



Management's Perceptions of Annual Financial Reporting

**An International City/County Management Association (ICMA)
White Paper**

December 2013



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Management’s Perceptions of Annual Financial Reporting

A Policy Issue White Paper

Prepared on behalf of the ICMA Governmental Affairs and Policy Committee

December 2013

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ICMA advances professional local government worldwide. Its mission is to create excellence in local governance by developing and advancing professional management of local government. ICMA, the International City/County Management Association, provides member support; publications, data, and information; peer and results-oriented assistance; and training and professional development to more than 9,000 city, town, and county experts and other individuals and organizations throughout the world. The management decisions made by ICMA’s members affect 185 million individuals living in thousands of communities, from small villages and towns to large metropolitan areas.

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Overview

The Governmental Accounting Standards Board (GASB) was established in 1984 as the second operating arm of the Financial Accounting Foundation (FAF), to serve as the authoritative accounting standard-setting body for state and local governmental entities in the United States.¹ In 2009, GASB began the third phase of Economic Condition Reporting: Financial Projections and issued guidelines for Service Efforts and Accomplishments Reporting (aka SEAs) in 2010. To date GASB has issued 70 Statements, with the most recent (No. 67 & No. 68) pertaining to accounting for and reporting of pensions. By far, No. 34 (issued in 1999) was the most significant change GASB made in its history. The ever-increasing evolution of our economy, governmental service provisions, and financing options help explain the continued changes in financial reporting and disclosures.

In 2012, the Center for Governmental Studies reviewed dozens of comprehensive annual financial

reports (CAFRs) from a variety of projects and found that those municipal CAFRs generally ranged from 110 pages to more than 250 pages, depending on the size of the community and its service offerings.² Additionally, this survey revealed that it can take approximately six months for some entities to complete the CAFR, rendering the data stale when introduced. Furthermore, new standards often require additional resources and system changes, and can add to the length of the CAFR and annual close. Yet, to describe the well-known, complex state of public sector financial reporting without taking action is of no use.

To better understand the current state of local government financial reporting, the International City/County Management Association (ICMA) engaged Northern Illinois University (NIU) and its Center for Governmental Studies (CGS) to explore management's perspectives on how the various financial statements issued by GASB:

1. affect management;
2. provide a net benefit to its stakeholders; and

Acknowledgements

We would like to thank the International City/County Management Association (ICMA) staff for their input and review of this report; the executive directors of the Illinois and Wisconsin ICMA and GFOA state chapters for assisting with the distribution of the survey; and all of those who participated in the survey. Without your input and assistance, this paper would not have been possible. We also appreciate the support of the Center for Governmental Studies at Northern Illinois University, which provided the resources to develop the survey as well as collect and compile the survey responses.

Almost 70 percent of the respondents believe the benefits of generating the financial statements outweigh their costs.

3. are accompanied with professional support/out-reach mechanisms from entities such as Governmental Accounting Standards Advisory Council (GASAC) (providing feedback to GASB), as well as assistance from organizations such as the Government Finance Officers Association (GFOA) and audit firms to assist preparers with understanding and implementing the changes to their year-end financial statements.

This white paper focuses mainly on the following two key local government consumers who, coincidentally, are also producers of the annual financial reports:

1. city/county managers and administrators, and
2. finance officers/directors/managers.

These two groups are collectively referred to as “management” going forward. Furthermore, not all local governments produce a CAFR; many produce some form of an annual financial report (AFR). Those that do not produce either a CAFR or AFR were excluded from the survey. Going forward, the AFR and CAFR will be used interchangeably and referred to as an “annual financial report” (AFR).

Overwhelmingly, management perceives there to be a net benefit to annual financial reports. However, there are aspects of governmental reporting that are in need of some improvements. Thus, the research team synthesized our findings with existing research and offered recommendations at the end of this paper to improve the state of governmental annual financial reporting.

Executive Summary

For entities reporting in accordance with generally accepted accounting principles, annual financial reports offer management a comprehensive view of their finances that acknowledges economic events. These annual financial reports are valuable resources for assessing fiscal conditions, conducting comparisons to comparable entities and integrating their other managerial roles such as capital improvement planning, budgeting, strategic planning, investing, financing, benchmarking, etc.

While this white paper reports management’s perceptions, the authors recognize that there are a variety of consumers of public sector financial reports; i.e.,

auditors, elected officials, taxpayers, investors, regulators, and bond rating agencies (see Figure 1). We also appreciate the fact that while management has access to the primary source data and, therefore, may place a greater emphasis on the production of CAFR data rather than on its use, their perceptions of financial reporting are valuable since the data in AFRs have been linked to policies such as bond ratings.

The list below recaps the key findings from management’s survey responses.

- For the most part (64 percent), management uses little to no audited financial statements to inform their policy decisions; less than 25 percent use their financial reports to inform their policy decisions.
- In those cases in which management uses their financial statements to inform policy decisions, more than a third tend to glean from the Management Discussion and Analysis (MD&A), note disclosures, and government-wide statements introduced via GASB 34; more than two-thirds still rely on fund financial statements, in particular, governmental funds (pre-GASB 34).
- 80 percent of respondents whose population is under 50,000 outsource their annual financial statements, compared with 50 percent of respondents with populations over 50,000.
- Complexity of reporting, as evidenced by preparation costs, appears to increase with the size of the organization. The larger the entity, the more complex the set of financial transactions and the higher the preparation costs. It is estimated that annual financial reporting costs taxpayers approximately \$10,000 to \$50,000, with some larger (more than 50,000 residents) communities spending more than \$200,000.
- Almost 70 percent of the respondents feel that the benefits of generating the financial statements outweigh their costs. Note: As mentioned earlier, management perceives the purpose (or key benefit) of financial statements to be for compliance and accountability, not as useful information for informing decisions.
- Management relies heavily on their auditors for assistance with their financial statements, followed by assistance from GFOA; very little assistance is sought from GASAC—an advisory body—or GASB. In the future, management expects to continue to

rely predominantly on their auditors for assistance. They expect that they may seek out assistance from GFOA, but very few to no managers anticipate requesting help from GASB or GASAC. It should be noted that auditors are heavily assisting as producers of financial reports (see third bullet) and might be the ones seeking input from the GASB and GASAC on behalf of management. This information would be requested in any future assessments of other financial report producers and consumers.

