



2016 Governmental GAAP Update

January 27, 2016

Webinar

Presented in association with



Presented by:



Stephen W. Blann, CPA, CGFM, CGMA
Director of Governmental Audit Quality
Rehmann

Session Outline

- Newly issued standards
- Newly effective standards
- Upcoming standards
- Exposure drafts and preliminary views

Newly Issued Standards

- GASB Pronouncements issued in 2015:

No.	Title	Effective
72	Fair Value Measurement and Application	06/15/2016
73	Pensions and Related Assets Not Within the Scope of GASB 68	06/15/2016
74	Postemployment Benefit Plans Other than Pension Plans (OPEB Plans)	06/15/2017
75	Postemployment Benefits Other than Pensions (OPEB)	06/16/2018

Newly Issued Standards

- GASB Pronouncements issued in 2015:

No.	Title	Effective
76	The Hierarchy of GAAP for SLGs	06/15/2016
77	Tax Abatement Disclosures	12/15/2016
78	Pensions Provided through Certain Multiple-Employer DB Pension Plans	12/15/2016
79	Certain External Investment Pools and Pool Participants	06/15/2016

Newly Effective Standards

- GASB Pronouncements effective in 2015:

No.	Title	Effective
68	Accounting and Financial Reporting for Pensions	06/15/2015
71	Pension Transition for Contributions Made Subsequent to the Measurement Date	with GASB 68

GASB Statement 72

Fair Value Measurement and Application

- *Fair value*
 - The price that would be received to sell an asset or paid to transfer a liability in an **orderly transaction** between **market participants** at the **measurement date**.
 - Market based, rather than entity-specific
 - Represents an **exit price**, rather than an **acquisition value**

GASB Statement 72

Fair Value Measurement and Application

- *Orderly transaction*
 - A transaction that assumes exposure to the market for a period before the measurement date to allow for marketing activities that are usual and customary for transactions involving such assets or liabilities. It is not a forced transaction (for example, a forced liquidation or distress sale).

GASB Statement 72

Fair Value Measurement and Application

- *Market participants*
 - Buyers and sellers that are:
 - In the principal (or most advantageous) market
 - Independent of each other
 - Knowledgeable about the transaction
 - Able and willing to enter into a transaction (not forced or otherwise compelled to do so)

GASB Statement 72

Fair Value Measurement and Application

- *Measurement date*
 - The date as of which the fair value of an asset or liability is determined.

GASB Statement 72

Fair Value Measurement and Application

- *Exit price*
 - The price that would be received to sell an asset or paid to transfer a liability.
- *Acquisition value*
 - The price that would be paid to acquire an asset with equivalent service potential in an orderly market transaction at the acquisition date, or the amount at which a liability could be liquidated with the counterparty at the acquisition date.

GASB Statement 72

Fair Value Measurement and Application

- *Asset or Liability*
 - The focus of a fair value measurement is on a particular asset or liability.
 - Therefore, when measuring fair value, a government should take into account the characteristics of the asset or liability that market participants would consider when pricing the asset or liability at the measurement date.

GASB Statement 72

Fair Value Measurement and Application

- *Unit of Account*

- The level at which an asset or a liability is aggregated or disaggregated for measurement, recognition, or disclosure purposes.
- Single asset/liability vs. group of assets/liabilities

GASB Statement 72

Fair Value Measurement and Application

- *Markets*

- A fair value measurement assumes that a transaction to sell an asset or transfer a liability takes place in either a government's:

- **Principal market**, or
- **Most advantageous market** (in the absence of a principal market)

GASB Statement 72

Fair Value Measurement and Application

- *Principal market*
 - The market with the greatest volume and level of activity for an asset or liability.
- *Most advantageous market*
 - The market that maximizes the amount that would be received to sell an asset or minimizes the amount that would be paid to transfer a liability, after taking into account **transaction costs** and **transportation costs**.

