

2020 Illinois GFOA Annual Conference



Preliminary Views, Revenue and Expense Recognition

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

Revenue and Expense Recognition

What?

The Board has proposed a comprehensive model for recognition of revenues and expenses

Why?

Guidance for exchange transactions is limited; guidance for nonexchange transactions could be improved and clarified

When?

Comment deadline
February 26, 2021

Public hearings and user forums
in March and April 2021

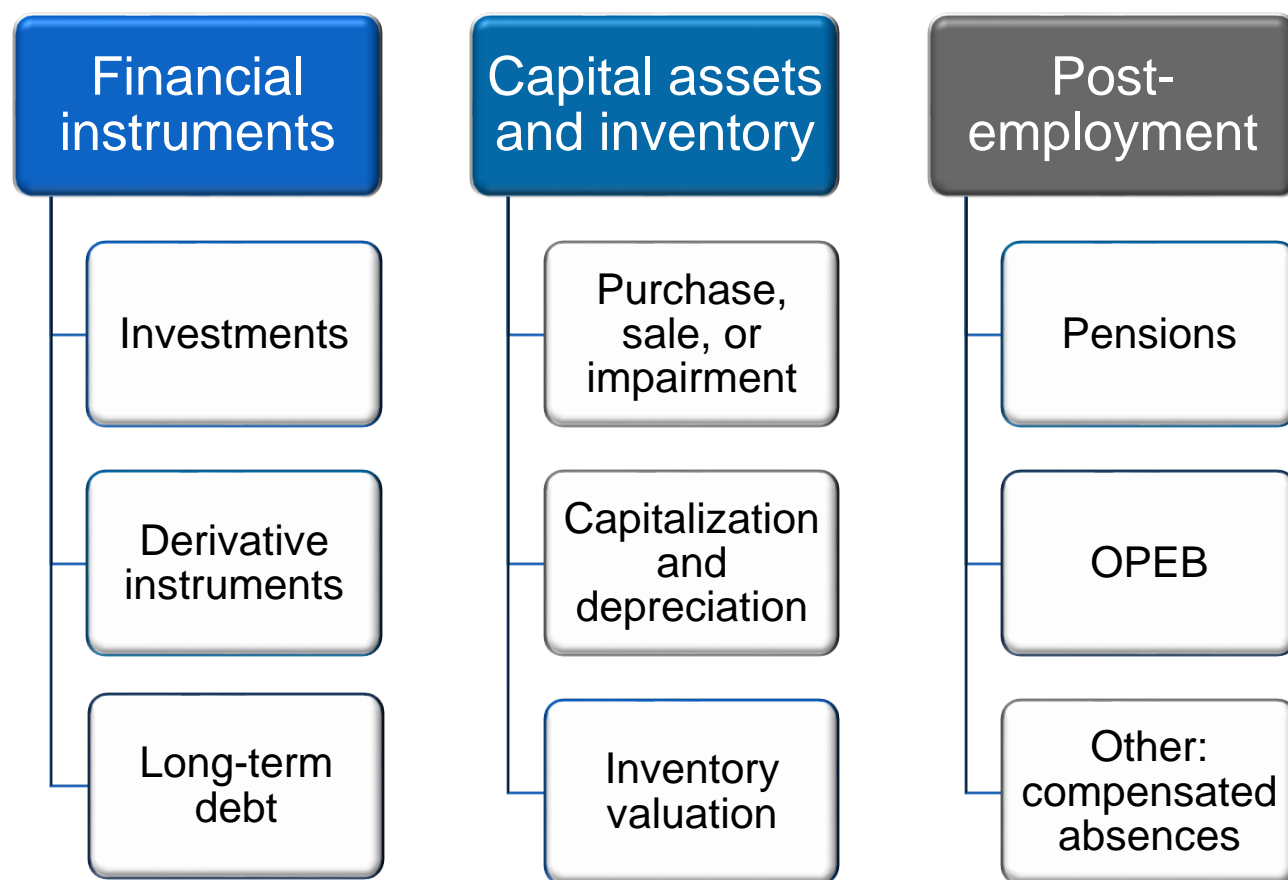
Broad Project Objective

Develop a comprehensive, principles-based model that establishes guidance applicable to a wide range of revenue and expense transactions to:

- Expand on areas where there is no guidance—expenses
- Expand on areas where there is limited guidance—certain revenues
- Consider practice issues and challenges identified in current guidance—Statement 33
- Consider the conceptual framework—issued after Statement 33
- Consider performance obligation recognition

Scope of the Project

- The scope is defined broadly to include revenues and expenses that are not ***explicitly excluded***



Scope in the Context of Standards

In Scope:

- Revenue and expense recognition from nonexchange transactions
 - Statements 6, 24, 33, 36
- Revenue and expense recognition from exchange transactions
 - Statements 34 and 62

Out of Scope:

- Statements issued since Statement 63
- Statements that result from projects added to the technical agenda after April 2016

Proposed Recognition Model Components

Categorization

Identify the *type* of transaction



Recognition

Determine *what* element should be reported and *when*



Measurement

Determine the *amount* to report

Poll Question #1

The GASB recently released a document for public comment on its Revenue and Expense Recognition Project. That document is a(n):

- a. Exposure Draft
- b. Preliminary Views
- c. Invitation to Comment
- d. Technical Bulletin

Chapter 2 – Model Principles

Proposed Revenue and Expense Recognition Model Assumptions

Revenues and expenses are of equal importance in resource flows statements

Revenues and expenses should be categorized independently and not in relation to each other

For accounting and financial reporting purposes, the government is an economic entity and not an agent of the citizenry

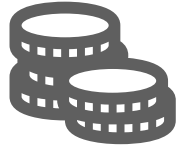
Symmetry should be considered, to the extent possible, in the application of the three components of the model

A consistent viewpoint, from the resource provider perspective, should be applied in the analysis of revenues and expenses

Chapter 3 - Categorization

Current Categorization

Value: equal,
unequal,
essentially equal



Benefit: direct,
indirect, exclusive

Cost recovery:
how much?



Market price:
what
proportion?



- Produces inconsistent results
- Subjective assessment
- Influenced by public policy

Proposed Categorization Methodology

Illegal or
unenforceable
transactions

Is there a binding arrangement?

No

Outside the Scope

Yes

Sales tax, income
tax

Is there mutual assent of the
parties?

No

Yes

Donations

Are there identifiable rights and
obligations that are substantive?

No

Yes

Purpose-
restricted grants

Are the rights and obligations
interdependent?

No

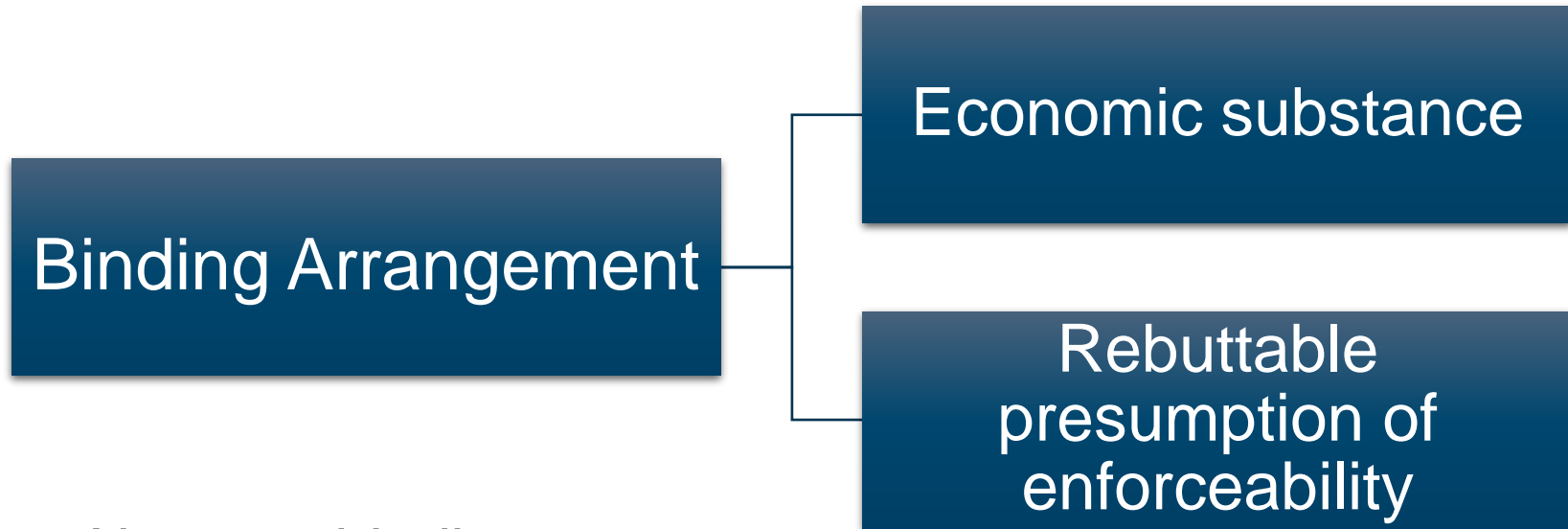
Yes

Eligibility grants,
contracts for services

Category A Transaction

Category B Transaction

Binding Arrangement



- Absent a binding arrangement, the transaction is outside the scope of the project
- Examples of binding arrangements: contracts, grant agreements, purchase orders, legislation

