GASB-77
Tax Abatement Disclosures
What Every Taxpayer (and Government) Needs to Know

By: Eric S. Berman, MSA, CPA, CGMA

In 2014, the state of Nevada won a hard-fought bidding war among several states to locate a massive Tesla, Inc. "gigafactory." At the time, the *Reno Gazette-Journal* estimated the net cost of tax incentives to Nevada at $1.25 billion. The article also listed other tax incentives provided by various states, including $8.7 billion provided by the state of Washington to Boeing, $5.6 billion for Alcoa by New York and $1.25 billion provided by Mississippi to lure Nissan. Tesla CEO Elon Musk only sought $500 million to lure the company to Nevada, but the aforementioned bidding war ensued.

The package results in Tesla operating in Nevada essentially tax-free for 10 years. Sales taxes will be abated for 20 years, equaling about 80 percent of the total state sales tax the state receives annually. More than $300 million will be abated in property taxes over 10 years, well in excess of what is received annually by Storey and Washoe counties. [The industrial park where the plant is located straddles the county boundaries]. Approximately $195 million in other tax credits may be transferrable to other Nevada companies, reducing their tax liabilities to the state. Reductions in payroll taxes and electricity rates, a purchase of a private parkway, and an adjustment to various provisions of car sales regulations all sweetened the deal to lure Tesla.

What does Nevada get in return? A 5-million-square-foot factory generating $100 million in economic impact over 20 years, according to economic development officials — more than three percent of the state's gross domestic product and 20 percent of the region's economy. Because of the project, the state's workforce is estimated to increase two percent, and the region's is estimated to increase 11 percent. All told, the state's indirect tax revenue could reach as high as $1.9 billion over 20 years.

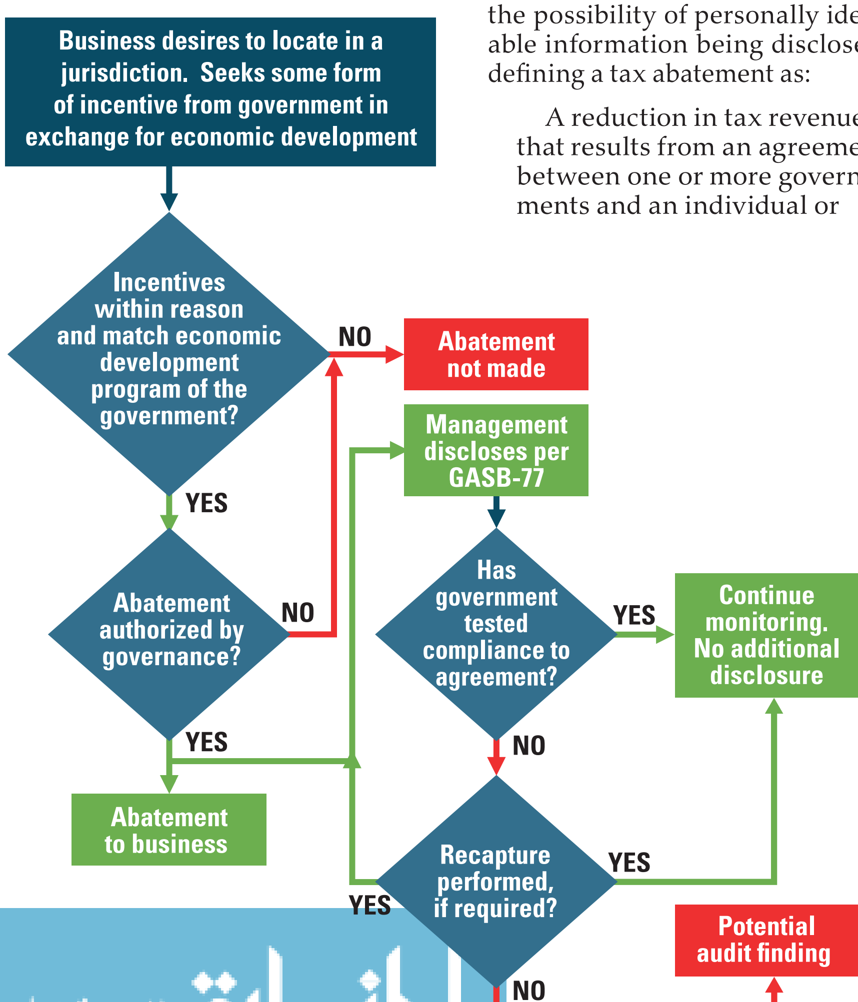
At the time, the state's economic development director remarked, "It will allow every underemployed person to reach full employment. It will lift up everyone in the region. Property values will go up. The prosperity of the region will be materially changed."[1]

The perspective on whether tax incentive programs are good policy is as varied as decision makers. After all, the amount of the tax abatements

The perspective on whether tax incentive programs are good policy is as varied as decision makers.

