North Carolina
Office of the State Controller

Preliminary Views on GASB’s New
Financial Reporting Model
June 5, 2019

Jerry E. Durham, CPA, CGFM, CFE

We will consider:

- Project objective and background
- Governmental funds
  - Concerns with current reporting
  - Short-term financial resources measurement focus
    - Alternative views
    - Presentation
- Proprietary fund presentation
- Budgetary comparison reporting
We will consider (cont’d)

- Major component unit information
- Schedule of government-wide expenses by natural classification
- Feedback and next steps

Project Objective and Background

- Reexamination of the effectiveness of the financial reporting model—Statements 34, 35, 37, 41, and 46, and Interpretation 6
- Pre-agenda research showed model generally effective, targeted improvements possible
- Preliminary Views, *Financial Reporting Model Improvements*, issued September 2018
Concerns with Governmental Funds Financial Statements

- Lack of effectiveness of governmental fund information
- Lack of conceptual consistency
- Lack of guidance for complex transactions
- Lack of consistency in applying the current financial resources measurement focus and modified accrual basis of accounting

Financial Reporting Model

- Financial Reporting Model Reexamination:
  - Governmental Fund F/S Measurement Focus (Near-Term Focus?)
  - Current Guidance
    - Current financial resources measurement focus – modified accrual basis of accounting
  - Question:
    - Do we need a more consistent approach? Yes!
  - Suggested solution:
    - Near-term – Financial Resources Approach
    - Short-term (formerly Working Capital Approach)
    - Long-term (formerly Total Financial Resources Approach)
The Candidates

- Near-Term Financial Resources Approach? 60 days?

- Short-term (Working-Capital Approach)? 1 year?

- Long-term (Total Financial Resources Approach)? No Capital Assets or Debt?

Recognition in Governmental Funds

- Short-term financial resources measurement focus
- Elements from short-term transactions recognized as the underlying transaction occurs
- Elements from long-term transactions recognized when payments are due
- Financial assets: cash, assets that are available to be converted to cash, and assets that are consumable in lieu of cash
Messages Conveyed by Short–Term Financial Resources Measurement Focus

- Consistency in the reporting of balance sheet elements and financial resource flows elements
- Period-end balances from short-term transactions
- Spending of the period
- Inflows of resources from short-term transactions as they occur and long-term transactions when payment are due
- Fund balance that is available for spending
- Results useful in evaluating budgetary information

Recognition in Governmental Funds

**Short–Term Transactions**
- *Normally* are **due** to convert to or generate cash or require the use of cash within one year from the inception of the transaction

**Long–Term Transactions**
- *Normally* are **due** to convert to or require the use of cash beyond one year from the inception of the transaction

An entire class of transactions will either be short-term transactions or long-term transactions. Transactions within classes (for example, investments) are not treated differently.
## Recognition in Governmental Funds

### Assets
- Assets include those from short-term transactions that are receivable at period-end, as well as cash and other financial assets that are available to be converted to cash, or expected to be consumed within the subsequent reporting period.
- Assets arising from long-term transactions are recognized when payments are due.

### Liabilities
- Liabilities arising from short-term transactions that are payable at year end.
- Liabilities arising from long-term transactions are recognized when payments become due.

### Recognition in Governmental Funds

#### Outflows of Resources
- As spending occurs.
- Spending from short-term transactions (such as use of goods and services and acquisition of capital assets) as the transactions occur.
- Spending from long-term transactions as payments are due.

#### Inflows of Resources
- Inflows of resources from short-term transactions (such as tax levies, grants, and changes in fair value of investments) as the transactions occur.
- Inflows of resources arising from long-term transactions are recognized when payments become due.
Recognition in Governmental Funds

Deferred Outflows of Resources and Deferred Inflows of Resources

- Governed by concept of *available for spending in a future period*
- Outflows of resources that do not meet the definition of an asset and are inherently related to future spending
- Inflows of resources that do not meet the definition of a liability and can only be used for future spending
- Limited to circumstances identified by the GASB

Deferred Outflows of Resources and Deferred Inflows of Resources

Beginning of year balance: $18,400,000
No maturities or purchase of investments;
Change in fair value of $100,000;
End of year balance: $18,500,000

Recognition Example—Investments in Permanent Fund

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Investments of $18,500,000</td>
<td>Inflows of resources of $100,000</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Investments of $18,500,000</td>
<td>Inflows of resources of $100,000</td>
</tr>
</tbody>
</table>

Normally Short-Term
## Recognition Example—Property Taxes Receivable

End of year balance: $28,954,754
Property taxes levied before period end for the subsequent fiscal year; property taxes are due 6 months after period-end

