GFOA is …

Rethinking Financial Reporting

Agenda

- Why is GFOA rethinking financial reporting?
- Need for Speed
- Materiality
- Estimates
- Three Clocks

Ask questions at any time during the presentation!

Why Rethink Financial Reporting — Context

Pain Points

For users:

- **Elected officials** – high interest in audit outcome ("clean opinion"); lower interest in most ACFR content
- **Public** – low engagement; reports often too technical and late to be decision-useful.
- **Bond market** – information value decays with time; audit/report times have trended longer.

Pain Points

For government preparers

- Implementation/maintenance of standards (e.g., GASB 87/94/96) raise reporting workload.
- Capacity constraints (finance staff & audit firms) exacerbate delays.
- Time and money spent on reporting displaces higher-impact activities (analytics, direct public services, affordability, etc.).

THE SPEED WE NEED

Unlocking the Secrets of the Accelerated ACFR

Fundamental Principles

Modularization

- Parts of ACFR be done without numbers
- Can be done throughout the year

Continuous Flow

- Not batch processing
- Moving work along to the next step in smaller pieces

Visualization

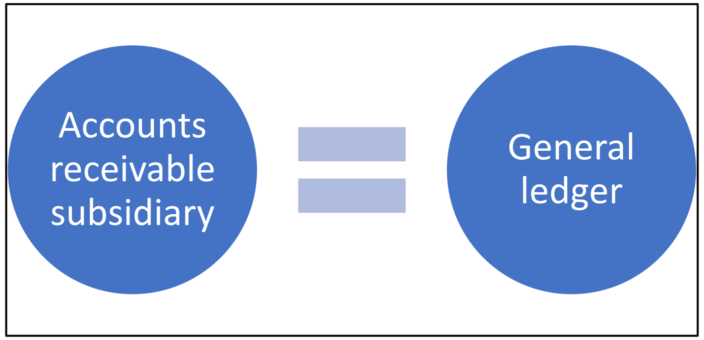
- Make process visible to all involved
- Identify hand-offs in the process

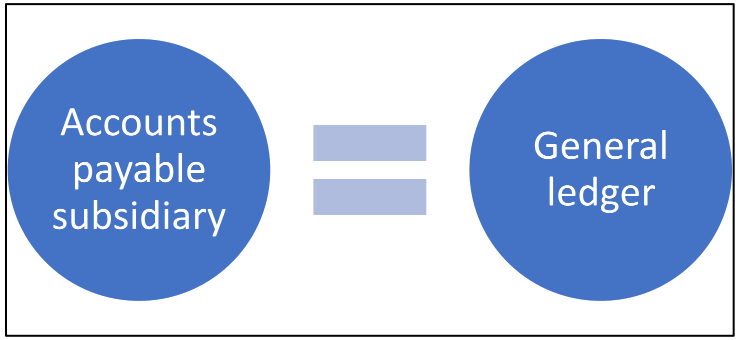
Standardization

- Reduces the amount of variation a task is subject to
- Develop standard operating procedure documents for ACFR production

Continuous Flow

- Reconciliations
  - Subledgers/modules
  - Balance sheet accounts
  - Property & sales tax workpapers
- Interim statement review
  - Budget vs. Actual





