

**State Bar of Texas**

Letter on Conduct of Audit  
and Management Letter Comments

May 31, 2012

To the Board of Directors  
State Bar of Texas  
Austin, Texas

This letter is intended to inform the Members of the Board of Directors of State Bar of Texas (the "State Bar") about significant matters related to the conduct of the annual audit for the year ended May 31, 2012, so they can appropriately discharge their oversight responsibility and that we comply with our professional responsibilities to the Audit and Finance Committee of the Board of the Directors.

Under *Section A – Communication Letter to the Members of the Board of Directors*, we have included various matters which must be communicated to the State Bar under auditing standards generally accepted in the United States of America.

This report is intended solely for the information and use of the Members of the Board of Directors of State Bar of Texas and management and is not intended to be, and should not be, used by anyone other than the specified parties.

We will be pleased to respond to any questions you may have, and we appreciate the opportunity to continue to be of service.

*Padgett, Stratemann & Co., L.L.P.*

Certified Public Accountants  
November 20, 2012

# State Bar of Texas

## Letter on Conduct of Audit and Management Letter Comments

May 31, 2012

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## **Section A – Communication Letter to the Board of Directors**

### ***The Auditors’ Responsibility Under Auditing Standards Generally Accepted in the United States of America***

As communicated in the arrangement letter dated July 13, 2012, our responsibility, as described by professional standards, is to form and express an opinion about whether the financial statements that have been prepared by management with your oversight are presented fairly, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your respective responsibilities.

Our responsibility, as prescribed by professional standards, is to plan and perform our audit to obtain reasonable, rather than absolute, assurance about whether the financial statements are free of material misstatement. An audit of financial statements includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity’s internal control over financial reporting. Accordingly, as part of our audit, we considered the internal control of the State Bar solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are also responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures for the purpose of identifying other matters to communicate to you.

### ***Planned Scope and Timing of the Audit***

We conducted our audit consistent with the planned scope and timing previously communicated to you.

### ***Qualitative Aspects of Significant Accounting Practices***

#### ***Significant Accounting Policies***

Management has the responsibility to select and use appropriate accounting policies. A summary of the significant accounting policies adopted by the State Bar is included in Note 1 to the financial statements. There has been no initial selection of accounting policies and no changes in significant accounting policies or their application during the year ended May 31, 2012 other than the required initial adoption of Governmental Accounting Standards Board (“GASB”) Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions* (“GASB Statement No. 54”).

GASB Statement No. 54 improves financial reporting by enhancing the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and clarifies the existing governmental fund type definitions. GASB Statement No. 54 establishes fund balance classifications that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds.

No matters have come to our attention that would require us, under professional standards, to inform you about (1) the methods used to account for significant unusual transactions and (2) the effect of significant accounting policies in controversial or emerging areas for which there is a lack of authoritative guidance or consensus.

#### *Significant Accounting Estimates*

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's current judgments. Those judgments are normally based on knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ markedly from management's current judgments.

The most sensitive accounting estimates affecting the financial statements are the estimated useful lives of capital assets, the fair value of investments, unearned revenue, and the collectibility of accounts receivable. Management's estimates are based on information currently available, and the process used to calculate these estimates should be monitored throughout the year. These estimates were reviewed and it was determined they are reasonable in relation to the basic financial statements taken as a whole.

#### *Financial Statement Disclosures*

Certain financial statement disclosures involve significant judgment and are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the State Bar's financial statements relate to revenue recognition and long-term debt.

#### ***Significant Difficulties Encountered During the Audit***

We encountered no significant difficulties in dealing with management relating to the performance of the audit.

#### ***Other Information in Documents Containing the Audited Financial Statements***

In connection with the State Bar's annual report, we did not perform any procedures or corroborate other information included in the annual report. However, we read the State Bar's annual report and considered whether the information or the manner in which it was presented was materially inconsistent with information or the manner of presentation of the financial statements. Based on our reading, we concluded the information did not require revision.

