



## National Association of State Auditors, Comptrollers and Treasurers

January 31, 2007

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Mr. David Bean  
Director of Research and Technical Activities  
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Governmental Accounting Standards Board  
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Norwalk, CT 06856-5116

Dear Mr. Bean:

On behalf of the members of the National Association of State Auditors, Comptrollers and Treasurers, I am pleased to submit these comments about the GASB's Invitation to Comment, *Fund Balance Reporting and Governmental Fund Type Definitions*. While our members' views on many of the questions which the Board has posed are quite similar, there are also interesting differences, and we have encouraged our members to send their comments directly to you as well as to us.

#### Question 1.

*What resources should be accounted for in a special revenue fund included in external financial reports—only a specific revenue source (Option A), a specific revenue source and transferred matching resources (Option B), or a specific revenue source, transferred matching resources, and other legally limited transferred resources (Option C)? (See paragraphs 8-13.) Why do you think that option is best?*

Our members show a marked preference for Option C. They approve of reporting all of the resources used for a specific purpose in the special revenue fund. They expect that Option C will result in more consistent reporting from one year to the next. One member observed that accounting practice has been moving in the direction of using special revenue funds to report all of the resources used for a specific purpose. Another member noted that the benefits realized from an activity-based approach outweigh the benefits realized from compliance-based reporting. The use of Option C would make the financial statements a more effective management tool because they would present the complete resource inflows and outflows related to a particular activity.

#### Question 2.

*Do you believe that special revenue funds should be created to report only restricted revenue sources (Option 1) or be defined more broadly to report legally limited revenue sources (Option 2)? (See paragraphs 14-22.) Why do you prefer that option?*

By about a two-to-one margin, responding members prefer Option 2. They believe that this approach will show more clearly how governments manage their resources, thereby providing useful information to users of the financial statements.

Question 3.

*If special revenue funds were to be defined under Option 2, is the approach to defining legally limited in paragraph 16 appropriate? If not, how would you recommend describing the action or level of authority necessary for establishing limitations other than restrictions?*

Our members agree that the approach to defining *legally limited* in paragraph 16 is appropriate. The definition is broad enough to be applicable to different types of governments.

Question 4.

*Do you agree that specified purposes means a use that is narrower than the basic activity of the government? (See paragraphs 23-26.) If not, how would you define specified purposes?*

Our members agree that *specified purpose* means a use that is narrower than the basic activity of the government.

Question 5.

*If rainy-day fund resources cannot be reported in a special revenue fund for external reporting purposes, then how should they be identified in the financial statements-(a) as a component of fund balance (for example, reserved or designated) in the general fund on the balance sheet, (b) in a note disclosure or separate schedule that disaggregates the general fund, (c) as a new rainy-day fund type, or (d) another approach (please specify)? (See paragraphs 27-30.) Why do you believe that is the best approach?*

Our members are in virtual agreement that the creation of a new rainy-day fund type is not a good idea. Well over half of our responding members chose option a, that rainy-day fund resources should be reported as a component of fund balance. They view rainy-days funds as a “set-aside” portion of the general fund to be used only when certain conditions are met. They also note that the resources for a rainy-day fund come from a government’s general revenues and are disbursed for whatever purposes are deemed necessary when those resources are called upon. Option b found favor with a few respondents, either on its own, as an acceptable alternative to option a or in combination with option a.

Question 6.

*Do you believe that an externally reported debt service or capital projects fund should contain only resources that are restricted or legally limited to purposes consistent with the fund (Alternative A) or that those funds also should be allowed to contain resources intended for purposes consistent with the fund (Alternative B)? (See paragraphs 31-35.) Why do you think that alternative is best?*

Those offices that came to a decision between Alternative A and Alternative B favored the former by two-to-one. Staff in several offices were evenly split on the matter. The arguments in favor of Alternative A were several:

- Alternative A is the more conservative approach.
- Capital projects and debt service funds are created for very specific purposes and should be displayed separately because of the long-term contractual commitments they report. The nature of these funds justifies the restrictions.

Some members appreciate that their position on this question is inconsistent with their preference for Option C in Question 1. However, they believe that the reasons cited above explain their choice of Alternative A for capital projects and debt service funds.

