Objective

To accurately report liabilities in the Comprehensive Annual Financial Report (CAFR) in accordance with Generally Accepted Accounting Principles (GAAP).

Policy

Annually, state agencies must report liability information to Minnesota Management & Budget (MMB) Financial Reporting for inclusion in the CAFR. These liabilities can only include transactions not already recorded in the accounting system as liabilities to avoid double counting. Payments made in the accounting system during the July through mid-August close period that are coded to the prior accounting year are automatically included in the CAFR and should not be separately reported to MMB Financial Reporting.

Liabilities include amounts arising from exchange, exchange-like, and nonexchange transactions as defined by GASB Statement No. 33 “Accounting and Financial Reporting for Nonexchange Transactions.” Long-term liabilities are defined by GASB Interpretation No. 6 “Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.”

Financial Reporting Structure of the State of Minnesota

The basic financial statements of the CAFR include government-wide and fund financial statements. The government-wide financial statements report on the state as a whole, while the fund financial statements emphasize major individual funds and fund types.

The focus of the government-wide statements is on financial information of the state as an entity and the change in the overall financial position of the state as a result of the activities of the fiscal year. Government-wide, proprietary, and fiduciary fund financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Under the economic resources measurement focus, all economic resources and obligations of the reporting government, both current and long-term, are reported in the statements. Under the accrual basis of accounting, revenues, expenses, gains, losses, assets, and liabilities resulting from exchange and exchange-like transactions are recognized when the exchange takes place.

The focus of all governmental funds is the current financial resources measurement and use the modified accrual basis of accounting. With this measurement focus, only current assets and current liabilities are included on the balance sheet. Governmental fund operating statements present increases (revenues and other financing sources) and decreases (expenditures and other financing uses) to fund balances.
Recognition of Liability and Related Expenses/Expenditures

Expenses are generally recognized in the government-wide, proprietary and fiduciary funds as soon as the related liability is incurred, regardless of the timing of the related cashflow. However, for governmental funds, expenditures and related liabilities are recognized when fund obligations are incurred, except for certain specific long-term liabilities, which are recorded when due and expected to be liquidated with available financial resources. These liabilities are not reported in governmental funds, but are reported as general long-term liabilities in the governmental activities column of the government-wide financial statement reporting only and include:

- Unmatured principal of long-term debt, such as bonds, loans, certificate of participation and capital leases.
- Accrued interest on long-term debt.
- Liabilities related to compensated absences, claims and judgments, special termination benefits, and landfill closure and postclosure costs when not payable from current financial resources.
- Pension and other postemployment benefits (OPEB).

These specific long-term liabilities are recorded as liabilities in the government-wide financial statements, rather than as an “other financing source.” Amounts paid to reduce long-term indebtedness of the reporting government are reported as a reduction of the related liabilities, rather than as expenditures.

In addition to the financial statements, the CAFR provides further information regarding liabilities in the Notes to the Financial Statements.

Liabilities for Activities Tracked in the Accounting System

Accounts Payable

Accounts payable is a promise to pay a supplier for assets purchased or services rendered. In other words, this is an amount payable by the state to individuals, governmental units and other entities. Agencies should report accounts payable to MMB Financial Reporting if the amount is greater than or equal to $100,000, if the payment is not posted to the current accounting fiscal year in the statewide accounting system, or the payment was not made by the close of the fiscal year. Other accounts payables reported in accordance with GAAP include goods and services and grants payments.

GASB Statement No. 33 “Accounting and Financial Reporting for Non-exchange Transactions” defines the classes of non-exchange transactions. Government-mandated non-exchange transactions are when a government at one level provides resources to a different level of government to use for specific purposes. Voluntary non-exchange transactions can result from a legislative or contractual agreement, other than exchanges, entered into willingly by the parties to the agreement. Purpose restrictions specify the purpose for which resources are required to be used, and should not affect when a non-exchange transaction is recognized. Governments receiving these resources should report the resulting net assets, equity or fund balance as restricted.

The state is obligated to recognize a liability for goods and service received on or before June 30th. The liability amount is the total amount of goods and services received on or before June 30th. A liability for an exchange amount transaction is recognized when the state receives goods and services in exchange for a promise to provide money or other resources in the future. Probable and measurable amounts that remain unpaid as of June 30th should be recognized as liabilities. Agencies may have to estimate unpaid liabilities.
The state recognizes a grants payment liability once the grantee has met all of the necessary eligibility requirements. For most grant programs, the final eligibility requirement is that the grantee must incur costs that are eligible for reimbursement. For these reimbursement-type grants, if the grantee has incurred costs or made payments that are eligible for reimbursement on or before June 30, the state has a liability on June 30. It may be necessary to estimate the liability amounts if the state has not yet received the grantee reimbursement requests.