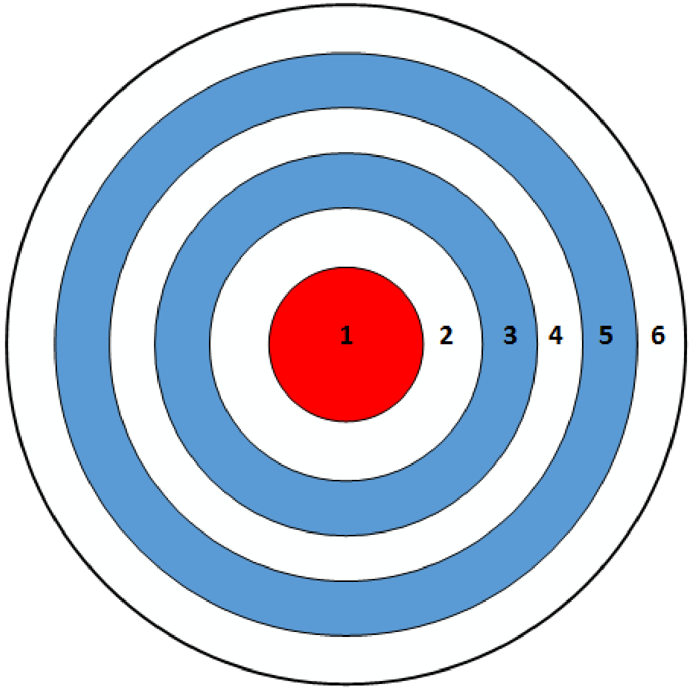
Bank Reconciliation

BALANCE PER BANK STATEMENT	3/31/20X1		$100,000
	Deposits in transit:		
		3/31/20X1	$25,000
	Outstanding Checks:		
		Check # 1234	(100)
		Check # 1235	(25)
		Check # 1236	(75)
		Check # 1237	(50)
		ADJUSTED BANK BALANCE	$124,750
BALANCE PER GENERAL LEDGER	3/31/20X1		$124,750
Deposits not recorded			$0
Checks/Electronic Transfers not Recorded			$0
		ADJUSTED LEDGER BALANCE	$124,750
		Variance	$0

Prepared by	Date	Reviewed by	Date

Standardization

- Standard operating procedures (SOPs)
  - Devote time to developing
  - Get comfortable with routines
- Error-proofing techniques
  - Checklists
  - Templates for tasks
  - Cross-checking numbers in ACFR
- Avoid Waste of Overproduction/Overprocessing
  - Estimates
  - Materiality



ACFR Preparation

- Identify the strategies to help accelerate ACFR prep
  - Where to start?
  - What are the highest leverage opportunities for your process?
- Lean process improvement
  - All processes include some form of waste
  - Identify waste and eliminating it

D.O.W.N.T.I.M.E.

- **Defects** - errors or mistakes that require rework
  - Where are the defects that cause rework?
- **Transportation** - unnecessary movement of materials between processes
  - Where are there too many back-and-forths?
- **Motion** - unnecessary movements by people
  - Where is info to perform non-routine tasks?

Materiality as a Process

What Really Counts

A Five Step Process for Rethinking Materiality

1. Identify the largest opportunities and screen for risks
2. Quantitatively evaluate the opportunities
3. Confirm that risks can be sufficiently mitigated
4. Consider the cumulative impact
5. Validate and communicate decisions

MATERIALITY AS A PROCESS
WHAT REALLY COUNTS

When applied thoughtfully, materiality helps focus effort on what matters to those who use the information. "Rethinking materiality" does not entail reducing accountability. It reduces low-value work so that finance officers can focus on what really matters.

START

1

FIND THE OPPORTUNITIES

Where is effort exceeding benefit?

Use professional intuition to find activities where detailed accounting may not meaningfully influence user decisions. This intuition will be tested as we go through the process.

Consider small leases, minor software agreements, minor accruals, or low-value/short lived capitalizable items, and compensated absences liabilities like jury duty.

BEFORE PROCEEDING, WHAT QUALITATIVE RISKS APPLY?

- Legislative & Regulatory requirements
- Political or public sensitivity
- Auditor scrutiny
- Control dependencies

ACFR Preparation

8 Forms of Waste

D.O.W.N.T.I.M.E.

