



August 31, 2004

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Project No. 3-16
Governmental Accounting Standards Board
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*Advancing
Government
Accountability*

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Dear Mr. Bean:

On behalf of the Association of Government Accountants (AGA), the Financial Management Standards Board (FMSB) appreciates the opportunity to provide comments on the Exposure Draft (ED) of the Governmental Accounting Standards Board's (GASB or the Board) Proposed Statement on *Net Assets Restricted by Enabling Legislation, an Amendment of GASB Statements No. 34 and No. 44*.

The FMSB, comprising 21 members with accounting and auditing backgrounds in federal, state, and local government, academia, and public accounting, reviews and responds to proposed standards and regulations of interest to AGA members. Local AGA chapters and individual members are also encouraged to comment separately.

The members of the FMSB have reviewed the proposed statement and we are generally supportive of the Board's proposals. We are also mindful of the Board's concurrent deliberations on fund balance reporting and suggest that if the concept of legally enforced restrictions on net assets impacts the decision on whether fund balance should be reserved, that the Board consider rejoining the guidance on net assets with guidance on fund balance reporting before issuing a final Statement. We offer the following comments and recommendations on the exposure draft.

Issue 1

Paragraphs 4 and 5 of this proposed Statement are intended to assist governments in applying the phrase "legally enforceable" to restrictions on net assets imposed by enabling legislation and to provide users with comparable information on these restrictions. Do you believe the proposals will be helpful to governments and users? If not, how would you suggest clarifying or improving them?

We would consider the additional language provided by paragraphs 4 and 5 as useful to preparers and auditors when deciding what should be considered legally enforceable. We also find the guidance in paragraph 5 and the Illustrations in Appendix C as helpful when dealing with legal changes to the restrictions and when the restrictions are deemed unenforceable.

We agree with the Board's position that the determination of legal enforceability should remain a matter of professional judgment. We also agree that requiring disclosure of a government's policy for determining whether its restrictions are legally enforceable would not improve the comparability or usefulness of net asset information.



Issue 2

Paragraph 5 would require that net assets restricted by enabling legislation be displayed on the government-wide statement of net assets separately from other restricted net assets. Do you think this will improve the usefulness and transparency of net assets information? Why or why not?

We would not consider the benefits of additional classification of restricted net assets on the face of the government-wide Statement of Net Assets as sufficient to warrant segregation of legally enforceable restricted net assets from external and constitutional restricted net assets. We suggest the Board consider requiring note disclosure of legally enforceable restricted net assets and agree with the Board in requiring the additional classification in the Statistical section. We also suggest the Board consider requiring note disclosure and inclusion in the Management's Discussion and Analysis (MD&A) when material changes occur in the legal enforceability of restrictions for major funds. The Board could consider including such a discussion in the basis for conclusion and include a question and answer in the next comprehensive implementation guide addressing the requirements and how such disclosures would be made.

Other Comments and Recommendations

1. Although in general the FMSB agrees with the intent of the proposed amendment, which is to clarify the definition, several members are uncertain as to the benefits of disclosure. They think that a disclosure requirement should not be instituted unless there is a clear benefit to users. Practice is not consistent and preparers are not clear about what "enabling legislation" means. They cite the results of the survey mentioned in the Statement and question how representative a response rate of 8% for users and 9% for preparers can be. Such response rates would not seem to represent a resounding mandate, unless some responders are major users.

In their opinion, this proposal will not alleviate the Board's concern of incompatibility among government CAFRs, because it does not affect a government official's original understanding or application of the enabling legislation criterion applied to restricted net assets. Many of the potential problems are government specific in that they are related to the way a particular government does business.

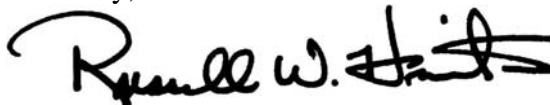
2. Almost half of the members agreed with displaying net assets restricted by enabling legislation separately from other restricted net assets on the financial statements and in the statistical section. They thought that it places more emphasis on the use of funds and the audit of those assets restricted by enabling legislation, and provides a helpful snapshot for users. However, they thought that, if the Board were to decide on separate disclosure on the face of the statement, this would result in the only two other means by which restrictions are imposed on net assets continuing to be combined. They recommend that the Board consider also separating the display of the remaining two means, external restrictions and constitutional provisions, on the financial statements, since users would find this information as useful.

3. One member believes that the criteria to be applied in determining enabling legislation will, at least in the state in which one member resides, severely restrict or eliminate restricted assets arising from enabling legislation. The Legislature has shown a marked ability to enact legislative language which diverts resources to other than the original statutory purpose without allowing external parties a means to compel adherence to the original statutory purpose. Once this ability has been used, it would be difficult to contend that any legislative restrictions would provide the protection envisioned in the ED's criteria for enabling legislation. This however, may well be realistic and appropriate.

4. The proposed definition would limit restrictions based on enabling legislation to when enforcement could be made by someone. Auditors may question this and seek to obtain independent verification through a separate legal opinion. In addition, from a local government's point of view, enabling legislation is only their own; legislation by the state (such as the motor fuel tax in Illinois) that applies to local governments would presumably be a part of the "external" category. Would that be subject to the same verification process?
5. The proposed ED is unclear as to the extent of the detail required to be displayed in the financial statements for net assets restricted by enabling legislation. However, nonauthoritative Illustration 1 shows specific purposes for restricted net assets on the face of the financial statements. The Board should explicitly state whether each specific purpose of enabling legislation is to be displayed on the face of the financial statements or whether it is permissible to display the aggregate net assets restricted by enabling legislation on the face of the financial statements with appropriate detailed disclosure in the footnotes.
6. Illustration 3 assumes the new enabling legislation did not redirect any balance remaining from the prior enabling legislation for the new purpose. Since, in practice, new enabling legislation may redirect the purpose of any balance remaining from the prior enabling legislation, we believe there should be an explicit statement that the purpose was not redirected. Alternatively, the differing results arising from a redirection of the remaining balance could also be shown, with appropriate explanation.
7. Illustration 5 and paragraph 5 acknowledge governments sometimes use restricted assets for other than their intended purposes and prescribe appropriate financial statement reporting for those circumstances. We believe the Board should consider including a statement that such circumstances require consideration of reporting a violation of a material finance-related legal provision.
8. Detailed explanation as to any restricted assets should also be in the accompanying MD&A (if it meets the criteria for disclosure set forth in GASB 34), as non-financial users will likely find that more understandable and useful than the financial statements.
9. The footnote pertaining to legal enforceability described in paragraph 4 on page 2 of the proposed Statement is ambiguous and does not add any additional value.

The FMSB appreciates the opportunity to comment on the ED. This response letter represents a consensus of the views of the FMSB members. We would be pleased to discuss this letter with you at your convenience. You can contact me at hintonrw@audits.state.ga.us or (404) 656-2174 or Anna D. Gowans Miller, CPA, AGA's Technical Manager and facilitator for this project, at amiller@agacgfm.org or (703) 684-6931, ext. 203.

Sincerely,



Russell W. Hinton, CGFM, Chair,
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C. Bobby A. Derrick, CGFM
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**Association of Government Accountants
Financial Management Standards Board**

July 2004 – June 2005

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