#### ***Uncorrected and Corrected Misstatements***

For purposes of this communication, professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those we believe are trivial, and communicate them to the appropriate level of management. Appendix I summarizes the uncorrected financial statement misstatements whose effects, as determined by management, are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

In addition, professional standards require us to communicate to you all material, corrected misstatements that were brought to the attention of management as a result of the audit procedures. See Appendix I for the material misstatement that was identified as a result of our audit procedures and brought to the attention of and corrected by management.

***Disagreements With Management***

For purposes of this letter, professional standards define a disagreement with management as a matter, whether or not resolved to our satisfaction, concerning a financial accounting, reporting, or auditing matter, which could be significant to the State Bar's financial statements or the auditors' report. No such disagreements arose during the course of the audit.

***Representations Requested From Management***

We have requested certain written representations from management, which are included in Appendix II, dated November 20, 2012.

***Management's Consultations With Other Accountants***

In some cases, management may decide to consult with other accountants about auditing and accounting matters. Management informed us that, and to our knowledge, there were no consultations with other accountants regarding auditing and accounting matters.

***Other Significant Findings or Issues***

In the normal course of our professional association with the State Bar, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the State Bar, and business plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition to our retention as the State Bar's auditors.

## Appendices

## Appendix I

State Bar of Texas

Summary of Corrected and Uncorrected Misstatements

Description	Statement of Revenues, Expenditures, and Changes in Fund Balance				
	Assets	Liabilities	Revenue	Expenditures	Change in Fund Balance
<b>Uncorrected Misstatements</b>					
Unrecorded adjustment for accrual for membership refunds at May 31, 2012.	\$ <u>-</u>	\$ <u>110,562</u>	\$ <u>-</u>	\$ <u>110,562</u>	\$ <u>(110,562)</u>
<b>Corrected Misstatements</b>					
To record Sections revenue collected in August 2012 for the year ended May 31, 2012.	\$ <u>147,128</u>	\$ <u>-</u>	\$ <u>147,128</u>	\$ <u>-</u>	\$ <u>147,128</u>

Appendix II  
Representation Letter

# STATE BAR OF TEXAS



November 20, 2012

Padgett, Stratemann & Co., L.L.P.  
811 Barton Springs Road, Suite 550  
Austin, Texas 78704

In connection with your audit of the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the State Bar of Texas (the "State Bar") as of and for the year ended May 31, 2012, we confirm that we are responsible for the fair presentation in the financial statements of financial position, changes in financial position, and cash flows in conformity with accounting principles generally accepted in the United States of America.

We confirm to the best of our knowledge and belief, as of November 20, 2012 the following representations made to you during your audit.

1. The financial statements referred to above are fairly presented in conformity with accounting principles generally accepted in the United States of America.
2. We have identified for you all organizations that are a part of this reporting entity or with which we have a relationship, as these organizations are defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards, that are:
  - a. Component units.
  - b. Other organizations for which the nature and significance of their relationship with State Bar are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.
  - c. Jointly governed organizations in which we participated.
3. We are a component unit of the State of Texas as this term is defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards.
4. We have identified for you all of our funds, governmental functions, and identifiable business-type activities.
5. We have properly classified all funds and activities.
6. We have properly determined and reported the major governmental and enterprise funds based on the required quantitative criteria. We have determined the following funds to be major for public interest reasons: Client Security Fund. We believe that all judgmentally determined major funds are particularly important to the financial statement users.
7. We are responsible for compliance with laws and regulations applicable to the State Bar including adopting, approving, and amending budgets.

