GASB No. 69: Government Combinations and Disposals of Government Operations

Presented by:

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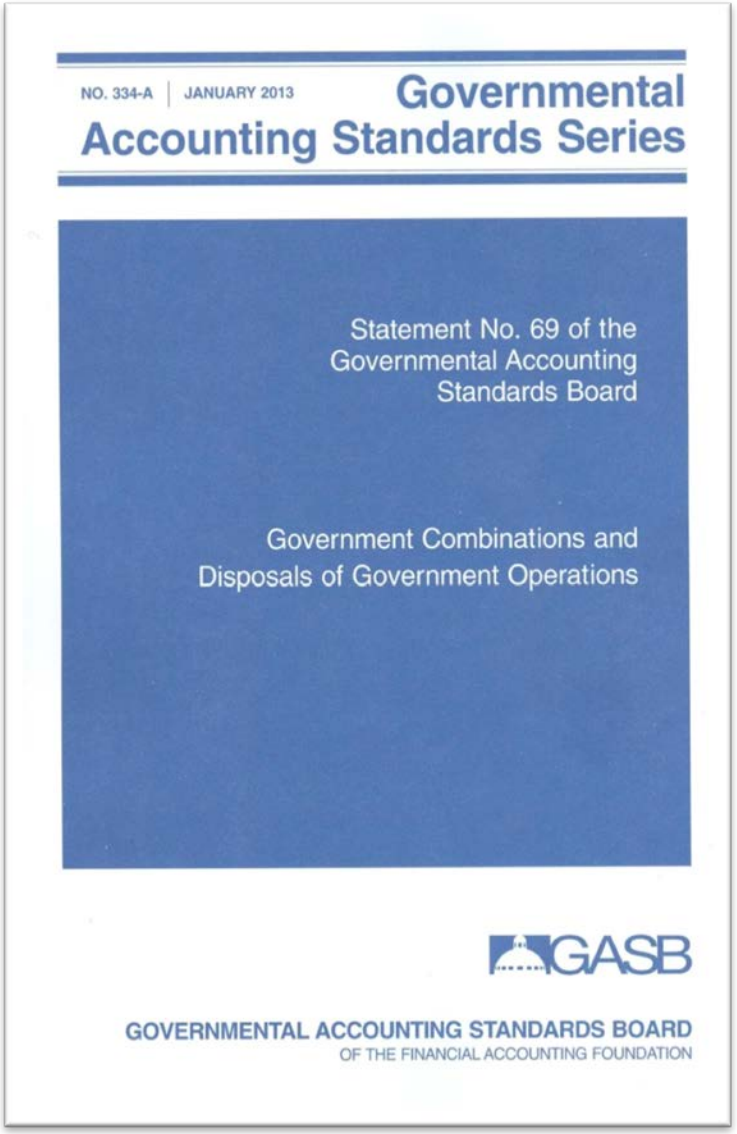
Issued January 2013

Effective for periods beginning after December 15, 2013



Project objectives

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- Consider the financial reporting requirements for government combinations that are accomplished through mergers, acquisitions, and transfers of operations
  - Addresses government's unique conditions and circumstances
- Analysis of government combinations that have taken place in both the general government area (ex. city/county consolidations), and the business type activities area (ex. healthcare organizations)
- Address certain spin-off issues (ex. A library district that was formerly a department in a primary government) – a transfer of operations

Existing guidance

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- Accounting Principles Board (APB) Opinion No. 16, Business Combinations
  - This guidance was never intended for the public sector and its application to the public sector has proven to often be problematic.
  - Addresses conditions and circumstances that are not normally encountered in government combinations.
- Because this separate project was on the Board's agenda, did not incorporate into Statement 62
- APB 30—Discontinued operations
- FASB 141 and revisions—Business combinations
- FASB 164—Not-for-profit entities, mergers and acquisitions (government healthcare entities?)

