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DEPARTMENT OF STATE TREASURER

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DALE R. FOLWELL, CPA

STATE AND LOCAL GOVERNMENT FINANCE DIVISION

Proposed Changes in Government GAAP

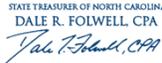
Sharon Edmundson, MPA, CPA
Deputy Treasurer

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Agenda:

- Financial Reporting Model Improvements – Exposure Draft
 - Basic concepts
 - Effects on various segments of financial reporting
 - Expected implementation timeframe
- Revenue and Expense Recognition – Preliminary Views
 - Basic concepts
 - Effects on types of revenues and expenses
 - Expected implementation timeframe

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GASB Projects

PROJECT	STATUS	COMMENTS DUE	FINAL DOCUMENT
Update on Implementation Guidance	ED	2/15/2021	2 ND Q 2021
Financial Reporting Model	ED	2/26/2021	2 ND Q 2022
Recognition of Elements of Financial Statements	ED	2/26/2021	2 ND Q 2022
Revenue and Expense Recognition	PV	2/26/2021	ED 2 ND Q 2023

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Financial Reporting Model Improvements

- Changing to a theory-based model
- Encompasses review of MD&A, government-wide statements, major funds, governmental/proprietary/fiduciary funds, and budgetary considerations

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Financial Reporting Model Improvements

MD&A

- Primary goal is to reduce boilerplate language and make a more meaningful document
- Focus on analysis of why things change from year to year
- Eliminate some of repetition
- Consolidated into 5 sections

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Financial Reporting Model Improvements

Five Sections

- Introduction
- Financial Summary
- Detailed analysis
- Significant capital and long-term debt activity
- Currently known facts, decisions, and/or conditions that will have a significant impact on the entity's financial position or cause significant differences from the current period financial results

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Financial Reporting Model Improvements

Change in terminology and classification

- No more special or extraordinary items
- Single category of unusual or infrequent in occurrence (can be both)
 - Management input or involvement no longer relevant

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POLLING QUESTION #1



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Financial Reporting Model Improvements

Governmental Fund Reporting

- Moving to a short-term financial resources measurement focus and accrual basis of accounting in lieu of modified accrual
- New titles for statements
 - Short-term financial resources balance sheet
 - Statement of short-term financial resource flows

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Financial Reporting Model Improvements

What is reported?

- Inflows and outflows of short-term financial resources
- All short-term financial assets
- Deferred outflows of resources
- Liabilities
- Deferred inflows of resources
- Fund balance

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Financial Reporting Model Improvements

- Recognize short-term transactions and other events as they occur
 - Duration from inception to conclusion is one year or less
- Recognize long-term transactions and other events when they are due
 - Duration from inception to conclusion is greater than one year
- Transactions – external events between the entity and another entity requiring action by one or more party and have financial consequences for the government
 - First occurs when one party takes an action that results in the recognition of an asset or liability

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Financial Reporting Model Improvements

- Other events – internal transactions and other events that don't meet the definition of a transaction
- Once classification is determined, it does not change regardless of any changes in the transaction

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Financial Reporting Model Improvements

Recognition of Assets and Liabilities

- Assets are those that result from short-term transactions and other events
 - Includes inventory and pre-pays
 - Investments are reported as assets consistent with the definition of financial assets
- Assets arising from long-term transactions and other events are recognized when payments are due

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Financial Reporting Model Improvements

- Liabilities
 - Those that arise from short-term transactions and other events
 - Long-term debt issued for short-term purposes
 - Tax anticipation notes with maturities beyond one year
 - Revenue anticipation notes with maturities beyond one year
 - Liabilities from long-term transaction and other events are recognized as they come due

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Financial Reporting Model Improvements

Inflows and Outflows of Resources

- Inflows recognized
 - Short-term transactions and other events as they occur
 - Long-term transactions and other events as they are due except for long-term debt issued for short-term purposes
 - Also includes on-behalf payments for fringes and salaries
 - Also includes direct vendor financings

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Financial Reporting Model Improvements

- Outflows recognized
 - Short-term transactions and other events as they occur
 - Long-term transactions and other events as they come due
 - Long-term debt for short-term purposes is recognized as short-term
 - Includes on-behalf payments for fringes and salaries
 - Includes outflows associated with direct vendor financings

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Financial Reporting Model Improvements

- **Deferred Inflows and Outflows**
 - Recognized for both short and long-term transactions and other events when the flow of resources is applicable to a future reporting period
 - Continue to be restricted to those instances identified in GASB Statements
 - Taxes collected or recorded as receivables that are applicable to a future period are deferred inflows

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POLLING QUESTION #2



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Financial Reporting Model Improvements

Proprietary Fund Reporting

- No change in measurement focus or basis of accounting
- Will report non-operating revenues and expenses somewhat differently

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Financial Reporting Model Improvements

Definitions

- Operating revenues and expenses are those other than non-operating revenues and expenses
- Non-operating revenues and expenses
 - Subsidies provided and received
 - Revenues and expenses related to financings
 - Resources from the disposal of capital assets and inventory
 - Investment income and expenses
 - Subsidies are resources received from or provided to another party or fund to keep rates lower or keep rates higher than is necessary to support operations