GASB Statement 72

Fair Value Measurement and Application

- *Transaction costs*
 - The costs to sell an asset or transfer a liability in the principal (or most advantageous) market for the asset or liability that:
 - Are directly attributable to the disposal of the asset or the transfer of the liability
 - Result directly from and are essential to that transaction
 - Would not have been incurred by the entity had the decision to sell the asset or transfer the liability not been made

GASB Statement 72

Fair Value Measurement and Application

- *Transaction costs*
 - Specific to a transaction
 - Considered only to determine the most advantageous market
 - *Not* considered as an adjustment to fair value
 - Separate from **transportation costs**

GASB Statement 72

Fair Value Measurement and Application

- *Transportation costs*
 - The costs that would be incurred to transport an asset from its current location to its principal (or most advantageous) market.
 - If location is a characteristic of the asset, the price in the principal (or most advantageous) market should be adjusted for the costs, if any, that would be incurred to transport the asset from its current location to that market.

CPE Prompt 1 of 4

- The focus of *fair value* is on
 - A. What it initially cost to acquire an asset
 - B. What it would cost to replace an asset
 - C. What an asset would sell for
 - D. What an asset is worth to the government

GASB Statement 72

Fair Value Measurement and Application

- *Valuation techniques*
 - A specific method or combination of methods used to determine the fair value of an asset or liability
 - Based on the use of **inputs**

GASB Statement 72

Fair Value Measurement and Application

- *Inputs*

- The assumptions that market participants would use when pricing an asset or liability, including:
 - The risk inherent in a particular valuation technique used to measure fair value
 - The risk inherent in the inputs to the valuation technique.
- Inputs may be **observable** or **unobservable**.

GASB Statement 72

Fair Value Measurement and Application

- *Observable inputs*
 - Inputs that are developed using market data, such as publicly available information about actual events or transactions, and which reflect the assumptions that market participants would use when pricing an asset or liability.

GASB Statement 72

Fair Value Measurement and Application

- *Unobservable inputs*
 - Inputs for which market data are not available and that are developed using the best information available about the assumptions that market participants would use when pricing an asset or liability.

GASB Statement 72

Fair Value Measurement and Application

- Valuation techniques should
 - Maximize the use of observable inputs
 - Minimize the use of unobservable inputs
 - Select inputs that are consistent with the characteristics of the asset or liability that market participants would take into account in a transaction for the asset or liability

GASB Statement 72

Fair Value Measurement and Application

- *Valuation approaches*
 - A government should use valuation techniques consistent with one or more of three approaches to measuring fair value:
 - Market approach
 - Cost approach
 - Income approach

GASB Statement 72

Fair Value Measurement and Application

- *Market approach*
 - A valuation technique that uses prices and other relevant information generated by market transactions involving identical or comparable (similar) assets, liabilities, or groups of assets and liabilities.

GASB Statement 72

Fair Value Measurement and Application

- *Cost approach*

- A valuation technique that reflects the amount that would be required currently to replace the service capacity of an asset (often referred to as current replacement cost).

GASB Statement 72

Fair Value Measurement and Application

- *Income approach*
 - A valuation technique that converts future amounts (e.g., cash flows or income and expenses) to a single current (discounted) amount.

GASB Statement 72

Fair Value Measurement and Application

- Consistent application
 - Should generally apply the same valuation techniques from period to period, unless:
 - New markets develop
 - New information becomes available
 - Information previously used is no longer available
 - Valuation techniques improve
 - Market conditions change

GASB Statement 72

Fair Value Measurement and Application

- Fair Value Hierarchy
 - **Level 1 inputs** are quoted prices (unadjusted) for identical assets or liabilities in active markets that a government can access at the measurement date.
 - **Level 2 inputs** are all other observable inputs not included within Level 1
 - **Level 3 inputs** are unobservable inputs for an asset or liability.

