

Annual state and local government accounting update – What's new and what's next?

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Today's presenter



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Learning objectives

- After completing this program, you should
 - Have a better understanding of recent accounting and reporting developments and issues impacting state and local governments
 - To address applicable standards in the preparation of the financial statements of a state or local government reporting entity
 - To prepare for implementation of applicable standards with future effective dates

Agenda and topics

- Accounting and reporting standards – GASB update
 - Recently issued and effective for period ending in 2014
 - Issued with future effective dates
 - Future projects

GASB 65, Items Previously Reported as Assets and Liabilities – REMINDER

- Issued – April 2012
- Effective – **Periods beginning after Dec.15, 2012**
- To provide guidance on which balances, currently reported as assets or liabilities should be reported as
 - Deferred outflows of resources
 - Deferred inflows of resources
- Limits use of term “deferred”

GASB 65, continued

- Deferred outflows of resources
 - Debit amount resulting from a refunding of debt (Statement 23)
 - Intra-entity transfers of future revenues reported by the transferee (Statement 48)
 - The loss resulting from sale-leaseback transactions (Statement 62)
 - Net balance (debit) of direct loan origination costs for mortgage loans held for resale prior to the point of sale (Statement 62)
 - Fees paid to permanent investors to ensure the ultimate sale of loans prior to the point of sale (Statement 62).
 - Advance payments made to other governments related to government-mandated and voluntary nonexchange transactions when time requirements are the only eligibility requirements that have not been met by the other government (Statement 33).

GASB 65, continued

- Outflows of resources
 - Acquisition costs for insurance entities and public entity risk pools (Statement 62 and Statement 10)
 - Initial direct costs of operating leases (Statement 62)
 - Debt issuance costs (Statement 62)
 - Net balance (debit) of direct loan origination costs related to lending activities (Statement 62)
 - Net balance (debit) of direct loan origination costs for mortgage loans held for investment (Statement 62)
 - Net balance (debit) of direct loan origination costs for mortgage loans held for resale after the sale occurs (Statement 62)
 - Fees paid related to a purchased loan or a group of loans (Statement 62)
 - Fees paid to permanent investors to ensure the ultimate sale of loans after the ultimate sale occurs (Statement 62)

GASB 65, continued

- Deferred inflows of resources
 - Advance payments received related to imposed nonexchange transactions (Statement 33)
 - Credit amount resulting from a refunding of debt (Statement 23)
 - Proceeds from the sale of future revenues to parties outside the financial reporting entity and intra-entity transfers of future revenues (Statement 48)
 - Unavailable revenue related to the application of modified accrual accounting (Statement 6 and Statement 33)
 - Gain resulting from sale-leaseback transactions (Statement 62)
 - Net balance (credit) of loan origination fees, including any portion related to points, for mortgage loans held for resale prior to the point of sale (Statement 62)
 - Net balance (credit) of loan origination fees related to points for lending activities and mortgage loans held for investment (Statement 62)
 - Resources generated by current rates intended to recover costs that are expected to be incurred in the future (Statement 62)
 - Gains or other reductions of net allowable costs intended to reduce rates over future periods (Statement 62)
 - Advance payments received from other governments related to government-mandated and voluntary nonexchange transactions when time requirements are the only eligibility requirements that have not been met (Statement 33)

GASB 65, continued

- Inflows of resources
 - Net balance (credit) of loan origination fees, excluding any portion related to points, related to lending activities (Statement 62)
 - Commitment fees realized upon exercise or expiration of the commitment (Statement 62)
 - Commitment fees charged when exercise is considered remote (Statement 62)
 - Fee received related to a purchased loan or a group on loans (Statement 62)
 - Net balance (credit) of loan origination fees, excluding any portion related to points, for mortgage loans held for investment (Statement 62)
 - Net balance (credit) of loan origination fees, including any portion related to points, for mortgage loans held for resale after the sale occurs (Statement 62)
 - Fees that are realized after the funding of mortgage loans has occurred or after the commitment to guarantee the funding of mortgage loans expires (Statement 62)
 - Fees realized when a commitments arranged directly between a permanent investor and a borrower (Statement 62)

