

GASB Financial Reporting Model Improvements

On December 7, 2016, the Governmental Accounting Standards Board (GASB) approved its first public comment document in its project re-examining the financial reporting model. The Invitation to Comment (ITC) on major issues related to *Financial Reporting Model Improvements—Governmental Funds* addresses potential improvements to the existing governmental fund financial reporting model. The two fundamental issues of GASB's larger financial reporting model re-examination project included in the ITC are governmental funds' measurement focus and basis of accounting and financial statement presentation.

An ITC is designed to seek comments at a relatively early stage of a project before the board reaches a consensus on how to address the project issues raised. The full ITC, as well as videos explaining key components and schedules of public hearings and user forums, can be downloaded at gasb.org. Answers to ITC questions and feedback are due by March 31, 2017.

GASB's project to re-examine the basic blueprint for state and local financial reporting is the first since issuance of GASB Statement No. 34, effective for periods beginning after June 15, 2001. Statement No. 34 established the basic financial statements' format and measurement focus, certain related notes and required supplementary information, including management's discussion and analysis. Because of the pervasive influence the accounting and financial reporting model has over reporting effectiveness, we encourage state and local governments to provide feedback at this critical stage of the project.

Governmental Fund Financial Reporting

GASB's pre-agenda research revealed most of the financial reporting model components are effective in providing essential decision-making information; however, members identified a number of improvement areas for both fund and entity-wide financial statements. In its phased project, GASB seeks feedback on alternatives to improving the financial statements' effectiveness in providing essential decision-making information and certain application issues.

In the ITC, GASB explores a conceptually consistent measurement focus and basis of accounting. Today's reporting model presents information using the *current financial resources* measurement focus and modified accrual basis of accounting. The three measurement focus and basis of accounting alternatives open for comment are based on a continuum of governmental fund recognition approaches from the cash-basis approach focusing on *near-term financial resources* to a full-accrual approach focusing on *long-term financial resources*. The third, a *short-term financial resources* approach, is a middle-ground approach. The ITC describes each recognition approach's key features, recognition concepts, financial statement messages and potential benefits and challenges. GASB seeks feedback on which alternative provides the most valuable information and how to improve and reduce the number of alternatives.

For all approaches, the ITC considers a presentation format alternative for the statement of resources flows that would be conceptually consistent with its measurement focus and basis of accounting. A current and long-term activity format would report inflows and outflows of resources related to capital assets and long-term debt separately from the inflows and outflows of resources of other governmental fund activities. The current accounting of more complex transactions such as those involving derivative instruments, service concession arrangements and other transactions, may not be appropriate under the current financial resources measurement focus conventions and requires a conceptual foundation that addresses governmental fund statements. The resources flows presentation would differ under each approach. Today's existing format generally presents inflows and outflows of resources considered revenues and expenditures separately from flows reported as other financing sources and uses.

For both the short-term and long-term financial resources recognition approaches, the ITC introduces a statement of cash flows as a potential enhancement to the basic financial statements. The ITC seeks feedback on whether this should be required, what difficulties may arise in presenting a statement of cash flows for governmental funds and whether the four existing statement of cash flow classifications are the most appropriate.

The ITC presents GASB's preliminary decision that governmental fund financial statements should present a shorter time perspective of a government's financial position and resources flows than the information conveyed in the government-wide financial statements and should focus on financial, rather than economic resources. GASB seeks feedback on whether and why this presentation should or should not be changed.

The ITC explores improved reconciliations from the information in governmental fund financial statements to information in the government-wide financial statements. The condensed reconciliations would be presented on the same page as the balance sheet or resources flows statement; examples are provided. Specific terminology is used to more clearly communicate the information in governmental fund financial statements is different than the information in government-wide financial statements. Clearer titles, descriptions and labels designate the governmental fund financial statements' shorter time perspective and focus on financial, rather than economic resources.

Because governmental fund financial statements' information is limited to a shorter time perspective than the information conveyed in government-wide financial statements and has a focus on financial resources, they convey information about fiscal accountability, not operational accountability. The ITC seeks feedback on improvements to this lack of conceptual foundation and guidance.

The definition of financial resources is a concept integral to all three recognition approaches. The ITC seeks feedback on what definition provides the most valuable information, including whether the definition should include specific items such as prepaid items and inventory. In conjunction with this topic, GASB would recommend addressing the conceptual framework project on recognition of financial statement elements, which also is in its preliminary stage.

Future Due Process Documents

- In the project's future phases, GASB will issue other due process documents (preliminary views and exposure drafts) to address the following topics and further consider improvements to the financial reporting model.
- *Government-Wide Financial Statements* – GASB would like to explore alternatives to the statement of activities format.
- *Proprietary Fund and Business-Type Activity Financial Statements* – GASB would like to evaluate operating indicator alternatives in conjunction with evaluating the guidance for the separate presentation of operating and nonoperating revenues and expenses.
- *Budgetary Comparisons* – GASB would like to explore the appropriate communication method—either as basic financial statements or required supplementary information—for budgetary comparison information and consider whether and, if so, which budget variances require presentation.
- *Permanent Funds* – GASB would like to explore alternatives for presenting permanent funds in the financial statements.
- *Management's Discussion and Analysis* – GASB would like to explore options for enhancing the financial statement analysis component, including eliminating requirements that are boilerplate and no longer necessary for understanding the financial reporting model. GASB also would like to explore providing clarifying guidance for presenting currently known facts, decisions or conditions expected to have a significant effect on financial position or results of operations.

- *Debt Service Fund Presentation* – GASB would like to explore options for providing additional information about debt service funds, either individual or in aggregate.
- *Extraordinary and Special Items* – The board will consider alternatives to improve the consistency of application of the guidance for reporting extraordinary and special items.
- *Other Issues* – GASB would like to explore options for permitting timelier financial reporting and reducing overall complexity.

Next Steps

In 2017, GASB will hold public hearings and user forums to obtain additional ITC feedback. Redeliberations will consider comments from these hearings and forums, ITC comment letters and other due process feedback and are expected to continue into 2018. While the comprehensive project is expected to take several years, your comments and input are vital throughout this process, particularly in the early stages. You are encouraged to comment on the ITC by the March 31, 2017, deadline. BKD will continue to follow GASB’s progress and keep you informed.

For more information, contact your BKD advisor.

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