

Organization Management Workshop
 April 10-12, 2011 :: Hyatt Regency Jersey City :: Jersey City, NJ

IBTTA
 International Bridge, Tunnel and Turnpike Association
 DRIVING CHANGE SINCE 1932

**Everything You Wanted to Know About
 Performance Audits and
 Recent GASB Pronouncements, But
 Were Afraid to Ask**

KPMG
 cutting through complexity™

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Objectives

- To provide participants with overall understanding of selected current key GASB pronouncements
- To learn how completing a performance audit can help your agency
- To learn from other participants on how the discussed topics have effected them

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Agenda Topics

- Impact of SAS 118, 119, 120 on Auditors and Auditee
- GASB 53 – Accounting and Financial Reporting for Derivative Instruments
- GASB 54 – Fund Balance
- GASB 57 – OPEB
- GASB 58 – Bankruptcies
- GASB 59 – Financial Instruments
- GASB 60 – Concession Arrangements
- GASB 61 – Reporting Entity
- GASB 62 – Codification of Pre 1989 FASB Statements
- Performance Audits
- Q & A

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**SAS 118 Other Information in Documents
 Containing Audited Financial Statements**

- Issued 2/2010
- Supersedes SAS No. 8 & portions of No. 29
- Effective for YB on/after 12/15/10
- Effect on SLGs preparing a CAFR
 - Statistical section
 - Transmittal letter

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**SAS 118 Other Information in Documents
 Containing Audited Financial Statements**

- Definitions
 - **Other information**
 - Financial & nonfinancial
 - Included in a document with audited FS & audit report thereon, excluding RSI
 - **Inconsistency**
 - Other information conflicts with audited FS
 - Material inconsistencies raise doubt re:
 - Audit conclusions drawn from previously obtained evidence
 - Basis for audit opinion
 - **Misstatement of fact**
 - Other information unrelated to FS matters incorrectly stated or presented
 - May undermine credibility of document containing FS

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**SAS 118 Other Information in Documents
 Containing Audited Financial Statements**

- Auditor requirements
 - Read other information – identify any material inconsistencies with audited FS
 - Arrange to obtain prior to report release date
 - Communicate with those charged with governance
 - Auditor responsibility
 - Any procedures performed
 - Results of procedures

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SAS 118 Auditor Actions

- Material inconsistencies – pre report release
 - Revision to FS needed
 - Management refuses to revise = revise opinion
 - Revision to other information needed
 - Management refuses to revise = communicate to those charged with governance
 - » Include explanatory paragraph in audit report
 - » Withhold audit report OR
 - » Withdraw if possible under applicable law or regulation
- Material inconsistencies – after report release
 - Revision to FS needed
 - Apply AU 561 (Subsequent Discovery of Facts)
 - Revision to other information needed
 - Management agrees to revise = take action specified in SAS
 - Management refuses to revise = notify those charged with governance & may need to contact legal counsel

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SAS 118 Auditor Actions

- Material misstatements of fact
 - Discuss with management
 - If no resolution, request management to consult with qualified third party
 - Consider advice received by entity
 - Conclude there is a material misstatement of fact
 - Management refuses to correct
 - » Notify those charged with governance re: concerns
 - » Take further action as suggested in SAS

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SAS 119 Supplementary Information In Relation to the Financial Statements as a Whole

- Issued 2/2010
- Supersedes portions of SAS No. 29
- Effective for YB on/after 12/15/10
- Affects
 - Governmental CAFR
 - Other SI required in a CAFR (combining schedules, etc.)
 - Annual Reports

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SAS 119

- “Information is fairly stated, in all material respects, in relation to the financial statements taken as a whole”
- Defines SI
 - Information presented outside BFS, excluding RSI
 - Not necessary for fair presentation under applicable framework
 - Included in document with audited FS & audit report or separate
- Conditions to be met
 - SI derived from & relates directly to the underlying records used to prepare FS
 - SI relates to same period as FS
 - FS audited & auditor was principal auditor
 - No adverse/disclaimer
 - SI will accompany auditing FS or audited FS will be made readily available by entity

