

Dear ProSystem *fx* Customer:

This *Government & Single Audit Knowledge-Based Audits™ Fall 2009 Update* is intended to provide you with the latest information as you head into your fall planning season. This update incorporates the most recent regulatory changes and decisions that may impact your government audits and should be viewed as a supplement to the KBA Government and Single Audit ProSystem *fx* Knowledge Tools Titles.

The update is organized into sections that describe each of the major changes in the governmental and single audit standards. At the end of each section, we have included a list of the affected KBA documents for your convenience.

It is our goal at CCH to keep our content as updated as possible and to deliver this updated content when it is the most relevant to our customers. Because of the varied schedule of government audits, we plan to continue to provide this update in the fall as auditors are preparing for their calendar year-end engagements. All of these changes will be incorporated in our next full release of our *Government & Single Audit Knowledge-Based Audits™* content in spring 2010.

Sincerely,

CCH, a Wolters Kluwer business

Government and Single Audit Knowledge-Based Audits Fall 2009 Update

Contents

Implementation of SAS-115 in Reporting on Internal Control over Financial Reporting and Compliance and Other Matters in Audits of Financial Statements Performed in Accordance with Government Auditing Standards.....	3
KBA Documents Affected (Government Module):	5
Issuance of 2009 OMB Circular A-133 <i>Compliance Supplement</i>	5
KBA Documents Affected (Single Audit Module):.....	7
Effect of the American Recovery and Reinvestment Act of 2009 on Circular A-133 Audits	8
KBA Documents Affected (Single Audit Module):.....	10
Update on Single Audit Electronic Data Collection Form	11
KBA Document Affected (Single Audit Module):	11
GASB Statement No. 56, Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards	12
KBA Documents Affected (Government Module):	13
GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions	14
KBA Documents Affected (Government Module):	17
Guide to Implementation of GASB Statement No. 53, Accounting and Financial Reporting for Derivative Instruments.....	17
KBA Documents Affected (Government Module):	18
Pending GASB Due Process Documents.....	18

Implementation of SAS-115 in Reporting on Internal Control over Financial Reporting and Compliance and Other Matters in Audits of Financial Statements Performed in Accordance with Government Auditing Standards

In October 2008, the American Institute of Certified Public Accountants (AICPA) Auditing Standards Board (ASB) issued [Statement on Auditing Standards No. 115 \(SAS-115\) \(AU 325\), *Communicating Internal Control Related Matters Identified in an Audit*](#), which supersedes [SAS-112](#) of the same name. [SAS-115](#) revises the [SAS-112](#) definitions of the terms “material weakness” and “significant deficiency” to be consistent with the definitions used in [Public Company Accounting Oversight Board \(PCAOB\) Auditing Standard No. 5 \(AS-5\), *An Audit of Internal Control over Financial Reporting That Is Integrated with an Audit of Financial Statements*](#), and [AICPA Statement on Standards for Attestation Engagements No. 15 \(SSAE-15\) \(AT 501\), *An Examination of an Entity’s Internal Control over Financial Reporting That Is Integrated with an Audit of Its Financial Statements*](#). [SAS-115](#) is effective for audits of financial statements for periods ending on or after December 15, 2009, with earlier implementation permitted.

[SAS-115](#) provides the following new definitions:

- A “deficiency in internal control” exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis.
- A “material weakness” is a deficiency, or combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity’s financial statements will not be prevented, or detected and corrected on a timely basis.
- A “significant deficiency” is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

[Generally accepted government auditing standards \(GAGAS\)](#) require that, in addition to providing an opinion or a disclaimer of opinion on the financial statements, auditors should: (1) report on the scope and results of testing of the entity’s internal control over financial reporting, compliance with laws, regulations, and provisions of contracts or grant agreements; and (2) report certain fraud or abuse. The Government Accountability Office (GAO) issued interim guidance that indicates the following regarding the implementation of the [SAS-115](#) definitions in the [GAGAS](#) report:

Auditors may satisfy the internal control reporting requirements in [GAGAS paragraph 5.11](#) by including in the [GAGAS](#) report on internal control all identified “material weaknesses” and “significant deficiencies” following the new definitions and requirements from [SAS 115](#) and [SSAE 15](#), as applicable, providing those definitions, and describing the scope of testing performed on the entity’s internal control over financial reporting.

In addition, the AICPA Government Audit Quality Center (GAQC) has released guidance and illustrative auditor’s reports that implement the provisions of [SAS-115](#). The GAQC guidance and illustrative reports can be viewed and downloaded at AICPA Web site (<http://gaqc.aicpa.org>).

Example reports are included in the State and Local Government Knowledge-Based Audit tools, which implement the requirements of [SAS-115](#) and the proposed wording changes included in the AICPA GAQC illustrations. These example reports include the following:

- RPT-917A: Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards (SAS-115) (*No Reportable Instances of Noncompliance or Other Matters and No Material Weaknesses or Significant Deficiencies in Internal Control over Financial Reporting Identified*);
- RPT-918A: Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards (SAS-115) (*Reportable Instances of Noncompliance or Other Matters Identified and Significant Deficiencies in Internal Control over Financial Reporting Identified, but No Material Weaknesses*); and
- RPT-918B: Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards (SAS-115) (*Reportable Instances of Noncompliance or Other Matters Identified and Material Weaknesses and Significant Deficiencies in Internal Control over Financial Reporting Identified*).