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Scope includes:

- Combinations in which NO consideration is provided
  - Government mergers
  - Transfers of operations
- Combinations in which consideration is provided
  - Government acquisitions
- Disposals of government operations

Scope does not include:

- Assets and liabilities comprising less than an operation
- Obtaining control of another organization that remains a legally separate entity (already addressed in Statement 14)
- Acquisition of equity interest (already addressed in Statement 14)

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To distinguish a combination from an acquisition of assets and related liabilities, consider:

- “Operations” is defined as an integrated set of activities conducted and managed for the purpose of providing identifiable services with associated assets and liabilities
- Service continuation: Obligation or responsibility (intent) to continue to provide the services that were provided by the previously separate governments, organizations, or operations

Government Combinations

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- To be considered a government combination, the arrangement should result in the continuation of a substantial portion of the services provided by the previously separate entities or their operations after the transaction has occurred.
  - Terms of arrangement usually establish whether service continuation was intended
  - If not, professional judgment should be used
- This distinguishes a combination from a contribution or purchase of assets and related liabilities

Overall approach

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- The requirements distinguish between government combinations that involve significant (or lack) of financial consideration
  - **Government merger**—combinations of legally separate entities without the exchange of significant consideration
  - **Government acquisitions**—transactions in which a government acquires another entity, or its operations, in exchange for the payment of significant consideration
- Combinations not involving entire legally separate entities and in which no significant consideration is exchanged (shared service arrangements, reorganizations, redistricting, annexations, arrangements where an operation is transferred to a new government created to provide those services) – transfer of operations

Types of government combinations

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Government merger

> Insignificant or no consideration exchanged, and either:
  - Two or more separate legal entities combine to form a new entity
  - One or more of the prior entities cease to exist

Government acquisition

> One government acquires another entity (or its operations) in exchange for significant consideration

Transfer of operations

> A government combination involving operations rather than a legally separate entity

> Could be a transfer to a continuing entity or creation of a new entity

Government mergers

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- Often guided by statute
- Some states have passed or considered legislation to cause or encourage streamlining (too many layers)

Government mergers

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An entirely new government is formed (A+B=C) OR

Two or more governments (or one or more governments and one or more nongovernmental entities) cease to exist as legally separate entities and are combined to form one or more new governments

- Merger date is the date the combination becomes effective
- Initial reporting period of the new government begins on the merger date
- The assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the merging entities would be recognized and measured in the statement of net position at their “carrying value” as of the merger date

Government mergers

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If the merging entities decide before the merger date to dispose of capital assets and the new government will use those capital assets until the disposal occurs

> Capital assets should be measured and reported at their carrying values by the new government

If the new government will not use the capital assets that have been identified for disposal or if the merging entities decide before the merger date that the manner or duration of use of capital assets will change

> Capital assets should be evaluated for impairment in accordance with provisions of Statement 42, as amended to determine if the carrying values should be adjusted

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A single continuing government remains (A+B=B+)

One or more legally separate governments or nongovernmental entities cease to exist and their operations are absorbed into, and provided by, one or more continuing governments

- Merger date is the beginning of the reporting period in which the combination occurs, (as though the entities were already combined as of that date) regardless of the actual date of the merger
- The assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the merging entities would be measured in the statement of net position at their “carrying value” as of the merger date

Government mergers

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- If the merging entities decide before the actual date of the merger to dispose of capital assets of the dissolving government but the continuing government will use those capital assets until the disposal occurs
  - Capital assets should be measured and reported at their carrying values by the continuing government
- If the continuing government plans to dispose of the capital assets that it will not use or if decisions are made before the actual date of the merger that the manner or duration of use of specific capital assets of the dissolving government will change
  - Capital assets should be evaluated for impairment in accordance with provisions of Statement 42, as amended

Government acquisitions

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- Acquisition date is the date the acquiring government obtains control of the acquired entity's assets or becomes obligated for its liabilities or its operations (typically when consideration is paid)
- Assets and liabilities normally would be recorded at their acquisition value as of the acquisition date – price that would be paid for acquiring similar assets, having similar service capacity, or discharging the liabilities assumed as of the acquisition date
- Deferred outflows of resources and deferred inflows of resources should be brought forward at their carrying values

