Governmental Accounting Standards Board
of the Financial Accounting Foundation

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GASB Statement Provides Guidance for Reporting *Government Combinations and Disposals of Government Operations*

The GASB recently issued Statement No. 69, *Government Combinations and Disposals of Government Operations,* which provides new accounting and financial reporting standards for government mergers and acquisitions and for government operations that have been transferred or sold.

The new standards explain how governments should measure the amounts for the assets and liabilities that are a part of a merger between two or more governments or are acquired by one government from another, as well as the date on which the measurement should take place. The merger and acquisition guidance also applies to transactions involving a government and a non-governmental entity, such as a not-for-profit organization or a business. Specific guidance is provided for governments that dispose of one or more of their services by transferring or selling them to another entity. Statement 69 also identifies information that governments should disclose in the notes to their financial statements about their mergers, acquisitions, and disposals of operations.

Why Did the GASB Issue This Guidance?

Due to the challenging economic and fiscal environment governments have found themselves in over the past few years, government combinations—which are commonly referred to as mergers and acquisitions—have become more prevalent than they were in the past. Often, these transactions are intended as a means of providing government services more efficiently while reducing costs. A number of states have either passed legislation or otherwise encouraged local governments to combine operations in order to eliminate layers of government and the inherent departmental, service, and staffing redundancies that may come with them. For example, in some communities a township's road service functions might be absorbed into the county transportation department. Essentially the same service is provided and the objectives of streamlining government and reducing related costs of government services are met.

Until now, governments have accounted for mergers and acquisitions by applying accounting and financial reporting guidance designed for the business environment.

That guidance addresses notions that are common when dealing with public companies—such as ownership, stock, and equity—but are seldom encountered in the government environment. Statement 69 provides appropriate guidance that is specifically intended for governmental entities and addresses circumstances and conditions that commonly arise in the public sector.

The new Statement provides governments with guidance for identifying and accounting for types of government combinations in a clear and consistent manner. Specifically, this guidance addresses (1) how the amounts of assets, deferred outflows of resources, liabilities, and deferred inflows of resources (the "financial statement elements") should be measured and (2) the date on which the measurement should take place, depending on the type of combination. Under Statement 69, the term *government combinations* refers to three types of transactions: government mergers, government acquisitions, and transfers of operations.

Government Mergers

Many of the combinations that take place in the government arena are transactions in which little or no "consideration" is given—in other words, no significant payments change hands and the separate governments combine. These are called *government mergers.* Government mergers involve two or more governments (or even not-for-profit entities or businesses) and result in either the creation of an entirely new government or the continuation of one of the merging governments.

When a new government results from a merger, the date on which the merging entities combine for financial reporting purposes (this date is referred to as the merger date) is the date on which the new government's initial financial reporting period begins. The combined assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the merging entities are included in the statement of net position at the beginning of that initial reporting period.

When the result of the merger is the continuation of an existing government, the date on which the merging entities combine for financial reporting purposes is the beginning of the reporting period in which the merger occurs—regardless of the specific date when the merger actually occurs. Continuing governments are to report the financial statement elements and the results of operations of the merging entities for the reporting period in which the combination occurs as though the entities had been combined at the beginning of the continuing government's reporting period.

From an accounting or reporting perspective, government mergers are relatively straight forward combinations to account for because the assets and liabilities and other items are simply combined at their carrying value (or "book" value). Both new and continuing governments that result from a government merger will measure financial statement elements as of the merger date at the carrying values as reported in the separate financial statements of the merging entities.

The initial net position of the merged government results from combining the carrying values of the financial statement elements of the separate entities. Governments may, however, choose to adjust some carrying values if the merging entities followed different accounting principles (for example, different approaches to accounting for inventory or depreciation on capital assets). In addition, governments may be required to adjust certain carrying values of capital assets for impairment as a result of the merger. For example, if two school districts merged, the new or continuing district might not need all of the school buildings to house the combined student enrollment, and therefore might need to consider whether the surplus buildings meet the definition of impairment. Additional adjustments also are required if one or more of the merging entities had applied accounting principles that are not in conformity with generally accepted accounting principles for state and local governments (for example, a merger with a not-for-profit organization).