Mutual Assent of the Parties

Approval of the terms and conditions of the binding arrangement

Parties have capacity to bind their entity (or themselves)

- Examples of lack of mutual assent Category B transactions include sales tax, property tax, income tax

Substantive Rights and Obligations

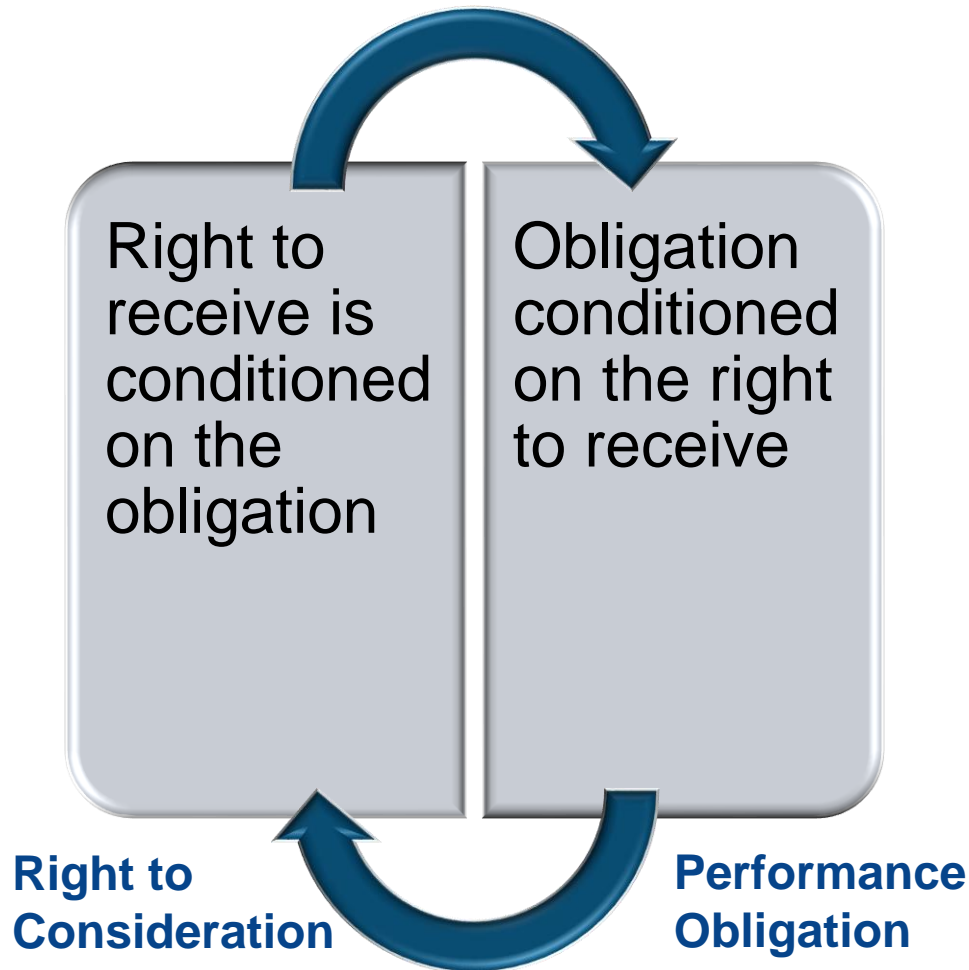
- Substantive rights and obligations are assessed in relationship to each other; for example, a bus fare is considered to have substantive rights and obligations

Substantive
Rights

Substantive
Obligations

- Example of lack of substantive rights and obligations is donations

Interdependent Rights and Obligations



- Example of lack of interdependence
Category B transaction is purpose-restricted grant
- Examples of Category A transactions include eligibility-driven grants, and purchase of services

Outcomes of the Proposed Model *

Category A	Category B
Fees for service (water, electric, garbage)	Taxes (property tax, income tax, sales tax)
Eligibility-based grants	Punitive fees
Research grants and revolving loans	Special assessments
Medicaid fees for services	Donations
Tuition fees	Regulatory fees (drivers licenses, building permits, marriage licenses, professional licenses)
Most expenses	Purpose-restricted grants
	Capital fees (developer fees, PFCs)
	Medicaid supplementary payments

* Transactions highlighted in blue would have different outcomes than under current literature

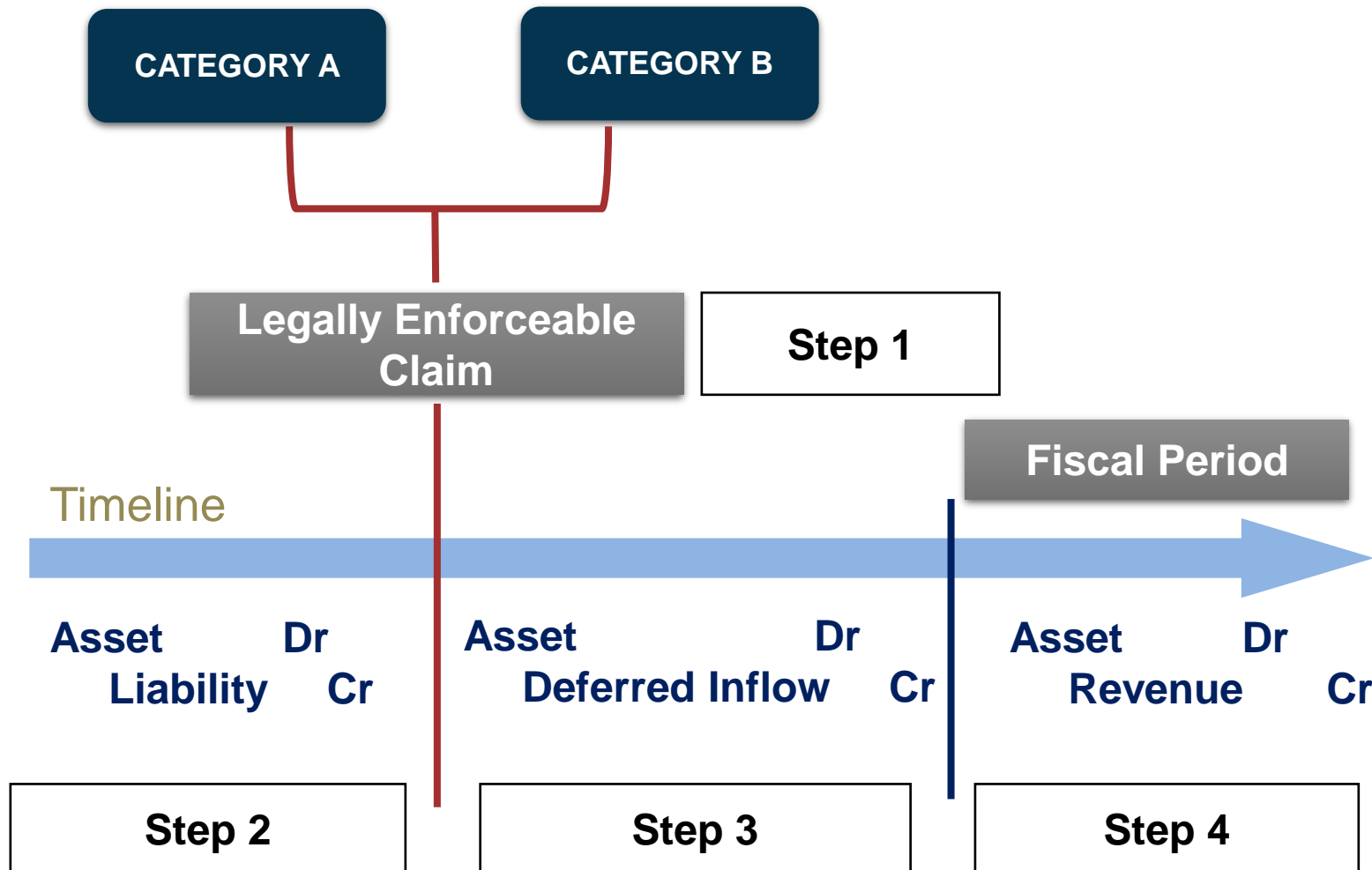
Poll Question #2

The GASB's proposed revenue and expense recognition model would distinguish transactions as:

