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Revisiting the Standards That Shaped Government Financial Reporting
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# Your Presenter

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# What We Are Covering Today

1. **GASB 54 — Fund balance**
   Why the standard exists, what each classification bucket means, and what evidence supports it

2. **Preparing for Audit - GASB 54 Classifications**
   Approvals for commitments, the nonspendable reclass, and support for restricted and assigned

3. **GASB 31 — Investments**
   Why the standard exists, how investments are measured, and how to prepare for audit

4. **GASB 72 — Fair value**
   The definition, the hierarchy, and the disclosures that support the number

5. **Putting it together**
   How 31, 54 and 72 interact in a single government audit

# 1. GASB 54 — Fund Balance Classifications

Why the standard exists, What the buckets mean, and what evidence supports each one

# GASB 54 — Why the Standard Exists, Purpose and Impact

### Why it was needed

Before GASB 54, fund balance was split into reserved and unreserved, labels that said little about who could release the money and did not consistently communicate who imposed a constraint or how binding it was.  Users could not compare governments or even years before this standard.

GASB 54 replaced them with five classifications built on one idea: how binding the constraint is, and who imposed it.

### What changed

Five classifications based primarily on constraints: nonspendable, restricted, committed, assigned and unassigned.

The standard also tightened the definition of a special revenue fund, which changed how many governments structure their funds

### Reasoning behind it

Clarity — each classification tells the reader the source and strength of the constraint.

Comparability — the same constraint is reported the same way across governments.

Accountability — commitments must come from formal action of the highest level of authority, so the label is backed by evidence we can test.

**GASB 54**
core principle

*Fund balance is classified by the extent to which the government is bound to honor constraints on how the amounts can be spent — nonspendable, restricted, committed, assigned and unassigned.*

# Two Frameworks — Know Which One You Are In

## Fund balance

Governmental funds only · GASB 54

- Nonspendable
- Restricted
- Committed
- Assigned
- Unassigned

*Reported on: Balance Sheet — Governmental Funds*

## Net position

Government-wide, proprietary and fiduciary · GASB 34 / 63

- Net investment in capital assets
- Restricted
- Unrestricted

*Reported on: Statement of Net Position*

*The same dollars can be "restricted fund balance" in the fund statements and "restricted net position" government-wide — but the amounts differ, because the measurement focus differs.*

# GASB 54 — Ordered by How Binding the Constraint Is

| | |
|---|---|
| **Nonspendable** | Not in spendable form, or legally required to stay intact<br>*Who imposes it: Form of the asset* |
| **Restricted** | Externally imposed, or imposed by enabling legislation<br>*Who imposes it: External party / law* |
| **Committed** | Formal action of the highest level of decision-making authority<br>*Who imposes it: Council — resolution or ordinance* |
| **Assigned** | Intent, expressed by the body or an official it delegated<br>*Who imposes it: Management or delegated official* |
| **Unassigned** | Residual — General Fund only, if positive<br>*Who imposes it: Nobody* |

*Top of the list = hardest to undo. The lower you go, the easier the government can change its mind — and the less external evidence exists for us to test.*

# Nonspendable Fund Balance

### Two ways to get here

1. Not in spendable form — the asset cannot be converted to cash

   Inventory · prepaid items · long-term portion of loans and notes receivable · property held for resale

2. Legally or contractually required to be maintained intact

   Principal (corpus) of a permanent fund

### Why it matters to auditors

Entities typically do not track fund balance by classification in the general ledger. The trial balance may show one lump fund balance number.

So nonspendable is normally a financial statement reclassification entry auditors will propose every year.

### Traps

- Only the portion of loans receivable that is not expected to be converted to cash is nonspendable — do not classify the full receivable balance without looking at the terms.
- Prepaids and inventory are nonspendable under the consumption method. If your entity uses the purchases method, the amount may already be reported differently — make sure you are in compliance with the accounting policy note.
- If the underlying asset is also restricted (e.g. inventory purchased with grant funds), nonspendable wins for the form of the asset, but the restriction still has to be disclosed appropriately.

