

GASB Update

Hawaii AGA

GASB Update

The views expressed in this presentation are those of Mr. Bean.
Official positions of the GASB are reached only after extensive due process and deliberations.

Effective Dates—June 30, 2018

- Statement 75— *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions* (OPEB—Employers)
- Statement 81— *Irrevocable Split-Interest Agreements*
- Statement 85— *Omnibus* (primarily OPEB—bring in line with Statements 78 and 82)
- Statement 86— *Certain Debt Extinguishment Issues*
- Implementation Guide—2017-1, *Implementation Guidance Update—2017*
- Implementation Guide—2017-2, *OPEB Plan Implementation Guide*
- Implementation Guide—2017-3, *OPEB Employer Implementation Guide*

Effective Date—June 30

- **2019**

- Statement 83—*Certain Asset Retirement Obligations*
- Statement 88—*Certain Debt Disclosures, including Direct Borrowing*

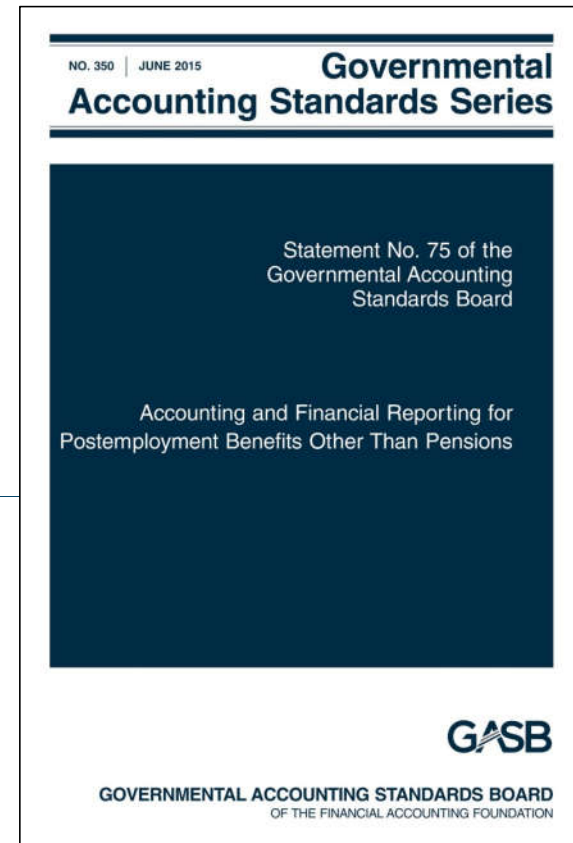
- **2020**—Statement 84—*Fiduciary Activities*

- **2021**

- Statement 87—*Leases*
- Statement 89—*Accounting for Interest Cost Incurred before the End of a Construction Period*
- Statement 90—*Majority Equity Interest*



Other Postemployment Benefits— Employer: Statement 75



What Is the Fundamental Approach Employed in Statement 75?

- Fundamental approach for OPEB is the same as required for pensions in Statement 68
 - Viewed in the context of an ongoing, career-long employment relationship
 - Focus on the cost to taxpayers over time of providing government services
 - Accounting-based versus funding-based approach to measurement

What Is Reported in Financial Statements?

- Government-wide and other accrual-basis statements
 - Net OPEB liability and deferrals, in the statement of net position
 - However, total OPEB liability if no assets have been set aside in a trust that meets specified criteria
 - OPEB expense allocated among programs and functions, in the statement of activities (total expense disclosed in notes)

- Governmental funds
 - Payable to OPEB plan for contributions/payments normally due and payable but not made prior to FYE, in the balance sheet
 - OPEB expenditure equal to contributions/payments normally due and payable, in statement of revenues, expenditures, and changes in fund balance

Descriptive Information

Members by type

Inactive employees or beneficiaries currently receiving benefit payments	1,307
Inactive employees entitled to but not yet receiving benefit payments	142
Active employees	<u>8,356</u>
	<u>9,805</u>