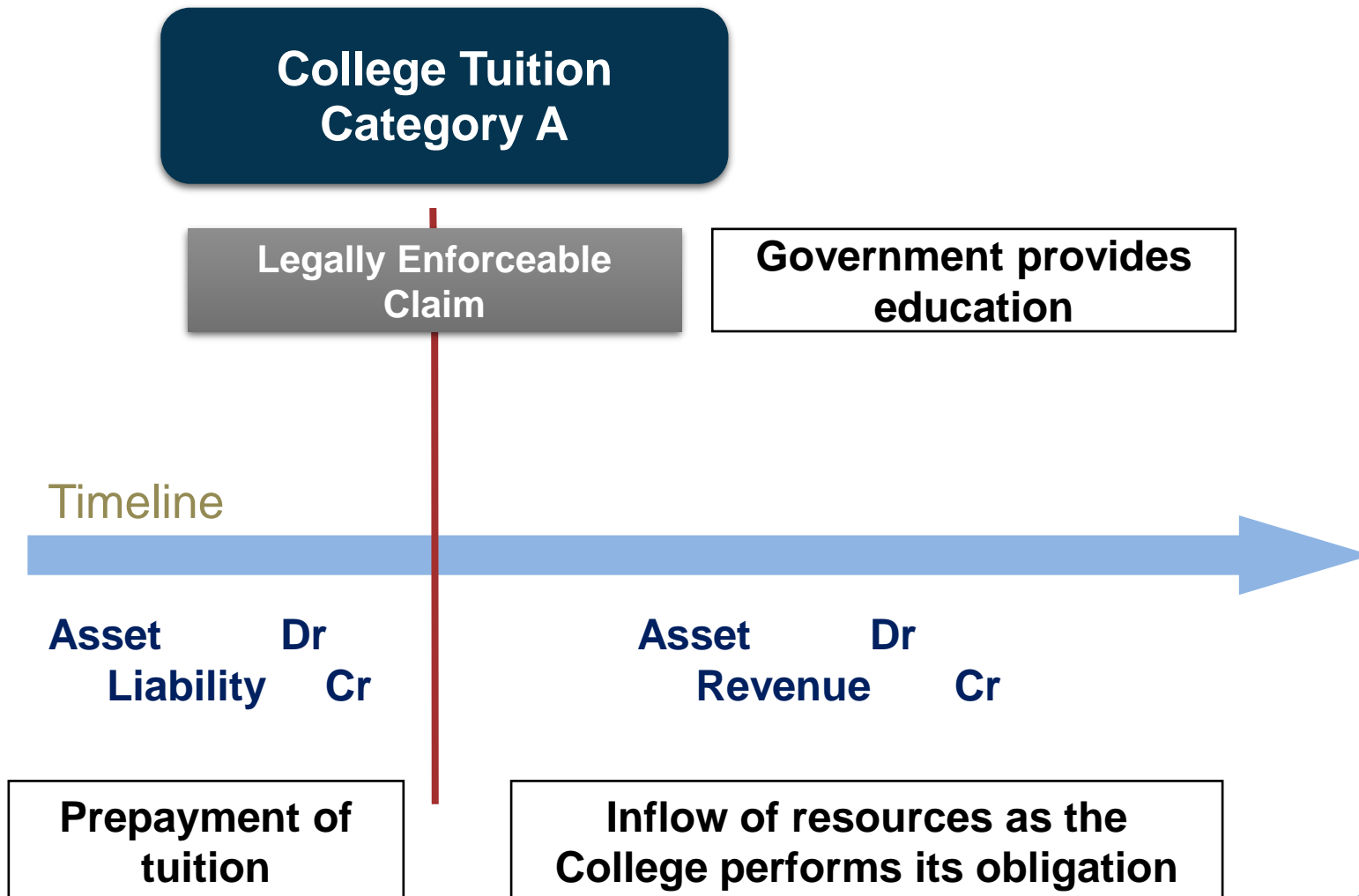
- a. Revenue or expense
- b. Exchange or nonexchange
- c. Category A or Category B
- d. Lantz flows or Caputo flows