GASB Statement 72

Fair Value Measurement and Application

- Developing level 3 inputs
 - Use the best information available under the circumstances
 - May begin with the government’s own data, as adjusted for risk and unique circumstances
 - “Unobservable inputs developed in [this] manner... are considered market participant assumptions and meet the objective of a fair value measurement.” [GASB 72 para. 43]

GASB Statement 72

Fair Value Measurement and Application

- Fair value considerations
 - Significant decreases to the volume or level of market activity
 - Transactions that are not orderly
 - Quoted prices from third parties

GASB Statement 72

Fair Value Measurement and Application

- Measurement principles
 - Highest and best use of nonfinancial assets
 - Physically possible
 - Legally permissible
 - Financially feasible
 - Determined from the perspective of market participants using relevant market data as of the measurement date

GASB Statement 72

Fair Value Measurement and Application

- Application of fair value to investments
 - **Investments** should generally be reported at fair value
 - Exceptions (reported at cost or amortized cost):
 - Non-participating interest-earning investment contracts
 - Money market and participating interest-earning investment contracts with a remaining maturity at the time of purchase of less than one year
 - Investments in 2a7-like external investment pools

GASB Statement 72

Fair Value Measurement and Application

- *Investment*
 - A security or other asset that:
 - Is **held primarily for income or profit** and
 - Has a **present service capacity** based solely on its ability to generate cash or to be sold to generate cash.
 - Determined at acquisition, and not changed

GASB Statement 72

Fair Value Measurement and Application

- *Held primarily for income or profit*
 - A government acquires an investment with the expectation of future income or profit. Evidence that a government holds an asset for income or profit also may be found in the fund that reports the asset. For example, income producing real property in a pension plan suggests that the asset is held primarily for income or profit.

GASB Statement 72

Fair Value Measurement and Application

- *Present service capacity*
 - Refers to a government's mission to provide services. While capital assets provide services directly, investments do not. Rather, investments are valuable to a government because investments can be used to pay for goods or services that in turn are used to provide services directly to its citizens.

CPE Prompt 2 of 4

- Level 1, 2, and 3 inputs reflect:
 - A. The relative risk/safety of an investment
 - B. The degree to which fair value is based on observable/unobservable inputs
 - C. The credit rating of investments
 - D. Whether investments are held by third parties or by the government itself

GASB Statement 72

Fair Value Measurement and Application

- *Net Asset Value per share (NAV)*
 - A government is permitted to establish the fair value of an investment in a nongovernmental entity that does not have a readily determinable fair value by using the NAV per share (or its equivalent), such as member units or an ownership interest in partners' capital to which a proportionate share of net assets is attributed.

GASB Statement 72

Fair Value Measurement and Application

- *Net Asset Value per share (NAV)*
 - Generally consistent with FASB requirements for investment companies.
 - Should be adjusted if, at the measurement date, it is probable that the government will sell the investment for a different amount

GASB Statement 72

Fair Value Measurement and Application

- Disclosures
 - Organized by type of asset or liability
 - Fair value measurement at the end of the reporting period
 - The level of the fair value hierarchy (1, 2, or 3)
 - Description of the valuation techniques used
 - Any significant changes from the prior year
 - Additional disclosures for investments at NAV

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- GASB 67/68 apply only to pensions administered through **trusts**
 - Contributions/earnings are irrevocable
 - Plan assets are dedicated to providing pensions (benefits) to plan members
 - Plan assets are legally protected from creditors
- Other pensions were instructed to continue following existing GAAP (GASB 25/27)

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- GASB considered non-trusted pension separately, and determined:
 - They have the same objective as other (more traditional) pensions
 - The only real difference is absence of **fiduciary net position**

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- *Fiduciary net position:*
 - The residual equity in a pension trust fund
 - Assets (cash, investments, and limited A/R)
 - Liabilities (generally short-term)
 - Deferred inflows/outflows (hedged investments)
 - No liability for the actuarial value of benefits to be paid (instead reported as net position held for pension benefits)

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- GASB considered non-trusted pension separately, and determined:
 - Apply the requirements of GASB 67/68
 - No netting (record *total pension liability* instead of *net pension liability*)
 - Use a discount rate consistent with an unfunded plan (AA 20 year muni bond rate)