Defects

Overproduction

Waiting

Non-utilized talent

Transportation

Inventory

Motion

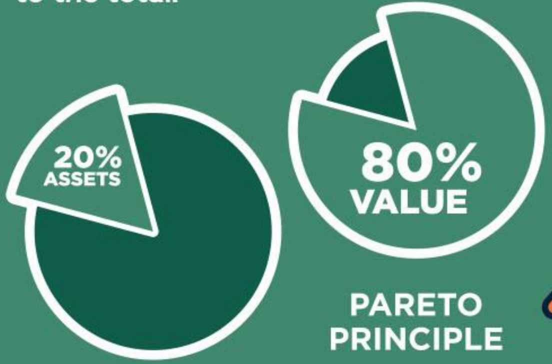
Extra processing


NO-GO
GO
2
QUANTITATIVELY EVALUATE THE OPPORTUNITIES
First, ask: is the entire activity immaterial? Should this activity be reported at all? Test whether excluding it meaningfully changes key ratios or indicators. If not it is a “no-go” for reporting.
If the activity is material it is a “go”, but reporting and precision thresholds could realize the opportunity for reducing detailed accounting work without reducing the decision usefulness of the data.
REPORTING THRESHOLD
What is included in the report? Determine a threshold below which items may be excluded without affecting decision-usefulness.
PRECISION THRESHOLD
How much measurement effort is warranted? Perhaps some smaller items can be estimated rather than measured precisely.

REPORTING THRESHOLDS DETERMINE INCLUSION

PRECISION THRESHOLDS DETERMINE EFFORT

Consider the concentration and shape of the data. The richest opportunities will usually be where a small number of items make up the vast majority of reported value and a large number of small items make a small collective contribution to the total.



PARETO PRINCIPLE

CONFIRM QUALITATIVE RISKS ARE MITIGATED

Revisit identified barriers and confirm that safeguards hold in practice.

3

- Verify consistency with governing regulations.
- Address politically sensitive topics through alternative transparency where appropriate.
- Engage auditors early to confirm reasonableness.
- Develop compensating controls if existing controls depend on prior treatment.

Quantitative decisions must remain defensible within qualitative constraints.

Precision vs Accuracy

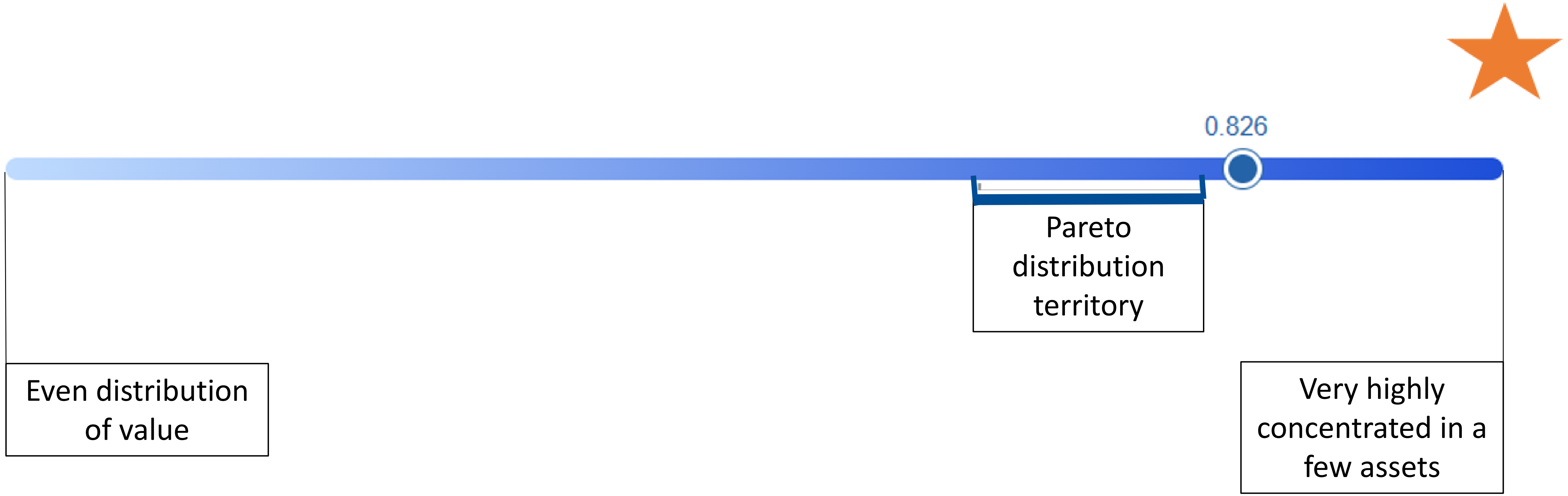
Precise

Fund Balance is: $34,539,932.16

Probably Just as Accurate (and maybe more)

Fund Balance is: $34.5 million

Many Govts are More Concentrated than 80/20



Multiple Thresholds Are Possible

Sweet Grass County, MT defined a tracking threshold separate from a depreciation threshold.