8. We have identified and disclosed to you all laws and regulations that have a direct and material effect on the determination of financial statement amounts including legal and contractual provisions for reporting specific activities in separate funds.
9. We have made available to you:
  - a. All financial records and related data of all funds and activities, including those of all special funds, programs, departments, projects, activities, etc., in existence at any time during the period covered by your audit.
  - b. All minutes of the meetings of the governing board and committees of board members or summaries of actions of recent meetings for which minutes have not yet been prepared.
  - c. All communications from grantors, lenders, other funding sources, or regulatory agencies concerning noncompliance with:
    - (1) Statutory, regulatory, or contractual provisions or requirements.
    - (2) Financial reporting practices that could have a material effect on the financial statements.
10. We have no knowledge of fraud or suspected fraud affecting the entity, except as previously disclosed to you, involving:
  - a. Management,
  - b. Employees who have significant roles in the internal control, or
  - c. Others where the fraud could have a material effect on the financial statements.
11. We acknowledge our responsibility for the design and implementation of programs and controls to provide reasonable assurance that fraud is prevented and detected.
12. We have no knowledge of any allegations of fraud or suspected fraud affecting the State Bar received in communications from employees, former employees, analysts, regulators, short sellers, or others.
13. We are aware of no significant deficiencies, including material weaknesses, in the design or operation of internal controls that could adversely affect the entity's ability to record, process, summarize, and report financial data.
14. There have been no communications from regulatory agencies concerning noncompliance with, or deficiencies in, financial reporting practices.
15. We have no plans or intentions that may materially affect the carrying value or classification of assets and liabilities.
16. The following have been properly recorded and/or disclosed in the financial statements:
  - a. Related-party transactions, including those with the primary government having accountability for State Bar, component units for which State Bar is accountable, other organizations for which the nature and significance of their relationship with State Bar are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete, joint ventures in which State Bar has an interest, and jointly governed organizations in which State Bar participates, all as defined in Section 2100 of the Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards, and interfund transactions, including interfund accounts and advances receivable and payable, sale and purchase transactions, interfund transfers, long-term loans, leasing arrangements, and guarantees, all of which have been recorded in accordance with the economic substance of the transaction and appropriately classified and reported.

- b. The fair value of investments.
  - c. All leases and material amounts of rental obligations under long-term leases.
  - d. All significant estimates and material concentrations known to management which are required to be disclosed in accordance with the AICPA's Statement of Position No. 94-6, *Disclosure of Certain Significant Risks and Uncertainties*. Significant estimates are estimates at the balance sheet date which could change materially within the next year. Concentrations refer to volumes of business, revenues, available sources of supply, or markets for which events could occur which would significantly disrupt normal finances within the next year.
  - e. Net assets and fund balance classifications.
17. We are responsible for making the accounting estimates included in the financial statements. Those estimates reflect our judgment based on our knowledge and experience about past and current events and our assumptions about conditions we expect to exist and courses of action we expect to take. In that regard, adequate provisions have been made:
- a. To reduce receivables to their estimated net collectable amounts.
  - b. To reduce obsolete, damaged, or excess inventories to their estimated net realizable values.
  - c. To reduce investments, intangibles, and other assets which have permanently declined in value to their realizable values.
  - d. For pension obligations, post-retirement benefits other than pensions, and deferred compensation agreements attributable to employee services rendered through May 31, 2012.
  - e. For any material loss to be sustained in the fulfillment of, or from the inability to fulfill, any service commitments.
18. There are no:
- a. Material transactions that have not been properly recorded in the accounting records underlying the financial statements.
  - b. Violations or possible violations of laws or regulations whose effects should be considered for disclosure in the financial statements or as a basis for recording a loss contingency. In that regard, we specifically represent that we have not been designated as, or alleged to be, a "potentially responsible party" by the Federal Environmental Protection Agency or any equivalent state agencies in connection with any environmental contamination.
  - c. Other material liabilities or gain or loss contingencies that are required to be accrued or disclosed by Statement of Financial Accounting Standards No. 5 and/or GASB Statement No. 10.
  - d. Guarantees, whether written or oral, under which the State Bar is contingently liable.
  - e. Arrangements with financial institutions involving compensating balances or other arrangements involving restrictions on cash balances.
  - f. Line of credit or similar arrangements.
  - g. Agreements to repurchase assets previously sold.
  - h. Security agreements in effect under the Uniform Commercial Code.
  - i. Any other liens or encumbrances on assets or revenues or any assets or revenues which were pledged as collateral for any liability or which were subordinated in any way.