> *"Consider whether amounts that cannot be spent because they are not in spendable form or are legally or contractually required to be maintained intact are reported in governmental funds as nonspendable fund balance."*

# Restricted Fund Balance

**Constraints placed on the use of resources are externally enforceable — the government cannot lift them on its own.**

### Creditors
Bond covenants and indentures

### Grantors & contributors
Grant agreements, donor stipulations

### Other governments
Laws and regulations of state or federal government

### Enabling legislation
Constitutional provisions, or a law that both creates the revenue and legally restricts its use

**Enabling legislation is the one to slow down on.**

A restriction from enabling legislation exists only if the legal enforceability is real — meaning an external party could compel the government to use the resources as specified. A council that can repeal the ordinance at will has created a commitment, not a restriction.

## Examples of Audit Procedures:

- Obtain the underlying document — grant agreement, bond covenant, statute — and read the restriction language.
- Agree the restricted amount to the source: unspent grant proceeds, restricted cash and investments, debt service reserves.
- Test that the resources were actually used for the restricted purpose (coordinate with expenditure testing).
- Confirm restrictions no longer needed have been removed.

> *“Determine whether restricted, committed, or assigned resources, as applicable, were used for their intended purpose and in accordance with management's policies.”*

# Committed Fund Balance — Three Things Must Be True

1 **Highest level of authority**

The constraint came from the government's highest decision-making body — the City Council, Board of Supervisors, Board of Trustees. A finance director memo is not a commitment.

2 **Formal action**

A resolution, ordinance or equivalent formal action — not a budget line, not a staff report on its own, not a verbal direction. The formal action can be verified through the city council minutes to confirm the vote happened.

3 **Before the end of the reporting period**

The formal action must occur on or before the balance sheet date. The dollar amount may be determined afterward — but the decision to commit cannot be.

**And one more: it can only be removed or changed by the same kind of formal action that created it.**

*"Determine whether formal action to commit fund balance to a specific purpose was taken at the highest level of decision-making authority prior to the end of the reporting period."*

# Assigned and Unassigned

## Assigned

Intent to use resources for a specific purpose, expressed by the governing body or by an official or committee the body has delegated authority to.

- Less formal than committed — no resolution required
- Delegation must itself be authorized; find it in the fund balance policy
- Encumbrances are reported within the applicable classification, not as a separate line
- In funds other than the General Fund, positive residual fund balance is assigned by definition
- Cannot cause a negative unassigned balance in the General Fund

## Unassigned

The residual. Everything in the General Fund that is not nonspendable, restricted, committed or assigned.

- The General Fund is the only fund that reports a positive unassigned balance
- Another governmental fund reports negative unassigned only when expenditures for a purpose exceeded the amounts restricted, committed or assigned to it
- A new or increased negative unassigned balance should raise awareness — investigate the cause
- Deficit fund balances of individual nonmajor funds must be disclosed

***Quick scan every year: sort the fund balance detail and look for unassigned outside the General Fund, and any negative balance anywhere.***

*“Determine whether a negative unassigned equity has increased or been created.”*

# Encumbrances — a Commitment, Not a Classification

### What an encumbrance is

A commitment of appropriated funds for goods or services ordered but not yet received — a purchase order, contract or similar.

It exists for budgetary control: the appropriation is set aside so the same dollars cannot be spent twice. Encumbering does not create an expenditure or a liability — nothing has been received yet.

### Where it lands under GASB 54

The old "reserved for encumbrances" line is gone. Encumbrances are no longer a fund balance classification of their own.

Encumbered amounts are reported inside restricted, committed or assigned, following the constraint on the underlying resources — if nothing else constrains them, the act of encumbering is itself evidence of intent, so they are assigned.

### Disclosure

Significant encumbrances are disclosed in the notes — by major fund, and by nonmajor funds in the aggregate — alongside other significant commitments.

*Check that the note exists and agrees to the year-end open encumbrance listing. It is a routine miss.*

### Examples of Audit Procedures:

- Obtain the open PO / encumbrance listing at year end and agree the total to the classification schedule.
- Sample POs: agree the date is on or before year end, and agree amount and vendor to the PO or contract.
- Confirm the goods or services were not received before year end — if they were, it is an expenditure and a payable.
- Confirm no separate encumbrance line appears on the face of the balance sheet.

