



State of North Carolina

Department of State Treasurer

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*State and Local Government Finance Division
and the Local Government Commission*

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Memorandum #974

TO: Officials of Local Governments and Certified Public Accountants

FROM: T. Vance Holloman, Director
Fiscal Management Section

SUBJECT: Financial Reporting Issues for Governmental Accounting Standards
Board (GASB) Statement No. 34

GASB Statement No. 34 permits the financial statement preparer a choice of options for several of the reporting requirements of the Statement. GASB Statement No. 34 changes also raise questions about the need for and format of supplemental schedules currently required to demonstrate that units are complying with the General Statutes. The staff of the Local Government Commission (LGC) has sought the assistance of task forces of the North Carolina Association of Certified Public Accountants (NCACPA) and the North Carolina Government Finance Officers Association (NCGFOA) in developing a uniform reporting format for local governments and public authorities in North Carolina. For many years, local units and their citizens have benefited from comparability of financial statements. Management and citizens of local units can compare their unit's operations between years, and with other units. Comparability of financial statements has also contributed to lower financing rates for debt. Citizens and other statement users must receive the information needed to judge and compare the performance of local governments and public authorities. For these reasons the LGC, in conjunction with the aforementioned groups, will standardize the financial report format under Statement 34 as needed to ensure comparability of statements.

The NCACPA and NCGFOA task forces made recommendations concerning capital asset reporting, preparing government wide statements, budgetary reporting, preparing combining and individual fund statements, and preparing for implementation. Their recommendations and the LGC staff's reporting standards on the issues follow.

NCACPA and NCGFOA RECOMMENDATIONS

Capital Assets Reporting

1. Retroactive reporting – should we encourage only minimum compliance?

NCACPA and NCGFOA Recommendation: Most governments will choose minimum compliance; however, the LGC staff should encourage units of government to minimize costs by only meeting the minimum requirements in GASB Statement No. 34

LGC Reporting Standard: The LGC encourages units of government to minimize costs by only meeting the minimum requirements in GASB Statement No. 34.

2. Use of the modified approach for infrastructure.

NCACPA and NCGFOA Recommendation: *For the present, the LGC staff should require that this method not be used for infrastructure reporting. Nationally, it will be very uncommon and if units of government follow this accounting method it will result in inconsistency between governments. The executive board of the National GFOA has also adopted a position statement discouraging governments from using the modified approach.*

LGC Reporting Standard: *To provide for comparability of units' financial statements, units should not use the modified approach for infrastructure reporting.*

3. "Gross" vs. "Net" reporting, display of asset classes on the face of statement.

NCACPA and NCGFOA Recommendation: *The LGC staff should recommend the use of the "net" method with the details of asset classes and accumulated depreciation being disclosed in the notes and not on the face of the financial statements.*

LGC Reporting Standard: *Units should use the net method of reporting and not report classes of assets on the face of the financial statements. Gross amounts and the details of asset classes should be reported in the notes to the financial statements.*

4. Capitalization thresholds.

NCACPA and NCGFOA Recommendation: *The LGC staff, as it has done in recent memos, should strongly encourage units of government to evaluate their capitalization thresholds to determine if they should be increased. Many units of government use extremely low capitalization thresholds. The national GFOA executive board has adopted a policy of recommending a minimum capitalization threshold of \$5,000 for every government in the United States. Since increased thresholds will facilitate implementation of the new reporting model, the LGC staff should continue to emphasize the importance of re-evaluating and increasing capitalization thresholds. \$5,000 should be the minimum suggested by the LGC staff for tangible personal property. For those governments having significant infrastructure assets, multiple capitalization thresholds should be used with a much higher threshold being used for infrastructure assets. No specific amount should be recommended, only that local governments and public authorities establish a threshold based on the size of the entity and in such a manner that a material amount of assets is recorded. The LGC staff should also ensure that local officials understand the distinction between which capital asset information should be included for financial reporting purposes and the inventory of assets that is necessary for insurance purposes.*

LGC Reporting Standard: *The LGC continues to encourage units to determine if their capitalization levels should be increased.*

5. The board of the national GFOA has adopted a policy that local governments are not required to implement the infrastructure reporting requirements of GASB Statement No. 34 in order to participate in the Certificate of Achievement Program. What should be North Carolina's response to this decision? Should the LGC staff allow governments to move in this direction?