Chapter 4 - Revenue Recognition

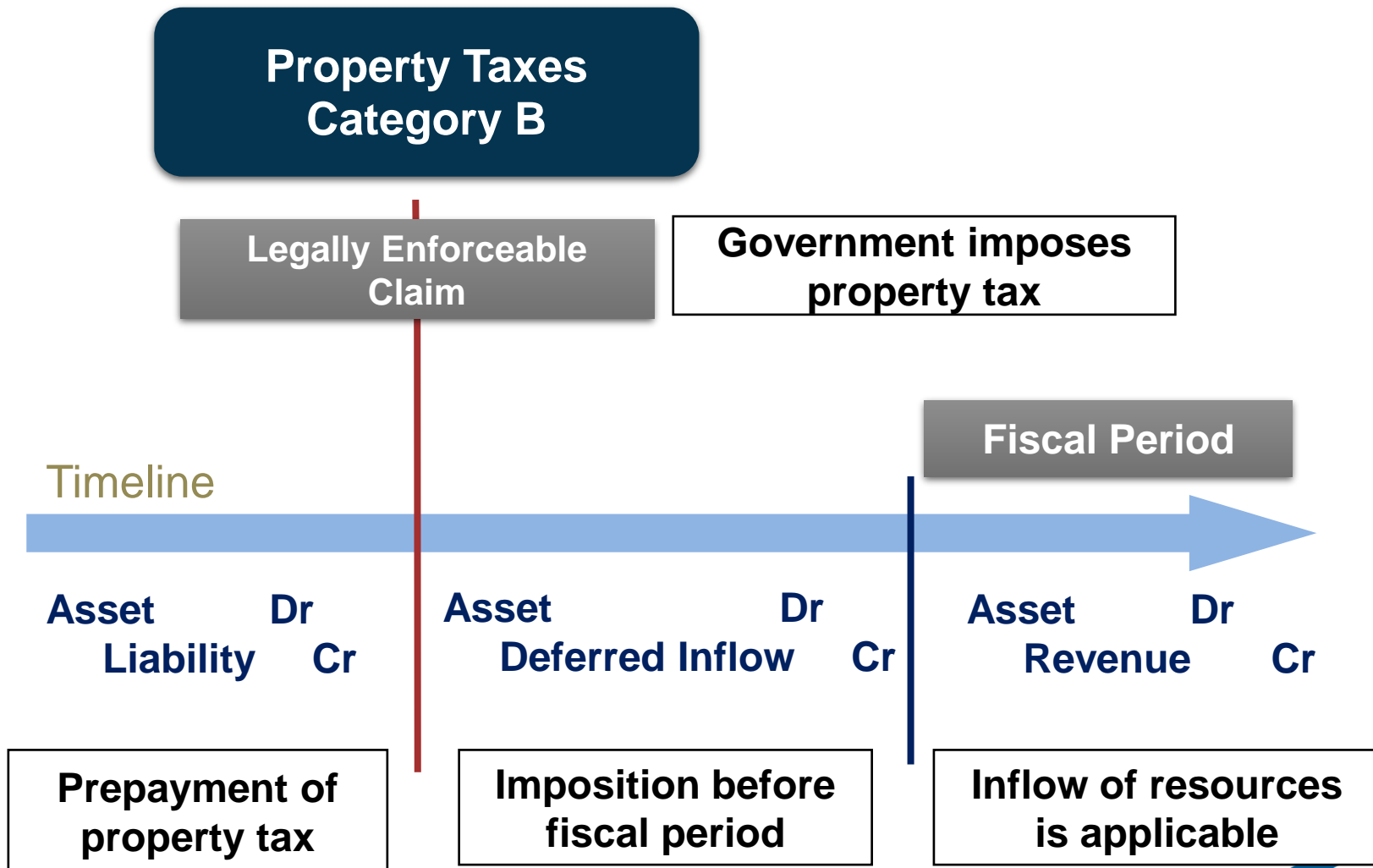
Proposed Revenue Recognition Principles



Category A Revenue Recognition Example



Category B Revenue Recognition Example



Proposed Category A Recognition Principles



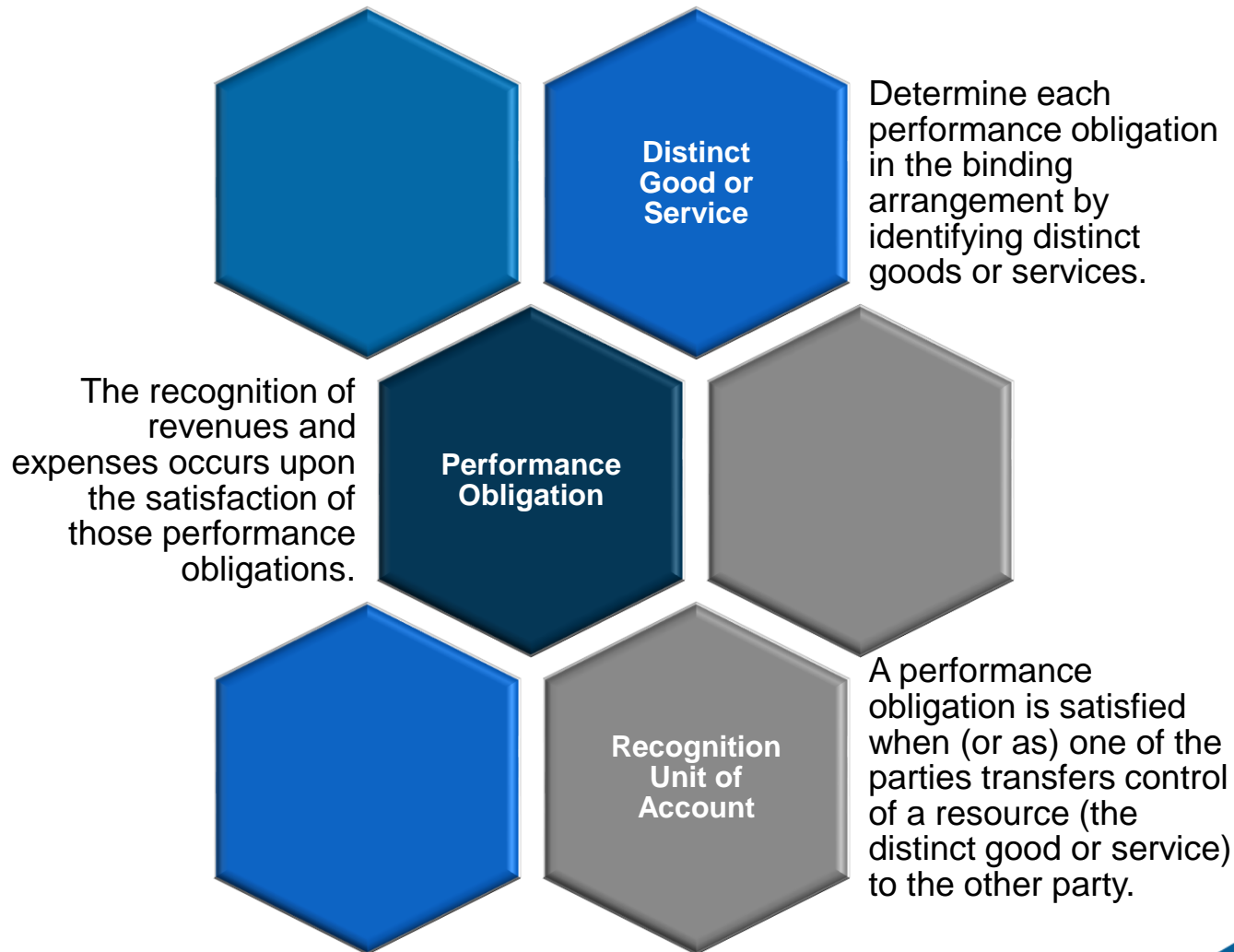
Categorization

- Category A transactions are those that contain all four characteristics:
 - Binding arrangement
 - Mutual assent of the parties
 - Identifiable rights and obligations that are substantive
 - Rights and obligations are interdependent

Recognition

- Category A revenues and expenses are recognized based on the satisfaction of a performance obligation.

Proposed Category A Recognition Principles



Category A Revenue Recognition Examples

A performance obligation is satisfied when there is a transfer of control of resources

Hospital provides an inpatient surgical procedure

- Revenue is recognized as the hospital provides healthcare services over time

State conducts a lottery

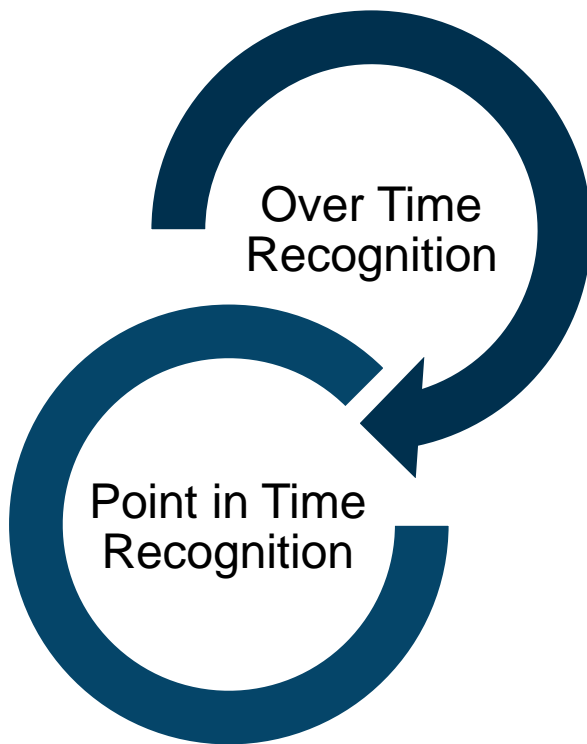
- Revenue is recognized at the drawing when the State provides an opportunity for financial gain

Park District runs a summer camp

- Revenue is recognized as summer camp activities are provided over time

Proposed Category A Revenue Recognition: Over Time or Point in Time

Criteria for Recognition Over Time



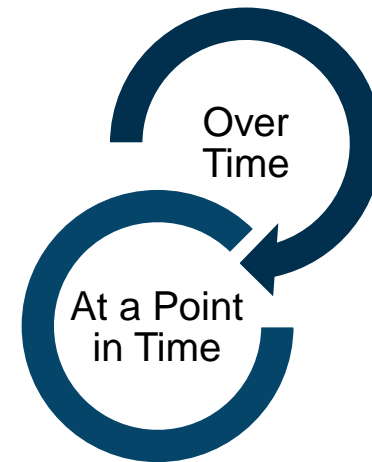
Criterion 1	Criterion 2	Criterion 3
<ul style="list-style-type: none">• Simultaneous consumption• Example: Electricity	<ul style="list-style-type: none">• Creates or enhances an asset• Example: Construction in progress	<ul style="list-style-type: none">• Creates a resource without an alternative use• Has right to payment• Example: Research work

- If one over time criterion is met, revenue is recognized over time.
- If no criterion is met, then recognition is at a point in time.

Proposed Category A Revenue Recognition: Over Time or Point in Time

What distinct good or service is the government providing?

When does the government transfer control of that resource?



Proposed Category B Recognition Principles



Categorization

- Category B transactions are those that do fail either of the following three characteristics:
 - Mutual assent of the parties
 - Identifiable rights and obligations that are substantive
 - Rights and obligations are interdependent

Recognition

- Category B revenues and expenses are recognized based on five subcategories.

