



Dave Yost • Auditor of State

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To: All Fiscal Officers and Independent Public Accountants

From: Dave Yost, Auditor of State

Subject: Governmental Accounting Boards Statement 77,
Tax Abatement Disclosures

Summary

Note: The following is only an overview. Governments preparing financial statements under generally accepted accounting principles (GAAP) or an other comprehensive basis of accounting (OCBOA) and their independent auditors are responsible for understanding of this Statement sufficiently to apply it to their financial statements and audit it, respectively. ¹ Examples included in this bulletin are not all inclusive. Consult your legal counsel for applicability of tax abatement programs.

Background Information

The Governmental Accounting Standards Board (GASB) Statement No. 77, “Tax Abatement Disclosures,” provides a definition of tax abatements which is for financial reporting purposes only and identifies required note disclosure related to tax abatements.

Local governments employ a variety of programs and policies that reduce the taxes an individual or entity otherwise would owe, with the intent of encouraging certain actions, such as constructing housing in a particular neighborhood or relocating/retaining businesses. The goal of GASB Statement No. 77 is to make tax abatement transactions more transparent, and to provide financial statement users with the information necessary to assess how tax abatements affect financial position and results of operations, including the future ability to raise resources and meet financial obligations.

The GASB issues an implementation guide (IG) each year to supplement the guidance found in the GASB pronouncements. The IG is organized in a question and answer format. This bulletin references specific questions related to tax abatement disclosures from the 2016-1 IG.

¹ You can view the entire statement at www.gasb.org.

This Statement applies to financial statements for reporting periods beginning after December 15, 2015. The Statement's provisions need not be applied to immaterial items. Governments should begin planning now to determine how to compile the information needed for these disclosures.

Tax Abatement Definition

For purposes of GASB Statement No 77, the definition of a tax abatement is as follows:

A reduction in tax revenues that results from an agreement between one or more governments and an individual or entity in which (a) one or more governments promise to forgo tax revenues to which they are otherwise entitled and (b) the individual or entity promises to take a specific action after the agreement has been entered into that contributes to economic development or otherwise benefits the governments or the citizens of those governments. (GASB 77, paragraph 4)

This definition is important in distinguishing abatements from; for example, tax deductions, exemptions or credits, which often relate to a taxpayer's *past* actions such as deducting charitable donations made during the preceding year.

The transaction's substance, not its form or title, is a key factor in determining whether the transaction meets the above definition of a tax abatement.

Since this definition is fundamental to implementing GASB Statement No. 77, following is a discussion of the key elements of the definition:

Existence of an Agreement GASB 77 tax abatements result from an identifiable agreement between a government and a specific individual or entity. This agreement should have two components:

- Promise by the government to reduce taxes
- Promise from the individual or entity to subsequently perform a certain beneficial action

The agreement may be in writing or may be implicitly understood by the government and the individual or entity. (See GASB 77 paragraph B9 and B10)

Individual or Entity GASB 77 tax abatements have agreements with individuals or entities. If there are no individuals or entities required to perform an action that contributes to economic development or otherwise benefits the government or its citizens, the transaction does not meet the GASB 77 definition. (See IG 4.77)

Forgo Tax Revenue The GASB 77 definition is specific to tax revenue, including property, income, sales or other taxes levied by the local government. However, if there is a tax abatement agreement at the State level to forgo certain tax money, the local government would not disclose information about the tax abatement agreement if the local government revenue that is reduced is shared revenue, which is not considered to be taxes revenue to the local government. (See IG 4.80)

Agreement Precedes Reduction GASB 77 requires the agreement precede the performance of the required action by the individual or entity. If the action is performed prior to the agreement, the transaction does not meet the GASB 77 definition. (See GASB 77 Paragraph B11)

Taxes Abated by Another Government

Governments can enter into agreements which abate their own taxes; however, a government's taxes can also be abated as a result of agreements that are entered into by another government. Both types of abatements require note disclosure, if they meet the GASB 77 definition.

Note Disclosure

As noted above, this standard requires note disclosure about tax abatements. It does not require recognizing abatements in the financial statements. The following discussion provides an overview of the disclosure principles and requirements. The specific principles and requirements are addressed in paragraphs 5 through 10 of GASB Statement No. 77. These disclosures encompass tax abatements resulting from both (a) the reporting government's agreements and (b) other governments' agreements, if they reduce the reporting government's tax revenues.

Disclosures for tax abatements may be provided individually or may be aggregated. If tax abatements are disclosed individually, the disclosure should include a brief description of the quantitative threshold the government used to determine which agreements to disclose individually.

Disclosure should commence in the period in which a tax abatement agreement is entered into and continue until the tax abatement agreement expires, except in cases where the government made commitments other than to reduce taxes as part of the tax abatement agreement. In these instances, disclosures should be made until the government has fulfilled the commitment.

