**BOBBY JINDAL**
GOVERNOR

**PAUL W. RAINWATER**
COMMISSIONER OF ADMINISTRATION

# State of Louisiana

Division of Administration

**Office of Statewide Reporting and Accounting Policy**

July 2, 2012

**OSRAP MEMORANDUM 13-01**

TO: Fiscal Officers

FROM: Afranie Adomako, CPA
Director

SUBJECT: Appendices to the Annual Fiscal Reports (AFR)

Attached are the appendices to the Annual Fiscal Reports (AFR) as developed by the Office of Statewide Reporting and Accounting Policy (OSRAP) for the fiscal year ended June 30, 2012. This memo supersedes OSRAP Memo 11-36, which contained the appendices for the 2011 AFRs. The appendices may be used as a reference for the various AFR packets; however, not all of the appendices are applicable to all of the reporting entities.

This year, Appendix G had been added for the Statement of Cash Flows. It contains information from the Governmental Accounting Standards Board's Comprehensive Implementation Guide related to the Statement of Cash Flows.

If you have questions about this memorandum and its contents, please contact your consultant as noted in your entity's AFR Packet or any member of my staff at (225) 342-0708.

AA:mr

Enclosure

**STATE OF LOUISIANA**
**Appendices to the Annual Fiscal Reports**
**Fiscal Year Ended June 30, 2012**

## TABLE OF CONTENTS


| | | |
|---|---|---|
| Appendix A | Deposits with Financial Institutions and Investments | 1 |
| Appendix B | Impairment of Capital Assets and Insurance Recoveries | 15 |
| Appendix C | Net Assets Restricted by Enabling Legislation | 17 |
| Appendix D | Other Postemployment Benefits | 18 |
| Appendix E | Revenues or Receivables – Pledged or Sold | 33 |
| Appendix F | Cooperative Endeavor Agreements | 35 |
| Appendix G | Cash Flow Statement | 37 |

**Appendix A**

# DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS
**(GASB Statements 3, 40, and 53)**

## I. Purpose:

Note C provides the required disclosures about the governmental entities' deposits with financial institutions and investments. The disclosures required for deposits and investments as of the fiscal year ended date provides information about the credit risk and market risk of the deposits and investments and are designed to provide users of the financial statements information about the potential for losses associated with the deposits and investments. GASB Statement 40 has modified or eliminated portions of GASB Statement 3 including:

- modified the custodial credit risk disclosures of Statement 3 for deposits and investments to limit the required disclosure to only those exposed to custodial credit risk (similar to GASB 3's category 3).
- established or modified disclosure requirements related to concentrations of credit risk of investments, credit risk of debt investments, and interest rate risks of debt investments (including sensitivity to changes in interest rates), and
- established disclosure requirements for foreign currency risks for both deposits and investments.

Although GASB Statement 40 eliminated some of the disclosures required for custodial credit risk (the three categories for example), the total reported amounts of all deposits and investments must still be reported.

## II. Comparison of amounts disclosed per requirements in Note C to amounts shown on the Balance Sheet (if Balance Sheet is required as part of AFR packet):

- Because the Balance Sheet reports cash and cash equivalents and investments and the note discloses deposits and investments, the amounts of cash and investments on the balance sheet will not be classified exactly the way they would be classified in Note C.
- "Deposits with Financial Institutions" and "Investments" in Note C may be reported on the balance sheet using titles or line items that are different than those in Note C, or they may be combinations of titles or line items. For instance, "Deposits" in Note C may come from several line items on the balance sheet such as "Cash in Bank" and "Certificates of Deposits (CDs)", or even "Investments" (See section III below that gives further guidance on what should be considered "Deposits" in note C).
- Line items on the balance sheet may include amounts that would be deposits in Note C, and may also include amounts that would be investments in Note C. Also, cash and cash equivalents line items on the balance sheet may include amounts that are not deposited in bank accounts of the entity and therefore would not be reported in Note C as deposits but as separate line items such as petty cash, cash on hand, and treasury cash. These amounts must be reported separately from the deposits in Note C.
- Each line item on the balance sheet that involves cash or investments, including any restricted cash and/or investments, needs to be analyzed to determine what is included in the item and how it should be disclosed in Note C.

## III. "Deposits with Financial Institutions" section of Note C:

- Generally, this section of the Note C disclosure refers to the various examples of "Deposits with Financial Institutions" (See "a" below for examples). The term "cash and cash equivalents" is used in reference to GASB Statement 9 that affects presentation for the balance sheet and statement of cash flows, not the note disclosures required by GASB Statement 3 & 40. "Deposits with Financial Institutions" include deposit accounts in banks, savings and loan associations, and credit unions. They can be demand, savings, or time accounts, including negotiable order of withdrawal (NOW) accounts and non-negotiable CDs. As stated previously, deposits for Note C may be a combination of balance sheet line items or titles.
- Do not include treasury cash, petty cash not in a bank account, or cash on hand in Note C as part of the deposits in bank accounts. As mentioned previously, these amounts would be reported separately.

a. Examples and/or definitions:

1. Nonnegotiable Certificates of Deposit – Nonnegotiable CDs are time deposits that are placed by depositors directly with financial institutions and generally are subject to a penalty if redeemed before maturity. These are treated as deposits for GASB 3 Note C disclosures. For Balance Sheet and Statement of Cash Flows treatment, see Note C(1).
2. Money Market Accounts – financial institution "money market" accounts are simply deposits that pay interest at a rate set to make the accounts competitive with money market mutual funds. They should be treated like any other deposit account for Note C disclosures.
3. Bank Investment Contracts (BICs) – A BIC is a general obligation instrument issued by a bank, typically to a pension plan, that provides for a guaranteed return on principal over a specified period . Since these are issued by a bank, they are treated as deposits for Note C disclosures.

b. Other definitions as applied to deposits:

1. Insured (Insurance) – deposits are insured by federal deposit insurance (FDIC), state deposit insurance, multiple financial institution collateral pools that insure public deposits, and even commercial insurance (if scope of coverage would be substantially the same as FDIC).
2. Collateral – Security pledged by a financial institution to a government entity for its deposits.

## IV. "Investments" section of Note C:

Types of investments for listing investments by type definitions/examples:

1. Negotiable Certificates of Deposit **-** securities with a minimum face value of $100,000, but are normally sold in $1 million units and can be traded in the secondary market. They appeal to institutions interested in low-risk investments with a high degree of liquidity. These are treated as investments for Note C disclosures. For Balance Sheet and Statement of Cash Flows treatment, see Note C(1).
2. Repurchase Agreements – An agreement in which a governmental entity (buyer-lender) transfers cash to a broker-dealer or financial institution (seller-borrower): the broker-dealer or financial institution transfers securities to the entity and promises to repay the cash plus interest in exchange for a) the same securities, or for b) different securities. Include under this category, overnight repos, term repos, open repos, and tri-party repos.

3. U.S. Government Obligations – Generally these investments are not exposed to custodial credit risk because they are issued directly by and backed by the full faith and credit of the U.S. Government. Examples include treasury bills, treasury notes and treasury bonds.
4. U.S. Agency Obligations – Fixed-income securities that are issued by U.S. government-sponsored entities (GSEs). Because of their special GSE status, the market doesn't demand as high of an interest rate as it would from an equivalent private sector issuer because of the perception that the government would step in to back the securities in the case of default. However, the U.S. government does not actually back these debt issues.
5. Common & Preferred Stock – A security that represents an ownership interest in an entity.
6. Mortgages - Examples include mortgage-backed securities and collateralized mortgage obligations. Mortgage-backed securities are created when a financial institution, such as Fannie Mae, purchases mortgages from the banks that issue the mortgages, then the financial institution packages the mortgages and resells them into the secondary market where investors purchase them to earn current income in a relatively safe investment. A collateralized mortgage obligation is a security that is backed by real estate and the issuer is not a governmental issuer, such as Fannie Mae.
7. Corporate Bonds
8. Mutual Funds –
   a. Closed-end Mutual Fund – The investment company sells shares of its stock to investors and it invests on the shareholders' behalf in a diversified portfolio of securities. A closed-end mutual fund has a constant number of shares, the value depends on the market supply and demand for the shares rather than directly on the value of the portfolio, the fund does issue certificates, and the securities are traded on a stock exchange.
   b. Open-end Mutual Funds – The investment company sells shares of its stock to investors and it invests on the shareholders' behalf in a diversified portfolio of securities. In contrast to a closed-end mutual fund, the open-end mutual fund creates new shares to meet investor demand, the value depends directly on the value of the portfolio, and the fund does not issue certificates but sends out periodic statements showing account activity. These investments are not evidenced by securities that exist in physical or book entry form.
9. Investments in real estate, annuity contracts, and direct investments in mortgages
10. Miscellaneous Other – It is not appropriate to present material amounts of investments as "Other", unless the note disclosure describes the composition of the "Other" category. The following are examples of other investments:
    a. Commercial Paper – An unsecured promissory note that is typically sold by a corporation, has a fixed maturity of 1 to 270 days, and is usually sold at a discount from face value.
    b. Guaranteed Investment Contracts - insurance contracts that guarantee the owner principal repayment and a fixed or floating interest rate for a predetermined period of time.
    c. Investments Held in Private Foundations
    d. Investments in pools managed by another government - Generally, these investments would not be exposed to custodial credit risk because the investments themselves are not evidenced by securities that exist in physical or book entry form.
    e. Other Bonds – Examples include foreign government bonds, bond issue trustee accounts, bond index funds, foreign bonds, private placement bonds, and yankee bonds.
    f. Private placements, such as venture capital and limited partnerships
    g. Reverse Repurchase Agreements - An agreement in which a broker-dealer or financial institution (buyer-lender) transfers cash to a governmental entity (seller-borrower); the entity transfers securities to the broker-dealer or financial institution and promises to repay the cash plus interest in exchange for a) the same securities, or for b) different securities.
    h. Any other unique investment not listed above or not included in another category type

**V. Risk Disclosures for Deposits and Investments:**

- Deposits and investments are subject to several types of risks, mainly credit risk, market risk, interest rate risk, and foreign currency risk.

  Credit risk - defined as the risk that a counterparty to an investment transaction will not fulfill its obligations and can be associated with the issuer of securities, with a financial institution holding deposits, or with a party holding investment or collateral securities.

  Concentration of credit risk – defined as the risk of loss attributed to the magnitude of a government's investment in a single issuer.

  Market risk – defined as the risk that the market value of investment securities, collateral securities protecting a deposit, or securities of a repurchase agreement will decline.

  Interest rate risk – defined as the risk that changes in interest rates will adversely affect the fair value of an investment.

  Foreign currency risk – defined as the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit.

A. Custodial Credit Risk Disclosures for Deposits:

Following GASB Statement 3, deposits were classified into three categories of custodial credit risk depending on whether they were insured or collateralized, and who holds the collateral and how the collateral is held.

1. Collateral – Securities pledged by the financial institution for the purpose of securing the governmental entity's deposits.
2. Collateralized – When the entity's deposits are secured with securities pledged by the financial institution holding the deposits.

GASB Statement 40 amended GASB Statement 3 to eliminate the requirement to disclose all deposits by the three categories of risk. GASB Statement 40 requires only the disclosure of deposits that are considered to be exposed to custodial credit risk. An entity's deposits are exposed to custodial credit risk if the deposit balances are 1) uninsured and uncollateralized, 2) uninsured and collateralized with securities held by the pledging financial institution, or 3) uninsured and collateralized with securities held by the pledging financial institution's trust department or agent, but not in the entity's name.

B. Custodial Credit Risk Disclosures for Investments:

Following GASB Statement 3, investments (listed by type) were either classified into three categories (depending on whether they are insured or registered and who holds the securities and how they are held), or listed as non-categorized investments.

GASB Statement 40 amended GASB Statement 3 to eliminate the requirement to disclose all investments by the three categories of risk. GASB Statement 40 requires only the separate

disclosure of investments that are considered to be exposed to custodial credit risk. However, the total reported amount and fair value columns still must be reported for total investments regardless of exposure to custodial credit risk. Those investments exposed to custodial credit risk are reported by type in one of two separate columns depending upon whether they are held by a counterparty, or held by a counterparty's trust department or agent not in the entity's name.