GASB 66, Technical corrections – 2012

- Issued – April 2012
- Effective – **Periods beginning after Dec. 15, 2012**
- Amends specific provisions of
 - GASB 10 that limits fund-based reporting of risk financing activities to GF and ISF – Use GASB 54 definitions
 - GASB 62 for
 - Operating lease payments
 - Purchased loans or groups of loans
 - Servicing fees related to mortgage loans sold

GASB 67 and 68 – Accounting and Financial Reporting for Pensions and Plans

- Statements issued in June 2012
- GASB 67 – Reporting of plans
 - Effective for fiscal years beginning after June 15, 2013
- GASB 68 – Employer/sponsor accounting/reporting
 - Effective for fiscal years beginning after June 15, 2014
- Standards address:
 - Changes in governmental accounting and financial reporting, principally the introduction of accrual-based government-wide financial statements
 - A perceived need among the users of governmental financial reports for comparable information about pensions
 - The continuing development of GASB concepts regarding what constitutes a liability and an outflow of resources

GASB 67, Financial Reporting for Pension Plans – An amendment of GASB Statement No. 25

- Establishes financial reporting standards for pension plans of SLGs
 - Defined benefit and defined contribution plans
 - Administered through trusts or equivalent arrangements, in which
 1. Contributions are irrevocable
 2. Assets are dedicated to providing pension benefits
 3. Plan assets are legally protected from the creditors of
 - a. Employers
 - b. Non-employer contributing entities
 - c. Plan administrators

Defined benefit plans (DBPs)

- DBPs should present the following financial statements prepared on accrual basis
 - **A statement of fiduciary net position**
 - Assets
 - Deferred outflows
 - Liabilities
 - Deferred inflows
 - Fiduciary net position
 - **State of changes in fiduciary net position**
 - Addition to plan
 - Deductions from plan
 - Net increase(decrease) in fiduciary net position

DBPs – Additional reporting considerations

- Notes to financial statements
 - Plan description
 - Plan investments
 - Receivables
 - Allocated insurance contracts excluded from plan assets
 - Reserves
 - Deferred retirement option (DROP) balances
 - Disclosures specific to
 - Single-employer plans
 - Cost-sharing plans

DBPs – Additional reporting considerations

- Required supplementary information (RSI) for single employer and cost sharing plans
 - 10 year schedule of changes in the net pension liability
 - 10 year schedule of the following for each year
 - Total pension liability
 - Plan's fiduciary net position
 - Net pension liability
 - Plan's fiduciary net position as a percent of total pension liability
 - Covered employee payroll
 - Net pension liability as a percent of covered employee payroll
 - 10 year schedule of actuarial determined information
 - 10 year schedule of annual money-weighted return on pension investments

GASB 67 also addresses

- Measurement of the DBP's net pension liability
 - Detailed considerations relative to the Pension liability
- Defined contribution pension plan reporting
 - Required disclosures

GASB 68, Accounting and Financial Reporting for Pensions – An amendment of GASB Statement No. 27

- Establishes standards of accounting and financial reporting for defined benefit pensions and defined contribution pensions provided to the employees of state and local governmental employers through pension plans (as defined earlier)
- **Focus is on accounting and reporting by employers for pension plans addressed in GASB 67**

GASB 68 – Basic considerations

- Defined benefit pensions originate from exchanges between the employer and employees resulting from employee services and are part of the total compensation for employee services
- Obligations for pensions meet the definition of a liability in Concepts Statement 4
- Compensation expense should be recognized in the period employee services are provided

GASB 68 – GASB’s fundamental approach

- View the cost of pensions within the context of an ongoing, career-long employment relationship
- Use an accounting-based versus funding-based approach to measurement
- Produce measures of the employer’s obligation to employees and the current period cost to taxpayers of providing governmental services

GASB 68 – Key GASB conclusions

- An employer is primarily responsible for the unfunded pension obligation resulting from an employment exchange
- The difference between the total pension liability and the plan net position would be reported as a net pension liability in the financial statements of the government

GASB 68 – Major accounting change

- A government employer will report in its financial statements a net pension liability for DBPs equal to the difference between the total pension liability and the value of assets set aside in a pension plan to pay benefits to current employees, retirees, and their beneficiaries