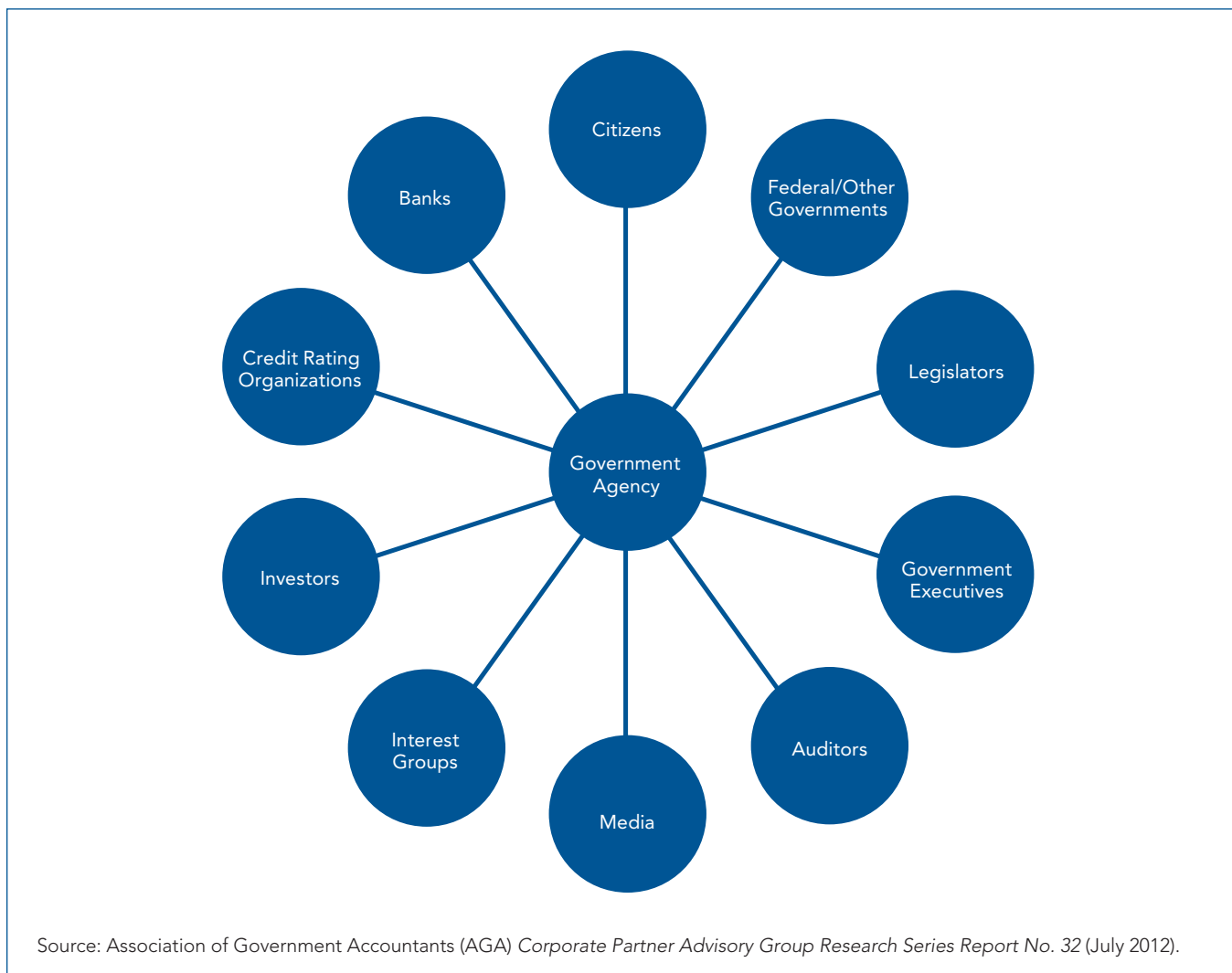
- More than 80 percent of the respondents implemented Statements No. 34, 43, 45, and 54. However, fewer than a third of those who implemented these statements found them to be beneficial.
- While less than five percent of the respondents intend to implement SEA or Economic Condition Reporting, only 15 percent stated they would not

implement these changes in reporting. Other respondents cited reasons such as “cost prohibitive” or “not sure of the benefits” for not implementing these reporting changes, while the remaining managers felt these changes encroach upon management practices. Thus, there are those in the middle who might consider implementing the suggested changes, but this might require more education on the benefits of SEA and Economic Condition Reporting and the availability of tools or resources to facilitate the change.

The key recommendations of this white paper include:

1. **Reassess content, semantics, and structure of annual financial reports.** More work must be done to determine how detailed the annual financial reports should be and how the information should be defined, standardized, and structured in order to increase its use in management’s decision-making.

Figure 1 Consumers of Annual Financial Reports



Currently, most respondents feel that these reports are predominantly a tool for compliance. However, there is rich data in these financial statements that could be used for added input in the decision-making process.

2. Leverage new technologies. New technologies (i.e., extensible business reporting language, aka XBRL) could lend themselves to include rich details about government’s finances without all the “noise” to better articulate the meaning of what is being reported based on the audience/consumer of information. For instance, digitized financial information could allow for consolidated reporting to present the big picture but still allow for others such as taxpayers or investors to go more deeply into the data. New technologies also allow for centrally managed reporting tools to help reduce production costs, as well as increase productivity and reporting timeliness, thanks to not having to change proprietary systems every time new standards are introduced. There are several other benefits to leveraging new technologies (i.e., ease in integrating with other data, increased data validation, etc.), but those discussed here focus predominantly on the concepts of the research conducted in this white paper (efficient preparation of the annual financial reports and usefulness of these completed reports to inform state and local governments’ policies).

3. Increase outreach/support efforts. Sometimes it is difficult for management to understand the value proposition of new standards or reporting requirements when they have not directly participated in the deliberation process. Thus, it would be helpful for local governments to receive a reminder of the mechanisms available to them to participate in the deliberation process (i.e., ability to sign up for email notifications to participate in proposed changes) in order to gain their direct participation whenever possible. Although GASB does have an option to “let us know who you are” and sign up to receive additional information, it might be helpful to advertise this option in other frequently read managerial publications, such as the ICMA Newsletter. Additionally, introduction of new standards or reporting needs should communicate to management aspects of the net benefit of the standard(s) or reporting recommendations. Added clarification is needed about how the benefits of implementing new standards or changes to existing standards outweigh the adoption costs. Additionally, information and examples pertaining to how management and/or their stakeholders can use the new or revised information to enhance their decision making process would be helpful.

These recommendations are expanded upon in greater detail in the *Concluding Remarks and Recommendations* section.

Objectives, Methodology, and Scope

The Center for Governmental Studies at Northern Illinois University developed an online survey with input from ICMA to capture management’s perspectives. The survey primarily intended to determine management’s perceived impacts of the recent GASB statements, including the net benefits or costs, and understand which organizations were either assisting them with the CAFR or allowing them to provide feedback for requesting changes to the reporting process. ICMA distributed the survey in its member newsletter in June 2013, encouraging all city and county managers/administrators to participate. Additionally, the research team invited partner organizations—all members of both the Wisconsin and the Illinois state chapters of the Government Finance Officers Association—to complete the survey as well. We received 73 responses from city/county managers/administrators/CAOs and 56 responses from finance/CFO-types. The authors asked questions pertaining to the GASB statements issued, beginning with Statement No. 34 issued in 1999, the most significant public sector financial reporting change, and all subsequent standards.