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SAS 119

- Management representations
 - Preparation of SI in accordance with applicable criteria
 - Provide auditor specific representations (outlined in the SAS)
 - Include auditor's report on SI in any document containing the SI & that indicates auditor reported on SI
 - Present SI with audited FS or make FS readily available to intended users of SI no later than issue date of SI by entity & auditor's report thereon
- Reporting – SI presented with FS
 - Explanatory paragraph after opinion or separate report on SI
 - Purpose of audit = FS opinion
 - SI presented for additional analysis, not required
 - SI responsibility of management
 - SI subjected to auditing procedures applied in FS audit & certain additional procedures
 - Delineate specific additional procedures
 - Unqualified & qualified opinions
 - Extend to SI if appropriate
 - Adverse opinion/disclaimer
 - Precluded from opining on SI

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SAS 119

- Reporting – SI not presented with FS
 - Separate report on SI
 - Same requirements as when SI presented with auditing FS
 - Date of report no earlier than date required SI procedures completed
 - Additional reference to
 - Report on FS
 - Date of report
 - Nature of opinion
 - Any report modifications
- Reporting – SI materially misstated in relation to FS as a whole
 - Discuss with management
 - Propose appropriate revision of SI
 - Management refuses to revise
 - Modify opinion on SI & describe misstatement OR
 - Withhold separate report on SI

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SAS 120 Required Supplementary Information

- Issued 2/2010
- Supersedes SAS No. 52
- Effective for YB on/after 12/15/10

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SAS 120 Required Supplementary Information

- Affects
 - Governmental BFS
 - MD&A
 - Pension & OPEB information
 - Budgetary schedule
 - Modified approach info, if applicable
 - NFPs
 - Functional expense matrix (maybe)
- Provides definitions
 - RSI
 - Required by designated standard setter
 - Designated accounting standard setter
 - GASB, FASB, FASAB, IASB

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SAS 120 Required Supplementary Information

- Required audit procedures
 - Management inquiries re: methods of preparation
 - Compare info for consistency with
 - Management response
 - Audited FS
 - Other knowledge obtained during audit
 - Obtain specific written management representations

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SAS 120 Required Supplementary Information

- Specific written management representations
 - Responsible for RSI
 - RSI measured & presented in accordance with prescribed guidelines
 - Any changes in methods of measurement or presentation & reasons
 - Significant assumptions/interpretations

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SAS 120 Required Supplementary Information

- Required reporting
 - Explanatory paragraph AFTER opinion
 - RSI required to supplement BFS & by whom
 - RSI included & specific required procedures applied
 - If RSI is omitted in whole or part
 - When some RSI presented within guidelines
 - Identified material departures from prescribed guidelines
 - Unable to complete required procedures
 - Unresolved doubts re: whether RSI conforms to prescribed guidelines
 - No opinion on or assurance given

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GASB 53 *Accounting and Financial Reporting for Derivative Instruments*

- Issued June 2008
- Effective for financial statements for periods beginning after June 15, 2009
- Applicable to all state & local governments that enter into derivative transactions, as derivatives are defined in statement

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How does it impact you?

- Prior to GASB 53, these derivatives were reported as a footnote disclosure.
 - The first impact will be new assets or liabilities on your statement of net assets. There is the possibility of having to report investment revenue or loss, depending on whether the derivative meets the definition of a hedge under GASB 53, or is an investment instrument.
- The GASB 53 testing requirements present an additional workload.
- The fair value of the derivatives is primarily driven by the level of underlying market rates.
 - With the relatively low level of interest rates compared to when these transactions were first executed, most governments will assume additional liabilities on their statement of net assets after adopting GASB 53, some amounts which could be material. If a derivative is a hedge, it will be offset by a corresponding deferred outflow.

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GASB 53 Core Concepts

- Report the fair value of a derivative on the statement of net assets (balance sheet).**
- All hedges must be evaluated for effectiveness**
- Recognize changes in the fair value** - of the derivative either:
 - on the balance sheet or statement of net assets, as **deferred inflows** or **deferred outflows** if the derivative passes its effectiveness test; OR
 - as investment revenue/loss (i.e., gain or loss through statement of revenues, expenses, changes in fund net assets, as appropriate) if the derivative fails, or is not a hedge.

