National State Auditors Association

GASB Update—Assessing Risks

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

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Risks

Assessing Risks—Overview

Auditors

- Audit risk
  - Inherent risk
  - Control risk
  - Detection risk

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- Risks associated with financial statement information
- Linked to qualitative characteristics
- Risks referred over 1000 times in GASB literature
  - 17 different types of risks identified in GASB standards

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GASB Identified Risks

- Perception is that risks are primarily associated with financial instruments
  - True—based on identified risks (all can be associated financial instruments)
  - Examples—credit risk, interest rate risk, liquidity risk, rollover risk, termination risk, foreign currency risk
- Other risks
  - Risk of omission—incomplete
  - Risk of misstatement—inaccurate
  - Risk of misunderstanding
  - Risk of untimely information

Qualitative Characteristics—GASB Concepts Statement 1

- Understandability
- Reliability (representational faithfulness)
- Relevance
- Timeliness
- Consistency
- Comparability

Understandability—Communicating Risks

- Understandable by whom?
  - GASB Concepts not clear
- Concepts Statement 1—General purpose financial reporting
  - Users of governmental reports tend to have different levels of knowledge and sophistication about governmental accounting and finance.
  - To be publicly accountable, a government should issue financial reports that can be understood by those who may not have a detailed knowledge of accounting principles.
    - Comprehensive annual financial report versus popular report
  - Financial reporting should not exclude information merely because it is difficult to understand or because some users choose not to use it.
- Concepts Statement 3—Basic financial statements
  - The user is responsible for obtaining a reasonable understanding of government and public finance activities and of the fundamentals of governmental financial reporting, for studying the messages with reasonable diligence, and for applying relevant analytical skills.

Reliability

- Most misunderstood qualitative characteristic
  - Information presented should be verifiable
  - Free from bias
  - Should faithfully represent what it purports to represent.
- To be reliable, financial reporting needs to be comprehensive.
  - Nothing material should be omitted from the information necessary to faithfully represent the underlying events and conditions, nor should anything be included that would cause the information to be misleading.
- Reliability does not imply precision or certainty. Affected by:
  - Degree of estimation in the measurement process
  - Uncertainties inherent in what is being measured
  - May need to include narrative explanations about the underlying assumptions and uncertainties inherent in this process.
- A properly explained estimate provides more meaningful information than no estimate at all.

Relevance

- Information is relevant if it is capable of making a difference in a user's assessment of a problem, condition, or event.
- Relevance depends on the types of financial information needed by the various users to make decisions and assess accountability.

Timeliness

- If financial reports are to be useful, they must be issued soon enough after the reported events to affect decisions.
- Timeliness alone does not make information useful, but the passage of time usually diminishes the usefulness that the information otherwise would have had.
- In some instances, timeliness may be so essential that it may require sacrificing a certain amount of precision or detail.
- Sometimes a timely estimate is more useful than precise information that takes a long time to produce.

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Consistency

- Financial reports should be consistent over time
- There is a presumption that once an accounting principle or reporting method is adopted, it will be used for all similar transactions and events (until changed).
- The concept of consistency in financial reporting extends to many areas such as valuation methods, basis of accounting, and determination of the financial reporting entity.
- If accounting principles have been changed or the financial reporting entity has changed, the nature and reason for the change as well as the effect of the change should be disclosed.

Comparability

- Comparability implies that differences between financial reports should be due to substantive differences in the underlying transactions or the governmental structure rather than due to selection of different alternatives in accounting procedures or practices.
- Financial reporting should help users make comparisons among governments
  - For example, comparisons of the costs of specific functions or components of revenue.