- j. Authorized but unissued bonds and/or notes.
  - k. Risk financing activities.
  - l. Derivative financial instruments.
  - m. Special and extraordinary items.
  - n. Deposits and investment securities categories of risk.
  - o. Arbitrage rebate liabilities.
  - p. Impairment of capital assets.
  - q. Debt issue repurchase options or agreements, or sinking fund debt repurchase ordinance requirements.
  - r. Debt issue provisions.
  - s. Liabilities which are subordinated in any way to any other actual or possible liabilities.
19. We are not aware of any pending or threatened litigation, claims, or assessments that are required to be accrued or disclosed in the financial statements as defined in Section 2300 Governmental Accounting Standards Board's Codification of Governmental Accounting and Financial Reporting Standards and we have not consulted a lawyer concerning litigation claims or assessments.
  20. We have no direct or indirect, legal or moral obligation for any debt of any organization, public or private, or to special assessment bond holders that is not disclosed in the financial statement.
  21. We have satisfactory title to all owned assets.
  22. We have complied with all aspects of contractual agreements that would have a material effect on the financial statements in the event of noncompliance.
  23. Net asset components invested in capital assets, net of related debt; restricted; and unrestricted and fund balances classifications (non-expendable, restricted, committed, assigned, and unassigned) are properly classified and, when applicable, approved.
  24. Expenses or expenditures have been appropriately classified in or allocated to functions and programs in the statement of activities, and allocations have been made on a reasonable basis.
  25. Revenues are appropriately classified in the statements of activities within program revenues.
  26. Capital assets, including infrastructure assets, are properly capitalized, reported, and depreciated.
  27. We are responsible for and have reviewed and approved the proposed adjustments to the trial balances identified during the audit, which are included in the summarized schedule of posted adjustments and will post all adjustments accordingly. These adjustments are attached as Appendix I. We have reviewed, approved, and are responsible for overseeing the preparation and completion of the basic financial statements and related notes.
  28. With respect to supplementary information presented in relation to the financial statements as a whole:
    - a. We acknowledge our responsibility for the presentation of such information.
    - b. We believe such information, including its form and content, is fairly presented in accordance with accounting principles generally accepted in the United States of America.

- c. The methods of measurement or presentation have not changed from those used in the prior period.
- 29 With respect to the Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget (GAAP Basis) and Actual – General Fund presented as required by Government Accounting Standards Board to supplement the basic financial statements:
- a. We acknowledge our responsibility for the presentation of such required supplementary information.
  - b. We believe such required supplementary information is measured and presented in accordance with guidelines prescribed by accounting principles generally accepted in the United States of America.
  - c. The methods of measurement or presentation have not changed from those used in the prior period.
30. We agree the unrecorded adjustment for the accrual of refunds, as previously disclosed to you, does not materially misstate the financial statements.
31. We are responsible for determining that significant events or transactions that have occurred since the balance sheet date and through November 20, 2012, have been recognized or disclosed in the financial statements. No events or transactions have occurred subsequent to the balance sheet date and through November 20, 2012 that would require recognition or disclosure in the financial statements. We further represent that as of November 20, 2012 the financial statements were complete in a form and format that complied with accounting principles generally accepted in the United States of America, and all approvals necessary for issuance of the financial statements had been obtained.
32. During the course of your audit, you may have accumulated records containing data that should be reflected in our books and records. All such data have been so reflected. Accordingly, copies of such records in your possession are no longer needed by us.