*“Consider whether encumbrances are included within the applicable fund balance classification (i.e., not displayed separately).”*

# Spending Order

**Two separate policies – to be disclosed in footnotes to the financial statements**

### Policy 1 — Restricted vs. unrestricted

When an expenditure could be paid from either restricted or unrestricted fund balance, which does the government use first?

*Most governments spend restricted first.*

### Policy 2 — Within unrestricted

When an expenditure could be paid from committed, assigned or unassigned, which order applies?

*Default if no policy exists: committed, then assigned, then unassigned.*

**Other items to consider: is there a minimum fund balance policy, and has stabilization been formally set aside?**

Stabilization only qualifies as committed or restricted if the formal action describes specific, non-routine circumstances — "for economic uncertainty" with no further definition is generally not specific enough, and the amount stays unassigned in the General Fund.

## Footnote Disclosure:

- The policies drive a note disclosure — check the fund balance note disclosure agrees to policies.
- If the government has no policy, apply the GASB 54 default.

*"Management's policy regarding whether to first apply restricted or unrestricted resources when an expenditure is incurred for which both restricted and unrestricted fund balance or net position are available."*

# Implementation Lessons and Recurring Challenges

1. Committed balances lack timely formal action or the action comes after year-end.
2. Assigned balances are unsupported because delegation authority is missing or unclear.
3. Encumbrances are shown as separate classification instead of within applicable category.
4. Nonspendable amounts are not rebuilt from inventory, prepaids and qualifying long-term receivables.
5. Special revenue funds continue even when restricted or committed proceeds are no longer a substantial inflow.
6. Spending-order and stabilization policies are inconsistent with note disclosures.

# POLLING QUESTION #1

Which fund balance classification causes your team the most difficulty at year end?

A. Nonspendable
B. Restricted
C. Committed
D. Assigned

# 2. Preparing for Audit - GASB 54 Classifications

Approvals, the nonspendable reclass, and supporting the rest

# Committed and Nonspendable — Tips to Prepare for Audit

## Committed

Support the constraint with formal action of the highest level of authority, taken on or before the balance sheet date.

- Obtain detail by purpose, then request the resolution, ordinance or minutes behind each amount
- Confirm the body that acted is the highest level of decision-making authority
- Check the date of the action against the balance sheet date — a staff report dated after year end does not support the commitment
- If the action came first but the amount was determined later, the amount is still reportable
- Agree and foot each amount, compare to prior year, and explain the movement
- Confirm nothing that is no longer needed is still sitting in committed

## Nonspendable

Usually, a financial statement entry proposed by auditors — entities typically do not track classifications in the general ledger, so build the number and support it.

- Prelim (client) + auditor adjustment = reported amount in the ACFR
- Build the total from its components — inventory, prepaid items, and the portion of loans receivable not expected to convert to cash
- Agree each component to its account balance, foot the total, and agree it back to the equity nonspendable account
- Total fund balance does not change — the entry only moves amounts between classifications

*"Inspect documentation supporting equity classifications" · "If formal action to commit fund balance occurred prior to the end of the reporting period, but specific amounts were not known until the subsequent period, determine whether the amounts were properly reported."*

# Restricted and Assigned – Tips to Prepare for Audit

## Restricted

1. **Obtain the source document**
   Grant agreement, bond covenant, statute, donor letter. Read the actual restriction language.
2. **Agree the amount**
   To unspent grant proceeds, restricted cash and investments, or the reserve requirement in the debt agreement.
3. **Determine the use**
   Were the resources spent on the restricted purpose? Coordinate with expenditure transactions.
4. **Should any be released?**
   A restriction that has been satisfied should no longer be reported.

## Assigned

1. **Find the delegation**
   The fund balance policy should say who may assign. Without that authority, the assignment is not supported.
2. **Obtain evidence of intent**
   Adopted budget, encumbrance report, council action short of a resolution, management memo.
3. **Check the encumbrance treatment**
   Encumbrances go inside the applicable classification — never on their own line.
4. **Check the residual rule**
   In funds other than the General Fund, positive residual fund balance is assigned by definition.