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Consideration Given:

If exceeds the net position acquired, the difference would be treated as a deferred outflow of resources

> Attributed to future periods in a systematic and rational manner, based on professional judgment

If net position exceeds the consideration given

> Considered a contribution – if the seller accepted the lower amount for the purpose of providing an economic benefit to the acquiring government

- If not – the difference would be eliminated by reducing the acquisition values assigned to noncurrent assets (other than investments reported at fair value).
- If the difference exceeded the acquisition value of all noncurrent assets (other than investments reported at fair value), the remainder would be treated as a special item in the flows statement.

Transfers of operations

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Government combination involving the operations of a government or nongovernmental entity, rather than a combination of legally separate entities, and in which no significant consideration is exchanged.

> Operation-an integrated set of activities with associated assets and liabilities that is conducted and managed for the purpose of providing identifiable services.

Transfers of operations

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- Entered into for similar reasons as government mergers
- Transfer date is the date the transferee government obtains control of the acquired operation's assets or becomes obligated for its liabilities.
  - If the transfer of operations results in the formation of a new government – the new government's initial reporting period begins at the effective transfer date
  - If the transfer of operations results in a continuing government – the continuing government should report the transfer as a transaction in the financial statements for the reporting period in which it occurs

Transfers of operations

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> Assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the transferred operation would be incorporated at their carrying value as of the effective transfer date

Disposals of government operations

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The disposing government would report a special item for any gain or loss on the disposal of operations in the period in which the disposal occurs, based on either:

> Effective transfer date of the transfer of operations, or

> The date of sale for operations that are sold

Disclosures

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The following disclosures are required for all government combinations:

Brief description of the combination that

- Identifies the entities involved and the primary reasons for the combination
- Mentions whether the entities combined were part of the same financial reporting entity
- Discloses the date of the combination

Additional disclosures for

- Mergers and transfers of operations
- Acquisitions
- Disposals of Operations

Disclosures: Mergers and transfers

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- Carrying values recognized as of the merger date
  - Current, capital, and other assets
  - Deferred outflows of resources
  - Current and noncurrent liabilities
  - Deferred inflows of resources
  - Net position by component
- Description of significant adjustments
- Initial amounts recognized, if different from adjusted carrying values

Disclosures: Acquisitions and disposals

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Acquisitions

> Brief description of consideration provided

> Total amount of net position acquired

> Brief description of contingent consideration arrangements

Disposals of operations

> Description of the circumstances leading to the discontinuation

> Operation's revenues, expense, and non-operating items

Effective date and transition

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Applied prospectively

Earlier application is encouraged

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Examples of combinations – GASB No. 69

Case 1

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Case 1:
Facts: A government acquires a governmental entity, and the entity remains legally separate
Question: Does this qualify as a government combination (merger, acquisition, transfer of operations)?

Case 1 (cont.)

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Case 1:
Answer: No.
Why is the answer no? This is not a government combination, because one or more of the entities <u>did not</u> cease to exist
Other consideration: The acquiring government should evaluate whether to include the other entity in its reporting entity as a component unit (or as an investment) and, if so, whether to discretely present or blend

Case 2

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Case 2:
Facts: Two villages decide to combine into a new government, with no exchange of significant consideration, and there will be continuation of service
Question: Does this qualify as a government combination (merger, acquisition, transfer of operations?

Case (cont.)

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Case 2:
Answer: Yes. This is a government merger.
Question: What is the merger date (the initial reporting period)? – Start of the villages former fiscal years, 7-1-11 – Date of the public referendum approving the merger, 11-2-11 – Date merger becomes effective, 1-1-12

Case 2 (cont.)