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- Treatment of assets:
 - Single employer plan
 - Report as employer assets
 - Multiple-employer plan
 - Report proportionate share of total as employer assets
 - Pension plans
 - Report resources held in an agency fund

GASB Statement 73

Pensions Not Within the Scope of GASB 68

- Technical amendments to GASB 67/68:
 - Notes to RSI about investment factors that significantly affect trends are limited to factors controlled by the government (e.g., changes in investment policies) rather than general market conditions
 - Separately financed specific liabilities
 - Revenue recognition for outside support

GASB Statement 74/75

Other Postemployment Benefits (OPEB)

- GASB 74
 - Applies to the financial statements of **OPEB plans** (trust funds)
 - Effective 06/30/2017
- GASB 75
 - Applies to the financial statements of **employers** providing OPEB
 - Effective 06/30/2018

GASB Statement 74/75

Defining Pension & OPEB

- Pensions
 - Retirement income and benefits (other than healthcare) provided through a pension plan

GASB Statement 74/75

Defining Pension & OPEB

- Other postemployment benefits (OPEB)
 - All postemployment healthcare benefits
 - Medical, dental, vision, hearing, etc.
 - Regardless of whether provided by a pension plan
 - Postemployment benefits other than retirement income not administered by a pension plan
 - Death benefits, life insurance, disability, long-term care
 - Excludes **termination benefits**

GASB Statement 74/75

Defining Pension & OPEB

- *Termination benefits* (GASB 47):
 - An inducement to hasten the termination of services (e.g., early retirement incentives)
 - May be voluntary or involuntary
 - Requires professional judgment to determine employer's intent and employee's understanding
 - Recorded at the NPV of the benefits to be paid when the agreement is made (*not* OPEB)

GASB Statement 74/75

Defining Pension & OPEB

- GASB has determined that OPEB plans are conceptually similar to pensions, and has largely replicated the guidance from GASB 67/68 in GASB 74/75
 - Retains requirement for actuaries to consider the **implicit rate subsidy**
 - Retains the option for small plans to use the **alternative measurement method**

GASB Statement 74/75

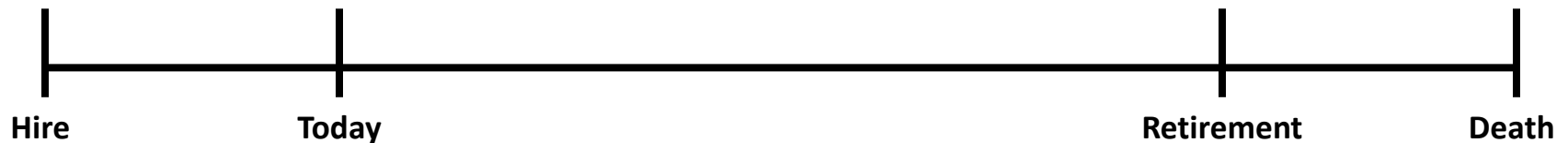
Net OPEB Liability

- Recorded by the employer (not the plan)
- Equal to the actuarially determined **total OPEB liability**, less the **net position** of the OPEB trust fund
- Recorded in full accrual financial statements (certain portions are offset by deferred inflows/outflows and amortized)

GASB Statement 74/75

Total OPEB Liability

- Calculated by the actuary:
 - Project future benefits
 - Discount to present value
 - Attribute present value to specific periods



GASB Statement 74/75

Total OPEB Liability

- Calculated by the actuary:
 - Project future benefits
 - Discount to present value
 - Attribute present value to specific periods