*"Determine whether equity classifications have been made in compliance with legal and contractual provisions and management policies."*

# Example: Committed or Assigned?

### Scenario

The city council discusses using year-end surplus for a future facility project.  A finance director memo is prepared in July, after a June 30 year-end.  No resolution or ordinance was adopted before year-end.

*What evidence would change the answer?*

### Likely conclusion

Not committed.  A post-year-end management memo does not demonstrate formal action by the highest decision-making authority before period-end.

### What to obtain

Fund balance policy, delegation language, council minutes, resolution or ordinance, approval date and the calculation supporting the reported amount.

# Special Revenue Funds

**A special revenue fund is appropriate only when the proceeds of specific revenue sources are restricted or committed to expenditure for a specified purpose — other than debt service or capital projects.**
Resources that do not meet that criterion belong in the General Fund or another fund type.

1. **Identify the source**
   Name the specific restricted or committed revenue source behind each fund. If this can not be determined, it could lead to an audit finding.
2. **Reported directly, not transferred**
   The restricted or committed revenue must be recorded in the fund itself — not collected in the General Fund and transferred out.
3. **Other resources constrained too**
   Anything else in the fund must be restricted, committed or assigned to the fund's purpose.
4. **Still a substantial portion**
   The restricted or committed proceeds must be expected to continue to be a substantial portion of the fund's inflows.
5. **Discontinue when it fails**
   If that expectation is gone, the fund should be discontinued and the remaining resources reported in the General Fund or another fund type.

*"Determine whether special revenue funds are used only when the proceeds of specific revenue sources are restricted or committed to expenditure for specified purposes other than debt service or capital projects."*

# Permanent Funds

**Resources legally restricted so that only earnings — not principal — may be spent, and only for purposes that benefit the government or its citizenry.**

## The distinction people get wrong

Permanent fund — benefits the government or its citizens. A governmental fund; it appears on the governmental funds balance sheet. Cemetery perpetual care, or an endowment whose earnings buy books for the public library.

Private-purpose trust — benefits individuals, private organizations or other governments. A fiduciary fund; it does not appear in the governmental fund statements at all. A scholarship trust for named individuals.

## How the fund balance splits

**Corpus / principal → nonspendable**

Legally required to be maintained intact, so it is not in spendable form.

**Accumulated earnings → restricted**

Available to spend, but only for the purpose the instrument specifies.

*The corpus is the second kind of nonspendable amount — it connects straight back to the nonspendable reclass.*

## Examples of Audit Procedures:

- Read the trust instrument, will, gift agreement or ordinance that created the fund — that document is the audit evidence.
- Agree the corpus to the instrument and to the prior-year balance; recompute any additions.
- Recompute investment earnings allocated to the fund; confirm the method matches the instrument.
- Vouch expenditures: only earnings spent, only on the specified purpose, only benefiting the government or its citizens.
- Confirm principal was not invaded. If it was, determine whether it must be restored, and disclose.

*"Determine whether only earnings (and not principal) were expended and only to benefit the government or its citizens and only for the purposes for which the earnings are restricted" · "Determine whether the amount of corpus legally required to be maintained in perpetuity has been properly maintained."*

# POLLING QUESTION #2

How does your entity support committed fund balance?

A. Council or board resolution
B. Adopted budget document
C. Finance director memo or internal policy
D. We are not sure

# 3. GASB 31 — Investments and Fair Value

Why the standard exists, how investments are measured, and how to prepare for audit

# GASB 31 — Why the Standard Exists

### What the standard requires

Issued March 1997, effective for periods beginning after June 15, 1997 — fiscal year 1998 for most governments.

Governments report most investments at fair value and report the change in fair value as investment income — realized and unrealized together.

GASB 31 was issued to move governmental investment reporting from a historical-cost focus to a fair-value focus so that financial statements better reflect the current economic value and performance of governmental investment portfolios.

### Why it matters

Investments are often the largest liquid asset a government holds. Reporting them at stale cost overstates or understates the resources available to fund services.

Fair value also makes performance visible: readers can see whether the portfolio gained or lost value during the year rather than only when a security is sold.

Because the adjustment is an audit-cycle entry, it is a recurring source of proposed adjustments and disclosure errors.

### Reasoning behind it

Comparability — two governments holding the same security report the same amount.