The focus of the survey questions are recapped below:

1. Are the recent GASB statements affecting management? If so, how?
 - a. Are managers (city, county, and assistant managers) using audit reports to affect policy?
 - b. If so, to what extent and which section(s) of their CAFRs are they using?
2. Measuring Managers’ Perceptions: Do the costs outweigh the benefits?
 - a. What are the various practices employed for generating annual financial reports (i.e., outsource all, some, or none)?
 - b. What are the organizations’ costs of preparing audit reports for the city or county?
 - c. What are the managers’ perceived benefits of having audit reports for the city or county?
 - d. Do managers perceive that the benefits of CAFRs outweigh the costs?
3. Professional Support/Outreach (GASB, GASAC, GFOA, NLC, AGA, etc.)

- a. What type of assistance are managers receiving from the various organizations in preparing audit reports?
- b. Are they aware of these organizations and their service offerings?
- c. How often do they seek assistance?
- d. How do they request assistance?
- e. How often do they receive assistance?
- f. How do they rate the assistance they receive? Is it helpful or not?
- g. How likely are they to use their services again?
- h. How likely are they to recommend their services to others?
- i. Are there recommended changes in the annual financial statement preparation process? Statement deliberations process? Support process? Training?

Finally, the research team contacted survey respondents who indicated their willingness to answer follow-up questions. These questions were also forwarded to 23 members of the Illinois GFOA Technical Advisory Committee (TAC) to incorporate their feedback with the findings of the survey. The research team submitted the following follow-up questions/requests for feedback from the survey respondents and TAC:

1. Please discuss your opinions on the usefulness and/or purposes of CAFRs beyond simply meeting compliance requirements.
2. One of the goals of CAFRs is that they be used to inform policy. Please discuss the extent to which CAFRs are being used to inform policy (it would be very helpful if you have specific examples). As a follow-up, please discuss any suggestions/improvements to CAFRs (e.g., content, accessibility, format, or timing) that would enhance their utility as a policy-aiding document.
3. There have been some significant changes to financial reporting, including but certainly not limited to GASB Statement 34, over the years. Please discuss your perceptions of these recent CAFR statement requirements. We are particularly interested in your take on the extent to which recent changes are helping to inform policy decisions.
4. Please discuss your assessment of GASB advising and/or input solicitation when it comes to proposed Statement changes. Once again, any specific examples would be very helpful.
5. In general, please provide your overall assessment of financial reporting today compared to, say, 10 to 15 years ago. Discuss in detail (if possible) where

you think there have been improvements and/or where reporting has gotten worse.

6. Finally, having thought of the past, please discuss what you think the future (perhaps 10 years from now) holds for financial reporting. Where do you see improvements and/or problems?

Survey Results

Survey results were aggregated to address management effects, net benefits, and outreach/support mechanisms.

A. Management Effects

Managers (city, county, and assistant managers) are not using audit reports to affect policy: primary purpose of AFRs is perceived to be compliance.

Managers see AFRs first and foremost as a check on their end-of-year financial status and as necessary to meet audit and state compliance. Less than a quarter (22.8 percent) of the respondents identified informing policy decisions as the purpose of AFRs (see Table 1 in the Appendix, pg. 15). The responses varied little when managers were compared to CFOs.

The following are excerpts from follow-up questionnaires:

The documents are very useful in helping the community understand their jurisdiction's financial position. I couldn't imagine NOT producing a CAFR.

CAFRs can be useful and serve as a resource of historical data. CAFRs can be useful in providing credibility to the stewardship responsibilities of elected officials. CAFRs can be useful in providing a level of comfort to citizens to know where and how their tax monies are being used. CAFRs should serve as the authoritative document for establishing a government's financial position.

CAFRs are useful in conducting research and preparing forecasts that rely upon historical information. Also, bond rating agencies and bond buyers use CAFRs to assess a local government's financial condition.

The CAFR provides an independent picture of how our financial plan/budget played out as well as a layman's explanation of our accounting system, revenue and expense practices and comments by auditors with regard to best and

usual practices; all of which are valuable for our elected officials and Department heads as well as the media to understand how good, bad or indifferent our biannual fiscal practices and checks and balances are performing and where change may or may not be needed or valuable. The single audit / federal funding companion piece as well as enterprise funds alignment with our General fund are also important bell wethers of the interrelationship of programs and projects reliance on non-County funding/ property taxes as well as another unbiased look and fiscal portrayal of the business of local government and can help assess whether or not we stay in said service/activity i.e. privatization, sale or cease and desist.

When managers were asked directly about the use of AFRs to inform policy, more than one-quarter replied that they don't use AFRs for that purpose. Slightly more than a third of respondents (36 percent) use AFRs to inform a "moderate" number of or "most" policy decisions (see Table 2, pg. 15). Again, the responses varied little based on who completed the survey.

The primary impediment to using AFRs to inform policy decisions is timing.

A recent report from GASB³ found that it takes approximately six months after the fiscal year for states and larger government entities to complete an audit. The same report also indicates that the usefulness of financial reports for affecting policy diminishes significantly after the first 45 days of the fiscal year. It thus appears that AFRs could be more influential if the reports could be completed in a timelier manner.

ARFs are getting more complicated but appear to be adding value.

One key explanation for the time it takes to complete AFRs is the number of changes required by GASB in recent years, including but not limited to Statement Nos. 34, 43, 45, and 54. Below are some of the managers' responses when asked to provide an assessment of financial reporting today compared to 10 to 15 years ago. Some respondents were pleased with the reporting changes, whereas others were clearly frustrated.

Financial reporting has become significantly more complicated than 10–15 years ago.

Financial reporting has definitely improved. While confusing at least initially for many, GASB

Statement No. 34 has revealed that the decisions of policymakers have long-term impacts. Also, the pension and OPEB pronouncements have enhanced transparency. I cannot see anywhere that financial reporting has gotten worse.

I feel the MD&A and stat section are much better because the reader has comparative information. The focus should be on requiring government to be more transparent. I feel we are still a ways off on standardized and consistent approaches on a national level. There is so much still deferred to the state level. GASB should have rules that further suggest uniform chart of accounts for various counties, cities, school, and special districts with the roll-up of the chart of accounts to the general categories defined in the CAFR. I am chairing the committee tasked with updating our chart of accounts for special districts with the state. I had two calls yesterday from Finance Managers looking to update their system of controls. Creating standard reporting guidance goes a long way to create a basis for comparative information. Once the data is consistent, providing clear definitions for the stat section information makes the data more comparative and reliable for the reader and markets.