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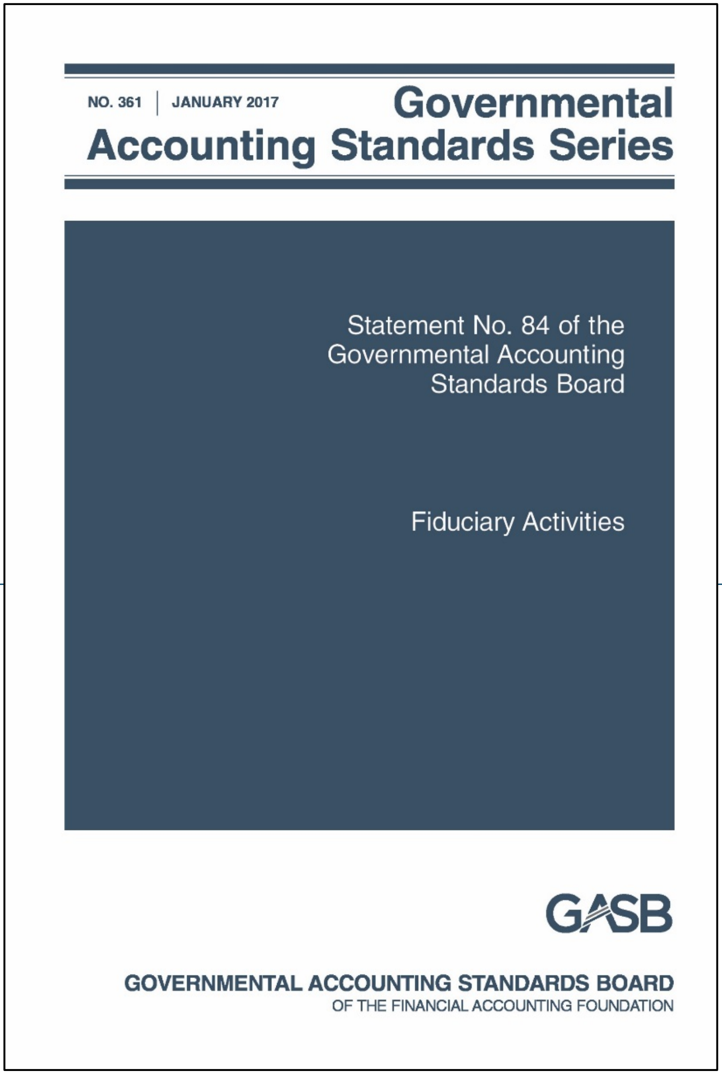
Implementation Issues

Fiduciary Activities: Statement 84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Fiduciary Activities

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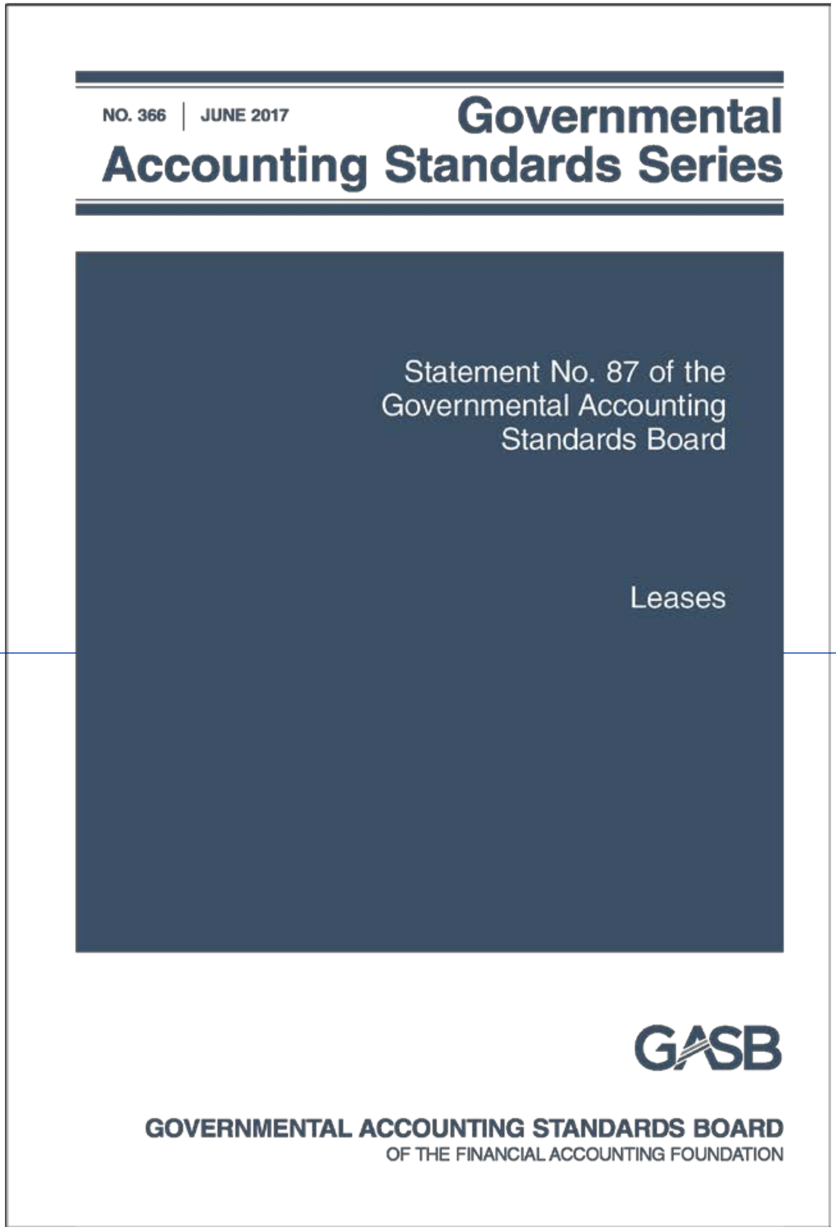
What Are Some Implementation Tips?