Accountability — the statements show stewardship over public funds at the balance sheet date, not at purchase date.

Decision usefulness — investment income measured on a fair value basis reflects the economics of the period.

**GASB 31**
core principle

*Investments are reported at fair value as of the statement of net position date, and all changes in fair value are reported in investment income.*

# GASB 31 — What Is In Scope, What Is Not

**Scope drives measurement. Before valuing anything, decide whether the instrument is inside GASB 31 at all — and whether an amortized cost exception applies.**

### In scope

Participating interest-earning investment contracts

External investment pools — LAIF, CAMP and similar local government investment pools

Open-end mutual funds

Debt securities

Equity securities, option contracts, stock warrants and stock rights with readily determinable fair values

### Outside the scope, or measured at amortized cost

**Governmental external investment pools, defined benefit pension plans, and IRC Section 457 plans follow other standards.**

**Money market investments and participating contracts maturing within one year of purchase may use amortized cost, as may pools meeting the GASB 79 criteria.**

### Examples of Audit Procedures:

Obtain the investment listing and agree it to statements from every institution and pool.

For each instrument, document the measurement basis chosen.

For amortized cost positions, verify the maturity at purchase and the qualifying criteria in writing.

Open-end mutual funds are valued at the fund's share price; 2a7-like pool positions at the pool's share price.

**GASB 31**
scope

*Investments should be marked to fair value at a minimum as of the date of the statement of financial position.*

# GASB 31 — Recording Fair Value at Year End

1

### Determine the fair value

Use the pool sponsor's reported fair value factor, the fund share price, or a quoted market price at the reporting date. Document the source for every position.

2

### Compute the adjustment

Fair value less carrying value equals the entry. Example: $100,000 invested in an external investment pool that reports a $1.05 per unit fair value at June 30 is carried at $105,000, with the $5,000 increase recorded as investment income.

3

### Record it — and reverse it

Debit or credit investments, with the offset to the change in fair value of investments within investment income. Many governments reverse the entry at the start of the next year so the ledger stays on transaction values.

**When the position is withdrawn at the stable value, the prior fair value increase reverses — a negative change in fair value, not a loss on sale.**

**GASB 31**
year-end entry

*The change in the fair value of investments is reported as part of investment income — realized and unrealized amounts are not displayed separately.*

# GASB 31 — Pooled Cash and Interest Allocation

1

## Report the pool correctly

An internal investment pool is reported in the fund that holds it, with amounts due to the other funds for their positions. Each participating fund reports equity in the cash management pool with the corresponding interfund balances.

2

## Allocate interest on a rational basis

The usual method is the weighted average investment balance of each fund multiplied by the monthly rate. Whatever method is used, it should be consistent, documented, and applied to every participating fund.

3

## Watch the negative balances

Interest should not be allocated to a negative pooled cash position. Negative investment income is reported as negative revenue — not as an expense — and funds with no cash should not receive an allocation at all.

**In proprietary funds that separate operating and nonoperating results, the change in fair value follows the same presentation as other investment income — generally nonoperating.**

**GASB 31**
allocation

*Income from investments associated with one fund that is assigned to another fund must be disclosed.*

# Prepare for Audit - Investments Under GASB 31

**The audit objective is that investments exist, are owned by the government, are complete, and are measured and presented at the right amount under GASB 31.**

Most exceptions are found in the reconciliation and in the fair value entry — not in the underlying securities.

1. **Obtain the complete listing**
   Get every account and the year-end statement for each. Completeness comes first; a missing account cannot be valued.

2. **Reconcile to the general ledger**
   Tie the investment listing, the fair value adjustment entry, and the note disclosures to the trial balance. Investigate every reconciling item.

3. **Confirm balances independently**
   Send confirmations to the institution or pool, or pull the published pool confirmation directly, and agree it to the pre-adjustment balance.

4. **Recompute the fair value entry**
   Recalculate the adjustment using the published factor or share price. Verify the effect flows to investment income and to the note disclosures.

5. **Test interest allocation and disclosures**
   Recompute the allocation, look for interest allocated to negative balances, and check the risk and fair value disclosures for completeness.