I believe that the financial statements are a more accurate portrayal of our financial status. It is a more useful tool for edification and education of our policy makers, interested publics, and the media which is always good in terms of accountability and transparency.

The questionnaire then asked respondents what they thought the future holds for financial reporting. Where do they see improvements and/or problems? Some of the responses are provided below:

Municipalities will be more accurately portrayed in their independent financial statements, our actual planning for and funding of previously undisclosed liabilities and the truth about our fiscal health and/or impending/present crises will be routine and there will more likely be more bankruptcies, bailouts, dissolutions and consolidations as policy makers and their advisors embrace long range fiscal plans and funding solutions to truly balance our fiscal houses of cards and represent to taxpayers and

investors and financial markets that we either do or don't have our affairs in order. To the extent that policy makers and some administrators take an ostrich approach in spite of what independent auditors and watchdogs like State and Federal inspector generals and attorney generals will be doing with special investigations and analyses, there will be more dire headlines, wailing and gnashing of teeth and little real change or reform. Best practices and new thinking on program offerings, employee commitments, capital projects and government viability as well making hard decisions instead of decisions related to the defer, delay and deny tactics of the past 50+ years have got to be an improvement over the one day at a time approach some of us have gotten away with over the years.

One major gap that still needs to be filled is reporting for OPEB in a manner similar to the approach we are using for pensions with GASB Statement Nos. 67 and 68. Statement No. 45 is certainly a step in the right direction. However, OPEB liabilities need to be added to the statement of position just like pension obligations will be. Also, policymakers need to gain a better appreciation or be better instructed in the significance of the accrual/economic resources measurement focus financial statements. They are generally comfortable with the fund-based statements. However, policymakers should see both the short- and long-term impacts of their decisions.

B. Net Benefits

Many AFRs are completed externally and can cost as much as \$25,000 to \$50,000 for mid-sized communities.

While slightly more than half (54 percent) of local governments with populations greater than 50,000 have their AFRs completed internally, the vast majority of smaller local governments have their audits completed externally (see Table 4, pg. 16).

What are the organizations' costs of preparing audit reports for the city or county? The cost is related to the entity's size/population. Entities with populations of less than 20,000 tend to spend \$25,000 or less on their AFR. This cost includes staff time and resources, and contractual services (if used). Mid-sized communities tend to spend \$50,000 or less whereas more than 25

percent of the communities with a population greater than 50,000 spend \$50,000 to \$100,000 on their AFR (see Table 5, pg. 17).

Net benefits of the AFR outweigh its costs.

Given the costs associated with the preparation of these documents, we asked managers and CFOs if they perceive the benefits of CAFRS to outweigh the costs (see Table 6, pg. 17). The overwhelming majority—66 percent of managers/administrators and 75 percent of finance officers/CFOs—said yes. *According to one of the respondents, it is "absolutely necessary to have this standard format report."*

C. Professional Support/Outreach Mechanisms

Management is primarily relying on auditors for support.

The complexity and continuous evolution of financial reporting requirements necessitates training, education, and assistance. We focused our attention on the extent to which respondents work with three organizations—the Governmental Accounting Standards Board (GASB), Governmental Accounting Standards Advisory Council (GASAC), and Government Finance Officers Association (GFOA)—and independent auditors.⁴ Nearly three-quarters (72 percent) of respondents sought assistance from auditors once or twice per year. Managers rated the auditors they used positively and intend to go to them for questions in the future (see Tables 7–10, pg. 18–19). Conversely, GASAC was rarely consulted for assistance. GFOA appears to be used for assistance less than auditors, but more frequently than GASB: a majority of respondents consulted GFOA infrequently (38 percent chose seldom; 26 percent, once or twice/year).

Managers who have had direct contact with GASB were generally satisfied.

Given the efforts made by GASB to solicit feedback, we asked those survey respondents willing to receive a follow-up questionnaire to discuss their assessment of GASB advice and/or input solicitation when it comes to proposed Statement changes.

Here are some of the responses:

I think they need to give more guidelines and samples of what polices and new procedures are needed. GASB 67 and 68 are very complex. Creating a pension fund policy from nothing is extremely difficult.

They don't listen to the folks in the trenches enough.

GASB's due process procedure is highly satisfactory. Interested parties have ample opportunity to weigh in on contemplated pronouncements.

I believe the GASB 45 draft and comments and vetting process was more robust and well received than the GASB 54 realignment of reserves and fund balances but in both cases our in house fiscal watchdogs and independent auditors were able to effectively explain the changes and provide some plausible rationale for this information to be included in our independent financial statements and who was really driving these changes to be the "law of the land" for municipal accounting and independent auditor's scope of work and the impact on our financial statements.

I liked the opportunity to interact with them during the pension hearings. They did take the effort to respond to my written questions. It would be helpful if we could register our email and have the pronouncements and drafts sent to us, because I do not remember to look at the website to see the latest information and requests for input and review.

D. Recent Financial Reporting Changes and Recommendations

Recent financial reporting changes appear to be less beneficial to managers.

Within the past 20 years GASB has implemented some significant changes to financial reporting requirements, including Statement Nos. 34, 43, 45 (Other Post-Employment Benefits; OPEBs), and 54 (fund balance reporting). We asked survey respondents if their entity had implemented these changes, and, if so, whether or not they found them beneficial (Table 11, pg. 19). Most have implemented the changes; by a ratio of two to one the respondents did not find the changes beneficial. These results varied little when compared to the entity's population or the position held by the survey respondent. The only difference worthy of note is that 70 percent of finance personnel implemented but did not find Statements 43 and 45 beneficial, and 53 percent of managers/administrators held the same belief.

Pension liability reporting not expected to affect bond/credit ratings or policy.

One of the more significant CAFR changes coming is the reporting of pension liabilities: Statements 67 and 68. We asked respondents several questions about Statements 67 and 68 (Table 12, pg. 20): more than half the respondents intend to implement GASB Statements 67 and 68 (59 percent) and few believe it will have an impact on their bond/credit ratings. Furthermore, only 17 percent of the respondents think that the adoption of these statements will affect policy decisions in their entity.

Economic Condition and Service Efforts and Accomplishments Reporting are implemented by few.

In addition to required CAFR changes, GASB has been working on suggested guidelines for a separate service efforts and accomplishments (SEA) report and has worked toward identifying standards for economic condition reporting.

These have prompted quite a bit of debate in the finance and management communities. Fewer than five percent of the respondents intend to report either SEA or Economic Condition per GASB suggestions (Table 13, page 20). The reasons for not implementing include:

- **cost**—19 percent have not reported SEA and 10 percent have not implemented Economic Condition Reporting due to cost
- **encroachment on management matters**—18 percent gave this response for SEA and 11 percent responded in the same manner for Economic Condition Reporting
- **not familiar enough**—17 percent gave this response for not adopting SEA vs. 43 percent for Economic Condition Reporting
- **not suitable**—Interestingly, only 15 percent said they would not implement SEA and 9 percent said they would not implement Economic Condition Reporting because it was not suitable for the entity.