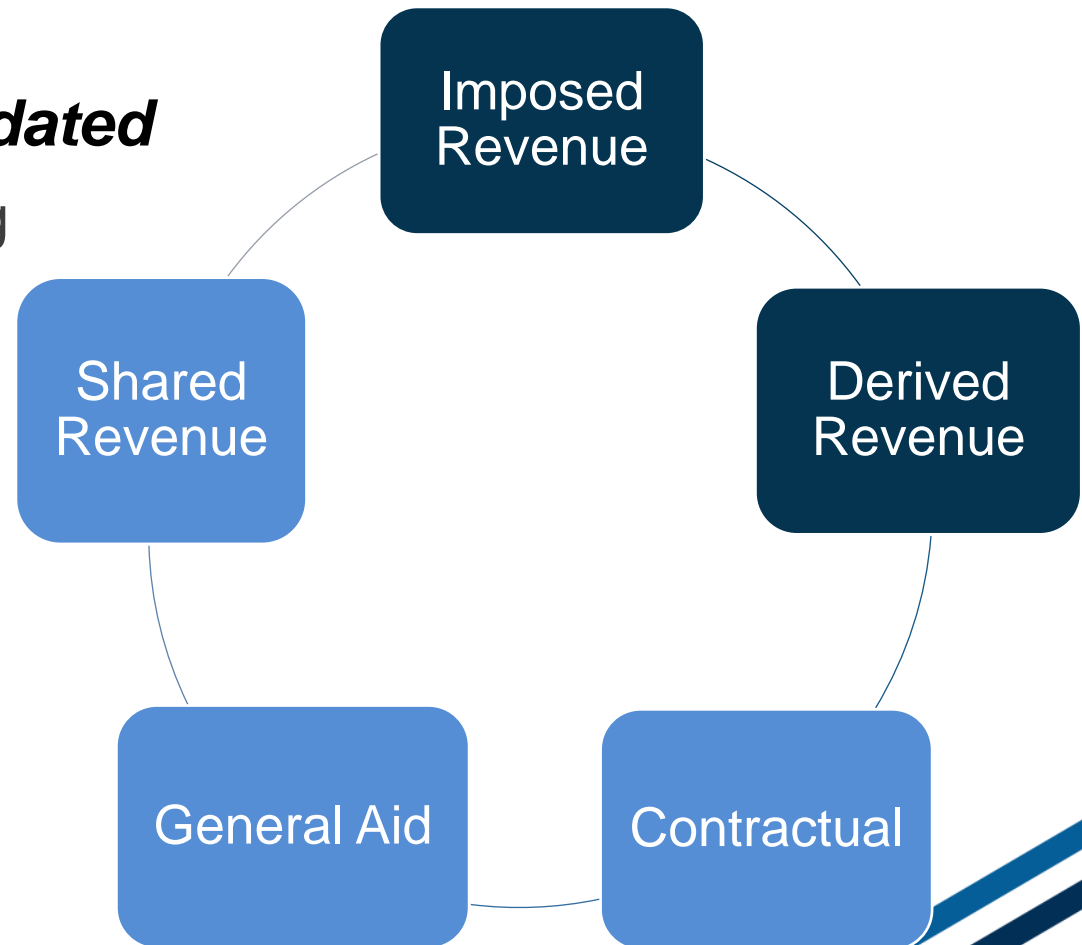
Category B Transactions

- ***Voluntary and Government-Mandated***

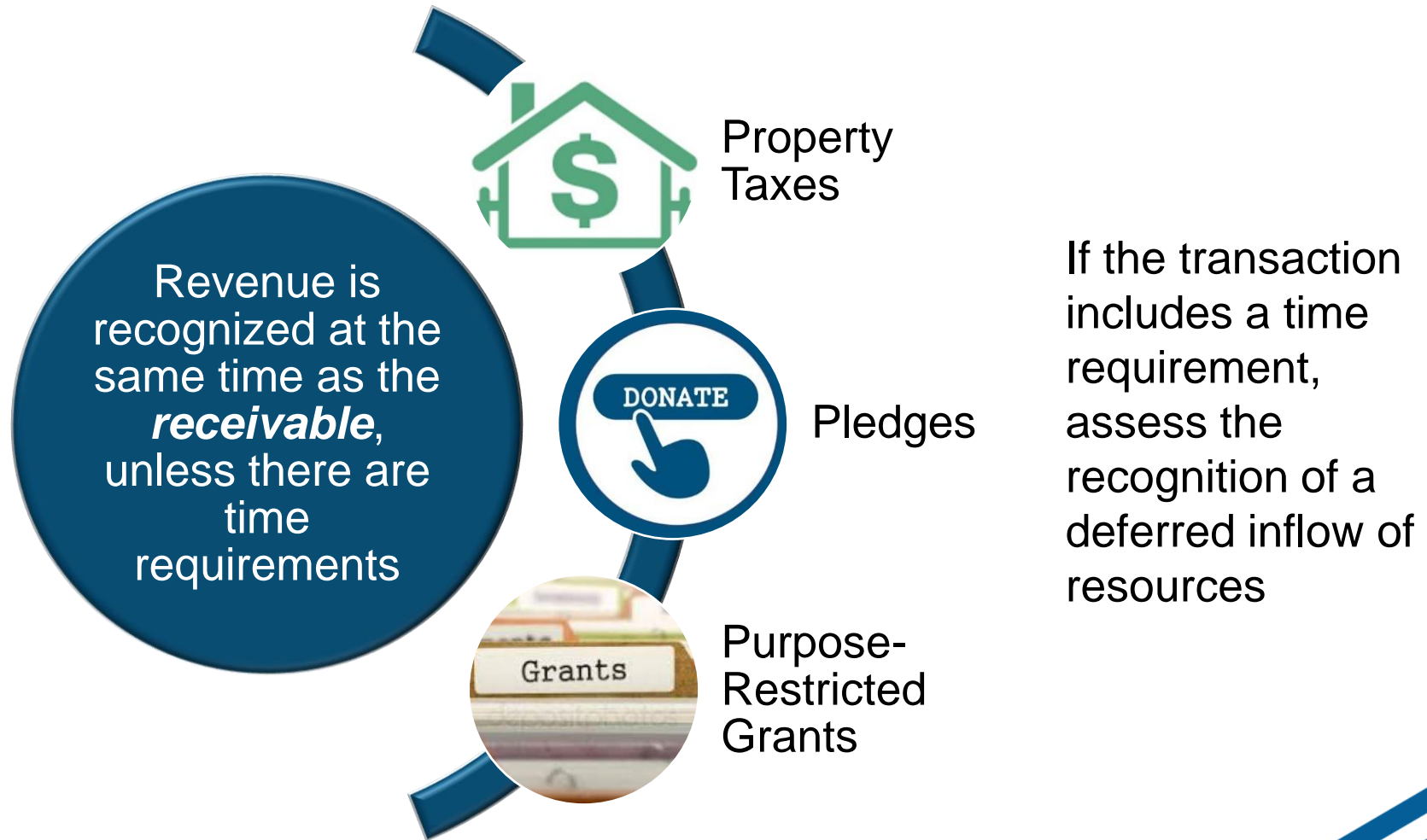
- Contractual binding arrangements
- General aid to governments
- Shared revenue