Assumptions used to measure the liability

Inflation	3.0 percent
Salary increases	3.25 percent, average, including inflation
Investment rate of return	7.0 percent, net of OPEB plan investment expense, including inflation
Healthcare cost trend rates	9.5 percent for 2019, decreasing 0.5 percent per year to an ultimate rate of 5.5 percent for 2029 and later

<u>Asset Class</u>	<u>Target Allocation</u>	<u>Long-Term Expected Real Rate of Return</u>
Domestic equity	40%	5.8%
Fixed income	35	1.0
Private equity	20	6.0
Real estate	3	5.9
Cash	2	0.0
Total	<u>100%</u>	

Changes in the NOL

	Increase (Decrease)		
	Total OPEB Liability (a)	Plan Fiduciary Net Position (b)	Net OPEB Liability/(Asset) (c) = (a) - (b)
Balance at June 30, 2016	\$ 122,536,000	\$ 23,238,000	\$ 99,298,000
Changes Recognized for the Measurement Period:			
Service Cost	2,528,000	-	2,528,000
Interest on the total OPEB liability	8,560,000	-	8,560,000
Changes of benefit terms	-	-	-
Difference between expected and actual experience	(436,000)	-	(436,000)
Changes of assumptions	-	-	-
Contributions from the employer	-	11,037,000	(11,037,000)
Net investment income	-	3,037,000	(3,037,000)
Administrative expenses	-	(15,000)	15,000
Benefit payments	(5,673,000)	(5,673,000)	-
Net Changes during July 1, 2016 to June 30, 2017	\$ 4,979,000	\$ 8,386,000	\$ (3,407,000)
Balance at June 30, 2017 (Measurement Date)	\$ 127,515,000	\$ 31,624,000	\$ 95,891,000



Sensitivity Analysis

Plan's Net OPEB Liability/(Asset)		
Discount Rate - 1% (6.00%)	Current Discount Rate (7.00%)	Discount Rate + 1% (8.00%)
\$ 112,777,000	\$ 95,891,000	\$ 82,033,000

Plan's Net OPEB Liability/(Asset)		
Discount Rate - 1% (6.2% decreasing to 4.0%)	Healthcare Cost Tread Rates (7.2% decreasing to 5.0%)	Discount Rate + 1% (8.2% decreasing to 6.0%)
\$ 78,869,000	\$ 95,891,000	\$ 116,898,000

Deferrals

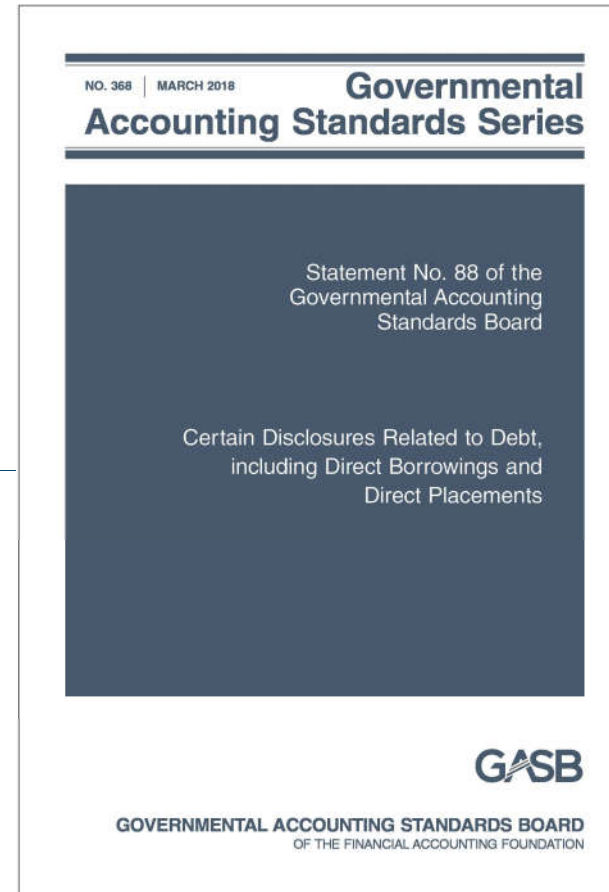
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between expected and actual experience	\$ 25,970	\$ 14,134
Changes of assumptions	-	855
Net difference between projected and actual earnings on OPEB plan investments	17,782	-
Total	<u>\$ 43,752</u>	<u>\$ 14,989</u>