At the present time, the U.S. Office of Management and Budget (OMB) has not issued any guidance that indicates that the provisions of [SAS-115](#) can be implemented in the reporting of internal control deficiencies in the report on compliance and internal control over compliance for major programs in conjunction with audits performed in accordance with [OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations](#). Therefore, practitioners are advised not to implement the [SAS-115](#) revised definitions of material weakness and significant deficiency in the reporting of internal control over compliance in the audit of federal awards, until such OMB guidance is provided and published in the Federal Register.

KBA Documents Affected (Government Module):

KBA-104	Evaluating and Communicating Control Deficiencies, Noncompliance, and Other Matters
COR-903	Communication with Those Charged with Governance
RPT-917A RPT-918A RPT-918B	Reports on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with Government Auditing Standards (SAS-115)

Issuance of 2009 OMB Circular A-133 Compliance Supplement

In May 2009, the OMB released the [2009 OMB Circular A-133 Compliance Supplement \(2009 Compliance Supplement\)](#). The [2009 Compliance Supplement](#) is effective for audits of fiscal years beginning after June 30, 2008, and supersedes the [2008 Compliance Supplement dated March 2008](#). [Circular A-133](#) provides for the issuance of the Compliance Supplement to assist auditors in planning and performing the required federal award compliance audits, including: (1) identifying material compliance requirements; (2) determining compliance audit objectives; and (3) providing suggested compliance

audit procedures that the federal government expects to be considered as part of a [Circular A-133](#) audit. The [2009 Compliance Supplement](#) can be obtained at the OMB Web site (http://www.whitehouse.gov/omb/circulars_a133_compliance_09toc/).

Each year, the OMB updates the Compliance Supplement for new programs, deleted programs, and modified program requirements. However, this year additional changes have been made that resulted from an enhanced federal agency review process to identify areas of the Compliance Supplement that could be improved in response to the results of the federal study on single audit quality. Additionally, the [2009 Compliance Supplement](#) introduces a new appendix that includes information and guidance for auditors on the American Recovery and Reinvestment Act of 2009 (ARRA) and its implications on [Circular A-133](#) audits, as well as a discussion of the common audit deficiencies noted in such audits. [Appendix V of the 2009 Compliance Supplement, List of Changes for the 2009 Compliance Supplement](#), is a key piece of guidance to help practitioners identify all of the changes that the OMB has made. Some of the more significant changes in the [2009 Compliance Supplement](#) include the following:

- Added 5 new programs:
 - Catalog of Federal Domestic Assistance (CFDA) 10.582, Fresh Fruit and Vegetable Program;
 - CFDA 15.623, North American Wetlands Conservation Fund;
 - CFDA 15.635, Neotropical Migratory Bird Conservation;
 - CFDA 20.000, Transit Cross-Cutting Section; and
 - CFDA 20.219, Recreational Trails Program, as part of the Highway Planning and Construction Cluster.
- Deleted 6 programs:
 - CFDA 14.219, Community Development Block Grants/Small Cities Program;
 - CFDA 17.263, Youth Opportunity Grants;
 - CFDA 84.288, Bilingual Education—Program Development and Implementation Grants;
 - CFDA 84.290, Bilingual Education—Comprehensive School Grants;
 - CFDA 84.291, Bilingual Education—Systemwide Improvement Grants; and
 - CFDA 97.008, Urban Areas Security Initiative.
- Modified the applicability of compliance requirements to certain programs in [Part 2, Matrix of Compliance Requirements](#):
 - CFDA 15.042, Indian School Equalization Program (added applicability of “Reporting”);
 - CFDA 15.426, Coastal Impact Assistance Program (added applicability of “Matching, Level of Effort, Earmarking”);
 - CFDA 15.614, Coastal Wetlands Planning, Protection and Restoration Act (added applicability of “Real Property Acquisition/Relocation Assistance”);
 - CFDA 93.210, Tribal Self-Governance Program: IHS Compacts/Funding Agreements (added applicability of “Cash Management”);
 - CFDA 93.268, Immunization Grants (deleted applicability of “Eligibility”); and
 - Student Financial Aid (deleted applicability of “Subrecipient Monitoring”).
- Revised the “Purpose and Applicability—Applicability—Safe Harbor Status” section of [Part 1, Background, Purpose, and Applicability](#), and the “Overview of This Supplement” section of [Part 3, Compliance Requirements](#), to clarify that the auditor is responsible for achieving the stated audit objectives for the applicable compliance requirements and the suggested audit procedures are, as the name implies, only suggested.

- Revised [Part 3, Compliance Requirements](#), to incorporate the following:
 - Added to each section (i.e., A through M) a new subsection, “Source of Governing Requirements,” which includes references to [2 CFR Part 215](#), the [OMB Circular A-102](#) Common Rule, and other potentially applicable requirements;
 - Updated or corrected citations in Section B, “Allowable Costs/Cost Principles,” and Section C, “Cash Management”;
 - Updated Section H, “Period of Availability of Federal Funds,” and Section L, “Reporting,” to clarify or revise testing under the suggested audit procedures; and
 - Updated Section I, “Procurement and Suspension and Debarment,” and Section M, “Subrecipient Monitoring,” to clarify the requirements under [Circular A-133](#).
- Revised [Part 4, Agency Program Requirements](#), to address over 75 programs with major and minor changes, including the addition of new guidance, the removal of outdated guidance, and clarifications. [Appendix V of the 2009 Compliance Supplement](#) will help identify the relevant program changes made.
- Revised [Part 5, Cluster of Programs](#), for multiple changes to the Student Financial Aid Cluster, including the addition of CFDA 84.379, Teacher Education Assistance for College and Higher Education Grants, and corrected the title of CFDA 93.342, Health Professions Student Loans, Including Primary Care Loans and Loans for Disadvantaged Students, where applicable.
- Added new [Appendix VII, “Other OMB Circular A-133 Advisories,”](#) to include coverage of the effect of the ARRA (discussed in more detail below) based on currently available information and to describe the common audit deficiencies noted in the federal study on single audit quality.

