*THE* ***GASB*** *REPORT*

***No. 315-A / June 2011***

*(The GASB Report No. 277)*

***GASB Calendar***

The GASB has scheduled the following public meeting dates:

***August 17–19***

***October 4–6***

The GASB also is scheduled to meet via **teleconference** on **July 26** and **September 8.** The precise time, as well as the agenda, will be announced approximately two weeks before each meeting. Unless otherwise indicated, all meetings are held at the Financial Accounting Foundation (FAF) offices in Norwalk, Connecticut.

In addition, the FAF Trustees will meet on August 23 in New York City.

Finally, the GASB will be holding public hearings and user forums on the pension Exposure Drafts on October 3 and 4, respectively, in East Elmhurst, New York (LaGuardia Plaza Hotel); October 13 and 14, respectively, in San Francisco, California (Sir Francis Drake Hotel); and October 20 and 21, respectively, in Chicago, Illinois (Renaissance Chicago O’Hare Hotel).

The GASB also will be holding public hearings on the concepts Preliminary Views at the above hotels in the morning on October 4, October 14, and October 21.

Please check the GASB website at www.gasb.org three working days prior to meetings to verify the final agenda.

If you plan to attend *any* meetings, please notify Ragan Vincent at (203) 956-5372 or via email at rpvincent@gasb.org. In addition, due to the FAF’s security procedures, visitors to the Norwalk meetings are required to go to www.gasb.org to register at least 24 hours before each meeting they are planning to attend.

***GASB Approves Statement 63 on the Statement of Net Position***

In June, the GASB unanimously approved Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* which establishes guidance for reporting deferred outflows of resources, deferred inflows of resources, and net position in a statement of financial position.

While prior to the issuance of Statement 63 it was unclear where these elements should be reported in the statement of financial position, the GASB has now provided a framework that specifies where deferred outflows of resources and deferred inflows of resources—as well as assets and liabilities—should be displayed. The Statement also discusses how net position—no longer net assets—should be displayed. Ultimately, this new framework will serve to standardize the presentation of deferred balances and their effects on a government’s net position and address uncertainty related to their display.

Concepts Statement No. 4, *Elements of Financial Statements,* identifies and defines five elements that make up a statement of financial position: assets, liabilities, deferred outflows of resources, deferred inflows of resources, and net position. Statement No. 34, *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments,* however, which was issued several years prior to that Concepts Statement, requires the presentation of assets, liabilities, and net assets in a statement of financial position. Therefore, guidance was needed to address the presentation of deferred outflows of resources, deferred inflows of resources, and net position in a financial statement.

The need for this guidance is more urgent because GASB pronouncements have already addressed transactions requiring the use of deferred outflows of resources or deferred inflows of resources. Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments,* for example, provides for the reporting of deferred outflows of resources and deferred inflows of resources for the changes in fair value of hedging derivatives. In addition, the guidance on service concession arrangements in Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements,* requires that at least a portion of the up-front payment a government receives under a service concession arrangement be reported as a deferred inflow of resources and recognized over the length of the transaction, rather than reported as revenue immediately. The GASB also is deliberating other projects that may result in the recognition of deferred outflows of resources and deferred inflows of resources. For example, the reexamination of the GASB’s pension accounting and financial reporting standards may ultimately result in the reporting of deferrals.

Statement 63 establishes a framework detailing how these elements should be reported, which will result in standardizing the presentation of deferred balances and their effects on a government’s net position. This should address uncertainty regarding the role of these financial statement elements.

The Statement specifies that the statement of net position should report all assets, deferred outflows of resources, liabilities, deferred inflows of resources, and net position and identifies two formats that may be used. Use of the net position format is encouraged (assets plus deferred outflows of resources minus liabilities minus deferred inflows of resources equal net position); however, use of the balance sheet format (assets plus deferred outflows of resources equal liabilities plus deferred inflows of resources plus net position) also is permitted. Statement 63 also specifies that the statement of net position should report the residual amount as net position rather than net assets.

Under the Statement, net position should be displayed in three components similar to those currently required for net assets: net investment in capital assets, restricted, and unrestricted.

With respect to the disclosure requirements in the Statement, if multiple types of deferred outflows or deferred inflows are aggregated on the face of the financial statements, then governments are required to provide details about the different types of deferrals in the note disclosures. If the amount reported for a component of net position is significantly impacted by deferrals, a government will include a note explaining the effect of the deferred amounts on the net position balances.