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Taxes receivable of $28,954,754 and deferred inflow of resources of $28,954,754</td>
<td>No inflows of resources</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Taxes receivable of $28,954,754 and deferred inflow of resources of $28,954,754</td>
<td>No inflows of resources</td>
</tr>
</tbody>
</table>

Normally Short-Term

## Recognition Example—Other Taxes Receivable

End of year balance: $13,342,623
Other taxes are associated with the current year; $3,342,623 of other taxes are due 3 months after year-end, $10,000,000 are due 6 months after year-end

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Taxes receivable of $13,342,623 and deferred inflow of resources of $10,000,000</td>
<td>Inflows of resources of $3,342,623</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Taxes receivable of $13,342,623</td>
<td>Inflows of resources of $13,342,623</td>
</tr>
</tbody>
</table>

Normally Short-Term
### Recognition Example—Prepaid Items

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Prepaid item and nonspendable fund balance of $13,800</td>
<td>Outflows of resources of $52,000</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Prepaid item of $13,800</td>
<td>Outflows of resources of $52,000</td>
</tr>
</tbody>
</table>

**Beginning of year balance:** $5,800  
**Spending on prepaid items during year:** $60,000  
**End of year balance:** $13,800

**Normally Short-Term**

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### Recognition Example—Inventory

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Inventory of and nonspendable fund balance $23,500 using consumption method</td>
<td>Outflows of resources of $176,700</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Inventory of $23,500</td>
<td>Outflows of resources of $176,700</td>
</tr>
</tbody>
</table>

**Beginning of year balance:** $15,200  
**Spending on inventory during year:** $185,000  
**End of year balance:** $23,500

**Normally Short-Term**
### Recognition Example—Special Assessments

<table>
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<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Receivable and deferred inflow of resources of $82,351</td>
<td>Inflow of resources of $41,500</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No amounts recognized</td>
<td>Inflow of resources of $41,500</td>
</tr>
</tbody>
</table>

**Normally Long–Term**

### Recognition Example—Notes Receivable Related to Lending

<table>
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<th>Balance Sheet</th>
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</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Notes receivable and nonspendable fund balance of $3,742,776</td>
<td>No amounts recognized</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No amounts recognized</td>
<td>Inflow of resources of $645,000</td>
</tr>
</tbody>
</table>

**Normally Long–Term**
Recognition Example—Hedging Derivative Instrument

Details of instrument: effective hedge, 9 years remaining in term, declining notional amount, associated with capital-related debt
Fair value at end of period: ($532,882)

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<tbody>
<tr>
<td>Current financial resources</td>
<td>No amounts recognized</td>
<td>No amounts recognized</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No amounts recognized</td>
<td>No amounts recognized</td>
</tr>
</tbody>
</table>

Normally Long–Term

Recognition Example—Compensated Absences

Beginning of year balance: $4,824,057
Earned in the current year: $146,014 (LIFO flow assumption)
End of year balance: $4,970,071
Additionally, $25,000 is due to employees who have separated from service

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</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Liability of $25,000</td>
<td>Outflows of resources of $25,000</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Liability of $25,000</td>
<td>Outflows of resources of $25,000</td>
</tr>
</tbody>
</table>

Normally Long–Term
Recognition Example—Accrued Interest on Long-Term Debt

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<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>No amounts recognized</td>
<td>Debt service expenditures of $2,448,950</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Accrued interest payable of $845,334</td>
<td>Outflows of resources of $2,394,534</td>
</tr>
</tbody>
</table>

Normally Short-Term

Recognition Example—Claims Payable

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</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>No amounts recognized</td>
<td>Expenditures of $1,500,000</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Claims payable of $2,550,000</td>
<td>Outflows of resources of $2,750,000</td>
</tr>
</tbody>
</table>

Normally Short-Term
## Recognition Example—Tax Anticipation Notes Payable

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<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>Tax anticipation note payable of $4,400,000</td>
<td>No amounts recognized.</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>Tax anticipation note payable of $4,400,000</td>
<td>No amounts recognized.</td>
</tr>
</tbody>
</table>

*Borrowings and repayments are disclosed.

Normally Short–Term

## Recognition Example—Leases Payable

<table>
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<tr>
<th>Recognition Approach</th>
<th>Balance Sheet</th>
<th>Resource Flows Statement</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>No amounts recognized</td>
<td>Expenditures of $233,200 for capital outlay, expenditures of $1,273,469 for debt service, other financing sources of $233,300</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No amounts recognized</td>
<td>Outflows of resources of $1,273,469 for debt service</td>
</tr>
</tbody>
</table>

Normally Long–Term
## Recognition Example—Postemployment Benefits

Pension plan is funded. Net pension liability is $826,333 at period-end. OPEB plan is pay-as-you-go. Net OPEB liability is $42,785,037 at period-end.