Amounts reported as deferred inflows of resources and deferred outflows of resources will be recognized in OPEB expense over an additional 5–7 years, as follows:

Year ended June 30:

2019	\$ 7,064
2020	7,384
2021	6,007
2022	4,482
2023	114
Thereafter	3,712

Debt Disclosures



What Is the Definition of Debt?

- For purposes of disclosure in notes to financial statements, debt is defined as:
 - A liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established.
 - For disclosure purposes, debt does not include leases, except those contracts reported as a financed purchase of the underlying asset, or accounts payable.
 - For purposes of this determination, interest to be accrued and subsequently paid (such as interest on variable-rate debt) or interest to be added to the principal amount of the obligation (such as interest on capital appreciation bonds) does not preclude the amount to be settled from being considered fixed at the date the contractual obligation is established.

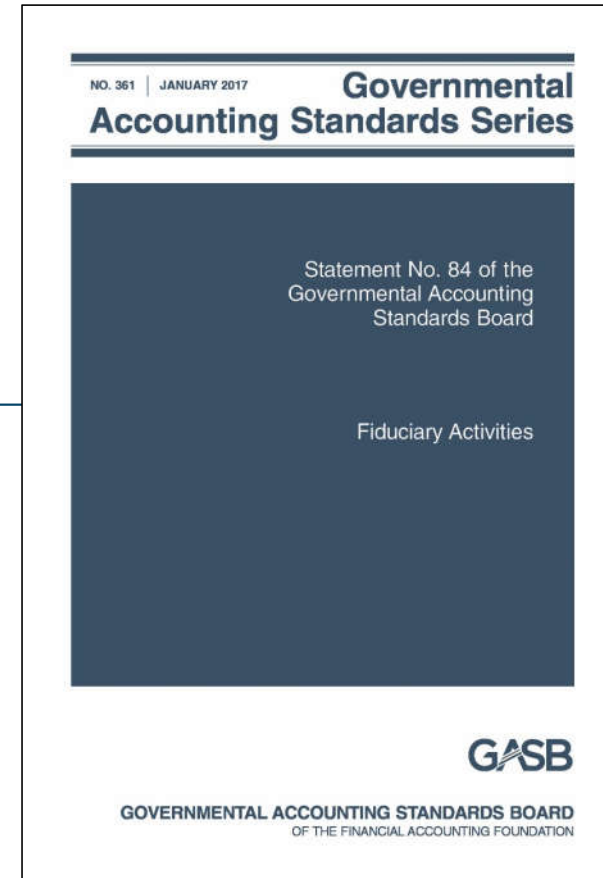
What New Note Disclosures Are Required by Statement 88?

- Summarized information about the following items:
 - Amount of unused lines of credit
 - Not limited to lines of credit associated with debt
 - Assets pledged as collateral for debt
 - Does not include assets constructed with the related debt proceeds
 - Terms specified in debt agreements related to significant:
 - Events of default with finance-related consequences
 - Termination events with finance-related consequences
 - Subjective acceleration clauses.
- Separate information in debt disclosures regarding (a) direct borrowings and direct placements of debt from (b) other debt

What Are Some Implementation Tips?