***Effective Date***

The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011, with earlier application encouraged.

***How to Order Copies***

Statement 63 (product code GS63) may be obtained through the GASB Order Department by calling (800) 748-0659 or through the GASB Store on the GASB website at [www.gasb.org](http://www.gasb.org).

***GASB Approves Pension Proposals, Statement 64 on the Application of Hedge Accounting Termination Provisions, Other Documents at June Board Meeting***

The GASB approved a number of documents and cleared one additional document at its June Board meeting in Norwalk, including two Exposure Drafts related to the pension accounting and financial reporting project, and GASB Statement No. 64, *Derivative Instruments: Application of Hedge Accounting Termination Provisions,* an amendment of GASB Statement No. 53. In addition, the Board cleared the 2011–2012 edition of the Comprehensive Implementation Guide.

The documents approved or cleared at this meeting will be described in detail in the July issue of *The GASB Report.* More information also will be available soon in the Projects section of the GASB website, www.gasb.org. The due process documents approved by the GASB at the June Board meeting are as follows:

Pension Accounting and Financial Reporting

• Exposure Draft, *Accounting and Financial Reporting for Pensions*

• Exposure Draft, *Financial Reporting for Pension Plans*

Conceptual Framework—Recognition and Measurement Approaches

• Preliminary Views, *Recognition of Elements of Financial Statements and Measurement Approaches.*

***Board Meeting Summary***

The GASB held a public meeting on May 23–25 in Washington, D.C. to discuss issues associated with its projects on pension accounting and financial reporting, the statement of net position, fiscal sustainability as it relates to economic condition reporting, the user guide series, government combinations, derivatives, and reporting balances previously recognized as assets and liabilities.

The Board also met via teleconference on June 14 to discuss issues associated with its projects on recognition and measurement approaches under its conceptual framework, derivatives, the statement of net position, and pension accounting and financial reporting.

In addition, the Board held a public meeting on June 27–29 at its office in Norwalk, Connecticut, to discuss issues associated with its projects on pension accounting and financial reporting, recognition and measurement approaches under its conceptual framework, derivatives, the 2011–2012 edition of the *Comprehensive Implementation Guide,* government combinations, the user guide series, reporting balances previously recognized as assets and liabilities, and fiscal sustainability as it relates to economic condition reporting. Due to publication deadlines, details of those deliberations are not described in this issue of The GASB Report but will be highlighted in the next issue.

***Pension Accounting and Financial Reporting***

In its project on pension accounting and financial reporting, the Board reviewed preballot drafts of two Exposure Drafts related to pensions. In addition, the Board discussed the Plain-Language Supplement that will accompany the Exposure Drafts. Individual Board members made recommendations and clarifying suggestions on the three documents.

At the June teleconference, the Board discussed five issues:

• The service cost attribution approach that should be used for benefit arrangements that are not pay related

• The definitions of pension plan, covered payroll, and actuarially calculated employer contributions

• The classification of component units as employers

• Disclosure requirements for nonemployer contributing entities involved in unconditional special funding situations

• Effective date provisions.

With regard to the service cost attribution approach for benefit arrangements that are not pay related, the Board tentatively agreed that the Exposure Draft should require use of the level percentage of pay approach unless there is no projected pay for the employee. In circumstances in which there is no pay, the inflation assumption should be substituted for the salary increase assumption when applying the level percentage of pay approach.

In considering the definitions of *pension plan,* the Board tentatively agreed that a pension plan should be defined as a trust or other fund through which assets dedicated to the payment of pensions are accumulated and pension benefits are paid as they come due in accordance with the benefit terms. The Board further agreed that the scope of the proposed plan Statements should extend only to pension plans that are administered through qualified trusts and equivalent arrangements. For pension plans that are not administered through qualified trusts and equivalent arrangements, the Board agreed that the requirements of Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans,* should continue to be applicable.

Similarly, the Board tentatively agreed that the scope of the proposed document related to accounting and financial reporting for pensions should be limited to pensions that are provided through plans that are administered through qualified trusts and equivalent arrangements. For benefits not administered in that way, the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers,* as amended, tentatively would continue to be applicable.

The Board also tentatively agreed to characteristics that should be included in the definitions of *covered payroll* and *actuarially calculated employer contributions.* The Board tentatively agreed that covered payroll should be a measure of the total salaries provided to all plan members that are provided with benefits through the terms of the plan. The Board also agreed that the term *actuarially calculated employer contribution* should include the notion that it is a target or recommended amount of contributions to a defined benefit pension plan for a reporting period that is determined in conformity with Actuarial Standards of Practice by the most recent calculations available when the contribution for the reporting period was adopted.