***Check the disclosures too: valuation methods and assumptions, the amortized cost policy, pool oversight, and the four risk disclosures.***

**GASB 31**
audit approach

*Determine whether investments are properly valued at fair value at the reporting date and whether the resulting change in fair value is properly reported in investment income.*

# Common Challenges and Lessons Learned

1. **Missing or stale valuation support.**
   Use reporting-date information and retain the source.
2. **Fair Value change posted outside investment income.**
   Map realized and unrealized components consistently.
3. **Pool position measure incorrectly**.
   Review sponsor documentation and whether an amortized-cost exception applies.
4. **Interest allocated to funds with negative or no pooled cash.**
   Use a rational, documented allocation basis and investigate anomalies.
5. **General ledger, investment schedule and note do not reconcile.**
   Design one rollforward that feeds the entry and disclosures.

# POLLING QUESTION #3

Which investment makes up the largest portion of your portfolio?

A. LAIF
B. CAMP or another local government pool
C. Certificates of deposit
D. Debt or equity securities

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# 4. GASB 72 — Fair Value Measurement

The definition, the hierarchy, and the disclosures that support the number

# GASB 72 — Why the Standard Exists

### What the standard does

Issued February 2015, effective for periods beginning after June 15, 2015 — fiscal year 2016 for most governments.

GASB 31 says to use fair value; GASB 72 defines it: the price received to sell an asset in an orderly transaction between market participants at the measurement date.

It is an exit price, set in the principal market from the market participant's perspective — not the government's own intent.

### Why it matters

Before GASB 72, "fair value" was applied inconsistently across governments and across asset classes. The standard gave one definition, one framework of valuation techniques, and one disclosure package.

It also expanded the population: donated capital assets, acquisitions, certain investments in life insurance and alternative investments all draw on the same framework.

### Reasoning behind it

Consistency — one measurement definition across every standard that calls for fair value.

Transparency — the hierarchy tells the reader how observable the inputs behind the number are.

Auditability — a documented technique and input level makes an estimate testable instead of asserted.

**GASB 72**
core principle

*Fair value is an exit price — what the government would receive to sell the asset in an orderly transaction between market participants at the measurement date.*

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# Comparison: GASB 31 vs. GASB 72

| Topic | GASB 31 – *Accounting and Financial Reporting for Certain Investments and for External Investment Pools* | GASB 72 – *Fair Value Measurement and Application* |
|---|---|---|
| Primary Objective | Require most investments to be reported at fair value and recognize changes in value as investment income. | Establish a consistent definition of fair value, valuation techniques, and disclosure requirements. |
| Key Question Addressed | What investments should be reported at fair value? | How do we determine fair value and disclose it? |
| Focus | Investment accounting and reporting | Fair value measurement methodology and disclosures |
| Major Result | Most investments moved from cost-based reporting to fair value reporting. | Introduced fair value hierarchy (Level 1, 2, 3) and enhanced disclosures. |
| Investment Income | Requires unrealized gains and losses to be reported as investment income. | Does not change investment income recognition; focuses on valuation methods. |

# GASB 72 — The Three-Level Hierarchy

1

**Level 1 — quoted prices**

Unadjusted quoted prices in active markets for identical assets that the government can access at the measurement date. Equity securities on a registered exchange and most open-end mutual funds land here.

2

**Level 2 — other observable inputs**

Quoted prices for similar assets, quoted prices in markets that are not active, or inputs such as interest rates and yield curves that are observable. Most government debt securities priced by a pricing service are Level 2.

3

**Level 3 — unobservable inputs**

Inputs developed using the best information available, including the government's own assumptions. Real estate held as an investment and alternative investments often fall here — and carry the most disclosure and the most audit work.

**The level follows the lowest-level input that is significant to the whole measurement — not the highest one available. Positions measured at amortized cost or at net asset value are presented outside the hierarchy.**

**GASB 72**
hierarchy

*A fair value measurement is categorized in its entirety in the level of the lowest significant input used in the valuation.*

# GASB 72 — Techniques and Disclosures

**One definition, three valuation approaches, and a disclosure package that lets the reader judge how reliable the measurement is.**

### The valuation approaches

Market approach — prices from identical or comparable transactions.

Cost approach — the amount currently required to replace the service capacity of the asset.