- Classify liabilities as debt/non-debt and review with auditor
- Establish mechanism to identify all lines of credit and pledged assets
- Review debt arrangement for specific terms
- Identify direct borrowings and direct placements (if any)

Fiduciary Activities: Statement 84

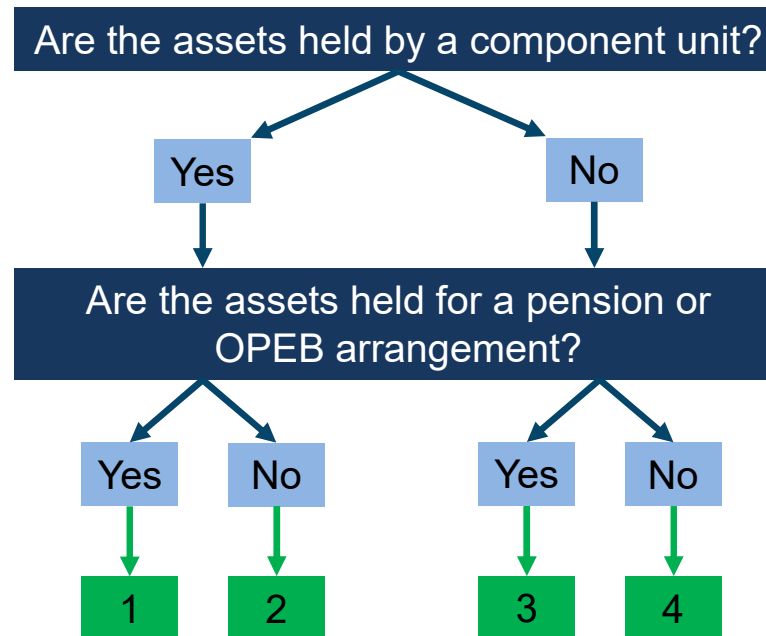


What Are Some Implementation Tips?

- Determine classification and fund category no later than 2018
- Determine how to capture inflow and outflow information for activities previously reported as agency funds
- Watch for implementation guide—December 2018 Exposure Draft

When Should a Government Report Assets in a Fiduciary Fund?

Four paths to making this determination:



How Can A Component Unit be a Fiduciary Activity?

- The activity needs to meet the definition of a component unit
 - Legally separate
 - Trusts generally are legally separate
 - Appointment of a majority of the governing body
 - What if there is no governing body?
 - Imposition of will or financial benefit or burden
 - Contributions to a pension or OPEB plan is a financial burden
 - Misleading to exclude

All Other Activities Are Fiduciary if...

All three of the following are met:

- The government **controls** the assets
- Those assets are *not* derived either:
 - Solely from the government's own-source revenues, or
 - From government-mandated nonexchange transactions or voluntary nonexchange transactions with the exception of pass-through grants and for which the government does not have administrative or direct financial involvement

When Is a Government Controlling Assets?

- A government controls the assets of an activity if:
 - The government *holds* the assets.
 - The government has the ability to *direct* the use, exchange, or employment of the assets in a manner that provides benefits to the specified or intended beneficiaries.

What Are Own-Source Revenues?

- Revenues that are generated by a government itself
 - Exchange and exchange-like revenues (investment income that can be used for activities of the government)
 - Nonexchange revenues
 - Derived tax revenues (sales and income taxes)
 - Imposed nonexchange revenues (property taxes)



Third Criterion—One of the Following Three

- The assets are
 - Administered through a trust agreement or equivalent arrangement in which the government itself is not a beneficiary,
 - Dedicated to providing benefits to recipients in accordance with the benefit terms, and
 - Legally protected from the creditors of the government.
- The assets are for the benefit of individuals and the government does not have administrative involvement with the assets or direct financial involvement with the assets. In addition, the assets are not derived from the government's provision of goods or services to those individuals.
- The assets are for the benefit of organizations or other governments that are not part of the financial reporting entity. In addition, the assets are not derived from the government's provision of goods or services to those organizations or other governments.

When Does a Government Have Administrative Involvement or Direct Financial Involvement?