GASB 34 remains the most challenging Statement change

More than 15 years after the Statement's adoption, GASB Statement 34 remains the most challenging (half of all responses). Also cited frequently were Statements 45 and 67–68.

Quotes from managers/administrators when asked to discuss the most challenging recent GASB statements to implement:

Most of them! On its face, to more than double the number of GASB requirements in a decade, appears excessive. It's like a full employment act for accountants.

The initiation of GASB 34 was very time-consuming. Annual updates much less of a problem.

Each year it seems GASB adds an additional requirement. GASB 34 was obviously the big one, but each of the little ones taken together add up. I am not always sure that the changes indeed add to the public's understanding of governmental finance.

The real answer is "maybe"—we are worried the new pension reporting requirements are going to be expensive to implement but no one will give us any costs yet and it isn't work we are even capable of doing in-house because we have no access to the data necessary to perform the calculations and we will HAVE to pay to get various reports.

Quotes from CFOs:

Accounting for OPEB has added direct costs for actuarial services. Future pension accounting will add even more outside service requirements and explanations for existing users of the financial statements.

GASB 34 was particularly costly. GASB 43/45, 44 also were costly. GASB 67 and 68 will require significant additional costs both direct and indirect.

GASB 34 & 45—Doubled the volume of financial statement presentation; required the on-going additional costs of hiring actuaries for future health care cost; increased on going audit cost for the additional testing; required additional cost to develop the fixed assets inventories and current book value.

GASB 34. I still do not believe it brought—particularly infrastructure asset reporting and ongoing reporting—any real benefit. Also, the explanation given that GASB 34 allows governmental financial statements to more closely

resemble private entity financials only serves to help the banking industry—not the taxpayers or elected officials. I think we are losing sight of what are annual reports are meant to do and that is allow the taxpayer a better understanding of their town's financial condition. GASB 34 just muddied the waters.

E. Limitations and Survey Respondents

The results here measure the perceptions, cost/benefits, and practices of municipal and county managers. Additionally, they were asked to provide insights into the support available through GASB, GASAC, GFOA, and ICMA, including ICMA's local chapters. Given the diversity of stakeholders (i.e., citizens, investors, rating agencies, auditors, fraud examiners, consultants, academicians, etc.) who may be consuming annual financial statement information and/or financial reporting assistance, we recommend that this research be expanded to incorporate the perceptions of others with regards to the benefits of annual financial reports. Each type of consumer may have a different purpose for utilizing annual financial statements; management happens to fall in the unique position of being both a consumer and a producer of annual financial information. Additionally, this survey was administered during a time when a highly salient and challenging set of statements (public pension reporting) is being required of entities that want to be GASB compliant.

The most significant limitation of the survey results is the lack of a generalizable sample. We supplemented these responses with solicitations to members of the Wisconsin and Illinois Government Finance Officers associations and City/County Managers associations due to our relationships (association management) with these organizations. As a result, the overwhelming majority of the responses are in Illinois and Wisconsin.

Table 17 Respondent's Professional Association

	Frequency	Percent
ICMA	51	30.7
IL and WI GFOA	58	34.9
WCMA and ILCMA	57	34.3
Total	166	100.0

Reflecting our efforts to supplement the analysis with managers/administrators and Chief Finance Officers in Wisconsin and Illinois, most of the respondents are from the states of Illinois and Wisconsin (see Table 18).

Of the 126 valid respondents, more than 40 percent work for communities with a population of less

Table 18 Respondent's State

	Frequency	Percent	Cumulative Percent
California	14	8.4	29.5
Florida	2	1.2	30.7
Illinois	66	39.8	70.5
Indiana	1	.6	71.1
Iowa	2	1.2	72.3
Maine	1	.6	72.9
Massachusetts	1	.6	73.5
Michigan	1	.6	74.1
Missouri	1	.6	74.7
New Hampshire	1	.6	75.3
New Jersey	1	.6	75.9
New York	1	.6	76.5
North Carolina	1	.6	77.1
Oregon	1	.6	77.7
Pennsylvania	3	1.8	79.5
Rhode Island	1	.6	80.1
South Carolina	2	1.2	81.3
Tennessee	1	.6	81.9
Texas	1	.6	82.5
Washington	1	.6	83.1
Wisconsin	28	16.9	100.0
Missing	35	21.1	21.1
Total	166	100.0	

than 20,000 (see Table 19). Just over 25 percent of the respondents work in communities with a population of greater than 50,000 residents.

We made a concerted effort to get a mix of respondents based on their position. More specifically, we wanted to examine differences in attitudes and perceptions between administrators/managers and chief financial officers (CFOs). Table 20 reflects our success in getting our desired mix of respondents: 55 percent are administrators/managers and more than 40 percent of the respondents are CFOs.

In addition to having a good mix of respondents based on position, we also got a nice mix of respondents based on the type of government they serve (see Table 21, pg. 11). The most commonly identified type of government was cities (45 percent), followed by villages (37 percent), and counties (13 percent).

Table 19 Population Size

	Frequency	Percent
Less Than 20,000	54	32.5
20,000–50,000	37	22.3
Greater Than 50,000	35	21.1
Valid Total	126	75.9
Missing	40	24.1
Total	166	100.0

Table 20 Position of survey respondent

	Frequency	Percent
Management (Manager/Administrator/CAO)	73	43.7
Finance/CFO	56	33.5
Other	2	1.2
Total	131	78.4
Missing	36	21.6
Total	167	100.0

Table 21 Type of Government Served by Respondent

	Frequency	Percent
County	15	9.0
City	52	31.3
Village	43	25.9
Town/Township	6	3.6
Total	116	69.9
Missing	50	30.1
Total	166	100.0

(for definitions see: census.gov/govs/cog)

Concluding Remarks and Recommendations

GASB’s vision statement is: “Greater accountability and well-informed decision-making through excellence in public-sector financial reporting.” Given the recent bankruptcy filings of Detroit, MI; Jefferson County, AL; San Bernardino, CA; and others, a case could be made that financial accountability is at a premium today. Recent GASB statement changes regarding fund balances, pensions and OPEB liabilities have made comprehensive annual financial reports (CAFRs) and other variations of annual financial reports (AFRs) more costly to generate, edit, validate, analyze, and share. “Today, state and local governments that prepare CAFR reports face an extensive challenge: completing an accurate and timely CAFR while using manual and error prone processes that are inefficient and lack strong internal controls. For many states, counties, cities and independent agencies, the annual CAFR reporting process usually takes months to complete.”⁵

The challenge with the timing of AFR completion has not been lost on GASB. In a recent report, GASB found that the average time to complete a CAFR by states, larger counties, municipalities, and special districts was approximately six months.⁶ In the same GASB report, users of AFRs—in this case, bond analysts, citizen/taxpayer groups, and legislative/oversight staff—responded that these financial reports were most useful if available within 45 days of the end of the fiscal year. The usefulness of the AFR falls off precipitously after those 45 days, meaning that the

average six-month delay may significantly hinder the utility of these documents.