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Case 2:
Question: What is the merger date (the initial reporting period)?
Answer: The date merger becomes effective, 1-1-12

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Sunday	Monday	Tuesday	Wednesday	Thursday	Friday	Saturday
1	2	3	4	5	6	7
8	9	10	11	12	13	14
15	16	17	18	19	20	21
22	23	24	25	26	27	28
29	30	31				

Case 2 (more details, cont.)

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Case 2:
More details: – Asset impairment of $4 million related to redundant capital assets that will be sold – Adjustment made to inventory valuation methods for consistency results in a reduction of $80,000
Question: What is the first step in establishing initial amounts for the new government?

Case 2 (cont.)

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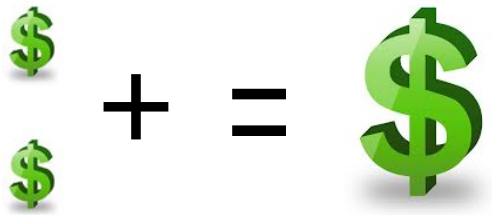
Case 2:

Answer: The first step in establishing initial amounts for the new government is to combine the carrying values as of the merger date



Case 2 (cont.)

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	Village A	Village B	Total
ASSETS			
Cash and cash equivalents	$ 23,877,042	$ 22,229,649	$ 46,106,691
Investments	27,365,221	29,314,866	56,680,087
Derivative instrument—rate swap	—	1,040,482	1,040,482
Receivables (net)	16,442,747	15,402,265	31,845,012
Inventories	448,823	250,000	698,823
Capital assets:			
Land, improvements, and construction in progress	153,408,694	34,843,175	188,251,869
Other capital assets, net of depreciation	168,002,817	282,572,377	450,575,194
Total assets	389,545,344	385,652,814	775,198,158
DEFERRED OUTFLOWS OF RESOURCES			
Accumulated decrease in fair value of a forward	—	127,520	127,520
LIABILITIES			
Accounts payable and accrued expenses	8,970,339	8,198,135	17,168,474
Advances from grantors	—	1,435,599	1,435,599
Forward contract	—	127,520	127,520
Long-term liabilities:			
Due within 1 year	13,662,286	9,547,351	23,209,637
Due in more than 1 year	157,784,651	91,463,340	249,247,991
Total liabilities	180,417,276	110,771,945	291,189,221
DEFERRED INFLOWS OF RESOURCES			
Accumulated increase in fair value of hedging	—	1,040,482	1,040,482
NET POSITION			
Net investment in capital assets	176,799,960	222,799,960	399,599,920
Restricted	24,203,913	49,985,155	74,189,068
Unrestricted	8,124,195	1,182,792	9,306,987
Total net position	$ 209,128,068	$ 273,967,907	$ 483,095,975

Case 2 (more details, cont.)

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Case 2:
<u>Second step</u> involves adjustments for asset impairment and differences in accounting methods (see below)
Details repeated: – Asset impairment of $4 million related to redundant capital assets that will be sold – Adjustment made to inventory valuation methods for consistency results in a reduction of $80,000

Case 2 (cont.)