Income approach — future amounts converted to a single present amount, such as a discounted cash flow.

The technique should be applied consistently; a change in technique is accounted for as a change in accounting estimate and disclosed.

### What must be disclosed

**The fair value measurement at period end, by asset class.**

**The hierarchy level for each class, and the reason for any transfer between levels.**

**The valuation techniques used and any change in technique.**

**For Level 3, the significant unobservable inputs; for net asset value positions, redemption terms and unfunded commitments.**

## Tips to prepare for audit and financial statement disclosure

Agree the classes disclosed to the investment listing — the note should sum to the statement.

Challenge the level assigned to each class; a Level 1 label on a thinly traded or pricing-service security is a common error.

Obtain and read the pricing service methodology or third-party valuation supporting Level 2 and Level 3 amounts.

For Level 3, evaluate the significant inputs for reasonableness and consider using a specialist when the estimate is material.

**GASB 72**
disclosure

*Disclosures are organized by asset class, by hierarchy level, and by the valuation techniques used — including the reason for any change in technique.*

# Auditing Fair Value Under GASB 72

**A fair value measurement is an accounting estimate. The audit approach follows the estimate: understand how management developed it, test the data and the method, and evaluate the disclosure.**
Risk rises as inputs become less observable — plan the most effort where Level 3 amounts are material.

1. **Understand the process**
   Document how management determines fair value, who reviews it, what pricing sources are used, and what controls exist over the pricing data.
2. **Test the inputs**
   Agree quoted prices to an independent source, obtain the pricing service methodology, and evaluate the observability of the inputs used.
3. **Evaluate the level assigned**
   Confirm the hierarchy level reflects the lowest significant input. Look for classes mislabeled Level 1 and for undisclosed transfers between levels.
4. **Assess Level 3 estimates**
   Evaluate the assumptions for bias and reasonableness, develop an independent range or point estimate where practical, and consider a valuation specialist.
5. **Tie out the disclosure**
   Foot the fair value table, agree it to the statements, and verify the technique descriptions, transfers, and net asset value terms are complete.

***Document the technique, the inputs, the level, and why the level is appropriate for each class.***

**GASB 72**
audit approach

*Evaluate whether fair value measurements and the related disclosures are in accordance with the framework, and whether the methods and significant assumptions used are reasonable.*

# Implementation Lessons and Common Challenges

1. Accepting a custodian or pricing-service level without understanding the valuation methodology.
2. Treating net asset value measurements as though they automatically belong in Level 3.
3. Inconsistent asset-class groupings between the investment note and fair value table.
4. Insufficient documentation of valuation techniques, assumptions and changes in technique.
5. Level 3 inputs are not subjected to an appropriate management review or specialist assessment.
6. Disclosure tables do not tie to the statement of net position or governmental fund balance sheet.

# POLLING QUESTION #4

Which fair value area is the biggest challenge for your entity?

A. Assigning the hierarchy level
B. Recording the year-end fair value entry
C. Interest allocation across pooled cash
D. Preparing the note disclosures

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# 5. Putting it Together

How 31, 54 and 72 interact in a single government audit

# GASB 31, 54 and 72 in One Audit

### How the three connect

GASB 72 defines fair value. GASB 31 tells you which investments are measured at that fair value and where the change in value is reported.

GASB 54 then determines how the resulting fund balance — including the investment gain or loss that flows through it — is classified and reported in the governmental funds.

A misstatement in any one of them moves the fund balance classification totals and the note disclosures together.

### How to sequence the work

Measure first: apply GASB 72 to set fair value and the hierarchy level for each class.

Record second: post the GASB 31 adjustment and allocate pooled interest.

Classify third: run the GASB 54 analysis on the resulting fund balance.

Disclose last: the investment, fair value and fund balance notes must reconcile.

## What we document either way

The measurement basis and hierarchy level for every investment class.

The recomputed fair value entry and interest allocation, with reconciling items resolved.

The formal action or external constraint supporting each fund balance classification.

A reviewed, cross-referenced set of note disclosures — the most common place all three standards fail at once.

**Wrap-up**
takeaway

*Measure it under GASB 72, record it under GASB 31, classify it under GASB 54 — and make the three notes agree before the file is released.*

# Questions?

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