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GASB 54 Fund Balance

- Clarify misunderstandings on fund balance
- Clarifies certain parts of fund definitions
- Effective date YB 6/15/10
- New categories based on relatively strength of control constraints
 - Nonspendable Fund Balance
 - Restricted Fund Balance
 - Committed Fund Balance
 - Assigned Fund Balance
 - Unassigned Fund Balance

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GASB 54 Fund Balance

- Nonspendable**
 - Can not be spent because EITHER
 - Not in spendable form**
 - Not expected to be converted to cash (e.g., inventories, prepaids)
 - Other (e.g., LT loans & notes receivable, property acquired for resale)
 - Legally/contractually required to be maintained intact**
 - Permanent fund corpus
- Restricted**
 - External parties, constitution, enabling legislation
- Committed**
 - Government constraint using its highest level decision-making authority (e.g., ordinance)
- Assigned**
 - Intended for specific use by government
- Unassigned**
 - No constraints – general fund only

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GASB 54 Encumbrances

✓	If the encumbering process meets the definition and criteria for committed fund balance, then encumbering an assigned or unassigned amount could result in the amount being reported as committed; however, it would be reported with other amounts committed to the same or similar purposes, not as “committed for encumbrances.”
✓	If a government has significant encumbrances, it should disclose them under the standards for significant commitments.

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GASB 54 Fund Balance

- Reporting negative balances
 - First reduce amounts assigned to other purposes within the fund
 - Any remaining negative residual balance = negative UNASSIGNED fund balance
- Required note disclosures
 - Accounting policies re: classifications when expended for purposes with multiple fund balance classifications
 - Provides default policy if none adopted – Use restricted amounts first, then committed, assigned, & unassigned (sequentially)
 - Information re: rainy day funds
 - Explanation of minimum fund balance requirements
 - Description of processes to commit & assign fund balance
 - Purpose of each SRF - Identify which specific revenues & other resources are authorized to be reported in each

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GASB 57 OPEB Measurements

- Issued December 2009
- Effective immediately
 - Certain agent employers can use alternative measurement method
 - Single employer - less than 100 members regardless of number members in total plan
- Effective PB after 6/15/11
 - Frequency & timing of measurements

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GASB 58 Chapter 9 Bankruptcies

- Issued December 2009
- Effective periods beginning after 6/15/10
 - Retroactive application required – all periods presented
 - Recognition & measurement of effect of bankruptcy process on assets & liabilities
 - Confirmed Plan of Adjustment amounts
 - Gains/losses = extraordinary items

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GASB 58 Chapter 9 Bankruptcies

Item	Treatment
Accounts payable, notes, debentures and bonds, and related interest payable	GASB No. 58 requires governments to base remeasurement on the new payment plan. Reductions in future interest payments would result in lower interest costs reported in future periods. Reductions to principal or to accrued interest payable may result in gains reported at the time of the reduction. If the new payment plan does not indicate whether it reduces principal payments or future interest payments that have not been accrued, the debt should be remeasured at the present value of the future payments using the original discount rate, and a gain should be reported at the time of the reduction.
Leases, pollution remediation liabilities, and liabilities for pension and other postemployment benefit plans	GASB No. 58 requires remeasurement based on existing authoritative guidance. However, if a benefit plan is rejected in bankruptcy and becomes general unsecured debt, GASB No. 58 requires the existing liability to be removed and a new approved payment plan to be recognized as a judgment, with a gain or loss recognized for the difference.

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GASB 59 Financial Instruments Omnibus

- Issued June 2010
- Effective periods beginning after 6/15/10
- Modifies/clarifies #25, 31, 40, 43 & 53
- Major provisions
 - Unallocated insurance contracts at FV not contract value
 - Definition of 2a7-like pool
 - Interest rate risk disclosed only for *bond* mutual funds not meeting requirements of 2a7-like pool
 - Certain financial guarantees & credit default swaps no longer exempt from #53
 - Leveraged yield criteria of #53 met if initial ROR on companion instruments has *potential* for a least doubled yield

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GASB 60 Service Concession Arrangements

- Issued December 2010
 - Effective periods beginning after December 15, 2011
 - Generally, provisions are required to be applied retroactively for all periods presented
- Service concession arrangements include, but are not limited to, arrangements in which an operator will
 - Design and build a facility and will obtain the right to collect fees from third parties
 - Provide significant consideration in exchange for the right to access an existing facility and collect fees from third parties for its usage
 - Design and build a facility for the transferor, finance construction costs, provide the associated services, collect the associated fees, and convey the facility to the government at the end of the arrangement.
- Provides guidance on
 - Whether the transferor or the operator should report the capital asset in its financial statements,
 - When to recognize up-front payments from an operator as revenue
 - How to record any obligations of the transferor to the operator.
- Also provides guidance for governments that are operators in an SCA.

