

GASB - 34: One Way to Protect your Assets

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Twice this year, I had the pleasure of being a co-presenter at training for wastewater plant operators. Each time I spoke it was about financial issues, with both sessions including material regarding accounting and reporting standards for municipal wastewater treatment plants. As these were my first forays into training specifically on such matters, I asked for a show of hands as to who had heard of GASB-34, the topic of presentation (and this article).

GASB what? The silence was deafening as you could have heard a pin drop each time after asking that question. At the first session, out of fifty attendees, only one raised his hand (and he was from Vermont and not New York state certified!) At the second session, not one hand was raised out of about twenty or so in attendance. Apparently, operators at the front-line level, my typical training audience member, are not aware of this important issue, let alone the potential impact this could have to their facility and communities.

What is GASB-34?

GASB is an acronym for the Governmental Accounting Standards Board, the group that sets accounting and financial reporting standards for state and local governments. A similar group, FASB, sets standards for private corporations. According to the GASB mission statement found on their website: www.gasb.org, a key goal of the organization is to develop and improve standards to provide useful information to users of financial reports. These end users would typically be elected or public officials, customers and ratepayers, auditors, and potential lenders.

Specifically, Statement 34 is a proclamation made by GASB in 1999 that requires state and local governments to begin reporting on the value of their infrastructure assets; roadways, collection systems, treatment facilities, etc. In addition, Statement 34 also requires these governments to develop procedures and methods for asset management systems. There are other features of Statement 34 that will not be presented, as the focus here will be on the reporting requirements for infrastructure assets.

Consider everything that your system “owns”. For a wastewater treatment facility this could include a multi-million dollar treatment facility, pump stations, collection system, solids handling units, etc. Each of these is considered “assets” and has tangible value to them. What Statement 34 does is provide the framework for your community to account for these assets and report the use of these assets as a cost of doing business.

Statement 34 is not a mandatory regulatory requirement, although adherence to it is strongly encouraged. Remember, the goal is to improve financial information to end users of this information, such as when a system is proposing a new rate structure or seeking funding for a capital improvement project. Besides, it is just good business practice to have current information on what systems are in place, what condition each is in, and what future repair and replacement needs are.

Why is this important?

Before answering this question it is important to highlight just where we are in terms of the condition of publicly owned infrastructure. For example, consider the facts about much of the wastewater treatment systems in New York. Much of the treatment units were the direct result of the need for clean water in the 1960's and 70's. Collections systems, if not new then, had been in place for some time, over 100 years in some cases. The useful life expectancy of much of this original infrastructure is nearing the end point.

Aging of the infrastructure (water, sewer, or roadway), fewer government grant funds, increasing regulatory issues, and additional service demands all combine today to form a "Perfect Storm" scenario with the potential for devastating effects on municipal finances and services. Further, many municipalities do not know just what they have in terms of these assets or what condition these are in. To address this, many groups have been pro-actively working to communicate these potential effects and provide the necessary tools to assist communities.

Now lets get back to why GASB-34 is important. Strictly from a financial point, there are several reasons. One is that it will provide information required by those whom you will be seeking money from when it comes time for a capital-intensive project requiring a bond, such as through the Environmental Facilities Corporation (EFC). EFC and other potential investors will likely require greater insight into the condition of both existing infrastructure and municipal finances. These will determine whether a loan will be made and on what terms (rate, covenants, etc.)

A second reason is that it makes good business practice to maintain existing assets is that it extends the useful life of infrastructure assets. This should ensure reliable and efficient service and reduce overall capital investment needs. Just as it is good practice to remove solids from a clarifier in smaller amounts more frequently, tending to the needs of infrastructure assets on an on-going basis is preferable to large, infrequent, and costly replacement.

Additional reasons for adhering to GASB-34 include the ability to better plan capital improvement projects, work schedules, and operate more efficiently. It is often said that knowledge is power and here it is no different. Having knowledge of the condition level of infrastructure assets in your community will allow you have options, be it for planning repairs or replacements, or when failure does occur, what the appropriate response should be.

What does it take to adhere to GASB-34?

Two approaches are explicitly offered by GASB, the Depreciation Method and the Modified Approach, each is detailed below.

Depreciation Method

For each asset you must know the year it was placed in service, the original acquisition cost (ancillary costs minus salvage value) and the useful life, in years.

To determine the amount to depreciate each year simply divide the asset cost by the number of years. This is the "cost of doing business" I referred to earlier, as depreciation is considered an expense item when determining net income.