Note: In August 2009, the OMB issued *OMB Circular A-133 Compliance Supplement Addendum #1* (Addendum #1) to amend and supplement the [2009 Compliance Supplement](#) for updated guidance on ARRA award expenditures. This addendum is discussed in detail in the section below.

It is important for the practitioner to remember that the Compliance Supplement is not considered an audit program “safe harbor.” The Compliance Supplement includes only “suggested” audit procedures. The suggested audit procedures should be considered in conjunction with other alternative or additional audit procedures when applying professional judgment to determine the most appropriate compliance audit procedures under the circumstances that are needed to achieve the stated audit objectives.

KBA Documents Affected (Single Audit Module):

KBA-400S	Identification of Material Compliance Requirements
KBA-402S through KBA-414S	Understanding Compliance Requirement-Level Controls
AUD-801S through AUD-816S	Audit Programs: Types of Compliance Requirements

Effect of the American Recovery and Reinvestment Act of 2009 on Circular A-133 Audits

In February 2009, the U.S. Congress approved and the President signed into law the ARRA, one of the most significant and far-reaching economic stimulus initiatives of recent times that will result in approximately \$300 billion dollars in additional federal funds being passed down from federal agencies to entities that are generally subject to single audits (e.g., state and local governments and institutions of higher education). Because of the magnitude of this funding and its high public profile, the ARRA mandates that there be an unprecedented amount of oversight and transparency around the spending of all ARRA funds.

The OMB expects the effects of the ARRA on [Circular A-133](#) single audits to increase significantly during calendar year 2009 and into 2010. Therefore, practitioners should be alert to determine whether audit clients (both recipients and subrecipients) have properly identified and segregated ARRA awards.

With the release of the [2009 Compliance Supplement](#), the OMB provided some guidance in new [Appendix VII, "Other OMB Circular A-133 Advisories,"](#) which is intended to highlight certain areas of the ARRA that will affect single audits. However, because of the short time period between the enactment of the ARRA and the issuance of the [2009 Compliance Supplement](#), the OMB was unable to completely revise or update the [2009 Compliance Supplement](#) for the full effect of the ARRA. Therefore, [Appendix VII](#) should be considered a "first step" in understanding the effect of the ARRA on [Circular A-133](#) single audits. The OMB has indicated that it expects to develop addenda to the Compliance Supplement and other guidance as time progresses to add new programs or modify certain sections (e.g., [Part 3, Compliance Requirements](#)) to address compliance requirement considerations of the ARRA. Therefore, when ARRA funds awards are identified, practitioners should first review [Appendix VII](#) and then follow up through a review of the OMB Web site for additional supplemental ARRA or Compliance Supplement information and guidance.

To date, the OMB has issued the following supplemental guidance:

- A memorandum dated June 22, 2009, *Implementing Guidance for the Reports on Use of Funds Pursuant to the ARRA*, which can be accessed at the OMB Web site (http://www.whitehouse.gov/omb/assets/memoranda_fy2009/m09-21.pdf). This memorandum provides guidance on ARRA reporting requirements.
- Addendum #1 dated June 30, 2009, which can be accessed at the OMB Web site (http://www.whitehouse.gov/omb/assets/a133_compliance/arra_addendum_1.pdf). This addendum supplements the [2009 Compliance Supplement](#) and provides additional guidance for programs, including clusters of programs, with expenditures of ARRA awards. Addendum #1 is effective for single audits of fiscal years beginning after June 30, 2008 (i.e., for June 30, 2009 single audits and periods ending thereafter) and should be used in conjunction with the other parts and appendixes of the [2009 Compliance Supplement](#).

Based on the guidance available at the present time, including Addendum #1, some of the most significant considerations for practitioners in the conduct of [Circular A-133](#) single audits related to the effects of ARRA awards include the following:

- **Effect on CFDA numbers.** [Appendix VII of the 2009 Compliance Supplement](#) indicates that federal agencies are required to specifically identify ARRA awards, regardless of whether the

funding is provided under a new or existing CFDA number. Addendum #1 supplements and amends [Part 2 of the 2009 Compliance Supplement, Matrix of Compliance Requirements](#), and [Part 4, Agency Program Requirements](#), by identifying ARRA-funded programs by **bolding** the program number and name. These bolded items include new CFDA numbers for new ARRA programs or clusters and existing CFDA numbers for programs or clusters that are ARRA funded and for which ARRA compliance requirements have been added.