	Village A	Village B	Total	Adjustments	Total
ASSETS					
Cash and cash equivalents	$ 23,877,042	$ 22,229,649	$ 46,106,691	$ —	$ 46,106,691
Investments	27,365,221	29,314,866	56,680,087	—	56,680,087
Derivative instrument—rate swap	—	1,040,482	1,040,482	—	1,040,482
Receivables (net)	16,442,747	15,402,265	31,845,012	—	31,845,012
Inventories	448,823	250,000	698,823	(80,000)	618,823
Capital assets:					
Land, improvements, and construction in progress	153,408,694	34,843,175	188,251,869	(4,000,000)	184,251,869
Other capital assets, net of depreciation	168,002,817	282,572,377	450,575,194	—	450,575,194
Total assets	389,545,344	385,652,814	775,198,158	(4,080,000)	771,118,158
DEFERRED OUTFLOWS OF RESOURCES					
Accumulated decrease in fair value of a forward	—	127,520	127,520	—	127,520
LIABILITIES					
Accounts payable and accrued expenses	8,970,339	8,198,135	17,168,474	—	17,168,474
Advances from grantors	—	1,435,599	1,435,599	—	1,435,599
Forward contract	—	127,520	127,520	—	127,520
Long-term liabilities:					
Due within 1 year	13,662,286	9,547,351	23,209,637	—	23,209,637
Due in more than 1 year	157,784,651	91,463,340	249,247,991	—	249,247,991
Total liabilities	180,417,276	110,771,945	291,189,221	—	291,189,221
DEFERRED INFLOWS OF RESOURCES					
Accumulated increase in fair value of hedging	—	1,040,482	1,040,482	—	1,040,482
NET POSITION					
Net investment in capital assets	176,799,960	222,799,960	399,599,920	(4,000,000)	395,599,920
Restricted	24,203,913	49,985,155	74,189,068	—	74,189,068
Unrestricted	8,124,195	1,182,792	9,306,987	(80,000)	9,226,987
Total net position	$ 209,128,068	$ 273,967,907	$ 483,095,975	$ (4,080,000)	$ 479,015,975

Case 2 (modified, cont.)

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Case 2:
Facts: Same combination as in original Case 2, but this time one of the merging villages continues in existence and absorbs the other village
Question: What is the initial reporting period? – Start of the villages former fiscal years, 7-1-11 – Date of the public referendum approving the merger, 11-2-11 – Date merger becomes effective, 1-1-12

Case 2 (cont.)

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Case 2:
Question: What is the initial reporting period?
Answer: Start of the villages former fiscal years, 7-1-11
Other considerations: Be alert for transactions between the two villages that occurred before the merger date and that may need to be eliminated or reclassified

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Case 3:

Facts: County purchases a privately-owned golf course for $3 million

Government combination: Acquisition

Carrying values of assets and liabilities of golf course:

Assets		
Cash and cash equivalents	$	41,204
Accounts receivable		4,239
Inventories		101,706
Land		3,161,975
Buildings and equipment (net)		4,081,972
Total assets		7,391,096
Liabilities		
Accounts payable and accrued expenses		19,473
Notes payable		6,850,445
Total liabilities		6,869,918
Net assets	$	521,178

Case 3 (cont.)

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Case 3:

More details:

- County determines the acquisition value of the golf course's assets and liabilities, arriving at values different from the carrying amounts for inventory, land, and buildings and equipment
- County renegotiates and lowers outstanding notes payable by $129,475
- County identifies an intangible asset with an acquisition value of $250,000 for water rights, based on GASB Statement 51, that was not reported by the golf course when it was a private entity

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Acquisition values:

Assets	
Cash and cash equivalents	$ 41,204
Accounts receivable	$ 4,239
Pro-shop inventory	95,000
Land	5,000,000
Buildings and equipment (net)	4,250,000
Intangible asset for water rights	250,000
Total assets	9,640,443
Liabilities	
Accounts payable and accrued expenses	19,473
Notes payable	6,720,970
Total liabilities	6,740,443
Net position	
Net investment in capital assets	2,779,030
Unrestricted	120,970
Total net position	$ 2,900,000

Assets	
Cash and cash equivalents	$ 41,204
Accounts receivable	4,239
Inventories	101,706
Land	3,161,975
Buildings and equipment (net)	4,081,972
Total assets	7,391,096
Liabilities	
Accounts payable and accrued expenses	19,473
Notes payable	6,850,445
Total liabilities	6,869,918
Net assets	$ 521,178

Case 3 (cont.)

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Case 3:
More details: – Net position acquired is $2.9 million, which is less than the $3 million consideration provided – Difference of $100,000 should be reported as a deferred outflow of resources
What should be the period over which the deferred $100,000 is recognized as expense? – Most of what the county has acquired is capital assets, so the remaining service life of the capital assets would be an appropriate period

Case 3 (cont.)