- Review classification and fund category no later than 2018
  - Including business type activities
- Review how inflow and outflow information is captured for activities previously reported as agency funds
- Watch for implementation guide

Statement 87: Leases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Leases

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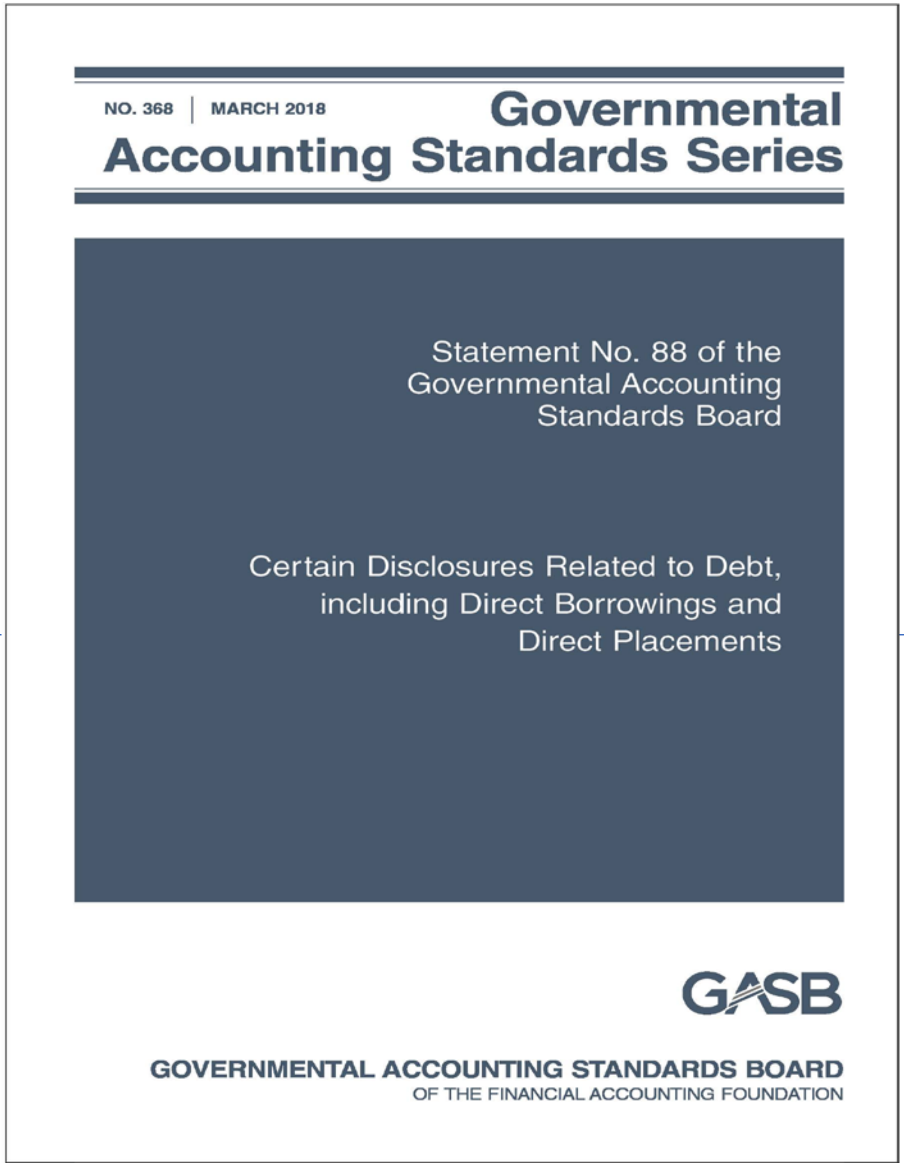
What Are Some Implementation Tips?

- Determine if bond covenants or debt limit provisions need to be modified
- Review policies now so that those policies can be applied to leases that are currently being entered into and still will be in effect when Statement 87 becomes effective
- Potential policies that could be considered
  - Identify a working threshold for assessing leases
  - Operationalize “reasonably certain”
  - Operationalize allocation procedures for nonlease components
- Review system to capture data related to lease terms, estimated lease payments, and other components of lease agreements that could effect the liability being reporting
- Watch for implementation guide

Debt Disclosures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Certain Disclosures Related to Debt, including Direct Borrowings and Direct Placements

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What Are Some Implementation Tips?

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

Technical Agenda—What Should Be On Your Radar

- Reporting model (reexamination)
- Revenue and expense recognition
- Capitalization of interest
- Equity interest ownership issues
- Conduit debt
- Cloud computing arrangements
- Public-private partnerships

Research Agenda

- Note disclosures (reexamination)
- Going concern
- Deferred compensation plans

Questions?

- Visit www.gasb.org