State Bar of Texas



Michelle Hunter, Executive Director



Cheryl Howell, Chief Financial Officer



Sharon Smith, Controller

**Appendix I**

<u>Description of Corrected Misstatements</u>	<u>Statement of Activities</u>				
	<u>Assets</u>	<u>Liabilities</u>	<u>Revenue</u>	<u>Expenses</u>	<u>Change in Net Assets</u>
To record Sections expenses at 5/31/12.	\$	\$ 49,370	\$	\$ 49,370	\$ (49,370)
To record Sections revenue collected in August 2012 for the year ended 5/31/12.	<u>147,128</u>		<u>147,128</u>		<u>147,128</u>
	\$ <u>147,128</u>	\$ <u>49,370</u>	\$ <u>147,128</u>	\$ <u>49,370</u>	\$ <u>97,758</u>

## Appendix III

### Recently Issued Accounting and Reporting Pronouncements

The Governmental Accounting Standards Board (“GASB”) has issued the following pronouncements: GASB Statements No. 60, 61, 62, 63, 65, 66, 67, and 68. Management has not yet determined the impact of these pronouncements on the financial statements. The following is a summary of these pronouncements and their effective dates.

***GASB Statement No. 60, Accounting and Financial Reporting for Service Concession Arrangements***

The objective of GASB Statement No. 60 is to improve financial reporting by addressing issues related to service concession arrangements (“SCAs”), which are a type of public-private or public-public partnership. As used in GASB Statement No. 60, an SCA is an arrangement between a transferor (a government) and an operator (governmental or nongovernmental entity) in which (1) the transferor conveys to an operator the right and related obligation to provide services through the use of infrastructure or another public asset (a “facility”) in exchange for significant consideration and (2) the operator collects and is compensated by fees from third parties.

GASB Statement No. 60 applies only to those arrangements in which specific criteria determines whether a transferor has control over the facility are met. A transferor reports the facility subject to an SCA as its capital asset, generally following existing measurement, recognition, and disclosure guidance for capital assets. New facilities constructed or acquired by the operator, or improvements to existing facilities made by the operator, are reported at fair value by the transferor. A liability is recognized, for the present value of significant contractual obligations to sacrifice financial resources imposed on the transferor, along with a corresponding deferred inflow of resources. Revenue is recognized by the transferor in a systematic and rational manner over the term of the arrangement.

GASB Statement No. 60 also provides guidance for governments that are operators in an SCA. The governmental operator reports an intangible asset at cost for its right to access the facility and collect third-party fees; it amortizes the intangible asset over the term of the arrangement in a systematic and rational manner. For existing facilities, a governmental operator’s cost may be the amount of an up-front payment or the present value of installment payments. For new or improved facilities, a governmental operator’s cost may be its cost of improving an existing facility or constructing or acquiring a new facility.

For revenue sharing arrangements, GASB Statement No. 60 requires governmental operators to report all revenues and expenses. A transferor reports its portion of the shared revenues.

GASB Statement No. 60 requires disclosures about an SCA including a general description of the arrangement and information about the associated assets, liabilities, and deferred inflows; the rights granted and retained; and guarantees and commitments.

The requirements of GASB Statement No. 60 are effective for financial statements for periods beginning after December 15, 2011. The provisions of GASB Statement No. 60 generally are required to be applied retroactively for all periods presented.

***GASB Statement No. 61, The Financial Reporting Entity, Omnibus, An Amendment to GASB Statements No. 14 and 34***

The requirements in GASB Statement No. 61 modify certain requirements for inclusion of component units in the financial reporting entity. For organizations that previously were required to be included as component units by meeting the fiscal dependency criteria, a financial benefit or burden relationship

also would need to be present between the primary government and that organization for it to be included in the reporting entity as a component unit. Further, for organizations that do not meet the financial accountability criteria for inclusion as component units but that, nevertheless, should be included because the primary government's management determines that it would be misleading to exclude them, GASB Statement No. 61 clarifies the manner in which that determination should be made and the types of relationships that generally should be considered in making the determination.