When a state agency is the provider in a government-mandated nonexchange or voluntary nonexchange transaction, the agency should recognize a liability as soon as the recipient meets all eligibility requirements. When a state agency is the recipient in either a government-mandated nonexchange or voluntary nonexchange transaction, it is possible that, as a result of failing to continue to comply with eligibility requirements or purpose restrictions, the agency is no longer entitled to resources that have already been recognized in the financial statements. In this case, the agency should recognize an expense and a liability for the amount of resources that the provider is expected to reclaim or cancel. If the agency is no longer entitled to resources that have been received but not recognized in the financial statements, the agency should recognize a revenue reduction for the amount expected to be repaid.

**Retainage Payable**

Retainage payable represents a portion of the agreed upon contract price deliberately withheld until the work is substantially complete to assure that contractor or subcontractor will satisfy its obligations and complete a construction project. Agencies should report withheld, unpaid retainage liabilities to MMB Financial Reporting if it is greater than $500,000 and the agency has not already reported it to MMB Financial Reporting as an encumbrance liability.

**Long-Term Liabilities Not Tracked in Accounting System**

GAAP requires the presentation of changes in long-term debt be presented by type of debt. The changes (increases and decreases) and current/noncurrent amounts must be presented separately for all the following long-term liabilities.

According to GASB Statement No. 38 “Certain Financial Statement Note Disclosures” governments should disclose the following details of debt service requirements to maturity:

1. Principle and interest requirements to maturity, presented separately, for each of the five subsequent fiscal years and in five-year increments thereafter.
2. Interest requirements for variable-rate debt should be determined using the rate in effect at the financial statement date.
3. The terms by which interest rates change for variable-rate debt.

In addition, GASB Statement No. 88 “Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements” requires the following to be disclosed:

1. Amount of unused lines of credit
2. Assets pledged as collateral for debt
3. Terms specified in debt agreements related to events of default with finance-related consequences, termination events with finance-related consequences, and subjective acceleration clauses.
General Obligation Bonds

General Obligation bonds are statewide bond issues that are secured by an unconditional pledge of the full faith and credit and taxing power of the state. The proceeds from the sale of general obligation bonds are used to pay the cost of building the capital projects that are approved by the Legislature. Certain tax-exempt bonds must receive an allocation from the state prior to the issuance. Minnesota Constitution Article XI, Section 5, states the requirement for incurring public debt (general obligation bonds).

Revenue Bonds

To authorize the issuance of revenue bonds, legislative action needs to occur. These bond issues do not involve a pledge of the full faith and credit of the state, but are backed by revenue. For example, Minnesota State Colleges and Universities (MnSCU) (enterprise fund) issues revenue bonds and the proceeds are used to finance the acquisition, construction, and remodeling of buildings for dormitory, residence hall, parking ramps, student union, and food service purposes at state universities. The bonds are payable solely from, and collateralized by, an irrevocable pledge of revenues to be derived from the operation of the financed buildings and from student fees.

State General Fund Appropriation Bonds

These bonds are payable each fiscal year only from amounts appropriated by the legislature of the state and according to the terms of an order of the Commissioner of MMB for the payment of the bonds. No other revenues or assets of the state are pledged for the payment of the principal of or interest on the bonds. The bonds are not public debt of the state for which the state has pledged its full faith, credit, and taxing powers.

Loans

These loans are agreements entered into by a state agency with principal and interest payments spanning over more than one year. An example is loans related to local governments’ financing projects to be completed earlier than the Minnesota Department of Transportation’s (MnDOT) scheduled completion date. MnDOT repays the local units of government at a future date.

Certificates of Participation

Certificates of participation (COPs) are used to finance the acquisition and development of computer software. The COPs are not general or moral obligations of the state and no revenues are pledged to repay them. If the state defaults on the debt, the trustee has the right to terminate the lease terms of either or both projects and to take whatever legal action may appear necessary to collect rental payment(s).