Question 7.

*What other recommendations do you have, if any, for ensuring that resources transferred to a debt service or capital projects fund are meant by a government to be used for those purposes and are not confused by users as available for any purpose?*

One member suggested that there should be an explanation that transfers *to* these funds must meet the legally limited definition and that it would be rare to have significant transfers *from* these funds. Perhaps note disclosures of any significant transfers from these funds might be required.

Question 8.

*Do you agree that legally segregated, as used in the definition of reserved fund balance, should be understood to mean a legal limitation that cannot be changed unless a government takes the same action it employed to impose the limitation initially or by taking a higher authority action? (See paragraphs 11 and 12.) If you disagree, how would you describe the authority necessary to establish a legal limitation?*

Our members generally agree that *legally segregated*, as used in the definition of reserved fund balance, should be understood to mean a legal limitation that cannot be changed unless a government takes the same action it employed to impose the limitation initially or by taking a higher authority action. They believe that the definition provided is broad enough to allow governments to apply the standard to their circumstances.

Question 9.

*Do you agree that encumbrances associated with appropriations that lapse at the end of the fiscal year and that a government intends to honor (and for which an appropriation is made in the subsequent year) should be reported differently than encumbrances with continuing appropriations? (See paragraphs 15-19.) If you disagree, how should encumbrances be reported?*

Our members generally agree that encumbrances associated with appropriations that lapse at the end of a fiscal year and that the government intends to honor (and for which an appropriation is made in the subsequent year) should be reported differently than encumbrances with continuing appropriations.

Question 10.

*Should the reporting of a government's intent to use resources for a particular purpose be required, optional, or prohibited? (See paragraphs 20-24.) Why do you believe that would best meet the need to understand a government's intended uses of resources?*

A majority of responding members believe that the reporting of a government's intent to use resources for a particular purpose should be required. They note that a consistent application of reporting these amounts will enhance comparability among reporting governments. Also, this reporting provides useful information about a governing body's intent and provides a link between the financial statements and a government's legally adopted budget.

Question 11.

*What actions, decisions, or expressions do you believe constitute an intent to use resources that should be reported as a designation of fund balance? (See paragraphs 25-29.)*

Most members agree that a formal action or decision should be the basis for reporting designations of fund balance. These actions would include public expressions as reported in the minutes of a governing body, joint resolutions, annual appropriations, or legislation. Most of the members who addressed the question of timing in paragraph 29 agree that the action constituting intent or the expression of intent should take place during or prior to the fiscal year reported by the financial statements.

Question 12.

*Which model, A, B, or C, most faithfully represents the important aspects of a government's fund balance and best meets the needs of financial statement users? (See paragraphs 33-53.)*

A slight majority of our members prefer Model A, although the state comptrollers demonstrated somewhat more enthusiasm for this model than did the state auditors. The preferences of the other members were evenly split between Models B and C.

Question 13.

*Why does the model you selected in Question 12 most faithfully represent the important aspects of a government's fund balance or best meet the needs of financial statement users?*

Those who prefer Model A believe that it will best meet the needs of financial statement users because it is closest to the current model, with which preparers and users are most familiar. Hence Model A will be the easiest to understand.

Question 14.

*What other issues relating to the reporting and interpretation of fund balance information are you aware of? What actions, if any, should be taken to address those issues?*

One member suggested that the GASB should provide better definitions and more guidance in the **Comprehensive Implementation Guide** about the application of the following terms: *legally segregated, legally limited, legally restricted, restricted assets, restricted net assets, reserved fund balances, encumbrances, unreserved fund balance, designated-unreserved fund balance and undesignated-unreserved fund balance.*

As always, we appreciate the opportunity to participate in the Board's due process. Should you have any questions about our comments, please feel free to contact me (615-741-2382 or [jan.sylvis@state.tn.us](mailto:jan.sylvis@state.tn.us)) or Pat O'Connor of the NASACT staff (859-276-1147 or [poconnor@nasact.org](mailto:poconnor@nasact.org)).

Sincerely,

A handwritten signature in black ink that reads "Jan Sylvis". The signature is written in a cursive, flowing style.

Jan Sylvis  
President