■ Examples of administrative involvement

- If it monitors compliance with the requirements of the activity that are established by the government or by a resource provider that does not receive the direct benefits of the activity
- If it determines eligible expenditures that are established by the government or by a resource provider that does not receive the direct benefits of the activity
- If it has the ability to exercise discretion in how assets are allocated

■ Example of direct financial involvement

- If it provides matching resources for the activities

Reporting Fiduciary Activities—Fiduciary Funds

- Definitions for pension trust funds, investment trust funds, and private-purpose trust funds that focus on the resources that should be reported within each.
 - Trust agreement or equivalent arrangement should be present for an activity to be reported in a trust fund.
- Custodial funds would report fiduciary activities for which there is no trust agreement or equivalent arrangement.
 - External portions of investment pools that are not held in trust should be reported in a separate column under the custodial fund umbrella



Liability Recognition

- A government should recognize a liability to the beneficiaries in a fiduciary fund when an event has occurred that compels the government to disburse fiduciary resources
 - Events that compel a government to disburse fiduciary resources occur when a demand for the resources has been made or when no further action, approval, or condition is required to be taken or met by the beneficiary to release the assets.
 - For example, a county would recognize a liability when it collects taxes for an authority, even though it may not be required to distribute the taxes to the authority for a prescribed period
- Liabilities other than those to beneficiaries should be recognized in accordance with existing accounting standards using the economic resources measurement focus.

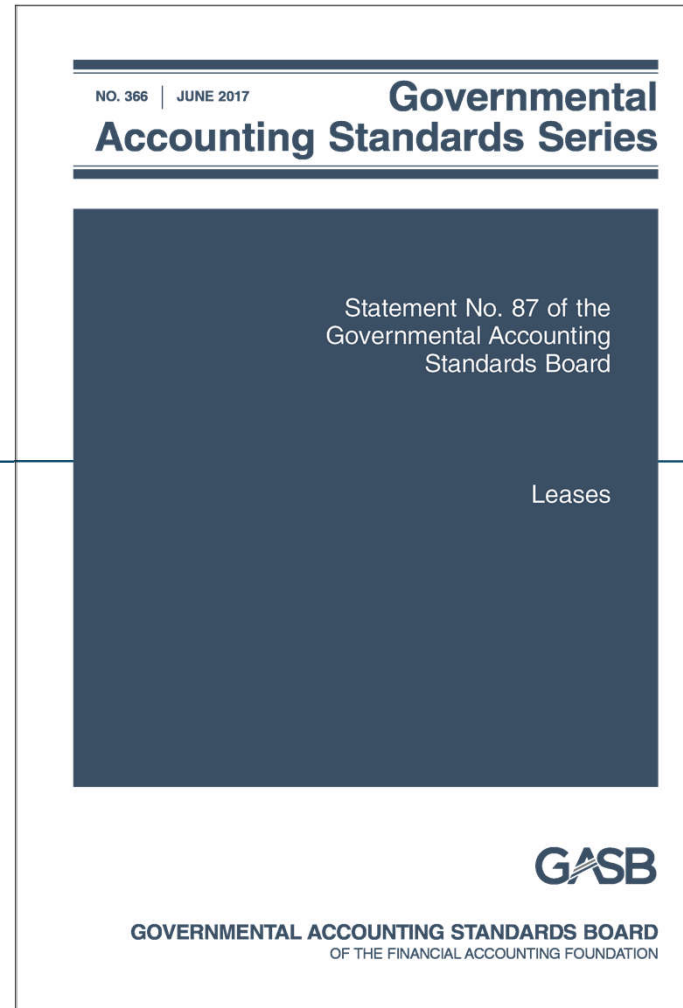
Other Reporting Requirements

- Statement of Changes in Fiduciary Net Position required for all fiduciary funds, including custodial funds
- Additions would be presented disaggregated by source and, if applicable, separately display investment earnings, investment costs, and net investment earnings
- Deductions would be presented disaggregated by type and, if applicable, separately display administrative costs
 - Disaggregated additions and deductions requirement would apply to the statement of changes in fiduciary net position for all fiduciary funds except custodial funds held for three months or less
 - For these custodial funds, governments would be allowed to report total additions and total deductions in the aggregate, as long as the descriptions of the totals are sufficient to indicate the nature of the resource flows