Asset	Tracking	Capitalize and Depreciate
Land	$1	Capitalize only
Land Improvements	$1	$100,000
Building and Improvements	$1	$100,000
Pioneer Medical Center Assets	$1	$5,000
Construction in Progress	$1	Capitalize only
Machinery and Equipment	$5,000	$75,000
Vehicles	$5,000	$50,000
Infrastructure	$5,000	$250,000
Any Federal Purchases	$1	$10,000

City of Bristol, CT

CAPITALIZATION THRESHOLD REVIEW							
	FY 2025				FY 2024		
	TOTAL FIXED ASSETS	ADDITIONS	# OF ITEMS		TOTAL FIXED ASSETS	ADDITIONS	# OF ITEMS
TOTAL	$834,119,532	84,611,515	272		$777,059,586	$112,185,913	257
<$20,000		929,092	95			912,074	90
% of total	0.11%	1.10%	34.9%		0.12%	0.81%	35.0%
<$25,000		1,183,437	106			1,362,804	111
% of total	0.14%	1.40%	39.0%		0.18%	1.21%	43.2%

City of Bristol, CT - Revised Capital Thresholds

	Old Threshold	New Threshold
Machinery, Equipment and Computer Software	$5,000	$10,000
Land Improvements	$5,000	$25,000
Buildings	$5,000	$50,000
Infrastructure	$5,000	$100,000

New thresholds will be effective with June 30, 2026, fiscal year

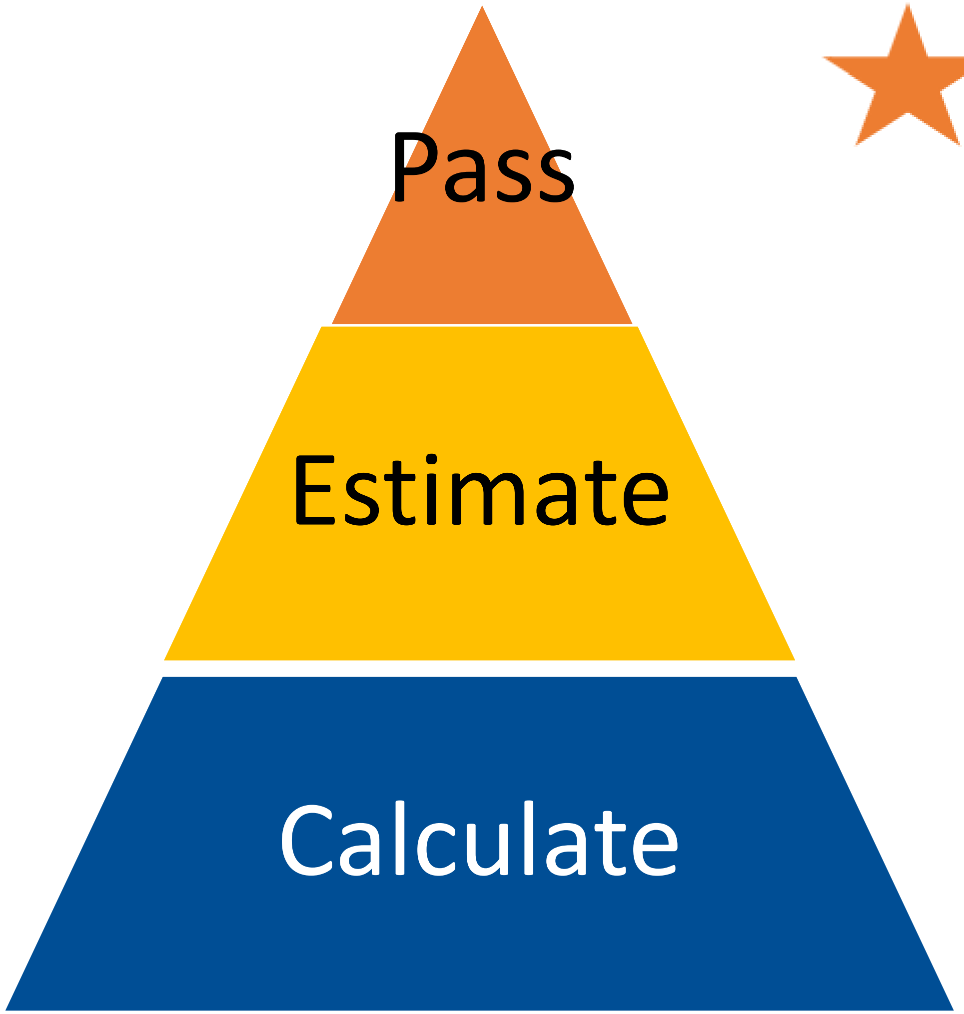
Estimated to save approximately 40-60 hours of staff time

