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To: County and City Chief Fiscal Officers

From: Division of Local Government Services and Economic Development

Subject: Accounting for Sales of Real Property Tax Receivables and Future Tobacco Settlement Receipts

Please give copies of this bulletin to others who may need this information.

Overview

The Governmental Accounting Standards Board (GASB) has issued Statement No. 48, *Sales and Pledges of Receivables and Future Revenues and Intra-Entity Transfers of Assets and Future Revenues*. Governments sometimes exchange specific receivables or future revenues for immediate cash payments. These transactions, like the exchange of delinquent property tax receivables or future tobacco settlement receipts for immediate cash, have become more prevalent. However, until now, there was no single standard that provided guidance for accounting and reporting of these transactions. Local governments that are planning to exchange delinquent property tax assets for cash and counties planning to sell their rights to future revenues arising from tobacco settlement agreements will be impacted by this new statement.

Statement 48 makes a distinction between sales of receivables and future revenues, and the pledging of receivables or future revenues to repay a collateralized borrowing. The distinction is important because the cash received from a borrowing would result in a liability while the cash received from a sale would most likely be recorded as revenue or deferred revenue, depending on the transaction.

The most significant factor distinguishing sales from borrowings is the continued involvement of the government doing the selling or borrowing, i.e., the extent to which the government retains or relinquishes control over the receivables or future revenues. This statement establishes that a transaction is a collateralized borrowing by default unless it meets criteria that demonstrate that the government is **no longer actively involved** with the receivable or future revenues it has transferred to other parties. For general overview purposes, criteria for determining whether a government continues to be involved include:

- Neither the government nor the buyer can cancel the sale agreement.
- The government cannot limit in any significant way the buyer's ability to subsequently sell or pledge the receivables or future revenues.
- For receivable transactions, the government cannot unilaterally substitute other receivables for those transferred.
- The government does not retain access to cash from the collection of receivables or there is appropriate isolation of cash collections from the government's other receivables and collections, all as more fully described in the statement.

Governments that have entered or are planning to enter into arrangements to exchange delinquent property tax receivables or future tobacco settlement receipts for immediate cash should review the substance of these transactions with their attorney's office and independent auditor to determine whether the transaction is a sale or merely a collateralized borrowing.

Reporting Collateralized Borrowings

If the criteria required for sale reporting are not met, the transaction is reported as a collateralized borrowing and the receivables or future revenues should be considered for financial statement purposes as pledged and not sold. The proceeds received from the borrowing should be reported as a liability in the statement of net assets (government-wide) and as an "other financing source" in the governmental fund statement of revenues, expenditures and changes in fund balance.

Reporting Sales

If the criteria for sale reporting are met, the transaction would be considered a sale. In a sale of delinquent property tax receivables reported on the government-wide financial statements, the receivables would be replaced by cash and the difference would be recorded as a gain or, most likely, a loss in the period of the sale. In governmental funds where delinquent property tax receivables are usually deferred, the receivable is also replaced by cash but real property tax revenues are now increased (credited) while the deferred tax revenue account is reduced (debited). The difference between the cash received and the higher carrying value of the receivables sold should be recorded as a reduction (debit) to real property tax revenues rather than a loss.

In an intra-entity transaction involving the sale of future revenues where the purchaser is a part of the same financial reporting entity as the selling government (as commonly found in New York counties that have created Tobacco Asset Securitization Corporations), the government must report the proceeds as deferred revenue in both the government-wide and fund financial statements. Revenue would then be recognized over the duration of the sales agreement. Because of the requirement under this statement to defer revenue in a sales transaction over the life of the sale agreement, the transaction would still provide cash flow but would not help the financial position of the government as it did prior to the issuance of this statement.

Implementation

Statement 48 should be implemented beginning with fiscal years ending December 31, 2007, though governments may apply the standards earlier. Because the requirements to defer revenues related to sales of future revenues differ from guidance previously provided by GASB in Technical Bulletin No. 2004-1, *Tobacco Settlement Recognition and Financial Reporting Entity Issues*, governments may apply the provisions of Statement 48 prospectively. **This means that governments do not have to adjust the accounting for sales of future revenues completed prior to the implementation date or to restate previous years' financial statements.**

Additional Information

If you have questions pertaining to this bulletin, please contact the State Comptroller's regional office that serves your local government. A listing of regional offices is enclosed.

End of Bulletin