C. Additional Risk Disclosures for Required by GASB Statement 40:

Credit Risk - Disclose the credit risk of debt investments by credit quality ratings as described by rating agencies as of the fiscal year end, including the rating agency used. All debt investments regardless of type can be aggregated by credit quality rating (if any are un-rated, disclose that amount). Examples of un-rated debt investments include U.S. Treasury Notes, external investment pools, or investments held by foundations. The preparer may need to contact their investment advisor for complete information relating to debt investments and their credit quality ratings.

Debt securities issued by a federal government-sponsored enterprise (GSE) and held by a state or local government as an investment are subject to credit risk. GSEs are independent organizations sponsored by the federal government. Examples include the Federal Farm Credit Banks, the Federal Home Loan Bank System, and Student Loan Marketing Association (SLMA). The liabilities of the GSE are **not** backed by the full faith and credit of the federal government.

In November 2008, Federal Home Loan Mortgage Corporation (FHLMC) and Federal National Mortgage Association (FNMA) were taken into conservatorship by the U.S. Government (government). The government entered into a Senior Preferred Stock Purchase Agreement with each of these entities which ensures that each enterprise maintains a positive net worth, which means they are currently backed by the full faith and credit of the federal government. As with U.S. Treasury Notes, a credit quality rating may not be available, but the amount of the investment should be disclosed. For more information on these agreements refer to the Federal Housing Finance Agency http://www.fhfa.gov/Default.aspx?Page=33.

Interest Rate Risk - Disclose the interest rate risk of debt investments by listing the investment type, total fair value, and breakdown of maturity in years of those investments. The preparer may need to contact their investment advisor for complete information relating to the related maturities of these investments.

Highly Sensitive Investments - Disclose the fair value and terms of any debt investments that are highly sensitive to changes in interest rates due to the terms (e.g. coupon multipliers, reset dates, embedded options, etc.) of the investment. Examples of debt investments that are highly sensitive to changes in interest rates include asset-backed securities such as mortgage pass-through securities issued by FNMA, Government National Mortgage Association (GNMA), and FHLMC.

Concentration of Credit Risk - List, by amount and issuer (not including U.S. government securities, mutual funds, and investment pools), investments in any one issuer that represents 5% or more of total investments.

Foreign Currency Risk - Disclose the U.S. dollar balances of any deposits or investments that are exposed to foreign currency risk (deposits or investments denominated in foreign currencies). List these by currency denomination and investment type, if applicable.

Deposits and Investments Policies Relating to Risk - Briefly describe the deposit and/or investment policies related to the custodial credit risk, credit risk of debt investments, concentration of credit risk, interest rate risk, and foreign currency risk disclosed in this note. If no policy exists concerning the risks disclosed, that fact should be stated.

## VI. Securities as Applied to Credit Risk of Deposits and Investments:

Securities defined – a transferable financial instrument that evidences ownership or creditorship. Securities can be in either paper or book-entry form.

1. Examples of securities that are often held by or pledged to (as collateral) governmental entities include:
   a. treasury bills, treasury notes, treasury bonds
   b. federal agency obligations
   c. corporate debt instruments (including commercial paper)
   d. corporate equity instruments
   e. negotiable CDs (key word here is negotiable)
   f. bankers' acceptances
   g. shares of closed-end mutual funds (key word here is closed-end)
   h. shares of unit investment trusts
2. Instruments or investments that are not securities include:
   a. investments made directly with another party (such as limited partnerships)
   b. real estate
   c. direct investments in mortgages and other loans
   d. investments in open-ended mutual funds (keyword here is open-ended)
   e. pools managed by other governments
   f. annuity contracts

## VII. Derivative Instruments:

### What is a derivative?

A derivative instrument is a complex financial instrument or other contract that has all three of the following characteristics:

a. It has (1) one or more reference rates and (2) one or more notional amounts or payment provisions or both. Those terms determine the amount of the settlement or settlements, and, in some cases, whether or not a settlement is required.
b. It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors.
c. Its terms require or permit net settlement, it can readily be settled net by a means outside the contract, or it provides for delivery of an asset that puts the recipient in a position not substantially different from net settlement.

A derivative instrument that is embedded in a financial instrument or contract should be evaluated in accordance with the hybrid instrument guidance in paragraphs 63-66 of GASB Statement No. 53. Fully benefit-responsive Synthetic Guaranteed Investment Contracts (SGICs) should be measured and reported in accordance with the guidance in paragraphs 67 and 79 of GASB Statement No. 53, respectively.

**What financial instruments are excluded from the scope of GASB Statement No. 53?**

a. Normal purchases and normal sales contracts
b. Insurance contracts
c. Certain financial guarantee contracts
d. Certain contracts that are not exchange-traded
e. Loan commitments

**How should derivative instruments be recognized and measured on the financial statements?**

Derivative instruments should be reported on the Statement of Net Assets and measured at fair value. Fair value should be measured by the market price if there is an active market for the derivative instrument. If a market price is not available, a forecast of expected cash flows may be used, provided that the expected cash flows are discounted. Formula-based methods and mathematical methods are acceptable. Fair values of options may be based on an option pricing model, such as the Black-Scholes-Merton model. That model considers probabilities, volatilities, time, settlement prices, and other variables. Fair values developed by pricing services are acceptable, provided that those values are developed using the methods described in this paragraph.

Potential hedging derivative instruments must be evaluated for effectiveness to determine whether it is an investment derivative instrument or a hedging derivative instrument.

Changes in the fair value of hedging derivative instruments are reported as either deferred inflows or deferred outflows in the Statement of Net Assets.

Changes in the fair value of investment derivative instruments should be reported within investment revenue on the Statement of Revenues, Expenses and Changes in Fund Net Assets.

An embedded derivative instrument that is a component of a hybrid instrument should be recognized and measured in accordance with this Statement. An embedded derivative instrument that is a component of a hybrid instrument may also be a hedging derivative if it meets the requirements of this Statement. The companion instrument should be recognized and measured in accordance with the reporting requirements that are applicable to that companion instrument – such as the financial reporting requirements for a debt instrument, a lease, or an insurance contract.

Costs associated with on-behalf payments included in derivative instrument payments should be reported as expenditures or expenses consistent with the manner in which those payments would have been reported if the government had made the payment directly.

**What are the methods for evaluating effectiveness and what does it mean to be effective and/or ineffective?**

Potential hedging derivative instruments should be evaluated for effectiveness as of the end of each reporting period using a method described in paragraphs 36-62 of GASB Statement No. 53. The extent to which these methods are required to be applied in the evaluation of effectiveness is as follows:

a. ***Evaluation of effectiveness in the first reporting period.*** If a potential hedging derivative instrument is first evaluated using the consistent critical terms method and does not meet the criteria for effectiveness of that method, at least one quantitative method also should be applied

before concluding that the potential hedging derivative instrument is ineffective. If a potential hedging derivative instrument is first evaluated using a quantitative method and does not meet the criteria for effectiveness of that method, a government may, but is not required to, apply another quantitative method(s) before concluding that the potential hedging derivative instrument is ineffective. If it is determined that a potential hedging derivative instrument is ineffective in the first reporting period, evaluation of effectiveness in subsequent reporting periods should not be performed for financial reporting purposes.

b. ***Evaluation of effectiveness in subsequent reporting periods.*** All potential hedging derivative instruments that were determined to be hedging derivative instruments in the prior reporting period should be re-evaluated as of the end of the current reporting period using the method that was applied in the prior reporting period. If that method is applied and the hedging derivative instrument no longer meets the criteria for effectiveness of that method, a government may, but is not required to, apply another method(s) before concluding that the hedging derivative instrument is no longer effective.

The methods for evaluating effectiveness discussed in GASB Statement No. 53 include the following:

a. Consistent Critical Terms Method – evaluates effectiveness by qualitative consideration of the critical terms of the hedgeable item and the potential hedging derivative instrument
b. Synthetic Instrument Method – this quantitative method evaluates effectiveness by combining the hedgeable item and the potential hedging derivative instrument to simulate a third synthetic instrument
c. Dollar-Offset Method – this quantitative method evaluates effectiveness by comparing the changes in expected cash flows or fair values of the potential hedging derivative instrument with the changes in expected cash flows or fair values of the hedgeable item
d. Regression Analysis Method – this quantitative method evaluates effectiveness by considering the statistical relationship between the cash flows or fair values of the potential hedging derivative instrument and the hedgeable item
e. Other Quantitative Methods – a government may use a quantitative method to evaluate effectiveness not specifically identified in GASB Statement No. 53 if the method meets ***all*** of the following criteria:
   i. Through identification and analysis of critical terms, the method demonstrates that the changes in cash flows or fair values of the potential hedging derivative instrument substantially offset the changes in cash flows or fair values of the hedgeable item
   ii. Replicable evaluation of effectiveness are generated that are sufficiently complete and documented such that different evaluators using the same method and assumptions would reach substantially similar results
   iii. Substantive characteristics of the hedgeable item and the potential hedging derivative instrument that could affect cash flows or fair values are considered

If the potential hedging instrument is deemed to be effective, it is a hedged derivative instrument; otherwise, it is an investment derivative instrument.

**What financial statement note disclosures should be presented for derivative instruments?**

A. Governments should provide a summary of their derivative instrument activity during the reporting period and balances at the end of the reporting period. The information disclosed should be organized by governmental activities, business-type activities, and fiduciary funds. The information should then be divided into the following categories – hedging derivative instruments (distinguishing

between fair value hedges and cash flow hedges) and investment derivative instruments. Within each category, derivative instruments should be aggregated by type (for example, receive-fixed swaps, pay-fixed swaps, swaptions, rate caps, basis swaps, or futures contracts).

Information presented in the summary should include:

a. Notional amount
b. Changes in fair value during the reporting period and the classification in the financial statements where those fair values are reported
c. Fair values as of the end of the reporting period and the classification in the financial statements where those fair values are reported (if derivative instrument fair values are based on other than quoted market prices, the methods and significant assumptions used to estimate those fair values should be disclosed)
d. Fair values of derivative instruments reclassified from a hedging derivative instrument to an investment derivative instrument, along with disclosure of the deferral amount that was reported within investment revenue upon reclassification

B. Governments should disclose contingent features that are included in derivative instruments held at the end of the reporting period, such as a government's obligation to post collateral if the credit quality of the government's hedgeable item declines. For derivative instruments with contingent features reported as of the end of the reporting period, disclosure should include:

a. The existence and nature of contingent features and the circumstances in which the features could be triggered
b. The aggregate fair value of derivative instruments that contain those features
c. The aggregate fair value of assets that would be required to be posted as collateral or transferred in accordance with the provisions related to the triggering of the contingent liabilities
d. The amount, if any, that has been posted as collateral by the government as of the end of the reporting period.

C. If a government reports a hybrid instrument, disclosures of the companion instrument should be consistent with disclosures required of similar transactions, for example, disclosures for debt instruments. In that case, the existence of an embedded derivative with the companion instrument should be indicated in the disclosures of the companion instrument. For example. if a government has entered into a hybrid instrument that consists of a borrowing for financial reporting purposes and an interest rate swap, the government's disclosure should indicate the existence of the interest rate swap within the debt disclosure.

Derivative instruments often are stand-alone instruments, such as futures contracts. A derivative instrument also may accompany a companion instrument such as a debt instrument, a lease, an insurance contract, or a sale or purchase contract. An embedded derivative instrument may be a call option in a bond, a cap, or floor in a sale or purchase contract, or an interest rate swap in a debt instrument. Alternatively, some derivative instruments may include investing or borrowing transaction. These instruments may give rise to a hybrid instrument, which consists of a derivative instrument and a companion instrument.

A hybrid instrument exists when the instrument meets **all** of the following criteria:

a. The companion instrument is not measured on the statement of net assets at fair value.

b. A separate instrument with the same terms as the derivative instrument would meet the definition of a derivative instrument.
c. The economic characteristics and risks of the derivative instrument are not closely related to the economic characteristics and risks of the companion instrument.

D. Governments that report a Synthetic Guaranteed Investment Contract (SGIC) that is fully benefit-responsive should disclose the following information in the notes to the financial statement as of the end of the reporting period:
   a. A description of the nature or the SGIC
   b. The SGIC's fair value (including separate disclosure of the fair value of the wrap contract and the fair value of the corresponding underlying investments).

