

To: James L. App, City Manager
From: Mike Compton, Director of Administrative Services
Subject: Governmental Accounting Standards Board Statement No. 34
DATE: March 4, 2003

Needs: To make a presentation to the City Council regarding the implementation of Governmental Accounting Standards Board Statement No. 34 and its impact upon the City's financial statements.

Facts:

1. The Governmental Accounting Standards Board (GASB) is a regulatory body that sets accounting standards for government entities in the United States.
2. In June 1999, GASB issued Statement No. 34 (GASB 34) titled "Basic Financial Statements – and Management Discussion and Analysis – for State and Local Governments" which represents a fundamental change in the current financial reporting model that has been in place since 1979.
3. The City must implement GASB 34 beginning with the current fiscal year, 2003.
4. The Council allocated \$40,000 for GASB 34 compliance assistance of which \$10,000 was approved for the purchase of financial reporting software. The remaining funds were earmarked for fixed asset/infrastructure inventory and valuation services.
5. The infrastructure inventory and valuation study is now complete and the City is ready to implement GASB 34.

Analysis &
Conclusion:

What is GASB 34?

GASB is a fundamental change in the financial reporting model for government entities. Its key new features are:

Government-wide financial reporting – Under the prior reporting model, financial statements were prepared on a modified accrual basis, i.e., statements excluded general long-term debt and fixed assets (non-utility). Under GASB 34, financial statements are reformatted to provide a picture of the City on a full accrual basis (long-term debt & general government fixed assets are included) and as a single, unified entity (rather than a collection of various special fund types).

Additional long-term focus for governmental activities – Currently, financial reports focus attention on *spendable* financial resources. The new model attempts to provide a long-term perspective by focusing on *net assets*, i.e., including long-term debt and general governmental fixed assets.

Infrastructure reporting – The new financial reports will include depreciation for general (non-enterprise) fixed assets and infrastructure on the balance sheet.

Narrative overview and analysis – Under the new model, the financial statement transmittal letter is simplified and a narrative analysis of the statements is required in the form of a management discussion and analysis (MD&A). The MD&A will be audited and must receive an unqualified audit opinion.

Information on major funds – The new model presents individual fund data for each *major*, but not necessarily every, fund.

Why implement GASB 34?

The merits of GASB 34 are still being debated. However, there are compelling reasons to implement including:

Generally accepted accounting principles (GAAP) – The most compelling reason is GAAP. Since GASB is the recognized authoritative body for setting accounting standards, non-compliance would generate a qualified opinion rather than an unqualified opinion. It is imperative that the City maintains citizen confidence and trust in our accounting and financial reporting systems. Preparation of GAAP financial statements is essential to gaining and sustaining this trust.

Financial markets and rating agencies – In most cases, those who monitor long-term financings and provide ratings on public debt require submission of audited financial statements. Receiving an unqualified opinion is critically important to bond ratings. Lower bond ratings could result if the City did not provide audited GAAP financial statements. Lower ratings would increase the interest cost of financings resulting in hundreds of thousands of dollars over the life of the bond issue.

Supported by professional organizations – The National Association of State Auditors, Comptrollers and Treasurers, the California Society of Municipal Finance Officers and the Government Finance Officers Associations have all recommended implementation.

Fiscal Impact:

The cost to prepare for implementation of GASB 34 was \$40,000. This included \$10,000 for specialty software and \$30,000 for the infrastructure inventory and valuation study.

Infrastructure and general fixed assets reporting, including depreciation, will have a reportable financial impact upon government-wide financial statements. Allocation of real resources to cover depreciation expense is not required. However, the City will need to address the maintenance and replacement needs of its facilities and infrastructure in the long-term.

Options:

- a. Receive presentation; or
- b. Amend, modify, or reject the above option.