- **Effect on federal award clusters.** In Addendum #1, the OMB has indicated that it will need to update the clustering guidance in [Part 5 of the 2009 Compliance Supplement, Clusters of Programs](#), because many of the ARRA awards will have new CFDA numbers even though they may be additions to and share common compliance requirements with an existing program. Addendum #1 updated [Part 5](#) by showing all new or revised clusters with ARRA funded programs displayed in **bold**, as well as providing specific ARRA cluster considerations or revisions for Student Financial Assistance, Research and Development, and Child Nutrition clusters.
- **Effect on major program determination.** [Appendix VII](#) describes the effect of ARRA award expenditures on major program determination. Generally, two scenarios could arise: (1) one CFDA number could be used for combined non-ARRA and ARRA funds; or (2) a new CFDA number could be used for the ARRA funds. In the first case, [Appendix VII](#) states that the auditor should consider all federal programs with expenditures of ARRA funds to be programs of higher risk in accordance with [Sections .525\(c\)\(2\) and .525\(d\) of Circular A-133](#). Also, when performing the risk-based approach under [Section .520\(c\)\(1\)](#), Type A programs with expenditures of ARRA funds should “not” be considered low risk except when the auditor determines, and clearly documents the reasons, that the expenditure of ARRA funds is low risk for the program. In the second case, [Appendix VII](#) states that for situations in which an ARRA CFDA number has been added to a cluster, the ARRA CFDA number should be considered a new program and the cluster would not qualify as a low-risk Type A program. Therefore, the cluster will not meet the requirement of having been audited in one of the last two audit periods and will have to be audited as a major program (assuming it is a Type A program).
- **Effect on determining applicable compliance requirements.** [Appendix VII](#) emphasizes that compliance requirements unique to the ARRA are not included in the 2009 Compliance Supplement. Therefore, auditors should: (1) review the award documents, including the terms and conditions; (2) check the OMB Web site for any addenda to the [2009 Compliance Supplement](#); and (3) use the framework provided by the [2009 Compliance Supplement](#) (e.g., in Parts 3, 4, 5, and 7) as guidance to identify ARRA compliance requirements material to the federal program and to determine the appropriate audit procedures. With the issuance of Addendum #1, the OMB has provided additional guidance and modifications to the [2009 Compliance Supplement](#) compliance requirements that:
 - Add new cross-cutting provisions (with new language shown in **bold**) to the following types of compliance requirements: (1) Activities Allowed or Unallowed; (2) Davis-Bacon Act; (3) Procurement and Suspension and Debarment; (4) Subrecipient Monitoring; and (5) Special Tests and Provisions.
 - List three new ARRA compliance requirements (i.e., R1, R2, and R3) to Special Tests and Provisions that apply to all programs expending ARRA awards (and should be added to Part 4 or Part 7 guidance) in addition to providing related audit objectives and suggested audit procedures for these new requirements.
 - Indicate that the new reporting requirements imposed by the ARRA are not applicable for audit periods with ending dates in June, July, and August of 2009, but that an additional addendum would be issued later addressing the reporting requirements and related audit

objectives and suggested procedures. For preliminary reporting guidance, refer to the June 22, 2009, OMB document, *Implementing Guidance for the Reports on Use of Funds Pursuant to the ARRA*.

- **Effect on the SEFA and DCF.** [Appendix VII](#) states that federal agencies (and recipients passing ARRA funds to subrecipients) are required to include specific ARRA requirements in their terms and conditions for ARRA awards to ensure separate identification in both the schedule of expenditures of federal awards (SEFA) and the data collection form (DCF). Generally, ARRA award terms and conditions require recipients to accomplish this by: (1) identifying ARRA expenditures separately on the SEFA; (2) identifying ARRA expenditures as separate rows under Item 9 of Part III of the DCF by CFDA number; and (3) including the prefix “ARRA-” in identifying the name of the federal program on the SEFA and as the first characters in Item 9d of Part III on the DCF. Addendum #1 also provides the added requirements for ARRA presentation matters in the SEFA and DCF, in addition to the requirements for recipients to separately identify (and document) to each subrecipient at the time of a subaward the federal award and CFDA numbers, and the amount of ARRA funds, as well as requiring subrecipients to meet the SEFA and DCF presentation requirements.
- **Effect on internal control guidance.** Addendum #1 also provides added emphasis related to internal control testing over compliance in regards to major programs funded with ARRA awards. This guidance to auditors includes the following:
 - Encouragement of interim communication to promptly notify auditee management (i.e., during the audit rather than merely at the engagement end in the auditor’s report) of any internal control significant deficiencies or material weaknesses identified that are related to ARRA funded programs.
 - Guidance to consider the entity’s control environment and other control activities in addressing the risks related to noncompliance with the requirements related to Activities Allowed or Unallowed, Allowable Costs and Cost Principles, and Eligibility that may exist because of: (1) the newness of the ARRA program; (2) the rapid growth in program funding; (3) changes in regulatory environment; and (4) similar risks.
 - Guidance to consider not only the volume of ARRA funding in the current audit period, but also the future anticipated volume, when evaluating the likelihood and magnitude of control deficiencies.

An ARRA page is available at the GAQC Web site (<http://gaqc.aicpa.org/Resources/Recovery+Act+Resource+Center.htm>), which is dedicated to helping its members locate auditor resources and information related to the ARRA and its effect on single audits.