GASB 68 – Another major accounting change

- A government participating in a cost-sharing DBP will report a liability in its own financial statements that is equivalent to its long-term proportionate share of the collective net pension liability
 - Approach uses a basis for allocation of proportionate share based on the employer's expected contribution effort relative to that of all contributors

GASB 68 – Yet another major accounting change

- Special funding situations for DBPs
 - Under certain conditions both governmental non-employer contributing entities and governmental employers will recognize a proportionate share of the collective net pension liability

GASB 68 – Three step approach for measurement DBPs

- Determine projected benefit payments
- Discount future payments to determine present value of payments
- Attribute PV of payment to employee periods of service

Selection of all actuarial assumptions should be made in accordance with Actuarial Standards of Practice (with consideration of specific guidance provided by the GASB)

GASB 68 – Actuarial considerations DBPs

- Benefit projections
 - The projection of pension benefit payments should include the effects of projected future salary increases and future service credits, if part of the benefits formula, as well as automatic COLAs
 - ad hoc COLAs would be incorporated into projections of pension benefit payments only if an employer's practice indicates that the COLAs are substantively automatic

GASB 68 – Actuarial considerations DBPs, continued

- Discount rate
 - Should be a single rate that reflects:
 - The long-term expected rate of return on plan investments to the extent that
 1. Plan net position is projected to be sufficient to make benefit payments that are projected to occur in the period, and
 2. Assets are projected to be invested using a long-term investment strategy
 - A high-quality tax exempt municipal bond index rate to the extent that plan net position is projected to no longer be available for long-term investment

GASB 68 – Actuarial considerations DBPs, continued

- Timing and frequency of measurement
 - Recognize a net pension liability that is measured as of a date (the measurement date) no earlier than the end of *its prior fiscal year, consistently applied from period to period*
 - Total pension liability component of the net pension liability at the measurement date is determined either by
 - An actuarial valuation as of that date or
 - The use of update procedures to roll forward amounts to the measurement date from an actuarial valuation as of a date no more than 30 months (plus 1 day) prior to the fiscal year-end
 - A single or agent employer should be required to obtain, for financial reporting purposes, actuarial valuations at least biennially
 - More frequent valuations are encouraged

GASB 68 – Measurement DBPs

Plan net assets

- In calculating the employer's net pension liability, plan net position should be measured in the same way as measured in the plan's statement of plan net position, including measurement of investments at fair value.

Pension Expense (next slide)

- Immediate
- Deferred

GASB 68 – Expense recognition DBPs

- Immediate
 - Pension benefits earned during the reporting period (service cost or normal cost)
 - Interest cost on the total pension liability
 - Changes in benefit terms that affect the total pension liability
- Deferred
 - Expense would be deferred and recognized over a period equal to the average remaining service periods of active and inactive (including retirees) employees for:
 - Differences between expected and actual changes in economic and demographic factors
 - Changes in assumptions about economic and demographic factors
 - Differences between actual and projected earnings on plan investments would be deferred and recognized as pension expense over a five-year, closed period

GASB 68 – Disclosures

- General information
 - Name of the plan through which benefits are provided
 - Identification of the public employee retirement system or other entity that administers the plan
 - Identification of the plan
 - A brief description of the benefit provisions
 - The number of employees covered by the plan
 - Whether the pension plan issues a stand-alone financial report, or is included in the report of a public employee retirement system or another entity, and, if so, how to obtain the report

GASB 68 – Disclosures DBPs

- Actuarial information
 - Assumptions used in measurement
 - Discount rate
 - Assumptions
 - Expected rate of return
 - Municipal bond rate
 - Sensitivity analysis
- Also
 - Changes in net pension liability
 - Deferred inflows and outflows

GASB 68 – Required Supplementary Information (RSI) DBPs

- 10-year schedules for all governments, regardless of type of plan (plus notes):
 - Changes in the net pension liability by source
 - Collective level for cost-sharing employers
 - Components of the net pension liability and ratios: plan net position ÷ total pension liability; net pension liability ÷ covered-employee payroll
 - Collective and individual level for cost-sharing
 - Contribution information, if a government has an actuarially determined contribution: actuarially calculated contribution – actual contributions; contributions ÷ payroll

