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American Institute of CPAs
1455 Pennsylvania Avenue, NW
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March 11, 2011

Mr. David R. Bean
Director of Research and Technical Activities
Project No. 3-22
Governmental Accounting Standards Board
401 Merritt 7
P.O. Box 5116
Norwalk, CT 06856-5116

Dear Mr. Bean:

The American Institute of Certified Public Accountants (AICPA) has reviewed the Governmental Accounting Standards Board (GASB) Exposure Draft (ED), *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position,* and is pleased to offer its comments. Previously, we expressed concerns to the Board regarding the lack of guidance regarding the appropriate display of deferred inflows of resources and deferred outflows of resources (deferred inflows and outflows of resources) and stated a need for more guidance from the Board. However, since expressing those concerns, the Board has added to its agenda the project titled, *Deferred Inflows of Resources and Deferred Outflows of Resources Omnibus* (Omnibus project). In light of the addition of the Omnibus project, we now strongly recommend that the topics covered in the ED be combined with the Omnibus project. We believe it is premature to conclude on the appropriate financial statement presentation for deferred inflows and outflows of resources since the presentation of these elements is dependent on the conclusions ultimately reached by the Board in the Omnibus project. In the event the Board does not accept our recommendation to postpone this project, we have provided our views on the most appropriate presentation below.

Our specific comments on the ED are included in the following section of this letter. The final section of the letter titled, "Concerns to Consider with Regard to the Board's Omnibus Project," includes our comments for the Board to consider in the Omnibus project. We continue to question the use and benefit of the deferred inflows and outflows of resources elements.

Comments on the ED

***Presentation Changes Should Be Considered with Omnibus Project*.** While we acknowledge a disparity in practice in the presentation of deferred inflows and outflows of resources, we now believe the issuance of this ED is premature in light of the new Omnibus project. Our understanding of that project is that the Board is identifying, in the existing authoritative literature, balances that appear to meet the definitions in Concepts Statement No. 4, *Elements of Financial Statements,* of deferred inflows and outflows of resources. Once identified, the Board is determining whether those balances should continue to be recognized as assets or liabilities or be reclassified for financial reporting purposes as deferred inflows or outflows of resources. We believe it is inappropriate to conclude on the appropriate presentation of these elements without also understanding what might be considered deferred inflows and outflows of resources in the future. Currently, there are very few balances that are identified as meeting the definition of these elements. However, we understand that the Omnibus project could change the classification of other, more significant, balances in the future which concerns us (see related comment below in the section titled, "Concerns to Consider with Regard to the Board's Omnibus Project").

The following explains the challenge in developing a final position on the ED's conclusion. The presentation proposed by the Board in the ED displays the deferred outflows of resources reported in a separate section following assets. The ED also requires deferred inflows of resources to be reported in a separate section following liabilities. This presentation would eliminate the presentation of net assets. We understand from the Basis of Conclusions of the ED that the Board is concerned that reporting deferred inflows and outflows of resources within a single financial statement section could suggest that they are closely related and could imply an "offsetting" relationship that does not exist.

In our November 30, 2009 response to the Board's ED, *Financial Instruments Omnibus,* we proposed the following presentation for deferred inflows and outflows of resources:

- Assets;
- Liabilities;
- Net Assets (as classified based on GASB Statement No. 34, *Basic Financial Statements and Management's' Discussion and Analysis for State and Local Governments);*
- Deferred Inflows and Deferred Outflows;
- Net Position

Our position was based on the limited transactions and balances that are currently reflected as deferred inflows and outflows of resources and a desire to maintain the integrity of net assets which is important for understandability and, practically speaking, compliance with bond covenants. We also believe that placing deferred inflows and outflows of resources below net assets would emphasize the notion that these elements are neither assets nor liabilities and that the "offsetting" concern raised by the Board in the Basis for Conclusions would be overcome with a better understanding of the elements by users. Such is the case with the Statement of Revenues, Expenses, and Changes in Fund Balances where other financial sources and uses (transfers in and transfers out) are included in a single section. In our experience, current financial users are not being misled by this presentation.

However, we now understand that the Board is considering major reclassifications of balances as part of the Omnibus project. If significant transactions and balances that are currently reflected as assets or liabilities (e.g., prepaid assets and unearned revenue) were to be reclassified to deferred inflows and outflows of resources, the importance of the presentation of net assets would likely be greatly reduced and our previous position on the most appropriate presentation could change. Given the potential for significant reclassifications and also in light of the limited transactions currently considered deferred inflows and outflows of resources, we believe the most prudent approach is for the Board to postpone the ED and combine the consideration of presentation with the Omnibus project.

