The Importance of Timely Government Financial Reporting

By Robert H. Attmore, CGFM, CPA

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From my vantage point at the organization that establishes generally accepted accounting principles for state and local governments, I cannot overstate how important it is for all governmental entities to prepare their annual financial reports in as timely a manner as possible. Having made that point, I understand that setting priorities and allocating limited resources is appropriately the responsibility of government policy-makers. Accountability professionals, however, can provide important information regarding the costs and benefits of timely financial reporting to help support policy-makers' decisions.

By preparing timely financial reports, governments allow interested citizens, taxpayers and other constituents to access decision-useful information that can be used to make a range of important decisions regarding housing, schools, voting and the services they receive in return for their tax dollars.

Although policy-makers may not think about it in these terms, governments that do not issue financial reports in a timely fashion, in effect, hinder the ability of those who live and work in their communities to make informed decisions about any number of issues related to the government's finances. Users of their financial reports are left to extrapolate from aging data and educated guesses. In doing so, these governments can diminish public confidence and trust, and may even cause residents and taxpayers to be subjected to higher borrowing costs and higher related debt service payments.

Merritt Research Services examined the length of time it takes municipal governments to issue their annual reports. Its 2010 report stated, "By the time many annual governmental audits are received, many capital markets analysts and investors believe they have lost significant value for assessing the current financial position of [an issuer]."

Merritt's analysis of 14,000 audits on more than 4,600 municipal bond-issuing entities, spanning the period 2007 to 2009, found that the average time it takes an audited annual financial report to be completed is roughly five months after the close of the fiscal year. The final approval of the report and its ultimate release to the public often takes an additional month or more, according to the report.

A March 2011 Governmental Accounting Standards Board (GASB) research brief examining timeliness of financial reporting by state and local governments during the 2006 to 2008 period outlined similar findings. The passage of time significantly impacts the perceived usefulness of reported financial information by financial report users. The GASB study found that 73 percent of larger governments and about 46 percent of smaller governments included in the study issued their annual financial reports within six months after the close of the fiscal year. While respondents to the GASB user research survey considered information made available in that timeframe to be useful (the mid-point on the survey Likert scale), they considered it markedly less useful than information received within 45 days to three months after the fiscal year-end.

To bring the issue into sharper focus, fewer than 9 percent of respondents to the GASB survey considered annual financial information received six months after year-end to be very useful (the top point on the survey Likert scale), and less than 2 percent considered information received a year or more later to be very useful.

Encouraging Timely Financial Reporting

GASB's mission is to establish and improve generally accepted accounting principles, which underlie the fair presentation of state and local governmental entities' financial statements. The timing of the release of a financial statement does not affect its fair presentation. That said, GASB certainly encourages timeliness, which is one of the six qualitative characteristics of financial information set forth in its conceptual framework.

Publicly traded companies are required under federal securities laws to submit annual financial reports that provide a comprehensive overview of the company's business, financial condition and audited financial statements within 75 or 90 days of the close of the fiscal year. State and local governments have no similar requirement under federal law regarding the preparation of their annual financial reports. With the exception of bond covenants and certain state-imposed regulatory or statutory requirements, there are generally no requirements relating to when a state or local government must complete and make available its financial report.

Municipal financial analysts deciding whether to buy a government's bonds, city council members allocating limited resources in the budget, or taxpayer associations assessing the efficiency and effectiveness with which a government has used its tax revenues are greatly challenged to do so with financial information that, in some cases, can be more than nine months old.

A 2011 report issued by the U.S. Government Accountability Office found that untimely government financial reports "may require analysts to rely on outdated information or to try to obtain additional, unaudited information from issuers."

Accounting and financial reporting standards are intended to result in financial reporting that produces reliable and relevant decision-useful information. An essential element of financial reporting is that it communicates information in time to be used to inform decisions and to hold government officials accountable.