Achieving the appropriate balance between the comprehensiveness of reporting and the ability to maintain accurate, timely, and meaningful financial reports remains elusive. As the focus of this project was on local governments, we found overwhelming support for AFRs and most statement changes; however, many local government managers faced with complicated updates in reporting standards may be reaching a point where they are getting frustrated with the cost and complexity associated with compliance. Economic Condition and SEA reporting are good examples of this tension: GASB put a great deal of time and effort into these voluntary reporting guidelines but our survey revealed that very few local government managers use them. Furthermore, given the small percentage of managers who reported using the AFR for policy decisions, it appears that many local governments are merely reporting for the sake of compliance and not necessarily to inform policy decisions, which is unfortunate given the rich information that is embedded in these reports.

Thus, it is only natural to ask why public sector reporting is in its current state. Some of the key contributors to this scenario include:

1. **Expanded financing options for government generate expanded disclosure:** Governmental entities have become more complex not only in the types of services they provide but also the manner in which they pay for them. Service provisions are made possible via either existing investments or cash reserves, GO bonds, revenue bonds, increased taxes or new taxes, user fees, reductions in expenditures, loans, shared services (i.e., internal service funds), internal borrowing (i.e., due to/due from), drawing down reserves, intergovernmental agreements, operating leases, capital leases, and, often, any combination of these and other financing tools. There have been 70 statements issued by GASB since its inception in 1984. Additionally, the GASB has issued Suggested Guidelines for Voluntary Reporting and SEA Performance Information in 2010 and is currently deliberating a project on Economic Condition Reporting: Financial Projections. GASB calls for two sets of financial statements (government-wide or accrual-based as well as Governmental Fund Statements or modified accrual-based). Furthermore, GFOA’s Certificate of Achievement for Excellence in Financial Reporting contains an 81-page checklist for obtaining this award.⁷

2. Fraud, abuse, and going-concern: State and local governments as well as standard setters continue to implement reporting changes and disclosures to mitigate negligence, waste, abuse, and fraud. The most notable and recent case of fraud occurred in Dixon, IL, where a former controller was convicted of stealing more than \$54 million dollars from the city. Eight municipalities have filed bankruptcy since 2010: San Bernardino, CA; Mammoth Lakes, CA; Stockton, CA; Boise County, ID; Jefferson County, GA; Harrisburg, PA; Central Falls, RI; and, most recently, Detroit, MI.⁸ Thus, disclosures related to going-concern are of even more importance to interested parties such as bond rating agencies, auditors, taxpayers, and investors.

3. Continued demand for increased transparency and accountability for finances: “The 2012 State of the States report, released in November by Harvard’s Institute of Politics, the University of Pennsylvania’s Fels Institute of Government, and the American Education Foundation, found that state and local governments are carrying more than \$7 trillion in debt, an amount equal to nearly half the federal debt. Often, the report said, ‘States do not account to citizens in ways that are transparent, timely or accessible.’”⁹ Taxpayers and stakeholders continue to demand answers to questions pertaining to loans, pensions, grants, budget details, and government finances. Furthermore, because transparency in government has become synonymous with good governance, multiple initiatives involving “big data” are springing up, generating even more questions of finances, particularly regarding what should be reported and to what level of detail. Big data may continue to generate more information for inclusion in financial reports.

4. Trying to meet the needs of many interested parties: Who are the stakeholders of a CAFR? For the most part, consumers of CAFR information include auditors, management, council members, citizens, taxpayers, bond rating agencies, investors, lenders, analysts, planners, consultants, regulating bodies, grant providers, etc. It’s no wonder the CAFR has become multi-faceted and very detailed. Yet, according to a report published this summer by the CFA Institute, investors believe the CAFR is not as informative as it should be (not to imply that it should be longer; it just needs to be more informative).¹⁰

5. Lagging Technology: With limited resources, efficiencies in reporting are critical but are not being captured. Annual financial reports are generally in a

static form of reporting (PDF or even Word document) and are difficult to analyze in terms of trend analysis or even comparison across locations, size, or types of jurisdictions. Companies reporting to the SEC use leading technologies such as XBRL for annual reporting to greatly increase efficiencies, accuracy, and transparency; but these tools have not yet made their way to governmental reporting.

It is time to take a fresh look at annual financial reporting. The current status is cumbersome, lengthy, and, in some cases, provides more information than is necessary; yet it often does not provide decision makers with timely information. Thus, we recommend the following steps be taken to increase accountability, transparency, and the usefulness of these annual financial reports for decision makers. We recognize that these are not quick fixes, but should be at the top of government’s priorities for year-end financial reporting.

1. Reassess content, semantics, and structure of annual financial reports. The Association of Government Accountants, in its 2012 assessment of governmental financial reporting, recognized the need for increased standardization, which might point to the reason for low reliance on the AFRs for informing policy decisions. Government must revisit what should be, at a minimum, in an annual financial report (i.e., fund reporting, statistical section, level of supporting detail, etc.); what is meant by the facts reported (e.g., definitions, assumptions, computations, exclusions or inclusions, etc.); and how information should be formatted to increase transparency (i.e., optimal format for reporting accrual-based/government-wide statements—respondents claim that the current structure is confusing). We recommend that a more comprehensive needs assessment be conducted across all types of consumers and producers relying on these annual financial reports. A national assessment of individuals’ needs should be conducted to determine what reporting content and format are meaningful and feasible. Additionally, standardization increases comparability needed to compare across years, departments, programs, or other entities. For instance, report consumers should be able to understand what is meant by public safety and expect that public safety in one entity means the same thing in another entity and is reported similarly. The timing is ripe for this reassessment as it also aligns with GASB technical plan.¹¹

2. Embrace new technologies. AFRs are usually prepared externally, are somewhat expensive documents, and, in many cases, take more than six months to prepare, rendering them less effective policy documents than they should be. Consumers and producers of governmental financial reports should come together to agree on tools that will help simplify and speed up the generation of annual financial reports as well as generate cost savings. Efficiencies gained from calculation mechanisms (i.e., a model with standardized inputs, assumptions, and computations to calculate unfunded pension liabilities) would help reduce some of the rising costs (i.e., actuarial costs).