GASB Statement No. 61 also amends the criteria for reporting component units as if they were part of the primary government (that is, blending) in certain circumstances. For component units that currently are blended based on the "substantively the same governing body" criteria, it additionally requires (1) the primary government and the component unit have a financial benefit or burden relationship or (2) management (below the level of the elected officials) of the primary government have operational responsibility (as defined in paragraph 8a) for the activities of the component unit. New criteria also is added to require blending of component units whose total debt outstanding is expected to be repaid entirely or almost entirely with resources of the primary government. The blending provisions are amended to clarify that funds of a blended component unit have the same financial reporting requirements as a fund of the primary government. Lastly, additional reporting guidance is provided for blending a component unit if the primary government is a business-type activity that uses a single column presentation for financial reporting.

GASB Statement No. 61 also clarifies the reporting of equity interests in legally separate organizations. It requires a primary government to report its equity interest in a component unit as an asset.

The provisions of GASB Statement No. 61 are effective for financial statements for periods beginning after June 15, 2012. Earlier application is encouraged.

***GASB Statement No. 62, Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements***

The objective GASB Statement No. 62 is to incorporate into the GASB's authoritative literature certain accounting and financial reporting guidance that is included in the following pronouncements issued on or before November 30, 1989, which does not conflict with or contradict GASB pronouncements:

- Financial Accounting Standards Board ("FASB") Statements and Interpretations
- Accounting Principles Board Opinions
- Accounting Research Bulletins of the American Institute of Certified Public Accountants' ("AICPA") Committee on Accounting Procedure

GASB Statement No. 62 also supersedes GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, thereby eliminating the election provided in paragraph 7 of GASB Statement No. 62 for enterprise funds and business-type activities to apply post-November 30, 1989 FASB Statements and Interpretations that do not conflict with or contradict GASB pronouncements. However, those entities can continue to apply, as other accounting literature, post-November 30, 1989 FASB pronouncements that do not conflict with or contradict GASB pronouncements, including GASB Statement No. 62.

The requirements of GASB Statement No. 62 are effective for financial statements for periods beginning after December 15, 2011. Earlier application is encouraged. The provisions of GASB Statement No. 62 generally are required to be applied retroactively for all periods presented.

***GASB Statement No. 63, Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position***

GASB Statement No. 63 provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined those elements as a consumption of net assets by the government that is applicable to a future reporting period, and an acquisition of net assets by the government that is applicable to a future reporting period, respectively. Previous financial reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities.

Concepts Statement No. 4 also identifies net position as the residual of all other elements presented in a statement of financial position. GASB Statement No. 63 amends the net asset reporting requirements in GASB Statement No. 34, *Basic Financial Statements – and Management’s Discussion and Analysis – for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets.

The provisions of GASB Statement No. 63 are effective for financial statements for periods beginning after December 15, 2011. Earlier application is encouraged.

***GASB Statement No. 65, Items Previously Reported as Assets and Liabilities***

GASB Statement No. 65 establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities.

Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined the elements included in financial statements, including deferred outflows of resources and deferred inflows of resources. In addition, Concepts Statement No. 4 provides that reporting a deferred outflow of resources or a deferred inflow of resources should be limited to those instances identified by the board in authoritative pronouncements that are established after applicable due process. Prior to the issuance of GASB Statement No. 65, only two such pronouncements have been issued. GASB Statement No. 53, *Accounting and Financial Reporting for Derivative Instruments*, requires the reporting of a deferred outflow of resources or a deferred inflow of resources for the changes in fair value of hedging derivative instruments, and GASB Statement No. 60, *Accounting and Financial Reporting for Service Concession Arrangements*, requires a deferred inflow of resources to be reported by a transferor government in a qualifying SCA. GASB Statement No. 65 amends the financial statement element classification of certain items previously reported as assets and liabilities to be consistent with the definitions in Concepts Statement No. 4.