NCACPA and NCGFOA Recommendation: The LGC staff should prohibit this option. G.S. 159 requires a detailed listing of all assets and exceptions cannot be made just because it is difficult to collect the information in some cases. It would result in audit opinion qualifications, which might have credit rating implications. It also would set the dangerous precedent of picking and choosing accounting standards.

LGC Reporting Standard: Units should comply with the requirement of G.S. 159-34 to maintain a detailed listing of all assets and to prepare their financial statements in accordance with generally accepted accounting principles.

Government-wide Statements

1. Use of "net assets" or "balance sheet" format.

NCACPA and NCGFOA Recommendation: In order to ensure consistent reporting from North Carolina units of government, the LGC should encourage the use of the net assets presentation in the Statement of Net Assets. This is the method preferred by the GASB and illustrated in the GFOA "Blue Book."

LGC Reporting Standard: Units are encouraged to use the net assets format.

2. Reporting entity totals and prior year totals.

NCACPA and NCGFOA Recommendation: At the present time the LGC staff should not encourage the use of either of these totals in the government-wide financial statements.

LGC Reporting Standard: The LGC does not encourage the use of reporting entity or prior year totals in government-wide financial statements.

3. Contact discretely presented component units for discussions on implementation.

NCACPA and NCGFOA Recommendation: The LGC should continue to encourage units of government to contact officials in any discretely presented component unit to ensure that they are preparing for implementation.

LGC Reporting Standard: Units should contact their discretely presented component units to verify that the discretely presented component units are preparing for implementation.

4. Differences in how activities are reported between the government-wide and fund financial statements (Example: Parks and Recreation Enterprise Fund reported with governmental activities.)

NCACPA and NCGFOA Recommendation: Governments should not reclassify various items between the fund and government-wide financial statements. An example would be reporting the sanitation department, which is accounted for in the general fund, in the business-type activities column of the government-wide statements because the sanitation department charged a user fee. Reclassifying activities in this manner, while allowed by GASB Statement No. 34, is confusing to financial statement users and requires unnecessarily complex reconciliations. The LGC staff should discourage this practice. If units of government desire this information, they should consider modifying their fund structures so that there is a consistent flow between the government-wide and fund financial statements. Some standardization of funds used for various activities also would be helpful. At a minimum the LGC staff should remind local governments that state law requires the use of enterprise funds in some circumstances.

LGC Reporting Standard: Activities accounted for and reported in enterprise funds in the fund statements should not be reported in the governmental activities column on the government-wide statements. Activities reported in the governmental funds on the fund statements should not be reported in the business-type activities column on the government-wide statements.

5. Presenting a separate column for indirect expenses on the Statement of Activities

NCACPA and NCGFOA Recommendation: Governments should not allocate indirect expenses in the financial statements. The information presented will not be consistent with other units of government and will potentially present information in an arbitrary manner. The financial statements are not an appropriate place to report cost accounting information.

LGC Reporting Standard: Units should not allocate indirect expenses in the Statement of Activities.

6. Other guidance on statement formats, allocation of depreciation expenses, whether different revenue sources are general or program revenues, etc.

NCACPA and NCGFOA Recommendation: The LGC staff is interested in the opinions of the NCACPA and NCGFOA members concerning revenue sources and the structure of the illustrative chart of accounts. In the near future the LGC staff will forward requests for information to task force members.

LGC Reporting Standard: The LGC staff has and will continue to get the opinions of the NCACPA and NCGFOA on financial reporting issues.

Budgetary Reporting

1. Basic statements or Required Supplementary Information (RSI)?

NCACPA and NCGFOA Recommendation: These statements should be included with the basic financial statements. The information in these statements is essential and is widely utilized by many persons, including elected officials. Reporting this information as RSI essentially reduces it to unaudited status. The LGC should mandate that it should be reported as an audited financial statement.