KBA Documents Affected (Single Audit Module):

KBA-104S	Circular A-133 Compliance Audit Significant Matters
KBA-302S	Understanding the Entity and Its Program Environment
KBA-400S	Identification of Material Compliance Requirements
AID-301S	Determining Single Audit Applicability
AID-303S	Determining Major Programs

Update on Single Audit Electronic Data Collection Form

Practitioners should remember that beginning with 2008 fiscal year-ends and forward, paper submissions of the single audit DCF required under [Circular A-133](#) are no longer accepted by the Federal Audit Clearinghouse (FAC). Only electronic submissions of the DCF and the required reporting package through the (FAC) Internet Data Entry System (IDES) are accepted.

For audit periods ending in 2004, 2005, 2006, and 2007, the previous version of the DCF should be used. It can be accessed at the FAC Web site (<http://harvester.census.gov/fac/>) by clicking on the Data Collection Form Options link. Further, reporting packages for previous fiscal periods ending prior to 2008 must be mailed in hard copy. However, for 2008 fiscal year-end submissions and beyond, all submissions must be in electronic form, and there will no longer be any paper copy submissions of the DCF and reporting package to the FAC.

The new IDES instructions for DCF submissions for 2008 and beyond are available at http://harvester.census.gov/fac/collect08/main_instruct.pdf and include the following:

- Chapter 1: Important Notes for Using the Internet Data Entry System;
- Chapter 2: Create a Report ID and New Form;
- Chapter 3: Update a Form From a Previous Session;
- Chapter 4: Enter Data in the Form SF-SAC;
- Chapter 5: How to Upload Page 3 (Optional);
- Chapter 6: How to Upload Page 4 Multiple EINs (Optional);
- Chapter 7: How to Upload Page 4 Multiple DUNS (Optional);
- Chapter 8: Check Data, Correct Errors & Print Draft Pages;
- Chapter 9: Upload the PDF File of the Audit Report;
- Chapter 10: Certify Form SF-SAC;
- Chapter 11: File a Revised Submission;
- Appendix I-A & I-B: Federal Agency Two-Digit Prefix Listing;
- Appendix II: Contact Information;
- Glossary; and
- Index.

To use the IDES, auditees and auditors must have Internet access and valid e-mail accounts. They must also have the ability to upload a PDF file to the IDES. Cookies must be enabled in the Internet browser to allow proper data transfers between the sending computer and the IDES. Instructions on how to enable cookies are provided in the IDES instructions. Before final submission of the DCF and reporting package (i.e., once both the auditee and auditor are ready to begin the certification process), the IDES will send an e-mail to the auditee and auditor, certifying officials with a unique number that will serve as a signature code.

KBA Document Affected (Single Audit Module):

GASB Statement No. 56, Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards

[Governmental Accounting Standards Board \(GASB\) Statement No. 56 \(GASB-56\), Codification of Accounting and Financial Reporting Guidance Contained in the AICPA Statements on Auditing Standards](#), incorporates the current AICPA audit literature guidance in three areas: (1) related party transactions; (2) subsequent events; and (3) going concern considerations. [GASB-56](#) was effective upon its issuance in March 2009.

Related Party Transactions

[GASB-56](#) incorporates the current AICPA disclosure guidance that references National Council on Governmental Accounting Interpretation No. 6 (NCGAI-6), *Notes to the Financial Statements*, and *Statement of Financial Accounting Standards No. 57 (FAS-57), Related Party Disclosures*, as its basis for disclosing related party transactions.

[GASB-56](#) concurs with the AICPA assessment that such related party considerations should focus on substance over form but recognizes that such assessments may pose challenges in a governmental context (e.g., governments often enter into transactions or engage in activities that are motivated by the needs of the public good or society concerns which may not have similar characteristics with the same transactions or activities occurring in an arm's length transaction in the nongovernmental sector or with unrelated parties).

Subsequent Events

[GASB-56](#) identifies and describes the accounting and disclosure treatment for the two types of subsequent events, as discussed in AICPA audit literature: (1) "type one events" that require adjustments to the financial statements (renamed "recognized" events in [GASB-56](#)); and (2) "type two events" that do not require financial statement adjustments but may require disclosure in the notes to the financial statements (renamed "non-recognized" events in [GASB-56](#)).

Recognized Event. This type of subsequent event provides additional evidence with respect to conditions that exist at the date of the financial statements and affect the estimates that were used in the preparation of the financial statements (i.e., the settlement of a lawsuit related to an event that occurred prior to the date of the financial statements). For recognized subsequent events, the financial statements should be adjusted for any changes in estimates resulting from this new evidence.

Nonrecognized Event. This type of subsequent event provides evidence with respect to conditions that did not exist at the financial statement date but arose subsequent to that date. These subsequent events do not result in an adjustment to the financial statement amounts but should be disclosed in the notes to the financial statements if they are considered essential to a user's understanding of the statements. For example, changes in the quoted market prices of a government's investments subsequent to year-end would generally not require adjustments to the financial statement amounts

because the change in market value typically reflects a concurrent evaluation of new conditions. However, this change in market value should be disclosed in the notes to the financial statements if it is considered significant and essential to a user’s understanding of the statements.

[GASB-56](#) also states that subsequent events may need to be included in management’s discussion and analysis depending on the specific facts and circumstances.