Fully benefit-responsive SGIC, the combination of the underlying investments and the wrap contract, should be reported at contract value. An SGIC is fully benefit-responsive if **all** of the following criteria are met:

a. The SGIC prohibits the government from assigning or selling the contract or its proceeds to another party without consent of the issuer.
b. Prospective interest crediting rate adjustments are provided to plan participants and the government on a designated pool of investments by a financially responsible third party. Those adjustments provide assurance that probable future rate adjustments that would result in an interest crediting rate of less than zero is remote. The pool of investments in total meets both of the following criteria:
   i. Is of high credit quality such that the possibility of credit loss is remote
   ii. May be prepaid or otherwise settled in such a way that the government and plan participants would recover contract value.
c. The terms of the SGIC require all permitted participant-initiated transactions with the government to occur at contract value with no conditions, limits, or restrictions. Permitted participant-initiated transactions are those transactions allowed by the government, such as withdrawals for benefits, loans, or transfers to other investment choices.
d. Some events may limit a government's ability to transact with participants at contract value. Examples are premature termination of contracts, layoffs, plan terminations, bankruptcies, and early retirement incentives. The probability of such an event occurring within one year of the date of the financial statements is remote.
e. The government allows participants reasonable access to their investments. The following conditions do not affect the benefit responsiveness of an SGIC:
   i. In plans with a single investment choice, restrictions on access to assets by active participants are consistent with the objective of the plan (for example, retirement benefits).
   ii. Participants' access to their account balances is limited to certain specified times during the plan year (for example, semiannually or quarterly) to control the administrative costs of the plan.
   iii. Administrative provisions that place short-term restrictions (for example, three or six months) on transfers to competing fixed-income investment options to limit arbitrage among those investment options (that is, equity wash provisions).

If plan participants are allowed access at contract value to all or a portion of their account balances only upon termination of their participation in the plan, participants would not have reasonable access to their investments.

The following should be disclosed for hedging derivative instruments:

a. ***Objectives*** - The government should disclose its objectives for entering into the instruments, the context needed to understand those objectives, its strategies for achieving those objectives, and the types of derivatives instruments entered into.

b. ***Terms*** - The government should disclose the significant terms of the transaction, including:
   i. Notional, face, or contract amount
   ii. Reference rates, such as indexes or interest rates
   iii. Embedded Options, such as caps, floors, or collars
   iv. The date when the hedging derivative instrument was entered into and the scheduled
   v. maturity/termination date
   vi. The amount of cash paid or received when the derivative was entered into

c. ***Risks*** - The government should disclose, when applicable, its exposure to the following risks that could give rise to financial loss. Risk disclosures are limited to hedging derivative instruments that are reported as of the end of the reporting period. Disclosures required by this paragraph may contain information that is also required by other paragraphs. However, these disclosures should be presented in the context of a hedging derivative instrument's risk.
   i. *Credit risk* is the risk that a counterparty will not fulfill its obligations. If a hedging derivative instrument exposes a government to credit risk, the government should disclose that exposure as credit risk and also disclose the following information:
      (1) The credit quality ratings of counterparties as described by nationally recognized statistical rating organizations—rating agencies—as of the date of the end of the reporting period. If a credit risk disclosure is required and the counterparty is not rated, the disclosure should indicate that fact.
      (2) The maximum amount of loss due to credit risk, based on the fair value of the hedging derivative instrument as of the date of the reporting period, that the government would incur if the counterparties to the hedging derivative instrument failed to perform according to the terms of the contract, without respect to any collateral or other security, or netting arrangement.
      (3) Information about the policy of requiring collateral or other security to support hedging derivative instruments subject to credit risk, a summary description and the aggregate amount of the collateral or other security that reduces credit risk exposure, and the information about the government's access to that collateral or other security.
      (4) Information about the policy of entering into any master netting arrangements, including a summary description and the aggregate amount of liabilities included in those arrangements, to mitigate credit risk.
      (5) The aggregate fair value of hedging derivative instruments in asset (positive) positions net of collateral posted by the counterparty and the effect of master netting arrangements.
      (6) Significant concentrations of net exposure to credit risk (gross credit risk reduced by collateral, other security, and setoff) with individual counterparties and groups of counterparties. A concentration of credit risk exposure to an individual counterparty may not require disclosure if its existence is apparent from the disclosures required by other parts of this paragraph.
   ii. *Interest rate risk* is the risk that changes in interest rates will adversely affect the fair values of a government's financial instruments or a government's cash flows. If a

hedging derivative instrument increases a government's exposure to interest rate risk, the government should disclose that increased exposure as interest rate risk and also the hedging derivative instrument's terms that increase such a risk. The determination of whether a hedging derivative instrument increases interest rate risk should be made after considering, for example, the effects of the hedging derivative instrument and any hedged debt.

iii. *Basis risk* is the risk that arises when variable rates or prices of a hedging derivative instrument and a hedged item are based on different reference rates. If a hedging derivative instrument exposes a government to basis risk, the government should disclose that exposure as basis risk and should also disclose the hedging derivative instrument's terms and payment terms of the hedged item that creates the basis risk.

iv. *Termination risk* is the risk that a hedging derivative instrument's unscheduled end will affect a government's asset/liability strategy or will present the government with potentially significant unscheduled termination payments to the counterparty. If a hedging derivative instrument exposes a government to termination risk, the government should disclose that exposure as termination risk and also the following information, as applicable:
   (1) Any termination events that have occurred.
   (2) Dates that the hedging derivative instrument may be terminated.
   (3) Out-of-the-ordinary termination events contained in contractual documents, such as "additional termination events" contained in the Schedule to the International Swap Dealers Association Master Agreement.

v. *Rollover risk* is the risk that a hedging derivative instrument associated with a hedgeable item does not extend to the maturity of that hedgeable item. When the hedging derivative instrument terminates, the hedgeable item will no longer have the benefit of the hedging derivative instrument. If a hedging derivative instrument exposes a government to rollover risk, the government should disclose that exposure as rollover risk and should also disclose the maturity of the hedging derivative instrument and the maturity of the hedged item.

vi. *Market-access risk* is the risk that a government will not be able to enter credit markets or that credit will become more costly. If the hedging derivative instrument creates market-access risk, the government should disclose that exposure as market-access risk.

vii. *Foreign currency risk* is the risk that changes in exchange rates will adversely affect the cash flows or fair value of a transaction. If a hedging derivative instrument exposes a government to foreign currency risk, the government should disclose the U.S. dollar balance of the hedging derivative instrument, organized by currency denomination and by type of derivative instrument.

d. ***Hedged debt*** – If the hedged item is a debt obligation, governments should disclose the hedging derivative instrument's net cash flow based on the requirements established by Statement No. 38, *Certain Financial Statement Note Disclosures*, paragraphs 10 and 11.

e. ***Other quantitative method of evaluating effectiveness*** – If effectiveness is evaluated by application of a quantitative method not specifically identified in this Statement, governments should disclose the following information:
   i. The identity and characteristics of the method used
   ii. The range of critical terms the method tolerates
   iii. The actual critical terms of the hedge

The following should be disclosed for investment derivative instruments:

a. ***Risks*** - The government should disclose, when applicable, its exposure to the following risks that could give rise to financial loss. Risk disclosures are limited to investment derivative instruments that are reported as of the end of the reporting period. Disclosures required by this paragraph may contain information that is also required by other paragraphs. However, these disclosures should be presented in the context of an investment derivative instrument's risk.
   i. *Credit risk* is the risk that a counterparty will not fulfill its obligations. If an investment derivative instrument exposes a government to credit risk, the government should disclose that exposure as credit risk and that disclosure should be consistent with the requirements stated above.
   ii. *Interest rate risk* is the risk that changes in interest rates will adversely affect the fair values of a government's financial instruments or a government's cash flows. If an investment derivative instrument exposes a government to interest rate risk, the government should disclose that exposure consistent with the disclosures required by Statement 40, paragraphs 14 and 15. Further, an investment derivative instrument that is an interest rate swap is an additional example of an investment that has a fair value that is highly sensitive to interest rate changes as discussed in Statement 40, paragraph 16. The fair value, notional amount, reference rate, and embedded options should be disclosed.
   iii. *Foreign currency risk* is the risk that changes in exchange rates will adversely affect the cash flows or fair value of a transaction. If an investment derivative instrument exposes a government to foreign currency risk, the government should disclose that exposure consistent with the disclosures required by Statement 40, paragraph 17.

**When should hedge accounting cease to be applied?**

Hedge accounting should cease to be applied upon the occurrence of one of the following termination events:
1. The hedging derivative instrument is no longer effective as determined by applying the criteria stated in a prior question.
2. The likelihood that a hedged expected transaction will occur is no longer probable.
3. The hedged asset or liability, such as a hedged bond, is sold or retired but not reported as a current refunding or advanced refunding resulting in a defeasance of debt.
4. The hedging derivative instrument is terminated.
5. A current refunding or advanced refunding resulting in the defeasance of the hedged debt is executed.
6. The hedged expected transaction occurs, such as the purchase of an energy commodity or the sale of bonds.

If a termination event described in #1 through #4 above occurs, the balance in the deferral account should be reported on the flow of resources statement within the investment revenue classification. If reported separately within investment revenue, the removal of the balance in the deferral account should be captioned *increase (decrease) upon hedge termination*. Once the termination event has occurred, hedge accounting should not be reapplied to that hedging relationship. A derivative instrument from a terminated hedge, however, may be employed as a hedging derivative instrument in a new hedge, provided that the derivative instrument meets the criteria as described in a previous question.

If the termination event is the current refunding or advanced refunding resulting in the defeasance of the

hedged debt, #5 above, the balance of the deferral account should be included in the net carrying amount of the old debt for purposes of calculating the difference between that amount and the reacquisition price of the old debt in accordance with paragraphs 4 and 5 of Statement 23. This approach should be applied regardless of whether the hedging derivative instrument is terminated, notwithstanding paragraph 23. The calculation of the difference between the cash flows required to service the old debt and the cash flows required to service the new debt and complete the refunding and the economic gain or loss resulting from the transaction, as required by paragraph 11 of Statement 7, should include the effects of a hedging derivative instrument.

If the termination event is the occurrence of the hedged expected transaction, #6 above, the disposition of the deferral balance depends on whether the hedged expected transaction results in a financial instrument or a commodity.

a. If the expected transaction results in a financial instrument, the accounting treatment depends on whether the government is re-exposed to the hedged risk.
    1. If the government is re-exposed to the hedged risk, the balance of the deferral account should be recognized on the flow of resources statement within the investment revenue classification.
    2. If the government is not re-exposed to the hedged risk, the balance in the deferral account should be reported on the flow of resources statement consistent with the hedged item. For example, a government hedges its exposure to interest rate risk associated with the expected issuance of fixed-rate debt using a hedging derivative instrument, an interest rate lock. The interest rate lock terminates on the date of the expected issuance of debt. If the fixed-rate bonds are issued and the interest rate lock is terminated, the government is no longer exposed to interest rate risk. In this case, the deferral account should be amortized in a systematic and rational manner over the life of the debt as an adjustment of interest expense.

       The decision as to whether a termination event re-exposes a government to a hedged risk should be based on specific facts and circumstances. If, for example, the interest rate lock in the earlier example is terminated shortly before fixed-rate bonds are issued, the government should consider whether during that interim period, the government's exposure to interest rate risk was significant. In the interim time period or the re-exposure to the identified financial risk is significant, the amount in the deferral account should be removed by recognizing that balance in the flow of resources statement.

b. If the expected transaction results in a commodity, the balance of the deferral account should be removed by reporting the balance as an adjustment to the actual transaction. For example, if the expected transaction is a hedge of market risk associated with the purchase of electricity and the purchase occurs, the balance of the deferral account related to the hedging derivative instrument should be removed by reporting the balance as an adjustment to the cost of energy.

# IMPAIRMENT OF CAPITAL ASSETS AND INSURANCE RECOVERIES (GASB Statement 42)

GASB 42 establishes accounting and financial reporting standards for impairment of capital assets and for insurance recoveries. Governments are required to evaluate prominent events or changes in circumstances affecting capital assets to determine whether impairment of a capital asset has occurred. GASB 42, paragraph 9 outlines five (5) common "indicators of impairment." They are:

1. Evidence of physical damage, such as for a building damaged by fire or flood, when the level of damage is such that restoration efforts are needed to restore service utility.
2. Enactment or approval of laws or regulations or other changes in environmental factors, such as new earthquake standards that a facility does not meet, and cannot be modified to meet.
3. Technological development or evidence of obsolescence, such as that related to a major piece of diagnostic or research equipment.
4. A change in the manner or expected duration of use of a capital asset, such as closure of a building prior to the end of its useful life.
5. Construction stoppage, such as stoppage of construction as a result of a lack of funding.