GASB Statement 74/75

Total OPEB Liability

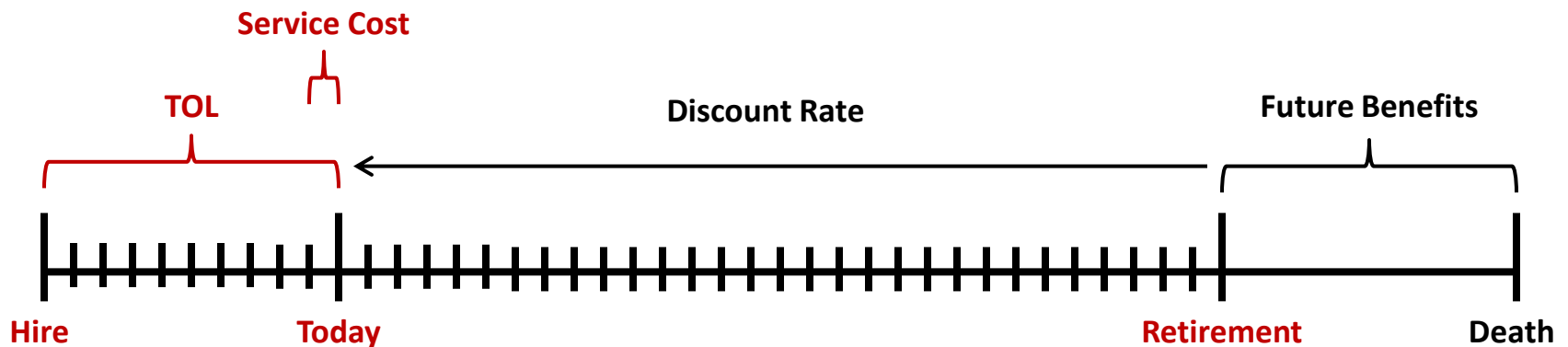
- Calculated by the actuary:
 - Project future benefits
 - Discount to present value
 - Attribute present value to specific periods



GASB Statement 74/75

Total OPEB Liability

- Calculated by the actuary:
 - Project future benefits
 - Discount to present value
 - Attribute present value to specific periods



CPE Prompt 3 of 4

- The Net OPEB Liability is:
 - A. The actuarial value of future benefits to be paid
 - B. The cumulative shortfall between the annual required contribution and actual contributions
 - C. The amount due for benefits owed at year end
 - D. The Total OPEB Liability, less any fiduciary net position of an OPEB trust fund

GASB Statement 74/75

Key Actuarial Changes

- Actuarial cost method
 - Entry Age, Level Percent of Pay
 - Project future benefits using age-adjusted premiums (implicit rate subsidy)
- Small plans (fewer than 100 members) may use the alternative measurement method that does not require an actuary

GASB Statement 74/75

Key Actuarial Changes

- Expected return/discount rate
 - Single blended rate comprised of:
 - Expected rate of return (years w/ sufficient assets)
 - AA 20 year muni bond rate (years w/ insufficient assets)
 - A lower discount rate produces a higher liability and vice versa

GASB Statement 74/75

Key Actuarial Changes

- Expected return/discount rate
 - Example:

	Target Allocation	Long-term Expected Real Rate of Return	Money Weighted Rate of Return
Domestic equity	46%	5.4%	2.48%
International equity	21%	5.5%	1.16%
Fixed income	26%	1.3%	0.34%
Real estate	6%	4.5%	0.27%
Cash	1%	0.0%	0.00%
	<u>100%</u>		<u>4.25%</u>
Inflation			<u>3.50%</u>
Investment rate of return			<u>7.75%</u>

GASB Statement 74/75

Key Actuarial Changes

- Annual Cost
 - GASB 45 required calculation of a “Annual Required Contribution (ARC)” equal to the service cost plus amortization of the unfunded actuarial liability
 - GASB 75 requires calculation of OPEB Expense equal to the benefits earned during the period with adjustments for deferred recognition of some gains/losses

GASB Statement 74/75

Key Actuarial Changes

- Asset method
 - GASB 45 permitted an actuarial asset method that smoothed gains and losses
 - GASB 75 requires market value of assets

GASB Statement 74/75

Key Actuarial Changes

- Amortization of unfunded liability
 - GASB 45 permitted wide latitude in amortization periods
 - GASB 75 requires:
 - Plan changes – immediately
 - Assets returns other than expected – 5 years
 - Other actuarial liability gains and losses – average future service