Technologies are also now available to digitize financial reports. In fact, the SEC's current reporting model consists of digitized financial reports. Based on the survey results found here, the timing may be good to adopt new technologies that transform government's PDF versions of annual reports to digitized formats, in order to significantly increase efficiencies in generating, editing, validating, and sharing financial information. For instance, those entities reporting statistical information would not need to do so each year if information was digitized. Popular Annual Reports and other reporting to reviewing or regulating bodies (i.e., reporting to various state agencies, bond rating agencies, the GFOA, and the Municipal Securities Rulemaking Board, to name a few) can be automated. Subscribing to a centrally maintained reporting tool (i.e., use of taxonomies or data dictionaries) allows for adjustments to only one reporting system when GASB issues new standards, rather than having each government change its own reporting system—much like the concept of “Turbo Tax,” which gives producers of yearend tax statements a credible and standardized reporting tool that maintains changes in the tax law. Annual financial reports contain rich data that could be extremely useful for decision makers, yet very few use this information to inform policy decisions although they cited relying on some of the historical information for decision making. Digitized reports would not only increase efficiencies in analyzing historical trends, they would also be useful for developing performance metrics and forecasts and could help automate some of the components of SEA and Economic Condition Reporting.

3. Increase outreach/support efforts. The goals and utility in the production of AFRs are agreed upon by

GASB and local managers, yet the lines of communication between local managers and GASB—GFOA too, for that matter—are indirect. The local managers we surveyed are primarily depending on their auditors for reporting assistance: very few have looked directly to GASB or GFOA in the past or expect to in the foreseeable future. This lack of direct dialogue may be an important reason why there is not a consensus on reporting standards. The questionnaire results suggest that for those managers who have had direct contact with GASB, the interaction was very positive. We strongly suggest that ICMA, GASB, and GFOA pursue avenues to facilitate greater direct interaction between government managers and GASB. Furthermore, a more robust engagement tool and deliberation process is needed to enhance standard setting. Users can be alerted when changes hit the radar screen and be given an opportunity to express their professional opinions but do not seem to be aware of this option. Once standards are deliberated, the results should be communicated in a manner that not only explains the rationale for the standard but also the benefits of adopting the standards. This may be helpful in increasing the adoption rate of SEA Reporting and Economic Condition Reporting, particularly for those who were unsure of the benefits (37 percent were unsure of the benefits of SEA Reporting, 57 percent unsure of the benefits of Economic Condition Reporting).

Endnotes

1. Roybark, H.M., Coffman, E.N. and Previts, G. J. (2012), “The First Quarter Century of the GASB (1984–2009): A Perspective on Standard Setting (Part One)”, *ABACUS*.
2. Entities that do not prepare CAFRs could have smaller annual financial reports, where the report only provides management discussion & analysis section, financial statements, notes, and required supplementary information (RSI).
3. “GASB Research Brief: The Timeliness of Financial Reporting by State and Local Governments Compared With the Needs of Users.” Accessed September 6, 2013. http://gasb.org/cs/ContentServer?site=GASB&c=Document_C&pagename=GASB%2FDocument_C%2FGASBDocumentPage&cid=1176158316214
4. We also asked about financial reporting assistance from ICMA but respondents do not use the services offered by ICMA.
5. <http://www.nexdimension.net/wp-content/uploads/2013/04/ibm-cognos-for-the-public-sector.pdf>
6. http://gasb.org/cs/ContentServer?site=GASB&c=Document_C&pagename=GASB%2FDocument_C%2FGASBDocumentPage&cid=1176158316214
7. See <http://www.gfoa.org/downloads/GENERALPURPOSECHECKLIST2011.pdf>
8. <http://www.usatoday.com/story/news/nation/2013/07/22/detroit-bankruptcy-how-fast-will-it-go/2574013/>

9. Malanga, Steve. "The Many Ways That Cities Cook Their Bond Books" *The Wall Street Journal*; wsjl.com (updated May 31, 2013).
10. CFA Institute (July 2013). "Financial Reporting Disclosures: Investor Perspectives on Transparency, Trust and Volume."
11. <http://www.gasb.org/cs/BlobServer?blobkey=id&blobwhere=1175820451972&blobheader=application%2Fpdf&blobcol=urldata&blobtable=MungoBlobs>

Appendix: Survey Responses

see page 4 for methodology and other details

Table 1 Purposes of Annual Financial Reports

	Responses		
	N	Percent	Percent of Cases
Year-end Financial Status	120	19.9%	80.5%
Audit Compliance	106	17.6%	71.1%
State Compliance	90	14.9%	60.4%
Accountability	90	14.9%	60.4%
Requirement of rating agencies and/or investors	87	14.4%	58.4%
Transparency	76	12.6%	51.0%
Inform Policy Decisions	34	5.6%	22.8%
Total	603	100.0%	

Table 2 Use of AFRs to Guide Policy

	Frequency	Percent	Cumulative Percent
We don't use financial reports to inform policy	38	26.2%	26.2%
Very few policy decisions are based on AFR	55	37.9%	64.1%
A moderate amount of policy decisions are based on AFR	43	29.7%	93.8%
Most policy decisions are based on AFR	9	6.2%	100.0%
Total	145	100.0%	

Table 3 Sections of CAFR Used for Policy Decisions

	Responses		
	N	Percent	Percent of Cases
Governmental Funds	82	24.3%	65.1%
Proprietary Funds	62	18.3%	49.2%
MD&A	55	16.3%	43.7%
Note Disclosures	48	14.2%	38.1%
Government-Wide Statements	32	9.5%	25.4%
Statistical Section	30	8.9%	23.8%
Fiduciary Funds	29	8.6%	23.0%
Total	338	100.0%	

Table 4 AFR Preparation By Population

		Population			Total
		Less Than 20,000	20,000 to 50,000	Greater Than 50,000	
Prepared in-house	Count	7	6	19	32
	%	13.0%	16.2%	54.3%	25.4%
Mainly in-house w/some portions externally	Count	13	14	6	33
	%	24.1%	37.8%	17.1%	26.2%
Mainly externally	Count	34	17	10	61
	%	63.0%	45.9%	28.6%	48.4%
Total	Count	54	37	35	126
	%	100.0%	100.0%	100.0%	100.0%

Table 5 Amount Spent on AFR by Population Size

		Population			Total
		Less Than 20,000	20,000 to 50,000	Greater Than 50,000	
< \$10K	Count	6	3	2	11
	%	11.1%	8.1%	5.7%	8.7%
\$10K – \$25K	Count	23	6	6	35
	%	42.6%	16.2%	17.1%	27.8%
\$25K – \$50K	Count	21	22	11	54
	%	38.9%	59.5%	31.4%	42.9%
\$50K – \$100K	Count	4	6	10	20
	%	7.4%	16.2%	28.6%	15.9%
\$100K – \$200K	Count	0	0	4	4
	%	0.0%	0.0%	11.4%	3.2%
> \$200K	Count	0	0	2	2
	%	0.0%	0.0%	5.7%	1.6%
Total	Count	54	37	35	126
	%	100.0%	100.0%	100.0%	100.0%

Table 6 Does AFR/CAFR Benefits Outweigh its Costs by Position of Respondent?

