



## The Use of Private-Sector Standards by State and Local Governments

By Stephen J. Gauthier

Private-sector accounting standards have played an important role in the public sector, even though state and local governments have always used different generally accepted accounting principles.

From the beginning, state and local governments have used different generally accepted accounting principles (GAAP) than their private-sector counterparts. All the same, private-sector accounting standards have played an important role in the public sector as well. This article will explore that relationship and its prospects for the future.

### BACKGROUND

Some operations of a typical state or local government “are financed and operated in a manner similar to private business enterprises.”<sup>1</sup> Traditionally, the basic principle was that accounting and financial reporting for such operations should follow the same standards used by similar private-sector activities.<sup>2</sup> That is, private-sector standards were presumed to apply automatically to proprietary funds as well.

The Governmental Accounting Standards Board (GASB) put an end to the automatic applicability of private-sector standards to proprietary funds in 1993 with the issuance of GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. That pronouncement distinguished private-sector standards issued prior to November 30, 1989,

from later private-sector guidance. Specifically, proprietary funds were *required* to follow all private-sector standards issued prior to November 30, 1989, “except for those that conflict with or contradict GASB pronouncements.”<sup>3</sup> They also were *permitted* to elect to consistently follow later private-sector standards, subject to those same conditions.<sup>4</sup>

GASB Statement No. 34, *Basic Financial Statements — and Management’s Discussion and Analysis — for State and Local Governments*, introduced government-wide financial reporting and required that the government-wide financial statements, like the proprietary fund financial statements, comply with all private-sector standards issued prior to November 30, 1989, that were consistent with GASB guidance. GASB Statement No. 34 did *not*, however, permit governments to elect to consistently follow later private-sector standards for government-wide financial reporting (other than for business-type activities). Indeed, it actually eliminated that option for internal service funds.

### PRACTICAL CHALLENGES

The Financial Accounting Standard Board (FASB) has continued to amend and supersede private-sector guidance issued prior to the

November 30, 1989, “cutoff” date. However, as a result of GASB Statement No. 20 and GASB Statement No. 34, it is only the version of those standards in effect as of the cutoff date that is authoritative for state and local governments. This situation has naturally led to some confusion in practice. Furthermore, the FASB elected in 2009 to make the codification of its standards, rather than the original pronouncements themselves, the primary authoritative source of GAAP, which will make it even more difficult for state and local government practitioners to determine the portions of that guidance specifically applicable to them (because it was effective prior to the cutoff date).

## PENDING DEVELOPMENTS

The GASB believes public-sector accounting professionals should be able to obtain all of the guidance they need to comply with GAAP from the GASB’s own technical literature without having to consult private-sector standards. To achieve this objective, the GASB is now in the process of preparing a codification of the relevant sections of private-sector standards issued prior to November 30, 1989. The GASB has also tentatively decided to eliminate the option for enterprise funds and business-type activities to elect to use later private-sector standards. (In practice, few enterprise funds have made use of this option.)

The GASB now plans to release an exposure draft of its *Codification of Pre-November 30, 1989, FASB Pronouncements*, in the first quarter of 2010. It hopes to release a final authoritative version by the end of the year. ■

### Notes

1. National Council on Governmental Accounting Statement 1, *Governmental Accounting and Financial Reporting Principles*, paragraph 26.
2. “Generally accepted accounting principles here are those applicable to similar businesses in the private sector” (NCGA Statement 1, paragraph 18).
3. GASB Statement No. 20, Paragraph 6.
4. GASB Statement No. 20, paragraph 7.

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