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Amounts to be included in county's financial statements as of acquisition date:

Assets	
Cash and cash equivalents	$ 41,204
Accounts receivable	$ 4,239
Pro-shop inventory	95,000
Land	5,000,000
Buildings and equipment (net)	4,250,000
Intangible asset for water rights	250,000
Total assets	9,640,443
Deferred outflow of resources	
Excess consideration provided for acquisition of XYZ Golf Inc.	100,000
Liabilities	
Accounts payable and accrued expenses	19,473
Notes payable	6,720,970
Total liabilities	6,740,443
Net position	
Net investment in capital assets	2,779,030
Unrestricted	220,970
Total net position	$ 3,000,000

Case 3 (cont.)

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Required Disclosures:

On September 30, 20X2, the City of Ammon Creek (City) acquired Bridgens Golf Inc., which owned the Barkas Ridge golf course and substantial water rights that attach to the golf course property in exchange for $3 million. The City will operate and maintain the golf course as a municipal golf course for public use and account for its operations in an enterprise fund. The acquisition included all of the assets of Bridgens Golf Inc., consisting of 160 acres of land; water rights; golf facilities; driving range; and inventories. In addition, the City assumed the liability for the accounts payable and accrued expenses of Bridgens Golf Inc. and renegotiated the terms and conditions of a bank note payable. The acquisition value of the net position acquired as of the acquisition date was determined to be $2.9 million.

There was no contingent consideration.

Case 4

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Case 4:

Facts: *Same facts as in Case 3, with the following differences:*

- The consideration provided by the county is $2.5 million rather than $3 million
- Acquired net position of $2.9 million is $400,000 greater than the consideration provided
- Noncurrent nonfinancial asset amounts should be reduced by $400,000

Case 4 (cont.)

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Acquired Assets	Acquisition Value	Allocation of Excess Net Position	Adjusted Acquisition Value
Cash and cash equivalents	$ 41,204	$ —	$ 41,204
Accounts receivable	4,239	—	4,239
Inventories	95,000	—	95,000
Land	5,000,000	(210,500)	4,789,500
Buildings and equipment	4,250,000	(179,000)	4,071,000
Intangible asset	250,000	(10,500)	239,500
Total acquired assets	$ 9,640,443	$ (400,000)	$ 9,240,443

Case 5

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Case 5:
Facts: A city joins a regional fire district and transfers its own fire protection operations to the district – assets of $6.3 million and related liabilities of $3.4 million (no deferrals) – There is no consideration provided by either entity – No adjustments need to be made for impairment or accounting methods
Government combination: This is a transfer of operations to an existing governmental entity

Case 5 (cont.)

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Case 5:

Outcome:

Regional Fire District

- The regional fire district recognizes the carrying value of the assets of $6.3 million and related liabilities of $3.4 million
- The regional fire district also recognizes a special item equal to the net position acquired from the city: $6.3 million – $3.4 million = $2.9 million

City

- The city derecognizes the assets and liabilities and recognizes a special item of $2.9 million for the net position transferred

Case 6

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Case 6:
Facts: Four cities decide to create a new regional fire district by combining their fire protection operations
Government combination: This is a transfer of operations to a new governmental entity

The cities' operations come with the following:

	Assets	Deferred Outflows	Liabilities	Deferred Inflows	Net Position
City 1	6,543,210	123,456	3,210,987	-	3,455,679
City 2	5,432,109	-	4,321,098	-	1,111,011
City 3	7,654,321	-	2,109,876	-	5,544,445
City 4	9,876,543	-	8,765,432	234,567	876,544
Total	29,506,183	123,456	18,407,393	234,567	10,987,679

Case 6 (cont.)

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Case 6:

Outcome:

Regional Fire District

- The regional fire district recognizes the combined carrying value of the assets, liabilities, and deferrals
- The regional fire district also recognizes a special item equal to the net position acquired from the four cities of almost $11 million

Cities

- The cities derecognize their transferred assets, liabilities, and deferrals and each recognizes a special item equal to the net position it transferred

Disclosure

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