GASB Statement 74/75

Key Actuarial Changes

- Sensitivity analyses
 - Changes in the discount rate

	<u>1% Decrease (6.0%)</u>	<u>Discount Rate (7.0%)</u>	<u>1% Increase (8.0%)</u>
Net OPEB liability (asset)	\$ 64,687	\$ 6,366	\$ (41,620)

- Changes in the healthcare cost trend rate

	<u>1% Decrease (8.5% decreasing to 4.5%)</u>	<u>Healthcare Cost Trend Rates (9.5% decreasing to 5.5%)</u>	<u>1% Increase (10.5% decreasing to 6.5%)</u>
Net OPEB liability (asset)	\$ (61,284)	\$ 6,336	\$ 88,512

GASB Statement 76

The Hierarchy of GAAP for SLGs

- Simplifies the sources of authoritative GAAP for state and local governments
 - Category A (primary)
 - Category B (secondary)
- Provided guidelines for evaluating non-authoritative sources

GASB Statement 76

The Hierarchy of GAAP for SLGs

- Category A (*GASB approval*)
 - GASB Statements
- Category B (*GASB clearance*)
 - GASB Technical Bulletins*
 - GASB Implementation Guides
 - AICPA literature cleared by the GASB
- *Included in the GASB Codification*

GASB Statement 76

The Hierarchy of GAAP for SLGs

- Non-authoritative sources
 - GASB Concepts Statements*
 - FASB and international standards
 - AICPA literature not cleared by the GASB
 - Literature of other professional associations
 - Textbooks, articles, etc.

GASB Statement 77

Tax Abatement Disclosures

- Effective 12/15/2016
 - State and local governments employ a variety of programs and policies that reduce the taxes an individual or entity otherwise would owe, with the intent of encouraging those individuals or entities to engage in certain behaviors
 - GASB 77 provides “essential information about the nature and magnitude of the reduction in tax revenues through tax abatement programs”

GASB Statement 77

Tax Abatement Disclosures

- *Tax expenditures*
 - Governmental programs employed to lower the taxes of broad classes of taxpayers, or the taxes of individuals or entities based on the performance of specific actions
 - Includes tax exemptions, tax deductions, and **tax abatements**
 - Based on the substance of an agreement, not its title or legal form

GASB Statement 77

Tax Abatement Disclosures

- *Tax abatements*
 - A reduction in tax revenues that results from an agreement between one or more governments and an individual or entity in which (a) one or more governments promise to forgo tax revenues to which they are otherwise entitled and (b) the individual or entity promises to take a specific action after the agreement has been entered into that contributes to economic development or otherwise benefits the governments or the citizens of those governments

GASB Statement 77

Tax Abatement Disclosures

- Disclosure principles:
 - Distinguish between
 - Agreements that are entered into by the reporting government
 - Agreements that are entered into by other governments and that reduce the reporting government's tax revenues

GASB Statement 77

Tax Abatement Disclosures

- Disclosure principles:
 - Tax abatements may be disclosed individually or be aggregated:
 - By major tax abatement program (own agreements)
 - By government (agreements of others)
 - Disclosures should be made from the date of agreement until its expiration

GASB Statement 77

Tax Abatement Disclosures

- Disclosure requirements:
 - Only disclose individual details for agreements that exceed a quantitative threshold set by the government
 - Brief description of the abatement (name of program, purpose, type of taxes abated, authority for program, criteria for eligibility, methods of abatement, terms for recapture if conditions unmet, commitments made by recipient)

GASB Statement 77

Tax Abatement Disclosures

- Disclosure requirements:
 - Gross amount that tax revenues were reduced by the abatement
 - Any amounts received/receivable from another government (name, authority, amount)
 - Commitments made by the government
 - The quantitative threshold used for individual disclosures

GASB Statement 77

Tax Abatement Disclosures

- Disclosure requirements:
 - If legally prohibited from disclosing details of certain agreements, a general description of what is omitted and why

