

# New “Full Accrual” Financial Statements

## Overview and strategies on how to prepare your 2009 financial statements

One of the main priorities for municipalities to date has been the collection and valuation of tangible capital assets, along with supporting policies and accounting processes. This has been, and continues to be a significant effort undertaken in order to be PSAB 3150 compliant by the time the 2009 audited financial statements are finalized.

Municipalities are also grappling with financial reporting changes which come into effect for the 2009 audited financial statements (including 2008 comparative amounts). Financial reporting changes are consistent with the move to a “full accrual” reporting approach that is documented in the new PSAB section 1200.

This newsletter will identify the significant changes involved and provide related background information and implementation strategies. Municipalities should familiarize themselves with the new reporting requirements as soon as possible, in order to avoid implementation complications when completing the 2009 financial statements.

In particular, the following changes to financial statement presentation will be discussed:

- Record and disclose tangible capital assets, related accumulated amortization, and all other PSAB 3150 disclosure requirements;
- Introduction of Accumulated Surplus;

- New Financial Statement Formats;
- Elimination of Capital and Reserve/Reserve Fund Schedules;
- Other changes involving financial statement presentation.

### Tangible Capital Assets

Tangible capital assets must be included in the Statement of Financial Position as part of Non-Financial Assets. It is sufficient to disclose the net book value only on the face of the Statement, as long as appropriate disclosure is also made in the Notes to the Financial Statements for cost and accumulated amortization at the beginning and end of the period, as well as the amount of amortization, write-downs, additions and disposals during the period.

There are also a number of note disclosures to the Financial Statements related to Tangible Capital Assets that need to be included, such as amortization methods, TCA's under construction or removed from service and therefore not being amortized, contributed TCA's, TCA's valued at nominal value, works of art and historical treasures, and amount of interest capitalized in the period.

### Introduction of Accumulated Surplus

A new balance, Accumulated Surplus, will be reported as part of the Statement of Financial Position. The balance represents the accumulated amount of current and

prior years' surpluses and deficits, as calculated under the full accrual approach and reflects the net economic resources of the municipality.

Unfortunately, some readers of the financial statements may misinterpret large Accumulated Surplus amounts with overly funded reserves and overestimated budgets. Therefore, many municipalities are choosing to include optional note disclosures on Accumulated Surplus within their Financial Statements. Including information such as the definition and components of Accumulated Surplus can assist in interpreting financial results. Municipalities may also want to consider reconciling the opening balance to the closing Accumulated Surplus balance for the reporting year.

### New Financial Statement Formats

In addition to the changes noted above, the Financial Statements will also be undergoing a change in format and content. A summary of the significant changes by statement is as follows:

**Statement of Operations:** Reports expenses incurred and all revenues raised during the period, and the resulting surplus/deficit for the year. Capital expenditures are no longer reflected as 'expenses', other than through the inclusion of amortization, write-offs, write-downs and gains/losses on disposal of tangible capital assets.

**Statement of Financial Position:** Similar format to



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prior years except for the inclusion of Tangible Capital Assets as part of Non-Financial Assets and the inclusion of Accumulated Surplus (opening balance, change for the year, and ending balance) which replaces the previously reported balances under 'Municipal Position'.

**Statement of Change in Net Financial Assets or Net Debt:** New statement outlining how the financial activities of the municipality have affected its net financial asset or net debt position. This statement reconciles the surplus/deficit for the year to the net financial asset/net debt level as shown on the Statement of Financial Position.

**Statement of Cash Flows:** Identifies the sources and uses of cash, as well as the change in cash for the year. The predominant change to this statement is reflected by showing cash inflows and outflows due to TCA acquisitions and disposals.

#### **Elimination of Capital Fund and Reserve/Reserve Fund Schedules**

Under the new full accrual approach, the concept of reporting on specific 'funds' (such as operating funds, capital funds, and reserve and reserve funds) no longer applies. As such,

the capital and reserve schedules or statements which have previously been included in prior year financial statements are now not included in the full accrual format. All transactions which were recorded within these funds must be properly reallocated within the new Statement of Operations, or shown as adjustments to the appropriate balances on the Statement of Financial Position (i.e. TCA's).

For example, costs incurred that have determined to be TCA acquisitions, betterment, or replacements may have been posted to various locations in a municipality's accounts (i.e. capital project or operating area). For year-end reporting purposes, these costs must be reallocated to TCA accounts that will be reported on the Statement of Financial Position.

#### **Other Financial Statement Presentation Changes**

The move to the full accrual approach will also bring about a few other changes to Financial Statement presentation:

- Debt principal payments will no longer be shown as an expense. They will be reported as a decrease in long-term debt liability, however the interest

incurred will continue to be reported as an operating expense.

- Some administrative 'studies' and other minor capital costs which may have been previously reported as capital, will now be treated as an operating expense, given that many of these costs do not meet the definition of a tangible capital asset.

#### **Conclusion**

There are a number of reporting changes to keep in mind when preparing your 2009 Financial Statements. Things to consider include how to reconcile the old financial statement format to the new format, and how to effectively communicate the results of the new financial statements to key stakeholders such as Council members and residents.

Watson & Associates has assisted numerous municipalities with full accrual reporting implementation, disclosure formatting, and best practices in conforming to PSAB. Our "working trial balance" approach to financial statement conversions has been adopted in a number of municipalities and has been accepted by their external auditors. For more information on this approach, please feel free to contact us.



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#### **Questions / Comments?**

If you have any questions or comments regarding this or any Watson Newsletter, please contact us. We welcome the opportunity to discuss your specific municipality's needs.

#### **Have a Suggestion for Additional Newsletters?**

If there is a related topic you would like covered in a future Watson Newsletter, please contact one of the Watson staff members indicated below with your ideas.

## **Watson & Associates Economists Ltd.**

Watson & Associates Economists Ltd. is a firm of economists, planners and accountants which has operated in Ontario for over 25 years. With a client base of more than 250 municipalities, utility commissions and school boards, many of which are long-term repeat clients, the firm is recognized as a leader in the municipal finance/local government field. The firm has a committed thirty person staff that has worked together for many years. The firm's principals have participated extensively as expert witnesses on municipal finance matters at the Ontario Municipal Board for 25 years.

Watson & Associates Economists Ltd. has been engaged by a number of municipalities across the province to provide water/wastewater financial planning, development charges, PSAB 3150 compliance and asset management related services. The Watson PSAB 3150 and asset management approaches have been created to assist in the development of policies and procedures that are unique to the situations in each municipality. Watson has provided PSAB 3150 related services to over 40 municipalities in Ontario, all differing in size and services provided (i.e. Municipalities, Towns, Townships, Cities, Regions, etc.). Also, the Watson approach to PSAB 3150 has been widely accepted among municipal auditors.

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