



STATE AND LOCAL GOVERNMENT FINANCE DIVISION
AND THE LOCAL GOVERNMENT COMMISSION

SHARON EDMUNDSON
DEPUTY TREASURER

June 4, 2021

Mr. Alan Skelton
Director of Research and Technical Activities
Project No. 4-7
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Skelton:

Thank you for the opportunity to comment on the Governmental Accounting Standards Board (GASB or Board) Exposure Draft – Compensated Absences. We believe that the issues being considered by the GASB in this project are important in the Board's efforts to provide more and better information to financial statement users.

The North Carolina General Statutes have given the responsibility to the Local Government Commission, through its staff, to monitor the financial condition of approximately 1,350 local governments and public authorities across the State. These units include municipalities, counties, schools, public hospitals, water and sewer authorities, and other public authorities, all of which are required to submit to us an annual audit prepared under generally accepted accounting principles. Another responsibility we have is to advocate for local governments with regulatory groups including the GASB. Our response was formulated considering not only our needs as users of the financial statements but also their needs for clear, reasonable, and cost-effective reporting standards.

After careful review of the material contained in the Exposure Draft and in consideration of our responsibilities, we offer the following comments.

FIFO Method

Under paragraph 14 of the proposed guidance, a government should use the first-in, first-out (FIFO) flows assumption when estimating the compensated absences liability that is due within one year. We believe this is a significant change for governmental funds when paired with the new reporting model requirements that are scheduled to be implemented in a few years. We also believe that this requirement is arbitrary and unnecessary as the total liability will be unchanged regardless of the flows assumption that is adopted. Requiring FIFO in conjunction with the paragraph 7 requirement to record a liability when compensated absences are more likely than not to be paid, will significantly increase the amount of the liability due within a year. We believe both LIFO and FIFO flows assumptions should be allowed, as is currently the case.

We recommend that the GASB allow both the LIFO and FIFO flows assumptions when estimating the compensated absences liability that is due within one year.

Accrual of Defined Contribution Pension and OPEB Salary-Related Payments

Under paragraph 20 of the proposed guidance, future employer contributions to defined contribution plans (i.e. a 401K plan) that are associated with payments to be made for compensated absences are to be recognized as OPEB or retirement expense and accrued as an OPEB or retirement liability when the compensated absence is recognized. We believe this will create a lack of reciprocity in contribution recognition between employers and cost-sharing defined contribution plans.

For example, North Carolina administers a cost-sharing 401K plan with over 1,000 participating employers including school systems, cities, counties, and state agencies. The employers have varying contribution rates and PTO policies. The 401K plan's fiscal year end is December 31, which is different from the majority of the participating employers. It is not remotely feasible that the plan can gather the information necessary to estimate and accrue a contribution revenue and receivable related to the employers' compensated absences to adequately reflect the amounts accrued as an expense and liability by each employer under the proposed guidance. We believe the proposed requirement will provide little to no benefit to users of financial statements and will increase the cost of reporting for employers and the defined contribution plans.

We recommend that future employer contributions to defined contribution plans associated with payments to be made for compensated absences not be accrued to OPEB/retirement expense and liability accounts. If the GASB determines that these charges need to be accrued, then we recommend they be accrued to the compensated absence liability and expense/expenditure accounts.

Sick Leave

The Exposure Draft adds sick leave as a compensated absence liability. Under GASB 16 sick leave had rarely been a compensated absences liability in North Carolina since it was based on a future event and rarely paid in cash. This will be a significant liability under the new model, especially when it is paired with the change in the flow assumption requirements. We do not believe that the resulting significant liability is economically substantive, since sick leave is based on a future economic event and is rarely paid in cash, but with time off.

We recommend that the GASB include separate guidance for sick leave in the new standard, similar to the guidance contained in GASB 16.

General

A significant amount of work is going to be required given that the GASB is proposing a host of factors to consider in the determination of whether a compensated absence is more likely than not to be either paid or settled through other means. The information is available from each unit's human resources department, but it may require significant effort to prepare. In North Carolina, there are over 400 municipalities with populations under 5,000 people. It is unrealistic to expect personnel in these governments to spend a great deal of time estimating these amounts in light of their other responsibilities. We believe that many smaller units will not have the trained personnel to perform the required calculations. We also believe that the net effect of the proposed guidance will not have a significant positive impact on current financial reporting. As a result, the effort that will be required is disproportionate to any resulting improvement in financial reporting.

We recommend that the GASB reconsider issuing any new guidance related to compensated absences without significant reductions in the requirements currently contained therein.

We agree with the Paragraph 11 requirements for recognizing liabilities for future pay changes in the period in which they occur and the Paragraph 24 requirements for recognizing liabilities and expenditures in Governmental Funds as the amounts come due each period in a continuation of the GASB Interpretation #6 requirements. We also agree with the Paragraph 25 provision that allows for a net change in compensated absences liabilities to be reported.

We are available to assist you in addressing each matter discussed in this response letter. If you have any questions, please contact me at susan.mccullen@nctreasurer.com.

Sincerely,

Susan McCullen

Susan McCullen CPA
Director, Fiscal Management Section
State and Local Government Finance Division