GASB 68 – RSI for Cost-Sharing Employer's DBPs

- 10-year schedules
 - Changes in the net pension liability (cost-sharing at collective level only)
 - Cost-sharing at both collective level and employer level with employer proportionate share percentage
 - Total pension liability, plan net position, net pension liability, and
 1. Plan net position as a percentage of the total pension liability
 2. Net pension liability as a percentage of covered-employee payroll
 - Actuarially calculated employer contributions needed, actual contributions made, the difference between them, and contributions made as a percentage of covered-employee payroll

GASB 68 – Audit Considerations

- Coordination of efforts and clear division of responsibility between auditor, auditee and actuary.
 - Consider nonaudit services and the impact of GAS
- Additional audit procedures relative to participant data, especially for cost sharing and agent plan situations
 - New auditing interpretations issued
- Coordination and communication when participating in cost sharing plans and special funding situations.

GASB 71 – Pension Transition for Contributions Made Subsequent to the Measurement Date

An amendment of GASB Statement No. 68

- Issued November 2013
- Effective simultaneously with the implementation of the provisions of GASB 68
- Address an issue regarding application of the transition provisions of Statement No. 68, *Accounting and Financial Reporting for Pensions*
 - The issue relates to amounts associated with contributions, if any, made by a state or local governments employer or non-employer contributing entity to a defined benefit pension plan after the measurement date of the government's beginning net pension liability

GASB 71, continued

- Amends paragraph 137 of Statement 68 to require that, at transition, **a government recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability.**
- Statement 68, as amended, continues to require that beginning balances for other deferred outflows of resources and deferred inflows of resources related to pensions be reported at transition only if it is practical to determine all such amounts

Suggested action items FOR pension standards implementation

- Determine the type of plan you have (single, agent, cost sharing) and read the appropriate sections of GASB 68 that pertain to your situation.
 - Be sure to review the illustrations in Appendix C.
- Determine if there are any legal requirements to contribute certain actuarially determined amounts to your plan(s).
 - If there are, discuss with your actuary to determine if there are any efficiencies (cost reductions) by engaging a single actuary to prepare all the needed calculations.
- Determine the measurement date you plan to use, and discuss it with your actuary.
 - If the actuarial valuation can be performed as of the measurement date, a roll-forward of the actuary's calculation will not be necessary.
 - This should be a simple matter for most single employer plans, but is not as simple for multiple employer plans.

Suggested action items, continued

- Plan net position is an important component of the net pension liability. Be sure to consider the expected issuance date of plan financial statements when selecting your measurement date.
- If you are in a multiple employer plan,
 - Try to arrange a meeting of all the employers involved (and the plan's administrator)
 - Discuss the timing and frequency of the actuarial valuation and how (and when) information will be disseminated to each employer
- For cost sharing plans,
 - Determine the method to be used for calculating proportionate shares. If the AV date is before the measurement date
 - Discuss how an individual employer can obtain sufficient detail to enable an independent roll-forward of the calculation (unless this will be provided by the administrator)

Suggested action items, continued

- If the measurement date and actuarial valuation date will not coincide, determine who will perform the necessary roll-forward.
 - This calculation is a significant estimate, and major changes since the original valuation date could have a material impact on the calculation. Your auditor may be unable (or unwilling) to perform this work. Consider you will need to engage another actuary to update the original valuation.
- Meet with officials of the plan.
 - Assumptions used for plan reporting and employer reporting have to be the same.
 - Agreeing to the assumptions in advance will help eliminate inconsistencies and should reduce the need for your actuaries to re-calculate data.

Suggested action items, continued

- **Cost sharing plan participants**
 - Make sure you understand the contribution requirements as they will significantly impact the “proportionate share” of the liability you will record
 - Determine how frequently the cost sharing allocations will be reviewed and the manner in which this will take place
 - Identify and communicate any concerns early in the process.

Suggested action items, continued

- Meet with your auditors
 - Discuss your plan for implementing this standard and ask for feedback
 - Find out what the auditor will require in terms of documentation and support
 - Provide information about the actuary to be engaged and what you know of their qualifications and professional reputation
 - Consider allowing your auditor to evaluate the significant assumptions you plan to use, particularly the long-term rate of return on investments, before the actuary finalizes the calculation.