GASB Statement No. 65 also provides other financial reporting guidance related to the impact of the financial statement elements deferred outflows of resources and deferred inflows of resources, such as changes in the determination of the major fund calculations and limiting the use of the term *deferred* in financial statement presentations.

The provisions of GASB Statement No. 65 are effective for financial statements for periods beginning after December 15, 2012. Earlier application is encouraged.

**GASB Statement No. 66, *Technical Corrections – 2012, An Amendment to GASB Statements No. 10 and No. 62***

The objective of GASB Statement No. 66 is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*.

GASB Statement No. 65 amends GASB Statement No. 10, *Accounting and Financial Reporting for Risk Financing and Related Insurance Issues*, by removing the provision that limits fund-based reporting of an entity's risk financing activities to the general fund and the internal service fund type. As a result, governments should base their decisions about fund type classification on the nature of the activity to be reported, as required in GASB Statement No. 54 and GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*.

GASB Statement No. 66 also amends GASB Statement No. 62 by modifying the specific guidance on accounting for (1) operating lease payments that vary from a straight-line basis, (2) the difference between the initial investment (purchase price) and the principal amount of a purchased loan or group of loans, and (3) servicing fees related to mortgage loans that are sold when the stated service fee rate differs significantly from a current (normal) servicing fee rate. These changes clarify how to apply GASB Statement No. 13, *Accounting for Operating Leases With Scheduled Rent Increases*, and result in guidance that is consistent with the requirements in GASB Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*, respectively.

The provisions of GASB Statement No. 66 are effective for financial statements for periods beginning after December 15, 2012. Earlier application is encouraged.

**GASB Statement No. 67, *Financial Reporting for Pension Plans, An Amendment of GASB Statement No. 25***

The objective of GASB Statement No. 67 is to improve financial reporting by state and local governmental pension plans. GASB Statement No. 67 results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency. GASB Statement No. 67 replaces the requirements of GASB Statement No. 25, *Financial Reporting for Defined Benefit Pension Plans and Note Disclosures for Defined Contribution Plans*, and GASB Statement No. 50, *Pension Disclosures*, as they relate to pension plans that are administered through trusts or equivalent arrangements (hereafter jointly referred to as "trusts") that meet certain criteria. The requirements of GASB Statements No. 25 and No. 50 remain applicable to pension plans that are not administered through trusts covered by the scope of GASB Statement No. 67 and to defined contribution plans that provide postemployment benefits other than pensions.

GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, establishes accounting and financial reporting requirements related to pensions for governments whose employees are provided with pensions through pension plans that are covered by the scope of GASB Statement No. 68, as well as for nonemployer governments that have a legal obligation to contribute to those plans.

GASB Statements No. 67 and No. 68 establish a definition of a pension plan that reflects the primary activities associated with the pension arrangement – determining pensions, accumulating and managing assets dedicated for pensions, and paying benefits to plan members as they come due. The scope of GASB Statement No. 67 addresses accounting and financial reporting for the activities of pension plans that are administered through trusts that have the following characteristics:

- Contributions from employers and nonemployer contributing entities to the pension plan and earnings on those contributions are irrevocable.
- Pension plan assets are dedicated to providing pensions to plan members in accordance with the benefit terms.
- Pension plan assets are legally protected from the creditors of employers, nonemployer contributing entities, and the pension plan administrator. If the plan is a defined benefit pension plan, plan assets also are legally protected from creditors of the plan members.

For defined benefit pension plans, GASB Statement No. 67 establishes standards of financial reporting for separately issued financial reports and specifies the required approach to measuring the pension liability of employers and nonemployer contributing entities for benefits provided through the pension plan (the net pension liability), about which information is required to be presented. Distinctions are made regarding the particular requirements depending upon the type of pension plan administered, as follows:

- Single-employer pension plans – those in which pensions are provided to the employees of only one employer (as defined in GASB Statement No. 67).
- Agent multiple-employer pension plans (agent pension plans) – those in which plan assets are pooled for investment purposes, but separate accounts are maintained for each individual employer so that each employer's share of the pooled assets is legally available to pay the benefits of only its employees.
- Cost-sharing multiple-employer pension plans (cost-sharing pension plans) those in which the pension obligations to the employees of more than one employer are pooled and plan assets can be used to pay the benefits of the employees of any employer that provides pensions through the pension plan.