Capital Leases

Capital leases meet the criteria of a capital lease as defined by GASB Statement No. 62 “Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements” which defines a capital lease as one that meets one of the following criteria:

- Transfer of ownership.
- Bargain purchase option.
- Lease term is greater than or equal to 75 percent of the life of the asset.
• Present value of the minimum lease payments is greater than or equal to 90 percent of the asset value.

Claims and Judgments

A claim is a loss that is recognized as a liability in the period in which the underlying event occurs. Often it is not immediately clear whether a particular underlying event will result in a loss. At other times, it may be clear that a loss has occurred, but it may not be possible to reasonably estimate the amount. It is only at the point where 1) it is considered probable that a loss has occurred and 2) the amount of the loss can be reasonably estimated, that a liability should be recognized.

A judgment is a decision by a court that describes the rights and obligations of both parties in a lawsuit.

Examples of claims recognized by the state:

Medical Reserves Liability

The state reports medical reserves liability and the remaining claim amount for reimbursement of supplementary and second injury benefits for workers’ compensation injuries.

The medical reserves liability consists of claims of employees of uninsured and bankrupt firms. These claims are funded by an assessment on insurers and are payable from the Special Compensation Fund (a special revenue fund).

The program for claims for reimbursements of supplementary and second injury benefits for workers’ compensation injuries was ended by legislative action. The claim amount represents the estimated discounted (5 percent) cost of supplementary benefits for injuries prior to October 1, 1995, and second injury program benefits for injuries prior to July 1, 1992.

Pollution Remediation Obligation

GASB Statement No. 49 “Accounting and Financial Reporting for Pollution Remediation Obligations” requires the state to report its liability for pollution remediation costs.

A liability for pollution remediation must be accrued when the state knows or reasonably believes that a site is polluted, and one or more of the following obligating events has occurred:

- The government is compelled to take remediation action because pollution creates an imminent endangerment to public health or welfare or the environment, leaving it little or no discretion to avoid remediation action.
- The government is in violation of a pollution prevention-related permit or license.
- The government is named, or evidence indicates that it will be named, by a regulator as a responsible party or potentially responsible party for remediation, or as a government responsible for sharing costs.
- The government is named, or evidence indicates that it will be named, in a lawsuit to compel the government to participate in remediation.
- The government commences, or legally obligates itself to commence, cleanup activities or monitoring or operation and maintenance of the remediation effort. If these activities are voluntarily commenced and none of the other obligating events have occurred relative to the entire site, the amount recognized should be based on the portion of the remediation project that the government has initiated and is legally required to complete.
All potential liabilities must be estimated using a weighted average percentage calculation. Each site should be estimated individually, using current costs of technology expected to be used in the cleanup. Only sites with original estimated liabilities exceeding $500,000 need to be reported. The entire estimated cost of cleanup should be reported, regardless of the proposed time frame for the remediation.

Estimates of pollution remediation liability should be adjusted when benchmarks are met or when new information indicates changes in estimated outlays due to, for example, changes in the remediation plan or operating conditions (e.g. changes in legal or regulatory requirements). Refer to paragraph 13 of GASB 49 for definitions of each benchmark and to paragraph 18 for examples of changes which trigger re-measurement.

State Employees Workers' Compensation Liability

The state reports the liabilities for workers’ compensation based on claims filed for injuries to state employees occurring prior to the reported fiscal year. The liability will be liquidated using future resources at unspecified times.

Termination Benefits

These are benefits which are provided by employers to employees as an inducement to hasten the termination of services or as a result of a voluntary early termination or as a consequence of the involuntary termination of services. Termination benefits include early-retirement incentives, severance benefits, and other termination-related benefits. They do not include unemployment compensation or postemployment benefits that are part of the compensation offered in exchange for services received.

GASB Statement No. 47 “Accounting for Termination Benefits” establishes that a liability and expense is recognized for voluntary termination benefits (for example, early-retirement incentives) when the offer is accepted and the amount can be estimated. A liability and expense for involuntary termination benefits (for example, severance benefits) should be recognized when a plan of termination has been approved by those with the authority to commit the state to the plan, the plan has been communicated to the employees, and the amount can be estimated.

This Statement requires employers to disclose a description of the termination benefit arrangement, the cost of the termination benefits (required in the period in which the employer becomes obligated if that information is not otherwise identifiable from information displayed on the face of the financial statements), and significant methods and assumptions used to determine termination benefit liabilities.