Fiduciary Fund Types

- New definitions for pension trust funds, investment trust funds, and private-purpose trust funds that focus on the resources that should be reported within each.
 - Trust agreement or equivalent arrangement should be present for an activity to be reported in a trust fund.
- *Custodial funds* would report fiduciary activities for which there is no trust agreement or equivalent arrangement.
 - External portions of investment pools that are *not* held in trust should be reported in a separate column under the custodial fund umbrella

Statement 87: Leases



Implementation Ideas



- Start reviewing existing leases as soon as possible
- Implement internal controls to identify leases and lease modifications
- Update accounting systems for new information needs
- Consider impact on capitalization policy
- Consider effects of reporting lease liabilities on—
 - Debt limitations
 - Bond covenants
 - Grant agreements

Unified Reporting Model for Leases

- No classification of leases into operating/capital or other categories
- Underlying assumption that leases are financings
- Exceptions (lessors and lessees)
 - Short-term leases
 - Leases that transfer ownership and do not contain termination options
- Exceptions for lessors
 - Leases of assets that are investments
 - Certain regulated leases

What Is the Definition of a Lease?

- A contract that conveys control of the right to use another entity's nonfinancial asset (the underlying asset) as specified by the contract for a period of time in an exchange or exchange-like transaction.

How Is Control Described in the Context of a Lease?

- Control requires both of the following:
 - The right to obtain the present service capacity from use of the underlying asset as specified in the contract, and
 - The right to determine the nature and manner of use of the underlying asset

Lease Term

- For financial reporting, when does the lease start and end?
 - Starts with the noncancelable period, plus periods covered by lessees' and lessors' options to:
 - Extend the lease, if the option is reasonably certain of being exercised
 - Terminate the lease, if the option is reasonably certain of NOT being exercised
 - Excludes "cancelable" periods
 - Periods for which lessee and lessor each have the option to terminate or both parties have to agree to extend
 - Rolling month-to-month leases
 - Fiscal funding/cancelation clauses ignored unless reasonably certain of being exercised

What Is a Short Term Lease?

- A short-term lease is one that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised
 - For a lease that is cancelable either by the lessee or lessor, such as month-to-month or year-to-year leases, the maximum possible term is the noncancelable period including any notice period

How Should Leases Be Initially Reported?

	Assets	Liability	Deferred Inflow
Lessee	Intangible asset (right to use underlying asset)—value of lease liability plus prepayments and initial direct costs that are ancillary to place asset in use	Present value of future lease payments (incl. fixed payments, variable payments based on index or rate, reasonably certain residual guarantees, etc.)	NA
Lessor	<ul style="list-style-type: none"> Lease receivable (generally including same items as lessee liability) Continue to report leased asset 	NA	Equal to lease receivable plus any cash received up front that relates to a future period

How Should Leases Be Subsequently Reported?

	Assets	Liability	Deferred Inflow
Lessee	Amortize over shorter of useful life or lease term	Reduce by lease payments (less amount of interest expense)	NA
Lessor	<ul style="list-style-type: none"> • Depreciate leased asset (unless indefinite life or required to be returned in its original or enhanced condition) • Reduce receivable by lease payments (less payment needed to cover accrued interest) 	NA	Recognize revenue over the lease term on a systematic and rational basis

Technical Agenda—What Should Be On Your Radar

- Current Agenda
 - Financial reporting model (reexamination)
 - Revenue and expense recognition
 - Disclosure framework
 - Subscription-based information technology arrangements

- Research Agenda
 - Going concern
 - Deferred compensation plans
 - Compensated absences
 - Prior period adjustments

Questions



Website information: www.gasb.org