For more information, we suggest

- All preparers read and become familiar with the text of all three GASB Standards
- Access GASB's recently published [Implementation Toolkit for Governments](#) which is available free of charge
 - <http://www.gasb.org/cs/ContentServer?c=Page&pagename=GASB%2FPage%2FGASBActionPage&cid=1176163527940>
 - The toolkit includes the following resources, among others:
 - [Guide to Implementation of GASB Statement 68 on Accounting and Financial Reporting for Pensions](#)
 - A video overview covering significant implementation issues arising from the pension standards
 - A background document and fact sheets answering frequently-asked questions regarding the pension standards
 - The executive summaries and the full texts of Statement 68 and 71
 - Eight podcasts discussing the most significant changes to accounting and financial reporting for pensions
 - An article outlining the key ways the pension standards will change how governments calculate and report pension costs and obligations
 - Read McGladrey's Whitepaper
 - GASB Statement No. 68, Accounting and Financial Reporting for Pensions - A Summary of the Changes and Recommended Implementation Steps
 - [GASB Statement No. 68, Accounting and Financial Reporting for Pensions](#)

GASB 69 – Government Combinations and Disposals of Government Operations

- Issued – January 2013
- Effective – **Periods beginning after Dec. 15, 2013**
 - Applied on a prospective basis

GASB 69, continued

- Standards for government combinations and disposals
 - Government merger - combination of legally separate entities in which no significant consideration is exchanged and either:
 - Two or more governments (or one or more governments and one or more nongovernmental entities) cease to exist as legally separate entities and are combined to form one or more new governments
 - One or more legally separate governments or nongovernmental entities cease to exist and their operations are absorbed into, and provided by, one or more continuing governments

GASB 69, continued

- Government acquisition – government combination in which a **government acquires** another entity, or the operations of another entity, **in exchange for significant consideration**.
 - The consideration provided should be significant in relation to the assets and liabilities acquired
 - The acquired entity or operation becomes part of the acquiring government's legally separate entity

GASB 69, continued

- Transfer of operations – government combination involving the operations of a government or nongovernmental entity, rather than a combination of legally separate entities, in which no significant consideration is exchanged.
 - Operations may be transferred to another existing entity or to a new entity.
 - Examples
 - Reorganizations
 - Redistricting
 - Annexations
 - New shared service arrangements

GASB 69 – Merger

- Merger date begins initial reporting period
 - Date combined assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the merging entities should be recognized and measured
 - Generally, measure the assets, deferred outflows of resources, liabilities, or deferred inflows of resources as of the merger date at the carrying values as reported in the separate financial statements of the merging entities
 - Consider impairments.
- For a continuing government merger described in paragraph 10b of this Statement, the merger date is the beginning of the reporting period in which the combination occurs, regardless of the actual date of the merger
- Transactions between the merging entities that occur before the combination should generally be eliminated in the combination process

GASB 69 – Acquisitions

- Date on which the acquiring government obtains control of the assets and becomes obligated for the liabilities of an acquiree entity or its operations is the acquisition date
 - Acquired assets, deferred outflows of resources, liabilities, or deferred inflows of resources, are measured acquisition value is a market-based entry price.
 - An entry price is assumed to be based on an orderly transaction entered into on the acquisition date.
 - Acquisition value represents the price that would be paid for acquiring similar assets, having similar service capacity, or discharging the liabilities assumed as of the acquisition date.
 - Statement also addresses
 - Consideration
 - Acquisition costs
 - Intra-entity government acquisitions
 - Reporting on a provisional basis
 - Reporting in governmental fund F/S

GASB 69 – Transfers of operations

- Effective transfer date is the date the transferee government obtains control of the assets and becomes obligated for the liabilities of the operation transferred
 - A continuing government should report a transfer of operations as a transaction in its financial statements for the reporting period in which it occurs
 - If transfer of operations results in the formation of a new government, the new government's initial reporting period begins at the effective transfer date
- Generally transferee government recognizes the carrying values of assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the operations of the transferor government or nongovernmental entity as of the effective transfer date

GASB 69 – Disposals of government operations

- Disposing government should recognize a gain or loss on the disposal of operations, if applicable.
 - Gains or losses on the disposal of operations should be reported as a special item in the period in which the disposal occurs, based on either the effective transfer date of a transfer of operations, or the date of sale for operations that are sold
 - Special provision for certain costs