Landfill Closure and Post-closure Liability

The state has assumed responsibility for the long-term care of certain closed municipal solid waste facilities and reporting requirements are defined in GASB Statement No. 18 “Accounting for Municipal Solid Waste Landfill Closure and Postclosure Care Costs.”

Minnesota Statutes Section 115B.39 established the landfill cleanup program to provide environmental response to qualified, state-permitted, closed landfills. The state is responsible, in perpetuity, for performing cleanup and final closure work, as well as all post-closure maintenance and monitoring, at qualifying sites.

Estimated landfill closure and post-closure liabilities include planned response actions, future unknown additional remedies which have some probability of occurring, future replacement of some remedial
systems, and administrative costs. Since costs are estimated at current value, actual costs could be different because of inflation, changes in technology, inclusion of additional qualifying sites or changes in regulations, and future unanticipated response actions.

**MMB Calculated Liabilities**

MMB centrally calculates the values for the following liabilities and provides the amounts to each agency as needed for reporting in the CAFR.

**Compensated Absences**

Compensated Absences Liability is the state’s liability to pay for employees’ absences. There are three leave balances that are evaluated for each paid employee position and then multiplied by the employee’s wage and applicable fringe rate and contract formulas to determine the liability. The three leave balances are:

- Annual leave (vacation);
- Compensatory leave; and
- Severance pay
  1. Severance pay is based on sick leave hours and a severance formula but it is not related to medical or other uses of sick leave hours
  2. Vested severance (employees are eligible if they meet length of service or other criteria)
  3. Non-vested severance (the probability of employees remaining with the state until they are eligible)

Compensated absences liability is long-term in nature, similar to bonds and capital leases payables.

An increase in the liability is an increase to (cash basis) salary expense (or salary component of the appropriate function) and a decrease in the liability is a decrease in the salary expense.

GASB Statement No. 16 “Accounting for Compensated Absences” provides guidance for the measurement of accrued compensated absences liabilities, regardless of the reporting model or fund type used to report the transactions. A liability is recognized only for potentially vested rights and not for contingent circumstances, such as medical leaves. The amount must be an estimate of the expected payments.

**Net Pension Liability**

GASB Statement No. 68 “Accounting and Financial Reporting for Pensions” establishes standards for measuring and recognizing liabilities, deferred outflows/inflows of resources, and expense/expenditures. This statement requires the liability of employers and nonemployer contributing entities to employees for defined benefit pensions (net pension liability) to be measured as the portion of the present value of projected benefit payments to be provided through the pension plan to current active and inactive employees that is attributed to those employees’ past periods of service (total pension liability), less the amount of the pension plan’s fiduciary net position.

Employers that participate as single or agent employers that do not have a special funding situation are required to recognize a liability equal to the net pension liability. The net pension liability is required to be measured as of a date no earlier than the end of the employer’s prior fiscal year (measurement date), consistently applied from period to period. If the pension plan’s fiduciary net position exceeds the total pension liability, the result is a net pension asset.
Net Other Postemployment Obligation

GASB Statement No. 75 “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions” establishes standards for measuring and recognizing liabilities, deferred outflows/inflows of resources, and expense/expenditures. This Statement requires the liability of employers and nonemployer contributing entities to employees for defined benefit OPEB (net OPEB liability) to be measured as the portion of the present value of projected benefit payments to be provided to current active and inactive employees that is attributed to those employees’ past periods of service (total OPEB liability), less the amount of the OPEB plan’s fiduciary net position.

Employers that participate as single or agent employers that does not have a special funding situation are required to recognize a liability equal to the net OPEB liability. The net OPEB liability is required to be measured as of a date no earlier than the end of the employer’s prior fiscal year (the measurement date), consistently applied from period to period.

Related Policies and Procedures


See Also


GASB Statement No. 47 “Accounting for Termination Benefits”

GASB Statement No. 49 “Accounting and Financial Reporting for Pollution Remediation Obligations”


GASB Statement No. 68 “Accounting and Financial Reporting for Pensions”

GASB Statement No. 75 “Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions”

GASB Statement No. 88 “Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements”

GASB Interpretation No. 6 “Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements.”

Minnesota Statute 115B.39; Environmental Response and Liability – Landfill Cleanup Program
(https://www.revisor.mn.gov/statutes/?id=115B.39)

GASB Codification Section 1500, “Reporting Liabilities”

GASB Codification Section 2300, “Notes to Financial Statements”