alternatively could have been used for current purposes such as better schools or infrastructure. By the time of this publication, batteries for Tesla cars and other products are expected to be produced at the factory. In exchange for the tax breaks, 6,500 positions are expected to be created. According to a recent *Bloomberg* report, 2,900 people already work at the facility, with more than 4,000 jobs (including temporary construction work) to be added this year due to Tesla's partnership with Panasonic.[2]

Figure 1. Operating Decisions in Implementing GASB-77



GASB-77 Disclosure

Governmental Accounting Standards Advisory Board (GASB) stakeholders have long asked for better disclosure of information about tax abatements. Private citizens, taxpayer groups, municipal bond analysts and other users of governmental financial reports have recognized the importance of this information for many years. However, the disclosure requirements needed to be crafted in such a way that abatements for senior citizens, veterans, those with disabilities, charities and others would not be disclosed. The board developed a narrow focus for disclosure, alleviating the possibility of personally identifiable information being disclosed by defining a tax abatement as:

> 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 promises 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 further stipulates that a transaction's substance, not its form or title, is key to determining whether a transaction meets the definition of a tax abatement in accordance with GASB-77.

A tax abatement agreement is sometimes difficult to understand. Often, to determine the disclosure structure, a flowchart may be helpful with various aspects of the agreement, as shown in **Figure 1**.

Five basic disclosure principles are included in GASB-77:

- Disclosures should distinguish between tax abatements resulting from (1) agreements that are entered into by the reporting government and (2) agreements that are entered into by other governments and that reduce the reporting government's tax revenues.
- Disclosures may be provided individually or aggregated.
- Disclosures by the reporting government should be organized by each major tax abatement program, such as economic development or a television and film production incentive.

- Disclosure information of abatements relating to agreements by other governments should be organized by the government that entered into the tax abatement agreement and the specific tax being abated.
- Disclosure should commence in the period in which a tax abatement agreement is entered into and continue until the tax abatement agreement expires.

A quantitative threshold may be set by the reporting government to a streamlined disclosure. For example, a government may choose to set up a threshold similarly to its capitalization threshold and only disclose tax abatements above that amount, as long as the provisions of GASB-77 are met.

The nature of the disclosures is dependent upon whether the reporting government is providing the abatement or is being forced to abate due to an agreement made by another government. In the Tesla example, Nevada will have different disclosures than Storey and Washoe counties, or other governments affected by the abatement. Abatement disclosure by the government entering into the agreement and other parties to the abatement are shown in **Figure 2**.

If a discretely presented component unit abates taxes that reduce the government's tax revenues, disclosure by the primary government should only be made if the primary government concludes such disclosure is essential to fair presentation. Otherwise, the reduced information (see right column of Figure 2) is presented.

Figure 2. Abatement Disclosures

GASB-77 Provision	Government entering into abatement	Other government enters into abatement, reducing reporting government's tax revenues
Brief descriptive information, including:		
• names and purposes of tax abatement programs	✓	✓
• specific taxes being abated	✓	
• authority under which tax abatement agreements are entered into	✓	
• criteria that make a recipient eligible to receive a tax abatement	✓	
• mechanism by which taxes are abated including reduction of assessed value or specific dollar amount of taxes owed	✓	
• types of commitments made by the recipients o f tax abatements	✓	
Gross dollar amount on an accrual basis of the tax revenue reduction during the period as a result of tax abatement agreements	✓	✓
If amounts are received or receivable from other governments associated with the foregone tax revenue, the names of the governments, the authority under which amounts were or will be paid, and the dollar amount received or receivable from other governments	✓	✓
If the government made commitments as part of the abatement, the types of commitments made and the most significant individual commitments made	✓	
If disclosure is by individual agreement, the threshold used to disclose individually	✓	✓
If legal provisions prohibit disclosure, a description of the general nature of the information and specific source of the legal prohibition	✓	✓

Best Practices in Implementing GASB-77

For most governments, disclosure of this information may be more challenging than some other GASB standards, as the information necessary for this disclosure may be kept by departments or agencies not normally part of the financial reporting process. Multiple-level agreements may also be difficult due to the coordination needed between governments for information. For example, Nevada may need to give information to Washoe County for proper disclosure on a timely basis regarding the Tesla abatements.

Governments that have tax abatement programs may want to survey departments or agencies about the existence of abatements. For departments or agencies that have abatements in place or in the process of agreement, the focus may be narrowed. Information-sharing mechanisms may be needed to transfer information required by GASB-77 from those governments issuing the abatement to those governments required to abate to allow for symmetrical reporting. Once the information is gathered, a lifecycle chart similar to Figure 1 can document the agreement and compliance requirements.