Going Concern Considerations

[GASB-56](#) incorporates the current AICPA guidance that defines the financial statement preparer’s responsibility to evaluate whether there is substantial doubt about the government’s ability to continue as a going concern for a reasonable period of time beyond the date of the financial statements. The GASB essentially retained the AICPA definition of “reasonable period of time” (i.e., 12 months beyond the financial statement date), but added some additional language indicating that if there is information that is currently known to the government that may raise substantial doubt shortly thereafter (e.g., within an additional 3 months), it should also be considered. [GASB-56](#) also provides guidance that is tailored to the going concern considerations that are unique to state and local governments. [GASB-56](#) clarifies that the going concern considerations are to be applied at the “legal entity level,” or in other words to a legally separate governmental entity, rather than the reporting units within the legally separate governmental entity.

If it is concluded that there is substantial doubt about the government’s ability to continue as a going concern, [GASB-56](#) requires consideration of the governmental environment, specific note disclosures and a discussion of such issues in management’s discussion and analysis. The specific required note disclosures include:

- Pertinent conditions and events giving rise to the assessment of substantial doubt about the government’s ability to continue as a going concern for a reasonable period of time;
- The possible effects of such conditions and events;
- Government officials’ evaluation of the significance of those conditions and events and any mitigating factors;
- Possible discontinuance of operations;
- Government officials’ plans, including relevant prospective financial information; and
- Information about the recoverability or classification of recorded asset amounts or the amounts or classification of liabilities.

KBA Documents Affected (Government Module):

KBA-901D	Financial Statement Presentation and Disclosures Checklist Part IV: Other Financial Statement Topics and Disclosures
AUD-814	Audit Program: Related Party Transactions, Commitments and Contingencies, Estimates, and Concentrations
AUD-901	Audit Program: Subsequent Events
AUD-902	Audit Program: Going Concern

GASB Statement No. 54, Fund Balance Reporting and Governmental Fund Type Definitions

[GASB Statement No. 54 \(GASB-54\), *Fund Balance Reporting and Governmental Fund Type Definitions*](#), changes fund balance presentation and disclosures for governmental funds and clarifies the definitions of the governmental fund types. The requirements of [GASB-54](#) are effective for financial statements for periods beginning after June 15, 2010, with early implementation encouraged.

Fund Balance Classifications

[GASB-54](#) introduces entirely new terminology and classification of fund balances in governmental funds to replace the previous classifications of “reserved,” “unreserved,” “designated,” and “undesignated.” In addition to identifying the portion of fund balance that is nonspendable, the new standards establish a hierarchy of fund balance classifications based primarily on the extent to which a government is bound to observe spending constraints imposed on how resources reported in governmental funds may be used. [GASB-54](#) distinguishes between fund balance amounts that: (1) are considered nonspendable because they are not available for current use (e.g., fund balance associated with inventories and long-term receivables); and (2) are available for use but are classified based on the relative strength of the constraints that control the purposes for which specific amounts can be spent. Beginning with the most binding constraints, these classifications are: (1) restricted; (2) committed; (3) assigned; and (4) unassigned.

The fund balance classifications are further defined below:

- ***Nonspendable fund balance.*** Amounts that cannot be spent because they are either: (1) not in spendable form; or (2) legally or contractually required to be maintained intact (i.e., inventories, prepaid amounts, long-term receivables, property held for resale, or the corpus or principal of a permanent fund).
- ***Restricted fund balance.*** Amounts that are constrained by external parties (i.e., creditors, grantors, contributors, or laws or regulations of other governments), or by constitutional provision, or enabling legislation for a specific purpose, pursuant to the definition of “restricted” in [paragraph 34 of GASB Statement No. 34 \(GASB-34\), *Basic Financial Statements—and Management’s Discussion and Analysis—for State and Local Governments*](#), as amended by [GASB Statement No. 46 \(GASB-46\), *Net Assets Restricted by Enabling Legislation*](#) (i.e., amounts that can be spent only for specific purposes pursuant to a state law, grant agreement, or donor agreement).
- ***Committed fund balance.*** Amounts that are constrained for specific purposes imposed by a formal action of the government’s highest level of decision-making authority (i.e., amounts that have been committed by a governing body legislation, ordinance, or resolution for a specific purpose, such as an amount from specific park and recreation revenues committed by resolution to be used only for park maintenance).
- ***Assigned fund balance.*** Amounts that are constrained by the government’s intent to be used for a specific purpose. Intent should be expressed by: (1) the governing body itself; or (2) a body (i.e., a budget or finance committee) or official to which the governing body has delegated the authority to assign amounts to be used for specific purposes (i.e., these amounts are intended

to be used by a government for specific purposes but do not meet the criteria to be classified as restricted or committed, such as an amount set aside by management to fund a projected budgetary deficit in a subsequent year's budget).

- **Unassigned fund balance.** The residual classification for a government's general fund, which includes all amounts that are not constrained as reported in the other classifications.