<table>
<thead>
<tr>
<th>Recognition Approach</th>
<th>Pension</th>
<th>OPEB</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current financial resources</td>
<td>No liability. No amount normally expected to be liquidated with available expendable resources.</td>
<td>No liability. No amount normally expected to be liquidated with available expendable resources.</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No liability. No amounts due.</td>
<td>No liability. No amounts due.</td>
</tr>
</tbody>
</table>

**Normally Long-Term**

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## Recognition Example—Bonds Payable

Beginning of year balance: $33,414,493, all capital-related. Principal paid during the current year: $8,331,457. End of year balance: $25,083,036.

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<tbody>
<tr>
<td>Current financial resources</td>
<td>No amounts recognized</td>
<td>Expenditures of $8,331,457</td>
</tr>
<tr>
<td>Short-term financial resources</td>
<td>No amounts recognized</td>
<td>Outflows of resources of $8,331,457</td>
</tr>
</tbody>
</table>

**Normally Long-Term**
Alternative Views

- Modify short-term financial resources
  - Recognize portion of long-term receivables due in the next reporting period (both as asset and inflows of resources)
  - Recognize portion of long-term liabilities due in the next reporting period (both as liability and outflows of resources) with exceptions:
    - Pensions and other postemployment benefits
    - Asset retirement obligations

- Replace concept of normally with contractual maturities (or amounts otherwise expected to be paid in cash or other fund financial resources)

Alternative Views (Continued)

- Examples
  - General obligation bond that will be called shortly after period-end using existing resources – AV would report a liability and lower fund balance
  - Long-term debt payment due 1 month after period-end – AV would report liability and lower fund balance
  - Long-term debt payment due 11 months after period-end – AV would report liability and lower fund balance yet it is likely that the taxes that will be used to fund the payment have no yet been levied.

- Government-wide statement of cash flows
Governmental Funds—Presentation

- Current and noncurrent format of resource flows statement
- Current includes all flows other than those that are noncurrent
- Noncurrent resource flows: those related to purchase and disposal of capital assets and issuance and repayment of long-term debt

Governmental Funds—Specific Terminology

**Titles**
- Short-Term Financial Resources
- Short-Term Financial Resource Flows

**Elements**
- Short-term assets
- Short-term liabilities
- Deferred outflows of short-term financial resources
- Deferred inflows of short-term financial resources
- Short-term financial resources fund balances
- Inflows of short-term financial resources for current activities
- Outflows of short-term financial resources for current activities
- Net flows of short-term financial resources for noncurrent activity
Governmental Funds—Specific Terminology

- “This financial statement presents a short-term view of governmental fund activities and reports items of a long-term nature differently from how they are reported in the government-wide financial statements.”

Illustration 3: Short-Term Financial Resources Balance Sheet

[Table and text related to the short-term financial resources balance sheet]
Proprietary Fund Financial Statement Presentation

- Continue separate presentation of operating and nonoperating revenues and expenses

- Operating revenues and expenses are those other than nonoperating

- Nonoperating revenues and expenses include:
  - Subsidies received and provided
  - Revenues and expenses related to financing
  - Resources from the disposal of capital assets and inventory
  - Investment income and expenses
Proprietary Fund Financial Statement Presentation

- **Subtotal for operating income (loss) and noncapital subsidies**

- **Subsidies are**: resources provided by another party or fund to keep rates lower than otherwise would be necessary to support the level of goods and services to be provided
Budgetary Comparison Information

- Presented in required supplementary information
  - Consistent with conceptual framework on methods of communication

- Required variance presentations
  - Final budget and actual amounts
  - Original and final budget

Major Component Unit Information

- If feasible, present in separate columns on the reporting entity’s government-wide financial statements
- If not feasible, present in combining financial statements after the fund financial statements (included in basic financial statements)
- The existing alternative to present condensed major component unit financial statements in the notes to financial statements would be eliminated
Government-Wide Expenses by Natural Classification

- Applicable to governments presenting a CAFR
- Presented as supplementary information
- Governmental activities by program or function (and natural classification)
- Business-type activities by different identifiable activity (and natural classification)
- No change to government-wide statement of activities

You get to choose the Natural Classifications. This proposal appears to be on its way out!
Small Government Considerations

- Are there opportunities to offer practical considerations for small governments without undermining the fundamentals of the model?
  - Recognition in governmental funds
  - Presentation of governmental funds
  - Presentation of proprietary funds
  - Budgetary comparison information
  - Major component unit information
  - Schedule of government-wide expenses by natural classification
- Continue to consider in future

Next Steps

- Additional issues for Exposure Draft
  - Extraordinary and special items
  - Management's discussion and analysis (MD&A)
  - Debt service funds
- Target issuance of Exposure Draft: June 2020