Spend Resources Where it Matters

Some balances won’t impact decisions; they should be excluded.

Some balances need to be included, but they are small enough to tolerate error; estimate these.

Some balances are large enough getting the precise number is “worth” the effort, because a small percentage error will impact decisions.



CONSIDER CUMULATIVE IMPACT

4

Individually immaterial decisions should not accumulate into material distortion. The guidance in rethinking materiality is designed to avoid the risk of cumulative misstatement.

For example, the dual threshold system prevents us from cutting excessive amounts from the report. Estimates provide an alternative to excluding an activity or transactions from the report.

VALIDATE AND COMMUNICATE

5

Show that materiality judgments are well-founded, risk-aware, and subject to appropriate oversight — so they can withstand scrutiny and deliver durable value. Record thresholds and rationale.

Materiality is not a one-time determination. It is an ongoing discipline.


11:50 PM
PERIOD 12 — CLOSE TODAY
INVOICES
P-CARDS
UTILITIES
PAYROLL
SUPPLIERS
ANOTHER CUP OF DETERMINATION
$42.17
DETAILS MATTER.
$88.44
INVOICE
TOTAL DUE $42.17
INVOICE
TOTAL DUE $1,201.83
Just $0.01
INVOICE
TOTAL DUE
INVOICE
TOTAL DUE $58.44
Verify twice

Here's a suggestion that may sound subversive:

Rely MORE on estimates.

However...

Turns out, we already rely on estimates...

- Pension liability — an estimate
- OPEB liability — an estimate
- Other long-term measures — assumptions about uncertain future events (e.g., useful lives for capital assets, collectability of receivables, **fair value of investments**, contingent liabilities)
- We accept them because they're accurate enough to support a decision