		Position			Total
		Management	Finance/CFO	Other	
No	Count	20	7	1	28
	%	27.4%	12.5%	50.0%	21.4%
Yes	Count	48	42	1	91
	%	65.8%	75.0%	50.0%	69.5%
Don't Know	Count	5	7	0	12
	%	6.8%	12.5%	0.0%	9.2%
Total	Count	73	56	2	131
	%	100.0%	100.0%	100.0%	100.0%

Table 7 Frequency of Financial Reporting Assistance Sought

	GASB		GASAC		GFOA		Auditors	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%
Never	71	42.8%	124	74.7%	24	14.5%	2	1.5%
Seldom	40	24.1%	6	3.6%	63	38.0%	9	5.4%
Once or twice/year	21	12.7%	0	0.0%	43	25.9%	119	71.7%
Valid Total	132	79.5%	130	78.3%	130	78.3%	130	78.3%
Missing	34	20.5%	36	21.7%	36	21.7%	36	21.7%
Total	166	100.0%	166	100.0%	166	100.0%	166	100.0%

Table 8 Frequency of Feedback Given by Respondents to Organizations and Committees

	GASB		GASAC		GFOA		Auditors	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%
Never	75	45.2%	125	75.3%	61	36.7%	13	7.8%
Seldom	53	31.9%	7	4.2%	50	30.1%	45	27.1%
Once or twice/year	5	3.0%	0	0.0%	22	13.3%	73	44.0%
Valid Total	133	80.1%	132	79.5%	133	80.1%	131	78.9%
Missing	33	19.9%	34	20.5%	33	19.9%	35	21.1%
Total	166	100.0%	166	100.0%	166	100.0%	166	100.0%

Table 9 Rating of Assistance Received by These Organizations and Committees

	GASB		GASAC		GFOA		Auditors	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%
Have not used their service	76	45.8%	122	73.5%	37	22.3%	3	1.8%
Exceeded expectations	2	1.2%	1	0.6%	14	8.4%	41	24.7%
Met expectations	45	27.1%	4	2.4%	79	47.6%	87	52.4%
Did not meet expectations	8	4.8%	2	1.2%	1	0.6%	0	0.0%
Valid Total	131	78.9%	129	77.7%	131	78.9%	131	78.9%
Missing	35	21.1%	37	22.3%	35	21.1%	35	21.1%
Total	166	100.0%	166	100.0%	166	100.0%	166	100.0%

Table 10 Likelihood of Using These Services in the Future

	GASB		GASAC		GFOA		Auditors	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%
Likely	38	22.9%	1	0.6%	78	47.0%	128	77.1%
Not Likely	71	42.8%	97	58.4%	24	14.5%	3	1.8%
Unsure	23	13.9%	29	17.5%	28	16.9%	0.0	0.0%
Valid Total	132	79.5%	127	76.5%	130	78.3%	131	78.9%
Missing	34	20.5%	39	23.5%	36	21.7%	35	21.1%
Total	166	100.0%	166	100.0%	166	100.0%	166	100.0%

Table 11 Adoption of Significant GASB Changes

	Statement 34		Statements 43 & 45		Statement 54	
	Frequency	%	Frequency	%	Frequency	%
Implemented: Found Beneficial	43	25.9%	34	20.5%	45	27.1%
Implemented: Didn't Find Beneficial	84	50.6%	80	48.2%	75	45.2%
Did not implement			8	4.8%	2	1.2%
Did not Implement: Not Beneficial	1	0.6%	3	1.8%	1	0.6%
Don't Know	9	5.4%	11	6.6%	13	7.8%
Valid Total	137	82.5%	136	81.9%	136	81.9%
Missing	29	17.5%	30	18.1%	30	18.1%
Total	166	100.0%	166	100.0%	166	100.0%

Table 12 GASB Statements 67 and 68

	Plan to Implement		Positive Impact		Negative Impact		No Impact		Affect Policy	
	Frequency	%	Frequency	%	Frequency	%	Frequency	%	Frequency	%
No	12	7.2%	65	39.2%	44	26.5%	24	14.5%	63	38.0%
Yes	98	59.0%	5	3.0%	23	13.9%	51	30.7%	28	16.9%
Don't Know	26	15.7%	55	33.1%	58	34.9%	55	33.1%	41	24.7%
Valid Total	136	81.9%	125	75.3%	125	75.3%	130	78.3%	132	79.5%
Missing	30	18.1%	41	24.7%	41	24.7%	36	21.7%	34	20.5%
Total	166	100.0%	166	100.0%	166	100.0%	166	100.0%	166	100.0%

Table 13 Implementation of SEA and Economic Condition Reporting

	SEA		Economic Condition	
	Frequency	%	Frequency	%
Yes, we have or soon will be implementing	5	3.0%	4	2.4%
Not yet: it is still too cost prohibitive	32	19.3%	17	10.2%
Will not implement: it encroaches on management issues	29	17.5%	18	10.8%
No, I am not familiar enough	28	16.9%	71	42.8%
No, we decided it is not suitable for us	24	14.5%	15	9.0%
Other	19	11.4%	12	7.2%
Valid Total	137	82.5%	137	82.5%
Missing	29	17.5%	29	17.5%
Total	166	100.0%	166	100.0%

Table 14 Adoption Will Increase Accountability/Transparency

	SEA		Economic Condition	
	Frequency	%	Frequency	%
Agree With	22	13.3%	13	7.8%
Disagree With	55	33.1%	35	21.1%
Don't Know	59	35.5%	88	53.0%
Valid Total	136	81.9%	136	81.9%
Missing	30	18.1%	30	18.1%
Total	166	100.0%	166	100.0%

Table 15 Will Improve Management Practices Portion of Bond/Credit Rating

	SEA		Economic Condition	
	Frequency	%	Frequency	%
Agree With	11	6.6%	7	4.2%
Disagree With	66	39.8%	38	22.9%
Don't Know	58	34.9%	91	54.8%
Valid Total	135	81.3%	136	81.9%
Missing	31	18.7%	30	18.1%
Total	166	100.0%	166	100.0%

Table 16 Benefits of Reporting Exceed Costs

	SEA		Economic Condition	
	Frequency	%	Frequency	%
Agree With	7	4.2%	5	3.0%
Disagree With	68	41.0%	37	22.3%
Don't Know	61	36.7%	94	56.6%
Valid Total	136	81.9%	136	81.9%
Missing	30	18.1%	30	18.1%
Total	166	100.0%	166	100.0%



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