With regard to the classification of component units as employers, the Board tentatively agreed that a primary government and its blended and discretely presented component units that participate in the same plan should be classified as one employer for purposes of the proposed pension standards if the primary government and its component unit(s) are the only governments whose employees are provided with benefits through the plan. The Board further clarified that the primary government and the component unit(s) should be required to apply the accounting and financial reporting requirements for cost-sharing employers when preparing information for their stand-alone financial reports. However, in the financial report of the reporting entity that includes the primary government and its component units, the Board tentatively agreed that the note disclosure requirements of a single employer should be presented.

The Board tentatively decided that a governmental nonemployer contributing entity involved in an unconditional special funding situation generally should follow the same requirements for note disclosures and required supplementary information with regard to the pensions that tentatively have been required for the employer, if the nonemployer contributing government is required to make a substantial portion of the required contributions to the plan.

The Board also tentatively agreed on the note disclosures that should be required if the governmental nonemployer contributing entity is not required to make a substantial portion of the contributions to the plan.

With regard to disclosure requirements for nonemployer contributing entities involved in unconditional special funding situations for defined contribution pensions, the Board tentatively decided that a governmental nonemployer contributing entity should be required to disclose information at the same level of detail as an employer, if the nonemployer contributing government is required to make a substantial portion of the legally required contributions to the plan.

The Board also tentatively agreed on the note disclosures that should be required if the governmental nonemployer contributing entity is not legally required to make a substantial portion of the contributions to the plan.

With regard to the effective date of the proposed pension standards, the Board tentatively agreed that the requirements of the proposed Statements should be effective for periods beginning after June 15, 2012, for governments that would be required to report information about pensions provided through a single-employer plan that has net assets of $1 billion or more in the plan’s first fiscal year ended after June 15, 2010. For all other governments, the proposals tentatively would be effective for periods beginning after June 15, 2013.

***Statement of Net Position***

The Board reviewed and discussed the preballot draft of a final Statement at the May public meeting. The draft highlighted the changes that were agreed upon at the prior meeting. While the Board generally agreed that the modifications were appropriate, individual Board members made a number of clarifying suggestions throughout the draft.

At the June teleconference, the Board reviewed the ballot draft of the final Statement, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* and agreed to certain minor clarifying changes. After considering these changes, the Board members unanimously approved the Statement for issuance.

***Economic Condition Reporting—Fiscal Sustainability***

The Board discussed and largely confirmed the previous tentative decisions reached in the economic condition reporting: fiscal sustainability project. Amendments were made to previous tentative decisions regarding specific measures of fiscal sustainability information and determining what is considered “major.”

The Board discussed and tentatively confirmed the previous decisions on the necessity and content of the proposed measures of fiscal sustainability and made a few clarifying amendments. The Board noted that from a practical standpoint, the project would propose four new specific measures of fiscal sustainability information because projections of annual debt service payments are already required to be disclosed in the notes to the financial statements.

Next, the Board discussed and reached a tentative agreement to amend the proposal with respect to the determination of “major” in relation to the measures of fiscal sustainability. The Board tentatively agreed that in order for an individual inflow, outflow, and financial obligation of a governmental or business-type activity to be considered major, it must represent 10 percent or more of total inflows, outflows, and financial obligations for all activities of that type in any of the projection periods reported. Cash outflows for capital outlays and capital-related cash inflows from bond proceeds, capital grants, or other cash inflows restricted or committed to capital outlays would be considered major.

Finally, the Board reached a tentative agreement that the determination of which intergovernmental service interdependencies are major is a matter of professional judgment.

***The User Guide Series***

The Board provided feedback on an outline of the contents and organization of a revised draft of the GASB user guide, *An Analyst’s Guide to Government Financial Statements.* The updated guide is being combined with the separate user guide, *What* Else *You Should Know about a Government’s Finances: A Guide to Notes to the Financial Statements and Supporting Information.* The Board provided feedback regarding the planned organization of the combined guides and the substantive topics to be covered as proposed by the project staff.

***Government Combinations***

The Board considered several types of government combination arrangements that occur without the presence of financial consideration and tentatively decided on a proposed definition for the term *government consolidations.* A government consolidation is the combination of (1) two or more legally separate governments that cease to exist as legally separate entities and are combined to form one or more new governments or (2) one or more legally separate governments that are dissolved and their service activities are absorbed into one or more existing governments.