This Statement requires governments that enter into agreements for the abatement of taxes to include the following in their note disclosures (see paragraph 7 of GASB 77 for more specific information):

- Brief descriptive information, including the name and purpose of the abatement, the tax being abated, the authority under which tax abatements are provided, eligibility criteria, the mechanism by which taxes are abated, provisions for recapturing abated taxes, and the types of commitments made by tax abatement recipients;
- The gross dollar amount of taxes abated during the period;
- Commitments made by a government, other than to abate taxes, as part of a tax abatement agreement; and,
- Amounts received or receivable from other governments in association with the foregone tax revenue.

Disclosure information for tax abatements resulting from agreements entered into by the reporting government should be organized by major tax abatement program and may disclose information for individual tax abatement agreements within those programs.

Tax abatement agreements of other governments which result in the reduction of the tax revenues of the reporting government should be organized in the reporting government's disclosures by the government that entered into the tax abatements agreement and the specific tax being abated. Governments may disclose information for individual tax abatement agreements of other governments within the specific tax

being abated. For those tax abatement agreements, a reporting government should disclose (see paragraph 8 of GASB 77 for more specific information):

- The names of the governments that entered into the agreements and the specific taxes being abated;
- The gross dollar amount of taxes abated during the period; and,
- Amounts received or receivable from other governments in association with the foregone tax revenue.

If information is omitted because it is legally prohibited from being disclosed, include a description of the general nature of the omitted information and the specific source of the legal prohibition.

Potential GASB 77 Tax Abatement Programs and Sources of Information

Although not an exhaustive list, some of the more common programs with the *potential* for GASB 77 tax abatements include:

- Community Reinvestment Areas (CRAs)
- Enterprise Zone Agreements
- Tax Increment Financing Agreement (TIFs)
- Income Tax

Most TIFs will not meet the GASB 77 definition of a tax abatement. In most TIFs, the property owner is still making compensation payments in the same amount as the property tax, so the revenue is not forgone, it is; however, redirected and restricted as to use. However, TIFs should still be reviewed as there is still the potential for a TIF to meet the definition.

In order to accumulate the necessary information for the GASB 77 note disclosure for taxes abated by the local government, first identify the tax abatement programs offered by the local government and review the corresponding agreements to identify the ones meeting the GASB 77 definition. In order to determine the amount of property taxes abated, look at the appropriate property tax information. The Form C utilized for CRA annual reporting may provide some tax information. Also, the County Auditor's office may be able to provide additional information. If the government abates income taxes, the local government's records should be the best source of information.

In order to accumulate the necessary information for the GASB 77 note disclosure for taxes abated by another government, first, contact the local governments with the ability to abate your taxes to determine what information they can provide. Also, the County Auditor's office may be able to provide some information.

Audit Considerations - Evaluating Disclosure Misstatements

While a government's management is responsible for the contents of the financial report, an independent auditor's primary responsibility is to report on whether the basic financial statements, including the notes thereto, are presented fairly in accordance with the financial reporting framework. GASB codification 2300.108 indicates notes to the financial statements provide necessary disclosure of material items, the omission of which would cause the financial statements to be misleading.

As noted in GASB No. 77, the disclosure requirements “improve financial reporting by giving users of financial statements essential information that is not consistently or comprehensively reported to the public at present. Disclosure of information about the nature and magnitude of tax abatements will make these transactions more transparent to financial statement users. As a result, users will be better equipped to understand (1) how tax abatements affect a government's future ability to raise resources and meet its financial obligations and (2) the impact those abatements have on a government's financial position and economic condition.”

Auditors opine not only on amounts but also on assertions related to disclosures. Auditors should use their professional judgment when evaluating a tax abatement disclosure misstatement or omission considering quantitative (such as the gross reduction in tax revenues that results from the agreement) and qualitative factors (such as identified in the preceding paragraph) related to the disclosure misstatements or omissions.

Auditors should document their evaluation and conclusions in their working papers.

Applicability to Non-GAAP Entities

Governments that prepare OCBOA financial statement (i.e. GAAP look-alike) will need to include the GASB 77 disclosures in their financial statements. Governments not *statutorily* required to prepare GAAP financial statements that prepare regulatory basis financial statements (i.e. AOS basis) will not need to include the GASB 77 disclosures in their financial statements but may include disclosures, if management chooses. However, governments *statutorily* required to prepare GAAP statements that choose to prepare regulatory financial statements instead, will need to make the GASB 77 disclosures in their notes to the financial statements.

Resources Available on the Auditor of State’s Website

The Auditor of State’s Office has a FAQ document related to GASB 77’s implementation available on our website at <http://www.ohioauditor.gov/references/gasb77.html>. This document will be updated as further information becomes available.

Questions

If you have any questions regarding the information presented in the Bulletin, please contact Local Government Services at the Auditor of State’s Office at (800) 345-2519. Questions from IPAs should be directed to the AOS Center for Audit Excellence at (800) 282-0370.