GASB 69, continued

- General and transaction specific disclosure requirements
- Statement also includes
 - Illustrations
 - Government merger
 - Government Acquisition with Excess Consideration Provided
 - Government Acquisition with Excess Net Position Received
 - Transfer of Operations

GASB 70 – Accounting and Financial Reporting for Non-exchange Financial Guarantees

- Issued April 2013
- Effective for periods beginning after June 15, 2013
- Requires a government that
 - extends a non-exchange financial guarantee to recognize a liability when qualitative factors and historical data, if any, indicate that it is more likely than not that the government will be required to make a payment on the guarantee
 - has issued an obligation guaranteed in a nonexchange transaction to report the obligation until legally released as an obligor
- Specifies the information required to be disclosed by governments that extend or receive nonexchange financial guarantees

GASB 70 – Non-exchange Financial Guarantees, continued

- Applies to non-exchange financial guarantees
 - Guarantee of obligation of a legally separate entity or individual (includes CUs)
 - Requires guarantor to indemnify 3rd-party obligation holder
- Does not apply to special assessment debt (GASB 6)

GASB 70 – Non-exchange Financial Guarantees, continued

- Government extending guarantee considers qualitative factor in assessing likelihood of payment
 - Bankruptcy proceedings or financial reorganization
 - Breach of debt contract or default
 - Other indicators of financial distress.
- Consider default frequency (likelihood) for a group of guarantees

GASB 70 – Non-exchange Financial Guarantees, continued

- When payment under the terms of a guarantee is more likely than not, government guarantor should recognize a liability and related expense
 - Discounted PV of best estimate of expected future outflows
 - If only a range can be determined, recognize at least minimum amount in the range

GASB 70 – Non-exchange Financial Guarantees, continued

- If government is required to repay a guarantor for payments made on its obligations, it should reclassify that portion of its previously recognized liability for the guaranteed obligation as a liability to the guarantor
 - Government continues to recognize its liability until that portion of the liability is legally released
 - Such as when a plan of adjustment is confirmed by the court in the case of bankruptcy
 - government recognizes revenue to the extent of the reduction of its guaranteed liabilities

GASB 70 – Non-exchange Financial Guarantees, continued

- When a government that extends a guarantee recognizes a liability for the guarantee, the government that issued the guaranteed obligation recognizes a corresponding receivable only when it is:
 - A blended component unit of that government
 - A primary government that includes the government that extended the guarantee as a blended component unit within its reporting entity
 - Within the same reporting entity and both parties are blended component units of the same primary government

GASB 70 – Nonexchange Financial Guarantees, continued

- A government that extends guarantees discloses information, by type of guarantee, for all guarantees, regardless of the likelihood of a payment being required
- A government that recognizes a guarantee liability or has made payments during the reporting period on guarantees extended should disclose additional information

GASB 70 – Non-exchange Financial Guarantees, continued

- A government that has one or more outstanding obligations at the reporting date that have been guaranteed by another entity should disclose the certain information about the guarantee(s) by type of guarantee
- A government that has issued a guaranteed obligation for which payments have been made during the reporting period by the entity that extended the guarantee and that guaranteed obligation is no longer outstanding at the end of the reporting period makes additional disclosures
 - Applies regardless of whether the government has any other outstanding guaranteed obligations at the end of the reporting period

GASB Projects

- Asset retirement Obligation – recognition and measurement of ARO other than landfills – **being deliberated**
- Blending requirements for certain business-type activities – inconsistent presentation of CU in BTA – **being deliberated**
- Fair value measurement and application – **comment deadline on exposure draft August 15, 2014**
- Fiduciary responsibilities – **being deliberated**
- GAAP hierarchy – **exposure draft issued; comment deadline December 2014**

GASB Projects

- Irrevocable Charitable Trusts – **being deliberated**
- Conceptual framework – develop recognition criteria for whether information (what and when) should be reported in State and local government financial statements *on hold*
- Economic conditions reporting – Financial projections *on hold*
- Leases – **being deliberated**
- OPEB accounting and financial reporting – **exposure draft issued; comment deadline August 2014**

GASB Projects

- Tax abatement disclosures – **being deliberated**

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