LGC Reporting Standard: Budget to actual statements for the General Fund and major annually budgeted Special Revenue Funds should appear in the basic financial statements.

Combining and Individual Fund Statements

1. Will individual fund statements be included?

NCACPA and NCGFOA Recommendation: Yes, even though these statements are not required for a minimum GAAP presentation, they do provide beneficial information to many users, including the credit community. GFOA's Certificate of Achievement Program requires that this information be presented as part of a CAFR and the combining and individual fund statements for non major (including internal service and fiduciary) funds are illustrated in the new "Blue Book". The task forces believe that the LGC staff should require reporting of non-major funds in the combining and individual fund financial statements as is the current requirement for local governments in North Carolina.

LGC Reporting Standard: Units should report non-major funds in the combining and individual fund financial statements in the supplemental schedules.

2. What individual budget / actual presentations will be required?

NCACPA and NCGFOA Recommendation: The recommendation for this item is similar to #2 above. These statements are required for local governments in North Carolina under current practice. They should also be required under the new reporting model, even for enterprise funds that are not required to present budget / actual comparisons under current GAAP.

LGC Reporting Standard: GASB Statement No. 34 has not changed the need for individual fund budget to actual statements to demonstrate compliance with General Statutes. These statements, for funds other than the General Fund or major annually budgeted Special Revenue Funds, should be included in the supplemental schedules.

Schedules

1. Will capital asset schedules be required?

NCACPA and NCGFOA Recommendation: The LGC staff, under current reporting practices for North Carolina local governments, does not require the 3 capital asset schedules. GFOA's Certificate of Achievement Program previously recommended them for program participants (failure to include these schedules would not result in a loss of a government's Certificate of Achievement). Similar versions of these schedules are included in GFOA's illustrative financial statements in the new "Blue Book", but they are no longer part of the program checklist. Since this information is included to a large extent in the notes to the financial statements, the task force believes that the LGC staff should not require the inclusion of these 3 schedules in the financial statements.

LGC Reporting Standard: The LGC will not require additional capital asset schedules to be included in the financial statements.

2. Will LGC-mandated schedules (analysis of current tax levy, etc.) be included?

NCACPA and NCGFOA Recommendation: Until such time as the information in these 3 schedules is required for GAAP reporting, the information should be presented in schedules that are required by the LGC staff.

LGC Reporting Standard: The Schedule of Ad Valorem Taxes Receivable and the Analysis Current Tax Levy are needed to report the efforts of the unit in fulfilling its fiduciary responsibility to citizens to collect property taxes and should be included in the supplemental schedules.

Units implementing Statement No. 34 will also be implementing Statement No. 38 that requires footnote disclosures of interfund transfers as well as receivables and payables. These schedules will no longer be required for units that have implemented Statement No. 38.

Preparation for Implementation

1. Opening balances for Statement of Net Assets.

NCACPA and NCGFOA Recommendation: The LGC staff should encourage units of government and their independent auditors to perform preliminary work prior to the year of implementation to ensure that opening statement of net asset balances are accurate and that accounting system and report formatting issues have been properly addressed. Local officials should also develop statement of activities classifications. In addition, they should begin developing the information that is needed to present a statement of cash flows using the direct method (if applicable).

LGC Reporting Standard: Units are encouraged to perform work prior to the year of implementation. This work should include determining beginning net assets for business-type and governmental activities. Units should determine if their accounting system can provide the

information needed to implement Statement 34 and what changes might be needed. This would include being able to generate the information needed to present a direct method cash flow statement. Units and their auditors should also address reporting issues, including identifying activities for the government wide statements.

2. Will early implementation be encouraged?

NCACPA and NCGFOA Recommendation: The task force believes that the LGC staff should strongly encourage units of government not to early implement GASB Statement No. 34 and the related GASB statements and interpretations. Many audit issues remain to be resolved and much will be learned as units of government implement the new reporting model in their required stages.

LGC Reporting Standard: The LGC encourages units not to early implement Statement No. 34. Any unit considering early implementation should contact our staff.

If you have any questions about this memorandum, please contact Sharon Edmundson at 919-807-2394 or Sara Shippee at 919-807-2386.