Fund Balance Disclosures

[GASB-54](#) requires that governments disclose the following information about their fund balance classification policies and procedures and other related information in the notes to the financial statements:

- **For committed fund balance.** The notes should disclose: (1) the government's highest level of decision-making authority; and (2) the formal action that is required to be taken to establish (and modify or rescind) a fund balance commitment.
- **For assigned fund balance.** The notes should disclose: (1) the body or official authorized to assign amounts to a specific purpose; and (2) the policy established by the governing body pursuant to which that authorization is given.
- **For all the classifications of fund balances.** The notes should disclose: (1) whether the government considers restricted or unrestricted amounts to have been spent when an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available; and (2) whether committed, assigned, or unassigned amounts are considered to have been spent when an expenditure is incurred for purposes for which amounts in any of those unrestricted fund balance classifications could be used.
- **For nonspendable fund balance displayed in the aggregate on the face of the balance sheet.** The notes should disclose the amounts for the two nonspendable components (i.e., (1) not in spendable form; or (2) legally or contractually required to be maintained intact), if applicable. If restricted, committed, or assigned fund balances are displayed in the aggregate, specific purposes information not portrayed on the face of the balance sheet should be disclosed.
- **For established stabilization arrangements.** Even if a stabilization arrangement does not meet the criteria to be classified as restricted or committed, the government should disclose the following information in the notes to the financial statements: (1) the authority for establishing stabilization arrangements (e.g., by statute or ordinance); (2) the requirements for additions to the stabilization amount; (3) the conditions under which stabilization amounts may be spent; and (4) the stabilization balance, if not apparent on the face of the financial statements.
- **For a formally adopted minimum fund balance policy.** If the governing body has formally adopted a minimum fund balance policy (e.g., in lieu of separately setting aside stabilization amounts), the government should describe in the notes to its financial statements the policy established by the government that sets forth the minimum amount.
- **For funds that use encumbrance accounting.** Encumbrances should be disclosed in the notes to the financial statements by major funds and nonmajor funds in the aggregate.

Governmental Fund Type Definitions

[GASB-54](#) includes a number of changes to the current definitions of governmental funds, including the general fund, special revenue funds, capital projects funds, debt service funds, and permanent funds. The changes in definitions are summarized in the following table:

Fund Type	Current Definition	GASB-54 Definition
General Fund	To account for all financial resources except those required to be reported in another fund.	To account for and report all financial resources not accounted for and reported in another fund.
Special Revenue Funds	To account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted to expenditure for specified purposes.	To account for and report the proceeds of specific revenue sources that are restricted or committed to expenditure for specified purposes other than debt service or capital projects.
Capital Project Funds	To account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments).	To account for and report financial resources that are restricted, committed, or assigned to expenditure for capital outlays, including the acquisition or construction of capital facilities and other capital assets.
Debt Service Funds	To account for the accumulation of resources for, and the payment of, general long-term debt principal and interest.	To account for and report financial resources that are restricted, committed, or assigned to expenditure for principal and interest.
Permanent Funds	To report resources that are legally restricted to the extent that only the earnings, and not the principal, may be used for purposes that support the reporting government's programs (i.e., for the benefit of the government or its citizenry).	To account for and report resources that are restricted to the extent that only earnings, and not principal, may be used for purposes that support the reporting government's programs (i.e., for the benefit of the government and its citizenry).

The most significant [GASB-54](#) definition change is for "special revenue funds." [GASB-54](#) indicates the term "proceeds of specific revenue sources" establishes that one or more specific restricted or committed "revenues" should be the foundation for a special revenue fund. These restricted or committed specific revenue sources may be initially received in another fund and subsequently distributed to and recognized as revenue in a special revenues fund where they will be expended. The restricted or committed specific revenue sources should be expected to continue to comprise a substantial portion of the fund's inflows or fund balances. Use of a special revenue fund should be discontinued (and the fund's remaining resources reported in the general fund) if the government no longer expects a substantial portion of the inflows to be derived from the restricted or committed revenue sources. If one of the major funds is a special revenue fund, the notes should: (1) disclose the purpose of each major fund; and (2) identify which revenues and other resources are reported in each of those funds.

KBA Documents Affected (Government Module):

KBA-901B	Financial Statement Presentation and Disclosures Checklist Part II: Fund Financial Statements
KBA-901D	Financial Statement Presentation and Disclosures Checklist Part IV: Other Financial Statement Topics and Disclosures
AUD-811	Audit Program: Fund Equity and Net Assets

Guide to Implementation of GASB Statement No. 53, Accounting and Financial Reporting for Derivative Instruments

Realizing the complexity of the new accounting and financial reporting standards for derivative instruments applicable to state and local governments resulting from the issuance of [GASB Statement No. 53 \(GASB-53\), Accounting and Financial Reporting for Derivative Instruments](#), the GASB staff has prepared the [Guide to Implementation of GASB Statement 53 on Accounting and Financial Reporting for Derivative Instruments \(GASB-53 Guide\)](#) to assist financial statement preparers and attestors in adapting to the new requirements. The questions and answers in the [GASB-53 Guide](#) serve two purposes: (1) they are ready references for implementers who may encounter similar questions or situations; and (2) they provide a basis for resolving issues that an implementer may apply to a question or situation not specifically addressed in the [GASB-53 Guide](#).

The GASB's Implementation Guides are intended to be used as reference guides and instructional tools. They are prepared by the GASB staff and then cleared by the GASB prior to issuance. As a result, they are presently considered Category (d) in the hierarchy of generally accepted accounting principles (GAAP) as defined in [GASB Statement No. 55 \(GASB-55\), The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments](#). While the questions and answers in the [GASB-53 Guide](#) are considered Category (d) GAAP, the illustrative examples and exercises accompanying the text are nonauthoritative guidance. The questions and answers included within the [GASB-53 Guide](#) are organized by topical area, including:

- Definition of Derivative Instruments;
- Financial Instruments Not Included in the Scope of [GASB-53](#);
- Recognition and Measurement of Derivative Instruments;
- Hedging Derivative Instruments;
- Hybrid Instruments;
- Notes to Financial Statements; and
- Effective Date and Transition.