City of Bristol – OPEB Trust Fund

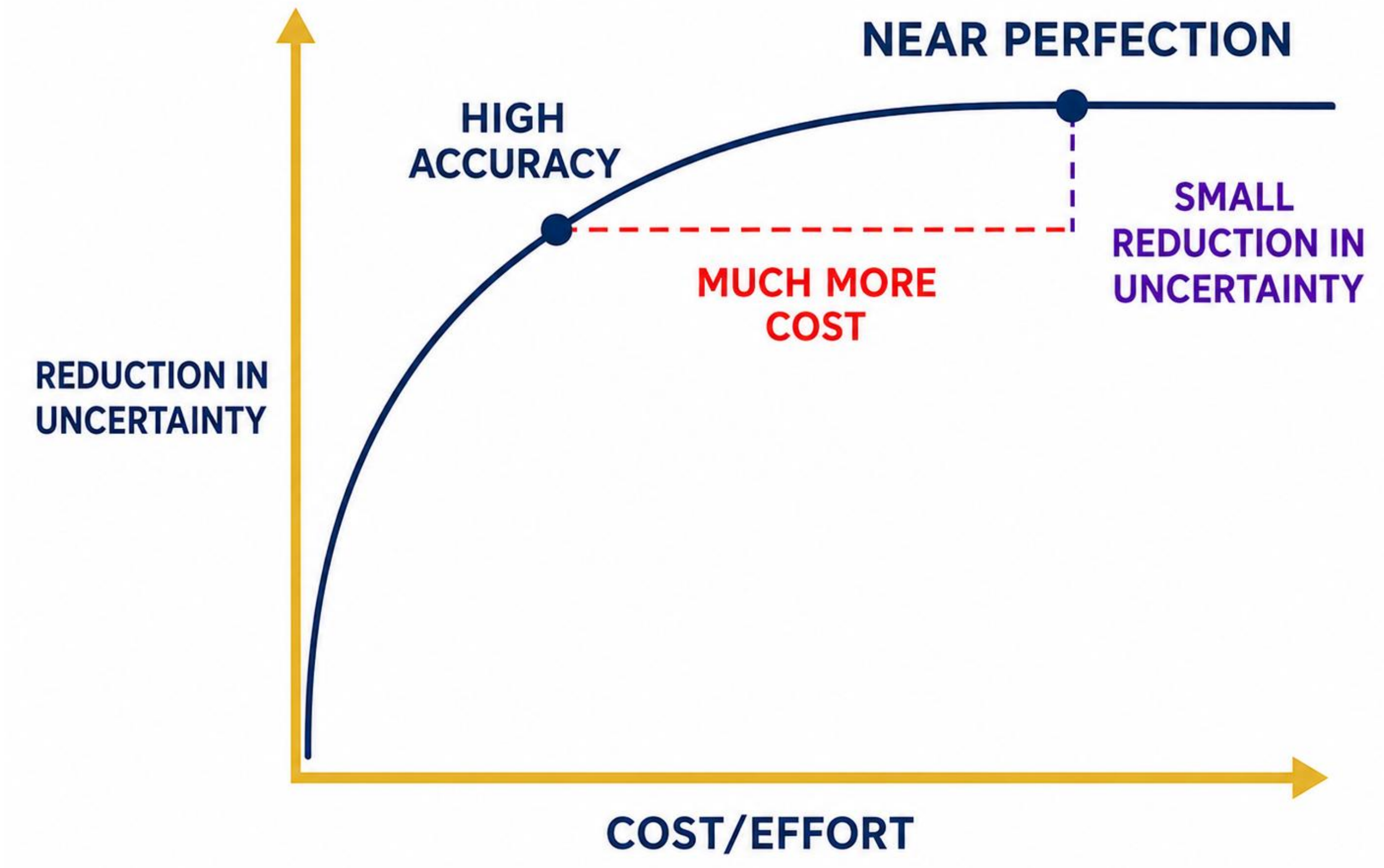
Asset	June 30, 2026 Market Value	%
Custodial Account (Equities/Bonds)	30,078,210	96.7%
Private Equity – Fixed Income	226,050	0.7%
Private Equity – Real Estate	685,285	2.2%
Private Equity – Global Credit*****	104,780	0.3%
Total	31,094,325	100.0%

Problem: Delays in receiving year-end financial statements from Private Equity delays completion of ACFR

Resolution: Based on materiality of investment - determine if estimates are feasible

Same issue with the City's $1 billion pension fund – this investment is < 0.5% of the total assets

Cost vs Uncertainty



The Model: The 80/20 rule and the effort curve

- Pareto / power-law: ~20% of causes drive ~80% of effects
- **Implication**: focus on small number of items that do most of the work, estimate the rest.
- The last ten percent can cost more than the first ninety

Does it hold up on a real ledger?

- Tested on a smaller city's recreation-department spending
- Easy-to-know items (payroll, benefits, utilities) accrued cheaply
- Focused on the messy accounts that would benefit from estimates
- The Pareto pattern showed up TWICE

The pattern, twice (across 3 years of data)

1. 27% of accounts drove 80% of annual cost — the predictable ones: payroll, benefits, etc.