GASB Statement 77

Tax Abatement Disclosures

- Discretely presented component units:
 - If agreement is “essential to fair presentation” then treat as government’s own program
 - Otherwise, treat as a program of another government

CPE Prompt 4 of 4

- Tax abatement disclosures are:
 - A. Only required to be made for agreements over a specified quantitative threshold
 - B. Only required to be made for a government's own programs
 - C. Only required to be made in the year a government initially enters into an agreement
 - D. None of the above

GASB Statement 78

Certain Multiple-Employer DB Pension Plans

- Amendment to GASB 68
 - Excludes cost-sharing pensions that:
 - Are not a state or local governmental pension plan
 - Are used by both governmental and non-governmental employees
 - Have no predominant governmental employer
 - Effective 12/15/2016

GASB Statement 78

Certain Multiple-Employer DB Pension Plans

- Accounting is essentially like a defined contribution plan
 - Expense = required contributions for the period
 - Liability = current contributions due at year end
 - Notes = plan description and contributions made
 - RSI = 10 years of required contributions

GASB Statement 79

Certain External Investment Pools

- Brings the guidance for 2a7-like investment pools within the GASB literature
 - SEC rule 2a7 was amended in 2014
 - No substantive change to current practice for governments
 - Effective 06/15/2016 (portions deferred to 12/15/2016)

GASB Statement 79

Certain External Investment Pools

- In general, investments should be carried at fair value
 - Exception made for short-term money market funds (2a7-like) carried at amortized cost, which is expected to approximate market
 - Use of fair value is always permitted
 - Once fair value is elected, you cannot later change back to amortized cost

GASB Statement 79

Certain External Investment Pools

- To qualify for amortized cost, an external investment pool must:
 - Have a stable net asset value (NAV) per share
 - Meet certain minimum requirements regarding: maturity, quality, diversification, liquidity, and shadow price
 - If noncompliant, switch to using fair value

Upcoming Standards

- GASB Pronouncements expected in 2016:
 - Blending Requirements for Certain CUs
 - Irrevocable Split-Interest Agreements
 - Pension Issues
 - Asset Retirement Obligations
 - Fiduciary Activities
 - Leases

Blending Requirements for Certain CUs

- Summary
 - Allows for certain government “owned” not-for-profit corporations to be blended if they function essentially as a part of the government
- Final standard expected 1Q16

Irrevocable Split-Interest Agreements

- Summary
 - Accounting for donations (largely to foundations) of charitable remainder trusts, annuity gifts, and life interests in real estate
 - Report a beneficial interest if under the control of the government with a present service capacity
- Final standard expected 1Q16

Pension Issues

- Summary
 - Various technical corrections
 - Pensionable wages vs. total wages in RSI
- Final standard expected 1Q16

Asset Retirement Obligations

- Summary
 - Addresses legal obligations associated with retiring (abandoning, selling, etc.) a capital asset
 - Excludes landfills and pollution remediation (covered by GASBs 18 and 49)
- Final standard expected 4Q16

Fiduciary Activities

- Summary
 - Redefines “control” in a fiduciary capacity
 - Distinguishes between trust agreements and “custodial” funds (replaces “agency” funds)
- Final standard expected 4Q16

Leases

- Summary
 - Addresses contracts that convey a legal right to use a nonfinancial asset for a period of time in an exchange or exchange-like transaction
 - Differs somewhat from parallel FASB project
 - Record intangible asset and related liability
- Final standard expected 4Q16

Looking Further Ahead

- Other GASB projects:
 - Certain Debt Extinguishments Using Existing Resources (ED 3Q16)
 - Conceptual Framework: Recognition (PV 2Q18)
 - Financial Reporting Model (PV 4Q16/2Q18)

Questions?



For more information...



CPAs & Consultants • Wealth Advisors • Corporate Investigation



Stephen W. Blann, CPA, CGFM, CGMA
Director of Governmental Audit Quality
Rehmann

stephen.blann@rehmann.com

www.rehmann.com/government