A copy of the [GASB-53 Guide](#) (Product Code No. GQA53) can be purchased from the GASB Web site (www.gasb.org).

KBA Documents Affected (Government Module):

KBA-901D	Financial Statement Presentation and Disclosures Checklist Part IV: Other Financial Statement Topics and Disclosures
AUD-818	Audit Program: Derivative Instruments

Pending GASB Due Process Documents

The GASB has recently issued a number of due process documents dealing with specific accounting and financial reporting topics, including the following Exposure Drafts (EDs), Invitations to Comment (ITCs), and other proposals:

- Pension Accounting and Financial Reporting;
- OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans;
- Accounting and Financial Reporting for Chapter 9 Bankruptcies;
- Accounting and Financial Reporting for Service Concession Arrangements;
- Financial Instruments Omnibus; and
- Proposed Suggested Guidelines for Voluntary Reporting—SEA Performance Information.

Pension Accounting and Financial Reporting. This ITC reexamines the issues of pension accounting and financial reporting established in 1994 with the issuance of [GASB Statement No. 25 \(GASB-25\), *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*](#), and [GASB Statement No. 27 \(GASB-27\), *Accounting for Pensions by State and Local Governmental Employers*](#).

The ITC is designed to elicit comments at an early stage of the GASB’s reexamination of pension accounting and financial reporting standards. It addresses several key issues and questions related to pension accounting and financial reporting, including: (1) the fundamental issue of which defined benefit pension processes, transactions, or other events should be the focus of financial reporting; (2) the recognition of employers’ pension liabilities and expenses; (3) alternative approaches to the measurement of pension obligations for accounting and financial reporting purposes; (4) the use of actuarial methods in accounting measurement approaches that involve the amortization of pension costs; (5) issues specific to employers’ participation in cost-sharing multiple-employer pension plans; and (6) issues specific to accounting and financial reporting by defined benefit pension plans.

OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans. This ED addresses issues related to the measurement of other post-employment benefits (OPEB) obligations by employers participating in agent multiple-employer OPEB plans and would amend or clarify existing OPEB standards related to such plans and plan participants. Specifically, it amends or clarifies issues related to: (1) the circumstances in which certain agent employers are eligible to use the alternative measurement method; (2) the requirement that a defined benefit OPEB plan obtain an actuarial valuation; and (3) requirements in the existing OPEB standards regarding the frequency and timing of determining OPEB measures by agent multiple-employer plans and participating employers.

Accounting and Financial Reporting for Chapter 9 Bankruptcies. This ED proposes new standards that would provide guidance for state and local governments that have petitioned for protection from

creditors by filing for bankruptcy under Chapter 9 of the U.S. Bankruptcy Code (Chapter 9). It would establish requirements for: (1) recognizing and measuring the effects of the bankruptcy process on assets and liabilities; and (2) classifying changes in those asset and liability items and related costs.

Accounting and Financial Reporting for Service Concession Arrangements. This ED proposes new standards that would establish accounting and financial reporting requirements for these types of partnership arrangements between governments and private entities and between multiple governmental entities. The ED includes proposed guidance on: (1) determining whether the transferor should report the facility subject to the service concession arrangement (SCA) as its capital asset; (2) reporting guidance for addressing upfront or installment payments related to the SCA; and (3) reporting guidance for governments acting as operators in an SCA.

Financial Instruments Omnibus. This ED proposes revisions to existing standards on financial instruments intended to update and improve the standards regarding financial reporting and disclosure requirements of some financial instruments for which significant issues have been identified in practice, including: (1) unallocated insurance contracts; (2) certain external investment pools (i.e., 2a7-like pools); (3) interest rate risk disclosures for investments in mutual funds; and (4) financial instruments within the scope of the new derivative instruments standards.

Proposed Suggested Guidelines for Voluntary Reporting—SEA Performance Information. The purpose of the proposal document is to obtain feedback from constituents on suggested guidelines intended to provide a common framework for the effective external communication of service efforts and accomplishments (SEA) performance information. The overall goal of reporting SEA performance information is to provide more information about a government's actual performance and accomplishments in providing services to its citizens than can be derived from the information included in traditional financial statements. To accomplish this goal, the GASB has developed proposed reporting guidelines for the voluntary communication of government performance. The GASB has indicated that its intent is to establish guidelines for "reporting" performance measurement not to establish "performance standards." The GASB is seeking feedback on the suggested guidelines, which include what the GASB has identified as: (1) the four essential components of an effective SEA report; (2) the six qualitative characteristics of SEA performance information; and (3) the three keys to effective communication of SEA performance information.

Public Comment Deadlines

The deadlines for submitting written comments on the due process documents are as follows:

- Pension Accounting and Financial Reporting (comments due by July 31, 2009);
- OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans (comments due by August 28, 2009);
- Accounting and Financial Reporting for Chapter 9 Bankruptcies (comments due by August 28, 2009);
- Accounting and Financial Reporting for Service Concession Arrangements (comments due by September 30, 2009);
- Financial Instruments Omnibus (comments due by October 30, 2009); and



- Proposed Suggested Guidelines for Voluntary Reporting—SEA Performance Information (comments due by October 30, 2009).

The due process documents and related instructions for submitting written comments to the GASB can be downloaded free of charge at the GASB Web site (www.gasb.org/exp).