2. Inside the accounts needing estimates: top 20% of invoices = 87% of dollars

Every one of those large invoices sat in ONE account of 23 (office and operating supplies)

An Illustration…

- Assume expenditures are known precisely for the first 11 periods
- Assume payroll, benefits, utilities, and other predictable items in period 12 can be measured with high precision at low cost
- Those items account for 97.8% of the true annual total
- Imagine we identify the largest period 12 invoices in the office and operating supplies account—the top 10% by dollar value.
- Even if we are only 80% effective in estimating those accrued expenditures, the annual total would be 99% accurate — before any attempt to estimate the remaining 90% of smaller invoices in the total.

**CLOCK 1:
ANNUAL CLOCK**

Running the Annual Clock at this stage helps ground upcoming budget decisions in current financial realities.

**CLOCK 2:
TRAJECTORY CLOCK**

Running the Trajectory Clock at this stage helps reveal whether current policies and spending patterns remain viable over future budget cycles.

**CLOCK 3:
GENERATIONAL CLOCK**

Running the Generational Clock at this stage helps ensure long-lived commitments are considered before setting priorities and making investments.

ARE WE MANAGING THIS YEAR WELL ?

WHERE IS THE MONEY GOING?

This speaks to whether the cost of government is worth it.

Example: Expenditure per capita
How much government spends per resident.

CAN WE AFFORD OUR COSTS?

This answers whether revenues are sufficient to cover costs.

Example: Revenues per capita
How much revenue the government generates per resident.

ARE WE HEADING IN THE RIGHT DIRECTION?

ARE WE BUILDING LONG-TERM STRENGTH OR ACCUMULATING LONG-TERM DEBTS?

This concerns assets and liabilities that effect value to taxpayers over the long-term.

Example: Change in net position
Shows overall financial position. Captures long-term debt, pension obligations, and more.

WHAT IS THE COMMUNITY'S FISCAL CAPACITY?

The government's financial condition depends on the health of its tax base.

Example: Resident Income
A community's income level supports public services through taxes and fees.

ARE WE MAINTAINING OUR RESERVE?

Reserves are the money local government has put aside to be prepared for a "rainy day". It shows the discipline to accumulate surpluses over many years.

Example: All-of-government fund balance
This is money set aside for the future.

CLOCK 3 GENERATIONAL CLOCK

WHAT ARE WE HANDING FORWARD?

ARE WE CREATING CONDITION THAT CAN BE SUSTAINED?

Costs like capital assets and employee pensions have generational impact. Getting these correct sets up future generations for success.

Example: Capital asset condition
Assets wear out. This shows about how much useful life remains.

CLOSE THE BOOKS
Financial reporting captures what happened and establishes a shared understanding of current financial condition. Reliable planning begins with reliable information.

RUN THE THREE CLOCKS
Before moving into planning and budgeting, use the data from financial reporting to assemble the Three Clocks.

BUILD A LONG-TERM FINANCIAL PLAN
Use insights from the clocks to project future conditions, test scenarios, and identify emerging risks and tradeoffs.

ALIGN STRATEGIC PRIORITIES
Connect financial capacity to organizational goals and desired outcomes.

DEVELOP THE CAPITAL PLAN
Translate priorities into investments and match commitments to long-term affordability.

ADOPT THE BUDGET
Make decisions about allocating resources for the coming year. The budget becomes the annual expression of longer-term priorities and financial stewardship.

REPEAT AND LEARN
Each budget cycle produces new information. Results are carried forward into the next review and planning cycle.

A Note About AI

- GFOA used Generative Artificial Intelligence (AI) tools, primarily ChatGPT4, to help develop the reports this presentation is based upon.
- GFOA acknowledges the limitations of AI-generated information, including potential biases and other limitations of generative artificial intelligence. All data, ideas, etc. from ChatGPT4 that were used in the report were independently verified/validated.

Trending **GFOA** Research

RETHINKING
FINANCIAL REPORTING