- **Imposed**

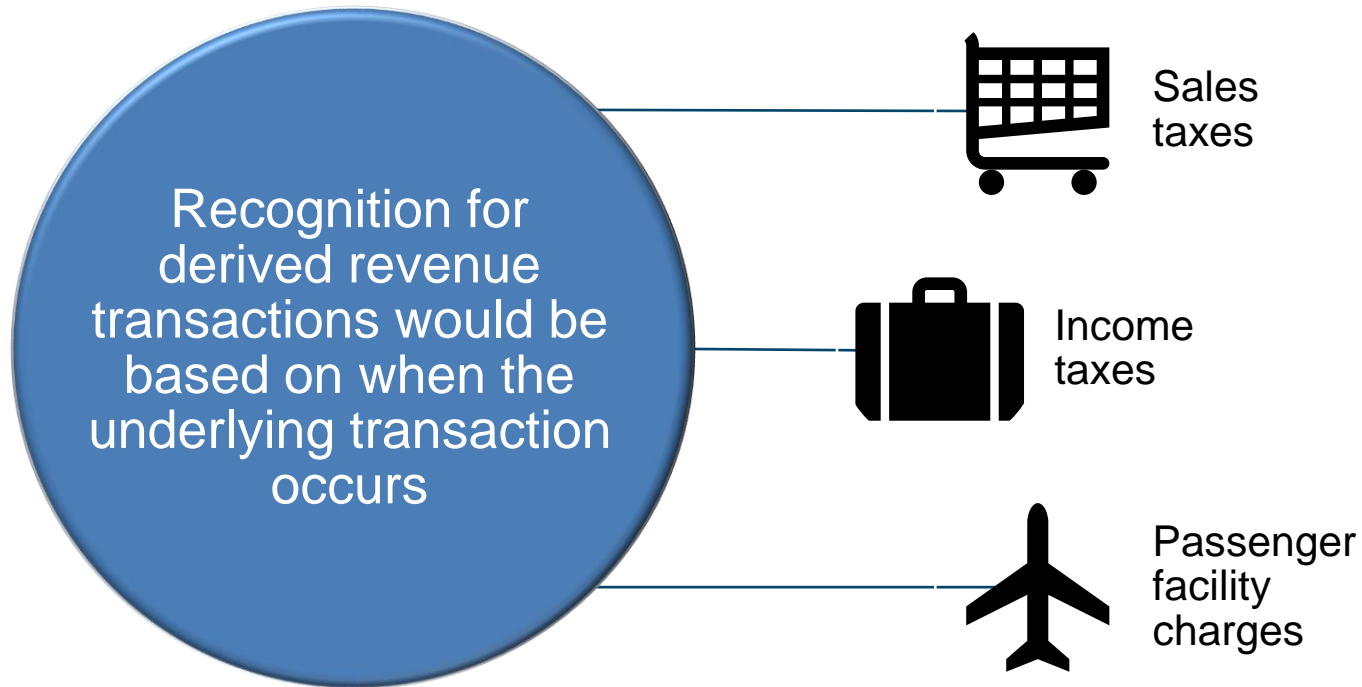
- **Derived**



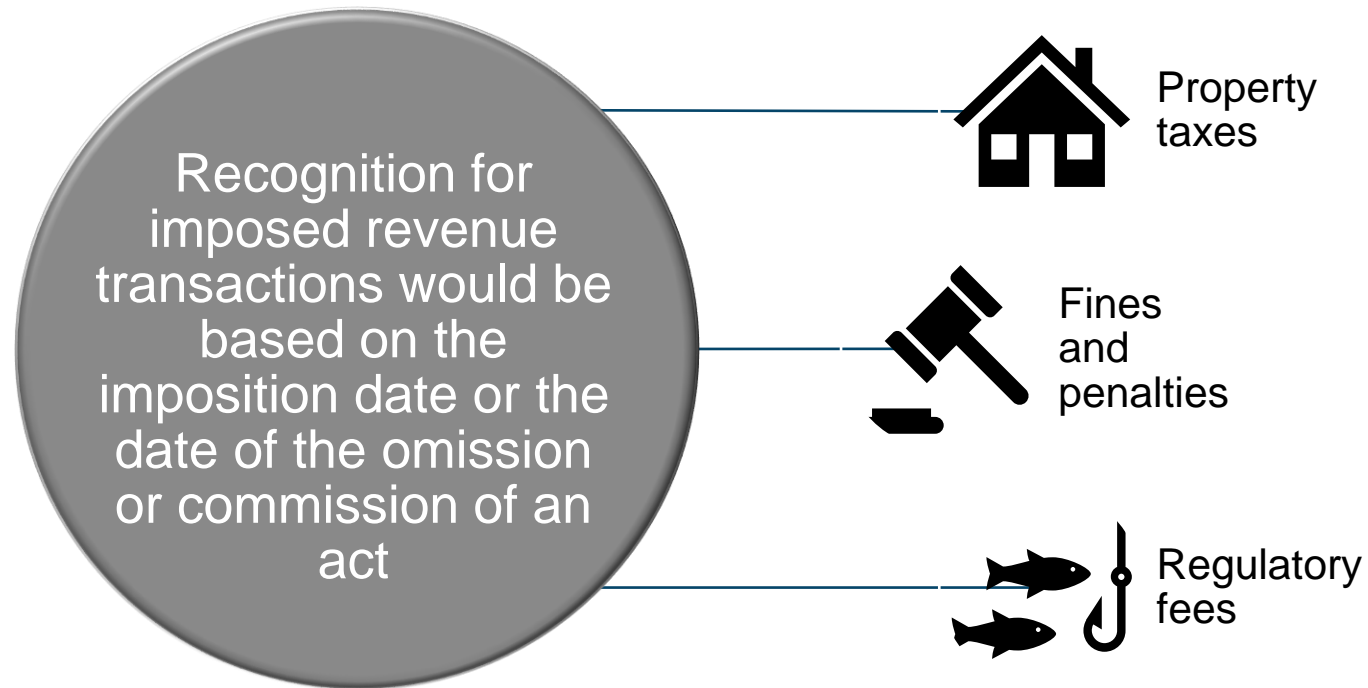
Proposed Category B Revenue Recognition



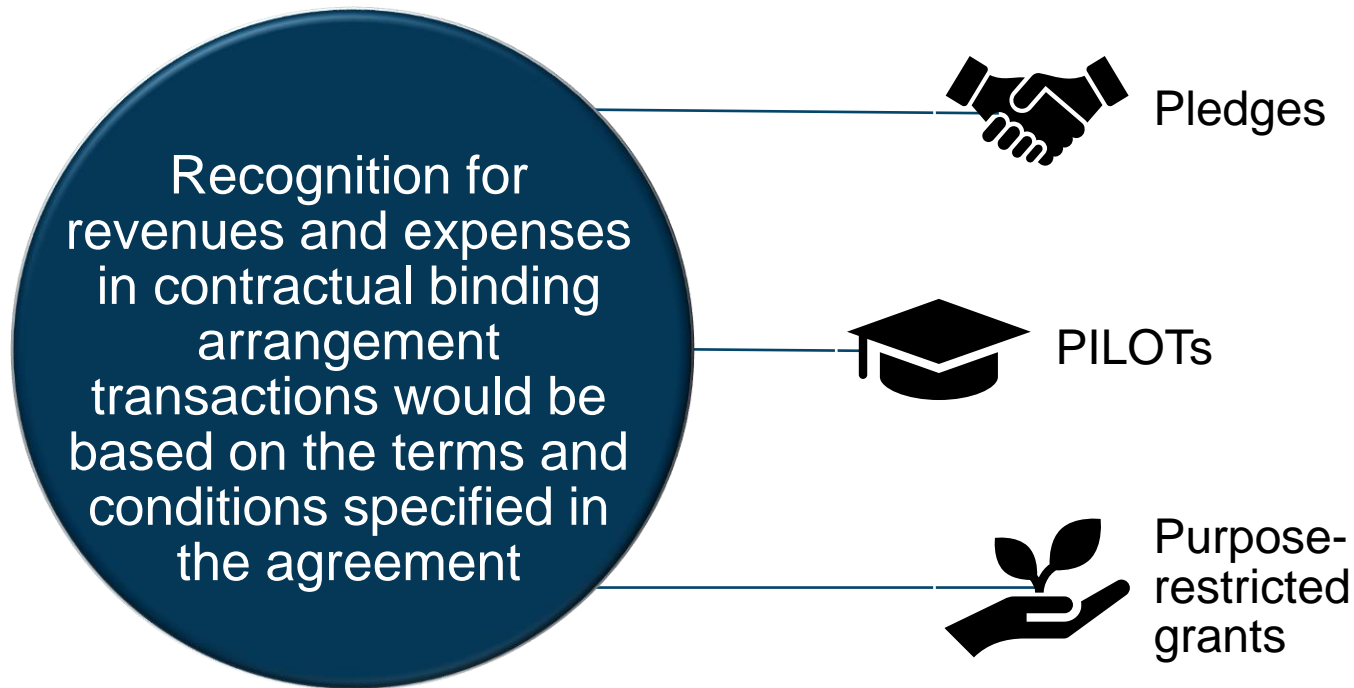
Derived Revenue



Imposed Revenue



Contractual Category B Binding Arrangements



General Aid to Governments and Shared Revenue

Recognition for revenues and expenses in general aid to governments and shared revenue transactions would be based on:

- the existence of a provider government's appropriation,
- the commencement of the appropriation period, and
- the provider government's intent to provide resources.