Commitment reporting and monitoring may face additional scrutiny by auditors. For commitments made by governments to recipients of tax abatements, whether the commitment has been fulfilled in accordance with the agreement becomes key. As an example, part of the agreement with Tesla was to acquire a parkway, and extend it to a highway near the plant for better access. If the state did not acquire the parkway or extend it, the commitment agreement would not be fulfilled, which may be material. Of course, not fulfilling the commitment may cause a legal action by Tesla, in this example.

The more common activity may be monitoring compliance with the terms and conditions of the agreement. The New York City comptroller recently reported that its Department of

Finance gave $10 million in property tax abatements to corporations. The abatements went to corporate-owned condominiums, parking spaces and gardens from 2013–2016 because the city's Department of Finance failed to conduct basic document checks aligning the provisions of the abatements to city ordinances, according to the comptroller.[3] The abatements were intended for individual homeowners in cooperatives and condominiums rather than corporate-owned properties, so the city violated a 2013 amendment to its tax abatement laws.

A larger-scale example was the result of an audit performed by the Texas state auditor in 2014 gauging compliance with the Texas Economic Development Act, which encouraged capital investment and job creation by businesses that have property tax appraisal limitation agreements with school districts (thereby abating taxes). The audit report found that, from 2005–2013, an estimated $905.2 million in property tax revenue was lost because of such agreements. Of the school districts surveyed by the state auditor, reliance was primarily based on annual certifications by the businesses receiving the abatement to confirm capital investments and job creation. The state statute did not require the comptroller's office or the Texas Education Agency to verify that information, and the audited school districts only certified that information provided is true and correct. In essence, the taxes were abated without verifying compliance, or in some cases, conflicts of interest. The state comptroller's office agreed with the audit report recommendations, but the school districts disagreed with certain findings and recommendations addressed to them.[4] The act requires school districts to submit information to the comptroller's office and the state education agency as a basis for additional state aid paid to the school districts for (1) property tax revenue losses associated with such agreements, and (2) tax credits associated with the agreements.

Whether the abatement of taxation is truly lost revenue can be viewed shrewdly as a risk/reward scenario, as illustrated in the example in which California, Texas, New Mexico, Oregon, Washington and Arizona competed with Nevada for Tesla's business with similar incentives. The decision then becomes a balance of opportunity cost framed by public policy. According to a definitive history of the transaction published in Fortune magazine, California was eliminated due to executional risk in their environmental laws, even though Tesla's headquarters are in California.[5]

Conclusion

For many stakeholders, the new disclosure afforded by GASB-77 provides welcome "sunshine" to some potentially opaque practices of state and local governments. Since GASB-77's release, there have been many articles and news reports on the levels of tax abatements provided by governments nationally. The impact of the new disclosure may not be fully realized until GASB-77 is fully implemented this year.

GASB-77 is by no means ideal disclosure for every potential stakeholder seeking this information. Many governments have already started to publish lists of all agreements on the government-sponsored websites; however, governments should be careful not to disclose personally identifiable information related to those agreements, as stakeholders reading the list online may get lost in the data without understanding the information. Therefore, GASB-77 presents a balance between such data and valuable information. J

Endnotes

1. Damon, Anjeanette, "Inside Nevada's $1.25 billion Tesla tax deal." Reno Gazette-Journal, Sept. 4, 2014; accessed April 14, 2017. www.rgj.com/story/news/2014/09/04/nevada-strikes-billion-tax-break-deal-tesla/15096777/
2. Randall, Tom, "Tesla Flips the Switch on the Gigafactory." Bloomberg Technology, Jan. 4, 2017; accessed April 14, 2017. www.bloomberg.com/news/articles/2017-01-04/tesla-flips-the-switch-on-the-gigafactory
3. Press release from Scott M. Stringer, New York City Comptroller, Jan. 28, 2016; accessed April 14, 2017. comptroller.nyc.gov/newsroom/comptroller-stringer-audit-department-of-finance-mistakenly-gave-away-10-million-in-property-tax-abatements-to-corporations/
4. State Auditor's Office of Texas, John Keel, CPA, State Auditor, "An Audit Report on Selected Major Agreements Under the Texas Economic Development Act," November 2014, Report No. 15-009; accessed April 14, 2017. https://www.sao.texas.gov/reports/main/15-009.pdf
5. Elkind, Peter, "Inside Elon Musk's $1.4 Billion Score." Fortune Magazine, Nov. 14, 2014; accessed April 14, 2017. http://fortune.com/inside-elon-musks-billion-dollar-gigafactory/

Eric S. Berman, MSA, CPA, CGMA, a partner with Eide Bailly LLP, has 26 years of governmental accounting and auditing experience, including as deputy comptroller for the Commonwealth of Massachusetts and chief financial officer of the Massachusetts Water Pollution Abatement Trust. Berman serves as chair of AGA's Audit Committee and as the Boston Chapter president; and he recently represented AGA as vice chair of the Government Accounting Standards Advisory Council to GASB, and as chair of the Financial Management Standards Board. He was recently named to GASB's Financial Reporting Model task force.