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GASB 61 Financial Reporting Entity

- Issued December 2010
 - Effective periods beginning after June 15, 2012
- Amends Statements No. 14 and No. 34
 - Amends criteria for including component units and for blending component units
 - Adds financial benefit/burden criteria to fiscal dependency criteria
 - Requires reporting condensed combining information in the notes to the financial statements for blended component units of primary governments that are business-type activities reporting in a single column (i.e. a state university)
 - New requirements for reporting equity interests in component units

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GASB 61 Financial Reporting Entity

- Major amendments
 - Misleading to exclude criterion
 - Inclusion under financial accountability concept
 - Major CU requirements
 - Blending criteria
 - Reporting funds of blended CUs
 - Reporting entity interests in CUs
 - CUs and related organizations with joint venture characteristics
 - Note disclosures

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GASB 61 Financial Reporting Entity

- Fiscally dependent CU must also create financial benefit/burden to continue as CU
- Clarifies manner for management to include CU not meeting financial accountability criteria
- Blended CUs
 - Additional criteria to remain blended
 - Required when total CU LTD expected to be repaid entirely/almost entirely with PG resources
 - Clarifies funds of blended CU virtually same as PG
 - Additional reporting guidance if PG a single column BTA
- Clarifies reporting of equity interests in legally separate organizations
 - PG required to report interest as asset
 - Asset eliminated in blending process if CU meets blending criteria

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GASB 62 Codification of Pre 11/1989 GAAP

- Issued December 2010
 - Effective periods beginning after December 15, 2011
- Incorporates guidance previously only found in certain FASB and AICPA pronouncements
- amends or supersedes various GASB statements and paragraphs and footnotes of the various GASB and NCGA standards and interpretations.
- Supersedes GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*

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Performance Audit Overview

- Provides assurance or conclusion based on an evaluation of sufficient, appropriate evidence against stated criteria
- Entails objective assessments of:
 - Program effectiveness, economy, and efficiency
 - Internal control
 - Compliance
- Provides independent assessment of performance and management of a program
 - Against objective criteria OR
 - Assessments that provide a prospective focus or that synthesize information on best practices or cross-cutting issues

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Yellow Book

- Principles of transparency and accountability
- Framework includes competence, integrity, objectivity and independence
- Established by the Comptroller General of the United States (US Government Accountability Office)
- Applies to CPA's, Auditor Generals, Inspector Generals and others in the accountability profession
- General Standards & Field Work Standards
- Financial Statement Audits, Attestation Engagements and Performance Audits

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General Standards "Audit Rigor"

- Independence
 - Personal Impairment
 - External Impairment
 - Organizational Independence (External & Internal Audit organizations)
 - Impact on Nonaudit Services (3 types of services - Safeguards)
 - Overarching Principles
 - Not step in the shoes of management
 - Not audit the work of the auditor
- Professional Judgment – reasonable care & skepticism
- Competence – CPE
- Quality Control and Assurance (Peer Review)




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Example of Audit Objectives

- Determine if an Entity complies with the deadlines in statutes and rules with respect to work programs and the factors responsible for any failure to meet the deadlines
- Determine if an Entity has implemented processes/controls that promote the disposition of ROW cases in a reasonably efficient and cost-effective manner
- Determine if the agreement between the ABC and XYZ specifically provides for the following:
 - specific performance period
 - three-year record retention period and right to audit
 - method of payment
 - references to cost principles set forth in CFR 48, Chapter 1, Part 31 for allowability of individual items of cost; CFR 49, Part 18, for administrative procedures; and OMB Circular 1-110, for nonprofit sub-recipients.

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Example of Audit Objectives

- Determine if XYZ's cost proposal contains a breakdown of the estimate for performing the work, and that the proposed costs are comparable in relation to actual historic costs and estimating procedures.
- Determine if XYZ's cost accounting system is capable of accumulating and allocating allowable costs.
- Evaluate the public perception of the quality of performance of the Entity

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QUESTIONS?

THANK YOU

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