Damaged assets can be separated into the following categories:

1. assets that will not be returned to service
2. assets temporarily out of service due to needed repairs, restoration, or recertification
3. assets remaining in service but needing repair
4. assets damaged that will continue to be used but will not be repaired

Category 1 assets that are destroyed or so badly damaged that it is not cost effective to restore them are considered to be 100% impaired, and the impairment loss will be equal to the carrying value of the asset at the beginning of the year of the impairment event. The impairment loss for category 1 assets that are not completely destroyed, will no longer be used, and will not be restored will equal the difference between the carrying value at the beginning of the year of the impairment event and the fair value after the impairment event. If the assets are going to be restored (category 2 and 3), then they need to be evaluated for impairment per GASB 42.

For assets impaired by physical damage, the restoration cost approach should be used to calculate the impairment loss. Under this approach, the amount of the impairment loss is derived from the estimated costs to restore the utility of the capital asset. According to the standard, an asset is not considered impaired unless its decline in service utility is significant; therefore, OSRAP has established impairment thresholds for assets impaired by physical damage. In order for an asset to be considered impaired by physical damage, the restoration cost (estimated restoration cost if the asset is not fully restored) of the impaired asset must be equal to or greater than the following:

| | |
|---|---|
| Infrastructure | Greater of $3 million or 20% of the capitalized cost of the infrastructure segment or asset |
| Building | Greater of $100,000 or 20% of the capitalized cost of the building |
| Movable Property | Greater of $20,000 or 20% of the capitalized cost of the asset |

Infrastructure – The magnitude in the decline in service utility will be considered significant if the (estimated) restoration cost exceeds the greater of $3 million or 20% of the capitalized cost of the impaired asset or segment.

Buildings – For buildings impaired by physical damage, the restoration cost threshold is equal to the greater of the capitalization threshold, $100,000, or 20% of the capitalized cost of the building. If the cost to restore the building is lower than the capitalization threshold or 20 percent of the capitalized cost of the impaired building (whichever is higher), we will not consider the "magnitude in the decline in service utility is significant" component of the impairment test to be met. If, however, the building's restoration costs are equal to or greater than the capitalization threshold or equal to or greater than 20 percent of the capitalized costs of the impaired building (whichever is higher), and the building's decline in service utility is "unexpected", we will conclude that the asset has met the impairment test criteria, and is impaired. Note: According to the provisions of GASB 42, an asset is impaired when there is a "significant" and "unexpected" decline in the service utility of a capital asset.

Movable property – For movable property impaired by physical damage, the restoration cost threshold is equal to $20,000, or 20 percent of the capitalized cost of the movable property. If the cost to restore the property is lower than $20,000 or 20% of the capitalized cost of the impaired property (whichever is higher), we will not consider the "magnitude in the decline in service utility is significant" component of the impairment test to be met. If the cost to restore the movable property is equal to or greater than the impairment threshold, $20,000, or 20 percent of the capitalized cost of the impaired movable property (whichever is greater), and the movable property's decline in service utility is unexpected, we will conclude that the asset has met the impairment test criteria, and is impaired according to the provisions of GASB 42.

Category 4 assets do not meet the impairment threshold test because the magnitude in the decline in service utility component of the impairment test would not be met, and no impairment loss will be calculated for these assets.

For assets impaired by enactment or approval of laws or regulations or other changes in environmental factors, technological development or evidence of obsolescence, or a change in the manner or expected duration of use, use the examples provided in GASB 42 for guidance in calculating the impairment loss. The thresholds developed by OSRAP for estimated restoration cost discussed above do not apply to these assets. Report capital assets impaired by construction stoppage at the lower of carrying value or fair value.

An insurance recovery associated with events or changes in circumstances resulting in impairment of a capital asset should be netted with the impairment loss when the recovery and the loss occur in the same year. Restoration or replacement of the capital asset using the insurance recovery should be reported as a separate transaction. Insurance recoveries should be disclosed if not apparent from the face of the financial statements.

GASB 42 requires that the carrying amount of impaired capital assets that are idle at year end be disclosed in the notes, regardless of whether the impairment is permanent or temporary. However, an impairment loss does not have to be calculated for a temporarily impaired asset. If management has to take action to reverse an impairment, such as restoration of a capital asset with physical damage, then the impairment should be considered permanent. In certain circumstances, temporary impairments could be associated with enactment or approval of laws or regulations or other changes in environmental factors, changes in technology or obsolescence, changes in manner or duration of use, or construction stoppage.

# NET ASSETS RESTRICTED BY ENABLING LEGISLATION (GASB Statement 46)

Summary of GASB Statement No. 46 - *Net Assets Restricted by Enabling Legislation*

**Introduction**

The purpose of GASB Statement 46 is to clarify GASB Statement 34's definition of enabling legislation and legal enforceability and give more guidance on how it should be reported in net assets. The goal is to reduce the difficulty of interpreting the requirement in GASB 34 that the restrictions of net assets be "legally enforceable". This statement specifies the reporting requirements if new enabling legislation replaces existing enabling legislation, or if the legal enforceability evaluation changes. Further, the statement requires that governments disclose the portion of total net assets that is restricted by enabling legislation in the notes to the financial statements.

**Enabling Legislation**

Enabling legislation authorizes a government to assess, levy, charge, or otherwise mandate payment of resources (from external resource providers) and includes a legally enforceable requirement that those resources be used only for the specific purposes stipulated in the legislation. For example, a state may pass enabling legislation to add an amount to the automobile registration fee to be used only to fund improvement to the state highway system.

**Legal Enforceability**

Per Statement 46, legal enforceability means that a party external to the government (citizens, public interest groups, judiciary) can compel the government to use the resources created by enabling legislation only for the purposes specified by the legislation. What is considered legally enforceable is a matter of professional judgment. Since enforceability cannot ultimately be proven unless tested through the judicial process, which may never occur, the determination should be based on the facts and circumstances surrounding each individual restriction. A "blanket" or general determination regarding the legal enforceability of enabling legislation should not be used.

**New Enabling Legislation Replacing Original Enabling Legislation**

If new enabling legislation replaces original enabling legislation by establishing new legally enforceable restrictions on the resources raised by the original legislation, then the resources accumulated from that period forward should be reported as restricted for that purpose. However, existing resources accumulated under the original enabling legislation could be restricted for the original purpose, restricted for the purpose specified in the new legislation, or unrestricted. This determination would be a matter of professional judgment.

**Reevaluation of Legal Enforceability**

If resources are used for a purpose other than the purpose stipulated in the enabling legislation, or some other factor causes a reconsideration, then the legal enforceability of those restricted resources should be reevaluated to determine if they should continue to be reported as restricted. If the reevaluation results in a determination that the restriction is no longer enforceable, then report the resources as unrestricted from the beginning of that period forward. If it is determined that the restrictions are still legally enforceable, then continue to report those resources as restricted net assets.

**Note Disclosure Required**

Governments should disclose the portion of total net assets that is restricted by enabling legislation at the end of the reporting period in the notes to the financial statements.

## OTHER POSTEMPLOYMENT BENEFITS (GASB Statement 45)

GASB Statement 45 establishes standards for the measurement, recognition, and display of OPEB expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local governmental employers.

### ANNUAL REQUIRED CONTRIBUTION (ARC)

- Key measure that is basis of OPEB expense recognition
- Represents the level of contribution effort necessary on an ongoing, sustained basis to
  - -cover the normal cost for each year (normal cost is the value of the portion of the ultimate benefit allocated to the current year by cost method), and
  - -amortize the unfunded actuarial liability (UAL), or the difference between the actuarial liability and plan assets (actuarial liability is the value of future plan benefits attributable to past service of members)
- In calculating UAL, due and unpaid or excess contributions should not be included in assets unless settlement is expected not more than one year after the deficiency has occurred or if excess is to be used within one year.

According to GASB 45, when a net OPEB obligation has a liability balance, annual OPEB cost is equal to

(a) the ARC,
(b) plus one year's interest on the beginning balance of the net OPEB obligation,
(c) less an adjustment to the ARC to offset, approximately the amount included in the ARC for amortization of the past contribution deficiencies. (Note: The adjustment is the beginning net OPEB divided by an amortization factor provided by the actuary.)

### NET OPEB OBLIGATION

Below is a sample of an annual OPEB expense and net OPEB obligation (NOO) calculation.

| **Fiscal year ending** | **6/30/2009** | **6/30/2010** |
|---|---|---|
| 1. ARC | $ 1141.1 | $ 852.1 |
| 2. Interest on NOO (4% x 7.) | 36.6 | 73.8 |
| 3. ARC Adjustment (Amortization factor = 26.17) (7. / 26.17) | 34.9 | 70.5 |
| 4. Annual OPEB expense (1. + 2. - 3.) | 1142.8 | 855.4 |
| 5. Contributions | 209.5 | 254.9 |
| 6. Increase in Net OPEB Obligation (4. - 5.) | 933.3 | 600.5 |
| 7. NOO, beginning of the year | 913.8 | 1847.1 |
| 8. NOO, end of year (6. + 7.) | $ 1847.1 | $ 2447.6 |

The actual annual OPEB expense and net OPEB obligation should be calculated based on actual contributions made.

## ALTERNATIVE MEASUREMENT METHOD

A sole employer in a plan with fewer than one hundred total plan members (including employees in active service, terminated employees who have accumulated benefits but are not yet receiving them, and retirees and beneficiaries currently receiving benefits) has the option to apply a simplified alternative measurement method instead of obtaining actuarial valuations. The option also is available to an agent employer with fewer than one hundred plan members, in circumstances in which the employer's use of the alternative measurement method would not conflict with a requirement that the agent multiple-employer plan obtain an actuarial valuation for plan reporting purposes. Those circumstances are:

- The plan issues a financial report prepared in conformity with the requirements of Statement 43 but is not required to obtain an actuarial valuation because (a) the plan has fewer than one hundred total plan members (all employers) and is eligible to use the alternative measurement method, or (b) the plan is not administered as a qualifying trust, or equivalent arrangement, for which Statement 43 requires the presentation of actuarial information.
- The plan does not issue a financial report prepared in conformity with the requirements of Statement 43.

This alternative method includes the same broad measurement steps as an actuarial valuation (projecting future cash outlays for benefits, discounting projected benefits to present value, and allocating the present value of benefits to periods using an actuarial cost method). However, it permits simplification of certain assumptions to make the method potentially usable by nonspecialists. The steps to use this method may be found in paragraphs 33 through 35 of GASB Statement 45 or contact your analyst at OSRAP for further assistance in implementation.

## GLOSSARY

This glossary contains definitions of certain terms; the terms may have different meanings in other contexts.

**Actuarial Accrued Liability, Actuarial Liability, Accrued Liability, or Actuarial Reserve -** That portion, as determined by a particular Actuarial Cost Method, of the Actuarial Present Value of pension plan benefits and expenses which is not provided for by future Normal Costs.

Note: The presentation of an Actuarial Accrued Liability should be accompanied by reference to the Actuarial Cost Method used; for example, by hyphenation ("Actuarial Accrued Liability—XYZ," where "XYZ" denotes the Actuarial Cost Method) or by a footnote.

**Actuarial Assumptions -** Assumptions as to the occurrence of future events affecting pension costs, such as: mortality, withdrawal, disablement and retirement; changes in compensation and Government provided pension benefits; rates of investment earnings and asset appreciation or depreciation; procedures used to determine the Actuarial Value of Assets; characteristics of future entrants for Open Group Actuarial Cost Methods; and other relevant items.

**Actuarially Equivalent -** Of equal Actuarial Present Value, determined as of a given date with each value based on the same set of Actuarial Assumptions.

**Actuarial Cost Method or Funding Method -** A procedure for determining the Actuarial Present Value of pension plan benefits and expenses and for developing an actuarially equivalent allocation of such value to time periods, usually in the form of a Normal Cost and an Actuarial Accrued Liability.

Note: An Actuarial Cost Method is understood to be a Closed Group Actuarial Cost Method unless otherwise stated.

**Actuarial Gain (Loss) or Experience Gain (Loss) -** A measure of the difference between actual experience and that expected based upon a set of Actuarial Assumptions, during the period between two Actuarial Valuation dates, as determined in accordance with a particular Actuarial Cost Method.

