



Changes for Component Units

By Stephen J. Gauthier

GASB Statement No. 61 amends the rules that govern how component units are identified and presented.

In November 2010, the Governmental Accounting Standards Board (GASB) issued GASB Statement No. 61, *The Financial Reporting Entity: Omnibus*. The new standard amends the rules that currently govern how component units are identified and presented. This article examines the most important changes that will result from the implementation of GASB Statement No. 61.

FISCAL DEPENDENCE AS A CRITERION FOR INCLUSION

Under current authoritative standards, the simple fact that a legally separate entity is *fiscally dependent* on another government is sufficient to warrant its inclusion as a component unit of that government. Fiscal dependency results whenever another government is able to do any of the following:

- Determine a potential component unit's budget;
- Establish a potential component unit's rates, tax levies, or charges; or
- Approve or modify the issuance of a potential component unit's debt.

Under GASB Statement No. 61, fiscal dependency will be a basis for including a potential component unit only if there is also financial interdependence between the potential component unit and the other government. That is, a legally separate entity will have to be included as a component unit if it is fiscally dependent on another government *and* there also is a relationship

of potential financial benefit or burden between the two.

APPLICATION OF THE MISLEADING TO EXCLUDE CRITERION

Under current authoritative standards, a legally separate entity must be included as a component unit of another government if the nature and significance of the relationship between the two is such that excluding the former would render the latter's financial statements *misleading* or *incomplete*. GASB Statement No. 61 makes two changes to this existing guidance.

As just noted, a potential component unit must be included if its exclusion would make the other government's financial statements *misleading* or *incomplete*. Since incomplete financial statements are inherently misleading, GASB Statement No. 61 has dropped the term *incomplete* as being redundant.

Of course, a variety of relationships can exist between a potential component unit and another government. GASB Statement No. 61 clarifies that relevant relationships for this purpose generally would be *financial* in nature.

IDENTIFYING MAJOR DISCRETELY PRESENTED COMPONENT UNITS

Governments are required to provide separate information on each major discretely presented component unit

somewhere within the basic financial statements (i.e., separate column, combining statements, note disclosure). Under existing standards, financial statement preparers must consider two factors in making a determination whether a given discretely presented component unit is *major*:

- The nature and significance of its relationship to the primary government; and
- Its significance relative to total discretely presented component units.

This second criterion has sometimes resulted in a relatively small discretely presented component unit being classified as *major* solely because of the significance of its relationship to other discretely presented component units, even though it is clearly insignificant in relation to the primary government

(i.e., “a big fish in a small pond”). To avoid such outcomes in the future, GASB Statement No. 61 will drop the second criterion entirely.

CRITERIA FOR BLENDING COMPONENT UNITS

Under existing standards, a component unit must be blended if its governing board is substantially the same as the governing board of the primary government. GASB Statement. 61 will require that at least one of two additional criteria be met:

- The primary government and the component unit are financially interdependent (i.e., there is a relationship of potential financial benefit or burden between them); or
- Management responsible for the day-to-day operations of the primary

government also manages the component unit’s day-to-day activities in much the same way (i.e., *operational responsibility*).

GASB Statement No. 61 also establishes an entirely new criterion for blending component units. Specifically, a component unit will need to be blended if its total debt will be repaid entirely, or almost entirely, from resources of the primary government.

EFFECTIVE DATE

State and local governments must implement the new guidance for the fiscal year that ends June 30, 2013. Earlier implementation is encouraged. ■

STEPHEN J. GAUTHIER is director of the GFOA’s Technical Services Center in Chicago, Illinois.

 Government Finance Officers Association

GFOA YIELD ADVANTAGE™

The •Fast
•Efficient
•Transparent Way
to Streamline the
Investment Process

IT'S AS EASY AS



Powered by
 GRANT STREET GROUP
Software That Works™

For more information visit <http://www.gfoayield.com/>