Typically, useful life amounts are consistent based upon unit. For example, the useful life of a wastewater treatment system is 25 years, while a concrete collection system is 50 years. Useful life

information is readily available via an on-line search or through a professional accountant.

Modified Approach

This alternative allows the municipality to substitute the expense of maintaining the system for depreciation. For this approach, the municipality sets a condition level at which the infrastructure assets must be maintained.

Then, at least every three years you must assess the condition of these infrastructure assets. Then, you would expense annually the amount to maintain these infrastructure assets to that pre-determined level. This expense will be in place of the "Depreciation" amount listed above.

Statement 34 does not prescribe a condition assessment system to use. Rather it must be designed to be "replicable" and must also be well documented. In practice, using this same assessment approach would result in "substantially similar" results regardless of the person doing the measurement. Examples of assessment systems that would meet the requirement of this approach include elimination of a percentage of Inflow & Infiltration (I&I), cleaning a percentage of the collection system annually, and reduction in the number of dry weather overflow events.

Of course, there are benefits and drawbacks with either option.

Using the Depreciation Method, some positives include the simplicity of the method and less of a likelihood that problems will be encountered during an audit. Most financial people in your organization will probably be familiar with depreciation and may even offer various strategies in using it.

On the downside, depreciation provides just a dollar figure and not the actual condition of your system. This is crucial. In older systems, depreciation presents an unreasonably low cost of doing business. This could result in significant overhang liabilities resulting from deferred repair and replacement (R&R) of infrastructure assets.

As for the Modified Approach, it is better at providing an actual assessment of the infrastructure asset conditions, and potentially an excellent survey depending upon the assessment system used. This approach also reflects the actual value of the infrastructure assets, providing more meaningful information to decision makers.

There are several downside features to this approach, however, the most significant being the up-front expense of developing an assessment system. These costs include establishing a database of assets and other source material. A crucial item to consider is when the Modified Approach does not result in the established target levels being met. If this happens, the Depreciation Method must then be used. This probably would not be well received by decision makers, politicians, customers, and lenders.

A third approach, that I first found at the informative Brown and Caldwell website, is to incorporate features from both the Depreciation Method and Modified Approach. For this third option, you would use the Depreciation Method to produce numbers for the financial reports (i.e. "Expenses"), and then use the Required Supplemental Information (RSI) section to report details of assets and condition assessments.

The RSI is where a utility is required to report budgetary, and asset and assessment condition measurement details if using the Modified Approach. However, when using the Depreciation Method, a utility can also use the RSI for additional information to report accomplishments and plans for the system. Essentially, this allows you to capture the benefits of the Modified Approach while avoiding many of the disadvantages it presents.

Additionally, no matter what reporting choice is made, you must include what Statement 34 calls "Management's Discussion and Analysis" or MD&A. The purpose of the MD&A section is for management to introduce the basic financial statements and provide an overview of the government's financial activities. This section should provide an objective and easy to read analysis of what the government knows to be factual. Management should make comparisons to prior years, indicate what financials measure have improved or deteriorated, and describe significant changes to budgets, capital assets, or long-term debt over the preceding year.

When does GASB-34 begin?

Answer: Now! Yes, by this time all communities should have adopted the requirements of Statement 34. Here are the dates provided in GASB-34 regarding implementation dates:

Large governments (> \$100 million in total revenues 1998-99)
Implement for financial periods beginning after June 15, 2001 (Fiscal Year 2002)

Medium governments (> \$10 million in total revenues 1998-99)
Implement for financial periods beginning after June 15, 2002 (FY 2003)

Small governments (< \$10 million in total revenues 1998-99)
Implement for financial periods beginning after June 15, 2003 (FY 2004)

If you'd like to learn more about Statement 34 and other financial management issues, here are several resources I've found useful:

EPA Finance Center www.maxwell.syr.edu/efc/ and <http://sspa.boisestate.edu/efc/>

GASB <http://www.gasb.org/>

Brown and Caldwell http://www.bcwaternews.com/socalh2onews/asset/am_index.htm

There are a number of pieces that are required in order to "solve" the financial management puzzle for your system. Anything that pertains to spending or receiving monies on your system can be included in the financial plan. Among the more visible, and more controllable elements of the financial plan are; rate setting, budgeting, capital improvement planning, and adherence to GASB Statement - 34. Addressing these collectively will allow your community to recognize current asset conditions, plan effectively for future needs, and continue delivering high quality service at rates that reflect realistic conditions and projections.