Note 1: The effect on the Actuarial Accrued Liability and/or the Normal Cost resulting from changes in the Actuarial Assumptions, the Actuarial Cost Method or pension plan provisions should be described as such, not as an Actuarial Gain (Loss).

Note 2: The manner in which the Actuarial Gain (Loss) affects future Normal Cost and Actuarial Accrued Liability allocations depends upon the particular Actuarial Cost Method Used.

**Actuarial Present Value** - The value of an amount or series of amounts payable or receivable at various times, determined as of a given date by the application of a particular set of Actuarial Assumptions. For purposes of this standard, each such amount or series of amounts is:

a. adjusted for the probable financial effect of certain intervening events (such as changes in compensation levels, Social Security, marital status, etc.),
b. multiplied by the probability of the occurrence of an event (such as survival, death, disability, termination of employment, etc.) on which the payment is conditioned, and
c. discounted according to an assumed rate (or rates) of return to reflect the time value of money.

**Actuarial Present Value of Total Projected Benefits -** Total projected benefits include all benefits estimated to be payable to plan members (retirees and beneficiaries, terminated employees entitled to benefits but not yet receiving them, and current active members) as a result of their service through the valuation date and their expected future service. The actuarial present value of total projected benefits as of the valuation date is the present value of the cost to finance benefits payable in the future, discounted to reflect the expected effects of the time value (present value) of money and the probabilities of payment. Expressed another way, it is the amount that would have to be invested on the valuation date so that the amount invested plus investment earnings will provide sufficient assets to pay total projected benefits when due.

**Actuarial Valuation -** The determination, as of a valuation date, of the Normal Cost, Actuarial Accrued Liability, Actuarial Value of Assets, and related Actuarial Present Values for a pension plan.

**Actuarial Valuation Date -** The date as of which an actuarial valuation is performed.

**Actuarial Value of Assets or Valuation Assets -** The value of cash, investments and other property belonging to a pension plan, as used by the actuary for the purpose of an Actuarial Valuation.

Note: The statement of Actuarial Assumptions should set forth the particular procedures used to determine this value.

**Agent Multiple-Employer Plan (Agent Plan) -** An aggregation of single-employer plans, with pooled administrative and investment functions. Separate accounts are maintained for each employer so that the employer's contributions provide benefits only for the employees of that employer. A separate actuarial valuation is performed for each individual employer's plan to determine the employer's periodic contribution rate and other information for the individual plan, based on the benefit formula selected by the employer and the individual plan's proportionate share of the pooled assets. The results of the individual valuations are aggregated at the administrative level.

**Aggregate Actuarial Cost Method -** A method under which the excess of the Actuarial Present Value of Projected Benefits of the group included in an Actuarial Valuation over the Actuarial Value of Assets is allocated on a level basis over the earnings or service of the group between the valuation date and assumed exit. This allocation is performed for the group as a whole, not as a sum of individual allocations. That portion of the Actuarial Present Value allocated to a valuation year is called the Normal Cost. The Actuarial Accrued Liability is equal to the Actuarial Value of Assets.

Note 1: The description of this method should state the procedures used, including:

a. whether the allocation is based on earnings or service;
b. how aggregation is used in the calculation process; and
c. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, reduce (increase) future Normal Costs.

**Allocated Insurance Contract -** A contract with an insurance company under which related payments to the insurance company are currently used to purchase an immediate or deferred benefit for individual members.

**Amortization (of Unfunded Actuarial Accrued Liability) -** That portion of the pension plan contribution which is designed to pay interest on and to amortize the Unfunded Actuarial Accrued Liability or the Unfunded Frozen Actuarial Accrued Liability.

**Annual OPEB Cost -** An accrual-basis measure of the periodic cost of an employer's participation in a defined benefit OPEB plan.

**Annual Required Contributions of the Employer (ARC) -** The employer's periodic required contributions to a defined benefit OPEB plan, calculated in accordance with the parameters.

**Attained Age Actuarial Cost Method -** A method under which the excess of the Actuarial Present Value of Projected Benefits over the Actuarial Accrued Liability in respect of each individual included in an Actuarial Valuation is allocated on a level basis over the earnings or service of the individual between the valuation date and assumed exit. The portion of this Actuarial Present Value which is allocated to a valuation year is called the Normal Cost. The Actuarial Accrued Liability is determined using the Unit Credit Actuarial Cost Method.

Note 1: The description of this method should state the procedures used, including:

a. whether the allocation is based on earnings or service;
b. where aggregation is used in the calculation process; and
c. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, reduce (increase) the Unfunded Actuarial Accrued Liability.

Note 3: The differences which regularly arise between the Normal Cost under this method and the Normal Cost under the Unit Credit Actuarial Cost Method will affect the determination of future Actuarial Gains (Losses).

**Closed Amortization Period (Closed Basis) -** A specific number of years that is counted from one date and, therefore, declines to zero with the passage of time. For example, if the amortization period initially is thirty years on a closed basis, twenty-nine years remain after the first year, twenty-eight years after the second year, and so forth. In contrast, an open amortization period (open basis) is one that begins again or is recalculated at each actuarial valuation date. Within a maximum number of years specified by law or policy (for example, thirty years), the period may increase, decrease, or remain stable.

**Contribution Deficiencies (Excess Contributions) -** The difference between the annual required contributions of the employer(s) (ARC) and the employer's actual contributions in relation to the ARC.

**Cost-Sharing Multiple-Employer Plan -** A single plan with pooling (cost-sharing) arrangements for the participating employers. All risks, rewards, and costs, including benefit costs, are shared and are not attributed individually to the employers. A single actuarial valuation covers all plan members, and the same contribution rate(s) applies for each employer.

**Covered Group -** Plan members included in an actuarial valuation.

**Covered Payroll -** Annual compensation paid to active employees covered by an OPEB plan. If employees also are covered by a pension plan, the covered payroll should include all elements included in compensation on which contributions to the pension plan are based. For example, if pension contributions are calculated on base pay including overtime, covered payroll includes overtime compensation.

**Defined Benefit OPEB Plan** - An OPEB plan having terms that specify the benefits to be provided at or after separation from employment. The benefits may be specified in dollars (for example, a flat dollar payment or an amount based on one or more factors such as age, years of service, and compensation), or as a type or level of coverage (for example, prescription drugs or a percentage of healthcare insurance premiums).

**Defined Benefit Pension Plan** - A pension plan having terms that specify the amount of pension benefits to be provided at a future date or after a certain period of time. The amount specified usually is a function of one or more factors such as age, years of service, and compensation.

**Defined Contribution Plan** - A pension or OPEB plan having terms that (a) provide an individual account for each plan member and (b) specify how contributions to an active plan member's account are to be determined, rather than the income or other benefits the member or his or her beneficiaries are to receive at or after separation from employment. Those benefits will depend only on the amounts contributed to the member's account, earnings on investments of those contributions, and forfeitures of contributions made for other members that may be allocated to the member's account. For example, an employer may contribute a specified amount to each active member's postemployment healthcare account each month. At or after separation from employment, the balance of the account may be used by the member or on the member's behalf for the purchase of health insurance or other healthcare benefits.

**Employer's Contributions** - Contributions made in relation to the annual required contributions of the employer (ARC). An employer has made a contribution in relation to the ARC if the employer has (a) made payments of benefits directly to or on behalf of a retiree or beneficiary, (b) made premium payments to an insurer, or (c) irrevocably transferred assets to a trust, or equivalent arrangement, in which plan assets are dedicated to providing benefits to retirees and their beneficiaries in accordance with the terms of the plan and are legally protected from creditors of the employer(s) or plan administrator.

**Entry Age Actuarial Cost Method or Entry Age Normal Actuarial Cost Method** - A method under which the Actuarial Present Value of the Projected Benefits of each individual included in an Actuarial Valuation is allocated on a level basis over the earnings or service of the individual between entry age and assumed exit age(s). The portion of this Actuarial Present Value allocated to a valuation year is called the Normal Cost. The portion of this Actuarial Present Value not provided for at a valuation date by the Actuarial Present Value of future Normal Costs is called the Actuarial Accrued Liability.

Note 1: The description of this method should state the procedures used, including:

a. whether the allocation is based on earnings or service;
b. where aggregation is used in the calculation process;
c. how entry age is established;
d. what procedures are used when different benefit formulas apply to various periods of service; and
e. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, reduce (increase) the Unfunded Actuarial Accrued Liability.

**Equivalent Single Amortization Period** - The weighted average of all amortization periods used when components of the total unfunded actuarial accrued liability are separately amortized and the average is calculated in accordance with the parameters.

**Excess Contributions (Contribution Deficiencies)** - See Contribution deficiencies (excess contributions).

**Frozen Attained Age Actuarial Cost Method** - A method under which the excess of the Actuarial Present Value of Projected Benefits of the group included in an Actuarial Valuation, over the sum of the Actuarial Value of Assets plus the Unfunded Frozen Actuarial Accrued Liability, is allocated on

a level basis over the earnings or service of the group between the valuation date and assumed exit. This allocation is performed for the group as a whole, not as a sum of individual allocations. The Unfunded Frozen Actuarial Accrued Liability is determined using the Unit Credit Actuarial Cost Method. The portion of this Actuarial Present Value allocated to a valuation year is called the Normal Cost.

Note 1: The description of this method should state the procedures used, including:

a. whether the allocation is based on earnings or service;

b. how aggregation is used in the calculation process; and

c. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, reduce (increase) future Normal Costs.

**Frozen Entry Age Actuarial Cost Method -** A method under which the excess of the Actuarial Present Value of Projected Benefits of the group included in an Actuarial Valuation, over the sum of the Actuarial Value of Assets plus the Unfunded Frozen Actuarial Accrued Liability, is allocated on a level basis over the earnings or service of the group between the valuation date and assumed exit. This allocation is performed for the group as a whole, not as a sum of individual allocations. The Frozen Actuarial Accrued Liability is determined using the Entry Age Actuarial Cost Method. The portion of this Actuarial Present Value allocated to a valuation year is called the Normal Cost.

Note 1: The description of this method should state the procedures used, including:

a. whether the allocation is based on earnings or service;

b. how aggregation is used in the calculation process; and

c. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, reduce (increase) future Normal Costs.

**Funded Ratio -** The actuarial value of assets expressed as a percentage of the actuarial accrued liability.

**Funding Excess -** The excess of the actuarial value of assets over the actuarial accrued liability.

**Funding Policy -** The program for the amounts and timing of contributions to be made by plan members, employer(s), and other contributing entities (for example, state government contributions to a local government plan) to provide the benefits specified by an OPEB plan.

**Healthcare Cost Trend Rate -** The rate of change in per capita health claims costs over time as a result of factors such as medical inflation, utilization of healthcare services, plan design, and technological developments.

**Insured Benefit -** An OPEB financing arrangement whereby an employer pays premiums to an insurance company, while employees are in active service, in return for which the insurance company unconditionally undertakes an obligation to pay the postemployment benefits of those employees or their beneficiaries, as defined in the employer's plan.

**Investment Return Assumption (Discount Rate) -** The rate used to adjust a series of future payments to reflect the time value of money.

**Level Dollar Amortization Method -** The amount to be amortized is divided into equal dollar amounts to be paid over a given number of years; part of each payment is interest and part is principal (similar to a mortgage payment on a building). Because payroll can be expected to increase as a result of inflation, level dollar payments generally represent a decreasing percentage of payroll; in dollars adjusted for inflation, the payments can be expected to decrease over time.

**Level Percentage of Projected Payroll Amortization Method -** Amortization payments are calculated so that they are a constant percentage of the projected payroll of active plan members over a given number of years. The dollar amount of the payments generally will increase over time as payroll increases due to inflation; in dollars adjusted for inflation, the payments can be expected to remain level.

**Market-Related Value of Plan Assets** - A term used with reference to the actuarial value of assets. A market-related value may be fair value, market value (or estimated market value), or a calculated value that recognizes changes in fair value or market value over a period of, for example, three to five years.

**Net OPEB Obligation** - The cumulative difference since the effective date of this Statement between annual OPEB cost and the employer's contributions to the plan, including the OPEB liability (asset) at transition, if any, and excluding (a) short-term differences and (b) unpaid contributions that have been converted to OPEB-related debt.

**Normal Cost** - That portion of the Actuarial Present Value of pension plan benefits and expenses which is allocated to a valuation year by the Actuarial Cost Method.

Note 1: The presentation of Normal Cost should be accompanied by reference to the Actuarial Cost Method used.