With that said, to the extent the Board does not accept our recommendation to postpone its decision on presentation, we would continue to support the presentation of deferred inflows and outflows of resources as outlined in our November 2009 letter to the Board (described above) which would preserve the current presentation of net assets. However, to the extent the Board ultimately reclassifies transactions that are currently assets and liabilities to deferred inflows and outflows of resources, we could alter our position. We strongly recommend that as the Board further deliberates the presentation of deferred inflows and outflows of resources that it make a careful assessment of the needs of users to determine the most appropriate and meaningful presentation.

The following comments are provided in the event the Board does not accept our recommendation to postpone the ED. Alternatively, if our postponement recommendation is accepted, the comments will assist the Board in identifying areas that should be clarified when the topics in the ED are added to the Omnibus project.

Attributable to Unspent Amount. Paragraph 10 states that if there are significant unspent debt proceeds or deferred inflows of resources at the end of the reporting period, the portion of the debt or deferred inflows of resources attributable to the unspent amount should not be included in the calculation of net investment in capital assets. We are unclear what deferred inflows of resources would be attributable to the unspent amount. The ED does not elaborate on the concept of "attributable to the unspent amount" nor is it covered in the Basis for Conclusions. We recommend that the Board add guidance to clarify this concept.

Relationship to Components of Net Position. If the Board maintains the display as presented in the ED, the Board is establishing a framework to report the various components of net position (i.e., net investment in capital assets, restricted, and unrestricted). Similar to our comments above, we have difficulty commenting on these components as we could not identify an example to illustrate the actual use of the proposal. However, we did note that paragraphs 10 and 11 of the ED do not mention deferred outflows of resources when describing the components of net position. Conceptually, it would seem that deferred outflows of resources could impact restricted amounts. Thus, we encourage the Board to add clarification to the proposed framework in paragraphs 10 and 11 with regard to deferred outflows of resources and to include an example to further illustrate the Board's intent.

Concerns to Consider with Regard to the Board's Omnibus Project

We continue to question the utility of reporting deferred inflows and outflows of resources since they are so difficult to define and differentiate from assets and liabilities. Further, it is our experience from discussing these elements with preparers and users of the financial statements that they also struggle in understanding the deferred inflows and outflows of resources elements. To highlight a specific instance in which we have such a difficulty, GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements,* classifies consideration received by a transferor as part of a service concession arrangement as a deferred inflow of resources. However, we believe it meets the definition of a liability as stated in paragraph 17 of GASB Concepts Statement No. 4. The Basis for Conclusions in GASB Statement No. 60 did not effectively clarify the matter for us.

For these reasons, we recommend that the Board give strong consideration to removing deferred inflows and outflows of resources as financial statement elements in Concepts Statement No. 4. If that is not an acceptable option, we recommend that the Board revise the definitions of these elements such that they are clear enough to ensure that other transactions and balances that are clearly assets or liabilities (e.g., prepaid assets and unearned revenue) would not meet the definition of deferred inflows or outflows of resources. Our views in this area are based on our experience in applying the current definitions and our belief that these elements add more complexity than benefit to governmental financial reporting.

However, if the Board ultimately retains the elements, we highly encourage the Board, as part of the Omnibus project, to provide a strong rationale for any reclassifications made and to avoid reclassifying elements that are clearly assets or liabilities. In our experience, most users of governmental financial statements are very familiar with the current reporting of balances such as prepaid assets or deferred revenues as assets and liabilities. If the Board were to reclassify these balances as deferred inflows and outflows of resources, guidance will be necessary to educate users as to any change in presentation and why the balances are better classified as deferred inflows or outflows of resources. Otherwise, users will have less of an understanding of governmental financial statements than they do today.

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The AICPA appreciates the opportunity to comment on the ED. This comment letter was prepared by members of the AICPA's State and Local Government Expert Panel and was reviewed by representatives of the Financial Reporting Executive Committee who did not object to its issuance. Representatives of the AICPA would be pleased to discuss these comments with you at your convenience.

Sincerely,

James C. Lanzarotta
Chair
AICPA State and Local Government
Expert Panel

Mary M. Foelster
Director
AICPA Governmental Auditing and
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cc: State and Local Government Expert Panel
Richard Paul
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