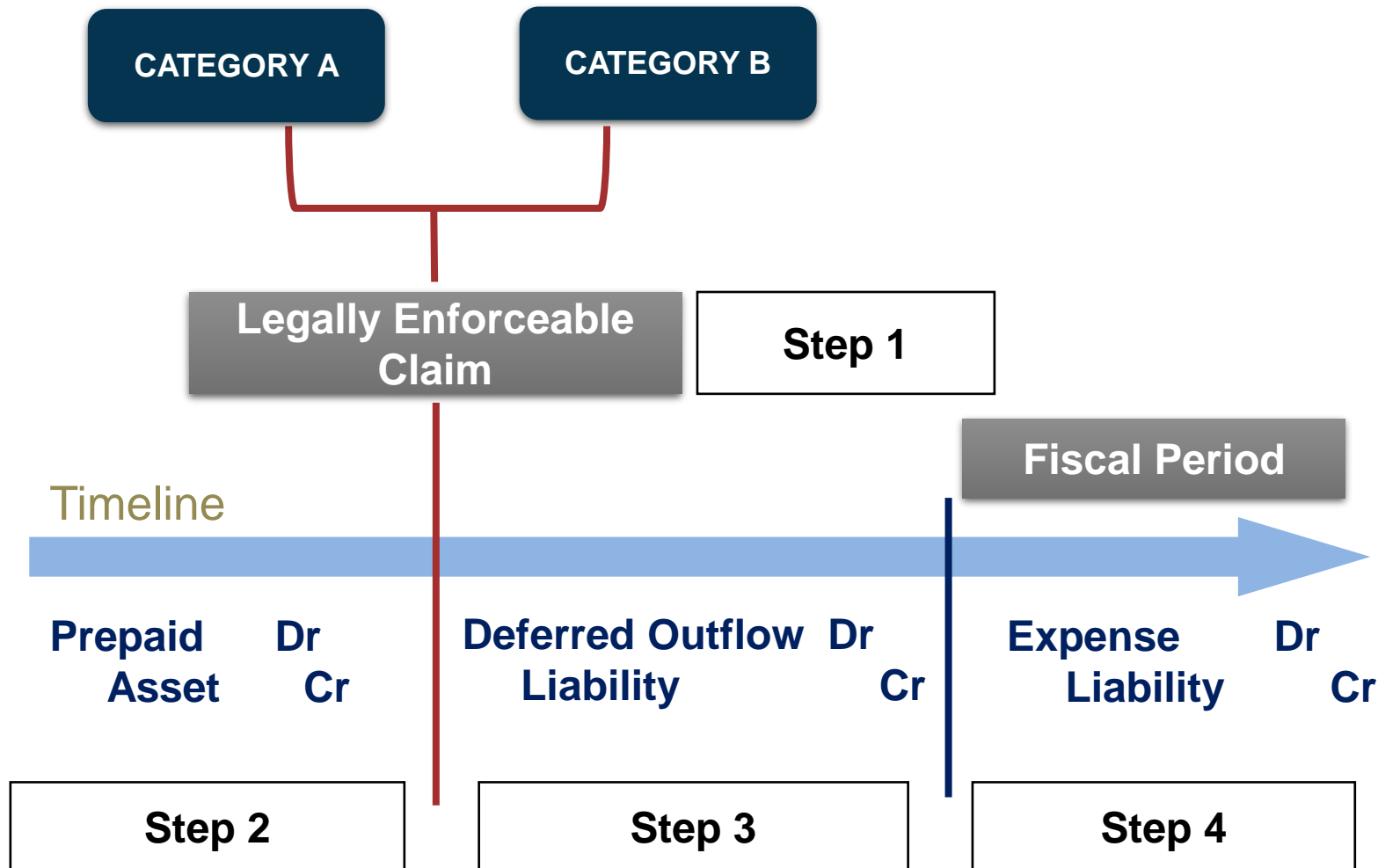
Poll Question #3

If a transaction **does not** include a binding arrangement, it could be potentially categorized as a:

- a. Category A transaction
- b. Category B transaction
- c. Category A or Category B transaction
- d. Neither a Category A nor a Category B transaction

Chapter 5 - Expense Recognition

Proposed Expense Recognition Principles



Category A Expense Recognition Examples

A performance obligation is satisfied when there is a transfer of control of resources

City orders supplies

- Expense is recognized as the city receives the supplies

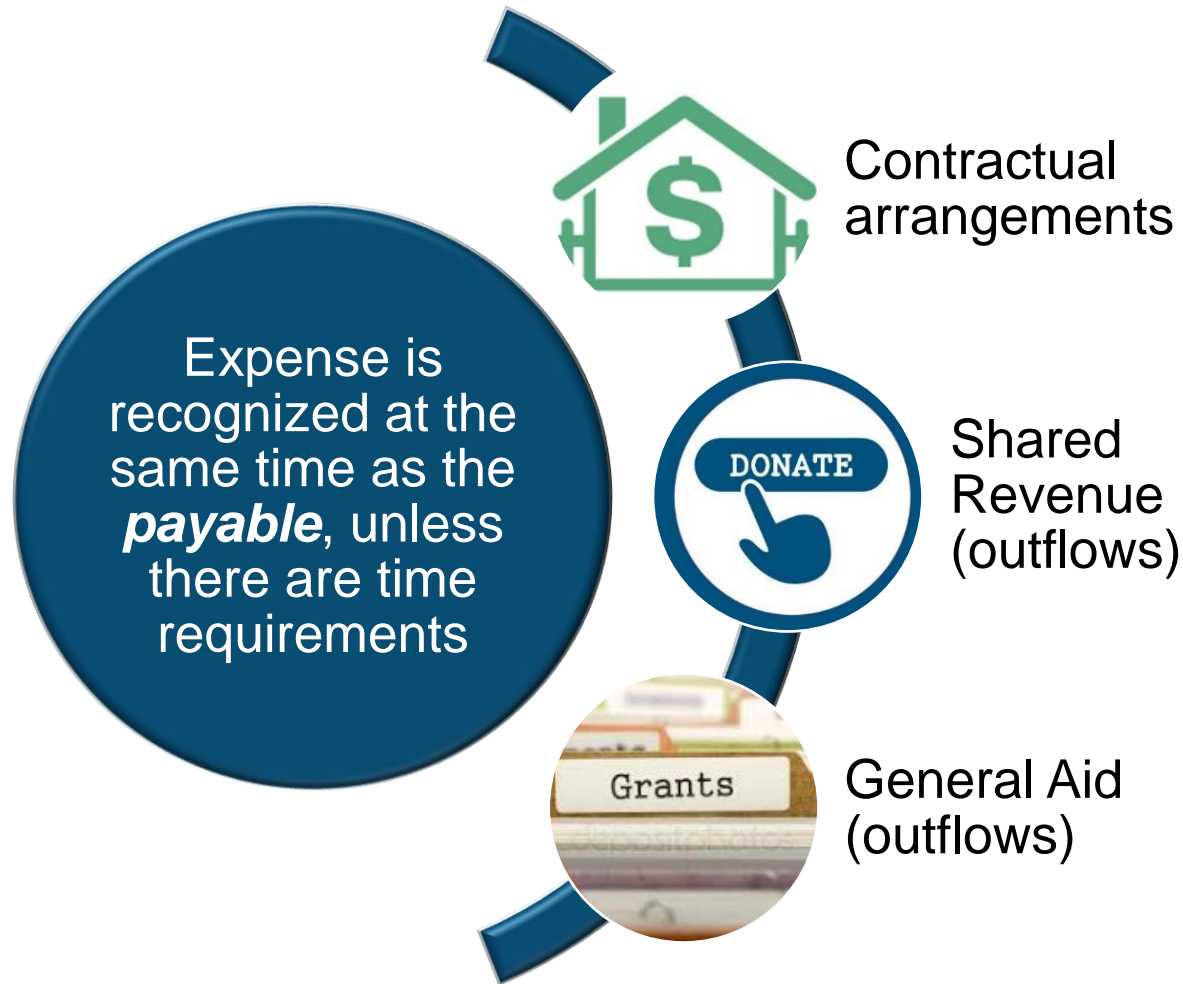
School District hires CPA

- Expense is recognized as the CPA firm carries out the expected work, such as an audit