Note 2: Any payment in respect of an Unfunded Actuarial Accrued Liability is not part of Normal Cost (see Amortization Payment).

Note 3: For pension plan benefits which are provided in part by employee contributions, Normal Cost refers to the total of employee contributions and employer Normal Cost unless otherwise specifically stated.

**Open Group/Closed Group** - Terms used to distinguish between two classes of Actuarial Cost Methods. Under an Open Group Actuarial Cost Method, Actuarial Present Values associated with expected future entrants are considered; under a Closed Group Actuarial Cost Method, Actuarial Present Values associated with future entrants are not considered.

**OPEB Assets** - The amount recognized by an employer for contributions to an OPEB plan greater than OPEB expense.

**OPEB Expenditures** - The amount recognized by an employer in each accounting period for contributions to an OPEB plan on the modified accrual basis of accounting.

**OPEB Expense** - The amount recognized by an employer in each accounting period for contributions to an OPEB plan on the accrual basis of accounting.

**OPEB Liabilities** - The amount recognized by an employer for contributions to an OPEB plan less than OPEB expense/expenditures.

**OPEB-Related Debt** - All long-term liabilities of an employer to an OPEB plan, the payment of which is not included in the annual required contributions of a sole or agent employer (ARC) or the actuarially determined required contributions of a cost-sharing employer. Payments generally are made in accordance with installment contracts that usually include interest. Examples include contractually deferred contributions and amounts assessed to an employer upon joining a multiple-employer plan.

**Open Amortization Period (Open Basis)** - See Closed amortization period (closed basis).

**Other Postemployment Benefits** - Postemployment benefits other than pension benefits. Other postemployment benefits (OPEB) include postemployment healthcare benefits, regardless of the type of plan that provides them, and all postemployment benefits provided separately from a pension plan, excluding benefits defined as termination offers and benefits.

**Parameters** - The set of requirements for calculating actuarially determined OPEB information included in financial reports.

**Pay-as-You-Go** - A method of financing a pension plan under which the contributions to the plan are generally made at about the same time and in about the same amount as benefit payments and expenses becoming due.

**Payroll Growth Rate** - An actuarial assumption with respect to future increases in total covered payroll attributable to inflation; used in applying the level percentage of projected payroll amortization method.

**<u>Pension Benefits</u> -** Retirement income and all other benefits, including disability benefits, death benefits, life insurance, and other ancillary benefits, except healthcare benefits, that are provided through a defined benefit pension plan to plan members and beneficiaries after termination of employment or after retirement. Postemployment healthcare benefits are considered other postemployment benefits, whether they are provided through a defined benefit pension plan or another type of plan.

**<u>Plan Assets</u> -** Resources, usually in the form of stocks, bonds, and other classes of investments, that have been segregated and restricted in a trust, or equivalent arrangement, in which (a) employer contributions to the plan are irrevocable, (b) assets are dedicated to providing benefits to retirees and their beneficiaries, and (c) assets are legally protected from creditors of the employer(s) or plan administrator, for the payment of benefits in accordance with the terms of the plan.

**<u>Plan Members</u> -** The individuals covered by the terms of an OPEB plan. The plan membership generally includes employees in active service, terminated employees who have accumulated benefits but are not yet receiving them, and retired employees and beneficiaries currently receiving benefits.

**<u>Postemployment</u> -** The period between termination of employment and retirement as well as the period after retirement.

**<u>Postemployment Healthcare Benefits</u> -** Medical, dental, vision, and other health-related benefits provided to terminated or retired employees and their dependents and beneficiaries.

**<u>Postretirement Benefit Increase</u> -** An increase in the benefits of retirees or beneficiaries granted to compensate for the effects of inflation (cost-of-living adjustment) or for other reasons. Ad hoc increases may be granted periodically by a decision of the board of trustees, legislature, or other authoritative body; both the decision to grant an increase and the amount of the increase are discretionary. Automatic increases are periodic increases specified in the terms of the plan; they are nondiscretionary except to the extent that the plan terms can be changed.

**<u>Projected Benefits</u> -** Those pension plan benefit amounts which are expected to be paid at various future times under a particular set of Actuarial Assumptions, taking into account such items as the effect of advancement in age and past and anticipated future compensation and service credits. That portion of an individual's Projected Benefit allocated to service to date, determined in accordance with the terms of a pension plan and based on future compensation as projected to retirement, is called the Credited Projected Benefit.

**<u>Projected Salary Increase Assumption</u> -** An actuarial assumption with respect to future increases in the individual salaries and wages of active plan members; used in determining the actuarial present value of total projected benefits when the benefit amounts are related to salaries and wages. The expected increases commonly include amounts for inflation, enhanced productivity, and employee merit and seniority.

**<u>Projected Unit Credit Actuarial Cost Method</u> -** A method under which the benefits (projected or unprojected) of each individual included in an Actuarial Valuation are allocated by a consistent formula to valuation years. The Actuarial Present Value of benefits allocated to a valuation year is called the Normal Cost. The Actuarial Present Value of benefits allocated to all periods prior to a valuation year is called the Actuarial Accrued Liability.

Note 1: The description of this method should state the procedures used, including:

a. how benefits are allocated to specific time periods;
b. the procedures used to project benefits, if applicable; and
c. a description of any other method used to value a portion of the pension plan's benefits.

Note 2: Under this method, the Actuarial Gains (Losses), as they occur, generally reduce (increase) the Unfunded Actuarial Accrued Liability.

**<u>Public Employee Retirement System (PERS)</u> -** A state or local governmental entity entrusted with administering one or more pension plans. A PERS also may administer other types of employee benefit plans, including postemployment healthcare plans and deferred compensation plans. A PERS

also may be an employer that provides or participates in a pension plan or other types of employee benefit plans for employees of the system.

**Required Supplementary Information (RSI) -** Schedules, statistical data, and other information that are an essential part of financial reporting and should be presented with, but are not part of, the basic financial statements of a governmental entity.

**Select and Ultimate Rates -** Actuarial assumptions that contemplate different rates for successive years. Instead of a single assumed rate with respect to, for example, the investment return assumption, the actuary may apply different rates for the early years of a projection and a single rate for all subsequent years. For example, if an actuary applies an assumed investment return of 8 percent for year 20W0, 7.5 percent for 20W1, and 7 percent for 20W2 and thereafter, then 8 percent and 7.5 percent are select rates, and 7 percent is the ultimate rate.

**Single-Employer Plan -** A plan that covers the current and former employees, including beneficiaries, of only one employer.

**Special Termination Benefits -** Benefits offered by an employer for a short period of time as an inducement to employees to hasten the termination of services. For example, to reduce payroll and related costs, an employer might offer enhanced pension benefits or OPEB to employees as an inducement to take early termination, for employees who accept the offer within a sixty-day window of opportunity.

**Sponsor -** The entity that established the plan. The sponsor generally is the employer or one of the employers that participate in the plan to provide benefits for their employees. Sometimes, however, the sponsor establishes the plan for the employees of other entities but does not include its own employees and, therefore, is not a participating employer of that plan. An example is a state government that establishes a plan for the employees of local governments within the state, but the employees of the state government are covered by a different plan.

**Stand-Alone Plan Financial Report -** A report that contains the financial statements of a plan and is issued by the plan or by the public employee retirement system that administers the plan. The term stand-alone is used to distinguish such a financial report from plan financial statements that are included in the financial report of the plan sponsor or employer (pension or other employee benefit trust fund).

**Substantive Plan** – The terms of an OPEB plan as understood by the employer(s) and plan members.

**Terminal Funding -** A method of funding a pension plan under which the entire Actuarial Present Value of benefits for each individual is contributed to the plan's fund at the time of withdrawal, retirement or benefit commencement.

**Termination Offers and Benefits -** Inducements offered by employers to employees to hasten the termination of services, or payments made in consequence of the early termination of services. Termination offers and benefits include special termination benefits, early-retirement incentive programs, and other termination-related benefits.

**Transition Year -** The fiscal year in which this Statement is first implemented.

**Ultimate Rate -** See Select and ultimate rates.

**Unfunded Actuarial Accrued Liability, Unfunded Actuarial Liability, Unfunded Accrued Liability, or Unfunded Actuarial Reserve -** The excess of the Actuarial Accrued Liability over the Actuarial Value of Assets.

Note: This value may be negative in which case it may be expressed as a negative Unfunded Actuarial Accrued Liability, the excess of the Actuarial Value of Assets over the Actuarial Accrued Liability, or the Funding Excess.

**Unfunded Frozen Actuarial Accrued Liability or Unfunded Frozen Actuarial Liability -** An Unfunded Actuarial Accrued Liability which is not adjusted ("frozen") from one Actuarial Valuation to the next to reflect Actuarial Gains (Losses) under certain Actuarial Cost Methods. Generally, this amount is adjusted by any increments or decrements in Actuarial Accrued Liability due to changes

in pension plan benefits or Actuarial Assumptions subsequent to the date it is frozen. Adjustments are made from one Actuarial Valuation to the next to reflect the addition of interest and deduction of Amortization Payments.

**Unprojected Unit Credit Actuarial Cost Method -** See Projected Unit Credit Actuarial Cost Method

**Year-Based Assumptions -** See Select and ultimate rates.

## SAMPLE NOTE AND REQUIRED SUPPLEMENTARY INFORMATION (RSI)

Following is the GASB 43 and 45 OPEB note to the financial statements and RSI that was used in the 2011 Comprehensive Annual Financial Report.

## EMPLOYEE BENEFITS - OTHER POSTEMPLOYMENT BENEFITS (OPEB)

### Background

The State of Louisiana compensates its employees in a variety of ways in exchange for their services. In addition to a salary, many employees are provided benefits over their years of service that will not be received until their employment with the State ends. The most common type of these postemployment benefits is a pension. Other postemployment benefits (OPEB) provided are healthcare and life insurance benefits. For fiscal year 2011, costs of providing the State's portion of retiree medical and life insurance benefit premiums were recognized as an expense when the benefit premiums were due and thus were financed on a pay-as-you-go basis.

## A. OFFICE OF GROUP BENEFITS (OGB) PLAN

### Plan Description

Governmental Accounting Standards Board (GASB) Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, effective for the fiscal year ending June 30, 2007, addresses the OPEB reporting requirements for the State's OPEB plan, Office of Group Benefits (OGB). Through self-insured and self-funded OGB programs, premiums are collected and benefits are paid as they come due in accordance with an agreement between the employers and plan members, and their beneficiaries. OGB is the administrator for the agent multiple-employer defined benefit OPEB plan; it provides healthcare coverage and life insurance to eligible participants who are employees of the State, some school systems, and certain non-state employers. A summary of employers and members participating in the plan at June 30, 2012, is as follows:

| | Number of Employers | | Plan Membership |
|---|---|---|---|
| States | 1 | Retirees and beneficiaries | 49,867 |
| School systems | 43 | | |
| Non-state agencies | 87 | Active plan members | 82,910 |
| State agencies | 236 | Total | 132,777 |
| Total | 367 | | |

Benefit provisions are established or may be amended under the authority of LRS 42:802. All benefits and premium structures are reviewed by the OGB Policy and Planning Board. A written report from this Board is forwarded to the House Appropriations Committee and Senate Finance Committee for oversight. OGB does not issue a stand alone financial report on the Plan; however, the financial information is included in the State's Comprehensive Annual Financial Report (CAFR). A copy of the CAFR can be obtained on the website at www.doa.la.gov/osrap-2.htm.

## Summary of Significant Accounting Policies

OGB's financial statements are prepared on the full-accrual basis of accounting using the economic resources measurement focus. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan. The financial statements of OGB include the financial transactions of only the state agencies and are reported in the General Fund. There were no long-term contracts for contributions to the plan, legally required reserves, or designations of net assets for the plan at the reporting date. The financial statements of the non-state agencies and school systems collectively are reported in the agency fund, Non-State Entities OPEB Fund. These agency fund statements are prepared on the accrual basis but do not have a measurement focus, as they report only assets and liabilities.