Government Acquisitions

Under a *government acquisition,* a government pays or exchanges another form of significant consideration (for instance, incurring a liability to the former owners) to acquire another entity or one or more of its operations. Acquisitions are somewhat infrequent in general purpose governments like cities and counties, but not uncommon in the business-type activities sector, which could include transactions involving such entities as hospitals or golf courses.

Under Statement 69, the acquiring government will measure the acquired financial statement elements—with certain exceptions—at their *acquisition value* as of the acquisition date. The acquisition date is the date on which the acquiring government obtains control of the assets or becomes obligated for the liabilities of the acquired entity or operations. The Statement describes acquisition value as a market-based entry price—that is, what it would cost to acquire a similar asset or transfer a similar liability.

Consideration provided by the acquiring government is measured at the acquisition date as the sum of the acquisition values of the assets remitted or liabilities incurred to the former owners of an acquired entity. For example, if the acquiring government pays $1 million and promises to pay an additional $1 million at a later date, the consideration would equal $2 million.

In situations in which the payment provided *exceeds* the net position acquired, the acquiring government should report the difference as a deferred outflow of resources that will be recognized as expense in future periods. In the previous example, the consideration was $2 million but the net position acquired (the net value of the combined financial statement elements) was $1.8 million; the acquiring government would therefore report a deferred outflow of $200,000.

For situations in which the consideration provided is *less* than the net position acquired, the acquiring government should eliminate the excess net position acquired generally by reducing the acquisition values assigned to the noncurrent assets. For instance, if the net position acquired in the previous example had been $2.2 million, then the acquiring government might have reduced the value assigned to the capital assets it received by $200,000. However, there may be situations where this difference is the result of a contribution by the owners of the acquired entity.

Transfers of Operations

In addition to combinations involving entire governmental entities, Statement 69 also provides guidance for combinations that involve only portions of a government (and in which no significant consideration is provided). These arrangements include transfers of *operations* to continuing governments or to form a new government. An operation is defined as an integrated set of activities with associated assets and liabilities that is conducted and managed for the purpose of providing identifiable services. For example, a county may transfer its public safety function to a regional government or to another county, but the county still exists—it has simply divested itself of that function.

Because transfers of operations are entered into by governments for similar reasons as government mergers, the use of carrying values to report the financial statement elements of the transferred operation also are applied for these arrangements.

Disposals of Governmental Operations

Disposals of government operations that have been transferred or sold are similar to transfers of operations, but are viewed from the perspective of the government selling or transferring the operation. Governments disposing of an operation should recognize a gain or loss, which generally is then reported as a special item in the period in which the disposal occurs.

What about Disclosures?

Taken together, the aim of the disclosures described in the Statement is to provide users with the information they need to know about the separate governments prior to the combination. For each government combination, governments should include a brief description of the combination, the date of the combination, and the primary reasons for the combination.

Government Mergers and Transfers of Operations

New governments or continuing governments disclose the amounts recognized as of the merger date or the effective transfer date for the financial statement elements and total net position by component (net investment in capital assets, restricted, and unrestricted). These governments also should briefly describe the nature and amount of significant adjustments, if any, made to bring into alignment the individual accounting policies or to adjust for impairment of capital assets resulting from the merger or transfer.

Government Acquisitions

An acquiring government should briefly describe the consideration provided, the total amount of net position acquired as of the date of acquisition, and any contingent consideration arrangements, including the basis for determining the amount of contingent payments. Contingent payments will happen in the future if certain events occur.

Disposals

A government should provide a brief description of the facts and circumstances leading to the disposal of those operations. The government also should identify and disclose the disposed operation's total expenses, revenues, and nonoperating revenues and expenses of the period, if this information is not presented separately in the government's financial statements.

When Will Governments Implement Statement 69?

The requirements of the Statement are effective for government combinations and disposals of government operations occurring in financial reporting periods beginning after December 15, 2013 (in other words, fiscal years beginning January 1, 2014, and later), and should be applied on a prospective basis. Governments are encouraged to implement earlier.

Obtaining Statement 69

The full text of Statement 69 is available to download free from the GASB website (www.gasb.org).

- Printed copies of Statement 69 will be available soon in the GASB Store
- Read the media advisory