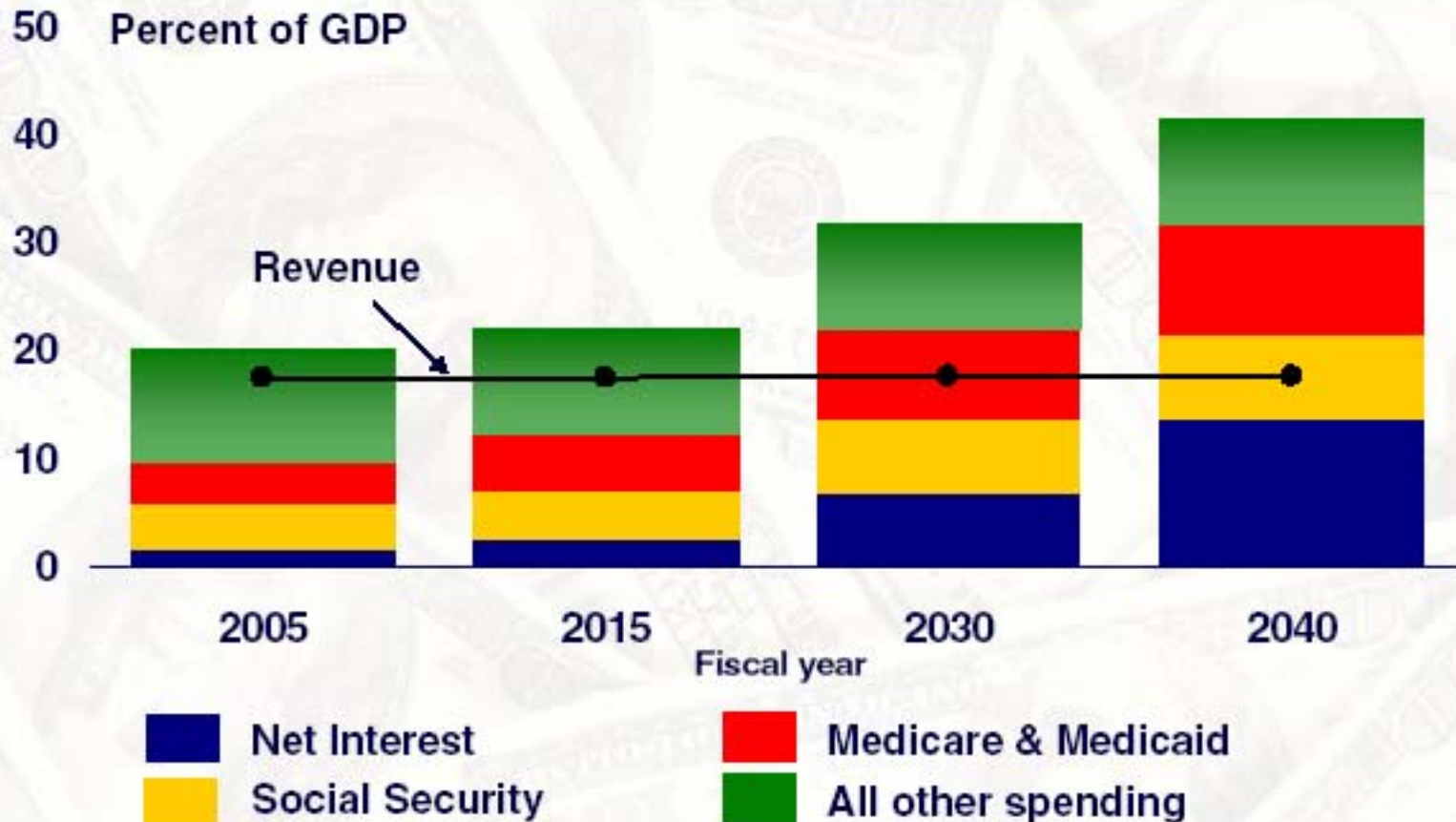
- ▶ Should amounts on face of financial statements be disaggregated to promote clarity?
- ▶ What kinds of associated disclosures should be made?
- ▶ What are the risks to intergovernmental exchanges, flows, and assets held that might impact the financial position and results of operations of a state or local government?

# Primary Assertions About Financial Dependency and Risk

1. Current intergovernmental financial flows are not sustainable
2. Ignoring factors controlling these flows increases risk to state and local governments
3. Continuing operations of Federal departments are at risk
4. Government preparers and their auditors need to better understand and communicate about these flows and related risks

# Composition of Spending as a Share of GDP

Assuming Discretionary Spending Grows with GDP after 2006  
and All Expiring Tax Provisions are Extended



Note: This includes certain tax provisions that expired at the end of 2005, such as the increased AMT exemption amount.

Source: GAO's May 2006 analysis.

# Pension Accounting and Reporting

- ▶ Added to GASB Technical Plan in January 2006
- ▶ Part of the GASB's commitment to review effectiveness of past standards in achieving their financial reporting objectives
  - Statements 25 and 27 became effective in periods beginning after June 15, 1996 and 1997, respectively
- ▶ There is no preconceived conclusion or agenda in regard to whether or how standards might be modified
- ▶ We do expect that a number of issues will be raised and considered

# Public/Private Partnerships

- ▶ To research the various types of PPPs in practice and determine whether current accounting and reporting guidance is sufficient
- ▶ Timetable:
  - Added to the research agenda in August 2006
  - Project prospectus to Board in December 2007

# Reporting Objectives and Requirements for Entities Within Governments—And Re-examination of Statement 14

- ▶ For separately-issued financial statements for reporting units that comprise less than a separate legal entity, determine:
  - *Whether* GAAP should be set
  - *What* that GAAP would be
  
- ▶ Determine whether current component-unit standards:
  - Include all appropriate related organizations
  - Exclude organizations that should not be included
  - Display and disclose component units in the most appropriate and useful manner

# Questions? And Contact Information

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