GASB Statement No. 67 also details the note disclosure requirements for defined contribution pension plans administered through trusts that meet the identified criteria.

GASB Statement No. 67 is effective for financial statements for fiscal years beginning after June 15, 2013. Earlier application is encouraged.

In the first period that GASB Statement No. 67 is applied, changes made to comply with GASB Statement No. 67 should be treated as an adjustment of prior periods, and financial statements presented for the periods affected should be restated. If restatement is not practical, the cumulative effect of applying GASB Statement No. 67, if any, should be reported as a restatement of beginning net position for the earliest period restated. In the period GASB Statement No. 67 is first applied, the financial statements should disclose the nature of any restatement and its effect. Also, the reason for not restating prior periods presented should be explained.

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

The primary objective of GASB Statement No. 68 is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by state and local governmental employers about financial support for pensions that is provided by other entities. GASB Statement No. 68 results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and interperiod equity, and creating additional transparency.

GASB Statement No. 68 replaces the requirements of GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of GASB Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements that meet certain criteria. The requirements of GASB Statements No. 27 and No. 50 remain applicable for pensions that are not covered by the scope of GASB Statement No. 68.

GASB Statement No. 67, *Financial Reporting for Pension Plans*, revises existing standards of financial reporting for most pension plans. GASB Statements No. 68 and No. 67 establish a definition of a pension plan that reflects the primary activities associated with the pension arrangement – determining pensions, accumulating and managing assets dedicated for pensions, and paying benefits to plan members as they come due.

The scope of GASB Statement No. 68 addresses accounting and financial reporting for pensions that are provided to the employees of state and local governmental employers through pension plans that are administered through trusts that have the following characteristics:

- Contributions from employers and nonemployer contributing entities to the pension plan and earnings on those contributions are irrevocable.
- Pension plan assets are dedicated to providing pensions to plan members in accordance with the benefit terms.
- Pension plan assets are legally protected from the creditors of employers, nonemployer contributing entities, and the pension plan administrator. If the plan is a defined benefit pension plan, plan assets also are legally protected from creditors of the plan members.

GASB Statement No. 68 establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit pensions, GASB Statement No. 68 identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service.

Note disclosure and required supplementary information requirements about pensions also are addressed. Distinctions are made regarding the particular requirements for employers based on the number of employers whose employees are provided with pensions through the pension plan and whether pension obligations and pension plan assets are shared. Employers are classified in one of the following categories for purposes of GASB Statement No. 68:

- Single employers are those whose employees are provided with defined benefit pensions through single-employer pension plans – pension plans in which pensions are provided to the employees of only one employer (as defined in GASB Statement No. 68).
- Agent employers are those whose employees are provided with defined benefit pensions through agent multiple-employer pension plans – pension plans in which plan assets are pooled for investment purposes, but separate accounts are maintained for each individual employer so that each employer’s share of the pooled assets is legally available to pay the benefits of only its employees.
- Cost-sharing employers are those whose employees are provided with defined benefit pensions through cost-sharing multiple-employer pension plans – pension plans in which the pension obligations to the employees of more than one employer are pooled and plan assets can be used to pay the benefits of the employees of any employer that provides pensions through the pension plan.

In addition, GASB Statement No. 68 details the recognition and disclosure requirements for employers with liabilities (payables) to a defined benefit pension plan and for employers whose employees are provided with defined contribution pensions. GASB Statement No. 68 also addresses circumstances in which a nonemployer entity has a legal requirement to make contributions directly to a pension plan.

GASB Statement No. 68 is effective for fiscal years beginning after June 15, 2014. Earlier application is encouraged.