Additional consideration will be necessary to identify specific circumstances when government combinations accounting would apply to other government combination activities such as annexations, redistricting, shared service arrangements, and service “spin-off” arrangements not included in the definition of government consolidations.

The Board discussed whether a definition or specified criteria were necessary to distinguish government combination transactions from acquisitions or contributions of assets and liabilities. The Board tentatively agreed to propose that the basic principle that should guide the combination versus contribution or acquisition decision is whether governments will continue to provide services to their constituents that were provided formerly by predecessor governments.

The Board tentatively agreed to propose the use of a “carryover” method as a potential basis for measuring and reporting government consolidations, and it tentatively decided that modifications to the carryover method may be necessary because it may be applied differently for governments. A different term may be used to describe the eventual method in order to avoid confusion about how the carryover method is applied by entities that follow Financial Accounting Standards Board standards, such as in mergers of not-for-profit entities.

***Derivatives***

The Board reviewed the due process comments received on the Exposure Draft, *Derivative Instruments: Application of Hedge Accounting Termination Provisions,* and further examined the criteria for application of the provisions of the proposed standard.

Based on the feedback received on the Exposure Draft, the Board tentatively agreed that the guidance should not be limited to swap liabilities. Swap assets may meet the criteria, provided that collection of payments is probable. The Board affirmed that the criteria should be limited to circumstances in which the counterparty, or the counterparty’s credit support provider, has committed or is the subject of an act of default.

At the June teleconference, the Board reviewed the preballot draft, *Derivative Instruments: Application of Hedge Accounting Termination Provisions,* and made editorial changes. The Board tentatively decided to include additional language to clarify that the provisions set forth in the proposed standard apply to the original and succeeding swap counterparties and swap counterparties’ credit support providers.

***Reporting Balances Previously Recognized as Assets and Liabilities***

The Board continued deliberations on the reporting balances previously recognized as assets and liabilities project by reviewing the staff’s analysis of prepayments and resources received in advance of an exchange transaction. Additionally, the Board reviewed a draft Standards section of the proposed Statement and addressed additional topics including the title of the project, certain offsetting issues, and transition.

The Board deliberated whether prepayments and resources received in advance of an exchange transaction should continue to be classified as an asset or liability, should be reclassified as deferred outflows or deferred inflows of resources, or should be recognized as an outflow or inflow of resources in the current period.

The Board tentatively concluded that whether a prepayment is refundable or nonrefundable should not be the main determining factor in the classification of the balance; instead, the Board tentatively decided to propose an approach that places more emphasis on the notion of control, recognizing “refundability” as a potential manifestation of control. The Board also tentatively decided to postpone any decisions on resources received in advance of an exchange transaction to allow the project staff time to further research the revenue recognition criteria and the notion of a performance obligation that is currently being deliberated by other standards setters.

The Board tentatively decided to propose that the resulting debit or credit due to a refunding or an advance refunding, as addressed in Statements No. 23, *Accounting and Financial Reporting for Refundings of Debt Reported by Proprietary Activities,* and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements,* should be reported separately from the new debt, rather than as an offset against the balance of the new debt, on the statement of net position. Additionally, the Board tentatively concluded that transactions for both sales-type leases and direct financing leases should be excluded from the scope of this project.

Finally, the Board reviewed the draft Standards section, and provided clarifying amendments.

***Conceptual Framework—Recognition and Measurement Approaches***

The Board reviewed the revised preballot draft of the Preliminary Views, *Recognition of Elements of Financial Statements and Measurement Approaches.* The Board offered various suggestions to improve the document and requested that the staff prepare a ballot draft of the Preliminary Views for review.

***GASB Seeks Participants for Pension Field Test***

The GASB is soliciting participants for a field test it is conducting in conjunction with the issuance of its Exposure Drafts related to the pension accounting and financial reporting project. All state and local governments that provide pension benefits and plans that administer pensions for state and local governments are eligible and welcome to participate.

Field tests are a part of the GASB’s due process activities and help the GASB to establish effective standards. Participating governmental entities volunteer to go through the exercise of “implementing” the proposed standards as if they were in place and then provide feedback to the GASB regarding that process.

Those interested in participating in the pension field test should contact GASB Project Manager Michelle Czerkawski either by email at mlczerkawski@gasb.org or by telephone at (203) 956-5293.

***The GASB Report***

The GASB welcomes feedback on *The GASB Report.*

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