Public Utility employees

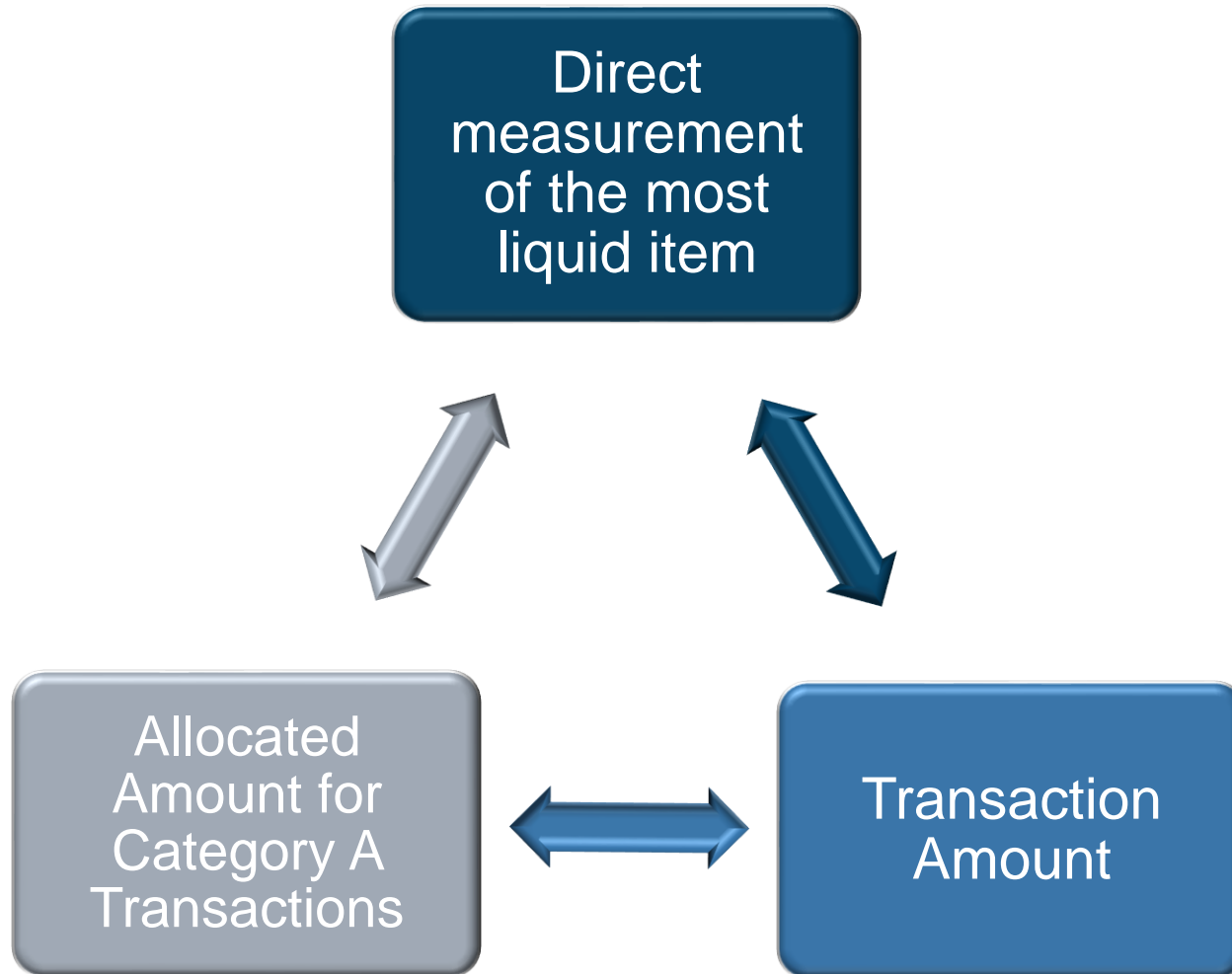
- Expenses for wages are recognized as the employees perform services over time

Category B Expense Recognition



Chapter 6 - Measurement

Proposed Measurement Principles



Measurement of the Most Liquid Item

Revenues and expenses should be measured based on the most liquid item in a transaction.

Revenue transactions would be measured by relying on the amount of consideration received or receivable:

The Asset

Expense transactions would be measured by relying on the amount of consideration paid or payable:

The Liability

Collectibility

Not included
in
categorization

Allowance for
uncollectible
amounts
(reduce
receivables)

Recognize
revenue NET
of
uncollectible
amounts

Allocation of the Transaction Amount



For Category A transactions, the transaction amount would be allocated to the performance obligations in the binding arrangement

Chapter 7 - Governmental Funds

Proposals included in the Financial Reporting Model Improvements Exposure Draft and the Recognition Concepts Statement Exposure Draft

Proposed Governmental Funds Recognition

Short-term financial resources measurement focus and accrual basis of accounting

Classify transactions as short-term or long-term

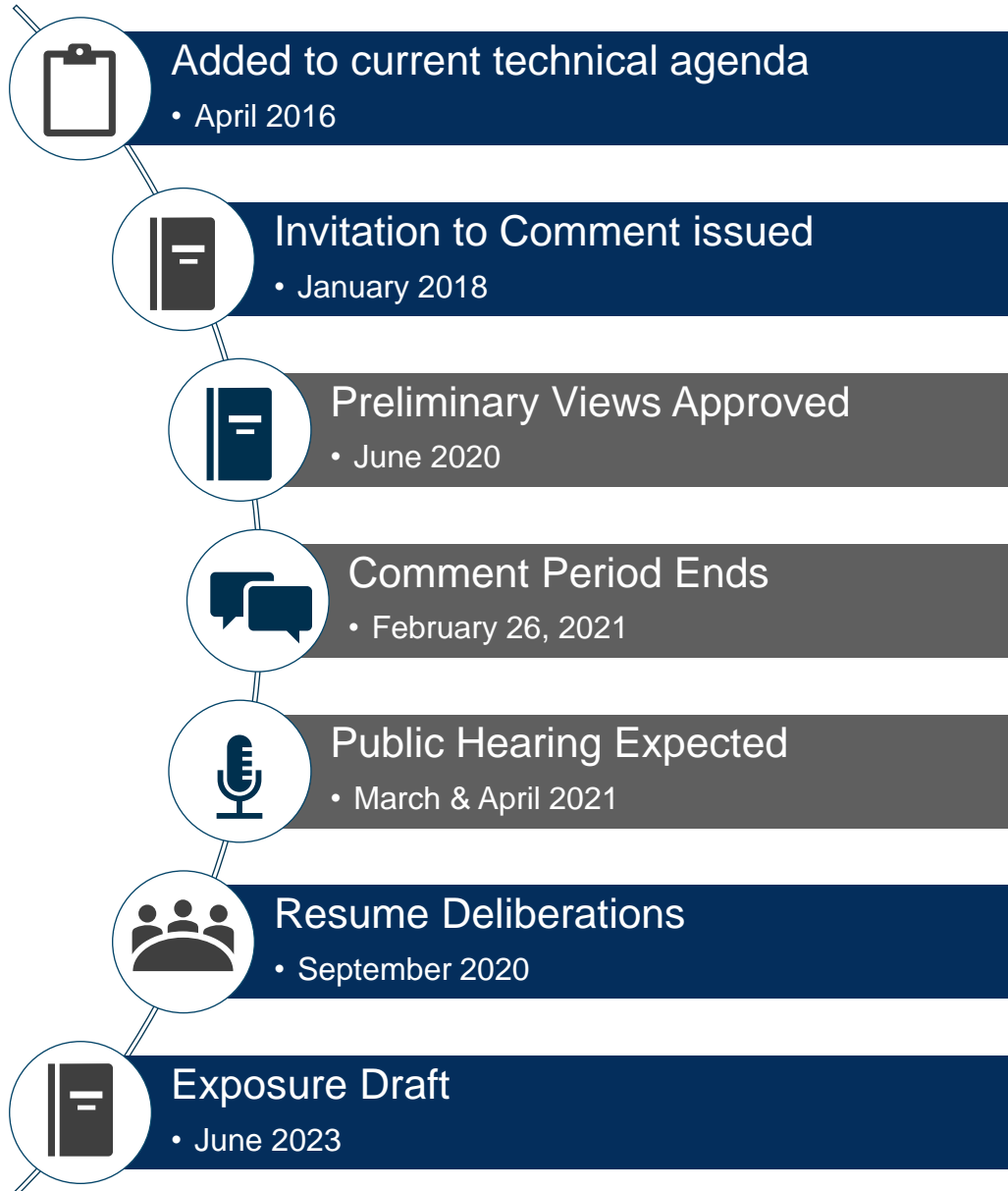
- Short term transactions are recognized in the same manner as economic measurement focus and accrual basis of accounting
- Long term transactions are recognized when due

This approach removes consideration of period of availability

Project Timeline

Field Test – two “tracks”

1. September to November 2020 for governments with December 31st FYE
2. January to March 2021 for governments with June 30th FYE



Questions?

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