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Financial Reporting Model Improvements

Exception

- If revenues and expenses that are typically considered non-operating constitute the main operations of a proprietary fund then they are considered operating
- Example – fund that provides funding for first-time homeowners

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Financial Reporting Model Improvements

Budgetary Reporting

- All RSI with no option to include in basic financial statements
- No longer subject to auditors' opinion
- Will report variances between original and final budget and variance between final budget and actual
- Analysis of significant variances will be in the notes to RSI
- Analysis should include any known reasons for those variances that are expected to have a significant effect on fund balance or produce results significantly different from current period

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Financial Reporting Model Improvements

Potential Implementation Timeline

- Two-tier phased-in approach with thresholds determined by FYE 6/30/23 (NC) – first fiscal year beginning after 6/15/22
 - \$75 million or more in revenue for governmental and enterprise funds less any revenue from special and/or extraordinary items
 - Implement FYE 6/30/25
 - \$75 million or less in revenue for governmental and enterprise funds less any revenue from special and/or extraordinary items
 - Implement FYE 6/30/26
- Fiduciary activities only governments will use additions instead of revenues

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Revenue and Expense Recognition

- Primarily focuses on measurement focus/basis of accounting for government-wide and enterprise funds
- Three components
 - Categorization
 - Recognition
 - Measurement

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Revenue and Expense Recognition

- Methodology for both revenue and expense recognition consists of four steps
- Revenue
 1. Does the government have an increase in net assets?
 2. Does the increase in net assets result in a related liability?
 3. Does the increase in net assets result in an inflow related to a future period?
 4. Recognize revenue

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Revenue and Expense Recognition

- Expenses
 1. Does the government have a decrease in net assets?
 2. Does the decrease in net assets result in a related asset?
 3. Does the decrease in net assets result in an outflow applicable to a future period?
 4. Recognize expense

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Revenue and Expense Recognition

Categorization Methodology

- Another four-step process
 1. Is there a binding arrangement?
 2. Is there mutual assent of the parties?
 3. Are there identifiable rights and obligations that are substantive?
 4. Are the rights and obligations interdependent?
- If no binding arrangement the transaction is out of scope of project

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Revenue and Expense Recognition

- If government believes that all four characteristics are present, transaction is a Category A transaction
- Any other transaction within the scope of the project is a Category B transaction
- Eliminate the exchange/non-exchange classification

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Revenue and Expense Recognition

Binding arrangement

- Intended to include a wide variety of arrangements
- Can be oral, written, or implied by the government's practices
- Examples include grant agreements, contracts, MOUs, legislation, issuance of a legally-enforceable purchase order
- Other examples based on a government's practices include creation of a new utility account with a public utility or the purchase of a ticket for a public transportation system

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Revenue and Expense Recognition

Other categorization considerations

- Determine at binding arrangement level, including binding arrangements with multiple transactions
- If the binding arrangement has both Category A and B transactions, then determine categorization at transaction level
- If term change in binding arrangement, reassess if rights or obligations have significantly changed
- Can use portfolio approach

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Revenue and Expense Recognition

- Recognize transactions based on determination of Category A or Category B transactions
 - Category A will be those with a performance obligation
 - Composed of acquisitions coupled with sacrifices or sacrifices coupled with acquisitions that are interdependent

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Revenue and Expense Recognition

- Category B transactions are
 - Acquisitions without sacrifices
 - Sacrifices without acquisitions
 - Acquisitions and sacrifices that are not interdependent
- Category B will be one of the following five: (1) derived revenue, (2) imposed revenue, (3) contractual binding arrangement, (4) general aid to governments, and (5) shared revenue

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Revenue and Expense Recognition

Category A Revenue Transactions

- Expenditure –drive grants
- Healthcare procedure
- Loan/grant – combination award from state to local government
- State lottery
- Summer camp
- Transit pass
- College tuition

PV has extensive discussion of the transaction details and how they reached the classification as Cat A for each transaction

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Revenue and Expense Recognition

Category B Revenue Transactions

- General state aid to school districts
- Passenger facility charge
- Pledge
- Professional license
- Property tax
- Purpose restricted grants and donations
- Special assessment
- State sales tax shared with counties
- Traffic ticket

Again, GASB has extensive discussions of each

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Revenue and Expense Recognition

Category A Expense Transactions

- Expenditure drive grant
- Loan/grant combination
- Supplies expense
- Teacher salaries

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Revenue and Expense Recognition

Category B Expense Transactions

- General state aid to school districts
- State sales tax shared with counties

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Revenue and Expense Recognition

- Comments due by February 26, 2021
- Public hearings Spring 2021
- Exposure Draft, second quarter, 2023
- Final standard, first quarter, 2025

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Revenue and Expense Recognition

GASB is offering several free webinars on the Revenue and Expense Recognition project – free CPE too!

<https://gasb.org/jsp/GASB/Page/GASBSectionPage&cid=1176158838207>

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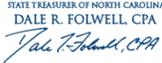
POLLING QUESTION #3



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Proposed Changes to Governmental GAAP

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