How might timely financial reporting benefit residents, taxpayers and constituents in general? All these users of annual financial reports benefit by getting the information they need in time to make important decisions, such as whether to buy a house in a particular school district, how to vote on a bond or budget referendum, and what kind of return in terms of services they get for their tax dollars.

Because investors in the municipal securities market do not enjoy the same timeliness in reporting requirements that their counterparts investing in public company bonds do, there is growing concern and discussion on this issue among investor groups, regulators at the Securities and Exchange Commission and the Municipal Securities Rulemaking Board, and financial analysts. Some question whether investors in the municipal securities market are, in effect, second-class citizens when compared with investors in publicly traded companies, who have the benefit of basing their investment decisions on far more current information. Issuing timely government financial reports has the effect of leveling the playing field for investors in the municipal securities market.

What Is Considered Timely?

When GASB interviewed more than 250 government financial statement users as part of a research project a few years ago, one of the concluding questions was, "What issues would you like to bring to the GASB's attention?" Invariably, the answer addressed a need for more timely financial reports. This desire was expressed particularly by municipal bond analysts in credit rating agencies, mutual funds and casualty insurance companies. The implication seems to be that providing information more quickly to bond market participants could improve a government's appearance of creditworthiness and potentially lower its borrowing costs.

Given the state of the art in government financial reporting, few would disagree that annual financial statements prepared in conformity with GAAP within three to six months of the close of the fiscal year are timely.

In recent years, federal government departments have been required to complete and make available their financial reports 45 days after the close of the fiscal year, and the government-wide consolidated financial report of the United States is due in 75 days. As required by state law, the state of New York and the city of New York routinely issue audited financial statements within four months of their year-ends. For a few years, Michigan has completed its audited financial statements within three months of its year-end. There is no question that it can be done—the only question is whether state and local government policy-makers will consider the benefits sufficient to warrant making timely financial reporting a priority.

Thousands of governments have already done just that. To qualify for consideration for the Government Finance Officers Association's (GFOA) Certificate of Achievement for Excellence in Financial Reporting, governments must issue their reports within six months of the close of their fiscal year. Approximately 3,500 governments receive the GFOA certificate each year. This program is a bright spot in its encouragement of timely financial reporting. But what about the remaining 85,000 government entities in the United States?

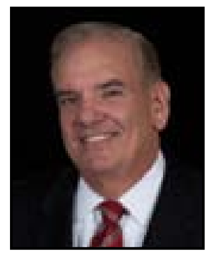
Some of these governments issue their financial reports in a timely way but simply do not participate in the GFOA's certificate program. Nevertheless, thousands of governments do not issue their financial reports within six months; some take significantly longer. The point is that nearly all of these governments could report more quickly if their policy-makers decide it is a priority. It is acknowledged that, in many of these cases, issuing financial reports sooner may require a greater degree of reliance on the use of reasonable estimates and may require financial reporting component units to comply with shorter reporting deadlines.

Final Thoughts

I am often asked how governments can be asked to produce their annual financial reports in a more timely way considering the current environment of across-the-board budget cuts, reductions in staffing resources and new accounting standards.

The answer is that it is not easy, but if policy-makers make this issue a priority, presumably adequate resources would be allocated to accomplish the desired outcome. It is my belief that the benefits to governments in terms of enhanced accountability and increased confidence in government officials are real and significant. At the same time, the benefits to citizens and taxpayers who live and work in communities are undeniable in terms of their ability to make informed decisions. They are more likely to favorably view the stewardship of government officials who report to them while the information is still relevant and meaningful for decision-making.

In summary, timely financial reporting indicates responsiveness to the public's concerns and demonstrates managerial capability. In a larger sense, producing timely, reliable financial reports helps to build trust and confidence in government. Conversely, delayed reporting reduces the relevance and usefulness of the information reported and tends to erode the trust of constituents. In a representative democracy, trust is an important commodity for policy-makers to pursue. Its benefits are tangible. ■



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