## Funding Policy

Substantially all employees become eligible for postretirement benefits if they reach normal retirement age while working for the State and are a member of OGB. Life insurance for the individual employee is financed by equal contributions from the State and the employee; insurance for eligible dependents and voluntary optional life products are funded totally through employees' contributions. To be eligible for retiree health insurance coverage, the coverage must be in effect prior to the retirement date. For those beginning participation or rejoining on or after January 1, 2002, the state subsidy of the premium is based on the number of years of participation in a Group Benefits Health Plan. This also applies to dependents who begin coverage after July 1, 2002. LRS 42:851 provides the authority under which the obligations of the plan members, employers, and other contributing entities that contribute to the plan are established or may be amended. OGB offers four standard healthcare plans for both active and retired employees: the Preferred Provider Organization (PPO) Plan, the Health Maintenance Organization (HMO) plan, the Consumer Driven Health Plan (CDHP) with a Health Savings Account (HSA), and the Medical Home Health HMO Plan ((MHHP). Retired employees who have Medicare Part A and Part B coverage also have access to five OGB Medicare supplemental plans. Administrative costs of the OGB plan are financed through the premiums collected for all classes of active and retired plan members. Contribution amounts vary depending on which healthcare provider is selected from the plan, years of participation, and if the member has Medicare coverage. Following is a summary of plan provisions:

## Summary of Plan Provisions

### Health Insurance Monthly Premiums

Employees hired before January 1, 2002, pay approximately 25% of the cost of coverage (except single retirees under age 65 pay approximately 25% of the active employee cost). Total annual per capita medical contribution rates for 2010-2011 are shown in the table below.

Employees hired on or after January 1, 2002, pay a percentage of the total contribution rate upon retirement based on the following schedule:

| Service | Employer Contribution Percentage | Employee Contribution Percentage |
|---|---|---|
| Under 10 years | 19% | 81% |
| 10-14 years | 38% | 62% |
| 15-19 years | 56% | 44% |
| 20+ years | 75% | 25% |

Total Premium Rates are as follows:

| | PPO | HMO | CDHP With HSA | MHHP |
|---|---|---|---|---|
| Active | | | | |
| Single | 558.64 | 527.76 | 433.64 | 532.00 |
| With Spouse | 1,186.56 | 1,120.84 | 921.04 | 1,129.96 |
| With Children | 681.32 | 643.64 | 529.04 | 649.04 |
| Family | 1,251.40 | 1,182.08 | 971.32 | 1,191.68 |
| Retired No Medicare & Re-employed Retiree | | | | |
| Single | 1,039.28 | 985.00 | N/A | 989.52 |
| With Spouse | 1,835.20 | 1,739.24 | N/A | 1,747.60 |
| With Children | 1,157.64 | 1,097.20 | N/A | 1,102.28 |
| Family | 1,826.32 | 1,730.92 | N/A | 1,739.12 |
| Retired with 1 Medicare | | | | |
| Single | 337.96 | 325.88 | N/A | 321.84 |
| With Spouse | 1,248.72 | 1,190.92 | N/A | 1,189.00 |
| With Children | 584.96 | 560.52 | N/A | 557.00 |
| Family | 1,663.80 | 1,585.20 | N/A | 1,584.28 |
| Retired with 2 Medicare | | | | |
| With Spouse | 607.48 | 584.12 | N/A | 578.28 |
| Family | 752.16 | 723.24 | N/A | 716.08 |

All members who retire on or after July 1, 1997, must have Medicare Parts A and B in order to qualify for the reduced premium rates.

| Medicare Supplemental Rates | Retired with 1 Medicare | Retired with 2 Medicare |
|---|---|---|
| Humana HMO | 145.00 | 290.00 |
| Peoples Health HMO | 115.00 | 230.00 |
| Vantage HMO | 258.00 | 516.00 |
| Humana PPO | 149.00 | 298.00 |
| Secure Horizons/United Healthcare PPO Direct | 198.50 | 397.00 |

- Retiree pays 50 cents for each $1,000 of life insurance.
- Retiree pays 88 cents for each $1,000 of spouse life insurance.

## Annual OPEB Cost and Net OPEB Obligation

The Annual Required Contribution (ARC) represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and to amortize any unfunded actuarial liabilities over a period not to exceed thirty years. Effective July 1, 2007, the State implemented GASB 45 prospectively which requires reporting on an accrual basis the liability associated with other postemployment benefits and the OPEB liability at transition was zero. The annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation at the end of the year were as follows (dollar amounts in thousands):

| | Primary Government | Component Units |
|---|---|---|
| Annual Required Contribution | $ 472,125 | $ 231,989 |
| Interest on OPEB Obligation | 66,243 | 33,086 |
| Adjustment to annual required Contribution | (63,282) | (31,607) |
| Annual OPEB cost (expense) | 475,086 | 233,468 |
| Contributions made | (152,871) | (71,125) |
| Increase in net OPEB obligation | 322,215 | 162,343 |
| Net OPEB obligation - beginning of year | 1,656,234 | 827,852 |
| Net OPEB obligation - end of year | $ 1,978,449 | $ 990,195 |

| Fiscal Year | Annual OPEB Cost | Percentage of Annual OPEB Cost Contributed | Net OPEB Obligation |
|---|---|---|---|
| **Primary Govt:** | | | |
| 6/30/2009 | 765,524 | 18.46% | 1,225,742 |
| 6/30/2010 | 578,667 | 25.46% | 1,656,234 |
| 6/30/2011 | 475,086 | 32.18% | 1,978,449 |
| **Component Units:** | | | |
| 6/30/2009 | 377,200 | 18.09% | 621,277 |
| 6/30/2010 | 275,945 | 25.16% | 827,852 |
| 6/30/2011 | 233,468 | 30.46% | 990,195 |

## Funded Status and Funding Progress

As of July 1, 2010, the most recent actuarial valuation date, the actuarial accrued liability for benefits was $6,405,570,000 for the primary government and $2,943,379,000 for component units, all of which was unfunded. The covered payroll (annual payroll of active employees covered by the plan) was $1,806,149,000 for the primary government and $1,447,577,000 for the component units, and the ratio of the unfunded actuarial accrued liability to the covered payroll was 355% for the primary government and 203% for the component units. As of June 30, 2011, the State did not have an OPEB trust. A trust was established with an effective date of July 1, 2008, but was not funded at all, had no assets, and hence had a funded ratio of zero.

Actuarial valuations of the State’s plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress presented as required supplementary information following the notes to the financial statements presents information that shows whether the actuarial value of plan assets is increasing or decreasing relative to the actuarial accrued liabilities for benefits.

## Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities consistent with the long-term perspective of the calculations.

In the July 1, 2010 actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% investment rate of return (net of administrative expenses), which is based on the expected long-term investment returns on the employer's own investments, and on initial annual healthcare cost trend rates of 8% and 9.1% for pre-Medicare and Medicare eligibles, respectively, scaling down to ultimate rates of 5% per year. The unfunded actuarial accrued liability is being amortized using the level percentage of projected payroll amortization method on an open basis. The remaining amortization period at June 30, 2011, was thirty years.

Below is the required supplementary information (RSI) that appeared in the 2011 CAFR:

## OTHER POSTEMPLOYMENT BENEFITS PLANS
## FOR THE YEAR ENDED JUNE 30, 2011
## OGB Plan

The State's Other Postemployment Benefits (OPEB) Plan is administered by the Office of Group Benefits (OGB) as an agent multiple-employer defined benefit OPEB plan. It provides health and life insurance coverage to eligible members. The following tables present the actuarially determined funding progress and required contributions for the OGB OPEB Plan using the projected unit credit cost method.

**Schedule of Funding Progress**
(Expressed in Thousands)

| | Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (AAL) (b) | Unfunded AAL (UAAL) (b-a) | Funded Ratio (a/b) | Covered Payroll (c) | UAAL as a Percentage of Covered Payroll [(b-a)/c] |
|---|---|---|---|---|---|---|---|
| Primary Government | 7/1/2008 | $0 | $9,317,980 | $9,317,980 | 0.00% | $1,641,049 | 567.81% |
| Primary Government | 7/1/2009 | $0 | $7,490,167 | $7,490,167 | 0.00% | $1,830,427 | 409.20% |
| Primary Government | 7/1/2010 | $0 | $6,405,570 | $6,405,570 | 0.00% | $1,806,149 | 354.65% |
| Component Units | 7/1/2008 | $0 | $4,409,394 | $4,409,394 | 0.00% | $1,452,549 | 303.56% |
| Component Units | 7/1/2009 | $0 | $3,413,382 | $3,413,382 | 0.00% | $1,491,615 | 228.84% |
| Component Units | 7/1/2010 | $0 | $2,943,379 | $2,943,379 | 0.00% | $1,447,577 | 203.33% |

**Schedule of Employer Contributions**
(Expressed in Thousands)

| | Fiscal Year Ended | Annual Required Contribution (ARC) (a) | Contributions (b) | Percentage Contributed (b/a) |
|---|---|---|---|---|
| Primary Government | 6/30/2009 | $764,448 | $141,309 | 18.49% |
| Primary Government | 6/30/2010 | $576,478 | $147,050 | 25.51% |
| Primary Government | 6/30/2011 | $472,125 | $152,871 | 32.38% |
| Component Units | 6/30/2009 | $376,648 | $68,234 | 18.12% |
| Component Units | 6/30/2010 | $274,834 | $69,427 | 25.26% |
| Component Units | 6/30/2011 | $231,989 | $71,125 | 30.66% |

# <u>REVENUES OR RECEIVABLES – PLEDGED OR SOLD</u>
# <u>(GASB Statement 48)</u>

## Future Revenues Reported as a Sale

A transaction in which an agency/entity receives proceeds in exchange for cash flows from specific future revenues should be reported as a sale if the agency/entity's continuing involvement with those revenues meets all of the following criteria:

a. The agency/entity does not maintain an active involvement in the future generation of those revenues.

b. The transferee's ability to subsequently sell or pledge the future cash flows is not significantly limited by constraints imposed by the agency/entity either in the transfer agreement or through other means.

c. The cash resulting from collection of the future revenues has been isolated from the agency/entity. Generally, banking arrangements should eliminate access by the agency/entity to the cash generated by collecting the future revenues. Access is eliminated when the revenues are received directly by the transferee or are deposited directly into a custodial account maintained for the benefit of the transferee. However, if the agency/entity is required to remain as the recipient, (1) the cash payments to the transferee should be made only from the resources generated by the specific revenue or receivable rather than from the agency/entity own resources and (2) the cash collected should be remitted to the transferee without significant delay.

d. The contract, agreement, or other arrangement between the original resource provider and the agency/entity does not prohibit the transfer or assignment of those resources.

e. The sale agreement is not cancelable by either party, including cancellation through payment of a lump sum or transfer of other assets or rights.

The agency/entity may cease active involvement in the generation of specific revenues yet remain involved with those revenues in some manner. ***Active involvement generally requires a substantive action or performance by the government.*** Agency/entity should determine whether the *primary* or *fundamental* activity or process that generates the specific revenue requires continuing active involvement. The criteria for active involvement in the future generation of revenues include the following:

a. The agency/entity produces or provides the goods or services that are exchanged for the revenues.

b. The agency/entity levies or assesses taxes, fees, or charges and can directly influence the revenue base or the rate(s) applied to that base to generate the revenues.

c. The agency/entity is required to submit applications for grants or contributions from other governments, organizations, or individuals to obtain the revenues.

d. The agency/entity is required to meet grant or contribution performance provisions to qualify for those revenues.

The agency/entity may remain associated with the specific revenues in ways that do not constitute the primary or fundamental activity that generates the revenues and thus would be considered to have a passive involvement in the generation of those revenues. Activities that would be considered passive involvement include the following:

a. Holding title to revenue-producing assets (leases, rents, or royalty income)

b. Owning a contractual right to a stream of future revenues (tobacco settlement revenues)

c. Satisfying the “required characteristics” eligibility criterion in paragraph 20 of GASB Statement 33, *Accounting and Financial Reporting for Nonexchange Transactions*

d. Agreeing to refrain from specified acts or transactions (agreeing to noncompetition restrictions)

If the criteria required for sale reporting are not met (as described above and in GASB Statement No. 48, paragraphs 6 through 9) a transaction should be reported as a collateralized borrowing.

# COOPERATIVE ENDEAVOR AGREEMENTS
## (Schedule 16)

LRS 33:9022 defines cooperative endeavors as any form of economic development assistance between and among the state of Louisiana, its local governmental subdivisions, political corporations, public benefit corporations, the United States government or its agencies, or any public or private association, corporation, or individual. The term cooperative endeavor includes cooperative financing, cooperative development, or any form of cooperative economic development activity. The state of Louisiana has entered into cooperative endeavor agreements with certain entities aimed at developing the economy of the state.

The net liability for fiscal year ending June 30, 2012, is reported according to funding source, as follows:

- State General Fund
- Self-generated revenue
- Statutorily dedicated revenue
- General obligation bonds
- Federal funds
- Interagency transfers
- Other funds/combination

NOTE: Amounts in excess of contract limits cannot be used to reduce the outstanding contract balance at June 30, 2012. For example, if a contract specifies a percentage of usage for each month (25%) and usage exceeds that percentage (75%), you cannot claim actual usage that exceeds contract requirements (50%).

NOTE: In order to compute the ending balances by funding source, you should begin with your **prior year balances at June 30, 2011**. These amounts will be increased by amounts for new contracts and amendments and decreased for payments as well as for liquidations.

INSTRUCTIONS:

- Use Schedule 16 to report your agency's cooperative endeavors and submit an electronic version via e-mail to katherine.porche@la.gov
- Submit a hard copy of the report with your agency's AFR
- Do not include encumbrances
- Report only the cooperative endeavors that you are obligated to pay
- **DO NOT REPORT** – if your agency is the recipient of the cooperative endeavor
- Payments made during the 45 day close (13th period) are included in the Paid-Inception amount
- Liquidation amounts are included in the Paid-Inception amount
- The seven (7) funding source column amounts must equal "Net Liability at June 30" column
- The "Paid-Inception" plus "Net Liability" columns must equal "Original Amount of Coop" column

TYPE OF APPROPRIATIONS:

- Multi-year appropriation – a contract with an annual obligation of a fixed amount over a number of years
- One-time appropriation – a contract that has an one-time obligation but any remaining amount can and does roll over into the next year or thereafter
- Other appropriation – a contract with an obligation that does not fall under multi-year or one-time appropriation. Attach a brief description of the obligation.

REQUIREMENTS:

1. No cooperative endeavor to report – record "None" on Schedule 16
    - Attach a copy of the Schedule 16 with the AFR
    - Do not send an electronic file to OSRAP
2. Have cooperative endeavor to report:
    - **Must** send an electronic file of Schedule 16 to katherine.porche@la.gov
    - **Must** attach a copy of Schedule 16 with the AFR

AGENCIES - using CFMS:

Most cooperative endeavor contracts are coded with a document type of "COP" in the Contract Financial Management Subsystem (CFMS); however, there are some that are considered cooperative endeavors, but are coded with other document types. Examples of document types are:

- Contracts that fall under delegated authority (AGY or IAT)
- Facility Planning and Control contracts (CEA)
- Certain federal government contracts (OTH or GOV)
- Contracts designated as such by legislative auditors (AGY or IAT)
- Work Incumbent programs (WIP)

# CASH FLOW STATEMENT

The following information is from the Governmental Accounting Standards Board's (GASB) Comprehensive Implementation Guide and provides guidance on reporting cash flows for proprietary funds.

## Operating Activities – General

*Nature of a fund's "operations":*
The primary purpose of a statement of cash flows is to provide relevant information about the cash receipts and cash payments of an entity during a period. The most useful presentation is to provide information about capital and related financing, noncapital financing, and investing activities, as well as cash flows from operating activities. The categories are defined from a functional perspective. Although the operating activities category also is defined, it serves as the residual category. Therefore, cash flow transactions should be evaluated first according to the definitions of capital and related financing, noncapital financing, and investing activities before being included in the operating activities category.

The operating activities category of the statement of cash flows is not intended to be a cash-basis operating statement. The format prescribed is intended to complement the accrual-basis financial statements. In addition, the presentation is not intended to imply that one category is more desirable than any other category. Therefore, there should be no predilection or preference for classifying cash flows in the operating activities category or any other category.

*All items reported as part of operating income be included in the operating activities:*
Classification of a transaction for operating statement purposes should not dictate its classification in the statement of cash flows. The transaction should be evaluated first according to the definitions of the capital and related financing, noncapital financing, and investing activities categories.

Cash flows from operating activities generally are the cash effects of transactions and other events that enter into the determination of operating income. Most nonoperating income items are classified in other than the operating activities category. The reconciliation of operating income to cash flows from operating activities would have fewer reconciling items if the operating activities category were highly correlated to operating income. However, the operating activities category includes all transactions and other events that are not defined as capital and related financing, noncapital financing, or investing activities. Therefore, operating income should not be considered a criterion for classifying cash flows.

If a transaction is included in operating income and its resulting cash flow meets the definition of a category other than operating activities, the item should be presented as a reconciling item in the reconciliation of operating income to net cash flow from operating activities. For example, if a finance authority reports interest income as a component of operating income, the cash received from interest income should be presented in the investing activities category. The reconciliation of operating income to net cash flow from operating activities should begin with reported operating income, and the interest income amount should be deducted as a reconciling adjustment to operating income, similar to depreciation.

## Presentation of Individual Line Items

*Level of Detail:*
In reporting cash flows from operating activities, seven classes of information serve as a minimum level of required detail:

1. Cash receipts from customers
2. Cash receipts from interfund services provided
3. Other operating cash receipts, if any
4. Cash payments to other suppliers of goods or services
5. Cash payments to employees for services
6. Cash payments for interfund services used, including payments "in lieu of taxes" that are payment for, and reasonably equivalent in value to, services provided or received
7. Other operating cash payments, if any.

In all cases, further detail should be provided if the information would be useful.

Gross cash flow information generally is required. Therefore, related transactions should not be netted. For example, bond proceeds should be reported separately from capital purchases made with the proceeds. In addition, separating the principal and interest portions of debt service payments is considered useful.

*Payroll taxes and employee-related costs, such as fringe benefits*
Group cash payments for payroll taxes and fringe benefits with "cash payments to employees," even though the cash is not paid directly to the employees. Payroll taxes and fringe benefits are paid on behalf of employees and are an integral part of employment costs.

*Purchases by internal service fund*
An internal service fund should report its purchases for supplies from vendors separately from purchases from funds of the primary government. Interfund services provided and used should be presented separately from other operating transactions. The intent is to highlight interfund activity.

*Receipts by enterprise fund from state entity and local government participants*
A state governmental enterprise (such as a workers' compensation fund) that has receipts from within the state's entity and also from local government participants, should distinguish from customers inside and outside the entity. Interfund services provided and used should be presented separately from other operating transactions. However, there is no requirement to separate the cash flows with discretely presented component units from cash flows with external parties.

*Debt Service interest payments*
All interest payments associated with "capital debt" should be presented in the capital and related financing activities category as "cash payments to lenders and other creditors for interest." The presentation of cash payments for interest should not be affected by the transaction's presentation on the operating statement or the statement of net assets/balance sheet. The fact that the amount of the cash flow is capitalized does not change the fact that the cash was paid to a lender for interest.

*Rent/Royalty income*
The characteristics of the rent-generating asset should be examined in order to classify rent income as an operating activity or some other activity. The definition of the investing activities category does not specifically address the possibility of an investment's being a tangible capital asset such as land; however, the list of investments described is not intended to be all-encompassing. If the land or other capital asset generating the rent is being held as an investment (because it is being held for appreciation or it is being held temporarily for resale), rent should be classified as an investing activity. Reporting the rent-generating asset on the statement of net assets/balance sheet as an investment rather than a capital asset is evidence that the cash flows should be classified as investing activities.

If, however, the land or capital asset is being managed solely as a rent-generating operation, the cash inflows

from rent should be classified with operating activities. Royalty income should be evaluated in the same manner.

*Miscellaneous income and expense*
Miscellaneous cash flows should be included in the operating activities category even if the income or the expense is considered a nonoperating income item. The operating activities category is not limited to the cash flows resulting from operating income items. Unless the cash flows specifically meet the definition of the noncapital financing, capital and related financing, or investing activities category, they should be presented in the residual category – operating activities. If nonoperating income items, such as miscellaneous income or expense, are included in the operating activities category, an adjustment should be made to operating income in the reconciliation of operating income to net cash flow from operating activities.

*Investment earnings*
Gains and losses on investments should not be presented in the statement of cash flows. Rather, proceeds from the sale of the investments (including gains and net of losses) should be reported as a cash inflow in the investing activities category.

Investment earnings are sometimes included in operating income. However, they should be classified in the investing activities category. The statement of cash flows is not intended to replicate, on a cash basis, the operating statement.

*Interfund transfers*
The cash portion of an interfund transfer out should be presented in the noncapital financing activities category. A governmental enterprise fund receiving a transfer to be used for the specific purpose of defraying the cost of acquiring, constructing, or improving capital assets, however, should classify the cash inflow as a capital and related financing activity.

**Investments, Cash, and Cash Equivalents**

*Cash equivalents*
A cash equivalent is limited to investments with an original maturity of three months or less. The definition of cash equivalents refers to short-term, highly liquid investments that are both (a) readily convertible to known amounts of cash and (b) so near their maturity that they present insignificant risk of changes in value because of changes in interest rates.

*Original maturity*
Original maturity is based on the date the investment is purchased. If, on the purchase date, a qualifying investment will mature in three months or less, it is a cash equivalent. The evaluation should be made only once, as of the purchase date.

*Investments and cash equivalents*
If an instrument is treated as a cash equivalent, its conversion to or from cash or another cash equivalent would not be reported on the statement of cash flows. The transaction is analogous to the transfer of cash between two checking accounts. If, on the other hand, an instrument is treated as an investment, its conversion to or from cash or a cash equivalent should be reported in the investing activities category of the statement of cash flows, and the cash flows usually should be presented gross.

## Identifying a Cash Flow

*Cash flow*

Sometimes there may be a question as to whether a cash transaction has occurred. It may be confusing to identify a cash flow in a banking environment. Generally, cash flows only if it changes hands; that is, ownership of cash legally changes. In an internal exchange transaction conducted totally within a bank, a cash transaction occurs only if a debit or credit is made to a governmental enterprise's bank account. For example, a service charge or interest income is considered to be a cash transaction on the date the bank posts the amount to the account. After that date, the interest amount is available for withdrawal or the amount posted for the service charge is no longer available for withdrawal. Another example is a loan granted by a bank. If the loan proceeds are credited to the borrower's bank account, a cash flow occurred. If the bank remitted the proceeds directly to the vendor, a noncash financing activity occurred.

*Bond issuance costs and underwriter fees*

If bond issuance costs and underwriter fees were deducted from bond proceeds, the governmental enterprise experiences only one cash flow. The net amount of bond proceeds actually received should be presented as a cash inflow in the appropriate category (either capital and related financing or noncapital financing, depending on the purpose of the borrowing).

On the other hand, if a governmental enterprise receives the proceeds from the sale of bonds and pays bond issuance costs and underwriter fees separately, the following cash flows should be presented: The total amount of bond proceeds should be presented as a cash inflow in the appropriate category (either capital and related financing or noncapital financing, depending on the purpose of the borrowing). The costs and fees that are paid from the governmental enterprise's cash or cash equivalents should be presented as cash outflows in the same category.

*Roll over of certificate of deposit*

If a certificate of deposit that does not meet the definition of a cash equivalent automatically rolls over at maturity, there is no cash flow. There is no cash flow unless there is a deposit to or withdrawal from cash or a cash equivalent. Therefore, a rollover does not affect the statement of cash flows. The certificate of deposit is merely converted from one investment instrument to another.

## Noncash Investing, Capital, and Financing Activities

*Required disclosure*

Information about all investing, capital, and financing activities of a governmental enterprise during a period that affect recognized assets or liabilities but do not result in cash receipts or cash payments in the period should be reported. Disclosure of noncash information is required if a transaction meets all of these three characteristics:

1. Some transactions are part cash and part noncash. Only the cash portion should be presented in the statement of cash flows. The noncash portion should be evaluated further.
2. Noncash assets and liabilities should be analyzed. Changes in the balance of a noncash asset or liability that are not attributable to cash transactions should be considered noncash transactions. For example, when an enterprise enters into a capital lease for a building, a noncash transaction occurred because a capital lease obligation and the building were recorded in the statement of net assets. The inception of an operating lease, on the other hand, requires no disclosure because there is no balance sheet effect.

3. A noncash transaction should be disclosed only when it (had it been a cash transaction) meets the definition of the investing, capital and related financing, or noncapital financing activities category. For example, a capital lease transaction meets the definition of a capital and related financing activity. However, an account receivable balance removed in exchange for the forgiveness of an account payable is an operating activity and is not required to be disclosed.